

Abandonment Costs

Overview of the SEC Requirements for Oil and Gas Reporting

Presentation By
John Hodgin
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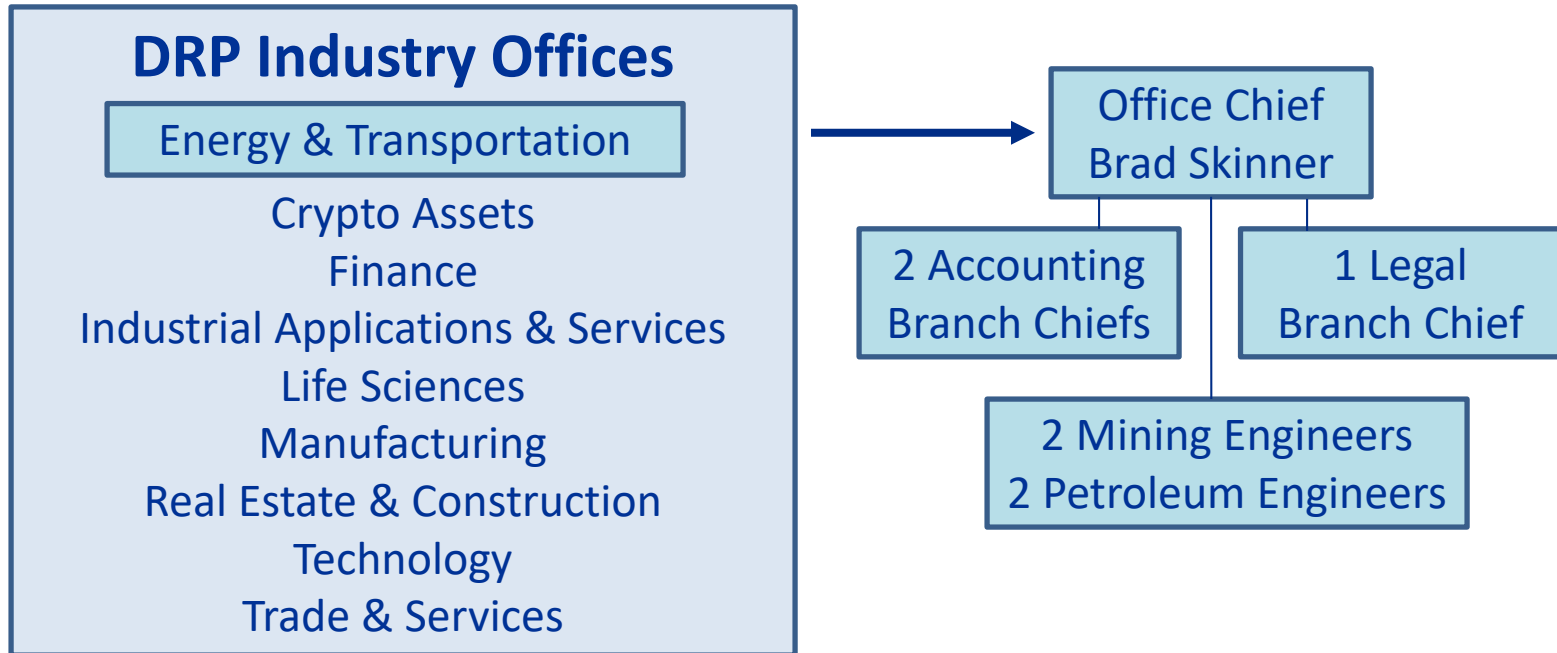
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Division of Corporation Finance

Disclosure Review Program



Statutes That Govern the Securities Industry



Securities Act of 1933

Objectives Relating to Registration

- Requires that investors receive financial and other significant information concerning securities being offered for public sale; and
- prohibits deceit, misrepresentations, and other fraud in the sale of securities.

