

# Financial Reporting and the IASB

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# Agenda

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- ▶ Stakeholders in the financial sector
  - ▶ ‘Internal’ / ‘External’ stakeholders
  - ▶ Characteristics
  - ▶ Useful information for stakeholders?
  
- ▶ IASB discussion paper
  - ▶ Responses received

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# Convergence

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▶ SEC

▶ IASB

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# Stakeholders

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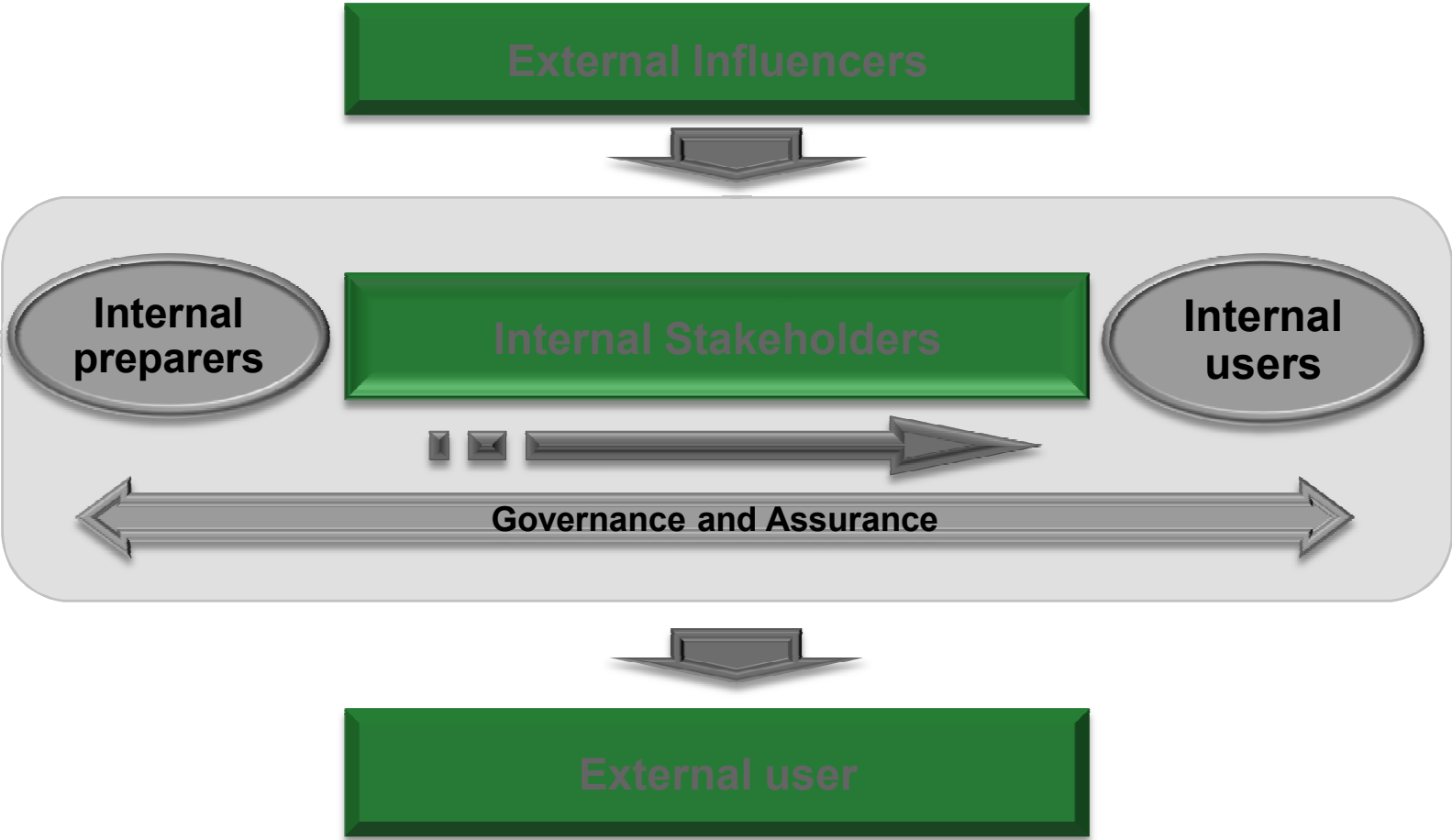
## Diversity in stakeholders and their characteristics

