

HESS CORP
Form 10-K
February 27, 2009

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

Form 10-K

**b ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2008

or

**o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File Number 1-1204

Hess Corporation

(Exact name of Registrant as specified in its charter)

DELAWARE

*(State or other jurisdiction of
incorporation or organization)*

**1185 AVENUE OF THE AMERICAS,
NEW YORK, N.Y.**

(Address of principal executive offices)

13-4921002

*(I.R.S. Employer
Identification Number)*

10036

(Zip Code)

(Registrant's telephone number, including area code, is (212) 997-8500)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock (par value \$1.00)	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The aggregate market value of voting stock held by non-affiliates of the Registrant amounted to \$36,438,000,000 computed using the outstanding common shares and closing market price on June 30, 2008.

At December 31, 2008, there were 326,132,740 shares of Common Stock outstanding.

Part III is incorporated by reference from the Proxy Statement for the annual meeting of stockholders to be held on May 6, 2009.

HESS CORPORATION

Form 10-K

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Hess Corporation (the Registrant) is a Delaware corporation, incorporated in 1920. The Registrant and its subsidiaries (collectively referred to as the Corporation or Hess) is a global integrated energy company that operates in two segments, Exploration and Production (E&P) and Marketing and Refining (M&R). The E&P segment explores for, develops, produces, purchases, transports and sells crude oil and natural gas. These exploration and production activities take place principally in Algeria, Australia, Azerbaijan, Brazil, Denmark, Egypt, Equatorial Guinea, Gabon, Ghana, Indonesia, Libya, Malaysia, Norway, Peru, Russia, Thailand, the United Kingdom and the United States. The M&R segment manufactures, purchases, transports, trades and markets refined petroleum products, natural gas and electricity. The Corporation owns 50% of a refinery joint venture in the United States Virgin Islands, and another refining facility, terminals and retail gasoline stations, most of which include convenience stores, located on the East Coast of the United States.

Exploration and Production

The Corporation's total proved reserves at December 31 were as follows:

	Crude Oil and Natural Gas Liquids		Natural Gas		Total Barrels of Oil Equivalent (BOE)*	
	2008	2007	2008	2007	2008	2007
	(Millions of barrels)		(Millions of mcf)		(Millions of barrels)	
United States	227	204	276	270	273	249
Europe	332	329	639	656	438	438
Africa	324	285	69	87	336	300
Asia and other	87	67	1,789	1,655	385	343
	970	885	2,773	2,668	1,432	1,330

* Reflects natural gas reserves converted on the basis of relative energy content (six mcf equals one barrel).

On a barrel of oil equivalent (boe) basis, 43% of the Corporation's worldwide proved reserves are undeveloped at December 31, 2008 (44% at December 31, 2007). Proved reserves held under production sharing contracts at December 31, 2008 totaled 28% of crude oil and natural gas liquids and 58% of natural gas reserves (25% and 57% respectively, at December 31, 2007).

Worldwide crude oil, natural gas liquids and natural gas production was as follows:

2008 2007 2006

Crude oil (thousands of barrels per day)

United States			
Onshore	17	15	15
Offshore	15	16	21
	32	31	36
Europe			
United Kingdom	29	38	50
Norway	16	19	22
Denmark	11	12	19
Russia	27	24	18
	83	93	109

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	2008	2007	2006
Africa			
Equatorial Guinea	72	56	28
Algeria	15	22	22
Gabon	14	14	12
Libya	23	23	23
	124	115	85
Asia and other			
Azerbaijan	7	16	7
Other	6	5	5
	13	21	12
Total	252	260	242
Natural gas liquids (thousands of barrels per day)			
United States			
Onshore	7	7	7
Offshore	3	3	3
	10	10	10
Europe			
United Kingdom	3	4	4
Norway	1	1	1
	4	5	5
Total	14	15	15
Natural gas (thousands of mcf per day)			
United States			
Onshore	41	42	54
Offshore	37	46	56
	78	88	110
Europe			
United Kingdom	223	231	244
Norway	22	18	22
Denmark	10	10	17
	255	259	283
Asia and other			

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Joint Development Area of Malaysia and Thailand (JDA)	185	115	131
Thailand	87	90	60
Indonesia	82	59	26
Other	2	2	2
	356	266	219
Total	689	613	612
Barrels of oil equivalent*	381	377	359

* Reflects natural gas production converted on the basis of relative energy content (six mcf equals one barrel).

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The Corporation presently estimates that its 2009 production will be approximately 380,000 to 390,000 barrels of oil equivalent per day (boepd).

A description of our significant E&P operations follows:

United States

At December 31, 2008, 19% of the Corporation's total proved reserves were located in the United States. During 2008, 16% of the Corporation's crude oil and natural gas liquids production and 11% of its natural gas production were from United States operations. The Corporation's production in the United States was principally from properties offshore in the Gulf of Mexico, which include the Llano (Hess 50%), Conger (Hess 38%), Baldpate (Hess 50%), Hack Wilson (Hess 25%) and Penn State (Hess 50%) fields, as well as onshore properties in North Dakota and in the Permian Basin of Texas.

In the deepwater Gulf of Mexico, development of the Shenzi Field (Hess 28%) progressed in 2008. Tension leg platform tendons, hull and topsides were installed and flowlines were laid and tested. First production is expected in the second quarter of 2009.

In the Williston Basin of North Dakota, the Corporation holds a net acreage position in the Bakken Play of approximately 570,000 acres. In 2009, the Corporation plans to drill additional production wells and expand production facilities.

The Corporation is developing a residual oil zone at the Seminole-San Andres Unit (Hess 34%) in Texas where carbon dioxide gas supplied from its interests in the West Bravo Dome and Bravo Dome fields in New Mexico will be injected to enhance recovery of crude oil.

In the Pony prospect on Green Canyon Block 468 (Hess 100%) in the deepwater Gulf of Mexico, the Corporation successfully completed drilling an appraisal well in June 2008. The Corporation is evaluating development options for Pony.

At the Corporation's Tubular Bells prospect (Hess 20%) located in the Mississippi Canyon area of the deepwater Gulf of Mexico, a third well was successfully drilled during 2008. The operator is evaluating development options for Tubular Bells.

At December 31, 2008, the Corporation had interests in more than 400 exploration blocks in the Gulf of Mexico, which included 1,442,020 net undeveloped acres.

Europe

At December 31, 2008, 31% of the Corporation's total proved reserves were located in Europe (United Kingdom 9%, Norway 13%, Denmark 3% and Russia 6%). During 2008, 33% of the Corporation's crude oil and natural gas liquids production and 37% of its natural gas production were from European operations.

United Kingdom: Production of crude oil and natural gas liquids from the United Kingdom North Sea was principally from the Corporation's non-operated interests in Nevis (Hess 39%), Schiehallion (Hess 16%), Clair (Hess 9%), Bittern (Hess 28%) and Beryl (Hess 22%) fields. Natural gas production from the United Kingdom was primarily from the Atlantic (Hess 25%) and Cromarty (Hess 90%), Easington Catchment Area (Hess 32%), Bacton area (Hess 23%), Beryl (Hess 22%), Everest (Hess 19%), Lomond (Hess 17%) and Nevis (Hess 39%) fields.

Norway: Substantially all of the 2008 and 2007 Norwegian production was from the Corporation's interest in the Valhall Field (Hess 28%). A field redevelopment for Valhall commenced in 2008 and is expected to be completed in 2010. The Corporation also holds an interest in the Snohvit Field (Hess 3%) located offshore Norway.

Denmark: Crude oil and natural gas production comes from the Corporation's interest in the South Arne Field (Hess 58%).

Russia: The Corporation's activities in Russia are conducted through its 80%-owned interest in a corporate joint venture operating in the Volga-Urals region of Russia.

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Africa

At December 31, 2008, 23% of the Corporation's total proved reserves were located in Africa (Equatorial Guinea 8%, Algeria 4%, Libya 10% and Gabon 1%). During 2008, 46% of the Corporation's crude oil and natural gas liquids production was from African operations.

Equatorial Guinea: The Corporation is the operator and owns an interest in Block G (Hess 85%) which contains the Ceiba Field and Okume Complex.

Algeria: The Corporation has a 49% interest in a venture with the Algerian national oil company that is redeveloping three oil fields.

Libya: The Corporation, in conjunction with its Oasis Group partners, has oil and gas production operations in the Waha concessions in Libya (Hess 8%). The Corporation also owns a 100% interest in offshore exploration Area 54, where a successful exploration well was drilled in 2008. The Corporation intends to obtain 3D seismic in Area 54 and further drilling is planned.

Gabon: The Corporation's activities in Gabon are conducted through its Gabonese subsidiary, where the Corporation has interests in the Rabi Kounga, Toucan and Atora fields. In the third quarter of 2008, the Corporation acquired the remaining 22.5% interest in the Gabonese subsidiary.

Egypt: The Corporation has a 25-year development lease for the West Mediterranean Block 1 concession (West Med Block) (Hess 55%), which contains four existing natural gas discoveries and additional exploration opportunities. During 2008, the Corporation drilled a successful exploration well on the block, which encountered natural gas and crude oil. The Corporation is currently conducting engineering studies and further exploratory drilling is planned.

Ghana: The Corporation holds a 100% interest in the Cape Three Points South Block located offshore Ghana. The Corporation is currently acquiring new 3D seismic in the unexplored western half of the license area.

Asia and Other

At December 31, 2008, 27% of the Corporation's total proved reserves were located in the Asia and other region (JDA 13%, Indonesia 9%, Thailand 3% and Azerbaijan 2%). During 2008, 5% of the Corporation's crude oil and natural gas liquids production and 52% of its natural gas production were from Asia and other operations.

Joint Development Area of Malaysia and Thailand: The Corporation owns an interest in Block A-18 of the JDA (Hess 50%) in the Gulf of Thailand. Phase 2 gas sales commenced in November of 2008 upon commissioning of a third-party gas export pipeline to Thailand.

Indonesia: The Corporation's natural gas production in Indonesia primarily comes from its interests offshore in the Ujung Pangkah project (Hess 75%), which commenced in 2007, and the Natuna A Field (Hess 23%). Additional production from a Phase 2 oil project at Ujung Pangkah is expected in mid 2009. The Corporation also owns an interest in the onshore Jambi Merang natural gas project (Hess 25%), which was sanctioned for development in 2007. In the fourth quarter of 2008, the Corporation acquired a 100% working interest in the offshore Semai V exploration block.

Thailand: The Corporation's natural gas production in Thailand primarily comes from the offshore Pailin Field (Hess 15%) and the onshore Sinphuhorm Block (Hess 35%).

Azerbaijan: The Corporation has an interest in the Azeri-Chirag-Gunashli (ACG) fields (Hess 3%) in the Caspian Sea. The Corporation also holds an interest in the Baku-Tbilisi-Ceyhan (BTC) Pipeline (Hess 2%).

Australia: The Corporation holds a 100% interest in an exploration license covering 780,000 acres in the Carnarvon basin offshore Western Australia (WA-Block 390-P). During 2008, the Corporation completed drilling its initial four exploration wells of a 16 well commitment on the block. Three of the four wells discovered natural gas and the Corporation plans to drill five additional exploration wells in 2009. The Corporation also holds a 50% interest in WA-Block 404-P located offshore Western Australia, which covers a total area of 680,000 acres. The operator plans to drill three wells on this block in 2009.

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Brazil: The Corporation has interests in two blocks located offshore Brazil, the BM-S-22 Block (Hess 40%) in the Santos Basin and the BM-ES-30 Block (Hess 60%) in the Espirito Santo Basin. The operator commenced drilling of the Azulao exploration well on BM-S-22 in 2008 and filed a Notice of Discovery with the regulators on January 16, 2009. The operator plans to drill another well on BM-S-22 in 2009.

Oil and Gas Reserves

The Corporation's net proved oil and gas reserves at the end of 2008, 2007 and 2006 are presented under Supplementary Oil and Gas Data on pages 75 through 81 in the accompanying financial statements.

During 2008, the Corporation provided oil and gas reserve estimates for 2007 to the United States Department of Energy. Such estimates are consistent with the information furnished to the SEC on Form 10-K for the year ended December 31, 2007, although not necessarily directly comparable due to the requirements of the individual requests. There were no differences in excess of 5%.

Sales commitments: The Corporation has no contracts or agreements to sell fixed quantities of its crude oil production. In the United States, natural gas is marketed by the M&R segment on a spot basis and under contracts for varying periods to local distribution companies, and commercial, industrial and other purchasers. The Corporation's United States natural gas production is expected to approximate 20% of its 2009 sales commitments under long-term contracts. The Corporation attempts to minimize supply risks associated with its United States natural gas supply commitments by entering into purchase contracts with third parties having reliable sources of supply, on terms substantially similar to those under its commitments and by leasing storage facilities.

Outside of the United States, the Corporation generally sells its natural gas production under long-term sales contracts at prices that are periodically adjusted due to changes in commodity prices or other indices. In the United Kingdom, the Corporation sells the majority of its natural gas production on a spot basis.

