

**ATTACHMENT 4 – Revised Exposure Draft,
Accounting for Federal Oil and Gas Resources
Comment Letters**

#	Respondent	Affiliation	Page
1	Osman Masahudu	Dept of Agriculture, Forest Service	63
2	Gerald Tucker	Dept of Housing and Urban Development, OCFO	66
3	Robert Childree	Assoc. of Government Accountants, FMSB	67
4	Mark Easton	Department of Defense, OCFO	73
5	Stefan Silzer	Environmental Protection Agency, OFM	79
6	Jeanette Franzel	Government Accountability Office	80
7	Andrew Lewis	Greater Washington Society of CPAs, FISC	87
8	Bert Edwards	Self	92
9	Dan Fletcher	Dept. of the Interior, CFO	96

[This page intentionally left blank.]

Osman Masahudu
US, Forest Service
Financial Management Staff
Financial Policy and Standards

FASAB Exposure Draft – Accounting for Federal Oil and Gas Resources**U.S Forest Service Comments – Revised****August 25, 2009**

Q1. Forest Service agrees that the value of any given commodity is relative to supply and demand. It is difficult however, to determine the future value of oil and gas because there is a correlation between technical conditions and demand. It is possible that our reliance on oil and gas may be replaced by another resource (technological advancement) that is more efficient and environmentally friendly.

Q2. Forest Service agrees we can estimate the value of royalties known to exist as of the reporting date. However, we need to take into consideration technical conditions that might have impact (positive or negative) on future values.

Q3: No comment.

Q4. Forest Service does not agree permitting federal entities to change their methodologies for valuing estimated federal petroleum royalties. FASAB needs to design a uniform standard methodology for the entire federal government in valuing estimated petroleum royalties. Allowing federal entities to use a different methodology could impair our ability to prepare consolidated financial statements for the federal government.

Q5: No comment.

Q6: No comment.

Q7: No comment.

Q8: No comment.

Q9: No comment.

General Comments

1. One consideration that Forest Service did not see mentioned in the Exposure Draft is the impact of asset value due to legal or management constraints that limit or preclude access to those reserves. For example, Congress recently withdrew the Wyoming Range from all forms of mineral entry and thereby put trillions of cubic feet of gas off limits. As such it could be argued that there is no value for that resource. The Energy Policy and conservation Act mandated a study "Scientific Inventory of Onshore Federal Lands' Oil and Gas Resources and Reserves and the Extent and Nature of Restrictions' or Impediments to Their Development" which evaluated the effects of management constraints have on resource accessibility. Therefore, Forest Service is uncertain how those aspects can be reflected in the asset value of "proven reserves".

2. Another area that needs consideration is that, USSGL posting models and general ledger accounts are not mentioned anywhere in the draft. For example, transfer accounts or receipts between DOI and U.S Forest Service. U.S Forest Service needs to know the general ledger account to use to transfer funds between Forest Service and DOI and vice versa. It is explicit in the draft that transfer receipts would no longer be revenue to the recipient agency after the implementation of this draft however, transfer receipts would be treated as financing source instead of revenue to the recipient agency. U.S Forest Service needs to know what general ledger account to use, to record this transaction so that appropriate posting models as well as cross-walk would be established in our financial accounting system to handle the change.

Thank you for the opportunity to provide comments on the above exposure draft.

The Department of Housing and Urban Development does not have any comment on the above exposure draft.

Please direct any questions concerning our response to me at the number listed below.

Jerry Tucker
Director
Financial Policies and Procedures Division
Office of the Chief Financial Officer for Financial Management

September 4, 2009

Ms. Wendy M. Payne, Executive Director
Federal Accounting Standards Advisory Board
441 G Street, NW, Suite 6814
Washington, DC 20548

Advancing
Government
Accountability

2208 Mount Vernon Ave
Alexandria, VA 22301

(703) 684-6931
(703) 548-9367 (fax)

Dear Ms. Payne:

On behalf of the Association of Government Accountants (AGA), the Financial Management Standards Board (FMSB) appreciates the opportunity to provide comments to the Federal Accounting Standards Advisory Board (FASAB or the Board) on its revised exposure draft on the proposed statement of federal financial accounting standards, *Accounting for Federal Oil and Gas Resources*. The FMSB, comprising 21 members with accounting and auditing backgrounds in federal, state and local government, academia and public accounting, reviews and responds to proposed standards and regulations of interest to AGA members. Local AGA chapters and individual members are also encouraged to comment separately. Our responses to the questions listed in the exposure draft follow

Q1. The original exposure draft (ED) issued on May 21, 2007, contained detailed asset valuation implementation guidance for valuing federal oil and gas resources. As a result of feedback received from field testing efforts, the Board has removed that detailed guidance from this revised ED and is instead proposing to provide federal entities with flexibility in developing the asset valuation estimation methodology due to the constantly changing economic and technical conditions. Do you agree or disagree with the Board's position (see paragraphs 14 through 26, A47 and A48)? Please explain the reasons for your position in as much detail as possible.

Response: The FMSB agrees as those federal entities who have been conducting asset valuation are in the best position to know what works for them and it would be too easy to omit a sound methodology. Trying to incorporate every valuation estimation methodology in use would make the document unwieldy.

Q2. The Board believes that the method for valuing the federal government's estimated petroleum royalties should approximate the present value of future federal royalty receipts on proved reserves known to exist as of the reporting date as described in paragraphs 19 through 21. Discount rates as of the reporting date for present value measurements of federal oil and gas assets and liabilities should be based on interest rates on marketable Treasury securities with maturities consistent with the cash flows being discounted. Do you agree or disagree with the Board's position (see paragraphs 19 through 21 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.

Response: The FMSB agrees as it is a reasonable basis, generally understood and already in widespread use throughout the federal government. Also, we found sample entries 6 through 11 in Appendix B to be very helpful with excellent explanations.

Q3. The Board is proposing to permit an alternative measurement method for valuing the federal government's estimated petroleum royalties if it is not reasonably possible to estimate the present value of future federal royalty receipts on proved reserves using the approach described in paragraphs 19 through 21. Specifically, the Board is permitting a market-based fair value measurement consistent with the Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards 157, *Fair Value Measurements*. Do you agree or disagree with the Board's position (see paragraphs 24 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.

Response: The FMSB disagrees. We reviewed SFAS 157 and find that it is primarily designed for marketable securities. Oil and gas reserves would be a Level 1 asset, with an observable price. But we could not find any information on how to deal with volatile markets. Oil prices have varied between \$31 and \$126 in the past year alone, which is a 4:1 ratio. We did not see any guidance in SFAS 157 that helped determine what market price to use when the market is so volatile. It appears that the market price is arbitrarily set at the closing price on the last day of the fiscal year, which could be meaningless a month later.

Q4. The Board is proposing to permit federal entities to change its methodology for valuing the federal government's estimated petroleum royalties if environmental or other changes would provide for the development of an improved methodology. Do you agree or disagree with the Board's position (see paragraphs 25, 26 and A49 through A51)? Please explain the reasons for your position in as much detail as possible.

Response: The FMSB agrees. A change in accounting estimate that is effected by a change in accounting principle should be made only if the new accounting principle is justifiable on the basis that it is preferable from the viewpoint that the new accounting principle better captures the economic reality of the situation under consideration. That is, if an entity concludes that the pattern of consumption of the expected benefits of an asset has changed, and determines that a new depreciation method better reflects that pattern, it may be justified in making a change in accounting estimate effected by a change in accounting principle.

Q5. The Board believes that it would be appropriate to provide guidance regarding reporting gains and losses from changes in assumptions and selecting the discount rates similar to that provided in SFFAS 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*, to long-term assumptions about oil and gas when using the present value method. Do you agree or disagree with the Board's position (see paragraphs 20, 40, and A64 through A66)? Please explain the reasons for your position in as much detail as possible.

Response: The FMSB agrees. This will help government entities to provide better transparency, improve understandability of the reports by the interested stakeholders and provide guidance during times of high volatility. SFFAS 33 requires that gains and losses from changes in long-term assumptions used to estimate certain liabilities be displayed on the statement of net cost separately from other costs. The FMSB agrees that it would be appropriate to apply similar guidance similar to long-term assumptions about oil and gas in order to increase the usefulness of reported operating results when the volatility of projections might otherwise result in large variations in the valuation of oil and gas royalty revenues, oil and gas resource valuation and resulting gains and losses from year to year. Specific guidance and examples will provide continuity of guidance and procedures.

Q6. SFFAS 31, *Accounting for Fiduciary Activities*, requires that agencies report on assets held in a fiduciary capacity. The Department of Interior (DOI) manages oil and gas resources on behalf of individual Indians and Indian tribes. This proposed standard – because it classifies oil and gas resources as assets – would result in additional information being disclosed for oil and gas assets managed in a fiduciary capacity. Note, however, that fiduciary reporting does not extend to inclusion of the additional disclosures or RSI that are proposed in this document for federal oil and gas resources. Thus, with respect to fiduciary activities, only disclosure of the assets, liabilities, and related inflows and outflows would result from this proposal.