- ▶ Demonstrated by parties responding to consultation papers (e.g., SEC and IASB)

## Internal and external

- ▶ Characteristics and priorities
  - ▶ Users versus preparers
  - ▶ Level of sophistication
  - ▶ View of cost/benefit
- ▶ Conflicts between stakeholder interests
- ▶ Influence on future reserves measurement, reporting and use

# Stakeholders in the financial sector



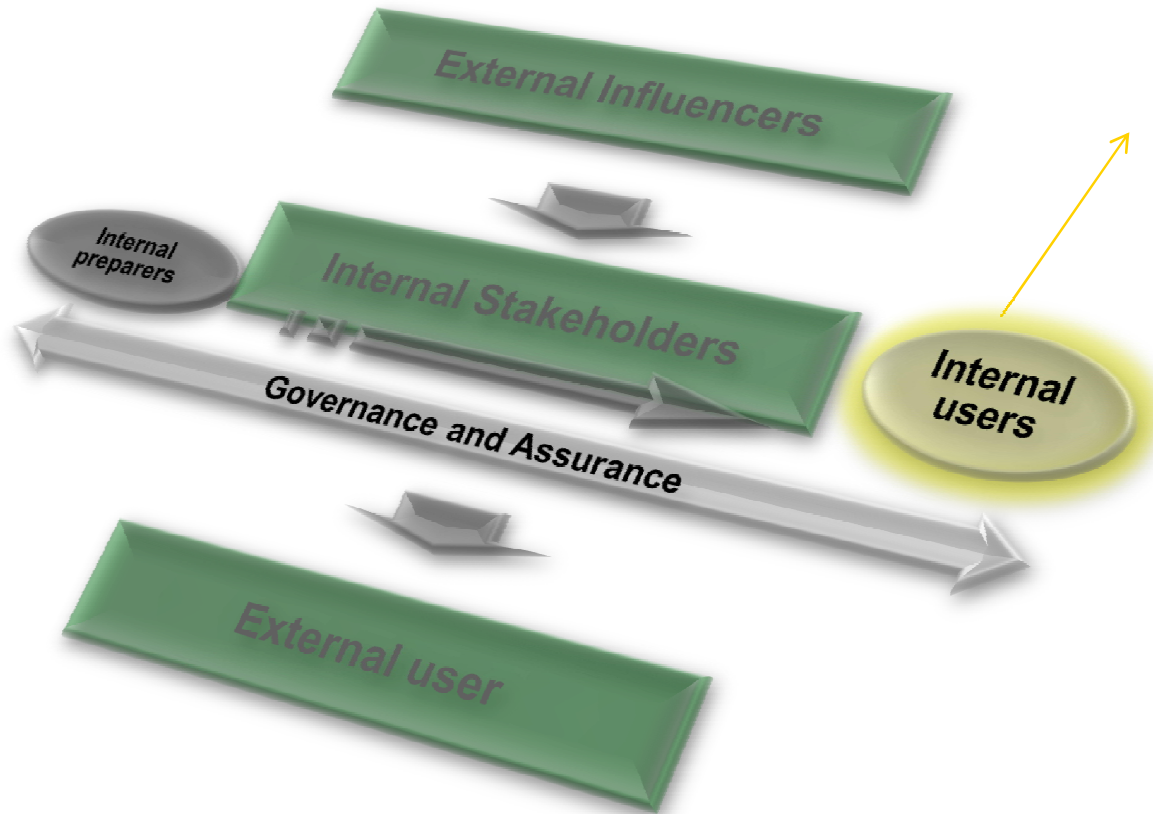
# Stakeholders in the financial sector

## Preparers

- ▶ Technical / Commercial specialists
- ▶ Internal use
- ▶ External use
- ▶ Partners