Table of Contents**Average selling prices and average production costs**

	2008	2007	2006
Average selling prices*			
Crude oil (per barrel)			
United States	\$ 96.82	\$ 69.23	\$ 60.45
Europe	78.75	60.99	56.19
Africa	78.72	62.04	51.18
Asia and other	97.07	72.17	61.52
Worldwide	82.04	63.44	55.31
Natural gas liquids (per barrel)			
United States	\$ 64.98	\$ 51.89	\$ 46.22
Europe	74.63	57.20	47.30
Worldwide	67.61	53.72	46.59
Natural gas (per mcf)			
United States	\$ 8.61	\$ 6.67	\$ 6.59
Europe	9.44	6.13	6.20
Asia and other	5.24	4.71	4.05
Worldwide	7.17	5.60	5.50
Average production (lifting) costs per barrel of oil equivalent produced**			
United States	\$ 18.46	\$ 13.56	\$ 9.54
Europe	17.12	14.06	10.73
Africa	10.22	9.09	9.03
Asia and other	8.48	8.41	6.54
Worldwide	13.43	11.50	9.55

* *Includes inter-company transfers valued at approximate market prices and the effect of the Corporation's hedging activities.*

** *Production (lifting) costs consist of amounts incurred to operate and maintain the Corporation's producing oil and gas wells, related equipment and facilities (including lease costs of floating production and storage facilities), transportation costs and production and severance taxes. The average production costs per barrel of oil equivalent reflect the crude oil equivalent of natural gas production converted on the basis of relative energy content (six mcf equals one barrel).*

The table above does not include costs of finding and developing proved oil and gas reserves, or the costs of related general and administrative expenses, interest expense and income taxes.

Gross and net undeveloped acreage at December 31, 2008

Undeveloped Acreage*	
Gross	Net
(In thousands)	

United States	2,919	1,971
Europe	2,099	673
Africa	9,979	6,464
Asia and other	8,849	4,323
Total**	23,846	13,431

* *Includes acreage held under production sharing contracts.*

** *Licenses covering approximately 33% of the Corporation's net undeveloped acreage held at December 31, 2008 are scheduled to expire during the next three years pending the results of exploration activities. These scheduled expirations are largely in Libya (offshore exploration Area 54), U.S. and Egypt.*

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	Developed Acreage Applicable to Productive Wells		Productive Wells*			
	Gross	Net	Oil		Gas	
			Gross	Net	Gross	Net
	(In thousands)					
United States	529	455	774	431	59	45
Europe	1,362	758	269	105	145	32
Africa	9,919	958	987	154		
Asia and other	2,185	624	64	7	385	85
Total	13,995	2,795	2,094	697	589	162

* Includes multiple completion wells (wells producing from different formations in the same bore hole) totaling 312 gross wells and 54 net wells.

Number of net exploratory and development wells drilled

	Net Exploratory Wells			Net Development Wells		
	2008	2007	2006	2008	2007	2006
Productive wells						
United States	2	1	1	50	54	24
Europe	11	3	1	11	14	20
Africa	1	1		23	23	17
Asia and other	5	3	6	25	15	11
	19	8	8	109	106	72
Dry holes						
United States		1	4	1		
Europe	3	1				
Africa	2	1				
Asia and other	1					
	6	3	4	1		
Total	25	11	12	110	106	72

Number of wells in process of drilling at December 31, 2008

	Gross Wells	Net Wells
United States	37	13
Europe	12	7
Africa	8	2
Asia and other	7	2
Total	64	24

Number of net waterfloods and pressure maintenance projects in process of installation at December 31, 2008 1

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Total refined product sales were as follows:

	2008*	2007*	2006*
	(Thousands of barrels per day)		
Gasoline	234	210	218
Distillates	143	147	144
Residuals	56	62	60
Other	39	32	37
Total	472	451	459

* *Of total refined products sold in 2008, 2007 and 2006 approximately 50% was obtained from HOVENSA and Port Reading. The Corporation purchased the balance from third parties under short-term supply contracts and spot purchases.*

Refining

The Corporation owns a 50% interest in HOVENSA L.L.C. (HOVENSA), a refining joint venture in the United States Virgin Islands with a subsidiary of Petroleos de Venezuela S.A. (PDVSA). In addition, it owns and operates a refining facility in Port Reading, New Jersey.

HOVENSA: Refining operations at HOVENSA consist of crude units, a fluid catalytic cracking unit and a delayed coker unit.

The following table summarizes capacity and utilization rates for HOVENSA:

	Refinery Capacity	Refinery Utilization		
	(Thousands of barrels per day)	2008	2007	2006
Crude	500	88.2%	90.8%	89.7%
Fluid catalytic cracker	150	72.7%	87.1%	84.3%
Coker	58	92.4%	83.4%	84.3%

The delayed coker unit permits HOVENSA to run lower-cost heavy crude oil. HOVENSA has a long-term supply contract with PDVSA to purchase 115,000 barrels per day of Venezuelan Merey heavy crude oil. PDVSA also supplies 155,000 barrels per day of Venezuelan Mesa medium gravity crude oil to HOVENSA under a long-term

crude oil supply contract. The remaining crude oil requirements are purchased mainly under contracts of one year or less from third parties and through spot purchases on the open market. After sales of refined products by HOVENSA to third parties, the Corporation purchases 50% of HOVENSA's remaining production at market prices.

Gross crude runs at HOVENSA averaged 441,000 barrels per day in 2008 compared with 454,000 barrels per day in 2007 and 448,000 barrels per day in 2006. The 2008 utilization rate for the fluid catalytic cracking unit at HOVENSA reflects lower utilization due to weak refining margins, planned and unplanned maintenance of certain units, and a refinery wide shut down for Hurricane Omar. During the second quarter of 2007, the coker unit at HOVENSA was shut down for approximately 30 days for a scheduled turnaround. The fluid catalytic cracking unit at HOVENSA was shut down for approximately 22 days of unplanned maintenance in 2006.

Port Reading Facility: The Corporation owns and operates a fluid catalytic cracking facility in Port Reading, New Jersey, with a capacity of 70,000 barrels per day. This facility, which processes residual fuel oil and vacuum gas oil, operated at a rate of approximately 64,000 barrels per day in 2008 compared with 61,000 barrels per day in 2007 and 63,000 barrels per day in 2006. Substantially all of Port Reading's production is gasoline and heating oil.

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Marketing

The Corporation markets refined petroleum products, natural gas and electricity on the East Coast of the United States to the motoring public, wholesale distributors, industrial and commercial users, other petroleum companies, governmental agencies and public utilities.

The Corporation had 1,366 HESS® gasoline stations at December 31, 2008, including stations owned by its WilcoHess joint venture (Hess 44%). Approximately 90% of the gasoline stations are operated by the Corporation or WilcoHess. Of the operated stations, 93% have convenience stores on the sites. Most of the Corporation's gasoline stations are in New York, New Jersey, Pennsylvania, Florida, Massachusetts, North Carolina and South Carolina.

Refined product sales averaged 472,000 barrels per day in 2008 compared with 451,000 barrels per day in 2007 and 459,000 barrels in 2006. Total energy marketing natural gas sales volumes, including utility and spot sales, were approximately 2.0 million mcf per day in 2008, 1.9 million mcf per day in 2007 and 1.8 million mcf per day in 2006. In addition, energy marketing sold electricity volumes at the rate of 3,200, 2,800 and 1,400 megawatts (round the clock) in 2008, 2007 and 2006, respectively. The increases reflect the impact of acquisitions and organic growth.

The Corporation owns 21 terminals with an aggregate storage capacity of 22 million barrels in its East Coast marketing areas. The Corporation also owns a terminal in St. Lucia with a storage capacity of 10 million barrels, which is operated for third party storage.

The Corporation has a 50% voting interest in a consolidated partnership that trades energy commodities and derivatives. The Corporation also takes energy commodity and derivative trading positions for its own account.

The Corporation also has a 92.5% interest in Hess LNG, which is pursuing investments in liquefied natural gas (LNG) terminals and related supply, trading and marketing opportunities. The joint venture is pursuing the development of LNG terminal projects located in Fall River, Massachusetts and Shannon, Ireland. In addition, a wholly-owned subsidiary of the Corporation is exploring the development of fuel cell technology.

Competition and Market Conditions

See Item 1A, *Risk Factors Related to Our Business and Operations*, for a discussion of competition and market conditions.

Other Items

Compliance with various existing environmental and pollution control regulations imposed by federal, state, local and foreign governments is not expected to have a material adverse effect on the Corporation's financial condition or results of operations. The Corporation spent \$23 million in 2008 for environmental remediation.

The number of persons employed by the Corporation at year end was approximately 13,500 in 2008 and 13,300 in 2007.

The Corporation's Internet address is www.hess.com. On its website, the Corporation makes available free of charge its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after the Corporation electronically files with or furnishes such material to the Securities and Exchange Commission. Copies of the Corporation's Code of Business Conduct and Ethics, its Corporate Governance Guidelines and the charters of the Audit Committee, the Compensation and Management Development Committee and the

Corporate Governance and Nominating Committee of the Board of Directors are available on the Corporation's website and are also available free of charge upon request to the Secretary of the Corporation at its principal executive offices. The Corporation has also filed with the New York Stock Exchange (NYSE) its annual certification that the Corporation's chief executive officer is unaware of any violation of the NYSE's corporate governance standards.

Table of Contents**Item 1A. *Risk Factors Related to Our Business and Operations***

Our business activities and the value of our securities are subject to significant risk factors, including those described below. The risk factors described below could negatively affect our operations, financial condition, liquidity and results of operations, and as a result, holders and purchasers of our securities could lose part or all of their investments. It is possible additional risks relating to our securities may be described in a prospectus supplement if we issue securities in the future.

Commodity Price Risk: Our estimated proved reserves, revenue, operating cash flows, operating margins, future earnings and trading operations are highly dependent on the prices of crude oil, natural gas and refined petroleum products, which are influenced by numerous factors beyond our control. Historically these prices have been very volatile and most recently have been adversely affected by falling demand caused by the global economic downturn. The major foreign oil producing countries, including members of the Organization of Petroleum Exporting Countries (OPEC), exert considerable influence over the supply and price of crude oil and refined petroleum products. Their ability or inability to agree on a common policy on rates of production and other matters has a significant impact on the oil markets. The commodities trading markets may also influence the selling prices of crude oil, natural gas and refined petroleum products. If crude oil and natural gas prices remain at year-end 2008 levels, our revenues, profitability and cash flow will be lower in 2009 compared with 2008. In addition, if crude oil and natural gas prices decline further from year-end 2008 levels, it could result in a reduction in the carrying value of our oil and gas assets, proved oil and gas reserves, deferred tax assets and goodwill. To the extent that we engage in hedging activities to mitigate commodity price volatility, we may not realize the benefit of price increases above the hedged price. Changes in commodity prices can also have a material impact on margin requirements under our derivative contracts.

Technical Risk: We own or have access to a finite amount of oil and gas reserves which will be depleted over time. Replacement of oil and gas reserves is subject to successful exploration drilling, development activities, and enhanced recovery programs. Reserve replacement can also be achieved through acquisition. Therefore, future oil and gas production is dependent on technical success in finding and developing additional hydrocarbon reserves. Exploration activity involves the interpretation of seismic and other geological and geophysical data, which does not always successfully predict the presence of commercial quantities of hydrocarbons. Drilling risks include unexpected adverse conditions, irregularities in pressure or formations, equipment failure, blowouts and weather interruptions. Future developments may be affected by unforeseen reservoir conditions which negatively affect recovery factors or flow rates. The costs of drilling and development activities have increased in recent years which could negatively affect expected economic returns. Although due diligence is used in evaluating acquired oil and gas properties, similar uncertainties may be encountered in the production of oil and gas on properties acquired from others.

Oil and Gas Reserves and Discounted Future Net Cash Flow Risks: Numerous uncertainties exist in estimating quantities of proved reserves and future net revenues from those reserves. Actual future production, oil and gas prices, revenues, taxes, capital expenditures, operating expenses, geologic success and quantities of recoverable oil and gas reserves may vary substantially from those assumed in the estimates and could materially affect the estimated quantities and future net revenues of our proved reserves. In addition, reserve estimates may be subject to downward or upward revisions based on production performance, purchases or sales of properties, results of future development, prevailing oil and gas prices, production sharing contracts which may decrease reserves as crude oil and natural gas prices increase, and other factors.

Political Risk: Federal, state, local, territorial and foreign laws and regulations relating to tax increases and retroactive tax claims, expropriation or nationalization of property, mandatory government participation, cancellation or amendment of contract rights, and changes in import regulations, limitations on access to exploration and development opportunities, as well as other political developments may affect our operations. Some of the international areas in which we operate are politically less stable than our domestic operations. In addition, the threat

of terrorism around the world poses additional risks to the operations of the oil and gas industry. In our M&R segment, we market motor fuels through lessee-dealers and wholesalers in certain states where legislation prohibits producers or refiners of crude oil from directly engaging in retail marketing of motor fuels. Similar legislation has been periodically proposed in the U.S. Congress and in various other states.