Some members have expressed concern that the costs may exceed the benefits of disclosing fiduciary assets and liabilities measured in conformance with this proposed standard. Since this proposal may significantly increase the fiduciary assets disclosed, we requested input on the cost-benefit of the requirement with respect to fiduciary activities in the May 2007 ED. One respondent was in favor of the disclosures while four expressed their opinion that the information would most likely not be cost-beneficial. However, the Board has not received any substantive information to enable it to make an informed decision regarding cost/benefit.

Since the removal of the fiduciary oil and gas resource disclosure requirements would require an exception to the requirements of SFFAS 31, we are again requesting detailed input on the cost-benefit of the requirement with respect to fiduciary activities. See paragraph 46.

Response: The FMSB agrees from the viewpoint of maintaining consistency with SFFAS 31 and existing systems should make the cost benefit a moot point. However, we believe only those within DOI can provide the in-depth information or justification as to why the cost/benefit analysis would override providing the transparency to the individual Indians and Indian tribes who most benefit from disclosure of the information.

Q7. The Board is proposing to provide a three-year phase-in of the proposed requirements from required supplementary information (RSI) beginning with fiscal year 2011 to basic in fiscal year 2014. This transitional period is being provided to allow for the asset valuation methodology to be improved upon before an audit opinion is required. Do you agree or disagree with the Board's position (see paragraphs 51 and A87)? Please explain the reasons for your position in as much detail as possible.

Response: The FMSB agrees as it allows sufficient time for any implementation questions to be addressed by the Board, accommodates DOI's request and seems a reasonable phase-in period.

Q8. This Statement addresses accounting for federal oil and gas resources only. While the Board may address accounting for other types of natural resources at some point in the future, the majority of the members acknowledge that it is not likely that a project devoted to other categories of natural resources will be marked as a high priority at future agenda-setting sessions due to their lesser significance. As a result, while not explicitly encouraging agencies to recognize other categories of natural resources, the Board included paragraph 10 to explicitly state that this Statement does not preclude entities from recognizing or otherwise reporting information about other types of federally-owned natural resources. Do you agree or disagree that the potential risk that the inclusion of paragraph 10 might lead to inaccurate or inconsistent reporting of other types of natural resources is outweighed by the potential benefits to financial statement users (see paragraphs 10, A9 and A10)? Please explain the reasons for your position in as much detail as possible.

Response: The FMSB does agree with the inclusion of paragraph 10 as the proposed standard needs to be specific in addressing the high-priority issues concerning accounting for federal oil and gas resources. We believe the issue of accounting for other types of natural resources, where material to the reporting entities, should be addressed as soon as practicable in the future, given the level of their significance. We have evidence that one agency had not updated some natural resource lease valuations in over twenty years - which raises questions about its stewardship and the accuracy of its financial statements. It is likely that there are a number of smaller agencies with similar issues. Even a brief standard should address regular review and update of costing and valuation of all federal natural resources to ensure that the government is receiving fair remuneration.

Q9. After a three-year transition period of reporting as RSI, the ED proposes to recognize an asset on the balance sheet for the federal government's royalty share of federal oil and gas resources under lease (see paragraphs A29 through A37 for a discussion of factors regarding asset recognition considered by the Board in reaching this conclusion). An alternative view prepared by Mr. Dacey proposes that the value of federal oil and gas resources and annual changes therein be reported as RSI for a three-year transition period and then disclosed as basic information in the notes, rather than recognized on the face of the financial statements. The notes would be part of an integrated disclosure that would include the discussion of all of the government's natural resources, including oil and gas resources that are not currently under lease as well as values and information concerning all other significant natural resources, such as coal, timber, and grazing rights. Do you agree or disagree with the alternative view (see paragraphs A89 through A92)? Please explain the reasons for your position in as much detail as possible.

Response: The Introduction to the Exposure Draft states "Extensive federal oil and gas resources exist on public lands throughout the country and on the Outer Continental Shelf (OCS). Currently, federal financial reporting does not provide information about the quantity or value of these assets. In addition, royalty revenues are recognized but expenses are not recognized for the asset exchanged to produce those revenues. [interpretive note: largely depletion]"

We accept that the quantity and value of those assets and the royalty revenues, and [depletion] expenses that will be recognized for the asset exchanged to produce those revenues, would be material to the Financial Statements of the entities reporting those items (the omission or misstatement of that information about the item makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or the misstatement.)

On that basis we disagree with the alternative view and agree with the ED proposal that the federal government's royalty share of federal oil and gas resources under lease be recognized as an asset on the balance sheet (after the 3 year transition period). However, to address the legitimate issues that Mr. Dacey has raised, we think that a discussion of all of the government's natural resources, including oil and gas resources that are not currently under lease as well as values and information concerning all other significant natural resources, such as coal, timber, and grazing rights should be provided in the Notes to the Financial Statements. We support the FASAB addressing issues of accounting for natural resources *additional to* those addressed by the current Exposure Draft as soon as practicable in the future, given the level of their significance. We are concerned that treating those additional natural resources only by note disclosure gives them the character of "contingent assets", while we do not believe they meet the criteria of being contingent, and that reliable estimates of their value can and should be made, with appropriate disclosure as to the methodology used.

We appreciate the opportunity to comment on this document and would be pleased to discuss this letter with you at your convenience. No member objected to its issuance. If you have questions concerning the letter, please contact Anna D. Gowans Miller, CPA, AGA's director of research and staff liaison for the FMSB, at amiller@agacgfm.org or 703.684.6931 ext. 313.

Sincerely,



Robert L. Childree, Chair,
AGA Financial Management Standards Board

cc: William A. Morehead, Ph.D., CPA, CGFM
AGA National President

**Association of Government Accountants
Financial Management Standards Board**

July 2009 – June 2010

Robert L. Childree, Chair
Katherine J. Anderson
Frank D. Banda
Eric S. Berman
Irwin T. David
Michael H. Granof
Jeffrey W. Green
David C. Horn
David R. Hancox
Albert A. Hrabak
Drummond Kahn
Simcha Kuritzky
Valerie A. Lindsey
Jeffrey A. Long
Edward J. Mazur
Craig M. Murray
Suesan R. Patton
Leslie I. Tanaka
Clarence L. Taylor, Jr.
Roger Von Elm
Stephen B. Watson

Relmond P. Van Daniker, Executive Director, AGA (Ex-Officio Member)
Anna D. Gowans Miller, Technical Manager, AGA, Staff Liaison



COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE
1100 DEFENSE PENTAGON
WASHINGTON, DC 20301-1100

SEP 08 2009

Ms. Wendy M. Payne
Executive Director
Federal Accounting Standards Advisory Board
441 G Street, NW, Suite 6814
Mail stop 6K17V
Washington, DC 20548

Dear Ms. Payne:

The Department of Defense's comments on the Exposure Draft, *Accounting for Federal Oil and Gas Resources*, are enclosed. Overall, we agree with the valuation methodologies proposed in the Exposure Draft. We believe the proposed changes will improve the reporting of this revenue in Federal financial reports.

We do, however, prefer the proposed alternative view in which the asset is disclosed in the notes to the financial statements in lieu of balance sheet recognition. Further, we believe that this Exposure Draft provides a reasonable foundation for the reporting of other types of natural resources assets.

My point of contact on this matter is Ms. Debra J. Carey. She can be reached at (703) 602-0155 or debra.carey@osd.mil.

Sincerely,

A handwritten signature in black ink, appearing to read "Mark E. Easton", written over a horizontal line.

Mark E. Easton
Deputy Chief Financial Officer

Enclosure:
As stated



**Accounting for Federal Oil and Gas Resources
Department of Defense Responses to Specific Questions**

Q1. The original exposure draft (ED) issued on May 21, 2007, contained detailed asset valuation implementation guidance for valuing federal oil and gas resources. As a result of feedback received from field testing efforts, the Board has removed that detailed guidance from this revised ED and is instead proposing to provide federal entities with flexibility in developing the asset valuation estimation methodology due to the constantly changing economic and technical conditions. Do you agree or disagree with the Board's position (see paragraphs 14 through 26, A47 and A48)? Please explain the reasons for your position in as much detail as possible.

A. The Department of Defense (DoD) concurs with this revision. We agree with the guidance proposed in the current Exposure Draft which provides agencies with the flexibility to determine appropriate and reasonable valuation methodologies.

Q2. The Board believes that the method for valuing the federal government's estimated petroleum royalties should approximate the present value of future federal royalty receipts on proved reserves known to exist as of the reporting date as described in paragraphs 19 through 21. Discount rates as of the reporting date for present value measurements of federal oil and gas assets and liabilities should be based on interest rates on marketable Treasury securities with maturities consistent with the cash flows being discounted. Do you agree or disagree with the Board's position (see paragraphs 19 through 21 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.

A. DoD concurs that the discount rate for any present value measurements of federal oil and gas assets and liabilities should be based on interest rates on marketable Treasury securities with maturities consistent with the cash flows being discounted. DoD also concurs that the present value of future federal royalty receipts on proved reserves is an appropriate and reasonable valuation methodology, subject to the response to question 3.

Q3. The Board is proposing to permit an alternative measurement method for valuing the federal government's estimated petroleum royalties if it is not reasonably possible to estimate the present value of future federal royalty receipts on proved reserves using the approach described in paragraphs 19 through 21. Specifically, the Board is permitting a market-based fair value measurement consistent with the Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards 157, Fair Value

Measurements. Do you agree or disagree with the Board's position (see paragraphs 24 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.

