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International Accounting Standards Board
30 Cannon Street
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Subject: Comment Letter Improvement Project IAS 2 (LIFO Valuation Method)

Dear Sirs,

I am writing you as Group Controller of the Royal Dutch/Shell Group ("Shell").

Shell is pleased to have this opportunity to comment on the question raised in the Improvements Exposure Draft on IAS 2 regarding the proposed elimination of the allowed alternative of using the Last-in First-out method (LIFO) for inventory valuations.

Shell is engaged in a full range of activities in the oil and gas business. We are fully supportive of the development of international standards leading to convergence of the accounting standards under which our companies and our competitors report. The development of converged standards is obviously dependent on the selected standards enabling accurate reporting of the results of the enterprise and this gives rise to issues especially in respect of particular industries.

In the case of inventory valuation, we do not see that the elimination of the LIFO method as an improvement for the oil and gas industry, particularly because of the volatility of oil prices. The LIFO method is used extensively in North America and provides a framework for comparability of financial data by US oil and gas majors. Shell agrees with the objective of the IASB to eliminate alternative methods when they detract from comparability of financial statements but as noted above, we do not see this as the case with this suggested change.

The purpose of a choice of a particular method of accounting for inventories is to arrive at the appropriate determination of income. Different industries have practised specific inventory valuation methods for a number of years. In the oil and gas industry, LIFO is a valid alternative to FIFO in providing a fair representation of the physical flow of products when it is not possible to track the actual cost of each individual product. LIFO, although not exact, offers a method to arrive at a representation measurement. Although LIFO is not the only method used to value inventories, it is an alternative that has credibility and therefore should continue to be an acceptable method.

In the oil and gas industry, inventory levels are driven by both business and political considerations, in that quantities held are the minimum required either by law or by operating needs. Typically, the greater part of these inventories are of a longer-term nature. Currently, Shell's financial statements provide a proforma estimated Current Cost of Supplies measurement to reflect the approximate cost of actual flows of product. By providing these figures in our performance highlights, Shell presents our financial data in a comparable form to other oil and gas majors.

Although some would argue that applying a FIFO inventory valuation method represents the fair value on the balance sheet, it does neglect the significant impact of changing prices that should be reflected in the income statement. The same balance sheet data can be made available through additional FIFO disclosures in the notes to the financial statements. Eliminating LIFO will not improve the quality of financial information and may be a serious obstacle in the convergence of accounting rules in our industry. This could lead to dual accounting and reporting for a number of companies.

While we note that standard setters do not take into account fiscal consequences of their proposals, it should be pointed out that the elimination of LIFO would lead to difficulty and additional expense since the US fiscal authorities are likely to continue to require LIFO based fiscal reporting.

As far as we are aware, no national standard setter is contemplating the elimination of the LIFO method.

As an integrated oil and gas group, Shell is concerned over the proposed elimination of the LIFO method as an alternative under MS. A possible approach would be to limit the use of the LIFO method. The Board could describe the circumstances when LIFO could be used; but could stress the circumstances in which another valuation method is thought to provide a higher quality of financial reporting. By examining the options in light of the physical flow of actual inventories, the method applied should be the one that correctly reflects the impact to the business. These ideas could perhaps be developed in more detail as part of the extractive industries discussion.

We would be pleased to discuss these issues further if that would be helpful,

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