Securities Exchange Act of 1934

Objectives Relating to Public Company Reporting

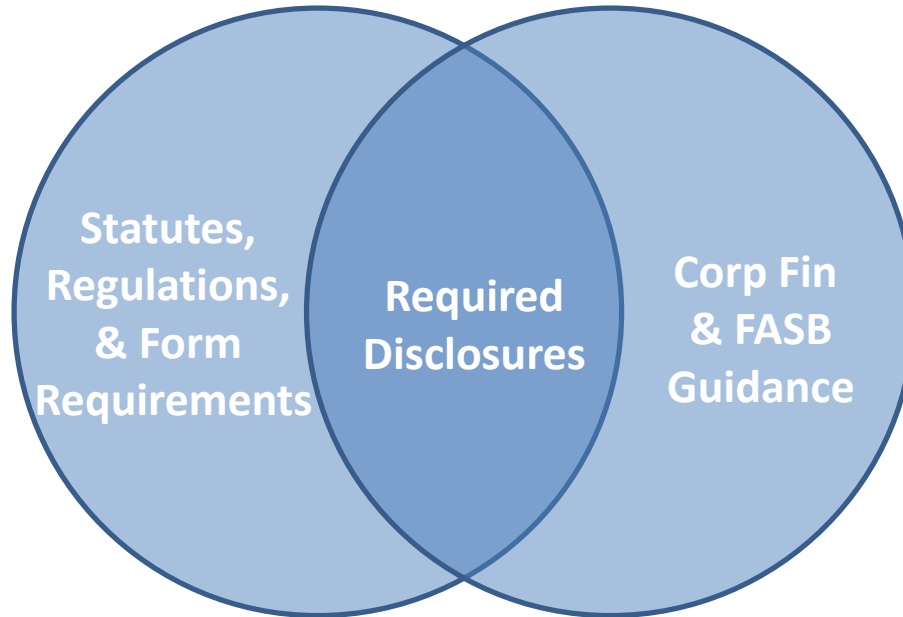
- Requires companies to make periodic reports on the current condition of the company since initial registration.
- Investors who purchase securities and suffer losses have important recovery rights if they can prove that there was incomplete or inaccurate disclosure of important information.



Key Standards for Reserve Reporting

- **Modernization of Oil and Gas Reporting; Final Rule**
 - Regulation S-X, 210.4-10(a)-Oil and Gas Definitions
 - Regulation S-K, Subpart 229.1200—Disclosure by Registrants Engaged in Oil and Gas Producing Activities
- **Compliance and Disclosure Interpretations, Oil and Gas Rules**
- **FASB ASC 932, Financial Accounting Series, Extractive Activities-Oil and Gas (Topic 932), Oil and Gas Reserve Estimation and Disclosures**

Required Disclosures for Abandonment Costs





Requirements for Reporting Abandonment Costs

- **FASB ASC 932, Financial Accounting Series, Extractive Activities-Oil and Gas (Topic 932), Oil and Gas Reserve Estimation and Disclosures**
 - FASB ASC 932-235-50-30 requirement for the disclosure of a standardized measure of discounted future net cash flows
 - FASB ASC 932-235-50-31 identifies the elements used in the calculation of the standardized measure of discounted future net cash flows



See the Definition of “Discounted Future Net Cash Flows Related to Proved Oil and Gas Reserves [Table] accompany the Standard Label in the Amendments to the XBRL Taxonomy; Codification Reference: 932-235-50-30, 50-31 and 55-6: **“Note that future cash flows related to the settlement of an asset retirement obligation are included in the disclosure.”**

Division of Corporation Finance Guidance



[Home](#) | [Previous Page](#)

U.S. Securities and Exchange Commission

Sample Letter Sent to Oil and Gas Producers

Letter Dated February 24, 2004 by the Division of Corporation Finance to registrants identified as being primarily engaged in the production of oil and gas. [Addresses questions regarding required disclosures in FAS 69 upon adoption of FASB Statement No. 143, Accounting for Asset Retirement Obligations.]

FAS 69-Paragraphs 30-34, Disclosure of a Standardized Measure of Discounted Future Net Cash Flows Relating to Proved Oil and Gas Reserve Quantities (Standardized Measure) [**now FASB ASC 932-235-50-30-36**]

- **“We believe that an entity should include the future cash flows related to the settlement of an asset retirement obligation in its Standardized Measure disclosure.”**

Division of Corporation Finance Guidance



[Home](#) | [Previous Page](#)

U.S. Securities and Exchange Commission

Sample Letter Sent to Oil and Gas Producers

Letter Dated February 24, 2004 by the Division of Corporation Finance to registrants identified as being primarily engaged in the production of oil and gas. [Addresses questions regarding required disclosures in FAS 69 upon adoption of FASB Statement No. 143, Accounting for Asset Retirement Obligations.]

Paragraph 30 states: “A standardized measure of discounted future net cash flows relating to an enterprise’s interests in (a) proved oil and gas reserves...shall be disclosed as of the end of the year.”

