

HESS CORP
Form 10-Q
November 06, 2008

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

Form 10-Q

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

For the quarter ended *September 30, 2008*

or

**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)
13-4921002
(I.R.S. Employer Identification Number)
1185 AVENUE OF THE AMERICAS, NEW YORK, N.Y.
(Address of Principal Executive Offices)
10036
(Zip Code)

(Registrant's Telephone Number, Including Area Code is (212) 997-8500)

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 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

At September 30, 2008, there were 326,068,288 shares of Common Stock outstanding.

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HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
STATEMENT OF CONSOLIDATED INCOME (UNAUDITED)
(In millions, except per share data)

| | Three Months Ended | | Nine Months Ended | |
|---|---------------------------|---------------|--------------------------|-----------------|
| | September 30, | | September 30, | |
| | 2008 | 2007 | 2008 | 2007 |
| REVENUES AND NON-OPERATING INCOME | | | | |
| Sales (excluding excise taxes) and other operating revenues | \$ 11,398 | \$ 7,451 | \$ 33,782 | \$ 22,191 |
| Equity in income of HOVENSA L.L.C | 52 | 19 | 23 | 156 |
| Gain on asset sales | | | | 21 |
| Other, net | (62) | 34 | 38 | 56 |
| Total revenues and non-operating income | 11,388 | 7,504 | 33,843 | 22,424 |
| COSTS AND EXPENSES | | | | |
| Cost of products sold (excluding items shown separately below) | 8,165 | 5,322 | 24,237 | 15,922 |
| Production expenses | 503 | 394 | 1,421 | 1,118 |
| Marketing expenses | 266 | 238 | 766 | 701 |
| Exploration expenses, including dry holes and lease impairment | 157 | 131 | 467 | 314 |
| Other operating expenses | 62 | 45 | 154 | 115 |
| General and administrative expenses | 170 | 133 | 478 | 406 |
| Interest expense | 68 | 59 | 200 | 185 |
| Depreciation, depletion and amortization | 497 | 365 | 1,431 | 1,046 |
| Total costs and expenses | 9,888 | 6,687 | 29,154 | 19,807 |
| INCOME BEFORE INCOME TAXES | 1,500 | 817 | 4,689 | 2,617 |
| Provision for income taxes | 725 | 422 | 2,255 | 1,295 |
| NET INCOME | \$ 775 | \$ 395 | \$ 2,434 | \$ 1,322 |
| NET INCOME PER SHARE | | | | |
| BASIC | \$ 2.40 | \$ 1.26 | \$ 7.60 | \$ 4.24 |
| DILUTED | 2.37 | 1.23 | 7.47 | 4.15 |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING (DILUTED) | 327.4 | 319.9 | 325.7 | 318.6 |
| COMMON STOCK DIVIDENDS PER SHARE | \$.10 | \$.10 | \$.30 | \$.30 |

See accompanying notes to consolidated financial statements.

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PART I FINANCIAL INFORMATION (CONT. D.)
HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
CONSOLIDATED BALANCE SHEET (UNAUDITED)
(In millions of dollars, thousands of shares)

| | September 30, 2008 | December 31, 2007 |
|--|-----------------------------------|----------------------------------|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 1,380 | \$ 607 |
| Accounts receivable | 4,652 | 4,708 |
| Inventories | 1,817 | 1,250 |
| Other current assets | 317 | 361 |
| Total current assets | 8,166 | 6,926 |
| INVESTMENTS IN AFFILIATES | | |
| HOVENSA L.L.C | 907 | 933 |
| Other | 201 | 184 |
| Total investments in affiliates | 1,108 | 1,117 |
| PROPERTY, PLANT AND EQUIPMENT | | |
| Total at cost | 28,153 | 24,831 |
| Less reserves for depreciation, depletion, amortization and lease impairment | 11,497 | 10,197 |
| Property, plant and equipment net | 16,656 | 14,634 |
| GOODWILL | 1,225 | 1,225 |
| DEFERRED INCOME TAXES | 2,109 | 1,873 |
| OTHER ASSETS | 314 | 356 |
| TOTAL ASSETS | \$ 29,578 | \$ 26,131 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| CURRENT LIABILITIES | | |
| Accounts payable | \$ 6,108 | \$ 5,741 |
| Accrued liabilities | 1,716 | 1,638 |
| Taxes payable | 897 | 583 |
| Current maturities of long-term debt | 39 | 62 |
| Total current liabilities | 8,760 | 8,024 |
| LONG-TERM DEBT | 3,893 | 3,918 |
| DEFERRED INCOME TAXES | 2,503 | 2,362 |

| | | |
|--|------------------|------------------|
| ASSET RETIREMENT OBLIGATIONS | 1,344 | 1,016 |
| OTHER LIABILITIES | 847 | 1,037 |
| Total liabilities | 17,347 | 16,357 |
| STOCKHOLDERS EQUITY | | |
| Preferred stock, par value \$1.00, 20,000 shares authorized 3% cumulative convertible series Authorized 330 shares Issued 0 shares at September 30, 2008; 284 shares at December 31, 2007 | | |
| Common stock, par value \$1.00 Authorized 600,000 shares Issued 326,068 shares at September 30, 2008; 320,600 shares at December 31, 2007 | 326 | 321 |
| Capital in excess of par value | 2,074 | 1,882 |
| Retained earnings | 11,749 | 9,412 |
| Accumulated other comprehensive income (loss) | (1,918) | (1,841) |
| Total stockholders equity | 12,231 | 9,774 |
| TOTAL LIABILITIES AND STOCKHOLDERS EQUITY | \$ 29,578 | \$ 26,131 |

See accompanying notes to consolidated financial statements.

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PART I FINANCIAL INFORMATION (CONT. D.)
HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
STATEMENT OF CONSOLIDATED CASH FLOWS (UNAUDITED)
(In millions)

| | Nine Months Ended September 30, | |
|--|--|---------------|
| | 2008 | 2007 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net income | \$ 2,434 | \$ 1,322 |
| Adjustments to reconcile net income to net cash provided by operating activities | | |
| Depreciation, depletion and amortization | 1,431 | 1,046 |
| Exploratory dry hole costs and lease impairment | 171 | 75 |
| Pre-tax gain on asset sales | | (21) |
| Provision for deferred income taxes | 18 | 66 |
| Distributed earnings of HOVENSA L.L.C., net | 27 | 44 |
| Changes in other operating assets and liabilities | (9) | 169 |
| Net cash provided by operating activities | 4,072 | 2,701 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Capital expenditures | (3,282) | (2,773) |
| Proceeds from asset sales | | 93 |
| Other, net | 50 | (6) |
| Net cash used in investing activities | (3,232) | (2,686) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Debt with maturities of greater than 90 days | | |
| Borrowings | 312 | 761 |
| Repayments | (360) | (548) |
| Cash dividends paid | (130) | (127) |
| Employee stock options exercised | 111 | 81 |
| Net cash (used in) provided by financing activities | (67) | 167 |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 773 | 182 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR | 607 | 383 |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD | \$ 1,380 | \$ 565 |

See accompanying notes to consolidated financial statements.

