

Reserve Overbooking – An Issue of Professional Ethics

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Abstract

Revelations of financial mismanagement and the resulting increase in legal and regulatory scrutiny have focused attention on how publicly-traded oil and gas companies report and book reserves. In spite of this, reserve overbooking remains a persistent problem, one that, while widely acknowledged, is only reluctantly discussed. We see two broad categories of reserve overbooking: 1) errors of omission; and 2) errors of commission. The first relates to errors resulting from ignorance, which can be addressed through education, training and mentoring. The second relates to those things we know about – the choices we face when we find ourselves 1) tempted to intentionally overstate reserves for motivational reasons; or 2) faced with the need to de-book reserves. These are not technical issues; they are ethical ones, often influenced by misguided incentives. Why is there so much reluctance and hand-wringing associated with de-booking reserves? It is because, for publicly traded companies, the market impacts can be quite negative, at least in the near term. But repeated experience has shown that ultimately, the “Piper must be paid”; unfortunately, it is the shareholders who often suffer the most. Are proper controls in place to mandate unbiased professional behavior? On paper they are, through stated company policies, governmental regulations and professional-society guidelines. Are these controls working? For the majority of firms who take seriously the fiduciary responsibilities entrusted to them, we believe they work most of the time. However, based on recent revelations of financial mismanagement, having the proper policies, controls and definitions in place is not enough. Ultimately, compliance is an issue of character and ethics – of personal and corporate values.

Biography

Mark A. McLane is a Partner in the international consulting firm of Rose & Associates, LLP. He holds a BSc with Honors in Petroleum Engineering from The University of Texas at Austin. He has a diverse technical and business background spanning more than 30 years in the petroleum industry. He joined Rose & Associates in January 2000 after three years with Pioneer Natural Resources and 17 Years with Exxon Company, U.S.A. He has co-authored several technical papers, served on the Professional Ethics/Registration Panel at the 2003 SPE ATCE in Denver, Colorado and was a Distinguished Lecturer of the Society of Petroleum Engineers on the topic of “Reserve Overbooking – An Issue of Professional Ethics” in 2004 and 2005.