

DOCUMENT RESUME

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[Relevance of GAO Report, "Improvements Needed in DOE's Efforts To Develop a Financial Reporting System"]. EMD-78-112; E-178205. November 1, 1978. 5 pp. + enclosure (pp.).

Report to Rep. John D. Dingell, Chairman, House Committee on Interstate and Foreign Commerce: Energy and Power Subcommittee; by Elmer B. Staats, Comptroller General.

Issue Area: Energy (1600); Accounting and Financial Reporting (2800).

Contact: Energy and Minerals Div.

Budget Function: Natural Resources, Environment, and Energy: Energy (305).

Organization Concerned: Department of Energy; Energy Information Administration.

Congressional Relevance: House Committee on Interstate and Foreign Commerce; House Committee on Interstate and Foreign Commerce: Energy and Power Subcommittee; Senate Committee on Energy and Natural Resources. Rep. John D. Dingell.

Authority: Energy Policy and Conservation Act. Department of Energy Organization Act. Federal Energy Administration Act of 1974. Energy Supply and Environmental Conservation Act. Energy Conservation and Production Act.

A GAO report issued on July 31, 1978, identified shortcomings in efforts by the Energy Information Administration (EIA) to meet its obligations under the Energy Policy and Conservation Act (EPCA) and recommended corrective actions. Questions were raised about the relevance of this report to EIA's Financial Reporting System (FRS). The principal concern expressed in the report, that EIA has not adequately defined its data needs nor planned its intended use, is directly relevant to the FRS. Subsection 205(h) of the act outlines four broad types of analyses that the FRS is to facilitate, but these analyses are not related to specific policy objectives. Before the reporting system is implemented, certain questions should be answered relating to policy issues, information needs, specifics of data collection, and accounting practices. Recommendations in the July report relating to a reporting form for small producers and obligations to collect data from all producers do not apply to subsection 205(h). (HTW)



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

8/99

B-178205

NOVEMBER 1, 1978

The Honorable John D. Dingell
Chairman, Subcommittee on Energy
and Power
Committee on Interstate and Foreign
Commerce
House of Representatives

Dear Mr. Chairman:

On July 31, 1978, we issued a report entitled "Improvements Needed in the Department of Energy's Efforts to Develop a Financial Reporting System" (EMD-78-95). In that report, we described certain shortcomings in efforts by the Energy Information Administration (EIA) of the Department of Energy (DOE) to meet its obligations under the Energy Policy and Conservation Act (EPCA) and recommended actions that we felt were needed to fully meet the intent of that act.

In a letter to us dated September 6, 1978, you expressed concern that our report could delay the implementation of EIA's Financial Reporting System (FRS) and raised certain questions about the relevance of our report to FRS. You stated that in your opinion the FRS is designed to meet only subsection 205(h) of the Department of Energy Organization Act and that the data system should not be delayed for noted shortcomings in meeting the requirements of EPCA.

While we cannot agree that FRS relates solely to subsection 205(h) of the DOE Organization Act, 1/ our view

1/DOE officials have continuously assured us since May 1977 that FRS would be used to meet the Department's responsibilities under EPCA (see the attached letter from The Honorable John F. O'Leary, Administrator, Federal Energy Administration, dated May 26, 1977). The present Administrator of the Energy Information Administration reinforced this view in our meeting with the Subcommittee staff on September 11, 1978. Subsection 205(c) of the DOE Organization Act provides that EIA must perform pre-existing energy information responsibilities such as those outlined in section 505 of EPCA.

EMD-78-112
(00200)

in that regard is not crucial to our basic concern regarding FRS. The principal concern expressed in our report is that EIA has not adequately defined its data needs and has not sufficiently planned the use it will make of the data collected. Essentially, we are concerned about the form's usefulness to data users. We believe the form may contain too much data, too little data, or simply data in the wrong format for its eventual users. We believe this concern is directly relevant to the Financial Reporting System and is valid regardless of the legislative mandate under which the form was developed. While we do not question the sufficiency of FRS to meet the legal requirements of subsection 205(h), we believe a serious question exists as to whether the proposed FRS form contains the data needed by the system's users.

Members of the subcommittee staff have asked that we relate the comments in our report directly to EIA's mandate under the DOE Organization Act. The purpose of this letter is to respond to that request.

