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From: Priestley, Don [mailto:Don.Priestley@santos.com]
Sent: 24 August 2004 05:29
To: Fleming Colin
Cc: gbrady@aasb.com.au; Wasow, Peter
Subject: ED6- Issue for Comment- level at which impairment is assessed

Dear Mr. Fleming

Santos Ltd is pleased to comment on the issue of the level at which impairment is to be assessed under ED 6.

Santos believes the concept "Cash-Generating Unit for Exploration and Evaluation Assets" should be retained and implementation guidance provided.

Companies in the upstream petroleum industry which apply either a "full cost" or an "area of interest" methodology in accounting for their exploration and evaluation activities generally **capitalise all** of their exploration costs when incurred and transfer those costs to the appropriate cost pool (country, geological province, or as otherwise defined) to be amortised as the reserves within the applicable costs pool are produced. These costs include "dry hole costs" or unsuccessful exploration and evaluation costs. The unamortised portions of the aggregate of these costs, even though they are "impaired", are carried forward on the statement of financial position so long as the costs are deemed to be recoverable from the aggregate of net cash flows from producing wells/fields within the relevant cost pool.

For companies accounting for their exploration and evaluation activities under "full cost" or "area of interest" methodologies, the capitalised dry hole costs (by definition) do not generate future cash flows nor are the Cash-Generating Units (i.e. existing producing wells/fields within a country or geological province) dependent on the past unsuccessful exploration to generate their own independent cash flows. Accordingly, under these accounting methodologies, the past unsuccessful exploration expenditure previously transferred to cost pools to be amortised will be written off when the Cash-Generating Unit concept imposed by IAS 36 is applied.

If it is the Board's intention to avoid wholesale changes to companies' accounting practices until such time as an IFRS for the Extractive Industries is developed, we believe that there is a need to specifically state that costs which are impaired within a Cash-Generating Unit for Exploration and Evaluation Assets should be transferred to the appropriate costs pool to be amortised. Where exploration and evaluation costs are incurred outside a producing cost pool (country, geological province or as otherwise defined) or "Cash-Generating Unit for Exploration and Evaluation Assets", and are deemed to be impaired, then they should be written down to their recoverable amounts (if any). It would be useful if ED 6 would clarify this process by further description and/or guidance by example.

The Australian Accounting Standards Board has recently announced that IASB has indicated that "full grandfathering of existing national GAAP will be permitted". If this is the case, then it will be necessary to clarify that the concept of Cash Generating Units will not apply to those companies who elect to fully grandfather a National GAAP that prescribes full cost or area of interests methodologies. It will also be necessary to clarify whether discounting is required where existing GAAP has no such requirement.

We note that in what ever form a "grandfather option" may take, the resulting accounting treatments for exploration and evaluation activities which may not be compatible with the IASB conceptual framework. Accordingly, **Santos strongly believes that companies in**

the extractive industries and in the absence of an industry specific standard should be allowed to determine its accounting policy for exploration and evaluation costs in accordance with IAS 8.

Regards,

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