# Stakeholders in the financial sector



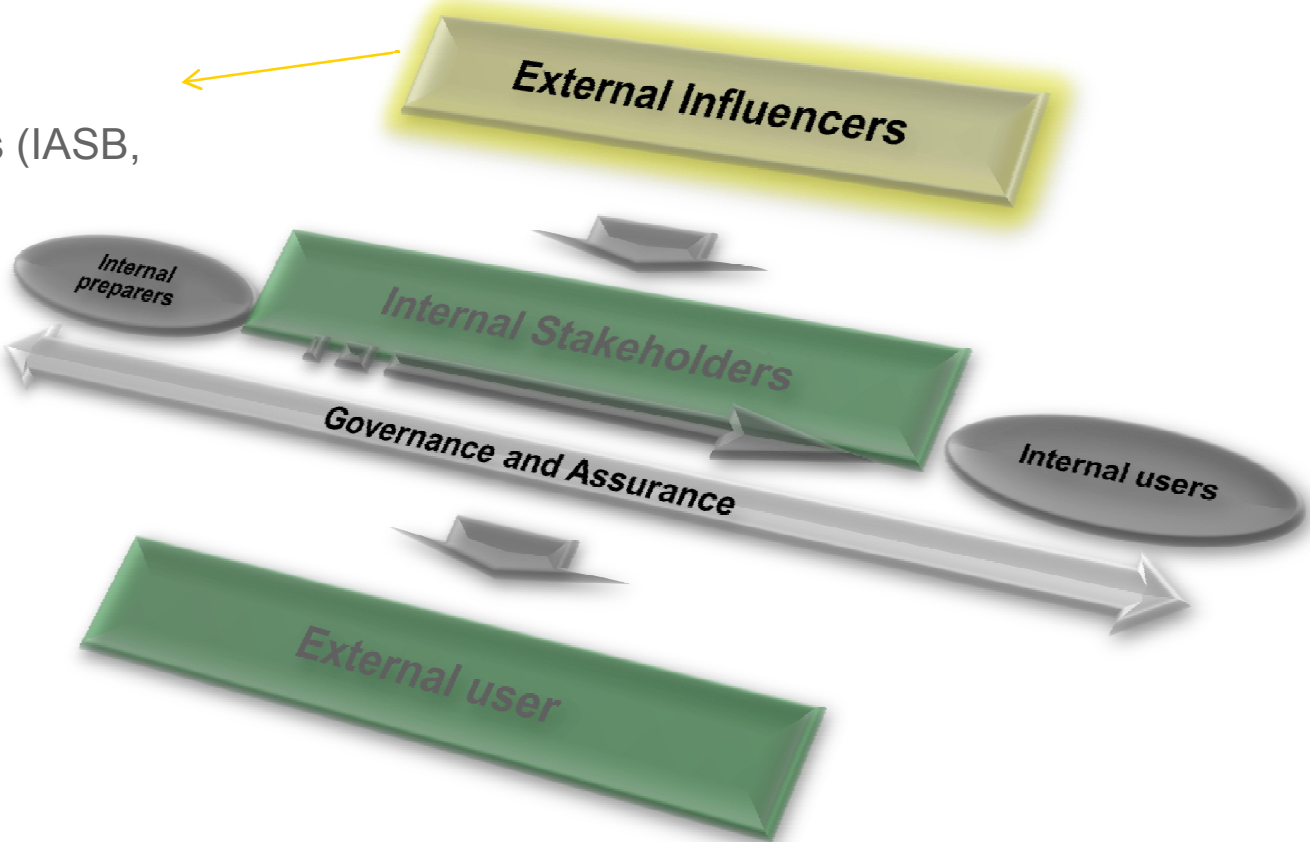
## Users

- Management
  - Strategic / business planning, forecasting and budgeting
  - Investment decisions-internal & external
  - Performance management and compensation awards
- Preparers of reporting
- Board, Audit Committee
- Partners

