

# COMPLIANCE WEEK

## Short On Clarity, FIN 47 Sows Confusion

By Tammy Whitehouse — August 29, 2006

The intent of the Financial Accounting Standards Board was clear: to clarify the rules and create more consistency in how companies account for asset retirement obligations.

The outcome, however, could not be murkier.

With Financial Interpretation No. 47, FASB wanted to delineate how companies should account for any future legal obligations they might face to dispose of assets carried on their books—principally, cleaning up environmentally damaged properties or ridding themselves of hazardous materials. Instead, nine months after FIN 47 went into effect, a wide range of interpretations by attorneys, accountants, engineers, environmental consultants and many others is leaving a wake of confusion.

The differences are evident in wildly disparate reporting of FIN 47 costs from otherwise very similar businesses. In theory, two companies of comparable size and industry should report roughly the same asset retirement liabilities. A study by the Corporate Executive Board examining filings made earlier this year, however, shows that companies' interpretations of FIN 47 and their estimates of its costs are all over the map.

Boeing, for example, is a \$54 billion company reporting a \$4 million liability based on its understanding of FIN 47. Honeywell International, however—also an aerospace and defense company, but half Boeing's size with revenues of \$27.7 billion—showed a \$21 million hit to comply with FIN 47.



Eastman Kodak and Whirlpool, both consumer product companies with revenues of \$14.2 billion and \$13.4 billion respectively, booked very different FIN 47 figures as well. Kodak booked a \$57 million liability; Whirlpool reported FIN 47 as immaterial.

Similar discrepancies appear in other sectors. Power utility Wisconsin Energy Corp. is a \$3.8 billion company reporting a \$38.4 million FIN 47 liability, while El Paso Corp. is a \$4 billion company reporting that FIN 47 is immaterial to its balance sheet. Even more extreme among utilities, \$82.2 billion Valero Energy says FIN 47 is immaterial while its \$11.7 billion brethren PG&E Corp. booked a \$202 million liability.

FASB issued FIN 47 in early 2005 to clarify FASB's intent in Financial Accounting Standard No. 143, Accounting for Asset Retirement Obligations; it took effect at the start of this year. FIN 47 requires companies to look more carefully at assets they likely will carry on their books for a long period of time, examine any legal obligations they may have with the eventual disposal of those assets, and report a current financial liability to meet those future legal obligations.

FIN 47 encompasses a wide variety of assets and prospective obligations, such as environmental rules that might come into play when closing a plant or selling a piece of real estate, or contractual obligations when turning in a leased piece of property or equipment. A host of sticky subjects such as asbestos, treated utility poles, underground storage tanks fall under the rule's domain.

### RELATED RESOURCES

-  [Financial Interpretation No. 47 \(March 2005\)](#)
-  [FAS No. 143, Accounting For Asset Retirement Obligations](#)
-  [FAS No. 5, Accounting For Contingencies](#)
-  [Corporate Executive Board Study On FIN 47 \(March 2006\)](#)
-  [Greg Rogers' Tally Of FIN 47 Disclosures](#)

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### Related White Paper

-  [Edison Electric Institute/AGA White Paper On FIN 47](#)

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### Related Coverage

-  [Costs Soaring For Asset Retirement Rule \(April 4, 2006\)](#)
-  [New Accounting Rule Snares Financial Reporting \(Jan. 31, 2006\)](#)
-  [IMA Issues Guidance On Accounting For Enviro. Costs, Liabilities. \(August 2005\)](#)
-  [New Regs, Standards Influencing Environmental Disclosures \(November 2004\)](#)

## Differences Of Opinion

If FIN 47's intent was to clarify, why the discrepancy in interpretation? The reasons vary almost as widely as the figures. "The consensus is that there is no consensus," says Gregory Rogers, an attorney, accountant and president of consultancy Advanced Environmental Dimensions.



Perellis

Foremost, the issues involved cut across numerous disciplines in a business, requiring judgment from professionals and executives with different perspectives. "I won't say it's a tension, but it's a very dynamic process with a particular company, with their financial accounting firm, their environmental managers, and their attorneys," says Andrew Perellis, a partner in the environmental practice of law firm Seyfarth Shaw. "There's an integration of analysis that takes place in order to get to the right result."

 SEC Issues Accounting Bulletin For Oil, Gas Companies (October 2004)

### Further Reading

 Details On Rogers' Book On Environmental Liabilities Post-SOX

Experts from different perspectives debate, for example, whether an obligation arises from "normal" or "proper" use of an asset, which puts it in the FIN 47 domain, or whether the obligation is the result of abnormal or improper use, which leaves it out. They also debate whether an obligation related to a particular asset is tied to its retirement, bringing it under FIN 47, or whether the obligation arises from something else, which renders it exempt.

#### EXCERPT

Below is an excerpt of FIN No. 47, *Accounting for Conditional Asset Retirement Obligations*.

An entity shall identify all its asset retirement obligations. If an entity has sufficient information to reasonably estimate the fair value of an asset retirement obligation, it must recognize a liability at the time the liability is incurred. An asset retirement obligation would be reasonably estimable if (a) it is evident that the fair value of the obligation is embodied in the acquisition price of the asset, (b) an active market exists for the transfer of the obligation, or (c) sufficient information exists to apply an expected present value technique. An expected present value technique incorporates uncertainty about the timing and method of settlement into the fair value measurement. However, in some cases, sufficient information about the timing and (or) method of settlement may not be available to reasonably estimate fair value. Examples 1 and 2 in Appendix A illustrate the application of this Interpretation when an entity has sufficient information to reasonably estimate the fair value of an asset retirement obligation at the time the obligation is incurred.