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Environmental Risk: Our oil and gas operations, like those of the industry, are subject to environmental risk such as oil spills, produced water spills, gas leaks and ruptures and discharges of substances or gases that could expose us to substantial liability for pollution or other environmental damage. Our operations are also subject to numerous United States federal, state, local and foreign environmental laws and regulations. Non-compliance with these laws and regulations may subject us to administrative, civil or criminal penalties, remedial clean-ups and natural resource damages or other liabilities. In addition, increasingly stringent environmental regulations, particularly relating to the production of motor and other fuels and the potential for controls on greenhouse gas emissions, have resulted, and will likely continue to result, in higher capital expenditures and operating expenses for us and the oil and gas industry in general.

Competitive Risk: The petroleum industry is highly competitive and very capital intensive. We encounter competition from numerous companies in each of our activities, including acquiring rights to explore for crude oil and natural gas, and in purchasing and marketing of refined products and natural gas. Many competitors, including national oil companies, are larger and have substantially greater resources. We are also in competition with producers and marketers of other forms of energy. Increased competition for worldwide oil and gas assets has significantly increased the cost of acquisitions. In addition, competition for drilling services, technical expertise and equipment has affected the availability of technical personnel and drilling rigs and has increased capital and operating costs.

Catastrophic Risk: Although we maintain a level of insurance coverage consistent with industry practices against property and casualty losses, our oil and gas operations are subject to unforeseen occurrences which may damage or destroy assets or interrupt operations. Examples of catastrophic risks include hurricanes, fires, explosions and blowouts. These occurrences have affected us from time to time. During 2008, our annual Gulf of Mexico production of crude oil and natural gas was reduced by an estimated 7,000 boepd due to the impact of Hurricanes Ike and Gustav.

Item 3. *Legal Proceedings*

The Registrant, along with many other companies engaged in refining and marketing of gasoline, has been a party to lawsuits and claims related to the use of methyl tertiary butyl ether (MTBE) in gasoline. A series of similar lawsuits, many involving water utilities or governmental entities, were filed in jurisdictions across the United States against producers of MTBE and petroleum refiners who produced gasoline containing MTBE, including the Registrant. While the majority of the cases were settled in 2008, the Registrant remains a defendant in approximately 20 cases. These cases have been consolidated for pre-trial purposes in the Southern District of New York as part of a multi-district litigation proceeding, with the exception of an action brought in state court by the State of New Hampshire. The principal allegation in all cases is that gasoline containing MTBE is a defective product and that these parties are strictly liable in proportion to their share of the gasoline market for damage to groundwater resources and are required to take remedial action to ameliorate the alleged effects on the environment of releases of MTBE. The damages claimed in these actions are substantial and in almost all cases, punitive damages are also sought. In the fourth quarter 2007, the Corporation recorded a pre-tax charge of \$40 million related to MTBE litigation, including amounts for the cases settled in 2008.

Over the last several years, many refiners have entered into consent agreements to resolve the United States Environmental Protection Agency's (EPA) assertions that refining facilities were modified or expanded without complying with New Source Review regulations that require permits and new emission controls in certain circumstances and other regulations that impose emissions control requirements. These consent agreements, which arise out of an EPA enforcement initiative focusing on petroleum refiners and utilities, have typically imposed substantial civil fines and penalties and required (i) significant capital expenditures to install emissions control equipment over a three to eight year time period and (ii) changes to operations which resulted in increased operating costs. The capital expenditures, penalties and supplemental environmental projects for individual refineries covered by the settlements can vary significantly, depending on the size and configuration of the refinery, the circumstances of

the alleged modifications and whether the refinery has previously installed more advanced pollution controls. EPA initially contacted Registrant and HOVENSA regarding the Petroleum Refinery Initiative in August 2003. Negotiations with EPA and the relevant states and the Virgin Islands are continuing and substantial progress has been made toward resolving this matter for both the Corporation and HOVENSA. While

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the effect on the Corporation of the Petroleum Refining Initiative cannot be estimated until a final settlement is reached and entered by a court, additional future capital expenditures and operating expenses will likely be incurred over a number of years. The amount of penalties, if any, is not expected to be material to the Corporation.

On September 13, 2007, HOVENSA received a Notice Of Violation (NOV) pursuant to section 113(a)(i) of the Clean Air Act (Act) from the EPA finding that HOVENSA failed to obtain proper permitting for the construction and operation of its delayed coking unit in accordance with applicable law and regulations. HOVENSA believes it properly obtained all necessary permits for this project. The NOV states that EPA has authority to issue an administrative order assessing penalties for violation of the Act. HOVENSA has entered into discussions with the EPA to reach resolution of this matter. Registrant does not believe that this matter will result in material liability to HOVENSA or Registrant.

In December 2006, HOVENSA received a NOV from the EPA alleging non-compliance with emissions limits in a permit issued by the Virgin Islands Department of Planning and Natural Resources (DPNR) for the two process heaters in the delayed coking unit. The NOV was issued in response to a voluntary investigation and submission by HOVENSA regarding potential non-compliance with the permit emissions limits for two pollutants. Any exceedances were minor from the perspective of the amount of pollutants emitted in excess of the limits. HOVENSA has entered into discussions with the appropriate governmental agencies to reach resolution of this matter and does not believe that it will result in material liability to HOVENSA or the Corporation.

Registrant received a directive from the New Jersey Department of Environmental Protection (NJDEP) to remediate contamination in the sediments of the lower Passaic River and NJDEP is also seeking natural resource damages. The directive, insofar as it affects Registrant, relates to alleged releases from a petroleum bulk storage terminal in Newark, New Jersey now owned by the Registrant. Registrant and over 70 companies entered into an Administrative Order on Consent with EPA to study the same contamination. NJDEP has also sued several other companies linked to a facility considered by the State to be the largest contributor to river contamination. In January 2009, these companies added third party defendants, including the Registrant, to that case. In June 2007, EPA issued a draft study which evaluated six alternatives for early action, with costs ranging from \$900 million to \$2.3 billion. Based on adverse comments from Registrant and others, EPA is reevaluating its alternatives. In addition, the federal trustees for natural resources have begun a separate assessment of damages to natural resources in the Passaic River. Given the ongoing studies, remedial costs cannot be reliably estimated at this time. Based on currently known facts and circumstances, the Registrant does not believe that this matter will result in material liability because its terminal could not have contributed contamination along most of the river's length and did not store or use contaminants which are of the greatest concern in the river sediments, and because there are numerous other parties who will likely share in the cost of remediation and damages.

In July 2004, Hess Oil Virgin Islands Corp. (HOVIC), a wholly owned subsidiary of the Registrant, and HOVENSA, each received a letter from the Commissioner of the Virgin Islands Department of Planning and Natural Resources and Natural Resources Trustees, advising of the Trustees' intention to bring suit against HOVIC and HOVENSA under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA). The letter alleges that HOVIC and HOVENSA are potentially responsible for damages to natural resources arising from releases of hazardous substances from the HOVENSA Oil Refinery. HOVENSA currently owns and operates a petroleum refinery on the south shore of St. Croix, United States Virgin Islands, which had been operated by HOVIC until October 1998. An action was filed on May 5, 2005 in the District Court of the Virgin Islands against HOVENSA, HOVIC and other companies that operated industrial facilities on the south shore of St. Croix asserting that the defendants are liable under CERCLA and territorial statutory and common law for damages to natural resources. HOVIC and HOVENSA do not believe that this matter will result in a material liability as they believe that they have strong defenses to this complaint, and they intend to vigorously defend this matter.

The Registrant periodically receives notices from EPA that it is a potential responsible party under the Superfund legislation with respect to various waste disposal sites. Under this legislation, all potentially responsible parties are jointly and severally liable. For certain sites, EPA's claims or assertions of liability against the Corporation relating to these sites have not been fully developed. With respect to the remaining sites, EPA's claims have been settled, or a proposed settlement is under consideration, in all cases for amounts that are not material. The ultimate impact of these proceedings, and of any related proceedings by private parties, on the

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business or accounts of the Corporation cannot be predicted at this time due to the large number of other potentially responsible parties and the speculative nature of clean-up cost estimates, but is not expected to be material.

The Securities and Exchange Commission (SEC) notified the Registrant that on July 21, 2005, it commenced a private investigation into payments made to the government of Equatorial Guinea or to officials and persons affiliated with officials of the government of Equatorial Guinea. The SEC has requested documents and information from the Registrant and other oil and gas companies that have operations or interests in Equatorial Guinea. Registrant has provided the documents and information requested.

The Corporation is from time to time involved in other judicial and administrative proceedings, including proceedings relating to other environmental matters. Although the ultimate outcome of these proceedings cannot be ascertained at this time and some of them may be resolved adversely to the Corporation, no such proceeding is required to be disclosed under applicable rules of the SEC. In management's opinion, based upon currently known facts and circumstances, such proceedings in the aggregate will not have a material adverse effect on the financial condition of the Corporation.

Table of Contents**Item 4. Submission of Matters to a Vote of Security Holders**

During the fourth quarter of 2008, no matter was submitted to a vote of security holders through the solicitation of proxies or otherwise.

Executive Officers of the Registrant

The following table presents information as of February 1, 2009 regarding executive officers of the Registrant:

Name	Age	Office Held*	Year Individual Became an Executive Officer
John B. Hess	54	Chairman of the Board, Chief Executive Officer and Director	1983
J. Barclay Collins II	64	Executive Vice President and Director	1986
Gregory P. Hill	47	Executive Vice President and President of Worldwide Exploration and Production	2009
John J. O Connor	62	Executive Vice President and Director	2001
F. Borden Walker	55	Executive Vice President and President of Marketing and Refining and Director	1996
Brian J. Bohling	48	Senior Vice President	2004
William T. Drennen	58	Senior Vice President	2007
John A. Gartman	61	Senior Vice President	1997
Timothy B. Goodell	51	Senior Vice President and General Counsel	2009
Scott Heck	51	Senior Vice President	2005
Lawrence H. Ornstein	57	Senior Vice President	1995
Howard Paver	58	Senior Vice President	2002
John P. Rielly	46	Senior Vice President and Chief Financial Officer	2002
Lori J. Ryerkerk	46	Senior Vice President	2008
George F. Sandison	52	Senior Vice President	2003
John J. Scelfo	51	Senior Vice President	2004
Gordon Shearer	54	Senior Vice President	2007
John V. Simon	55	Senior Vice President	2007
Sachin Mehra	38	Vice President and Treasurer	2008

* All officers referred to herein hold office in accordance with the By-Laws until the first meeting of the Directors following the annual meeting of stockholders of the Registrant and until their successors shall have been duly chosen and qualified. Each of said officers was elected to the office opposite his or her name on May 7, 2008, except for Messrs. Hill and Goodell and Ms. Ryerkerk, who were elected effective January 1, 2009, January 5, 2009 and November 5, 2008, respectively. The first meeting of Directors following the next annual meeting of stockholders of the Registrant is scheduled to be held May 6, 2009.

Except for Messrs. Hill, Bohling, Drennen, Goodell, Mehra, Shearer and Ms. Ryerkerk, each of the above officers has been employed by the Registrant or its subsidiaries in various managerial and executive capacities for more than five years. Prior to joining the Corporation, Mr. Hill served in senior executive positions in exploration and production operations of Royal Dutch Shell and its subsidiaries for 25 years. Mr. Bohling was employed in senior human resource positions with American Standard Corporation and CDI Corporation before joining the Registrant in 2004. Mr. Drennen served in senior executive positions in exploration and technology at ExxonMobil and its subsidiaries prior to joining the Corporation in 2007. Before joining the Corporation in 2009, Mr. Goodell

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was a partner in the law firm of White & Case LLP. Ms. Ryerkerk was employed in senior managerial positions principally in the refining and marketing operations of ExxonMobil prior to joining the Corporation in 2008. Mr. Mehra was employed in treasury and financial functions at General Motors before joining the Corporation in 2007. Prior to joining Hess LNG, a joint venture subsidiary of the Corporation, in 2004, Mr. Shearer was a consultant at Poten Partners, and held other senior positions in the liquefied natural gas industry.

PART II**Item 5. *Market for the Registrant's Common Stock, Related Stockholder Matters and Issuer Purchases of Equity Securities******Stock Market Information***

The common stock of Hess Corporation is traded principally on the New York Stock Exchange (ticker symbol: HES). High and low sales prices were as follows:

Quarter Ended	2008		2007	
	High	Low	High	Low
March 31	\$ 101.65	\$ 76.67	\$ 58.00	\$ 45.96
June 30	137.00	88.20	61.48	54.55
September 30	129.00	71.16	69.87	53.12
December 31	82.03	35.50	105.85	63.58

Performance Graph

Set forth below is a line graph comparing the Corporation's cumulative total shareholder return for five years, assuming reinvestment of dividends on common stock, with the cumulative total return of:

Standard & Poor's 500 Stock Index, which includes the Corporation, and

AMEX Oil Index, which is comprised of companies involved in various phases of the oil industry including the Corporation.

Comparison of Five-Year Shareholder Returns
Years Ended December 31,

Holdings

At December 31, 2008, there were 5,909 stockholders (based on number of holders of record) who owned a total of 326,132,740 shares of common stock.

Table of Contents***Dividends***

Cash dividends on common stock totaled \$.40 per share (\$.10 per quarter) during 2008 and 2007.