A. DoD concurs with this proposal. Specifically, we believe that either the present value of future federal royalty receipts or a market-based fair value measurement should be acceptable.

However, we do not concur with the language currently in paragraph 24 of the Exposure Draft. This paragraph states that the alternative method described "may be acceptable if it is not reasonably possible" to estimate the present value of future federal royalty receipts on proved reserves. This language, especially the phrases "may be acceptable" and "not reasonably possible" does not clearly state that the alternative is acceptable while placing a high burden of proof on the agency before this alternative may be used. The Basis for Conclusions indicates that the Board considers either approach acceptable. If the intent of the Board is that either approach is acceptable, then that intent should be clearly stated in the text of the standard. The presentation of limitations on the applicability of the alternate method merely creates opportunities for disagreements in judgment between preparers and auditors, which may effectively prevent the use of this alternative.

Again, DoD believes that either approach should be acceptable if adequately disclosed. This flexibility will be especially important if the provisions of this standard are applied to other less significant categories of natural resources as permitted by paragraph 10.

Q4. The Board is proposing to permit federal entities to change its methodology for valuing the federal government's estimated petroleum royalties if environmental or other changes would provide for the development of an improved methodology. Do you agree or disagree with the Board's position (see paragraphs 25, 26 and A49 through A51)? Please explain the reasons for your position in as much detail as possible.

A. DoD concurs with this proposal. Provided that adequate disclosure is made of the change in accounting methodology, this proposal will ensure the presentation of the most meaningful information to users of financial reports.

Q5. The Board believes that it would be appropriate to provide guidance regarding reporting gains and losses from changes in assumptions and selecting the discount rates similar to that provided in SFFAS 33, Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions

and Selecting Discount Rates and Valuation Dates, to long-term assumptions about oil and gas when using the present value method. Do you agree or disagree with the Board's position (see paragraphs 20, 40, and A64 through A66)? Please explain the reasons for your position in as much detail as possible.

A. DoD concurs with the proposed guidance regarding reporting gains and losses from changes in assumptions. If the asset is to be presented on the Balance Sheet, the changes in asset value must be reflected in the financial statements, preferably on the Statement of Net Cost of Operations. These changes, although often material, are normally unrelated to the operation of the program. Clear disclosure of these amounts on the Statement of Net Cost would improve the quality of information provided to the user of the financial statements.

Q6. SFFAS 31, Accounting for Fiduciary Activities, requires that agencies report on assets held in a fiduciary capacity. The Department of Interior (DOI) manages oil and gas resources on behalf of individual Indians and Indian tribes. This proposed standard – because it classifies oil and gas resources as assets – would result in additional information being disclosed for oil and gas assets managed in a fiduciary capacity. Note, however, that fiduciary reporting does not extend to inclusion of the additional disclosures or RSI that are proposed in this document for federal oil and gas resources. Thus, with respect to fiduciary activities, only disclosure of the assets, liabilities, and related inflows and outflows would result from this proposal.

Some members have expressed concern that the costs may exceed the benefits of disclosing fiduciary assets and liabilities measured in conformance with this proposed standard. Since this proposal may significantly increase the fiduciary assets disclosed, we requested input on the cost-benefit of the requirement with respect to fiduciary activities in the May 2007 ED. One respondent was in favor of the disclosures while four expressed their opinion that the information would most likely not be cost-beneficial. However, the Board has not received any substantive information to enable it to make an informed decision regarding cost/benefit.

Since the removal of the fiduciary oil and gas resource disclosure requirements would require an exception to the requirements of SFFAS 31, we are again requesting detailed input on the cost-benefit of the requirement with respect to fiduciary activities. See paragraph 46.

A. DoD does not concur with the proposal to report Fiduciary Natural Resource Assets. DoD does not see a benefit to this disclosure, since the data would be too summarized to provide meaningful information to fiduciary beneficiaries. However, since DoD does not

have Fiduciary Natural Resource assets to report under this standard, the cost of developing that information cannot be estimated.

Q7. The Board is proposing to provide a three-year phase-in of the proposed requirements from required supplementary information (RSI) beginning with fiscal year 2011 to basic in fiscal year 2014. This transitional period is being provided to allow for the asset valuation methodology to be improved upon before an audit opinion is required. Do you agree or disagree with the Board's position (see paragraphs 51 and A87)? Please explain the reasons for your position in as much detail as possible.

A. DoD concurs with the three-year phase in of the proposed requirements, as this phase-in period will permit agencies to test and refine asset valuation methodologies. This phase in period is necessary whether the information is presented in the basic Financial Statements, as proposed by the Exposure Draft, or in the Notes to the Financial Statements, as proposed by the alternative view.

Q8. This Statement addresses accounting for federal oil and gas resources only. While the Board may address accounting for other types of natural resources at some point in the future, the majority of the members acknowledge that it is not likely that a project devoted to other categories of natural resources will be marked as a high priority at future agenda-setting sessions due to their lesser significance. As a result, while not explicitly encouraging agencies to recognize other categories of natural resources, the Board included paragraph 10 to explicitly state that this Statement does not preclude entities from recognizing or otherwise reporting information about other types of federally-owned natural resources. Do you agree or disagree that the potential risk that the inclusion of paragraph 10 might lead to inaccurate or inconsistent reporting of other types of natural resources is outweighed by the potential benefits to financial statement users (see paragraphs 10, A9 and A10)? Please explain the reasons for your position in as much detail as possible.

A. DoD concurs with the provision of paragraph 10 for other types of natural resource assets. This provision gives agencies the ability to recognize natural resource assets determined by the agency to be significant to the operations and financial position of the agency. The management and sale of Natural Resources are ancillary to most Federal agency missions and are generally immaterial to the agency from both a financial and operational stand point. Paragraph 10 gives management the responsibility for the determination of whether to recognize such assets. DoD believes this flexibility will result in presentation decisions most useful to users of Federal financial statements.

In addition, DoD proposes that footnote disclosure of other types of Natural Resource assets in lieu of Balance Sheet recognition be clearly stated as permissible, even if this presentation (as described in the Alternative View) is not accepted for Oil and Gas Resources.

Q9. After a three-year transition period of reporting as RSI, the ED proposes to recognize an asset on the balance sheet for the federal government's royalty share of federal oil and gas resources under lease (see paragraphs A29 through A37 for a discussion of factors regarding asset recognition considered by the Board in reaching this conclusion). An alternative view prepared by Mr. Dacey proposes that the value of federal oil and gas resources and annual changes therein be reported as RSI for a three-year transition period and then disclosed as basic information in the notes, rather than recognized on the face of the financial statements. The notes would be part of an integrated disclosure that would include the discussion of all of the government's natural resources, including oil and gas resources that are not currently under lease as well as values and information concerning all other significant natural resources, such as coal, timber, and grazing rights. Do you agree or disagree with the alternative view (see paragraphs A89 through A92)? Please explain the reasons for your position in as much detail as possible.

A. DoD concurs with the alternative view, including the transition period and footnote disclosure of the asset in lieu of Balance Sheet recognition of Natural Resource assets. While Balance Sheet recognition improves information available to users of financial statements regarding the assets managed by the agency, this recognition has a negative impact on the Statement of Net Cost (SNC). Specifically, the SNC is impacted by periodic changes in recognized value of the asset, distorting the activity resulting from the activities of the agency. These changes result from changes in interest rates and changes in amounts considered to be "proved reserves" offset by resources extracted and sold. Disclosure of Natural Resource assets in the Notes to the Financial Statements in lieu of Balance Sheet recognition would provide users of financial statements information regarding the value of the assets without the corresponding negative impact on the SNC.

>>> <Gillam.Constance@epamail.epa.gov> 9/8/2009 2:12 PM >>>

Good afternoon.

On behalf of Stefan Silzer, the Acting Director of the Office of Financial Management, thank you for the opportunity to review the exposure draft, "Accounting for Federal Oil and Gas Resources." EPA has no comments on this draft.

Constance Gillam
Special Assistant to the Director
U.S. EPA Office of Financial Management
1200 Pennsylvania Avenue
Washington, D.C. 20460



G A O

Accountability • Integrity • Reliability

United States Government Accountability Office
Washington, DC 20548

September 8, 2009

Ms. Wendy M. Payne
Executive Director
Federal Accounting Standards Advisory Board
441 G Street, NW, Suite 6814
Washington, DC 20548

Dear Ms. Payne:

The U.S. Government Accountability Office (GAO) is pleased to provide its comments on the Federal Accounting Standards Advisory Board (FASAB) Exposure Draft entitled *Accounting for Federal Oil and Gas Resources*, (ED). The FASAB's current efforts and deliberations on the presentation of oil and gas resources are an important step in recognizing the need for greater transparency in connection with the federal government's current financial condition and future fiscal path.

Consistent with the alternative view in the ED, we believe that the notes to the financial statements should include an integrated disclosure of all of the federal government's natural resources, including information on the value of resources under lease and changes therein, rather than recognize on the balance sheet only those resources that are valued because they are under lease. In addition, natural resources should be excluded from reporting on the schedule of fiduciary net assets.