- “We believe that the requirement to disclose “net cash flows” relating to an entity’s interest in oil and gas reserves requires an entity to include the cash outflows associated with the settlement of an asset retirement obligation. Exclusion of the cash outflows associated with a retirement obligation would be a departure from the required disclosure. However, an entity is not prohibited from disclosing the fact that cash flows associated with asset retirement obligations are included in its Standardized Measure disclosure as a point of emphasis.”

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[Home](#) | [Previous Page](#)

U.S. Securities and Exchange Commission

Frequently Requested Accounting and Financial Reporting Interpretations and Guidance March 31, 2001

Existing economic and operating conditions are the product prices, operating costs, production methods, recovery techniques, transportation and marketing arrangements, ownership and/or entitlement terms and regulatory requirements that are extant on the effective date of the estimate. **“These conditions include estimated net abandonment costs to be incurred and duration of current licenses and permits.”**



FASB Statement No. 143

Accounting for Asset Retirement Obligations

Standards of Financial Accounting and Reporting

2. Scope

- Applies to all entities.
 - ❖ Even if an oil and gas company intends to retire an asset by using internal resources, it must recognize an ARO.

- Encompasses the obligations for dismantlement, restoration, and abandonment costs. Estimated residual salvage values shall be taken into account.
 - ❖ Will include plugging of wells, future dismantlement and removal of production equipment and facilities, and the restoration and reclamation of the surface or subsurface lands to an ecological condition similar to that existing before oil and gas extraction began.



FASB Statement No. 143

Accounting for Asset Retirement Obligations

Standards of Financial Accounting and Reporting

2. Scope

- Relates to the legal obligations associated with the retirement of a tangible long-lived asset that results from the acquisition, construction, or development and (or) normal operation.
- A legal obligation is an obligation that a party is required to settle as a result of an existing or enacted law, statute, ordinance, or written or oral contract. Retirement is defined as the other-than temporary removal of a long-lived asset from service.
 - ❖ Usually required by federal, state and local government regulations or lease contracts and depend on the jurisdiction in which the related property resides.



FASB Statement No. 143

Accounting for Asset Retirement Obligations

Standards of Financial Accounting and Reporting

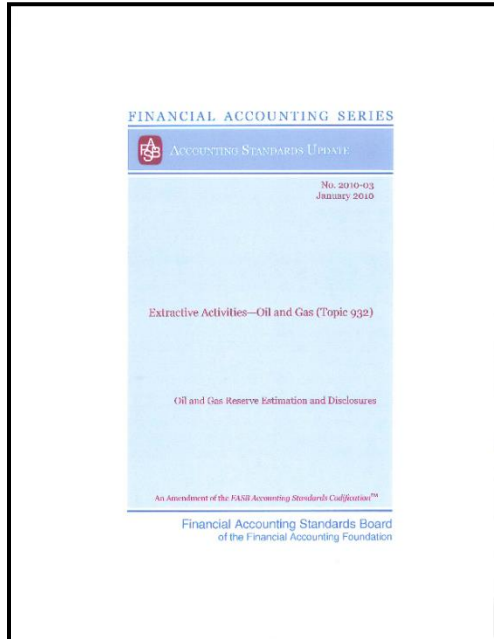
16. Effects of Funding and Assurance Provisions

- Providing assurance (surety bonds, letters of credit, or guarantees by others) that an entity will be able to satisfy its asset retirement obligation does not satisfy or extinguish the related liability.
- Prepayment would not relieve the entity of its liability for future changes in its asset retirement obligations.

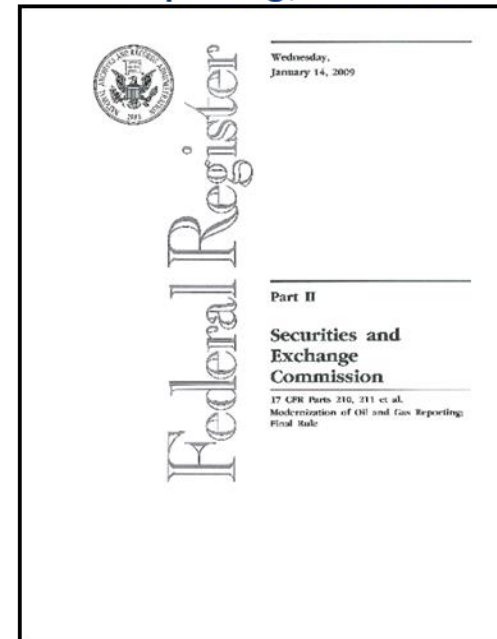
Disclosure Relating to Abandonment Costs