Equity Compensation Plans

Following is information on the Registrant's equity compensation plans at December 31, 2008:

Plan Category	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights (a)	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights (b)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a)) (c)
Equity compensation plans approved by security holders	9,700,000	\$ 52.73	12,804,000*
Equity compensation plans not approved by security holders**			

* *These securities may be awarded as stock options, restricted stock or other awards permitted under the Registrant's equity compensation plan.*

** *Registrant has a Stock Award Program pursuant to which each non-employee director receives \$150,000 in value of Registrant's common stock each year. These awards are made from shares purchased by the Corporation in the open market. Stockholders did not approve this equity compensation plan.*

See Note 8, Share-Based Compensation, in the notes to the financial statements for further discussion of the Corporation's equity compensation plans.

Table of Contents**Item 6. Selected Financial Data**

A five-year summary of selected financial data follows:

	2008	2007	2006	2005	2004
	(Millions of dollars, except per share amounts)				
Sales and other operating revenues					
Crude oil and natural gas liquids	\$ 7,764	\$ 6,303	\$ 5,307	\$ 3,219	\$ 2,594
Natural gas (including sales of purchased gas)	8,800	6,877	6,826	6,423	4,638
Refined petroleum products	19,765	14,741	13,339	11,317	7,907
Electricity	2,926	2,322	1,064	363	207
Convenience store sales and other operating revenues	1,910	1,404	1,531	1,425	1,387
Total	\$ 41,165	\$ 31,647	\$ 28,067	\$ 22,747	\$ 16,733
Income from continuing operations	\$ 2,360(a)	\$ 1,832(b)	\$ 1,920(c)	\$ 1,226(d)	\$ 970(e)
Discontinued operations					7
Net income	\$ 2,360	\$ 1,832	\$ 1,920	\$ 1,226	\$ 977
Less preferred stock dividends			44	48	48
Net income applicable to common shareholders	\$ 2,360	\$ 1,832	\$ 1,876	\$ 1,178	\$ 929
Basic earnings per share*					
Continuing operations	\$ 7.35	\$ 5.86	\$ 6.75	\$ 4.32	\$ 3.43
Net income	7.35	5.86	6.75	4.32	3.46
Diluted earnings per share*					
Continuing operations	\$ 7.24	\$ 5.74	\$ 6.08	\$ 3.93	\$ 3.17
Net income	7.24	5.74	6.08	3.93	3.19
Total assets	\$ 28,589	\$ 26,131	\$ 22,442	\$ 19,158	\$ 16,312
Total debt	3,955	3,980	3,772	3,785	3,835
Stockholders' equity	12,307	9,774	8,147	6,318	5,597
Dividends per share of common stock*	\$.40	\$.40	\$.40	\$.40	\$.40

* Per share amounts in all periods reflect the 3-for-1 stock split on May 31, 2006.

(a) Includes net after-tax expenses of \$26 million primarily relating to asset impairments and hurricanes in the Gulf of Mexico.

(b) Includes net after-tax expenses of \$75 million primarily relating to asset impairments, estimated production imbalance settlements and a charge for MTBE litigation, partially offset by income from LIFO inventory liquidations and gains from asset sales.

- (c) *Includes net after-tax income of \$173 million primarily from sales of assets, partially offset by income tax adjustments and accrued leased office closing costs.*
- (d) *Includes after-tax expenses of \$37 million primarily relating to income taxes on repatriated earnings, premiums on bond repurchases and hurricane related expenses, partially offset by gains from asset sales and a LIFO inventory liquidation.*
- (e) *Includes net after-tax income of \$76 million primarily from sales of assets and income tax adjustments.*

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Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations*

Overview

The Corporation is a global integrated energy company that operates in two segments, Exploration and Production (E&P) and Marketing and Refining (M&R). The E&P segment explores for, develops, produces, purchases, transports and sells crude oil and natural gas. The M&R segment manufactures, purchases, transports, trades and markets refined petroleum products, natural gas and electricity.

Net income in 2008 was \$2,360 million compared with \$1,832 million in 2007 and \$1,920 million in 2006. Diluted earnings per share were \$7.24 in 2008 compared with \$5.74 in 2007 and \$6.08 in 2006. A table of items affecting comparability between periods is shown on page 21.

Exploration and Production

The Corporation's strategy for the E&P segment is to profitably grow reserves and production in a sustainable and financially disciplined manner. The Corporation's total proved reserves were 1,432 million barrels of oil equivalent (boe) at December 31, 2008 compared with 1,330 million boe at December 31, 2007 and 1,243 million boe at December 31, 2006. Total proved reserves at year end 2008 increased 102 million boe or 8% from the end of 2007.

E&P net income was \$2,423 million in 2008, \$1,842 million in 2007 and \$1,763 million in 2006. The improved results in 2008 as compared to 2007 were primarily driven by higher average crude oil selling prices. At December 31, 2008, crude oil selling prices were significantly below the average prices in 2008.

Production averaged 381,000 barrels of oil equivalent per day (boepd) in 2008 compared with 377,000 boepd in 2007 and 359,000 boepd in 2006. Production in 2008 increased 4,000 boepd or 1% from 2007. In 2009, the Corporation currently estimates total worldwide production to be approximately 380,000 boepd to 390,000 boepd.

During 2008, the Corporation progressed the following development projects that will add to its production in future years:

In November 2008, upon the commissioning of a third-party gas export pipeline to Thailand, Phase 2 gas sales commenced at Block A-18 of the Joint Development Area of Malaysia and Thailand (JDA) (Hess 50%).

In the deepwater Gulf of Mexico, development of the Shenzi Field (Hess 28%) progressed. Tension leg platform tendons, hull and topsides were installed and flowlines were laid and tested. First production is expected in the second quarter of 2009.

Additional production from a Phase 2 oil project at the Ujung Pangkah Field (Hess 75%) in Indonesia is expected in mid 2009.

Development of a residual oil zone advanced at the Seminole-San Andres Unit (Hess 34%) with the installation of facilities and equipment.

During 2008, the Corporation's exploration activities included:

In the Pony prospect on Green Canyon Block 468 (Hess 100%) in the deepwater Gulf of Mexico, the Corporation successfully completed drilling an appraisal well. The Corporation is evaluating development options for Pony.

At the Corporation's Tubular Bells prospect (Hess 20%) located in the Mississippi Canyon area of the deepwater Gulf of Mexico, a third well was successfully drilled during 2008. The operator is evaluating development options for Tubular Bells.

The Corporation completed drilling its initial four exploration wells of a 16 well commitment on the WA-Block-390-P offshore Western Australia (Hess 100%). Three of the four wells discovered natural gas and the Corporation plans to drill five additional exploration wells in 2009. The operator of the WA-Block 404-P (Hess 50%) offshore Western Australia plans to drill three exploration wells in 2009.

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The Corporation drilled a successful exploration well in Area 54 offshore Libya (Hess 100%). The Corporation intends to obtain 3D seismic in Area 54 and further drilling is planned.

The Corporation drilled a successful exploration well on the West Med Block (Hess 55%) in Egypt, which encountered natural gas and crude oil. The Corporation is currently conducting engineering studies and further exploratory drilling is planned.

The operator commenced drilling of an exploration well on the BM-S-22 Block (Hess 40%) in the Santos Basin offshore Brazil and filed a Notice of Discovery with the regulators on January 16, 2009.

The Corporation was successful in acquiring new deepwater blocks in the Central and Western Gulf of Mexico and the offshore Semai V exploration block in Indonesia.

Marketing and Refining

The Corporation's strategy for the M&R segment is to deliver consistent operating performance and generate free cash flow. M&R net income was \$277 million in 2008, \$300 million in 2007 and \$394 million in 2006. Earnings in 2008 and 2007 reflect lower average margins compared to the prior periods.

Refining operations contributed net income of \$73 million in 2008, \$193 million in 2007 and \$240 million in 2006. The Corporation received cash distributions from HOVENSA totaling \$50 million in 2008, \$300 million in 2007 and \$400 million in 2006. Gross crude runs at HOVENSA averaged 441,000 barrels per day in 2008 compared with 454,000 barrels per day in 2007 and 448,000 barrels per day in 2006. In 2007, HOVENSA successfully completed the first turnaround of its delayed coker unit. The Port Reading refinery operated at an average of 64,000 barrels per day in 2008 versus 61,000 barrels per day in 2007 and 63,000 barrels per day in 2006. Marketing earnings were \$240 million in 2008, \$83 million in 2007 and \$108 million in 2006. Total refined product sales volumes averaged 472,000 barrels per day in 2008 compared with 451,000 barrels per day in 2007 and 459,000 barrels per day in 2006.

Liquidity and Capital and Exploratory Expenditures

Net cash provided by operating activities was \$4,567 million in 2008, \$3,507 million in 2007 and \$3,491 million in 2006, principally reflecting increased earnings. At December 31, 2008, cash and cash equivalents totaled \$908 million compared with \$607 million at December 31, 2007. Total debt was \$3,955 million at December 31, 2008 compared with \$3,980 million at December 31, 2007. The Corporation's debt to capitalization ratio at December 31, 2008 was 24.3% compared with 28.9% at the end of 2007. The Corporation has debt maturities of \$143 million in 2009 and \$31 million in 2010. In February 2009, the Corporation issued \$250 million of 5 year notes with a coupon of 7% and \$1 billion of 10 year notes with a coupon of 8.125%.

Capital and exploratory expenditures were as follows for the years ended December 31:

	2008	2007
	(Millions of dollars)	
Exploration and Production		
United States	\$ 2,164	\$ 1,603
International	2,477	2,183

Total Exploration and Production	4,641	3,786
Marketing, Refining and Corporate	187	140
Total Capital and Exploratory Expenditures	\$ 4,828	\$ 3,926
Exploration expenses charged to income included above:		
United States	\$ 211	\$ 192
International	179	156
Total exploration expenses charged to income included above	\$ 390	\$ 348

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The Corporation anticipates \$3.2 billion in capital and exploratory expenditures in 2009, of which \$3.1 billion relates to E&P operations.

Consolidated Results of Operations

The after-tax results by major operating activity are summarized below:

	2008	2007	2006
	(Millions of dollars, except per share data)		
Exploration and Production	\$ 2,423	\$ 1,842	\$ 1,763
Marketing and Refining	277	300	394
Corporate	(173)	(150)	(110)
Interest expense	(167)	(160)	(127)
Net income	\$ 2,360	\$ 1,832	\$ 1,920
Net income per share diluted	\$ 7.24	\$ 5.74	\$ 6.08

In the discussion that follows, the financial effects of certain transactions are disclosed on an after-tax basis. Management reviews segment earnings on an after-tax basis and uses after-tax amounts in its review of variances in segment earnings. Management believes that after-tax amounts are a preferable method of explaining variances in earnings, since they show the entire effect of a transaction rather than only the pre-tax amount. After-tax amounts are determined by applying the income tax rate in each tax jurisdiction to pre-tax amounts.

The following table summarizes, on an after-tax basis, items of income (expense) that are included in net income and affect comparability between periods. The items in the table below are explained, and the pre-tax amounts are shown, on pages 25 through 27.

	2008	2007	2006
	(Millions of dollars)		
Exploration and Production	\$ (26)	\$ (74)	\$ 173
Marketing and Refining		24	
Corporate		(25)	
	\$ (26)	\$ (75)	\$ 173

Table of Contents**Comparison of Results*****Exploration and Production***

Following is a summarized income statement of the Corporation's Exploration and Production operations:

	2008	2007	2006
	(Millions of dollars)		
Sales and other operating revenues*	\$ 9,806	\$ 7,498	\$ 6,524
Other, net	(167)	65	428
Total revenues and non operating income	9,639	7,563	6,952
Costs and expenses			
Production expenses, including related taxes	1,872	1,581	1,250
Exploration expenses, including dry holes and lease impairment	725	515	552
General, administrative and other expenses	302	257	209
Depreciation, depletion and amortization	1,952	1,503	1,159
Total costs and expenses	4,851	3,856	3,170
Results of operations from continuing operations before income taxes	4,788	3,707	3,782
Provision for income taxes	2,365	1,865	2,019
Results of operations	\$ 2,423	\$ 1,842	\$ 1,763

* Amounts differ from E&P operating revenues in Note 17 Segment Information primarily due to the exclusion of sales of hydrocarbons purchased from third parties.

After considering the Exploration and Production items in the table on page 21, the remaining changes in Exploration and Production earnings are primarily attributable to changes in selling prices, production volumes, operating costs, exploration expenses, foreign exchange, and income taxes, as discussed below.

Selling prices: Higher average selling prices increased Exploration and Production revenues by approximately \$2,100 million in 2008 compared with 2007. At December 31, 2008, the selling prices of crude oil and natural gas had decreased significantly from the average 2008 selling prices indicated below. In 2007, an increase in average crude oil selling prices and reduced hedge positions compared with 2006 increased revenues by approximately \$740 million.