The enclosure to this letter provides our responses to the questions set forth in the Exposure Draft. If you have any questions, please call me at (202) 512-2600 or Robert Dacey, Chief Accountant at (202) 512-7439.

Sincerely yours,

Jeanette Franzel
Managing Director
Financial Management and Assurance

Enclosure

Enclosure**GAO Responses to the Questions set forth in the Exposure Draft,
Accounting for Federal Oil and Gas Resources****Question 1:**

The original exposure draft (ED) issued on May 21, 2007, contained detailed asset valuation implementation guidance for valuing federal oil and gas resources. As a result of feedback received from field testing efforts, the Board has removed that detailed guidance from this revised ED and is instead proposing to provide federal entities with flexibility in developing the asset valuation estimation methodology due to the constantly changing economic and technical conditions. Do you agree or disagree with the Board's position (see paragraphs 14 through 26, A47 and A48)? Please explain the reasons for your position in as much detail as possible.

Response:

We agree with providing flexibility in the valuation estimation methodology. However, as discussed in our comments, we believe that such valuation information is more appropriately presented in the notes to the financial statements as part of an integrated disclosure of all federal natural resources rather than reported on the balance sheet.

Question 2:

The Board believes that the method for valuing the federal government's estimated petroleum royalties should approximate the present value of future federal royalty receipts on proved reserves known to exist as of the reporting date as described in paragraphs 19 through 21. Discount rates as of the reporting date for present value measurements of federal oil and gas assets and liabilities should be based on interest rates on marketable Treasury securities with maturities consistent with the cash flows being discounted. Do you agree or disagree with the Board's position (see paragraphs 19 through 21 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.

Response:

Yes, the method proposed for valuing estimated petroleum royalties allows sufficient flexibility in measurement methods and appears reasonable. Also, we caution that the Board's current project on measurement attributes, when completed, may affect how requirements for applying measurement methods in current standards are applied. However, as discussed in our comments, we believe that such valuation information is more appropriately presented in the notes to the financial statements as part of an integrated disclosure of all federal natural resources rather than reported on the balance sheet.

Question 3:

The Board is proposing to permit an alternative measurement method for

valuing the federal government's estimated petroleum royalties if it is not reasonably possible to estimate the present value of future federal royalty receipts on proved reserves using the approach described in paragraphs 19 through 21. Specifically, the Board is permitting a market-based fair value measurement consistent with the Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards 157, *Fair Value Measurements*. Do you agree or disagree with the Board's position (see paragraphs 24 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.

Response:

Yes, the alternative method appears reasonable and allows sufficient flexibility for valuing federal estimated petroleum royalties if it is not reasonably possible to estimate present value of future federal royalty receipts on proved reserves using the methodology described in paragraphs 19-21. However, as discussed in our comments, we believe that such valuation information is more appropriately presented in the notes to the financial statements as part of an integrated disclosure of all federal natural resources rather than reported on the balance sheet. One of the reasons for our views is that such significant flexibility, in combination with paragraphs 25 and 26 of the ED, provides a potentially broad range of acceptable accounting bases and valuation methodologies and consequently is better presented in the notes to the financial statements

Question 4:

The Board is proposing to permit federal entities to change its methodology for valuing the federal government's estimated petroleum royalties if environmental or other changes would provide for the development of an improved methodology. Do you agree or disagree with the Board's position (see paragraphs 25, 26 and A49 through A51)? Please explain the reasons for your position in as much detail as possible.

Response:

Yes, allowing a change in methodology is reasonable as long as the nature and reason for the change and its effect are properly disclosed. However, as discussed in our comments (including our response to question 4), we believe that such valuation information is more appropriately presented in the notes to the financial statements as part of an integrated disclosure of all federal natural resources rather than reported on the balance sheet.

Question 5:

The Board believes that it would be appropriate to provide guidance regarding reporting gains and losses from changes in assumptions and selecting the discount rates similar to that provided in SFFAS 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*, to long-term assumptions about oil and gas when using the present value method. Do you agree or disagree with the Board's position (see paragraphs 20, 40, and A64 through A66)? Please explain the reasons for your position in as much detail as possible.

Response:

It would be appropriate to present gains and losses from changes in long-term assumptions as a separate line item or items on the statement of net cost, if the valuation of oil and gas resources were placed on the balance sheet. However, as discussed elsewhere in this letter, we believe that such valuation information is more appropriately presented in the notes to the financial statements as part of an integrated disclosure of all federal natural resources rather than reported on the balance sheet.

Question 6:

SFFAS 31, *Accounting for Fiduciary Activities*, requires that agencies report on assets held in a fiduciary capacity. The Department of Interior (DOI) manages oil and gas resources on behalf of individual Indians and Indian tribes. This proposed standard – because it classifies oil and gas resources as assets – would result in additional information being disclosed for oil and gas assets managed in a fiduciary capacity. Note, however, that fiduciary reporting does not extend to inclusion of the additional disclosures or RSI that are proposed in this document for federal oil and gas resources. Thus, with respect to fiduciary activities, only disclosure of the assets, liabilities, and related inflows and outflows would result from this proposal. Some members have expressed concern that the costs may exceed the benefits of disclosing fiduciary assets and liabilities measured in conformance with this proposed standard. Since this proposal may significantly increase the fiduciary assets disclosed, we requested input on the cost-benefit of the requirement with respect to fiduciary activities in the May 2007 ED. One respondent was in favor of the disclosures while four expressed their opinion that the information would most likely not be cost-beneficial. However, the Board has not received any substantive information to enable it to make an informed decision regarding cost/benefit. Since the removal of the fiduciary oil and gas resource disclosure requirements would require an exception to the requirements of SFFAS 31, we are again requesting detailed input on the cost-benefit of the requirement with respect to fiduciary activities. See paragraph 46.

Response:

We continue to have concerns about the costs versus the benefits of accumulating, preparing, and auditing information reported in the schedule of fiduciary activities. Requiring the Federal entities to disclose the value of oil and gas reserves for fiduciary activities will incur additional preparation and audit costs and result in information that is inconsistent with information currently reported to beneficiaries of these fiduciary activities. In addition, it will reflect only the value of reserves for which the entity has fiduciary responsibility, which may not represent all reserves owned by beneficiaries. For example, it would place a heavy burden on the Federal Government to put a value on what beneficiaries own. Therefore, for these reasons and the reasons discussed in the ED, such natural resources should be excluded from reporting as assets on the schedule of fiduciary net assets. Instead, fiduciary reporting of natural resources should consist of appropriate narrative describing the general nature and extent of such resources.

Question 7:

The Board is proposing to provide a three-year phase-in of the proposed requirements from required supplementary information (RSI) beginning with fiscal year 2011 to basic in fiscal year 2014. This transitional period is being provided to allow for the asset valuation methodology to be improved upon before an audit opinion is required. Do you agree or disagree with the Board's position (see paragraphs 51 and A87)? Please explain the reasons for your position in as much detail as possible.

Response:

Phasing in the requirements is very important to the reporting of the oil and gas resources. However, for reasons discussed in our comments, we believe the value of federal oil and gas resources and annual changes therein should be disclosed as basic information in notes rather than recognized on the face of the financial statements.

Question 8:

This Statement addresses accounting for federal oil and gas resources only. While the Board may address accounting for other types of natural resources at some point in the future, the majority of the members acknowledge that it is not likely that a project devoted to other categories of natural resources will be marked as a high priority at future agenda-setting sessions due to their lesser significance. As a result, while not explicitly encouraging agencies to recognize other categories of natural resources, the Board included paragraph 10 to explicitly state that this Statement does not preclude entities from recognizing or otherwise reporting information about other types of federally owned natural resources. Do you agree or disagree that the potential risk that the inclusion of paragraph 10 might lead to inaccurate or inconsistent reporting of other types of natural resources is outweighed by the potential benefits to financial statement users (see paragraphs 10, A9 and A10)? Please explain the reasons for your position in as much detail as possible.

Response:

We believe that the notes should have a comprehensive disclosure that would include an integrated discussion of all of the government's natural resources, including oil and gas resources that are not currently under lease as well as values and information concerning all other significant natural resources, such as coal, timber, and grazing rights. Such information should include, as appropriate, valuation of other types of natural resources under lease, unless they are not material.

Question 9:

After a three-year transition period of reporting as RSI, the ED proposes to recognize an asset on the balance sheet for the federal government's royalty share of federal oil and gas resources under lease (see paragraphs A29 through A37 for a discussion of factors regarding asset recognition considered by the Board in reaching this conclusion). An alternative view prepared by Mr. Dacey proposes that the value of federal oil and gas resources and annual changes therein be reported as RSI for a three-year transition period and then disclosed as basic information in the notes,

rather than recognized on the face of the financial statements. The notes would be part of an integrated disclosure that would include the discussion of all of the government's natural resources, including oil and gas resources that are not currently under lease as well as values and information concerning all other significant natural resources, such as coal, timber, and grazing rights. Do you agree or disagree with the alternative view (see paragraphs A89 through A92)? Please explain the reasons for your position in as much detail as possible.