Subsection 205(h) of the DOE Organization Act outlines four broad types of analyses that the Financial Reporting System is to facilitate. These analyses are described in very general terms, however, and are not related to specific policy objectives or policy questions. EIA is given considerable freedom to determine what specific data it will collect, what analyses it will make, and consequently what the system will accomplish.

For example, paragraph (2) of subsection 205(h) states that the FRS shall permit "* * * an evaluation of company revenues, profits, cash-flow, and investments in total, for the energy-related lines of commerce in which such company is engaged and for all significant energy-related functions within such company." The act does not state what kind of evaluation is to be made or what policy questions are to be answered, and it is not intuitively obvious what specific revenue, profit, investment, and cash-flow data is needed. Revenues, profits, investments, and cash-flow can be evaluated in many different ways and on many different bases. The type of evaluation to be made should be dictated by the policy questions to be answered, and that evaluation should, in turn, dictate the basis on which financial concepts such as revenues and profits are to be computed to render the most relevant and meaningful answer.

To be somewhat more specific, profitability can be analyzed on many different geographical and geological bases, and functional breakdowns can be made before or after the allocation of various joint costs such as corporate taxes. Further, profits can be measured on a value basis as opposed to the historical cost basis as presently contemplated by FRS and can be augmented by the presentation of projected cost and revenue information. The techniques used to measure profits and the geographical and corporate boundaries on which profits are computed depend very heavily on what policy questions are going to be addressed and how "corporate profitability" is going to be used in answering those questions. If "profits" are going to be used in resolving pricing policy questions, a measure of companywide or functional profits on a historical cost basis may be totally inappropriate. For other purposes, such a measure may be useful. If changes are needed in the measurement techniques used to compute profits, or in the corporate, geographical, and geological boundaries on which those computations are made, significant changes may be required in the data collected from industry firms through FRS.

We believe that fundamental decisions concerning the system's objectives, the policy questions to be answered, and the specific analyses to be made form the foundation of any information system and provide the appropriate basis on which to judge the relevancy and usefulness of various forms of input data. We were never able to find satisfactory evidence that this foundation was laid or that it served as the basis for selecting the data in the proposed FRS collection form. It is important that DOE collect the data that is needed to meet the system's objectives and not simply all the data that can be expeditiously collected from reporting companies.

DOE staff members have told us that they considered the system's objectives in designing FRS forms, but that the thought process linking the objectives to specific FRS data was not formally documented. We believe it is both impractical and insufficient to develop a system as large and important as this one (approximately 8,000 data items forming one of the most comprehensive energy data systems inside the Federal Government) without formally documenting the key elements of this important thought process. As we stated in our July report, we believe the reporting system should be implemented only after the following questions have been answered:

1. What policy issues are most relevant and potentially useful in accomplishing the public policy objectives to which the system is oriented?
2. What specific questions need to be answered in resolving the policy issues relevant to this system?
3. What analyses and industrywide information are needed to answer the specific questions?
4. What specific data must be collected from individual companies to compile the needed information and make the required analyses?
5. Who should be required to submit the data?
6. What accuracy tolerances should be placed on the data?
7. What accounting practices are needed to insure that data is adequately comparable and reliable?

Lacking a well-documented system, EIA runs the risk of imposing an unnecessary reporting burden on industry, inundating policymakers with irrelevant data, and delaying the collection of relevant information on which energy policy should be based. We recommended in our July report that the Secretary of Energy document the needs and uses of the data in the proposed collection forms and insure that the data relates directly to the reporting system's objectives. We made this recommendation following our review of EIA's efforts under the Energy Policy and Conservation Act, but as indicated earlier, we believe the recommendation is just as important for purposes of satisfying the intent of subsection 205(h) of the DOE Organization Act as it is for satisfying section 505 of EPCA.

We expressed two additional concerns in our July 31 report regarding the adequacy of EIA's efforts under EPCA. We stated that EIA had not developed a reporting form for small producers who must report under the act and that DOE had ignored its obligations under EPCA to collect data from all producers, whether or not sample basis reporting would satisfy the agency's needs. Both of these concerns and the corresponding recommendations stated in our report

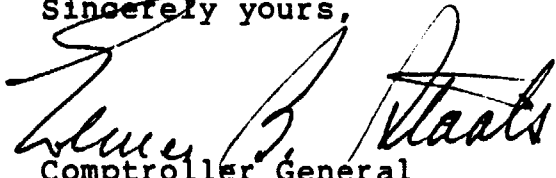
relate solely to EIA's obligations under EPCA.^{1/} Subsection 205(h) of the DOE Organization Act allows less stringent reporting by small producers for purposes of that subsection, and the two recommendations in our report dealing with small producers do not apply to that particular provision.