An entity would have sufficient information to apply an expected present value technique and therefore an asset retirement obligation would be reasonably estimable if either of the following conditions exists:

- The settlement date and method of settlement for the obligation have been specified by others. For example, the law, regulation, or contract that gives rise to the legal obligation specifies the settlement date and method of settlement. In this situation, the settlement date and method of settlement are known and therefore the only uncertainty is whether the obligation will be enforced (that is, whether performance will be required). Uncertainty about whether performance will be required does not defer the recognition of an asset retirement obligation because a legal obligation to stand ready to

A prime example are underground storage tanks—which exist by the thousands at gas stations throughout the country and in many other industrial settings. Companies are required eventually to remove underground tanks to comply with environmental rules, so experts agree that constitutes an asset retirement obligation subject to FIN 47 treatment.

But tanks have a propensity to leak and contaminate nearby soil; the Environmental Protection Agency says that even with recent efforts to make them safer and less likely to leak, it has identified 5,000 to 15,000 leaky tanks annually since 2000. So should companies assume it's "normal" for a certain percentage of its underground storage tank to leak, and include the prospective cleanup cost when booking a liability to remove the tank? Opinions differ on what FIN 47 requires.

"Most people have been silent on this, probably because they're just confused," Rogers says. "I don't know for sure that I've got an obligation associated with this tank, but the evidence is strong that I probably will have leaks with some percentage of these tanks. That's a liability."



Rogers

Randall Sogoloff, a partner with Deloitte & Touche, said he would generally agree that companies should factor in historical data—from their own archives or industry sources, depending on the circumstances—in determining whether they must face such a liability. "FIN 47 specifically, explicitly requires enterprises to identify all their asset retirement obligations," Sogoloff says. "It's a fine line, so it depends on each company's specific situation, but all companies are required to identify all their [asset retirement obligations]."

### Questions Of Latitude

Douglas Clark, a partner with the law firm Foley & Lardner who

perform the retirement activities still exists, and it does not prevent the determination of a reasonable estimate of fair value because the only uncertainty is whether performance will be required. In certain cases, determining the settlement date for the obligation that has been specified by others is a matter of judgment that depends on the relevant facts and circumstances.

- The information is available to reasonably estimate (1) the settlement date or the range of potential settlement dates, (2) the method of settlement or potential methods of settlement, and (3) the probabilities associated with the potential settlement dates and potential methods of settlement. Examples of information that is expected to provide a basis for estimating the potential settlement dates, potential methods of settlement, and the associated probabilities include, but are not limited to, information that is derived from the entity's past practice, industry practice, management's intent, or the asset's estimated economic life. In many cases, the determination as to whether the entity has the information to reasonably estimate the fair value of the asset retirement obligation is a matter of judgment that depends on the relevant facts and circumstances.

If sufficient information is not available at the time the liability is incurred, paragraph 3 of Statement 143 requires a liability to be recognized initially in the period in which sufficient information becomes available to estimate its fair value. Paragraph 22 of Statement 143 requires that if the liability's fair value cannot be reasonably estimated, that fact and the reasons shall be disclosed. Example 3 in Appendix A illustrates the application of this Interpretation when an entity does not have sufficient information to reasonably estimate the fair value of an asset retirement obligation. Example 4 in Appendix A illustrates the application of this Interpretation when an entity initially does not have sufficient information but later has sufficient information to reasonably estimate the fair value of an asset retirement obligation.

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#### Source

 Financial Accounting Standards Board



John Hepp, a senior manager with Grant Thornton's national professional standards group, says the room for debate is healthy. "There's always an element of judgment in such matters," he says. "Personally, I think gray areas are a good thing. Past efforts to create bright lines have not been particularly successful ... There must be some room to consider the individual facts and circumstances."

Hepp Rogers, however, is eager to achieve greater consistency. "Eventually these issues have to get resolved," he says. "Right now we're comparing apples to oranges. That's not what accounting standards are supposed to create. At some point, these issues have to become better understood."

focuses on environmental and energy regulation, doesn't see the obligation that clearly. "In the context of underground storage tanks, neither FAS 143 nor FIN 47 require companies to go out and look," he says. "There are no new investigative requirements associated with those rules. If you reasonably don't anticipate it, you don't have to go look for it."

Clark says if companies detect a leak or contamination, it probably would be reported under other requirements besides FIN 47, such as state or federal environmental laws. "For most situations, it's the discovery of the contamination, not the retirement of the asset, that triggers the obligation to report it," he contends. "If it's an abnormal event and everyone agrees it's abnormal, you clearly don't report it under FAS 143 or FIN 47. On the other hand, if it's a contamination that occurred during normal operation, the obligation to do something about it is triggered not by the retirement of the asset, but by some standard that requires it to be cleaned up."



Clark

Perellis doesn't interpret FIN 47 to require companies to investigate whether tanks might have caused contamination, but the existence of historical data (as exists for underground storage tanks) could muddy the issue. "Assume I have 100 storage tanks and although they're not designed to leak, it's possible they can leak," he says. "If I'm managing a large portfolio of tanks, should I assume a certain percentage of those tanks would leak? That's something to consider."

In addition to those debates, companies still have some latitude under FIN 47 to say they can't reasonably know when or how an asset will be decommissioned, meaning they don't have to book a liability at all—which further invokes some judgment calls.

Steve Courcier, senior vice president with environmental and engineering consultancy GaiaTech, says that decommissioning provision dominates interpretations. "Companies are eager to say they just don't know [when or how they'll ultimately dispose of an asset] because they're eager to not book a liability," he says. "That's the most common position out there."

Among those who drill deeper into the issues, Courcier reports hearing broad interpretations of what FAS No. 143 and FIN 47 require, both from companies themselves and from the attorneys and accountants who are advising their clients on how to apply it.