Response:

As discussed in the ED, we believe that the value of federal oil and gas resources and annual changes therein, consistent with the valuation basis discussed in the ED, should be disclosed as basic information in the notes rather than recognized on the face of the financial statements as proposed in this ED. The disclosures should include an integrated discussion of all of the federal government's natural resources, including oil and gas resources that are not currently under lease as well as values for resources under lease and similar information concerning all other significant federal natural resources, such as coal, timber, and grazing rights. This type of reporting would be similar to current reporting for stewardship assets. Such reporting in the notes would provide transparency as to the value and changes in value of these significant assets and result in information that contributes to meeting federal financial reporting objectives. As basic financial information, this information would be subject to audit. Similar to stewardship assets, FASAB could require a non-financial disclosure on the balance sheet that refers to the note without an asset dollar amount being shown.

The ED includes a discussion of the reasoning for reporting this information in the notes in paragraph A91. In summary,

- financial statement users should clearly understand the full extent of natural resources that are owned by the federal government and the valuation of the resources that are currently under lease and not be potentially misled by an amount on the balance sheet that represents only a portion of the federal government's natural resources,
- the current recognition of oil and gas royalties at the time of extraction when royalties are receivable relates the revenues to the period benefitted and are matched with related costs incurred by the federal government; also, bonus bid and rent are recorded when receivable,
- the valuation of oil and gas resources is subject to significant annual fluctuations based on changing market prices for the resources and changes in quantities based on recoverability; such fluctuations would affect the federal government's net cost and net operating cost (thereby reducing the usefulness of reported operating results of the government's operations during the year); and the valuation would not likely reflect the value of the royalties to be received in future periods, and
- in addition to significant uncertainty inherent in the valuation methodology, the ED provides for significant flexibility in the basis used to calculate the valuation; consequently, such less certain information would be more appropriately reflected in the notes to the financial statements.

Further, publicly traded enterprises that have significant oil and gas producing activities are required to disclose information on proved oil and gas reserve quantities and discounted future net cash flows as supplementary information, rather than record them on the balance sheet.



Greater Washington Society of CPAs and GWSCPA Educational Foundation

1111 19th Street, NW, Suite 1200, Washington, DC 20036
202-464-6001 (v) 202-238-9604 (f) www.gwscpa.org info@gwscpa.org

September 8, 2009

Wendy Payne, Executive Director
Federal Accounting Standards Advisory Board
Mail Stop 6K17V
441 G Street, NW – Suite 6814
Washington, DC 20548

Dear Ms. Payne:

The Greater Washington Society of Certified Public Accountants (GWSCPA) Federal Issues and Standards Committee (FISC) appreciates the opportunity to provide comments on the Federal Accounting Standards Advisory Board's (FASAB or Board) revised Exposure Draft (ED) of the proposed standard, *Accounting for Federal Oil and Gas Reserves*.

FISC consists of 16 GWSCPA members who are active in accounting and auditing in the Federal sector. This comment letter represents the consensus comments of our members. Our responses to the ED question follows.

- Q1. The original exposure draft (ED) issued on May 21, 2007, contained detailed asset valuation implementation guidance for valuing federal oil and gas resources. As a result of feedback received from field testing efforts, the Board has removed that detailed guidance from this revised ED and is instead proposing to provide federal entities with flexibility in developing the asset valuation estimation methodology due to the constantly changing economic and technical conditions. Do you agree or disagree with the Board's position (see paragraphs 14 through 26, A47 and A48)? Please explain the reasons for your position in as much detail as possible.
- A1. FISC agrees with the flexibility provided in the current ED, and supports ongoing efforts by the FASAB to adopt 'principles-based' standards. FISC repeats our concerns expressed in our January 23, 2008 response to the initial ED (dated May 21, 2007) that actual journal entries are not necessary if properly described in the eventual standard. We believe that a FASAB Implementation Guide or Department of Treasury (Treasury) or Office of Management and Budget (OMB) directive should address journal entries to insure that entries meet Treasury's Standard General Ledger (SGL) requirements.
- Q2. The Board believes that the method for valuing the federal government's estimated petroleum royalties should approximate the present value of future federal royalty receipts on proved reserves known to exist as of the reporting date as described in paragraphs 19 through 21.

Discount rates as of the reporting date for present value measurements of federal oil and gas assets and liabilities should be based on interest rates on marketable Treasury securities with maturities consistent with the cash flows being discounted. Do you agree or disagree with the Board's position (see paragraphs 19 through 21 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.

- A2. FISC agrees with the current ED to require present value measurements as of the reporting date using discount rates from a common source, namely the marketable Treasury securities. Absent the explicit reference to a common source, FISC members expressed concerns that arbitrary or inconsistent determinations might be used by Federal agencies. As discussed in our response to questions 3 and 4, the current ED provides too much latitude by the preparers to use potentially contradictory methodologies for valuing natural resources.
- Q3. The Board is proposing to permit an alternative measurement method for valuing the federal government's estimated petroleum royalties if it is not reasonably possible to estimate the present value of future federal royalty receipts on proved reserves using the approach described in paragraphs 19 through 21. Specifically, the Board is permitting a market-based fair value measurement consistent with the Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards 157, *Fair Value Measurements*. Do you agree or disagree with the Board's position (see paragraphs 24 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.
- A3. FISC agrees that an alternative measurement method is appropriate due to the complexity and unique situations faced by different Federal agencies. However, FISC recommends that stronger or more explicit language be included in the final standard that would explain what circumstances or situations might make it 'reasonably possible' for a Federal agency to avoid use of the preferred measurement method. Further, FISC members advise that there is a significant disparity between the defined steps in the preferred measurement method and the open-ended reference in the ED to FASB's Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*. FISC recommends that the final standard provide more definite reference to paragraphs, sections, or methods contained in SFAS No. 157 that would be acceptable to the Board.
- Q4. The Board is proposing to permit federal entities to change its methodology for valuing the federal government's estimated petroleum royalties if environmental or other changes would provide for the development of an improved methodology. Do you agree or disagree with the Board's position (see paragraphs 25, 26 and A49 through A51)? Please explain the reasons for your position in as much detail as possible.
- A4. FISC supports including the broad provisions of paragraph 25, allowing for an "improved methodology" based upon environmental or other changes. FISC believes that it is important that Federal agencies be provided the latitude to use the most accurate methodology for estimating future federal royalty receipts on proven reserves.
- Q5. The Board believes that it would be appropriate to provide guidance regarding reporting gains and losses from changes in assumptions and selecting the discount rates similar to that provided in SFFAS 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*, to long-term assumptions about oil and gas when using

the present value method. Do you agree or disagree with the Board's position (see paragraphs 20, 40, and A64 through A66)? Please explain the reasons for your position in as much detail as possible.

- A5. FISC supports the financial statement presentation of gains and losses from changes in assumptions, but encourages the Board to consider segregating unrealized gains and losses from operating results on the Statement of Net Cost. FISC believes that commingling unrealized gains and losses with operating results could confuse a reader of federal financial statements, and cause a reader to draw a false understanding of the annual operating costs or deficit of a Federal agency. The process of segregating unrealized transactions from operating results would parallel the Board's proposal to separate the reporting of social insurance balances, as was proposed by the Board in its recent exposure draft of a proposed standard, *Accounting for Social Insurance, Revised*.
- Q6. SFFAS 31, *Accounting for Fiduciary Activities*, requires that agencies report on assets held in a fiduciary capacity. The Department of Interior (DOI) manages oil and gas resources on behalf of individual Indians and Indian tribes. This proposed standard – because it classifies oil and gas resources as assets – would result in additional information being disclosed for oil and gas assets managed in a fiduciary capacity. Note, however, that fiduciary reporting does not extend to inclusion of the additional disclosures or RSI that are proposed in this document for federal oil and gas resources. Thus, with respect to fiduciary activities, only disclosure of the assets, liabilities, and related inflows and outflows would result from this proposal.

Some members have expressed concern that the costs may exceed the benefits of disclosing fiduciary assets and liabilities measured in conformance with this proposed standard. Since this proposal may significantly increase the fiduciary assets disclosed, we requested input on the cost-benefit of the requirement with respect to fiduciary activities in the May 2007 ED. One respondent was in favor of the disclosures while four expressed their opinion that the information would most likely not be cost-beneficial. However, the Board has not received any substantive information to enable it to make an informed decision regarding cost/benefit.

Since the removal of the fiduciary oil and gas resource disclosure requirements would require an exception to the requirements of SFFAS 31, we are again requesting detailed input on the cost-benefit of the requirement with respect to fiduciary activities. See paragraph 46.

- A6. FISC supports the current ED, which requires that assets, including oil and gas resources, which are held in a fiduciary capacity be reported in accordance with the provisions of SFFAS No. 31 using the valuation methods contained in the current ED (subject to the comments made in our answers to questions 3 and 4 above). Although we appreciate the concerns regarding cost-benefit considerations, comparability in reporting is vital, and inconsistently applied measurement methods for equivalent assets would be confusing to a reader of the financial statements.

However, one of our members disagreed with this response. One member expressed concerns that there is no explanation in the ED as to why FASAB would depart from the private sector's recording of non-monetary assets held in trust, in accordance with the *Uniform Principal and Income Act* (the Act), which provides guidance on fiduciaries. According to this member, the Act is very clear that fiduciaries are responsible for assets received by them, but are not responsible for the value of non-cash assets (although they will normally report the

value of readily marketable securities). Residences and real estate improvements, land and forestry holdings, and other assets are merely disclosed, but only rarely valued. Requiring U.S. government fiduciary funds to record the discounted value of proven reserves would be in conflict to practices under the Act and at odds with comparable fiduciaries outside of the United States Government.