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PART I FINANCIAL INFORMATION (CONT. D.)
HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Basis of Presentation

The financial statements included in this report reflect all normal and recurring adjustments which, in the opinion of management, are necessary for a fair presentation of Hess Corporation's (the Corporation) consolidated financial position at September 30, 2008 and December 31, 2007, and the consolidated results of operations for the three and nine month periods ended September 30, 2008 and 2007 and the consolidated cash flows for the nine month periods ended September 30, 2008 and 2007. The unaudited results of operations for the interim periods reported are not necessarily indicative of results to be expected for the full year.

The financial statements were prepared in accordance with the requirements of the Securities and Exchange Commission (SEC) for interim reporting. As permitted under those rules, certain notes or other financial information that are normally required by U.S. generally accepted accounting principles (GAAP) have been condensed or omitted from these interim financial statements. These statements, therefore, should be read in conjunction with the consolidated financial statements and related notes included in the Corporation's Form 10-K for the year ended December 31, 2007.

Effective January 1, 2008, the Corporation adopted Financial Accounting Standards Board (FASB) Statement No. 157, *Fair Value Measurements* (FAS 157) for financial assets and liabilities that are required to be measured at fair value. FAS 157 established a framework for measuring fair value and requires disclosure of a fair value hierarchy (see Note 8, *Fair Value Measurements*). 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 approximately \$190 million, after income taxes.

In December 2007, the FASB issued FAS No. 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 is currently evaluating the impact of adoption on its financial statements and, as required, will adopt the provisions of FAS 160 effective January 1, 2009.

2. Inventories

Inventories consist of the following (in millions):

| | September 30, 2008 | December 31, 2007 |
|-------------------------------------|--------------------------|-------------------------|
| Crude oil and other charge stocks | \$ 519 | \$ 338 |
| Refined products and natural gas | 2,193 | 1,577 |
| Less: LIFO adjustment | (1,336) | (1,029) |
| | 1,376 | 886 |
| Merchandise, materials and supplies | 441 | 364 |
| Total inventories | \$ 1,817 | \$ 1,250 |

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PART I FINANCIAL INFORMATION (CONT. D.)
HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

3. Refining Joint Venture

The Corporation accounts for its investment in HOVENSA L.L.C. (HOVENSA) using the equity method. Summarized financial information for HOVENSA follows (in millions):

| | September 30, 2008 | December 31, 2007 |
|----------------------------------|--------------------------|-------------------------|
| Summarized balance sheet | | |
| Cash and short-term investments | \$ 305 | \$ 279 |
| Other current assets | 1,240 | 1,183 |
| Net fixed assets | 2,149 | 2,181 |
| Other assets | 61 | 62 |
| Current liabilities | (1,546) | (1,459) |
| Long-term debt | (356) | (356) |
| Deferred liabilities and credits | (85) | (75) |
| Members' equity | \$ 1,768 | \$ 1,815 |

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|-------------------------------------|----------|------------------------------------|----------|
| | 2008 | 2007 | 2008 | 2007 |
| Summarized income statement | | | | |
| Total sales | \$ 5,404 | \$ 3,539 | \$ 15,143 | \$ 9,181 |
| Cost and expenses | (5,299) | (3,500) | (15,092) | (8,866) |
| Net income | \$ 105 | \$ 39 | \$ 51 | \$ 315 |
| Hess Corporation's share, before income taxes | \$ 52 | \$ 19 | \$ 23 | \$ 156 |

During the first nine months of 2008 and 2007, the Corporation received cash distributions from HOVENSA of \$50 million and \$200 million, respectively.

4. Capitalized Exploratory Well Costs

The following table discloses the net changes in capitalized exploratory well costs pending determination of proved reserves for the nine months ended September 30, 2008 (in millions):

| | |
|---|--------|
| Balance at beginning of period | \$ 608 |
| Additions to capitalized exploratory well costs pending the determination of proved reserves | 455 |
| Reclassifications to wells, facilities, and equipment based on the determination of proved reserves | (65) |
| Capitalized exploratory well costs charged to expense | (7) |
| Balance at end of period | \$ 991 |

The preceding table excludes costs related to exploratory dry holes of \$83 million which were incurred and subsequently expensed in 2008. Approximately 60% of the capitalized well costs are related to two projects in the deepwater Gulf of Mexico where further appraisal drilling is planned or development plans are being prepared.

Capitalized exploratory well costs greater than one year old after completion of drilling were \$380 million as of September 30, 2008 and \$304 million as of December 31, 2007.

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PART I FINANCIAL INFORMATION (CONT. D.)
HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

5. Long-Term Debt and Capitalized Interest

At September 30, 2008, the Corporation classified an aggregate of \$515 million of borrowings under short-term credit facilities as long-term debt, based on the available capacity under its \$3 billion syndicated revolving credit facility, substantially all of which is committed through May 2012.

Capitalized interest on development projects amounted to the following (in millions):

| | Three months ended September 30, | | Nine months ended September 30, | |
|----------------------|-------------------------------------|-------|------------------------------------|-------|
| | 2008 | 2007 | 2008 | 2007 |
| Capitalized interest | \$ 2 | \$ 18 | \$ 4 | \$ 49 |

6. Foreign Currency

Foreign currency gains (losses) amounted to the following (in millions):

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|-------------------------------------|-------|------------------------------------|-------|
| | 2008 | 2007 | 2008 | 2007 |
| Pre-tax foreign currency gains (losses) | \$ (76) | \$ 20 | \$ (32) | \$ 14 |
| After-tax foreign currency gains (losses) | (10) | 1 | 2 | (10) |

The pre-tax amount of foreign currency gains (losses) is included in Other, net within Revenues and non-operating income.

7. Retirement Plans

Components of net periodic pension cost consisted of the following (in millions):

| | Three months ended September 30, | | Nine months ended September 30, | |
|--------------------------------|-------------------------------------|-------|------------------------------------|-------|
| | 2008 | 2007 | 2008 | 2007 |
| Service cost | \$ 9 | \$ 11 | \$ 29 | \$ 29 |
| Interest cost | 15 | 18 | 55 | 52 |
| Expected return on plan assets | (15) | (18) | (55) | (52) |
| Amortization of net loss | 6 | 6 | 12 | 16 |
| Pension expense | \$ 15 | \$ 17 | \$ 41 | \$ 45 |

In 2008, the Corporation expects to contribute approximately \$65 million to its funded pension plans and \$15 million to the trust established for its unfunded pension plan. Through September 30, 2008, the Corporation contributed \$76 million to its pension plans.

