

## Oil and Gas Reporting Modernization

### A Small Entity Compliance Guide\*

#### Introduction

The Securities and Exchange Commission has adopted revisions to its oil and gas reporting disclosures which previously were dispersed in Regulation S-K and Regulation S-X, as well as Industry Guide 2. The amendments revise Rule 4-10 of Regulation S-X. They also update the Commission's disclosure requirements for oil and gas producing companies and consolidate them in a new Subpart 1200 to Regulation S-K. The amendments concurrently align the full cost accounting rules with the revised disclosures.

Oil and gas producing companies will be required to present disclosures pursuant to the new rules in registration statements and annual reports on Forms 10-K and 20-F containing financial statements for fiscal years ending on or after December 31, 2009.

The primary purpose for the amendments is to provide investors with a more meaningful and comprehensive understanding of oil and gas reserves, which should help investors evaluate the relative value of oil and gas companies. The amendments are designed to modernize and update the oil and gas disclosure requirements to align them with current practices and changes in technology.

#### No Early Compliance

Companies must continue to report information regarding their oil and gas operations, including oil and gas reserves, under the old rules until the new rules go into effect in order to maintain comparability among company disclosures.

#### Overview of New Rules

##### 1. Changes to Oil and Gas Definitions in Rule 4-10 of Regulation S-X

The new rules and amendments revise the current oil and gas definitions in Rule 4-10 of Regulation S-X in the following manner:

- **Average price:** The rules require the use of a 12-month average price — instead of a current single-day price (the current standard) — to calculate reserves to enhance comparability of reserves estimates among oil and gas companies, while reducing the effects of seasonality and short-term price volatility.
- **First-of-the month pricing:** The rules also direct companies to use first-of-the-month pricing to calculate the 12-month average to give companies more time to prepare estimates.
- **Reliable Technologies:** The rules permit the use of "reliable technologies" to establish reserves estimates instead of the current prescribed specific field tests. This extends the possible technologies permitted (previously specified) to establish reserves.
- **Nontraditional Resources:** The rules require that nontraditional resources (such as oil sands, bitumen, and shale) be included in oil and gas reserves instead of mining reserves because their products are essentially the same as those produced using traditional resources.

- **Eliminate “Certainty” Test:** The amendments change the definition of the term “proved undeveloped reserves” to use a “reasonable certainty” standard instead of a “certainty” standard, as required under the prior rules.
- **Supporting Definitions:** The rules also add and revise other definitions to the Commission’s oil and gas reporting requirements for supporting terms used in the new definitions for proved, probable, and possible reserves — including a definition for the term “reserves.”

## 2. Consolidation of Disclosure Requirement in Subpart 1200

The rules also create a new Subpart 1200 in Regulation S-K. This new subpart consolidates the industry-specific disclosure requirements for oil and gas companies currently found in Item 102 of Regulation S-K and Industry Guide 2. The new subpart contains the following disclosure items:

- **Item 1201. General instructions.**
- **Item 1202. Reserves:** Codifies existing reserves disclosure from Item 102 of Regulation S-K. The new Item requires disclosure of:
  - Non-traditional resources (*i.e.*, bitumen, shale, coalbed methane) as oil and gas reserves.
  - Technologies used to establish new or added reserves, because the rule no longer specifies the technology required to establish reserves.
  - Preparer/auditor qualifications. A description of the company’s internal controls for its reserves estimation and the qualifications of the technical person primarily responsible for overseeing the preparation of the reserves estimates or reserves audit.
  - Third party reports. If a company represents that its oil and gas disclosure is based on the authority of a third party that prepared the reserves estimates or conducted a reserves audit or process review, the company would need to file a report prepared by the third party. This report mirrors the Society of Petroleum Evaluation Engineers guidelines for preparers’ and auditors’ reports.

Item 1202 also permits, but does not require, disclosure of:

- Probable and possible reserves, to provide a more comprehensive view of a company’s potential; and
  - Reserves price sensitivity, allowing companies to show estimates based on futures or management’s estimated prices.
- **Item 1203. Proved Undeveloped Reserves (PUDs):** Requires narrative disclosure of the following information:
    - The total quantity of PUDs at year end;
    - Any material changes in PUDs that occurred during the year, including PUDs converted into proved developed reserves;
    - Investments and progress made during the year to convert PUDs to proved developed oil and gas reserves; and

- An explanation of the reasons why material concentrations of PUDs in individual fields or countries have remained undeveloped for five years or more after disclosure as PUDs.
- **Item 1204. Production:** Codifies production disclosure from Industry Guide 2, except that it provides greater clarity by requiring separate production disclosure for countries and fields that contain greater than 15% of the company's total oil and gas reserves.
- **Items 1205-1208:** Codify the remaining Industry Guide 2 disclosure requirements in Regulation S-K, without substantive changes, regarding drilling activities, present activities, delivery commitments, and wells and acreage.

### 3. Other Significant Issues

#### a. MD&A Guidance

The adopting release also includes interpretative guidance regarding the types of issues an oil and gas company should consider when preparing its MD&A, including disclosure regarding material changes due to technology, prices and concession conditions.

#### b. Ceiling Test Limitation for Capitalized Costs under Full Cost Method

The amendments change the Commission's full cost method of accounting to use a 12-month average price for reserves quantity disclosures and for accounting purposes.

#### c. Accounting Treatment and No Retroactive Revision

The adopting release includes accounting guidance stating that any change to accounting figures that result from the amendments should be treated as a change in the method of applying an accounting principle that is inseparable from a change in accounting estimate, which would not require retroactive revision.

### Other Resources

The adopting release for the amendments can be found on the SEC's Web site at <http://www.sec.gov/rules/final/2008/33-8995.pdf>.

Regulations S-X and S-K can be accessed through the "Corporation Finance" section of the SEC's Web site at <http://www.sec.gov/divisions/corpfin/ecfrlinks.shtml>.

The SEC's forms described above can be accessed on the SEC's Web site at <http://www.sec.gov/about/forms/secforms.htm>.

Compliance and disclosure interpretations related to the amendments can be found on the SEC's website at <http://www.sec.gov/divisions/corpfin/guidance/oilandgas-interp.htm>.

### Contacting the SEC

The SEC's Division of Corporation Finance and Office of the Chief Accountant are available to assist small companies and others with questions regarding the new interactive data submission and posting requirements. You can contact the Division and Offices for this purpose as follows:

Division of Corporation Finance — 202-551-3500 or <https://tts.sec.gov/cgi->

[bin/corp\\_fin\\_interpretive](#)

Office of the Chief Accountant — 202-551-5300 or [OCA@sec.gov](mailto:OCA@sec.gov)

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\* This guide was prepared by the staff of the U.S. Securities and Exchange Commission as a “small entity compliance guide” under Section 212 of the Small Business Regulatory Enforcement Fairness Act of 1996, as amended. The guide summarizes and explains rules adopted by the SEC, but is not a substitute for a rule itself. Only a rule itself can provide complete and definitive information regarding its requirements.

<http://www.sec.gov/info/smallbus/secg/oilgasreporting-secg.htm>

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