

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Significant accounting judgments and estimates (continued)

Judgements (continued)

In selecting the most relevant and reliable accounting policies for IES contracts the main considerations are as follows:

- Determination of whether the joint arrangement is a joint venture or joint operation; though not directly related to revenue recognition this element has a material impact on the presentation of revenue for each project
- Whether the multiple service elements under the contract should be bifurcated such as construction phase followed by an operations and maintenance stage
- Whether the Group has legal rights to the production output and therefore is able to book reserves in respect of the project
- The nature and extent, if any, of volume and price financial exposures under the terms of the contract
- The extent to which the Group's capital investment is at risk and the mechanism for recoverability under the terms of the contract
- At what point can the revenues from each type of contract be estimated/reliably measured in accordance with IAS 18
- Whether there are any other remaining features unique to the contract that are relevant to the assessment

Revenue recognition on Integrated Energy Services (IES) contracts: the Group assesses on a case by case basis the most appropriate treatment for its various commercial structures which include Production Enhancement Contracts (PECs) and Prodcustio Sharing Contracts (PSCs) (see accounting policies note on page 27 for further details).

Statement of financial position classification of Integrated Energy Services (IES) contracts:

- The Group assesses on a case by case basis the most appropriate balance sheet classification of its Production Enhancement Contracts (PECs) (see accounting policy notes on page 27)
- In selecting the most appropriate policies for IES contracts, the main judgement is as follows:
 - The Mexican PEC assets are classified as tangible oil and gas assets in the consolidated statement of financial position as they have direct exposure to variable field production levels, and indirect exposure to changes in commodity prices. These exposures impact the generation of cash from the assets and any financial return thereon, including the risk of negative financial return. We believe this classification is most appropriate due to the nature of expenditure and it is aligned with our treatment in respect of PSC type arrangements where the risk/reward profile is similar

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the statement of financial position date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below:

- *Provisions for liquidated damages claims (LDs):* the Group provides for LD claims where there have been significant contract delays and it is considered probable that the customer will successfully pursue such a claim. This requires an estimate of the amount of LDs payable under a claim which involves a number of management judgements and assumptions regarding the amounts to recognise. A provision for liquidated damages of US\$ 48,546 thousand was created as at 31 December 2016 (2015: US\$ nil);
- *Project cost to complete estimates:* at each reporting date the Group is required to estimate costs to complete on fixed-price contracts. Estimating costs to complete on such contracts requires the Group to make estimates of future costs to be incurred, based on work to be performed beyond the reporting date. This estimate will impact revenues, cost of sales, work-in-progress, billings in excess of costs and estimated earnings and accrued contract expenses;
- *Recognition of contract variation orders (VOs):* the Group recognises revenues and margins from VOs where it is considered probable that they will be awarded by the customer and this requires management to assess the likelihood of such an award being made by reference to customer communications and other forms of documentary evidence;