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The Corporation's average selling prices were as follows:

	2008	2007	2006
Crude oil-per barrel (including hedging)			
United States	\$ 96.82	\$ 69.23	\$ 60.45
Europe	78.75	60.99	56.19
Africa	78.72	62.04	51.18
Asia and other	97.07	72.17	61.52
Worldwide	82.04	63.44	55.31
Crude oil-per barrel (excluding hedging)			
United States	\$ 96.82	\$ 69.23	\$ 60.45
Europe	78.75	60.99	58.46
Africa	93.57	71.71	62.80
Asia and other	97.07	72.17	61.52
Worldwide	89.23	67.79	60.41
Natural gas liquids-per barrel			
United States	\$ 64.98	\$ 51.89	\$ 46.22
Europe	74.63	57.20	47.30
Worldwide	67.61	53.72	46.59
Natural gas-per mcf (including hedging)			
United States	\$ 8.61	\$ 6.67	\$ 6.59
Europe	9.44	6.13	6.20
Asia and other	5.24	4.71	4.05
Worldwide	7.17	5.60	5.50
Natural gas-per mcf (excluding hedging)			
United States	\$ 8.61	\$ 6.67	\$ 6.59
Europe	9.79	6.13	6.20
Asia and other	5.24	4.71	4.05
Worldwide	7.30	5.60	5.50

The after-tax impacts of hedging reduced earnings by \$423 million (\$685 million before income taxes) in 2008, \$244 million (\$399 million before income taxes) in 2007 and \$285 million (\$449 million before income taxes) in 2006. In October 2008, the Corporation closed its Brent crude oil hedge positions by entering into offsetting contracts with the same counterparty covering 24,000 barrels per day from 2009 through 2012 at a per barrel price of \$86.95 each year. The deferred after-tax loss as of the date the hedge positions were closed will be recorded in earnings as the contracts mature. The estimated annual after-tax loss from the closed positions will be approximately \$335 million from 2009 through 2012. The pretax amounts will continue to be recorded as a reduction of revenue and allocated to the selling prices of the Corporation's African production.

Production and sales volumes: The Corporation's crude oil and natural gas production was 381,000 boepd in 2008 compared with 377,000 boepd in 2007 and 359,000 boepd in 2006. The Corporation currently estimates that its 2009 production will average between 380,000 and 390,000 boepd.

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The Corporation's net daily worldwide production was as follows:

	2008	2007	2006
Crude oil (thousands of barrels per day)			
United States	32	31	36
Europe	83	93	109
Africa	124	115	85
Asia and other	13	21	12
Total	252	260	242
Natural gas liquids (thousands of barrels per day)			
United States	10	10	10
Europe	4	5	5
Total	14	15	15
Natural gas (thousands of mcf per day)			
United States	78	88	110
Europe	255	259	283
Asia and other	356	266	219
Total	689	613	612
Barrels of oil equivalent* (thousands of barrels per day)	381	377	359

* Reflects natural gas production converted on the basis of relative energy content (six mcf equals one barrel).

United States: Crude oil production in the United States was higher in 2008 compared with 2007, principally due to production from new wells in North Dakota and the deepwater Gulf of Mexico. This increased production was partially offset by the impact of hurricanes in the Gulf of Mexico. Natural gas production was lower in 2008, primarily reflecting hurricane downtime and natural decline. Hurricane impacts reduced full year 2008 production by an estimated 7,000 boepd. At December 31, 2008, approximately 15,000 boepd remained shut-in from the hurricanes and this production is expected to be brought back on line by the end of the first quarter of 2009. Crude oil and natural gas production in 2007 decreased compared with 2006 principally due to natural decline and asset sales.

Europe: Crude oil production in 2008 was lower than in 2007, due to temporary shut-ins at three North Sea fields, cessation of production at the mature Fife, Fergus, Flora and Angus Fields, and natural decline. These decreases were partially offset by increased production in Russia. Crude oil production in 2007 was lower than in 2006, reflecting natural decline, facilities work on three North Sea fields, and the sale of the Corporation's interests in the Scott and Telford Fields in the United Kingdom, partially offset by higher Russian production. Natural gas production was comparable in 2008 and 2007, but decreased in 2007 compared with 2006 principally due to lower nominations related to the shut-down of a non-operated pipeline and natural decline. The decreases were partially offset by higher natural gas production from the Atlantic and Cromarty Fields in the United Kingdom which commenced in June 2006.

Africa: Crude oil production increased in 2008 compared with 2007, primarily due to higher production at the Okume Complex in Equatorial Guinea, partially offset by a lower entitlement to Algerian production. Crude oil production increased in 2007 compared with 2006 primarily due to the start-up of the Okume Complex in December 2006.

Asia and other: The change in crude oil production from 2006 through 2008 principally reflects changes to the Corporation's entitlement to production in Azerbaijan. The increase in 2007 compared with 2006 also reflects increased gross production from the fields in Azerbaijan. Natural gas production increased in 2008 compared with 2007 due to increased production from Block A-18 in the Joint Development Area of Malaysia and Thailand (JDA) and a full year of production from the Ujung Pangkah Field in Indonesia. Higher natural gas

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production in 2007 compared with 2006 was principally due to new production from the Sinphuhorm onshore gas project in Thailand which commenced in November 2006 and production from the Ujung Pangkah Field which commenced in April 2007. These increases were partially offset by the planned shut-down of the JDA to install facilities required for Phase 2 gas sales.

Sales volumes: Higher sales volumes and other operating revenues increased revenue by approximately \$200 million in 2008 compared with 2007 and \$240 million in 2007 compared with 2006.

Operating costs and depreciation, depletion and amortization: Cash operating costs, consisting of production expenses and general and administrative expenses, increased by \$321 million in 2008 and \$409 million in 2007 compared with the corresponding amounts in prior years (excluding the charges for hurricane related costs in 2008 and vacated leased office space in 2006 that are discussed below). The increases in 2008 and 2007 were primarily due to higher production volumes, increased production taxes (due to higher realized selling prices), increased costs of services and materials and higher employee costs. Cash operating costs per barrel of oil equivalent were \$15.49 in 2008, \$13.36 in 2007 and \$10.92 in 2006. Cash operating costs in 2009 are estimated to be in the range of \$15.00 to \$16.00 per barrel of oil equivalent.

Excluding the pre-tax amount of asset impairments, depreciation, depletion and amortization charges increased by \$531 million and \$232 million in 2008 and 2007, respectively. The increases were primarily due to higher production volumes and per barrel costs. Depreciation, depletion and amortization costs per barrel of oil equivalent were \$13.79 in 2008, \$10.11 in 2007 and \$8.85 in 2006. Depreciation, depletion and amortization costs for 2009 are estimated to be in the range of \$13.00 to \$14.00 per barrel.

Exploration expenses: Exploration expenses were higher in 2008 compared with 2007, principally due to higher dry hole costs. Exploration expenses were lower in 2007 compared with 2006, primarily reflecting lower dry hole costs, partially offset by increased seismic studies.

Income taxes: After considering the items in the table below, the effective income tax rates for Exploration and Production operations were 49% in 2008, 50% in 2007 and 54% in 2006. The effective income tax rate for E&P operations in 2009 is estimated to be in the range of 57% to 61%. The increase from the 2008 effective rate largely reflects the impact of Libyan taxes in a lower commodity price environment.

Foreign Exchange: The after-tax foreign currency loss was \$84 million in 2008, compared with a loss of \$7 million in 2007 and a gain of \$10 million in 2006. The increased foreign currency loss reflects the effect of significant exchange rate movements in the fourth quarter of 2008 on the remeasurement of assets, liabilities and foreign currency forward contracts by certain foreign businesses.

Reported Exploration and Production earnings include the following items of income (expense) before and after income taxes:

	Before Income Taxes			After Income Taxes		
	2008	2007	2006	2008	2007	2006
	(Millions of dollars)					
Gains from asset sales	\$	\$ 21	\$ 369	\$	\$ 15	\$ 236
Asset impairments	(30)	(112)		(17)	(56)	
Hurricane related costs	(15)			(9)		
Estimated production imbalance settlements		(64)			(33)	

Accrued office closing costs	(30)	(18)
Income tax adjustments		(45)

\$ (45) \$ (155) \$ 339 \$ (26) \$ (74) \$ 173

2008: The charge for asset impairments relates to mature fields in the United States and the United Kingdom North Sea. The pre-tax amount of this charge is reflected in depreciation, depletion and amortization. The hurricane costs relate to expenses associated with Hurricanes Gustav and Ike in the Gulf of Mexico and are recorded in production expenses.

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2007: The gain from asset sales relates to the sale of the Corporation's interests in the Scott and Telford fields in the United Kingdom North Sea. The charge for asset impairments relates to two mature fields also in the United Kingdom North Sea. The estimated production imbalance settlements represent a charge for adjustments to prior meter readings at two offshore fields, which are recorded as a reduction of sales and other operating revenues.

2006: The gains from asset sales relate to the sale of certain United States oil and gas producing properties located in the Permian Basin in Texas and New Mexico and onshore Gulf Coast. The accrued office closing cost relates to vacated leased office space in the United Kingdom. The related expenses are reflected principally in general and administrative expenses. The income tax adjustment represents a one-time adjustment to the Corporation's deferred tax liability resulting from an increase in the supplementary tax on petroleum operations in the United Kingdom from 10% to 20%.

The Corporation's future Exploration and Production earnings may be impacted by external factors, such as political risk, volatility in the selling prices of crude oil and natural gas, reserve and production changes, industry cost inflation, exploration expenses, the effects of weather and changes in foreign exchange and income tax rates.

Marketing and Refining

Earnings from Marketing and Refining activities amounted to \$277 million in 2008, \$300 million in 2007 and \$394 million in 2006. After considering the liquidation of LIFO inventories reflected in the table on page 21 and discussed below, the earnings were \$277 million, \$276 million and \$394 million, respectively.

Refining: Refining earnings, which consist of the Corporation's share of HOVENSA's results, Port Reading earnings, interest income on a note receivable from PDVSA and results of other miscellaneous operating activities, were \$73 million in 2008, \$193 million in 2007, and \$240 million in 2006.

The Corporation's share of HOVENSA's net income was \$27 million (\$44 million before income taxes) in 2008, \$108 million (\$176 million before income taxes) in 2007 and \$124 million (\$201 million before income taxes) in 2006. The lower earnings in 2008 and 2007, compared with the respective prior years, were principally due to lower refining margins. The 2008 utilization rate for the fluid catalytic cracking unit at HOVENSA reflects lower utilization due to weak refining margins, planned and unplanned maintenance of certain units, and a refinery wide shut down for Hurricane Omar. In 2007, the coker unit at HOVENSA was shutdown for approximately 30 days for a scheduled turnaround. Certain related processing units were also included in this turnaround. In 2006, the fluid catalytic cracking unit at HOVENSA was shutdown for approximately 22 days of unscheduled maintenance. Cash distributions received by the Corporation from HOVENSA were \$50 million in 2008, \$300 million in 2007 and \$400 million in 2006.

Pre-tax interest income on the PDVSA note was \$4 million, \$9 million and \$15 million in 2008, 2007 and 2006, respectively. Interest income is reflected in other income in the income statement. At December 31, 2008, the remaining balance of the PDVSA note was \$15 million, which was fully repaid in February 2009.

Port Reading and other after-tax refining earnings were \$43 million in 2008, \$79 million in 2007 and \$107 million in 2006, also reflecting lower refining margins.

The following table summarizes refinery utilization rates:

Refinery Capacity	Refinery Utilization		
	2008	2007	2006

(Thousands
of
barrels per
day)

HOVENSA				
Crude	500	88.2%	90.8%	89.7%
Fluid catalytic cracker	150	72.7%	87.1%	84.3%
Coker	58	92.4%	83.4%	84.3%
Port Reading	70*	90.7%	93.2%	97.4%

* Refinery utilization in 2007 and 2006 is based on capacity of 65 thousand barrels per day.

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Marketing: Marketing operations, which consist principally of retail gasoline and energy marketing activities, generated income of \$240 million in 2008, \$59 million in 2007 and \$108 million in 2006, excluding income from the liquidation of LIFO inventories in 2007 totaling \$38 million before income taxes (\$24 million after income taxes).

The increase in 2008 primarily reflects higher margins on refined product sales, including sales of retail gasoline operations. Refined product margins were lower in 2007 compared with 2006. Total refined product sales volumes were 472,000 barrels per day in 2008, 451,000 barrels per day in 2007 and 459,000 barrels per day in 2006. Total energy marketing natural gas sales volumes, including utility and spot sales, were approximately 2.0 million mcf per day in 2008, 1.9 million mcf per day in 2007 and 1.8 million mcf per day in 2006. In addition, energy marketing sold electricity volumes at the rate of 3,200, 2,800 and 1,400 megawatts (round the clock) in 2008, 2007 and 2006, respectively.

The Corporation has a 50% voting interest in a consolidated partnership that trades energy commodities and energy derivatives. The Corporation also takes trading positions for its own account. The Corporation's after-tax results from trading activities, including its share of the earnings of the trading partnership, amounted to a loss of \$36 million in 2008, compared with earnings of \$24 million in 2007 and \$46 million in 2006.

Marketing expenses increased in 2008, principally reflecting growth in energy marketing activities, higher credit card fees in retail gasoline operations, and increased transportation costs.

The Corporation's future Marketing and Refining earnings may be impacted by external factors, including volatility in margins, competitive industry conditions, government regulations, credit risk, and supply and demand factors, including the effects of weather.