- Q7. The Board is proposing to provide a three-year phase-in of the proposed requirements from required supplementary information (RSI) beginning with fiscal year 2011 to basic in fiscal year 2014. This transitional period is being provided to allow for the asset valuation methodology to be improved upon before an audit opinion is required. Do you agree or disagree with the Board's position (see paragraphs 51 and A87)? Please explain the reasons for your position in as much detail as possible.
- A7. FISC supports the proposed requirements of a phased-in reporting approach to allow key agencies sufficient time to address challenges in implementation of this ED, and to work with the auditors to develop an approach that allows for the agencies' methodologies to be reviewed by the auditors prior to inclusion in the basic financial statements or footnotes.
- Q8. This Statement addresses accounting for federal oil and gas resources only. While the Board may address accounting for other types of natural resources at some point in the future, the majority of the members acknowledge that it is not likely that a project devoted to other categories of natural resources will be marked as a high priority at future agenda-setting sessions due to their lesser significance. As a result, while not explicitly encouraging agencies to recognize other categories of natural resources, the Board included paragraph 10 to explicitly state that this Statement does not preclude entities from recognizing or otherwise reporting information about other types of federally-owned natural resources. Do you agree or disagree that the potential risk that the inclusion of paragraph 10 might lead to inaccurate or inconsistent reporting of other types of natural resources is outweighed by the potential benefits to financial statement users (see paragraphs 10, A9 and A10)? Please explain the reasons for your position in as much detail as possible.
- A8. FISC understands the challenges faced by the Board in balancing all of the matters on the Board's agenda, and appreciates the concerns by Board members that other projects will take precedence over additional standards covering other types of natural resources. However, FISC recommends that paragraph 10 include a statement that any additional types of natural resources reported by an agency use valuation, accounting, and financial reporting methods consistent with the provisions of the final standard, and that such methods be required for all types of natural resources.

Further, FISC repeats our concerns expressed in our January 23, 2008 response to the initial ED that the Board has not explained why capitalization is restricted solely for proved oil and gas resources, and why the reporting concept is not required for other "proven" assets (e.g., coal, uranium, gold, silver, zinc, and other metals, timber, other subsurface minerals, and even water). The ED, as written, provides no requirement or strong language to compel agencies to account for and report all "proven" resources. Absent such a requirement, the ED, as written, would not provide for a comprehensive reporting model for comparable assets.

- Q9. After a three-year transition period of reporting as RSI, the ED proposes to recognize an asset on the balance sheet for the federal government's royalty share of federal oil and gas resources

under lease (see paragraphs A29 through A37 for a discussion of factors regarding asset recognition considered by the Board in reaching this conclusion). An alternative view prepared by Mr. Dacey proposes that the value of federal oil and gas resources and annual changes therein be reported as RSI for a three-year transition period and then disclosed as basic information in the notes, rather than recognized on the face of the financial statements. The notes would be part of an integrated disclosure that would include the discussion of all of the government's natural resources, including oil and gas resources that are not currently under lease as well as values and information concerning all other significant natural resources, such as coal, timber, and grazing rights. Do you agree or disagree with the alternative view (see paragraphs A89 through A92)? Please explain the reasons for your position in as much detail as possible.

- A9. FISC supports the eventual presentation of natural resources on the face of federal financial statements. However, FISC repeats our concerns, expressed in response to question 8 above, that FASAB has not yet explained, in sufficient detail, its position of restricting capitalization to proved oil and gas resources and not mandating reporting of other types of natural resources. Selective recognition of assets by Federal agencies impairs the value of Federal financial reporting, and limits the usefulness of information contained within agency financial statements and the Consolidated Financial Report of the United States Government.

Other Comments

- In paragraph 21, FISC recommends that the phrase “why it is inappropriate to do so” should be replaced with something akin to “why the entity’s own assumptions are a preferred method.”
- In paragraph 28, it is unclear why only expected payments of royalties to non-federal entities are recognized. Consideration should be given to the disclosure of expected payments of royalties to other federal components.

This comment letter was reviewed by the members of FISC, and represents the consensus views of our members.

Very truly yours,



Andrew C. Lewis
FISC Chair

>>> <Bert_Edwards@ios.doi.gov> 9/9/2009 12:00 PM >>>

Wendy - I apologize for not getting to FASAB sooner with my thoughts. On July 24, 2009, the Appeals Court for the Federal Circuit issued its 11th (and we hope final) decision on the individual Indian trust litigation, and I have been devoted almost full-time to working with the new Interior officials, OMB, Congressional committees and others on the possible impact of the decision, which is very favorable to the US Government. I also apologize for the informality of an e-mail response to a FASAB "due process" document, but time is of the essence on getting this to you.

I have an overriding comment on recording the present valuation of proven O & G reserves at a discounted value, using the apparently much favored "principles-based" accounting approach,

(1) Oil and gas are not the only "proven" assets that the USG owns. How about "hard rock" minerals (coal, uranium and many other metals - gold, silver, etc., aggregates, timber, etc.)? How could the officials of an USG agency or its auditor agency concur that the financial statements are "fairly presented" when such other similar future recoverable assets are ignored? Timber alone would be the most significant asset of the US Forrest Service, part of the US Department of Agriculture, and perhaps for the overall USDA. Present value of all the land held by various Interior agencies (Land Management, Reclamation, National Parks, Fish and Wildlife), USDA (Forrest Service), DOD (military installations), etc., is only valued is purchased relatively recently in the USG's history. Certainly, nobody would question the value of the purchase of Alaska ("Seward's Folly") in today's economy; the gold alone extracted from Alaska more than equalled its purchase price from Russia, and the continuing value of, O & G, gold and other metals, salmon fishery, and tourism value make this one of the most fortuitous purchased in our history. Consider the value of the Louisiana Purchase.

(2) Practically all other future revenue streams of the USG, income taxes among them, are estimable with likely the same accuracy as discounted O & G proven reserves. I do not see any discussion why O & G are singled out for valuation and other assets are not. Disclosures now required for Social Security liabilities are net of the estimated FICA taxes to be paid by future workers and matching employer amounts.

In summary, unless there is a total re-visiting of assets of the USG, recording the estimated discounted value of proven O & G reserves seems to be "counting the chickens before the eggs are laid."

With respect to the various questions asked in the ED, I have the following comments.

Question 1 - "Principles-based" accounting can - and undoubtedly will - produce enormous swings in the discounted present value of proven O & G reserves or a number of reasons. We have already seen this in the "mark-to-market" experience in the past two years for not readily salable securities.

(1) Currently, using the benchmark suggested of USG securities, most USG securities funds are earning less than 1% interest. This rate is extremely low due to the USG's various recession-fighting stimulus programs. Nobody believes that this low interest rate can or will continue. In fact many commentators are predicting substantial increases in the USG borrowing rate. The change in the discounted value with a change to, say, a 5-6% USG borrowing rate would cause a tremendous write-down in the value of discounted proven O & G reserves in future years.

(2) From time to time, the amount of royalties the USG collects and is remitted to states has changed. Currently, all states except Alaska receive 50% of all royalties (O&G and all other royalties), and Alaska gets 90%. Recent legislation increased the rates of royalties paid to adjacent coastal states for off-shore O & G royalties. Any changes in royalty rates will change the "phantom" estimated payable to states, perhaps substantially given the severe deficits facing all 50 states except Montana and North Dakota. With respect to amounts payable to the states for royalty sharing, I suspect that not a single state will report its "receivable" related to the estimated royalties payable by the USG.

(3) Proven reserves depends of the prevailing market rates for O & G. Market rates depend on the overall world economic status, the "find" rate of new reserves (gas rates are falling rapidly as new "finds" have occurred in the Appalachian states and elsewhere in the world, and oil rates may be impacted by the "find" recently announced by BP in the off-shore Gulf area southeast of Houston, TX). Technology could well reduce the cost to extract shale oil in the US west and the tar sands in Canada, both of which have estimates of oil (nobody knows if it is economically recoverable, but the tar sands are currently being extracted) greater than all proven reserves in the world according to some media reports. These swings are not controllable by the USG, but will impact the annual amounts of discounted O & G proven reserves.

(4) "Proven" can be immensely affected by uncontrollable situations such as hurricanes in the Gulf, local, state or Federal environmental laws and regulations, interruption of transportation (e.g., a long-term pipeline damage via earthquake, flood, storm, or terrorism). I am not sure how this can be figured into the valuation methodology.

Question 2 - I concur with the ED, but keep in mind that the Treasury borrowing rate can be influenced by many factors as included in the comment (1) to Question 1 above.

Questions 3 and 4 - I concur with the ED. I do have concerns to citing FASB's SFAS 157 since it appears that this pronouncement will undergo continuing refinements, e.g., the recent FASB action to "soften" SFAS 157 for private commercial companies.