FASB Topic 932



Modernization of Oil and Gas Reporting; Final Rule





FASB ASC 932

Standardized Measure of Discounted Future Cash Flows

932-235-50-31 Abandonment Costs in the Disclosure of the Standardized Measure

- a. Future cash inflows.
- b. Future (undiscounted) development and production costs.**
 - **If estimated development expenditures are significant, they shall be presented separately from estimated production costs.**
- c. Future income tax expenses.
- d. Future net cash flows.
- e. Discount.
- f. Standardized measure of discounted future net cash flows.**

FASB ASC 932

Standardized Measure of Discounted Future Cash Flows



932-235-50-36 Abandonment Costs in the Disclosure of the Standardized Measure

- Additional information necessary to prevent the disclosure of the standardized measure of discounted future net cash flows and the changes therein from being misleading also shall be provided.

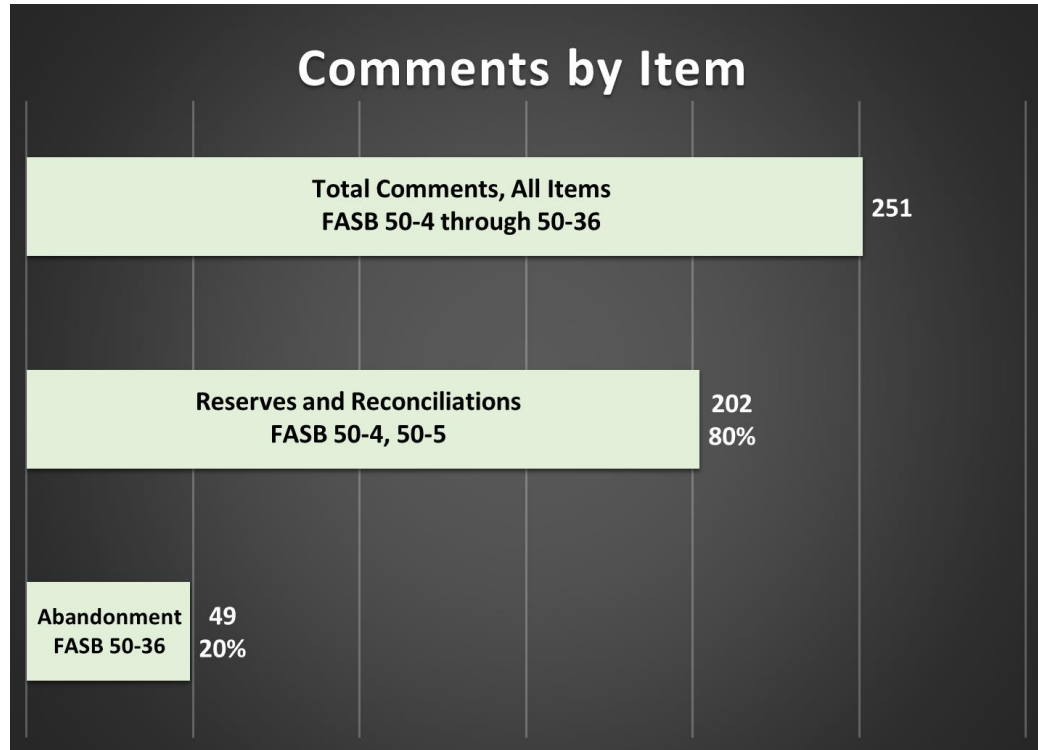


Item 1202(a)(8) of Regulation S-K

Third Party Reports

- If the registrant represents that a third party prepared, or conducted a reserves audit of, the registrant's reserves estimates, or any estimated valuation thereof, or conducted a process review, the registrant shall file a report of the third party as an exhibit to the relevant registration statement or other Commission filing.
- If the report relates to the preparation of, or a reserves audit of, the registrant's reserves estimates, it must include the following disclosure, if applicable to the type of filing:
 - (v) A discussion of **primary economic assumptions**;
 - (ix) A brief summary of the third party's **conclusions with respect to the reserves estimates**

Analysis of FASB ASC 932 Comments October 2019 Through September 2023





FASB ASC 932-235-50-30

Standardized Measure of Discounted Future Cash Flows

🚩 Lack of Clarity Regarding Abandonment Costs

Typical Disclosure Issue and Comments

1. Expand the discussion accompanying the presentation of the standardized measure to **clarify, if true, that future cash flows take into account the estimated abandonment costs for your proved properties.** Refer to FASB ASC 932-235-50-36.