Corporate

The following table summarizes corporate expenses:

	2008	2007	2006
	(Millions of dollars)		
Corporate expenses (excluding the item described below)	\$ 260	\$ 187	\$ 156
Income taxes (benefits) on the above	(87)	(62)	(46)
	173	125	110
Item affecting comparability between periods, after tax			
Estimated MTBE litigation		25	
Net corporate expenses	\$ 173	\$ 150	\$ 110

Excluding the item affecting comparability between periods, the increase in corporate expenses in 2008 compared with 2007 primarily reflects losses on pension related investments, higher employee costs, and higher professional fees. The increase in net corporate expenses in 2007 compared with 2006 principally reflects higher employee costs, including stock based compensation. Recurring after-tax corporate expenses in 2009 are estimated to be in the range of \$165 to \$175 million.

In 2007, Corporate expenses include a charge of \$25 million (\$40 million before income taxes) related to MTBE litigation. The pre-tax amount of this charge is recorded in general and administrative expenses.

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After-tax interest expense was as follows:

	2008	2007	2006
	(Millions of dollars)		
Total interest incurred	\$ 274	\$ 306	\$ 301
Less capitalized interest	7	50	100
Interest expense before income taxes	267	256	201
Less income taxes	100	96	74
After-tax interest expense	\$ 167	\$ 160	\$ 127

The decrease in interest incurred in 2008 principally reflects lower average debt. The decrease in capitalized interest in 2008 reflects the completion of several development projects in 2007 and 2006. Interest expense in each period includes the cost of letters of credit primarily issued to counterparties in hedging and trading activities. After-tax interest expense in 2009 is expected to be in the range of \$230 to \$240 million. See Future Capital Requirements and Resources for discussion of a \$1,250 million note issuance in the first quarter of 2009.

Sales and Other Operating Revenues

Sales and other operating revenues totaled \$41,165 million in 2008, an increase of 30% compared with 2007. In 2007, sales and other operating revenues totaled \$31,647 million, an increase of 13% compared with 2006. The increase in each year reflects higher selling prices and sales volumes of crude oil, higher refined product selling prices and increased sales volumes of electricity.

The change in cost of goods sold in each year principally reflects the change in sales volumes and prices of refined products and purchased natural gas and electricity.

Liquidity and Capital Resources

The following table sets forth certain relevant measures of the Corporation's liquidity and capital resources as of December 31:

	2008	2007
	(Millions of dollars)	
Cash and cash equivalents	\$ 908	\$ 607
Current portion of long-term debt	\$ 143	\$ 62
Total debt	\$ 3,955	\$ 3,980
Stockholders' equity	\$ 12,307	\$ 9,774
Debt to capitalization ratio*	24.3%	28.9%

* *Total debt as a percentage of the sum of total debt plus stockholders' equity.*

Table of Contents***Cash Flows***

The following table sets forth a summary of the Corporation's cash flows:

	2008	2007	2006
	(Millions of dollars)		
Net cash provided by (used in):			
Operating activities	\$ 4,567	\$ 3,507	\$ 3,491
Investing activities	(4,444)	(3,474)	(3,289)
Financing activities	178	191	(134)
Net increase in cash and cash equivalents	\$ 301	\$ 224	\$ 68

Operating Activities: Net cash provided by operating activities, including changes in operating assets and liabilities, increased to \$4,567 million in 2008 from \$3,507 million in 2007, reflecting increased earnings. Operating cash flow was comparable in 2007 and 2006. The Corporation received cash distributions from HOVENSA of \$50 million in 2008, \$300 million in 2007 and \$400 million in 2006.

Investing Activities: The following table summarizes the Corporation's capital expenditures:

	2008	2007	2006
	(Millions of dollars)		
Exploration and Production			
Exploration	\$ 744	\$ 371	\$ 590
Production and development	2,523	2,605	2,164
Acquisitions (including leaseholds)	984	462	921
	4,251	3,438	3,675
Marketing, Refining and Corporate	187	140	169
Total	\$ 4,438	\$ 3,578	\$ 3,844

Capital expenditures in 2008 include leasehold acquisitions in the United States of \$600 million and \$210 million for the acquisition of the remaining 22.5% interest in the Corporation's Gabonese subsidiary. In 2008, the Corporation also selectively expanded its energy marketing business by acquiring fuel oil, natural gas, and electricity customer accounts, and a terminal and related assets, for an aggregate of approximately \$100 million. In 2007, capital expenditures include the acquisition of a 28% interest in the Genghis Khan Field in the deepwater Gulf of Mexico for \$371 million. In 2006, capital expenditures included payments of \$359 million to re-enter the Corporation's former oil and gas production operations in the Waha concessions in Libya and \$413 million to acquire a 55% working interest in the West Med Block in Egypt.

In 2007, the Corporation received proceeds of \$93 million for the sale of its interests in the Scott and Telford fields located in the United Kingdom. Proceeds from asset sales in 2006 totaled \$444 million, including the sale of the Corporation's interests in certain producing properties in the Permian Basin and onshore U.S. Gulf Coast.

Financing Activities: During 2008, net repayments of debt were \$32 million compared with net borrowings of \$208 million in 2007. In 2006, the Corporation reduced debt by \$13 million.

Total common and preferred stock dividends paid were \$130 million, \$127 million and \$161 million in 2008, 2007 and 2006, respectively. The Corporation received net proceeds from the exercise of stock options, including related income tax benefits, of \$340 million, \$110 million and \$40 million in 2008, 2007 and 2006, respectively.

Future Capital Requirements and Resources

The Corporation anticipates \$3.2 billion in capital and exploratory expenditures in 2009, of which \$3.1 billion relates to Exploration and Production operations. Of the total E&P amount, \$1.4 billion is for production and \$900 million is for developments, with the remainder for exploration. The anticipated 2009 capital program

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represents a decrease of approximately \$1.6 billion from 2008, primarily as a result of lower crude oil selling prices. The Corporation also has maturities of long-term debt of \$143 million in 2009. The Corporation anticipates that it can fund its 2009 operations, including planned capital expenditures, dividends, pension contributions and required debt repayments, with existing cash on-hand, projected cash flow from operations and available credit facilities. Crude oil and natural gas prices are volatile and difficult to predict in the near term as a result of the recent global economic recession. In addition, unplanned increases in the Corporation's capital expenditure program could occur. The Corporation will take steps as necessary to protect its financial flexibility, and may pursue other sources of liquidity, including the issuance of debt or equity securities, or asset sales.

The table below summarizes the capacity, usage, and remaining availability of the Corporation's borrowing and letter of credit facilities at December 31, 2008 (in millions):

	Expiration Date	Capacity	Borrowings	Letters of Credit Issued	Total Used	Remaining Capacity
Revolving credit facility	May 2012*	\$ 3,000	\$ 350	\$ 176	\$ 526	\$ 2,474
Asset backed credit facility	October 2009	500	500		500	
Committed lines	Various**	1,993		1,973	1,973	20
Uncommitted lines	Various	1,686		1,686	1,686	
Total		\$ 7,179	\$ 850	\$ 3,835	\$ 4,685	\$ 2,494

* \$75 million of capacity expires in May 2011.

** Committed lines have expiration dates ranging from 2009 through 2011.

The Corporation maintains a \$3.0 billion syndicated, revolving credit facility (the facility), of which \$2,925 million is committed through May 2012. The facility can be used for borrowings and letters of credit. At December 31, 2008, additional available capacity under the facility was \$2,474 million.

The Corporation has a 364-day asset-backed credit facility securitized by certain accounts receivable from its Marketing and Refining operations. Under the terms of this financing arrangement, the Corporation has the ability to borrow or issue letters of credit up to \$500 million, subject to the availability of sufficient levels of eligible receivables. At December 31, 2008, outstanding borrowings under this facility were collateralized by \$1,249 million of accounts receivable, which are held by a wholly-owned subsidiary. These receivables are not available to pay the general obligations of the Corporation before repayment of outstanding borrowings under the asset-backed facility. At December 31, 2008, \$500 million of outstanding borrowings under the asset-backed credit facility are classified as long-term based on the Corporation's available capacity under the committed revolving credit facility.

In February 2009, the Corporation issued \$250 million of 5 year senior unsecured notes with a coupon of 7% and \$1 billion of 10 year senior unsecured notes with a coupon of 8.125%. The majority of the proceeds were used to repay revolving credit debt and outstanding borrowings on other credit facilities. The remainder of the proceeds is available for working capital and other corporate purposes.

The Corporation also has a shelf registration under which it may issue additional debt securities, warrants, common stock or preferred stock.

A loan agreement covenant based on the Corporation's debt to equity ratio allows the Corporation to borrow up to an additional \$16.6 billion for the construction or acquisition of assets at December 31, 2008. The Corporation has the ability to borrow up to an additional \$2.8 billion of secured debt at December 31, 2008 under the loan agreement covenants.

In order to reduce credit risk, the Corporation has agreements with counterparties to exchange collateral which is determined based on the fair values of positions held under these agreements. The Corporation's \$3.8 billion of letters of credit outstanding at December 31, 2008 were primarily issued to satisfy collateral requirements. Additionally, the Corporation has posted cash collateral of approximately \$394 million and has received cash

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collateral of approximately \$705 million from its hedging and trading counterparties. Changes in commodity prices can have a material impact on collateral requirements under these agreements.

Credit Ratings

There are three major credit rating agencies that rate the Corporation's debt. All three agencies have currently assigned an investment grade rating to the Corporation's debt. The interest rates and facility fees charged on the Corporation's credit facilities, as well as margin requirements from non-trading and trading counterparties, are subject to adjustment if the Corporation's credit rating changes.

Contractual Obligations and Contingencies

Following is a table showing aggregated information about certain contractual obligations at December 31, 2008:

	Total	Payments Due by Period			Thereafter
		2009	2010 and 2011	2012 and 2013	
		(Millions of dollars)			
Long-term debt*	\$ 3,955	\$ 143	\$ 733	\$ 907	\$ 2,172
Operating leases	3,561	551	725	638	1,647
Purchase obligations					
Supply commitments	24,252	8,602	8,204	7,344	102**
Capital expenditures	1,356	929	427		
Operating expenses	1,011	486	321	77	127
Other long-term liabilities	2,011	134	474	93	1,310

* At December 31, 2008, the Corporation's debt bears interest at a weighted average rate of 6.7%.

** The Corporation intends to continue purchasing refined product supply from HOVENSA. Estimated future purchases amount to approximately \$4.0 billion annually using year-end 2008 prices.

In the preceding table, the Corporation's supply commitments include its estimated purchases of 50% of HOVENSA's production of refined products, after anticipated sales by HOVENSA to unaffiliated parties. The value of future supply commitments will fluctuate based on prevailing market prices at the time of purchase, the actual output from HOVENSA, and the level of sales to unaffiliated parties. Also included are term purchase agreements at market prices for additional gasoline necessary to supply the Corporation's retail marketing system and feedstocks for the Port Reading refining facility. In addition, the Corporation has commitments to purchase refined products, natural gas and electricity to supply contracted customers in its energy marketing business. These commitments were computed based on year-end market prices.

The table also reflects future capital expenditures, including a portion of the Corporation's planned \$3.2 billion capital investment program for 2009 that is contractually committed at December 31, 2008. Obligations for operating expenses include commitments for transportation, seismic purchases, oil and gas production expenses and other normal business expenses. Other long-term liabilities reflect contractually committed obligations on the balance sheet at December 31, 2008, including asset retirement obligations, pension plan liabilities and anticipated obligations for uncertain income tax positions.

The Corporation and certain of its subsidiaries lease gasoline stations, drilling rigs, tankers, office space and other assets for varying periods under leases accounted for as operating leases. During 2007, the Corporation entered into a lease agreement for a new drillship and related support services for use in its global deepwater exploration and development activities beginning in the middle of 2009. The total payments under this five year contract are expected to be approximately \$950 million.

The Corporation has a contingent purchase obligation, expiring in April 2010, to acquire the remaining interest in WilcoHess, a retail gasoline station joint venture, for approximately \$175 million as of December 31, 2008.

The Corporation guarantees the payment of up to 50% of HOVENSA's crude oil purchases from certain suppliers other than PDVSA. The amount of the Corporation's guarantee fluctuates based on the volume of crude oil

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purchased and related prices and at December 31, 2008 amounted to \$78 million. In addition, the Corporation has agreed to provide funding up to a maximum of \$15 million to the extent HOVENSA does not have funds to meet its senior debt obligations.

The Corporation is contingently liable under letters of credit and under guarantees of the debt of other entities directly related to its business, as follows:

	Total (Millions of dollars)
Letters of credit	\$ 126
Guarantees	93
	\$ 219

Off-Balance Sheet Arrangements

The Corporation has leveraged leases not included in its balance sheet, primarily related to retail gasoline stations that the Corporation operates. The net present value of these leases is \$491 million at December 31, 2008 compared with \$493 million at December 31, 2007. The Corporation's December 31, 2008 debt to capitalization ratio would increase from 24.3% to 26.5% if these leases were included as debt.

See also Note 4, Refining Joint Venture, and Note 16, Guarantees and Contingencies, in the notes to the financial statements.

Foreign Operations

The Corporation conducts exploration and production activities principally in Algeria, Australia, Azerbaijan, Brazil, Denmark, Egypt, Equatorial Guinea, Gabon, Ghana, Indonesia, Libya, Malaysia, Norway, Peru, Russia, Thailand, the United Kingdom and the United States. Therefore, the Corporation is subject to the risks associated with foreign operations, including political risk, tax law changes, and currency risk.