Question 5 - I concur with the ED. I am very concerned that future Administrations may be encouraged to focus on the unrealized gains when interest rates decline, world market prices increase, new "finds" become "proven," or new technology permits previously uneconomic "finds" to now be extracted profitably and/or possible. The opposite focus on unrealized losses could well occur when the USG debt interest rates increase (a factor certainly sure to come during the next several years), "proven" reserves decline due to market price declines, increased environmental standards particularly in non-US areas, war or terrorism risks no longer sustaining continued extraction, etc. Thus, at least separating the unrealized gains and losses would decrease these tendencies. See response below to Question 9.

Question 6 - This is the ED requirement that I have the greatest concern with. Even though SSFAS 31 requires assets held in a fiduciary capacity to be reported, neither FASB (banks, investment companies, etc.) or GASB generally require valuation of non-monetary assets. All 50 states and DC have adopted the principles of the Uniform Principal and Income Act, which provides guidance on fiduciaries. A few states already had incorporated the provisions of the Act in their laws prior to the first issuance of the Act, which is now in a second revised version. The Act is very clear that fiduciaries are responsible for assets received by them, i.e. initial transfer of assets, assets purchased during the trust existence, etc. Fiduciaries are not responsible for the value of non-cash assets or even monetary assets not received (e.g., dividends and interest payments due, but not received), although they will normally report the value of readily marketable securities and disclose the non-receipt of investment returns.. Residences and real estate improvements, land and forestry holdings, other assets are merely disclosed, but only rarely valued; in my consultations with commercial bank trust officials, almost all ask a depositor of non-monetary assets to waive any responsibility for current valuations due to the cost of such recurring appraisals. Requiring USG fiduciary funds (probably limited to Interior's two Indian Trust Funds) to record discounted value of proven reserves on land interests owned by individual Indians and Tribes will likely double the work of Interior. Further and importantly, there is no legal or fiduciary obligation of the USG to pay beneficiaries of the two Indian Trusts for such future discounted O & G

royalties until they are received in cash. Currently - and for at least two years - Interior has regularly reported (1) land holdings and (2) "encumbrances" (i.e., surface and subsurface leases, rights-of-way, etc. on such holdings) in quarterly (individual Indians) and monthly (Tribes) fiduciary reports. This is what a private-sector fiduciary would do under the Act. These land holdings and any value for O & G (but excluding present value of surface farming and grazing leases, coal and other subsurface minerals) as well as monetary equivalent holdings are not the assets of the USG. While I am not an expert on commercial bank trust functions, I understand that their disclosures of asset holdings is limited to monetary equivalents and excludes non-monetary assets held in trust. Thus, I disagree with the ED in this respect since there is no explanation in the ED as to why FASAB would depart from the fiduciary practice in the private sector, which in almost all other respects requires all assets and liabilities to be recorded in the financial statements.

Question 7 - As indicated in Question Except for the FASAB ED's requirement for fiduciary funds, I agree with the ED..

Question 8 - The ED does not require disclosures of estimated values of other natural resources - surface (timber, land itself), subsurface minerals, and even water itself. Therefore, it is not possible to form a concurring or disagreeing answer to this question. See answers to Question 1 above. Any expansion of the valuation to other types of natural resources should be essentially in concurrence with the O & G RSI and/or basic disclosures.

Question 9 - Since nobody "owes" the USG for discounted future proven O & G royalties, I concur with the minority view of Mr. Dacey. .

."Bottom Line" - In informal chats with USG and private sector individuals interested in FASAB GAAP, the overall conclusion is that FASAB may be "reaching" for assets to offset the increasingly accumulating deficit. Almost all the liabilities reported by the USG in its CFS have basis in fact, only the recording methodology may be arguable. Discounted proven O & G reserves seems to stand out as a potential asset, but subject to a multiplicity of uncontrollable factors, including some day the elimination of continuing to burn carbon fuels due to global warring treaties.

I realize that this is coming at the last minute. This response represents my personal views, and not necessarily those of the Department of the Interior.

Bert T. Edwards.



United States Department of the Interior

OFFICE OF THE SECRETARY
Washington, DC 20240**SEP 09 2009**

Wendy M. Payne, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Subject: FASAB Exposure Draft, *Accounting for Federal Oil and Gas Resources.*, dated
May 21, 2007.

Dear Ms. Payne:

Attached is the Department of the Interior's consolidated response to the subject
Exposure Draft.

If you have any questions or concerns please contact Don Geiger at 202-208-5542.

Sincerely,

Daniel L. Fletcher
Director
Office of Financial Management

Attachment

Overall, the U.S. Department of the Interior agrees with the intent of the proposed Statement, to enhance accountability and transparency, and provide readers of Federal financial reports with greater information about the quantity and estimated value of assets that generate cash to finance government operations over time.

Response to FASAB Questions for Respondents

Q1. The original exposure draft (ED) issued on May 21, 2007, contained detailed asset valuation implementation guidance for valuing federal oil and gas resources. As a result of feedback received from field testing efforts, the Board has removed that detailed guidance from this revised ED and is instead proposing to provide federal entities with flexibility in developing the asset valuation estimation methodology due to the constantly changing economic and technical conditions. Do you agree or disagree with the Board's position (see paragraphs 14 through 26, A47 and A48)? Please explain the reasons for your position in as much detail as possible.

Response: Interior generally agree with the flexibility provided in developing the asset valuation estimation methodology, with the caveat that a more detailed implementation guide also be developed in the future. There are a number of details that, by their omission, could create a void in needed guidance that may prove problematic in the future.

Additionally, over the years that the Statement has been under development, much research and verification has gone into the determination made by the Board that EIA should be the authoritative source from which quantity information should be obtained. By crafting the Statement so that it no longer explicitly designates EIA as the source of quantity information, significant ambiguity could be cast upon preparers' decisions regarding valuation. Because the asset value will be a significant estimate, comprised of numerous assumptions, we believe the Statement should continue to explicitly designate EIA as the authoritative source for quantity information. We believe it is unlikely that EIA data as it currently is reported to the public will become unavailable in the foreseeable future.

Q2. The Board believes that the method for valuing the federal government's estimated petroleum royalties should approximate the present value of future federal royalty receipts on proved reserves known to exist as of the reporting date as described in paragraphs 19 through 21. Discount rates as of the reporting date for present value measurements of federal oil and gas assets and liabilities should be based on interest rates on marketable Treasury securities with maturities consistent with the cash flows being discounted. Do you agree or disagree with the Board's position (see paragraphs 19 through 21 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.

Response: Interior generally agrees, although we had originally designed the valuation methodology to be based upon OMB's economic assumptions about future Treasury marketable security rates.

- Q3. The Board is proposing to permit an alternative measurement method for valuing the federal government's estimated petroleum royalties if it is not reasonably possible to estimate the present value of future federal royalty receipts on proved reserves using the approach described in paragraphs 19 through 21. Specifically, the Board is permitting a market-based fair value measurement consistent with the Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards 157, *Fair Value Measurements*.¹ Do you agree or disagree with the Board's position (see paragraphs 24 and A38 through A46)? Please explain the reasons for your position in as much detail as possible.

Response: Interior would generally agree with the latitude provided by permitting an alternative measurement method. However, in this instance we do not agree that measuring this federal asset using market based fair value is appropriate. We do not think the asset value should be measured at a market exit price, because it is extremely unlikely that it would ever be sold. Discounting at the public sector rate and valuing according to the expectation of future prices as proposed in the present value method is a much more accurate representation of the value of this federally owned asset.

By adding this provision for alternative measurement using FAS 157, considerable uncertainty and potential inaccurate valuation has been explicitly added to the Statement, and expert respondents disagree with the premise.

For example, FAS 157 provides for "Level 3 Inputs", being the lowest level in the allowable fair value hierarchy. Those inputs are considered 'unobservable inputs', and should be used to measure fair value when observable inputs are not available. They may be developed by the reporting entity, using its own data and reflecting the reporting entities own assumptions about the assumptions market participants would likely have in arriving at an exit price for the asset. Technically this could probably be done, but the valuation would be much less accurate or meaningful, potentially resulting in either a 'fire sale' or 'overvalued' estimate and greatly increasing the already volatile aspects of the asset value.

One must consider that the asset is comprised entirely of federally owned proved reserves. In practice, there is virtual certainty that volumes of oil and natural gas will be produced in the future, at least equal to the estimated volumes of proved reserves of oil and natural gas at any point in time. This is because new proved reserves are constantly being added as prospects are developed. Therefore, there is effectively a 100% chance that all proved reserves will eventually be produced, and there is no uncertainty on that matter. The only uncertainty would be the price in the future and how that production would emerge over time. If the government were to ever sell the assets, we would likely value them at today's price and discount them more or less heavily, to account for market risk, as FAS 157 suggests. But future cash flows from federally owned proved reserves are

¹ FASB Accounting Standards Codification™ (ASC) 820.10

legislated, and thus not subject to risk factors otherwise found in the market, and most importantly, the underlying assets are very unlikely to ever be sold.

Accordingly, Interior disagrees with adding the FAS 157 provision. We believe that the existing proposed present value methodology is the most appropriate measure for this unique federal asset. Also, this may have significant ramifications for other federally owned natural resources to which this Statement may be applied in the future.