If the abandonment costs, including such costs related to your proved undeveloped locations, have not been included, tell us the undiscounted dollar amounts and the dollar amounts discounted at ten percent for each of the periods presented, and **explain to us your rationale for excluding these costs from your calculation of the standardized measure.** Refer to the definition of “Discounted Future Net Cash Flows Related to Proved Oil and Gas Reserves” under Amendments to the XBRL Taxonomy, Accounting Standards Update 2010-03, Extractive Activities-Oil and Gas (Topic 932), Oil and Gas Reserve Estimation and Disclosures, January 2010.



FASB ASC 932-235-50-30

Standardized Measure of Discounted Future Cash Flows

❏ Omission of Abandonment Costs

Typical Disclosure Issue and Comments

1. We believe the impact of the error (systematic omission) related to your treatment of abandonment costs for purposes of calculating the standardized measure of discounted future net cash flows was quantitatively material to the net measure. Further, we believe the qualitative factors you describe do not overcome the quantitative impact of the errors. Accordingly, we do not agree with your conclusion that the errors are immaterial. Please amend you Form 10-K to restate your presentation of the standardized measure. Additionally, in light of the restatement, please reassess your conclusion that your disclosure controls and procedures were effective.

For additional information regarding materiality refer to the speech by SEC Staff: Assessing Materiality, Focusing on the Reasonable Investor When Evaluating Errors; Paul Munter, Acting Chief Accountant, March 9, 2022. <https://www.sec.gov/news/statement/munter-statement-assessing-materiality-030922>



FASB ASC 932-235-50-30

Standardized Measure of Discounted Future Cash Flows

Impacts to Third Party Reserve Reports

Typical Disclosure in the Reserve Report

If Abandonment Costs are included:

The estimates in this report conform to the FASB Accounting Standards Codification Topic 932, Extractive Activities-Oil and Gas [with the exception of the exclusion of future income taxes].

If Abandonment Costs not are included:

The estimates in this report conform to the FASB Accounting Standards Codification Topic 932, Extractive Activities-Oil and Gas with the exception of the exclusion of abandonment costs as requested.

Filing Review Outcomes



A Review May Result in Requests to:

- Revise the disclosure in a document on file with the SEC*
 - Amendments to text or factual information
- Provide additional disclosure in a document on file with the SEC*
- Provide additional or different disclosure in a future filing with the SEC

*File the revised or corrected document in EDGAR as an amendment for public disclosure



Mandatory Release of Information

Increased Transparency of the Review Process

When the Division completes a filing review it makes its comment letters and company responses to those comment letters public on the SEC's EDGAR system. The SEC began publicly releasing comment letters between the SEC staff and SEC filers in 2005 for filings made after August 1, 2004.

Timing on Release of Correspondence

The Division makes this correspondence public no earlier than 20 business days after it has completed its review of a periodic or current report or declared a registration statement effective.





Limitations of Using Comment Letters



Comments are formulated based on the staff's **“understanding of that company’s facts and circumstances.”**

Caution should be exercised when attempting to interpret the exchange of comments and responses contained in comment letters as a proxy or substitute for SEC guidance.

Not all of the items considered and discussed may be part of the public record as certain information may be subject to confidential treatment under Rule 83 or the object of internal staff conversations.

Sarbanes-Oxley Act of 2002



Signed into law on July 30, 2002

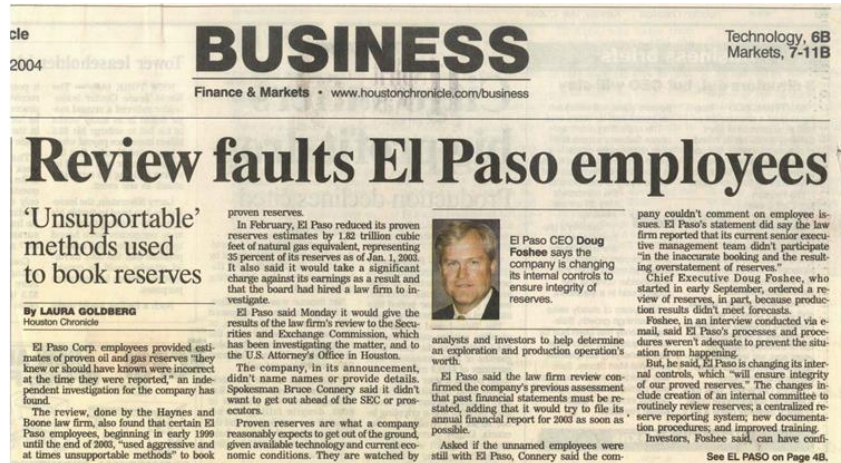
- The Act mandated a number of reforms to enhance corporate responsibility, enhance financial disclosures and combat corporate and accounting fraud, and created the "Public Company Accounting Oversight Board," also known as the PCAOB, to oversee the activities of the auditing profession.