HOVENSA owns and operates a refinery in the United States Virgin Islands. In 2002, there was a political disruption in Venezuela that reduced the availability of Venezuelan crude oil used in refining operations; however, this disruption did not have a material adverse effect on the Corporation's financial position.

See also Item 1A. *Risk Factors Related to Our Business and Operations.*

Accounting Policies***Critical Accounting Policies and Estimates***

Accounting policies and estimates affect the recognition of assets and liabilities on the Corporation's balance sheet and revenues and expenses on the income statement. The accounting methods used can affect net income, stockholders equity and various financial statement ratios. However, the Corporation's accounting policies generally do not change

cash flows or liquidity.

Accounting for Exploration and Development Costs: Exploration and production activities are accounted for using the successful efforts method. Costs of acquiring unproved and proved oil and gas leasehold acreage, including lease bonuses, brokers' fees and other related costs, are capitalized. Annual lease rentals, exploration expenses and exploratory dry hole costs are expensed as incurred. Costs of drilling and equipping productive wells, including development dry holes, and related production facilities are capitalized.

The costs of exploratory wells that find oil and gas reserves are capitalized pending determination of whether proved reserves have been found. Exploratory drilling costs remain capitalized after drilling is completed if (1) the well has found a sufficient quantity of reserves to justify completion as a producing well and (2) sufficient progress is being made in assessing the reserves and the economic and operating viability of the project. If either of those criteria is not met, or if there is substantial doubt about the economic or operational viability of the project, the

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capitalized well costs are charged to expense. Indicators of sufficient progress in assessing reserves and the economic and operating viability of a project include: commitment of project personnel, active negotiations for sales contracts with customers, negotiations with governments, operators and contractors and firm plans for additional drilling and other factors.

Crude Oil and Natural Gas Reserves: The determination of estimated proved reserves is a significant element in arriving at the results of operations of exploration and production activities. The estimates of proved reserves affect well capitalizations, the unit of production depreciation rates of proved properties and wells and equipment, as well as impairment testing of oil and gas assets and goodwill.

The Corporation's oil and gas reserves are calculated in accordance with SEC regulations and interpretations and the requirements of the Financial Accounting Standards Board. For reserves to be booked as proved they must be commercially producible, government and project operator approvals must be obtained and, depending on the amount of the project cost, senior management or the board of directors must commit to fund the project. The Corporation's oil and gas reserve estimation and reporting process involves an annual independent third party reserve determination as well as internal technical appraisals of reserves. The Corporation maintains its own internal reserve estimates that are calculated by technical staff that work directly with the oil and gas properties. The Corporation's technical staff updates reserve estimates throughout the year based on evaluations of new wells, performance reviews, new technical data and other studies. To provide consistency throughout the Corporation, standard reserve estimation guidelines, definitions, reporting reviews and approval practices are used. The internal reserve estimates are subject to internal technical audits and senior management review.

The oil and gas reserve estimates reported in the Supplementary Oil and Gas Data in accordance with Statement of Financial Accounting Standards (FAS) 69 *Disclosures about Oil and Gas Producing Activities* (FAS 69) are determined independently by the consulting firm of DeGolyer and MacNaughton (D&M) and are consistent with internal estimates. Annually, the Corporation provides D&M with engineering, geological and geophysical data, actual production histories and other information necessary for the reserve determination. The Corporation's and D&M's technical staffs meet to review and discuss the information provided. Senior management and the Board of Directors review the final reserve estimates issued by D&M.

On December 31, 2008, the Securities and Exchange Commission published a final rule which revises its oil and gas reserve estimation and disclosure requirements. The revisions are effective for filings on Form 10-K for fiscal years ending December 31, 2009. The Corporation is evaluating the impact of these requirements on its oil and gas reserve estimates and disclosures.

Impairment of Long-Lived Assets and Goodwill: As explained below there are significant differences in the way long-lived assets and goodwill are evaluated and measured for impairment testing. The Corporation reviews long-lived assets, including oil and gas fields, for impairment whenever events or changes in circumstances indicate that the carrying amounts may not be recovered. Long-lived assets are tested based on identifiable cash flows that are largely independent of the cash flows of other assets and liabilities. If the carrying amounts of the long-lived assets are not expected to be recovered by undiscounted future net cash flow estimates, the assets are impaired and an impairment loss is recorded. The amount of impairment is based on the estimated fair value of the assets generally determined by discounting anticipated future net cash flows.

In the case of oil and gas fields, the present value of future net cash flows is based on management's best estimate of future prices, which is determined with reference to recent historical prices and published forward prices, applied to projected production volumes and discounted at a risk-adjusted rate. The projected production volumes represent reserves, including probable reserves, expected to be produced based on a stipulated amount of capital expenditures. The production volumes, prices and timing of production are consistent with internal projections and other externally

reported information. Oil and gas prices used for determining asset impairments will generally differ from those used in the standardized measure of discounted future net cash flows, since the standardized measure requires the use of actual prices on the last day of the year.

The Corporation's impairment tests of long-lived Exploration and Production producing assets are based on its best estimates of future production volumes (including recovery factors), selling prices, operating and capital costs, the timing of future production and other factors, which are updated each time an impairment test is performed. The

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Corporation could have impairments if the projected production volumes from oil and gas fields decrease, crude oil and natural gas selling prices decline significantly for an extended period or future estimated capital and operating costs increase significantly.

In accordance with FAS 142, *Goodwill and Other Intangible Assets*, the Corporation's goodwill is not amortized, but is tested for impairment at a reporting unit level, which is an operating segment or one level below an operating segment. The impairment test is conducted annually in the fourth quarter or when events or changes in circumstances indicate that the carrying amount of the goodwill may not be recoverable. The reporting unit or units used to evaluate and measure goodwill for impairment are determined primarily from the manner in which the business is managed. The Corporation's goodwill is assigned to the Exploration and Production operating segment and it expects that the benefits of goodwill will be recovered through the operation of that segment.

The Corporation's fair value estimate of the Exploration and Production segment is the sum of: (1) the discounted anticipated cash flows of producing assets and known developments, (2) the estimated risk adjusted present value of exploration assets, and (3) an estimated market premium to reflect the market price an acquirer would pay for potential synergies including cost savings, access to new business opportunities, enterprise control, improved processes and increased market share. The Corporation also considers the relative market valuation of similar Exploration and Production companies.

The determination of the fair value of the Exploration and Production operating segment depends on estimates about oil and gas reserves, future prices, timing of future net cash flows and market premiums. Significant extended declines in crude oil and natural gas prices or reduced reserve estimates could lead to a decrease in the fair value of the Exploration and Production operating segment that could result in an impairment of goodwill.

Because there are significant differences in the way long-lived assets and goodwill are evaluated and measured for impairment testing, there may be impairments of individual assets that would not cause an impairment of the goodwill assigned to the Exploration and Production segment.

Asset Retirement Obligations: The Corporation has material legal obligations to remove and dismantle long lived assets and to restore land or seabed at certain exploration and production locations. In accordance with generally accepted accounting principles, the Corporation recognizes a liability for the fair value of required asset retirement obligations. In addition, the fair value of any legally required conditional asset retirement obligations is recorded if the liability can be reasonably estimated. The Corporation capitalizes such costs as a component of the carrying amount of the underlying assets in the period in which the liability is incurred. In order to measure these obligations, the Corporation estimates the fair value of the obligations by discounting the future payments that will be required to satisfy the obligations. In determining these estimates, the Corporation is required to make several assumptions and judgments related to the scope of dismantlement, timing of settlement, interpretation of legal requirements, inflationary factors and discount rate. In addition, there are other external factors which could significantly affect the ultimate settlement costs for these obligations including: changes in environmental regulations and other statutory requirements, fluctuations in industry costs and foreign currency exchange rates, and advances in technology. As a result, the Corporation's estimates of asset retirement obligations are subject to revision due to the factors described above. Changes in estimates prior to settlement result in adjustments to both the liability and related asset values.

Derivatives: The Corporation utilizes derivative instruments for both non-trading and trading activities. In non-trading activities, the Corporation uses futures, forwards, options and swaps, individually or in combination to mitigate its exposure to fluctuations in the prices of crude oil, natural gas, refined products and electricity, and changes in foreign currency exchange rates. In trading activities, the Corporation, principally through a consolidated partnership, trades energy commodities and derivatives, including futures, forwards, options and swaps, based on expectations of future market conditions.

All derivative instruments are recorded at fair value in the Corporation's balance sheet. The Corporation's policy for recognizing the changes in fair value of derivatives varies based on the designation of the derivative. The changes in fair value of derivatives that are not designated as hedges under FAS 133, *Accounting for Derivative Instruments and Hedging Activities*, are recognized currently in earnings. Derivatives may be designated as hedges of expected future cash flows or forecasted transactions (cash flow hedges) or hedges of firm commitments (fair

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value hedges). The effective portion of changes in fair value of derivatives that are designated as cash flow hedges is recorded as a component of other comprehensive income (loss). Amounts included in accumulated other comprehensive income (loss) for cash flow hedges are reclassified into earnings in the same period that the hedged item is recognized in earnings. The ineffective portion of changes in fair value of derivatives designated as cash flow hedges is recorded currently in earnings. Changes in fair value of derivatives designated as fair value hedges are recognized currently in earnings. The change in fair value of the related hedged commitment is recorded as an adjustment to its carrying amount and recognized currently in earnings.

Derivatives that are designated as either cash flow or fair value hedges are tested for effectiveness prospectively before they are executed and both prospectively and retrospectively on an on-going basis to determine whether they continue to qualify for hedge accounting. The prospective and retrospective effectiveness calculations are performed using either historical simulation or other statistical models, which utilize historical observable market data consisting of futures curves and spot prices.

Fair Value Measurements: The Corporation's derivative instruments and supplemental pension plan investments are carried at fair value, with changes in fair value recognized in earnings or other comprehensive income each period. In determining fair value, the Corporation uses various valuation approaches, including the market and income approaches. The Corporation's fair value measurements also include non-performance risk and time value of money considerations. Counterparty credit is considered for receivable balances, and the Corporation's credit is considered for accrued liabilities.

The Corporation adopted the provisions of FAS 157, *Fair Value Measurements* (FAS 157), effective January 1, 2008. FAS 157 establishes a hierarchy for the inputs used to measure fair value based on the source of the input, which generally range from quoted prices for identical instruments in a principal trading market (Level 1) to estimates determined using related market data (Level 3). Multiple inputs may be used to measure fair value, however, the level of fair value for each financial asset or liability is based on the lowest significant input level within this fair value hierarchy. Details on the methods and assumptions used to determine the fair values of the financial assets and liabilities are as follows:

Fair value measurements based on Level 1 inputs:

Measurements that are most observable are based on quoted prices of identical instruments obtained from the principal markets in which they are traded. Closing prices are both readily available and representative of fair value. Market transactions occur with sufficient frequency and volume to assure liquidity. The fair value of certain of the Corporation's exchange traded futures and options are considered Level 1. In addition, fair values for the majority of the Corporation's supplemental pension plan investments are considered Level 1, since they are determined using quotations from national securities exchanges.

Fair value measurements based on Level 2 inputs:

Measurements derived indirectly from observable inputs or from quoted prices from markets that are less liquid are considered Level 2. Measurements based on Level 2 inputs include over-the-counter derivative instruments that are priced on an exchange traded curve, but have contractual terms that are not identical to exchange traded contracts. The Corporation utilizes fair value measurements based on Level 2 inputs for certain forwards, swaps and options. The liability related to the Corporation's crude oil hedges is classified as Level 2.

Fair value measurements based on Level 3 inputs:

Measurements that are least observable are estimated from related market data, determined from sources with little or no market activity for comparable contracts or are positions with longer durations. For example, in its energy marketing business, the Corporation sells natural gas and electricity to customers and offsets the price exposure by purchasing forward contracts. The fair value of these sales and purchases may be based on specific prices at less liquid delivered locations, which are classified as Level 3.

Income Taxes: Judgments are required in the determination and recognition of income tax assets and liabilities in the financial statements. These judgements include the requirement to only recognize the financial statement effect of a tax position when management believes that it is more likely than not, that based on the technical merits, the position will be sustained upon examination.

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The Corporation has net operating loss carryforwards or credit carryforwards in several jurisdictions, including the United States, and has recorded deferred tax assets for those losses and credits. Additionally, the Corporation has deferred tax assets due to temporary differences between the book basis and tax basis of certain assets and liabilities. Regular assessments are made as to the likelihood of those deferred tax assets being realized. If it is more likely than not that some or all of the deferred tax assets will not be realized, a valuation allowance is recorded to reduce the deferred tax assets to the amount that is expected to be realized. In evaluating realizability of deferred tax assets, the Corporation refers to the reversal periods for temporary differences, available carryforward periods for net operating losses and credit carryforwards, estimates of future taxable income, the availability of tax planning strategies, the existence of appreciated assets and other factors. Estimates of future taxable income are based on assumptions of oil and gas reserves and selling prices that are consistent with the Corporation's internal business forecasts. The Corporation does not provide for deferred U.S. income taxes applicable to undistributed earnings of foreign subsidiaries that are indefinitely reinvested in foreign operations.