Even for purposes of reporting under EPCA, we would point out that these last two recommendations do not relate to a reporting form designed exclusively for large producers. We stated in our report that efforts in designing a reporting scheme for small producers (as discussed in our last two recommendations) could be affected by changes in response to our first recommendation regarding the agency's data needs and uses. We believe, therefore, that efforts in developing a reporting form for small producers should be closely coordinated with results obtained under the first recommendation in our report. We believe, however, that a form designed exclusively for large producers does not need to be entwined with efforts under the last two recommendations as long as it fully responds to the first recommendation as discussed above.

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We hope these comments are useful to you and other members of the Subcommittee and its staff. We are sending copies of this letter to the Chairman, Subcommittee on Oversight and Investigations, House Committee on Interstate and Foreign Commerce; the Secretary, U.S. Department of Energy; the Director, Office of Management and Budget; and the Administrator, Energy Information Administration, U.S. Department of Energy.

^{1/}In this regard, we note that subsection 205(h) is in addition to pre-existing information responsibilities consolidated in subsection 205(c) and thus, according to its legislative history "neither expands nor limits" authority such as that in EPCA.

Sincerely yours,

Comptroller General
of the United States

Enclosure



FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

OFFICE OF THE ADMINISTRATOR

May 26, 1977

Mr. Monte Canfield, Jr.
Director, Energy and Minerals Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Canfield:

This letter responds to your inquiry of April 22, 1977, in which you posed eight questions relating to our interpretation of Title V of the Energy Policy and Conservation Act (EPCA).

We appreciate this opportunity to set forth our views on this matter of critical importance to both our agencies. The significant improvement in oil and gas financial information that will emerge from the EPCA mandated accounting standards should improve the Federal Government's ability to make well-founded and credible judgments about oil and gas economics and related policy questions. We are deeply committed to this interagency effort which will help advance the Nation's energy program.

At my direction, and in response to President Carter's request, the Federal Energy Administration (FEA) is currently engaged in a project to define the agency's requirements for financial information from the petroleum industry. Our requirements, of course, extend beyond the exploration and production phase of the petroleum industry to include refining, marketing, and transportation activities. The EPCA is the key source of data requirements for the exploration and production phase. However, FEA must also fulfill mandates outlined in the Federal Energy Administration Act (FEAA), the Energy Supply and Environmental Conservation Act (ESECA), and the Energy Conservation and Production Act (ECPA).

To assure the development of the most relevant and comprehensive set of data requirements, we have solicited assistance from certain key parts of the Federal Government. All of the Offices within FEA have been asked to provide input to the requirements process. FEA has also established a procedure to utilize the expertise of other agencies to aid us in the definition of data requirements. The Federal Power Commission (FPC), Securities and Exchange Commission (SEC), Federal Trade Commission (FTC), Office of Management and Budget (OMB), Interstate Commerce Commission (ICC), Department of Justice, Bureau of the Census, as well as the General Accounting Office (GAO) are cooperating with us to define the data base envisioned in Title V of EPCA and Section 52 of ECPA. We are also planning to meet in the near future with the Energy Research and Development Administration and Department of the Interior to obtain input on their data requirements.

The types of information that our study has defined as requirements so far fall into four broad categories:

- A. profitability of the functional segments of the petroleum industry;
- B. control of energy resources;
- C. cash flow and investment patterns; and
- D. efficiency of energy supply.

FEA's overall responsibility is specifying the data base and data collection program required under EPCA, and assuring that this data base is developed in a manner consistent with and integral to other energy data programs in the Government.

Specific responses to your questions follow:

1. FEA's responsibility under Section 503 of EPCA is to consult with the SEC, Financial Accounting Standards Board (FASB), GAO, and FPC during the process of establishing accounting standards for the oil and gas producing industry. The primary purpose of the standards-setting process is to remove the ambiguity in the oil and gas producing industry's financial data. Ambiguity stems from the variety of alternate methods that currently exist for reporting similar transactions.

