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ASC 842 Expected to Impact Natural Resource Sector

AUDIT, ENERGY & RESOURCES, LEASES
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Accounting Standard Codification (ASC) Topic 842 - Leases, the new FASB lease accounting standard aimed at closing a major concern of stakeholders in lease accounting in accordance with ASC 840, went live for public companies this past January 1 and will be effective for nonpublic companies beginning January 1, 2020. Although the new standard scopes out leases for the exploration of minerals, oil, natural gas and other non-regenerative resources subject to the guidance of *FASB ASC 930, Extractive Activities - Mining* and *ASC 932, Extractive Activities - Oil and Gas*, companies in the natural resource sector are paying particular attention to the implementation rules.

Under ASC 842, more arrangements are expected to meet the definition of a lease compared with previous accounting standards. In accordance with the new guidance, a contract is or contains a lease if it conveys the right to control the use of identified property, plant or equipment for a period of time in exchange for consideration. That means agreements for processing and pipelines, gathering and transportation, and drill rig contracts may meet the definition of a lease under ASC 842.

Additionally, many lease arrangements include both lease and non-lease components as part of the consideration a company pays throughout a contract. In accordance with ASC 842, unless a company adopts a practical expedient to combine them, companies are now required to allocate a portion of the consideration paid to the different components based on standalone selling prices. Drill rig contracts deemed to be within the scope of ASC 842 could require such a review of the various components.

The new lease accounting standard is a significant change from the prior accounting rule. Assessing the impact will be important for companies as they communicate the changes to stakeholders.

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