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PART I FINANCIAL INFORMATION (CONT. D.)
HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

8. Fair Value Measurements

The Corporation adopted the provisions of FAS 157 effective January 1, 2008 (see Note 1, Basis of Presentation). 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 presented below is based on the lowest significant input level within this fair value hierarchy. The following table provides the fair value hierarchy of the Corporation's financial assets and (liabilities) as of September 30, 2008 (in millions):

| | Level 1 | Level 2 | Level 3 | Collateral and counterparty netting | Total |
|---------------------------------------|---------|---------|---------|--|---------|
| Supplemental pension plan investments | \$ 73 | \$ | \$ 15 | \$ | \$ 88 |
| Derivative contracts | | | | | |
| Assets | 306 | 1,178 | 316 | (811) | 989 |
| Liabilities | (268) | (3,812) | (284) | 674 | (3,690) |

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 pension 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 hedging program is classified as Level 2.

Fair value measurements based on Level 3 inputs:

Measurements that are least observable are estimated from related market data or determined from sources with little or no market activity for comparable contracts. For example, in its energy marketing business, the Corporation sells natural gas and electricity to customers and economically hedges 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. There may be offsets to these positions that are priced based on more liquid markets, which are, therefore, classified as Level 1 or Level 2.

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PART I FINANCIAL INFORMATION (CONT. D.)
HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

The following table provides changes in financial assets and liabilities that are measured at fair value based on Level 3 inputs (in millions):

| | Three months ended September 30, 2008 | Nine months ended September 30, 2008 |
|---|--|--|
| Balance at beginning of period | \$ 559 | \$ (4) |
| Unrealized gains (losses) | | |
| Included in earnings (*) | 259 | 224 |
| Included in other comprehensive income | (708) | (93) |
| Purchases, sales or other settlements during the period | (18) | (21) |
| Net transfers in to (out of) Level 3 | (45) | (59) |
| Balance at end of period | \$ 47 | \$ 47 |

(*) Reflected in
Sales and other
operating
revenue.

9. Weighted Average Common Shares

The weighted average number of common shares used in the basic and diluted earnings per share computations are as follows (in thousands):

| | Three months ended September 30, | | Nine months ended September 30, | |
|-------------------------------|-------------------------------------|---------|------------------------------------|---------|
| | 2008 | 2007 | 2008 | 2007 |
| Common shares basic | 322,365 | 313,617 | 320,159 | 311,986 |
| Effect of dilutive securities | | | | |
| Stock options | 2,985 | 2,856 | 3,228 | 2,889 |
| Restricted common stock | 1,670 | 2,802 | 1,866 | 3,078 |
| Convertible preferred stock | 366 | 590 | 467 | 601 |
| Common shares diluted | 327,386 | 319,865 | 325,720 | 318,554 |

During the third quarter of 2008, the Corporation's remaining 284,139 outstanding shares of 3% cumulative convertible preferred shares were converted into common stock at a conversion rate of 1.8783 shares of common stock for each preferred share. The Corporation issued 533,697 shares of common stock for the conversion of these preferred shares and fractional shares were settled by cash payments.

10. Comprehensive Income

Comprehensive income (loss) was as follows (in millions):

Three months Nine months

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| | ended September 30, | | ended September 30, | |
|--|------------------------|--------|------------------------|----------|
| | 2008 | 2007 | 2008 | 2007 |
| Net income | \$ 775 | \$ 395 | \$ 2,434 | \$ 1,322 |
| Deferred gains (losses) on cash flow hedges, after tax | | | | |
| Effect of hedge losses recognized in income | 83 | 98 | 270 | 209 |
| Net change in fair value of cash flow hedges | 326 | (91) | (327) | (267) |
| Change in minimum postretirement plan liabilities, after tax | 3 | 4 | 8 | 12 |
| Change in foreign currency translation adjustment and other | (61) | 30 | (28) | 36 |
| Comprehensive income | \$ 1,126 | \$ 436 | \$ 2,357 | \$ 1,312 |

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PART I FINANCIAL INFORMATION (CONT. D.)
HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

The Corporation reclassifies hedging gains and losses included in other comprehensive income (loss) to earnings at the time the hedged transactions are recognized. Hedging decreased Exploration and Production results for the three and nine months ended September 30, 2008 by \$224 million (\$138 million after income taxes) and \$610 million (\$377 million after income taxes), respectively. For the three and nine months ended September 30, 2007, hedging decreased Exploration and Production results by \$101 million (\$60 million after income taxes) and \$258 million (\$155 million after income taxes), respectively.

At September 30, 2008, accumulated other comprehensive income (loss) included net after-tax unrealized deferred losses of \$1,729 million related to crude oil contracts used as hedges of future Exploration and Production sales and derivatives used to manage the risk in its Marketing activities. The pre-tax amount of any deferred hedge losses and gains is reflected in accounts payable and accounts receivable, respectively, and the related income tax impact is recorded as deferred income taxes on the balance sheet. See Note 12, Subsequent Event for additional activity related to the crude oil hedge positions after September 30, 2008.

11. Segment Information

The Corporation's results by operating segment were as follows (in millions):

| | Three months ended September 30, | | Nine months ended September 30, | |
|------------------------------------|-------------------------------------|----------|------------------------------------|-----------|
| | 2008 | 2007 | 2008 | 2007 |
| Operating revenues | | | | |
| Exploration and Production | \$ 2,773 | \$ 1,803 | \$ 8,659 | \$ 5,283 |
| Marketing and Refining | 8,683 | 5,691 | 25,330 | 17,058 |
| Less: Transfers between affiliates | (58) | (43) | (207) | (150) |
| Total (*) | \$ 11,398 | \$ 7,451 | \$ 33,782 | \$ 22,191 |
| Net income (loss) | | | | |
| Exploration and Production | \$ 699 | \$ 414 | \$ 2,548 | \$ 1,259 |
| Marketing and Refining | 161 | 46 | 125 | 269 |
| Corporate, including interest | (85) | (65) | (239) | (206) |
| Total | \$ 775 | \$ 395 | \$ 2,434 | \$ 1,322 |

(*) Operating revenues exclude excise and similar taxes of approximately \$550 million and \$500 million in the third quarter of 2008 and 2007,

respectively,
and
\$1,650 million
and
\$1,500 million
during the first
nine months of
2008 and 2007,
respectively.

