

College of Business Academic Research Seminar



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Title:

Toxic Disclosures: The Case of British Petroleum

ABSTRACT

The Oil and Gas industry is subject to a substantial number of internal and external risks. The external risks are mostly classified as macro-economic or political. There are also many risks that are internal to the industry and to each firm. Combinations of various types of risk are likely. From an accounting perspective, the industry itself is characterized by high fixed costs, large capital expenditures and uncertainty regarding numerous factors such as the failure to find oil. Many events in the industry may be classified as high risk and reporting and disclosure these issues are of important as they may have catastrophic consequences. The industry also faces several ongoing financial reporting and valuation issues such as how to account for proven and probable reserves and the cost of operations. Measuring proven and probable reserves is problematic since in-ground oil and gas deposits are unobservable. Reserves presented on the balance sheet are subject to frequent revisions. The accounting industry partially attempts to deal with the cost issue by providing

managers with the option to use either the successful efforts or full cost method (Bryant, 2003).

In this paper, we focus on British Petroleum's disclosure of events relating to the recent oil spill in the Gulf of Mexico, often mentioned as the largest environmental disaster in US history. The blowout of BP's drilling platform in the Gulf of Mexico is an example of a rare high consequence event. In this exploratory study, we evaluate how the disclosure of the events surrounding the oil spill affects stock price returns and volatilities. During the time frame of the oil spill, BP disclosed 99 events, 77 of which were directly related to the oil spill. We break the disclosures into four categories: primary, secondary, other, and public relation events. The primary and secondary categories were directly related to the spill. The "other" category was not related to the oil spill. During the time frame of our study, BP also disclosed 13 events that were considered public relation related events.



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