# Stakeholders in the financial sector

## Influencers

- ▶ Standard setting bodies (IASB, FASB, SEC etc)

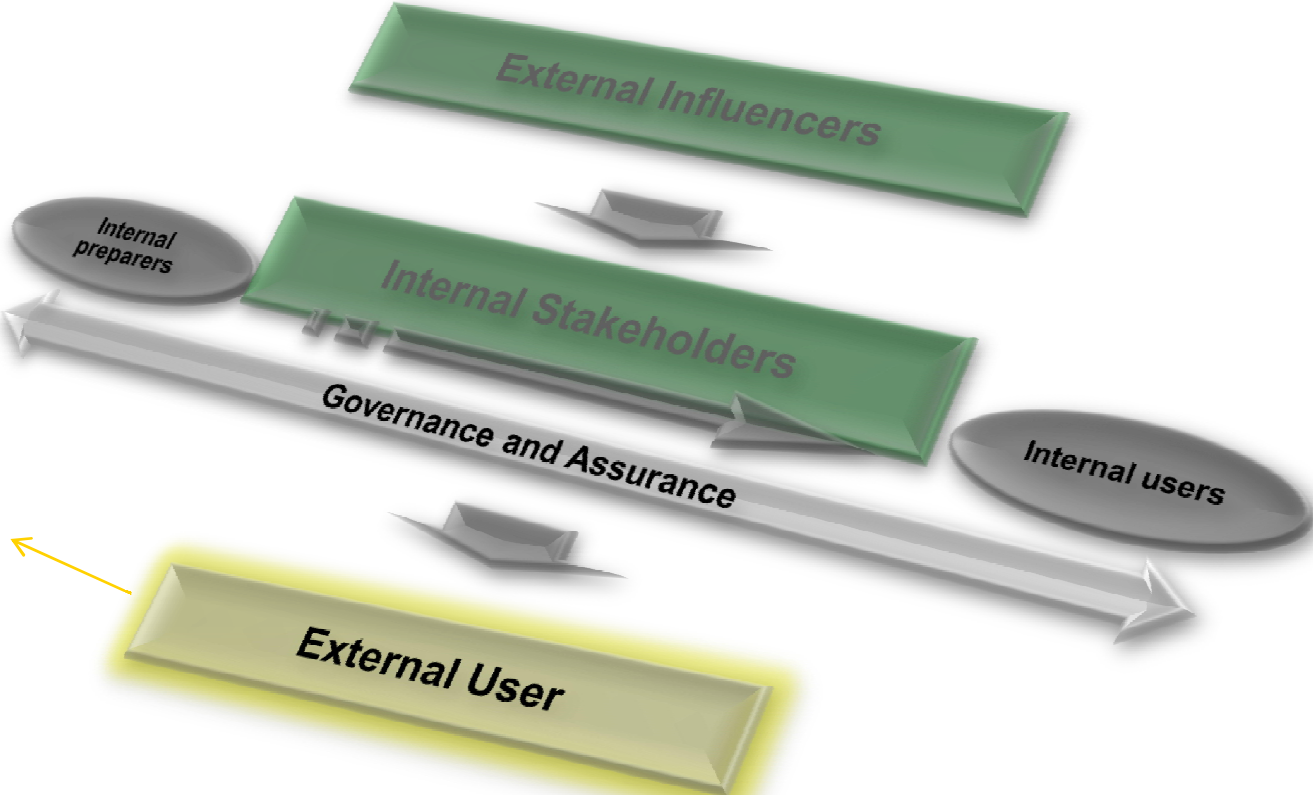




# Stakeholders in the financial sector

## Users

- ▶ Investor community
- ▶ Lenders
- ▶ Competitors
- ▶ M&A
- ▶ Government/ public interest bodies
- ▶ Technical consultants
- ▶ Accounting profession
- ▶ Interested public