Identifiable assets by operating segment were as follows (in millions):

| | September 30, 2008 | December 31, 2007 |
|----------------------------|--------------------------|-------------------------|
| Exploration and Production | \$ 19,567 | \$ 17,008 |
| Marketing and Refining | 7,208 | 6,667 |
| Corporate | 2,803 | 2,456 |
| Total | \$ 29,578 | \$ 26,131 |

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PART I FINANCIAL INFORMATION (CONT. D.)
HESS CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

12. Subsequent Event

At September 30, 2008, the Corporation had outstanding Brent crude oil hedge positions on 24,000 barrels per day of production through 2012 at prices ranging from \$25.54 to \$26.90 per barrel. 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 fourth quarter 2008 hedges were not affected by these transactions and are still open. The deferred after-tax loss as of the date the hedge positions were closed will be recorded in earnings as the contracts mature.

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Item 2. Management's Discussion and Analysis of Results of Operations and Financial Condition.****Overview**

Hess Corporation (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 was \$775 million for the third quarter of 2008, compared with \$395 million in the third quarter of 2007.

Exploration and Production: E&P earnings were \$699 million for the third quarter of 2008, compared with \$414 million in the third quarter of 2007. In the third quarter of 2008, the Corporation's average worldwide crude oil selling price, including the effect of hedging, was \$93.36 per barrel compared with \$65.26 per barrel in the third quarter of 2007. The Corporation's average worldwide natural gas selling price, including the effect of hedging, was \$7.60 per Mcf in the third quarter of 2008 compared with \$5.38 per Mcf in the third quarter of 2007. Worldwide crude oil and natural gas production was 361,000 barrels of oil equivalent per day (boepd) in the third quarter of 2008 compared with 357,000 boepd in the same period of 2007. Facilities downtime associated with hurricanes in the Gulf of Mexico reduced third quarter production by an average of approximately 11,000 boepd and will also reduce fourth quarter production. As a result, full year production is now expected to be approximately 380,000 boepd.

The following is an update of recent Exploration and Production activities:

The Corporation continued progressing its field developments during the third quarter. Production from Phase 2 at Block A-18 of the Joint Development Area of Malaysia and Thailand (Hess 50%) and the Shenzi Field (Hess 28%) in the deepwater Gulf of Mexico are expected to start up in early 2009 and oil production from the Ujung Pangkah Field (Hess 75%) in Indonesia is planned to commence in mid-2009.

The Corporation completed its initial four exploration well program on Block WA-390-P (Hess 100%) located in Australia's Northwest Shelf. Following the Glencoe and Briseis discoveries, the Corporation's Nimblefoot-1 exploration well encountered 93 feet of net gas pay in September. In October, the Corporation completed the fourth well, Warrior-1, which failed to find commercial quantities of hydrocarbons. The Corporation plans to integrate the results of this drilling campaign with recently acquired seismic data to determine its 2009 drilling program, which is currently expected to commence in the second half of the year.

In the third quarter of 2008, the Corporation commenced drilling deepwater wells on Block 54 (Hess 100%) in Libya and Cape Three Points (Hess 100%) in Ghana. In October 2008, drilling of an exploration well commenced on the BMS 22 Block in the Santos Basin (Hess 40%) located offshore Brazil.

Marketing and Refining: M&R results generated income of \$161 million in the third quarter of 2008, compared with income of \$46 million in the third quarter of 2007, primarily reflecting higher refining and marketing margins.

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Results of Operations**

The after-tax results by major operating activity were as follows (in millions, except per share data):

| | Three months ended | | Nine months ended | |
|--------------------------------|--------------------|---------|-------------------|----------|
| | September 30, | | September 30, | |
| | 2008 | 2007 | 2008 | 2007 |
| Exploration and Production | \$ 699 | \$ 414 | \$ 2,548 | \$ 1,259 |
| Marketing and Refining | 161 | 46 | 125 | 269 |
| Corporate | (42) | (28) | (114) | (91) |
| Interest expense | (43) | (37) | (125) | (115) |
| Net income | \$ 775 | \$ 395 | \$ 2,434 | \$ 1,322 |
| Net income per share (diluted) | \$ 2.37 | \$ 1.23 | \$ 7.47 | \$ 4.15 |

Items Affecting Comparability Between Periods

The following table reflects the total after-tax impact of items affecting comparability of earnings between periods (in millions):

| | Three months ended | | Nine months ended | |
|----------------------------|--------------------|---------|-------------------|---------|
| | September 30, | | September 30, | |
| | 2008 | 2007 | 2008 | 2007 |
| Exploration and Production | \$ | \$ (33) | \$ | \$ (18) |
| Marketing and Refining | | | | |
| Corporate | | | | |
| | \$ | \$ (33) | \$ | \$ (18) |

In the third quarter of 2007, the Corporation recorded charges totaling \$33 million (\$64 million before income taxes) for adjustments to prior meter readings at two offshore fields. During the second quarter of 2007, the Corporation recorded a net gain of \$15 million (\$21 million before income taxes) related to the sale of its interests in the Scott and Telford fields located in the United Kingdom North Sea.

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 preferable to pre-tax amounts for explaining variances in earnings, since they show the entire effect of a transaction. After-tax amounts are determined by applying the appropriate income tax rate in each tax jurisdiction to pre-tax amounts.

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Results of Operations (continued)****Comparison of Results*****Exploration and Production***

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

| | Three months ended September 30, | | Nine months ended September 30, | |
|--|-------------------------------------|----------|------------------------------------|----------|
| | 2008 | 2007 | 2008 | 2007 |
| Sales and other operating revenues(*) | \$ 2,661 | \$ 1,747 | \$ 8,343 | \$ 5,060 |
| Non-operating income (expenses) | (71) | 30 | (2) | 52 |
| Total revenues | 2,590 | 1,777 | 8,341 | 5,112 |
| Cost and expenses | | | | |
| Production expenses, including related taxes | 503 | 394 | 1,421 | 1,118 |
| Exploration expenses, including dry holes and lease impairment | 157 | 131 | 467 | 314 |
| General, administrative and other expenses | 84 | 64 | 220 | 183 |
| Depreciation, depletion and amortization | 479 | 345 | 1,375 | 991 |
| Total costs and expenses | 1,223 | 934 | 3,483 | 2,606 |
| Results of operations before income taxes | 1,367 | 843 | 4,858 | 2,506 |
| Provision for income taxes | 668 | 429 | 2,310 | 1,247 |
| Results of operations | \$ 699 | \$ 414 | \$ 2,548 | \$ 1,259 |

(*) Amounts differ from E&P operating revenues in Note 11 Segment Information primarily due to the exclusion of sales of hydrocarbons purchased from unrelated third parties.