Retirement Plans: The Corporation has funded non-contributory defined benefit pension plans and an unfunded supplemental pension plan. In accordance with FAS 158, *Employer's Accounting For Defined Benefit Pension and Other Postretirement Plans* (FAS 158), the Corporation recognizes on the balance sheet the net change in the funded status of the projected benefit obligation for these plans.

The determination of the obligations and expenses related to these plans are based on several actuarial assumptions, the most significant of which relate to the discount rate for measuring the present value of future plan obligations; expected long-term rates of return on plan assets; and rate of future increases in compensation levels. These assumptions represent estimates made by the Corporation, some of which can be affected by external factors. For example, the discount rate used to estimate the Corporation's projected benefit obligation is based on a portfolio of high-quality, fixed-income debt instruments with maturities that approximate the expected payment of plan obligations, while the expected return on plan assets is developed from the expected future returns for each asset category, weighted by the target allocation of pension assets to that asset category. Changes in these assumptions can have a material impact on the amounts reported in the Corporation's financial statements.

Changes in Accounting Policies

As discussed on page 35, the Corporation adopted FAS 157 effective January 1, 2008. The impact of adopting FAS 157 was not material to the Corporation's results of operations. Upon adoption, the Corporation recorded a reduction in the net deferred hedge losses reflected in accumulated other comprehensive income, which increased stockholders' equity by \$193 million, after income taxes.

Effective December 31, 2008, the Corporation applied the provisions of Emerging Issues Task Force 08-5, *Issuer's Accounting for Liabilities Measured at Fair Value with a Third-Party Credit Enhancement* (EITF 08-5). Upon adoption, the Corporation revalued certain derivative liabilities collateralized by letters of credit to reflect the Corporation's credit rating rather than the credit rating of the issuing bank. The adoption resulted in an increase in sales and other operating revenues of approximately \$13 million and an increase in other comprehensive income of approximately \$78 million, with a corresponding decrease in derivative liabilities recorded within accounts payable.

Recently Issued Accounting Standard

In December 2007, the FASB issued FAS 160, *Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51* (FAS 160). FAS 160 changes the accounting for and reporting of noncontrolling interests in a subsidiary. The Corporation will adopt the provisions of FAS 160 effective January 1, 2009 and estimates that adoption will result in a decrease in other long term liabilities and an increase in stockholders' equity of approximately \$85 million.

Environment, Health and Safety

The Corporation has implemented a values-based, socially-responsible strategy focused on improving environment, health and safety performance and making a positive impact on communities. The strategy is supported by the Corporation's environment, health, safety and social responsibility (EHS & SR) policies and by

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environment and safety management systems that help protect the Corporation's workforce, customers and local communities. The Corporation's management systems are designed to uphold or exceed international standards and are intended to promote internal consistency, adherence to policy objectives and continual improvement in EHS & SR performance. Improved performance may, in the short-term, increase the Corporation's operating costs and could also require increased capital expenditures to reduce potential risks to assets, reputation and license to operate. In addition to enhanced EHS & SR performance, improved productivity and operational efficiencies may be realized as collateral benefits from investments in EHS & SR. The Corporation has programs in place to evaluate regulatory compliance, audit facilities, train employees, prevent and manage risks and emergencies and to generally meet corporate EHS & SR goals.

The Corporation and HOVENSA produce and the Corporation distributes fuel oils in the United States. Proposals by state regulatory agencies and legislatures have been made that would require a lower sulfur content of fuel oils. If adopted, these proposals could require capital expenditures by the Registrant and HOVENSA to meet the required sulfur content standards.

As described in Item 3 Legal Proceedings, in 2003 the Corporation and HOVENSA began discussions with the U.S. EPA regarding the EPA's Petroleum Refining Initiative (PRI). The PRI is an ongoing program that is designed to reduce certain air emissions at all U.S. refineries. Since 2000, the EPA has entered into settlements addressing these emissions with petroleum refining companies that control nearly 90% of the domestic refining capacity. Negotiations with the EPA are continuing and substantial progress has been made toward resolving this matter for both the Corporation and HOVENSA. While the effect on the Corporation of the Petroleum Refining Initiative cannot be estimated until a final settlement is reached and entered by a court, additional future capital expenditures and operating expenses will likely be incurred over a number of years. The amount of penalties, if any, is not expected to be material to the Corporation.

The Corporation has undertaken a program to assess, monitor and reduce the emission of greenhouse gases, including carbon dioxide and methane. The Corporation recognizes that climate change is a global environmental concern with potentially significant consequences for society and the energy industry. The Corporation is committed to the responsible management of greenhouse gas emissions from our existing assets and future developments and is developing and implementing a strategy to control our carbon emissions.

The Corporation will have continuing expenditures for environmental assessment and remediation. Sites where corrective action may be necessary include gasoline stations, terminals, onshore exploration and production facilities, refineries (including solid waste management units under permits issued pursuant to the Resource Conservation and Recovery Act) and, although not currently significant, Superfund sites where the Corporation has been named a potentially responsible party.

The Corporation accrues for environmental assessment and remediation expenses when the future costs are probable and reasonably estimable. At year-end 2008, the Corporation's reserve for estimated environmental liabilities was approximately \$61 million. The Corporation expects that existing reserves for environmental liabilities will adequately cover costs to assess and remediate known sites. The Corporation's remediation spending was \$23 million in 2008, \$23 million in 2007 and \$15 million in 2006. Capital expenditures for facilities, primarily to comply with federal, state and local environmental standards, other than for the low sulfur requirements, were \$15 million in 2008 and \$22 million in 2007 and 2006.

Forward-Looking Information

Certain sections of Management's Discussion and Analysis of Financial Condition and Results of Operations and Quantitative and Qualitative Disclosures about Market Risk, including references to the Corporation's future results of

operations and financial position, liquidity and capital resources, capital expenditures, oil and gas production, tax rates, debt repayment, hedging, derivative, market risk and environmental disclosures, off-balance sheet arrangements and contractual obligations and contingencies include forward-looking information. Forward-looking disclosures are based on the Corporation's current understanding and assessment of these activities and reasonable assumptions about the future. Actual results may differ from these disclosures because of changes in market conditions, government actions and other factors.

Table of Contents**Item 7A. *Quantitative and Qualitative Disclosures About Market Risk***

In the normal course of its business, the Corporation is exposed to commodity risks related to changes in the price of crude oil, natural gas, refined products and electricity, as well as to changes in interest rates and foreign currency values. In the disclosures that follow, these operations are referred to as non-trading activities. The Corporation also has trading operations, principally through a 50% voting interest in a consolidated partnership that trades energy commodities. These activities are also exposed to commodity risks primarily related to the prices of crude oil, natural gas and refined products. The following describes how these risks are controlled and managed.

Controls: The Corporation maintains a control environment under the direction of its chief risk officer and through its corporate risk policy, which the Corporation's senior management has approved. Controls include volumetric, term and value-at-risk limits. In addition, the chief risk officer must approve the use of new instruments or commodities. Risk limits are monitored daily and exceptions are reported to business units and to senior management. The Corporation's risk management department also performs independent verifications of sources of fair values and validations of valuation models. These controls apply to all of the Corporation's non-trading and trading activities, including the consolidated trading partnership. The Corporation's treasury department is responsible for administering foreign exchange rate and interest rate hedging programs.

Instruments: The Corporation primarily uses forward commodity contracts, foreign exchange forward contracts, futures, swaps, options and energy commodity based securities in its non-trading and trading activities. These contracts are generally widely traded instruments with standardized terms. The following describes these instruments and how the Corporation uses them:

Forward Commodity Contracts: The Corporation enters into contracts for the forward purchase and sale of commodities. At settlement date, the notional value of the contract is exchanged for physical delivery of the commodity. Forward contracts that are designated as normal purchase and sale contracts under FAS 133 are excluded from the quantitative market risk disclosures.

Forward Foreign Exchange Contracts: The Corporation enters into forward contracts primarily for the British pound, the Norwegian krone, and the Danish krone, which commit the Corporation to buy or sell a fixed amount of these currencies at a predetermined exchange rate on a future date.

Exchange Traded Contracts: The Corporation uses exchange traded contracts, including futures, on a number of different underlying energy commodities. These contracts are settled daily with the relevant exchange and may be subject to exchange position limits.

Swaps: The Corporation uses financially settled swap contracts with third parties as part of its hedging and trading activities. Cash flows from swap contracts are determined based on underlying commodity prices and are typically settled over the life of the contract.

Options: Options on various underlying energy commodities include exchange traded and third party contracts and have various exercise periods. As a seller of options, the Corporation receives a premium at the outset and bears the risk of unfavorable changes in the price of the commodity underlying the option. As a purchaser of options, the Corporation pays a premium at the outset and has the right to participate in the favorable price movements in the underlying commodities. These premiums are a component of the fair value of the options.

Energy Securities: Energy securities include energy related equity or debt securities issued by a company or government or related derivatives on these securities.

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Value-at-Risk: The Corporation uses value-at-risk to monitor and control commodity risk within its trading and non-trading activities. The value-at-risk model uses historical simulation and the results represent the potential loss in fair value over one day at a 95% confidence level. The model captures both first and second order sensitivities for options. The following table summarizes the value-at-risk results for trading and non-trading activities. These results may vary from time to time as strategies change in trading activities or hedging levels change in non-trading activities.

	Trading Activities	Non-trading Activities
	(Millions of dollars)	
2008		
At December 31	\$ 17	\$ 13
Average	13	90
High	17	140
Low	11	13
2007		
At December 31	\$ 10	\$ 72
Average	12	63
High	13	72
Low	10	54

Non-trading: The Corporation's non-trading activities may include hedging of crude oil and natural gas production. Futures and swaps are used to fix the selling prices of a portion of the Corporation's future production and the related gains or losses are an integral part of the Corporation's selling prices. In October 2008, the Corporation closed its Brent crude oil hedge positions by entering into offsetting contracts with the same counterparty covering 24,000 barrels per day from 2009 through 2012 at a per barrel price of \$86.95 each year. The after-tax deferred losses related to closed crude oil contracts will be recorded in earnings as the contracts mature.

There were no hedges of WTI crude oil or natural gas production at December 31, 2008. The Corporation also markets energy commodities including refined petroleum products, natural gas and electricity. The Corporation uses futures, swaps and options to manage the risk in its marketing activities. Accumulated other comprehensive income (loss) at December 31, 2008 includes after-tax deferred losses of \$1,478 million primarily related to closed crude oil contracts that were used as hedges of exploration and production sales.

The Corporation uses foreign exchange contracts to reduce its exposure to fluctuating foreign exchange rates by entering into forward contracts for various currencies including the British pound, the Norwegian krone and the Danish krone. At December 31, 2008, the Corporation had \$896 million of notional value foreign exchange contracts maturing in 2009. The fair value of the foreign exchange contracts was a payable of \$75 million at December 31, 2008. The change in fair value of the foreign exchange contracts from a 20% change in exchange rates is estimated to be approximately \$165 million at December 31, 2008.

The Corporation's outstanding debt of \$3,955 million has a fair value of \$3,883 million at December 31, 2008. A 15% decrease in the rate of interest would increase the fair value of debt by approximately \$85 million at December 31, 2008.

Trading: In trading activities, the Corporation is primarily exposed to changes in crude oil, natural gas and refined product prices. The trading partnership in which the Corporation has a 50% voting interest trades energy commodities, securities and derivatives. The accounts of the partnership are consolidated with those of the Corporation. The Corporation also takes trading positions for its own account. The information that follows represents 100% of the trading partnership and the Corporation's proprietary trading accounts.

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Gains or losses from sales of physical products are recorded at the time of sale. Total realized gains (losses) on trading activities amounted to \$(317) million in 2008 and \$303 million in 2007. Derivative trading transactions are marked-to-market and unrealized gains or losses are reflected in income currently. The following table provides an assessment of the factors affecting the changes in fair value of trading activities and represents 100% of the trading partnership and other trading activities.

	2008	2007
	(Millions of dollars)	
Fair value of contracts outstanding at the beginning of the year	\$ 154	\$ 365
Change in fair value of contracts outstanding at the beginning of the year and still outstanding at the end of year	(257)	193
Reversal of fair value for contracts closed during the year	42	(230)
Fair value of contracts entered into during the year and still outstanding	925	(174)
Fair value of contracts outstanding at the end of the year	\$ 864	\$ 154

The Corporation measures fair value and summarizes the sources of fair value for derivatives in accordance with the provisions of FAS 157. See the discussion on page 35 for more details on how the Corporation measures fair value.

The following table summarizes the sources of fair values of derivatives used in the Corporation's trading activities at December 31, 2008:

	Total	2009	2010	2011	2012 and Beyond
	(Millions of dollars)				
Source of fair value					
Level 1	\$ 35	\$ (22)	\$ 63	\$ 2	\$ (8)
Level 2	885	564	180	82	59
Level 3	(56)	(42)	(12)	(1)	(1)
Total	\$ 864	\$ 500	\$ 231	\$ 83	\$ 50

The following table summarizes the receivables net of cash margin and letters of credit relating to the Corporation's trading activities and the credit ratings of counterparties at December 31:

2008 **2007**
(Millions of dollars)

Investment grade determined by outside sources