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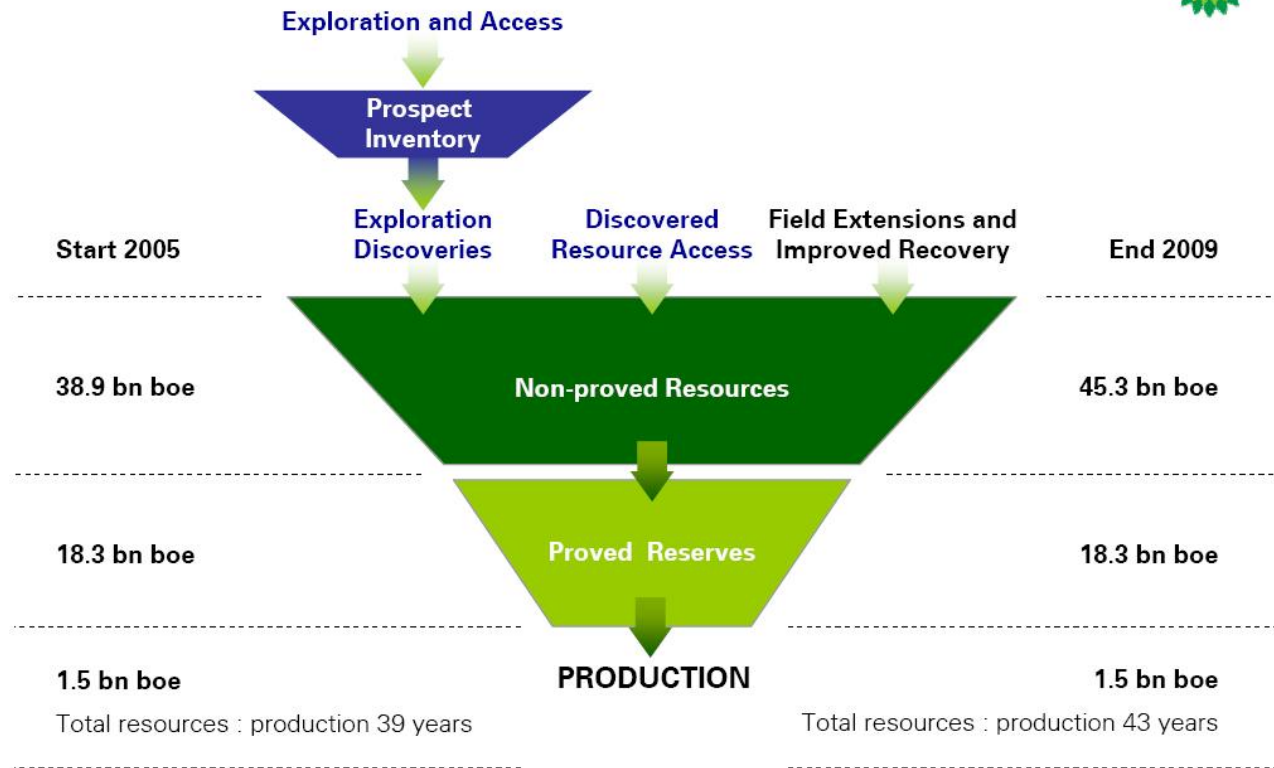
# Useful information provided to financial stakeholders?