After considering the items affecting comparability between periods, the remaining changes in Exploration and Production earnings are primarily attributable to changes in selling prices, sales volumes, operating costs, exploration expenses and income taxes, as discussed below.

Selling prices: Higher average realized selling prices of crude oil and natural gas increased Exploration and Production revenues by approximately \$800 million and \$2,950 million in the third quarter and first nine months of

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2008, respectively, compared with the corresponding periods of 2007. The Corporation's average selling prices were as follows:

| | Three months ended September 30, | | Nine months ended September 30, | |
|--|-------------------------------------|---------|------------------------------------|---------|
| | 2008 | 2007 | 2008 | 2007 |
| Average selling prices | | | | |
| Crude oil per barrel (including hedging) | | | | |
| United States | \$116.14 | \$73.20 | \$109.39 | \$62.88 |
| Europe | 83.23 | 62.06 | 90.69 | 56.95 |
| Africa | 91.72 | 64.38 | 89.66 | 57.72 |
| Asia and other | 105.58 | 70.69 | 106.09 | 66.59 |
| Worldwide | 93.36 | 65.26 | 93.62 | 58.82 |
| Crude oil per barrel (excluding hedging) | | | | |
| United States | \$116.14 | \$73.20 | \$109.39 | \$62.88 |
| Europe | 83.23 | 62.06 | 90.69 | 56.95 |
| Africa | 108.49 | 73.49 | 106.91 | 66.47 |
| Asia and other | 105.58 | 70.69 | 106.09 | 66.59 |
| Worldwide | 102.80 | 69.85 | 102.03 | 62.66 |
| Natural gas liquids per barrel | | | | |
| United States | \$ 77.50 | \$51.27 | \$ 72.79 | \$47.43 |
| Europe | 81.84 | 48.44 | 84.77 | 51.55 |
| Worldwide | 78.50 | 50.58 | 75.96 | 48.83 |

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Results of Operations (continued)**

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|-------------------------------------|---------|------------------------------------|---------|
| | 2008 | 2007 | 2008 | 2007 |
| Natural gas per Mcf (including hedging) | | | | |
| United States | \$ 8.57 | \$ 5.80 | \$ 9.35 | \$ 6.75 |
| Europe | 10.12 | 6.09 | 9.75 | 5.03 |
| Asia and other | 5.77 | 4.69 | 5.33 | 4.55 |
| Worldwide | 7.60 | 5.38 | 7.48 | 5.08 |
| Natural gas per Mcf (excluding hedging) | | | | |
| United States | \$ 8.57 | \$ 5.80 | \$ 9.35 | \$ 6.75 |
| Europe | 10.84 | 6.09 | 10.16 | 5.03 |
| Asia and other | 5.77 | 4.69 | 5.33 | 4.55 |
| Worldwide | 7.85 | 5.38 | 7.64 | 5.08 |

Crude oil and natural gas hedges reduced Exploration and Production earnings by \$138 million and \$377 million in the third quarter and first nine months of 2008, respectively (\$224 million and \$610 million before income taxes). Crude oil hedges reduced Exploration and Production earnings by \$60 million and \$155 million in the third quarter and first nine months of 2007, respectively (\$101 million and \$258 million before income taxes). See the Non-Trading section of Market Risk Disclosures on page 21 for additional activity related to these hedge positions after September 30, 2008.

Sales and production volumes: The Corporation's crude oil and natural gas production, on a barrel of oil equivalent basis, was 361,000 boepd in the third quarter of 2008 compared with 357,000 boepd in the same period of 2007. Production in the first nine months of 2008 was 382,000 boepd compared with 372,000 boepd in the first nine months of 2007. Facilities downtime associated with hurricanes in the Gulf of Mexico reduced third quarter production by an average of approximately 11,000 boepd. Delays from the hurricanes in bringing back the operations of third-party transportation infrastructure will also reduce fourth quarter production. The Corporation anticipates that its production for the full year of 2008 will average approximately 380,000 boepd and that production impacted by the hurricanes will be fully restored by January 2009.

The Corporation's net daily worldwide production by region was as follows (in thousands):

| | Three months ended September 30, | | Nine months ended September 30, | |
|---------------------------------------|-------------------------------------|------|------------------------------------|------|
| | 2008 | 2007 | 2008 | 2007 |
| Crude oil (barrels per day) | | | | |
| United States | 31 | 31 | 34 | 31 |
| Europe | 80 | 83 | 82 | 96 |
| Africa | 121 | 123 | 123 | 112 |
| Asia and other | 12 | 20 | 14 | 20 |
| Total | 244 | 257 | 253 | 259 |
| Natural gas liquids (barrels per day) | | | | |
| United States | 9 | 11 | 10 | 10 |
| Europe | 4 | 3 | 4 | 5 |

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| | | | | |
|---------------------------------------|-----|-----|-----|-----|
| Total | 13 | 14 | 14 | 15 |
| Natural gas (Mcf per day) | | | | |
| United States | 76 | 87 | 84 | 87 |
| Europe | 216 | 188 | 260 | 249 |
| Asia and other | 333 | 241 | 346 | 254 |
| Total | 625 | 516 | 690 | 590 |
| Barrels of oil equivalent per day (*) | | | | |
| | 361 | 357 | 382 | 372 |

(*) Natural gas production is converted assuming six Mcf equals one barrel.

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Results of Operations (continued)**

United States: Crude oil production in the United States was higher in the first nine months of 2008, principally due to production from new wells in North Dakota and the deepwater Gulf of Mexico. In the third quarter of 2008, this increased production was offset by the impacts of hurricanes in the Gulf of Mexico.

Europe: Crude oil production in Europe in the third quarter and first nine months of 2008 was lower than the comparable periods of 2007, due to temporary shut-ins at two North Sea fields, cessation of production at the Fife Field and natural decline. These decreases were partially offset by increased production in Russia. Natural gas production in the third quarter and first nine months of 2008 was higher than in the same periods of 2007, principally reflecting increased production from the Cromarty Field in the United Kingdom, which was shut-in for a portion of 2007 in response to market conditions, partially offset by natural decline. In addition, third quarter 2008 natural gas nominations at certain fields were higher because a third-party pipeline was shut down in the third quarter of 2007.

Africa: Higher crude oil production in the first nine months of 2008 was principally due to the continued development of the Okume Complex in Equatorial Guinea, partially offset by a lower entitlement to Algerian production.