FEA's responsibility under Section 505 of EPCA is to implement a quarterly financial reporting system regarding the revenues, costs, investments, and operating results of the oil and gas exploration and production industry. To assure consistent reporting, the FEA has the responsibility to require companies to maintain information in accordance with the accounting standards developed by the SEC and FASB (in consultation with FEA, GAO, and FPC), to enable the reporting of such information to FEA.

The quarterly reporting system will not be implemented until accounting standards for exploration and production have been established by the SEC pursuant to Section 503 of EPCA.

2. As indicated above, the FEA is currently developing the specification of its data requirements for the quarterly report. The development of the reporting form will follow the definition of the data requirements. These tasks have high priority in FEA based on our commitments to GAO and SEC. The Office of Energy Information and Analysis, which has the responsibility for this effort, has previously assured the SEC of its full cooperation in establishing data needs and the associated accounting practices.

We have identified a preliminary series of objectives for the overall financial reporting program and the types of data items which would be necessary to analyze specific policy questions. These objectives and data are listed in the enclosure.

3. FEA has not designed the report that would be sent to Congress. However, it is possible to outline the kinds of data and analyses that the FEA would provide. The report would address the categories of information outlined in Section 503 of EPCA and would include types of information such as:

- o revenues shown separately for oil and gas production;
- o operating costs for current oil and gas production;

- o expenditures for developing oil and gas discoveries into producing properties; and
- o assets involved in oil and gas exploration and production.

Analytic studies would include rate of return comparisons of small and large companies and an examination of the trend of finding and development costs for oil and gas.

4. The primary users of the data base mandated by the EPCA are the Congress, FEA, the agencies mentioned earlier, as well as the Council of Economic Advisors, Department of Treasury, and Department of Commerce. It is clearly the intent of the Congress, expressed in EPCA, to provide itself with useful information on which to base its decisions regarding energy supply. FEA is planning to analyze the information in the data base for its policy and program evaluation. We have already initiated a series of discussions with other potential users as indicated above and have asked these agencies to provide ongoing assistance in specifying and using the energy data base.

5. Currently identified tasks for satisfying the EPCA reporting requirement are:

- o consult with the SEC and other agencies to develop uniform accounting standards for oil and gas producers;
- o develop the specific data requirements for the quarterly report mandated by EPCA;
- o design a report form to collect the required data;
- o organize and staff a group to validate, process, and analyze the information; and
- o design an analytical and reporting program for the President and the Congress.

6. The approach to this project was discussed in the general comments above.

Our timetable for developing the quarterly reporting system required by EPCA is as follows:

- o complete specification of data requirements July 77
- o complete selection of the data elements to be reported quarterly and develop a reporting form Aug. 77
- o public comment period Sep. 77
- o develop final form Oct. 77
- o request GAO approval of the quarterly reporting form Early 78
- o send the reporting package to respondents Dec. 78
- o receive and process data covering first quarter 1979 (the first reporting quarter under the Act) June 79

7. To date, FEA's main efforts have been to identify data requirements and to develop a reporting form for an annual survey of financial conditions in the oil industry. The design of this system is not yet firm. Because of the extensive interagency coordination involved, this effort will not be complete for several weeks.

Based on the set of requirements for annual exploration and production information that the FEA has developed, FEA has recently begun development of its quarterly data requirements. This effort will not be complete until July 1977. However, we expect to be able to provide the SEC staff with a list of tentative data requirements very shortly.

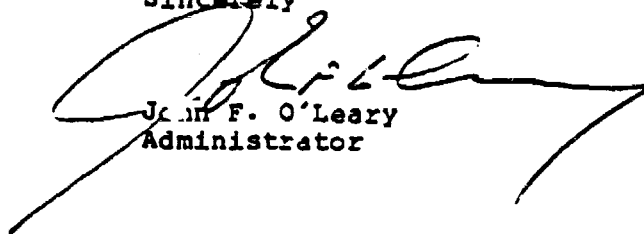
8. FEA's responsibilities under Section 505 of EPCA are: (1) to require companies to maintain information in accordance with the accounting standards developed by the SEC and FASB (in consultation with FEA, GAO, and FPC), to enable the reporting of such information to FEA; and (2) to collect and report oil and gas exploration and production information to the President and the Congress.

Regarding the required quarterly reporting by the companies, FEA will collect data according to the categories specified in paragraphs 1 and 2 of Section 503(c) of EPCA. These categories will contain more or less detailed information depending on FEA's needs.

