

Comparison of the Successful Efforts Method and the Full Cost Method

The successful efforts method and the full cost method are two different methods of accounting for exploration and development costs in the extractive industries. The successful efforts method expenses exploration and development costs as they are incurred, while the full cost method capitalizes these costs and amortizes them over the life of the reserves.



A Comparison of the Successful Efforts Method and the Full Cost Method of Accounting for Oil and Gas Wells Operating Costs by Patricia Springer

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Successful Efforts Method

Under the successful efforts method, exploration and development costs are expensed as incurred. This means that these costs are not included in the cost of the proved reserves and are not amortized over the life of the reserves. The successful efforts method is often used by companies that

are exploring for new reserves, as it allows them to expense these costs immediately and reduce their current income taxes.

Advantages of the Successful Efforts Method

* Reduces current income taxes * Provides a more conservative estimate of proved reserves * Is simpler to apply than the full cost method

Disadvantages of the Successful Efforts Method

* May not provide a true picture of the company's financial position * Can lead to large fluctuations in earnings * May not be in accordance with GAAP

Full Cost Method

Under the full cost method, exploration and development costs are capitalized and amortized over the life of the reserves. This means that these costs are included in the cost of the proved reserves and are gradually expensed as the reserves are produced. The full cost method is often used by companies that have a large number of proved reserves, as it allows them to spread these costs over a longer period of time and reduce their current income taxes.

Advantages of the Full Cost Method

* Provides a more accurate picture of the company's financial position * Reduces fluctuations in earnings * Is in accordance with GAAP

Disadvantages of the Full Cost Method

* Increases current income taxes * Provides a less conservative estimate of proved reserves * Is more complex to apply than the successful efforts

method

Comparison of the Two Methods

The following table compares the successful efforts method and the full cost method:

Feature	Successful Efforts Method	Full Cost Method
Exploration and development costs	Expensed as incurred	Capitalized and amortized over the life of the reserves
Income taxes	Reduced current income taxes	Increased current income taxes
Estimate of proved reserves	More conservative	Less conservative
Complexity	Simpler to apply	More complex to apply
GAAP compliance	May not be in accordance with GAAP	In accordance with GAAP

The successful efforts method and the full cost method are two different ways of accounting for exploration and development costs in the extractive industries. Each method has its own advantages and disadvantages, and the choice of which method to use depends on the specific circumstances of the company.



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