Asia and other: Crude oil production in Asia was lower in the third quarter and first nine months of 2008, reflecting a reduced entitlement to production in Azerbaijan and production interruptions. Natural gas production increased in the third quarter of 2008 principally due to increased production from Block A-18 of the Joint Development Area of Malaysia and Thailand (JDA). In the third quarter of 2007, operations at Block A-18 of the JDA were impacted by a planned shut-down in order to install facilities required for phase 2 gas sales. In the first nine months of 2008 production also increased as a result of production from the Pangkah Field in Indonesia, which commenced in April 2007.

Sales volumes: Higher crude oil sales volumes increased revenue by approximately \$50 million in the third quarter and \$260 million in the first nine months of 2008 compared with the corresponding periods of 2007.

Operating costs and depreciation, depletion and amortization: Cash operating costs, consisting of production expenses and general and administrative expenses, increased by \$129 million and \$340 million in the third quarter and first nine months of 2008, respectively, compared with the corresponding periods of 2007. The increases principally reflect higher production volumes, increased production taxes (due to higher realized selling prices), higher costs of services and materials and increased employee related costs. Depreciation, depletion and amortization charges were higher in 2008 reflecting higher production volumes and per barrel rates.

Exploration expenses: Exploration expenses were higher in the third quarter and first nine months of 2008 compared with the corresponding periods of 2007, reflecting higher dry hole costs and increased costs of seismic studies.

Income Taxes: The effective income tax rate for Exploration and Production operations in the first nine months of 2008 was 48% compared with 50% in the first nine months of 2007. The effective income tax rate for Exploration and Production operations for the full year of 2008 is expected to be in the range of 47% to 51%.

Other: The after-tax foreign currency loss related to Exploration and Production activities was \$8 million in the third quarter of 2008 compared with income of \$1 million in the third quarter of 2007. The after-tax foreign currency gain was \$3 million for the nine months ended September 30, 2008 and a loss of \$8 million for the nine months ended September 30, 2007.

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Results of Operations (continued)**

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

Marketing and Refining

Marketing and Refining income amounted to \$161 million and \$125 million in the third quarter and first nine months of 2008, respectively, compared with \$46 million and \$269 million in the third quarter and first nine months of 2007. The Corporation's downstream operations include HOVENSA L.L.C. (HOVENSA), a 50% owned refining joint venture with a subsidiary of Petroleos de Venezuela S.A. (PDVSA), which is accounted for using the equity method. Additional Marketing and Refining activities include a fluid catalytic cracking facility in Port Reading, New Jersey, as well as retail gasoline stations, energy marketing and trading operations.

Refining: Refining operations generated income of \$46 million in the third quarter and first nine months of 2008 compared with income of \$25 million in the third quarter and \$166 million in the first nine months of 2007. The Corporation's share of HOVENSA's income, after income taxes, was \$32 million in the third quarter of 2008 compared with \$12 million in the third quarter of 2007. The Corporation's share of HOVENSA's income, after income taxes, was \$14 million in the first nine months of 2008 compared with \$96 million in 2007, principally reflecting lower refining margins.

At September 30, 2008, the remaining balance of the PDVSA note was \$30 million, which is scheduled to be fully repaid by February 2009. Interest income on the PDVSA note, after income taxes, was \$2 million in the first nine months of 2008 compared with \$5 million in the first nine months of 2007, reflecting a lower outstanding balance.

Port Reading's after tax earnings were \$14 million and \$30 million in the third quarter and first nine months of 2008, respectively, compared with \$10 million and \$62 million in the corresponding periods of 2007, also reflecting lower margins.

The following table summarizes refinery capacity and utilization rates:

| | Refinery capacity (thousands of barrels per day) | Refinery utilization | | | |
|-------------------------|---|-------------------------------------|-------|------------------------------------|-------|
| | | Three months ended September 30, | | Nine months ended September 30, | |
| | | 2008 | 2007 | 2008 | 2007 |
| HOVENSA | | | | | |
| Crude | 500 | 91.3% | 91.9% | 91.5% | 88.4% |
| Fluid catalytic cracker | 150 | 72.8% | 82.4% | 73.4% | 87.8% |
| Coker | 58 | 105.4% | 92.6% | 98.8% | 78.1% |
| Port Reading | 70* | 92.4% | 93.8% | 90.3% | 92.2% |

* Refinery utilization in 2007 is based on a capacity of 65,000 barrels per day.

Marketing: Marketing operations, which consist principally of energy marketing and retail gasoline operations, generated earnings of \$110 million in the third quarter of 2008 compared with \$21 million in the third quarter of 2007. The increase was primarily due to increased margins in retail gasoline operations and energy marketing activities. Marketing operations had earnings of \$102 million in the first nine months of 2008 compared with earnings of \$64 million in the first nine months of 2007. Total refined product sales volumes were 470,000 barrels per day in the

first nine months of 2008 compared with 447,000 barrels per day in the first nine months of 2007.

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Results of Operations (continued)**

Trading: 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 results from the trading partnership, amounted to earnings of \$5 million in the third quarter and a loss of \$23 million in the first nine months of 2008 compared with breakeven results in the third quarter of 2007 and income of \$39 million in the first nine months of 2007.

Marketing expenses increased in the third quarter and first nine months of 2008 compared with the corresponding periods of 2007, 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 volatility in marketing and refining margins, competitive industry conditions, government regulatory changes, credit risk and supply and demand factors, including the effects of weather.

Corporate

After-tax corporate expenses were \$42 million in the third quarter of 2008 compared with \$28 million in the third quarter of 2007. After-tax corporate expenses were \$114 million in the first nine months of 2008 compared with \$91 million in the first nine months of 2007. The increases principally reflect higher employee related expenses, losses on pension related investments and higher professional fees.

Interest

Interest expense was as follows (in millions):

| | Three months ended September 30, | | Nine months ended September 30, | |
|--------------------------------------|-------------------------------------|-------|------------------------------------|--------|
| | 2008 | 2007 | 2008 | 2007 |
| Total interest incurred | \$ 70 | \$ 77 | \$ 204 | \$ 234 |
| Less: capitalized interest | 2 | 18 | 4 | 49 |
| Interest expense before income taxes | 68 | 59 | 200 | 185 |
| Less: income taxes | 25 | 22 | 75 | 70 |
| After-tax interest expense | \$ 43 | \$ 37 | \$ 125 | \$ 115 |

The decrease in interest incurred in the first nine months of 2008 principally reflects lower average debt. The decrease in capitalized interest in 2008 reflects the completion of several development projects in 2007.