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- ▶ Published reserves and resources
  - ▶ Regulatory drivers
  - ▶ Published information likely to be different to management's view / decision making process
  - ▶ May in turn be different to an investor's view
  
- ▶ Financial reporting for extractive activities
  - ▶ Principally based on historic cost
  - ▶ Reserves and resources a key driver for financial reporting
  
- ▶ Annual reports (including reserves/ resources) just one source of information for investment decisions

# BP resources

## Resources to reserves to production

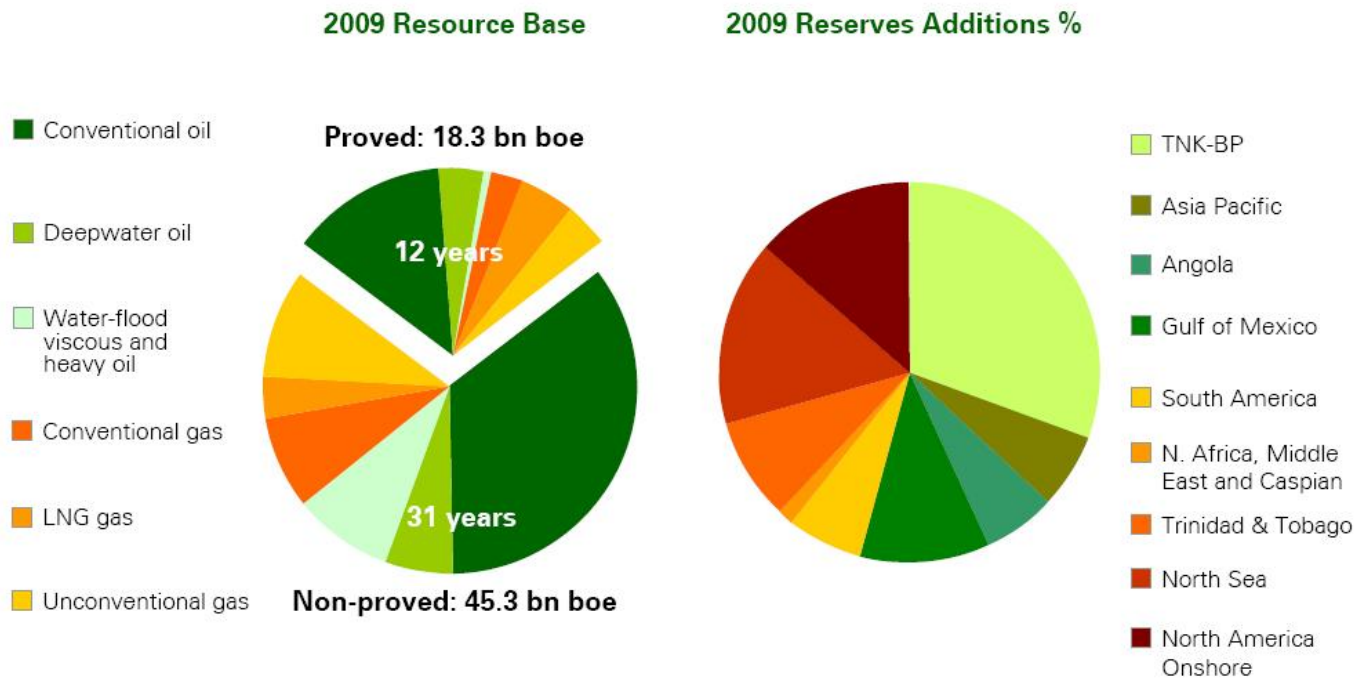


*Resources and reserves on a combined basis of subsidiaries and equity-accounted entities*

Source: Extract from BP Full Year 2010 Results and Strategy Update

# BP resources

## Diverse resource base and reserves additions



*Resources at end-2009 on a combined basis of subsidiaries and equity-accounted entities. 2009 reserves additions are price adjusted*

# Net assets and market capitalisation

	Net Assets 30 June 2011 \$m	Market Capitalisation 23 September 2011 \$m
Total	82,630	96,286 <sup>b</sup>
BP	108,408	111,684
Shell	167,316	194,727 <sup>a</sup>
Exxon	155,551	336,653
Chevron	116,430	180,609
	Net Assets - 30 June 2011 \$m	Market Capitalisation 23 September 2011 \$m
Anglo American	41,639	46,024
BHP Billiton	57,755	166,150
Rio Tinto	69,299	94,220
Xstrata	45,533	37,355
Barrick Gold	23,533	48,738