Paragraph 3 of Section 503(c) gives FEA further flexibility in specifying the content of the data base and the quarterly report to facilitate compilation or interpretation of the data base.

If you have any further questions regarding FEA's energy data base program, please do not hesitate to contact us.

Sincerely



Jean F. O'Leary
Administrator

Enclosure

cc: Chairman, Subcommittee on Oversight and Investigations,
House Committee on Interstate and Foreign Commerce
Chairman, Federal Power Commission
Chairman, Securities and Exchange Commission

PURPOSE OF FRS

THE FINANCIAL REPORTING SYSTEM (FRS) WILL MONITOR WITHIN
THE PETROLEUM (OIL AND GAS) INDUSTRY:

- PROFITABILITY OF MAJOR ELEMENTS
- CONTROL OF ENERGY RESOURCES
- USES OF PROFITS AND CASH FLOWS
- EFFICIENCY OF ENERGY SUPPLY

TO AID IN ANALYZING ENERGY POLICY ISSUES.

POLICY_QUESTION_1

ARE UNREASONABLE PROFITS BEING REALIZED IN DIFFERENT SEGMENTS OF THE PETROLEUM INDUSTRY?

SUCH AS:

- o Upstream vs. downstream profitability
- o Oil and gas vs. alternative fuel profitability
- o Domestic vs. foreign profitability
- o Majors vs. independents profitability

FRS DATA ITEMS:

- o Profits
- o Costs
- o Operating Margins
- o Inventory Values
- o Unsuccessful wells

POLICY QUESTION 2

WHAT IS THE DEGREE OF INFLUENCE OR CONTROL EXERCISED BY
A COMPANY OR A GROUP OF COMPANIES WITHIN THE PETROLEUM
INDUSTRY?

SUCH AS:

- o Ownership of domestic reserves
- o Control of production
- o Access to foreign sources of oil

FRS DATA ITEMS:

- o Domestic proved reserves by ownership
- o Domestic and foreign production
- o Sales of refined product

POLICY_QUESTION_3

TO WHAT EXTENT DOES THE RELATIVE SIZE OF A PETROLEUM
FIRM INFLUENCE ITS PERFORMANCE?

SUCH AS:

- o Economies of scale
- o Profitability
- o Market control
- o Barriers to entry

FRS DATA ITEMS:

- o Cash flows
- o Assets
- o Refinery capacity
- o Profits available for reinvestment
- o Costs
- o Sales

POLICY QUESTION 4

TO WHAT EXTENT DO PETROLEUM COMPANIES INFLUENCE OR CONTROL OTHER ENERGY INDUSTRIES? TO WHAT EXTENT DOES THIS CONTROL ENCOURAGE OR DISCOURAGE DEVELOPMENT OF ENERGY SUPPLIES?

SUCH AS:

- o Ownership and development of coal supplies
- o Ownership and development of uranium supplies

FRS DATA ITEMS:

- o Ownership of reserves
- o Sources of funds
- o Capital spending
- o Production

POLICY QUESTION 5

HOW EFFICIENT ARE THE VARIOUS PARTS OF THE ENERGY SYSTEM?

SUCH AS:

- o Independents vs majors
- o Comparison of costs of production, processing, and distribution
- o Identifying cash flows between segments and fuels

FRS DATA ITEMS:

- o Operating costs
- o Profits and losses by segment

POLICY QUESTION 6

WHAT PRICES ARE NEEDED TO COVER AVERAGE COSTS OF
SUPPLYING ENERGY?

SUCH AS:

- o Offshore vs. onshore cost and prices
- o Alaska vs. lower 48 cost and prices

FRS DATA ITEMS:

- o Exploration, development, and production costs
- o Additions to proved reserves

POLICY QUESTION 7

WHAT HAVE BEEN THE EFFECTS OF GOVERNMENT REGULATIONS ON
DIFFERENT SEGMENTS OF THE INDUSTRY?

SUCH AS:

- o EPAA/EPCA/ECPA
- o FPC Opinion 770
- o Price and Allocation Regulations

FRS DATA ITEMS:

- o Cost (Exploration, development)
- o Revenues
- o Cash flows
- o Profitability
- o Operating Margins
- o Capital Expenditures



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

ENERGY AND MINERALS
DIVISION

The Honorable John F. O'Leary
Administrator, Federal Energy
Administration

April 22, 1977

Dear Mr. O'Leary:

Section 503 of the Energy Policy and Conservation Act (Act) mandates that the Securities and Exchange Commission (SEC) develop accounting practices to be followed by persons engaged in the production of crude oil and natural gas. The purpose for the development of accounting practices, as stated in the Act, is to help assure the development of a reliable energy data base related to the exploration and production of crude oil and natural gas.