Sales and Other Operating Revenues

Sales and other operating revenues increased by 53% in the third quarter and 52% in the first nine months of 2008 compared with the corresponding periods of 2007, primarily due to higher crude oil and refined product selling prices and increased sales of electricity. The increase in cost of goods sold principally reflects higher refined product costs and increased purchases of electricity.

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Liquidity and Capital Resources**

The following table sets forth certain relevant measures of the Corporation's liquidity and capital resources (in millions, except ratios):

| | September 30, 2008 | December 31, 2007 |
|-----------------------------------|--------------------------|-------------------------|
| Cash and cash equivalents | \$ 1,380 | \$ 607 |
| Current portion of long-term debt | 39 | 62 |
| Total debt | 3,932 | 3,980 |
| Stockholders' equity | 12,231 | 9,774 |
| Debt to capitalization ratio(*) | 24.3% | 28.9% |

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

Cash Flows

The following table sets forth a summary of the Corporation's cash flows (in millions):

| | Nine months ended September 30, | |
|---|------------------------------------|----------|
| | 2008 | 2007 |
| Net cash provided by (used in): | | |
| Operating activities | \$ 4,072 | \$ 2,701 |
| Investing activities | (3,232) | (2,686) |
| Financing activities | (67) | 167 |
| Net increase in cash and cash equivalents | \$ 773 | \$ 182 |

Operating Activities: Net cash provided by operating activities, including changes in operating assets and liabilities, amounted to \$4,072 million in the first nine months of 2008 compared with \$2,701 million in 2007, reflecting increased earnings. In the first nine months of 2008, the Corporation received cash distributions of \$50 million from HOVENSA compared with \$200 million in 2007.

Investing Activities: The following table summarizes the Corporation's capital expenditures (in millions):

| | Nine months ended September 30, | |
|-----------------------------------|------------------------------------|----------|
| | 2008 | 2007 |
| Exploration and Production | \$ 3,185 | \$ 2,679 |
| Marketing, Refining and Corporate | 97 | 94 |
| Total | \$ 3,282 | \$ 2,773 |

Financing Activities: In the first nine months of 2008, there was a net decrease in borrowings of \$48 million from year-end 2007. Dividends paid were \$130 million in the first nine months of 2008 (\$127 million in the first nine

months of 2007). During the first nine months of 2008, the Corporation received proceeds from the exercise of stock options totaling \$111 million (\$81 million in the same period of 2007).

Future Capital Requirements and Resources

The Corporation anticipates investing a total of approximately \$5 billion in capital and exploratory expenditures during 2008. The Corporation expects that it will fund its 2008 operations, including capital expenditures, dividends, pension contributions and required debt repayments, with existing cash on-hand, cash flow from operations and its available credit facilities.

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Liquidity and Capital Resources (continued)**

Commodity prices have decreased considerably subsequent to September 30, 2008. Such decreases will have an impact on the Corporation's future revenues, earnings and cash flows. As a result, the Corporation will make an appropriate reduction to its 2009 capital and exploratory expenditures.

At September 30, 2008, the Corporation has \$2,683 million of available borrowing capacity under its \$3 billion syndicated revolving credit facility (the Revolver), substantially all of which is committed through May 2012. Outstanding borrowings under the Revolver were \$317 million at September 30, 2008 compared with \$220 million at December 31, 2007. In addition, at September 30, 2008, the Corporation had \$315 million in outstanding borrowings and \$534 million of outstanding letters of credit under its 364-day asset-backed credit facility (the Asset-backed Facility) compared with \$250 million and \$534 million, respectively, at December 31, 2007. The borrowings and outstanding letters of credit under the Asset-backed Facility were collateralized by approximately \$1,200 million of Marketing and Refining accounts receivable. These receivables are not available to pay the general obligations of the Corporation before satisfaction of the Corporation's obligations under the Asset-backed Facility. At September 30, 2008, the Corporation classified an aggregate of \$515 million of borrowings under short-term credit facilities and the Asset-backed Facility as long-term debt, based on the available capacity under the Revolver. In October 2008, the Corporation renewed its Asset-backed Facility for an additional 364 days with a total capacity of \$500 million, subject to available accounts receivable.

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

Outstanding letters of credit were as follows (in millions):

| | September 30, 2008 | December 31, 2007 |
|---------------------------------------|--------------------------|-------------------------|
| Revolving credit facility | \$ | \$ |
| Asset backed credit facility | 534 | 534 |
| Committed letter of credit facilities | 1,982 | 995 |
| Uncommitted facilities | 1,277 | 1,510 |
| | \$ 3,793 | \$ 3,039 |

A loan agreement covenant based on the Corporation's debt to equity ratio allows the Corporation to borrow up to an additional \$16.5 billion for the construction or acquisition of assets at September 30, 2008. The Corporation has the ability to borrow up to an additional \$3.1 billion of secured debt at September 30, 2008 under the loan agreement covenants.

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 September 30, 2008. The Corporation's September 30, 2008 debt to capitalization ratio would increase from 24.3% to 26.6% if the leases were included as debt.

The Corporation guarantees the payment of up to 50% of HOVENSA's crude oil purchases from suppliers other than PDVSA. At September 30, 2008, the guarantee amounted to \$342 million. This amount fluctuates based on the volume of crude oil purchased and related prices. 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.

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Change in Accounting Policies**

Effective January 1, 2008, the Corporation adopted Financial Accounting Standards Board (FASB) Statement No. 157, *Fair Value Measurements* (FAS 157) for financial assets and liabilities that are required to be measured at fair value. FAS 157 established a framework for measuring fair value and requires disclosure of a fair value hierarchy (see Note 8, *Fair Value Measurements*). 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 approximately \$190 million, after income taxes.

Recently Issued Accounting Standard

In December 2007, the FASB issued FAS No. 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 is currently evaluating the impact of adoption on its financial statements and, as required, will adopt the provisions of FAS 160 effective January 1, 2009.

Market Risk Disclosures

In the normal course of its business, the Corporation is exposed to commodity risks related to changes in the prices 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 trading partnership. These activities are also exposed to commodity risks primarily related to the prices of crude oil, natural gas and refined products.

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. Generally, these contracts are widely traded instruments with standardized terms.

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 pre-tax loss in fair value over one day at a 95% confidence level. The model captures both first and second order sensitivities for options. The potential change in fair value based on commodity price risk is presented in the non-trading and trading sections below.