Sources: Consolidated market capitalisation – Thomson  
Datastream; Net Assets – Company reports

<sup>a</sup>Exchange rate 1GBP= 1.55USD

<sup>b</sup>Exchange rate 1EUR= 1.35USD

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# IASB Discussion Paper on Extractive Activities- the responses

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# Discussion Paper- introduction

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- ▶ Current lack of comprehensive financial reporting guidance for the extractive industries under IFRS
- ▶ Variation in industry practice
  - ▶ Variety of practice under IFRS
  - ▶ Jurisdiction specific reporting requirements
- ▶ *Discussion Paper – Extractive Industries* issued in April 2010
  - ▶ Findings from international project team established by IASB
  - ▶ Invitation for comment
- ▶ Over 140 responses received
  - ▶ Minerals and oil and gas majors, accountancy bodies, regulators accountancy firms
  - ▶ More limited responses from small and medium sized extractive industry participants
  - ▶ Variety of views from respondents

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# Scope

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- ▶ Need for a separate standard?
  - ▶ Some challenge around the need for a separate recognition and measurement standard
    - ▶ Implementation/ application guidance of existing IFRS an alternative?
  - ▶ Also some support
  - ▶ Some general acknowledgement of a need for a separate disclosure standard
  - ▶ Degree of similarity between oil and gas and minerals?
- ▶ Upstream focus
  - ▶ Broad agreement that if new IFRS is justified, the scope should be specific to upstream activities
- ▶ Some key issues not addressed
  - ▶ Narrower scope than IFRS 6- other non-regenerative resources and activities?
  - ▶ Current scope does not address many complex accounting areas such as:
    - ▶ Farm in/ out transactions
    - ▶ Accounting for production sharing and royalty arrangements



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# Reserves and resources- definitions

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- ▶ Adopting definitions of CRIRSCO template and PRMS definitions
  - ▶ Effective reliance on unregulated 3<sup>rd</sup> parties
- ▶ Clarification required as to how changes in reserves and resources definitions would be incorporated into a future IFRS
- ▶ IASB governance framework required?
  - ▶ Ensure definitions remain appropriate for financial reporting
- ▶ Remain numerous reporting bodies that require different definitions

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# Asset recognition

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- ▶ Potential increase in capitalised costs
  - ▶ Capitalisation of costs that may not have future economic benefits?
    - ▶ Inconsistent with current IFRS capitalisation principles- probable future economic benefits
  - ▶ Certain information may detract from the value of the legal right?
- ▶ Differing views of an appropriate model- largely reflect industry practice
  - ▶ Oil & Gas companies
    - ▶ Preferred approach appears to be successful efforts
    - ▶ DP proposal more aligned to the full cost method?
  - ▶ Mining
    - ▶ Typically expense costs early in the project lifecycle
    - ▶ Discomfort with capitalising costs prior to a clear expectation of economic benefit - move away from expensing costs early in the project lifecycle
- ▶ Companies with an exploration focus may prefer the proposed model
  
- ▶ BUT- response rate from smaller industry participants low

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# Unit of account

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- ▶ Uncertainty amongst respondents on application of proposal in practice
  - ▶ Complex to apply in practice
  - ▶ Significant judgment required
- ▶ Geographical area does not always contract, ie, acquisition of adjacent leasehold rights
- ▶ Respondents seek further guidance on practical application for matters such as price/cost allocation
- ▶ Likely comparison to predecessor GAAP
- ▶ Interpretative area that gives rise to significant variations in current practice

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# Asset measurement: Historical cost and impairment