Section 505 of the Act mandates that the Administrator of the Federal Energy Administration submit quarterly reports to the President and Congress containing petroleum information kept in accordance with the accounting practices developed under Section 503. The Act further requires the SEC to consult with the Federal Energy Administration (FEA), the General Accounting Office (GAO), and the Federal Power Commission with respect to the accounting practices required by the Act.

The GAO has two principal roles to play in this project; one in the consultant capacity to the SEC provided for in the Act, and the other in its general oversight capacity to the Congress. Further, the responsibility vested in GAO under the Act to verify energy data submitted to Federal agencies dictates that we do the best possible job at this time to encourage the development of accounting practices which will help insure the integrity and credibility of energy data reported to the Federal Government.

Because of our responsibilities, we have closely followed the efforts of the SEC, the Financial Accounting Standards Board (FASB), and others in the development of accounting practices required by Section 503 of the Act. Members of my staff have served as observers to the FASB task force on the extractive industries and have informally exchanged views with FEA staff members on the matters under consideration by the FASB as well as other matters regarding the overall requirements of the Act.

From the inception of the project, we have been continuously concerned with the scope of the intended data base and associated accounting practices which are required by the Act. While the Act specifies certain financial and operating data, it is not clear as to what type of exploration and production data should be included for data base purposes.

We believe that the data base should have broad application to the energy information users contemplated by the Act. Consequently, any financial or operating information that FEA collects or intends to collect could be part of this data base, the reliability of which may necessitate some development of accounting practices by the SEC.

In their letter to the FEA dated February 8, 1977, SEC requested that FEA advise them of any uses FEA plans to make of the information that is collected under Section 505 of the Act. They further requested FEA to identify the implications that such uses might have on the development of accounting practices. We believe this letter recognizes the need for FEA to coordinate its efforts under Section 505 with those of the SEC. This coordination will assure that the accounting practices developed by SEC address the data FEA plans to collect under Section 505 and the uses that will be made of that data. We have discussed the need for this coordination on several occasions with representatives of both the FEA and SEC.

We have formally requested that SEC clarify its position regarding the scope of the data base and the relationship that exists between accounting practices required by Section 503 and the data that FEA will collect under Section 505. We indicated in our request that we believed, at a minimum, that the data base addressed by SEC should encompass the information that the FEA collects and reports to the Congress and the President under Section 505 of the Act.

We request that you clarify for us the position taken by the FEA on the following questions. Please indicate in your answers the basis or rationale underlying such positions.

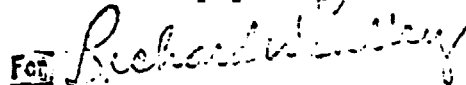
1. How has FEA defined its responsibilities as they relate to Section 503 and 505 of the Act?
2. What information does FEA intend to collect from persons engaged in the production of crude oil and natural gas under Section 505? Be as specific as possible in your answer.

3. What information will FEA report to the Congress and the President under Section 505? Be as specific as possible in your answer.
4. Who, in your opinion are the users of the data base contemplated in the Act?
5. What specific tasks will FEA address in satisfying its responsibilities under the Act?
6. What approach will FEA follow in completing the required tasks and what timeframe has been established for key events?
7. What has FEA done to date toward satisfying the requirements of Section 505 of the Act?
8. How, in your opinion, do your responsibilities under Section 505 relate to paragraphs 1, 2, and 3 of Section 503(c) and the accounting practices required thereunder?

Copies of this letter are being sent today to the Chairman of the Securities and Exchange Commission and the Chairman of the Federal Power Commission, consulting agencies named in the Act; and to the Chairman of the Subcommittee on Oversight and Investigations, House Committee on Interstate and Foreign Commerce, who has a continuing interest in this project.

We appreciate the courtesy and cooperation extended to our staff. Because we have been working informally with your staff on these matters, we would appreciate receiving your response within 15 days of receipt of this letter.

Sincerely yours,

The image shows a handwritten signature in dark ink, which appears to read "Monte Canfield, Jr.". The signature is written in a cursive style and is positioned above the typed name and title.

Monte Canfield, Jr.
Director