Required and Selective Review

- As required by the Sarbanes-Oxley Act of 2002, the Division of Corporation Finance undertakes some level of review of each reporting company at least once every three years and reviews a significant number of companies more frequently.
- In its filing reviews, the Division concentrates its resources on critical disclosures that appear to conflict with Commission rules or the applicable accounting standards and on disclosure that appears to be materially deficient in explanation or clarity.



Penalties for Noncompliance



Sarbanes-Oxley Act of 2002

- Up to 10 years in federal prison for destroying, altering, concealing, or falsifying records
- Up to 10 years in prison for failing to maintain all audit or review work papers for 5 years pertaining to an issuer of securities
- Up to 25 years in federal prison for knowingly defrauding shareholders

- Possible fines of 25 MM\$ per offense for corporations
- Fines for individuals possible
- Increased penalties up to 20 years in prison for violations under the SEC Act of 1934

Individual Accountability



From the March 31, 2001 SEC Interpretations and Guidance

“The SEC staff reminds professionals engaged in the practice of reserve estimating and evaluation that the Securities Act of 1933 subjects to potential civil liability every expert who, with his or her consent, has been named as having prepared or certified any part of the registration statement, or as having prepared or certified any report or valuation used in connection with the registration statement. These experts include accountants, attorneys, engineers or appraisers.”



Reference Documents

1. **Division of Corporation Finance: Regulation S-K Subpart 229.1200 [17 CFR Part 229];**
<http://www.sec.gov/divisions/corpfin/ecfrlinks.shtml>
2. **Regulation S-X, 210.4-10(a)-Oil and Gas Definitions**
<https://www.ecfr.gov/current/title-17/chapter-II/part-210#210.4-10>
3. **Securities and Exchange Commission: Modernization of Oil and Gas Reporting; Final Rule [17 CFR Parts 210, 211 et al.]**
<http://www.sec.gov/rules/final/2009/33-8995fr.pdf>

Securities and Exchange Commission: Staff Accounting Bulletin No. 99 Materiality

<https://www.sec.gov/interps/account/sab99.htm>

Securities and Exchange Commission: Sample Letter Sent to Oil and Gas Producers, February 24, 2004

<http://www.sec.gov/divisions/corpfin/guidance/oilgasletter.htm>

5. **Division of Corporation Finance: Compliance and Disclosure Interpretations; Issued Oct. 26, 2009; Updated May 16, 2013**
<https://www.sec.gov/divisions/corpfin/guidance/oilandgas-interp.htm>



Reference Documents

- 1. Financial Accounting Standards Board: Extractive Activities-Oil and Gas (Topic 932), Oil and Gas Reserve Estimation and Disclosures**
<https://www.fasb.org/Page/ShowPdf?path=ASU+2010-03+-+Extractive+Industries+Oil+and+Gas+Topic+932+Oil+and+Gas+Reserve+Estimation+and+Disclosures.pdf&title=UPDATE+NO.+2010-03%E2%80%94EXTRACTIVE+ACTIVITIES%E2%80%94OIL+AND+GAS+%28TOPIC+932%29%3A+OIL+%26+GAS+RESERVE+ESTIMATION+AND+DISCLOSURES&acceptedDisclaimer=true&Submit=>
- 2. Financial Accounting Standards Board Statement 143: Accounting for Asset Retirement Obligations**
<https://fasb.org/Page/ShowPdf?path=fas143.pdf&title=FAS+143+%28AS+ISSUED%29&acceptedDisclaimer=true&Submit=>

Acknowledgements



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Closing Remarks



My Time's Up!
Thanks for Listening



Contact Information

John Hodgin, P.G., P.E.
Petroleum Engineer
Office of Energy and Transportation
Division of Corporation Finance
U.S. Securities & Exchange Commission
100 F Street, N.E.
Mail Stop 3233
Washington, District of Columbia 20549
Office Direct Phone: (202) 551-3699
Email: hodginj@sec.gov