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- ▶ **Historic cost basis**
  - ▶ Majority of respondents agreed that historical cost is the preferred measurement basis
  - ▶ More compelling reasons that just resulting in the “least harm”.
    - ▶ Historical cost is easily measurable and universally understood amongst financial statement users.
    - ▶ Allows users to assess how effectively companies use capital resources (ie, return on capital employed)
    - ▶ Current and fair value require significant judgments and assumptions, making this difficult, costly, and less comparable across companies
    - ▶ Users may not welcome/understand significant balance sheet (and consequent P&L) movements resulting from fair value measurement
  
- ▶ **Impairment**
  - ▶ Some concern expressed around removal from the scope of IAS36
  - ▶ Is a separate impairment approach for E&E assets necessary?
    - ▶ With appropriate measurement basis and clarity on the unit of account concept
  - ▶ Shift in burden of proof, from “why carried” to “why expensed”, will increase burden on preparers and likely result in inconsistent application across companies

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# Disclosure

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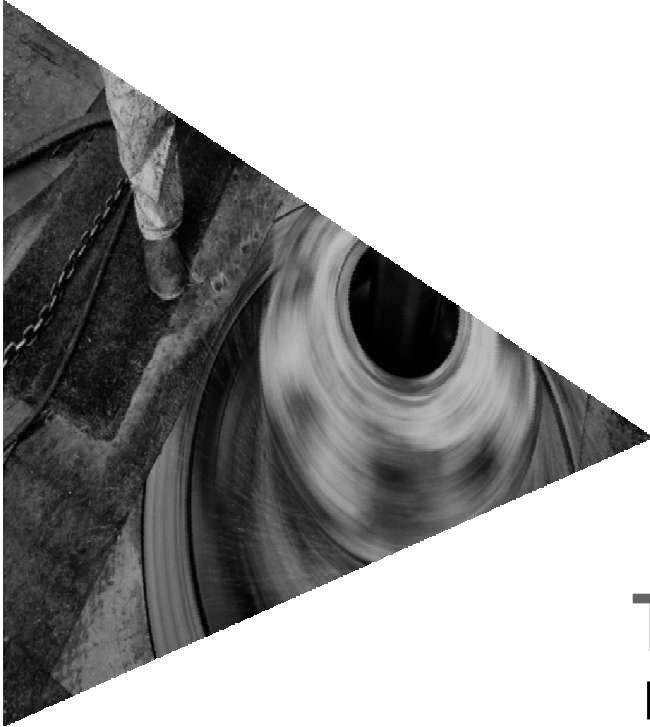
- ▶ Reserves
  - ▶ Probable reserves- large oil and gas respondents advocated optional disclosure
    - ▶ Heightened risk and uncertainty- litigation and compliance costs
  - ▶ Commercial sensitivity- concern from mining sector re disclosure of quantitative assumptions
  - ▶ Sensitivity analysis- inputs into reserve and resource estimates are non-linear- loss of meaning and value if a single input is changed
- ▶ Current value disclosures
  - ▶ Complexity and significant judgment involved reduces usefulness
  - ▶ Appropriate for IASB to require current value disclosures by the extractive sectors only?
- ▶ Differences to US GAAP
  - ▶ Disclosure of key assumptions and reserve sensitivities/ probable reserves
  - ▶ Need for IASB to work with FASB/SEC and other regulators
- ▶ Cost/ benefit?
- ▶ Publish What You Pay

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# Closing remarks and next steps

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- ▶ A number of concerns raised by respondents
  - ▶ Differing views from Minerals and Oil and Gas respondents
  - ▶ Challenges in reconciling these views
  
- ▶ Low response rate from small and medium sized participants
  
- ▶ Importance of continued engagement by stakeholders with the IASB
  
- ▶ Many complex areas of accounting not addressed by the DP
  - ▶ Depending on final scope- potential need for future interpretation
  
- ▶ Considerable way to go before a new IFRS
  - ▶ Decision as to whether it becomes part of IASB's agenda



# Thank you

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**UN Expert Group on Resource Classification**

<http://live.unece.org/energy/se/reserves.html>

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