- Q4. The Board is proposing to permit federal entities to change its methodology for valuing the federal government's estimated petroleum royalties if environmental or other changes would provide for the development of an improved methodology. Do you agree or disagree with the Board's position (see paragraphs 25, 26 and A49 through A51)? Please explain the reasons for your position in as much detail as possible.

Response: Interior agrees and appreciates the latitude to develop and provide the most accurate estimates possible.

- Q5. The Board believes that it would be appropriate to provide guidance regarding reporting gains and losses from changes in assumptions and selecting the discount rates similar to that provided in SFFAS 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*, to long-term assumptions about oil and gas when using the present value method. Do you agree or disagree with the Board's position (see paragraphs 20, 40, and A64 through A66)? Please explain the reasons for your position in as much detail as possible.

Response: Interior agrees that this would be a reasonable approach in keeping with the similar development of a more detailed oil and gas implementation guide.

- Q6. SFFAS 31, *Accounting for Fiduciary Activities*, requires that agencies report on assets held in a fiduciary capacity. The Department of Interior (DOI) manages oil and gas resources on behalf of individual Indians and Indian tribes. This proposed standard – because it classifies oil and gas resources as assets – would result in additional information being disclosed for oil and gas assets managed in a fiduciary capacity. Note, however, that fiduciary reporting does not extend to inclusion of the additional disclosures or RSI that are proposed in this document for federal oil and gas resources. Thus, with respect to fiduciary activities, only disclosure of the assets, liabilities, and related inflows and outflows would result from this proposal.

Some members have expressed concern that the costs may exceed the benefits of disclosing fiduciary assets and liabilities measured in conformance with this proposed standard. Since this proposal may significantly increase the fiduciary assets disclosed, we requested input on the cost-benefit of the requirement with respect to fiduciary activities in the May 2007 ED. One respondent was in favor of

the disclosures while four expressed their opinion that the information would most likely not be cost-beneficial. However, the Board has not received any substantive information to enable it to make an informed decision regarding cost/benefit.

Since the removal of the fiduciary oil and gas resource disclosure requirements would require an exception to the requirements of SFFAS 31, we are again requesting detailed input on the cost-benefit of the requirement with respect to fiduciary activities. See paragraph 46.

Response: As with onshore proved reserves under federal domain, there is no authoritative published quantity information regarding oil and gas resources managed by Interior on behalf of individual Indians or Indian tribes. However, a similar method for estimating onshore proved reserves under federal domain could potentially be employed to estimate an asset value for this category of oil and gas reserves. Like the onshore federal value, it would be an estimate, subject to significant fluctuation and based upon numerous assumptions. Sufficient disclosure would be required to help readers understand amounts presented and their relationship to royalties ultimately received. By applying a similar methodology to the federal domain category, consistency could be fairly readily achieved.

- Q7. The Board is proposing to provide a three-year phase-in of the proposed requirements from required supplementary information (RSI) beginning with fiscal year 2011 to basic in fiscal year 2014. This transitional period is being provided to allow for the asset valuation methodology to be improved upon before an audit opinion is required. Do you agree or disagree with the Board's position (see paragraphs 51 and A87)? Please explain the reasons for your position in as much detail as possible.

Response: Interior agrees with the three-year phase-in, and appreciates the additional time provided in the Statement to perform the significant and complex changes that will be necessary. Interior is optimistic that this should provide adequate time to resolve outstanding issues and should facilitate an orderly implementation of the Statement.

- Q8. This Statement addresses accounting for federal oil and gas resources only. While the Board may address accounting for other types of natural resources at some point in the future, the majority of the members acknowledge that it is not likely that a project devoted to other categories of natural resources will be marked as a high priority at future agenda-setting sessions due to their lesser significance. As a result, while not explicitly encouraging agencies to recognize other categories of natural resources, the Board included paragraph 10 to explicitly state that this Statement does not preclude entities from recognizing or otherwise reporting information about other types of federally-owned natural resources. Do you agree or disagree that the potential risk that the inclusion of paragraph 10 might lead to inaccurate or inconsistent reporting of other types of natural resources is outweighed by the potential benefits to financial statement users (see paragraphs

10, A9 and A10)? Please explain the reasons for your position in as much detail as possible.

Response: Interior appreciates the latitude that the Board is seeking to provide in this paragraph and believed that it aids in acknowledging the potential treatment of other natural resources. With some related clarification, it could substantially help to resolve potential confusion and help to ensure consistent reporting. However, as it is presented, it illustrates a significant void in authoritative guidance which inherently facilitates the risk of potentially inaccurate or inconsistent reporting.

First, Interior believes that to remove any ambiguity in the intent of the paragraph, it should also indicate that application of the Statement is not mandatory for other federal natural resources. For example,

“This Statement does not preclude, nor does it require, entities recognizing or otherwise reporting information about other types of federally-owned natural resources.”

Second, the current Exposure Draft guidance on accounting for federal oil and gas assets is quite different from FASB guidance covering oil and gas accounting in the private sector. This was emphasized in the response to Question 3 regarding the application of a private sector standard to a federally owned asset such as oil and gas. To ensure that preparers and auditors understand the relationship and application of this federal oil and gas Statement to other types of federal natural resources, we recommend that paragraph 10 be expanded to incorporate the intent from paragraph A10 into the formal governing Statement;

“...this Statement should be considered when applying SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*, to other types of federal natural resources.”

Third, paragraph 10 as presented creates a dichotomy for preparers and auditors in that there are numerous types of federal natural resources for which no significant costs are incurred in the production of revenue, such as coal royalties, or revenues from renewable resource leases. Accordingly, the preparer must infer that SFFAS 7 applies to these resources. SFFAS 7, paragraph 45 as proposed, contains the ‘custodial’ provision for circumstances where there is no significant cost incurred to earn exchange revenue. Interior believes that the Statement should provide clarifying guidance to determine when to apply this ‘custodial’ provision to natural resources, or if it should always apply when there is no significant cost incurred.

For example, with certain renewable energy revenues derived from technologies such as geothermal, wind, wave, or current, there is not a ‘depletable asset’ for which a depletion expense could be matched against revenue earned. Similar to the auction of the radio spectrum, addressed in the revised SFFAS 7 paragraph

45, there are virtually no costs incurred in connection with earning this revenue. Interior interprets this to mean that for these types of 'non-depletable' activities, custodial accounting would still apply under SFFAS 7. Because other federal natural resource cases may not be so clear cut and to assist preparers and auditors, Interior believes that the guidance in the Statement should clarify if or when certain characteristics such as depletion could or should determine if custodial provisions apply, or if they should always apply when no significant costs are incurred.

The obvious result is that for commodities such as coal, which is a depletable natural resource, custodial accounting may or may not apply, depending on whether SFFAS 7 includes depletable natural resources. If not covered, then by default it would be required to be valued and accounted for in a manner similar to federal oil and gas. The 'optional' clause in paragraph 10 would be moot. If the Board intends that custodial accounting would apply, regardless if a natural resource is depletable or not, Interior recommends that this be explicitly stated in SFFAS 7, or the oil & gas Statement or implementation guide, to aid preparers and auditors in the proper and consistent treatment.

- Q9. After a three-year transition period of reporting as RSI, the ED proposes to recognize an asset on the balance sheet for the federal government's royalty share of federal oil and gas resources under lease (see paragraphs A29 through A37 for a discussion of factors regarding asset recognition considered by the Board in reaching this conclusion). An alternative view prepared by Mr. Dacey proposes that the value of federal oil and gas resources and annual changes therein be reported as RSI for a three-year transition period and then disclosed as basic information in the notes, rather than recognized on the face of the financial statements. The notes would be part of an integrated disclosure that would include the discussion of all of the government's natural resources, including oil and gas resources that are not currently under lease as well as values and information concerning all other significant natural resources, such as coal, timber, and grazing rights. Do you agree or disagree with the alternative view (see paragraphs A89 through A92)? Please explain the reasons for your position in as much detail as possible.

Response: Interior believes that this significant asset would best be disclosed as basic information in the notes, consistent with the approach recently expressed by Mr. Dacey in the alternate view. Interior believes that the Board's objectives of enhanced accountability and increased information about the asset can be more efficiently and effectively achieved by disclosing the information in the notes rather than on the face of the financial statements.

The proposed Statement as presented in the ED will require extensive and costly changes to existing Interior (specifically Minerals Management Service (MMS)) business processes, system requirements, and accounting events. These significant changes, impacts, and costs were presented *in the previous field test questionnaires*. Interior believes that the potential benefits of reporting depletion

expense and the gain or loss on revaluation on the Statement of Net Cost do not provide the reader with more meaningful information than could be obtained through disclosure, and in fact may be confusing.

For example, due to volatility in prices, quantity estimate revisions, and other factors, recording gains and losses on net cost may potentially mislead readers. In the MMS field test study, although the overall asset value declined over a year period, depletion expense recorded in the year exceeded the difference in the ending valuation, and required a gain on revaluation to be recorded. This gain would likely be misleading to the general reader, and renders the utility of the information questionable. Interior believes that disclosures regarding the asset valuation and royalties reported over a given span of time, combined with a discussion and presentation of any theoretical change due to revaluation of the estimated asset, would provide a clearer picture and would much more efficiently and cost effectively meet the Board's objectives.