Non-Trading: The Corporation's Exploration and Production segment uses futures and swaps to fix the selling prices of a portion of its future production and the related gains or losses are a component of its selling prices. Following is a summary of the Corporation's outstanding Brent crude oil hedges at September 30, 2008:

| | Average Selling Price | Thousands of Barrels per Day |
|------------|-----------------------------|------------------------------------|
| Maturities | | |
| 2008 | \$25.56 | 24 |
| 2009 | 25.54 | 24 |
| 2010 | 25.78 | 24 |
| 2011 | 26.37 | 24 |
| 2012 | 26.90 | 24 |

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Market Risk Disclosures (continued)**

Accumulated other comprehensive income (loss) at September 30, 2008 included net after-tax unrealized deferred losses of \$1,729 million related to crude oil contracts used as hedges of future Exploration and Production sales and derivatives used to manage risk in its Marketing activities. The pre-tax amount of any deferred hedge losses and gains is reflected in accounts payable and accounts receivable, respectively, and the related income tax impact is recorded as deferred income taxes on the balance sheet. The Corporation estimates that at September 30, 2008, the value-at-risk for commodity related derivatives used in non-trading activities was \$139 million compared with \$72 million at December 31, 2007.

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 fourth quarter 2008 hedges were not affected by these transactions and are still open. The deferred after-tax loss as of the date the hedge positions were closed will be recorded in earnings as the contracts mature. As a result of entering into the offsetting contracts, the value-at-risk for commodity related derivatives used in non-trading activities as of September 30, 2008 would have been reduced to approximately \$20 million.

Trading: In trading activities, the Corporation is 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 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.

Total net realized losses for the first nine months of 2008 amounted to \$97 million (\$358 million of realized gains for the first nine months of 2007). The following table provides an assessment of the factors affecting the changes in fair value of trading activities (in millions):

| | 2008 | 2007 |
|--|--------|--------|
| Fair value of contracts outstanding at January 1 | \$ 154 | \$ 365 |
| Change in fair value of contracts outstanding at the beginning of the year and still outstanding at September 30 | 141 | (69) |
| Reversal of fair value for contracts closed during the period | 49 | (133) |
| Fair value of contracts entered into during the period and still outstanding | (60) | (37) |
| Fair value of contracts outstanding at September 30 | \$ 284 | \$ 126 |

The Corporation uses observable market values for determining the fair value of its trading instruments. In cases where actively quoted prices are not available, other external sources are used which incorporate information about commodity prices in actively quoted markets, quoted prices in less active markets and other market fundamental analysis. Internal estimates are based on internal models incorporating underlying market information such as commodity volatilities and correlations. The Corporation's risk management department regularly compares valuations to independent sources and models. The following table summarizes the sources of fair values of derivatives used in the Corporation's trading activities at September 30, 2008 (in millions):

Table of Contents**PART I FINANCIAL INFORMATION (CONT. D.)****Market Risk Disclosures (continued)**

| | Total | Instruments Maturing | | | 2011 and beyond |
|------------------------|--------|----------------------|--------|--------|-----------------------|
| | | 2008 | 2009 | 2010 | |
| Source of Fair Value | | | | | |
| Prices actively quoted | \$ 216 | \$ (239) | \$ 207 | \$ 222 | \$ 26 |
| Other external sources | 64 | 73 | (9) | | |
| Internal estimates | 4 | 4 | | | |
| Total | \$ 284 | \$ (162) | \$ 198 | \$ 222 | \$ 26 |

The Corporation estimates that at September 30, 2008, the value-at-risk for trading activities, including commodities, was \$12 million compared with \$10 million at December 31, 2007. The value-at-risk for trading activities may vary from time to time as strategies change to capture potential market rate movements and market conditions change.

The following table summarizes the fair values of net receivables relating to the Corporation's trading activities and the credit ratings of counterparties at September 30, 2008 (in millions):

| | |
|--|--------|
| Investment grade determined by outside sources | \$ 289 |
| Investment grade determined internally (*) | 155 |
| Less than investment grade | 107 |
| Fair value of net receivables outstanding at end of period | \$ 551 |

(*) Based on information provided by counterparties and other available sources.

Forward-Looking Information

Certain sections of Management's Discussion and Analysis of Results of Operations and Financial Condition, 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 and market risk disclosures and off-balance sheet arrangements 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.

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PART I FINANCIAL INFORMATION (CONT. D.)

Item 3. Quantitative and Qualitative Disclosures about Market Risk

The information required by this item is presented under Item 2, Management's Discussion and Analysis of Results of Operations and Financial Condition - Market Risk Disclosure.

Item 4. Controls and Procedures

Based upon their evaluation of the Corporation's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of September 30, 2008, John B. Hess, Chief Executive Officer, and John P. Rielly, Chief Financial Officer, concluded that these disclosure controls and procedures were effective as of September 30, 2008.

There was no change in internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rules 13a-15 or 15d-15 in the quarter ended September 30, 2008 that has materially affected, or is reasonably likely to materially affect, internal control over financial reporting.

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PART II OTHER INFORMATION

Item 1. 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. Various state and local government entities and water authorities filed a series of similar lawsuits in jurisdictions across the United States against producers of MTBE and petroleum refiners who produce gasoline containing MTBE, including the Registrant. These cases have been consolidated for pre-trial proceedings in the Southern District of New York. In the fourth quarter of 2007, the Registrant recorded a pre-tax charge of \$40 million related to the Registrant's MTBE litigation. In October 2008, 31 of these cases have been settled and dismissed, but the Registrant remains a defendant in over 20 cases. The principal allegation in all cases is that gasoline containing MTBE is a defective product and that defendants are strictly liable for damage to groundwater resources. The plaintiffs seek substantial compensatory and punitive damages in addition to injunctive relief.

Item 6. Exhibits and Reports on Form 8-K

a. **Exhibits**

31(1) Certification required by Rule 13a-14(a) (17 CFR 240.13a-14(a)) or Rule 15d-14(a) (17 CFR 240.15d-14(a))

31(2) Certification required by Rule 13a-14(a) (17 CFR 240.13a-14(a)) or Rule 15d-14(a) (17 CFR 240.15d-14(a))

32(1) Certification required by Rule 13a-14(b) (17 CFR 240.13a-14(b)) or Rule 15d-14(b) (17 CFR 240.15d-14(b)) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350)

32(2) Certification required by Rule 13a-14(b) (17 CFR 240.13a-14(b)) or Rule 15d-14(b) (17 CFR 240.15d-14(b)) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350)

b. **Reports on Form 8-K**

During the quarter ended September 30, 2008, Registrant filed one report on Form 8-K:

(i) Filing dated July 30, 2008 reporting under Items 2.02 and 9.01 a news release dated July 30, 2008 reporting results for the second quarter of 2008.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HESS CORPORATION
(REGISTRANT)

By /s/ John B. Hess
JOHN B. HESS
CHAIRMAN OF THE BOARD AND
CHIEF EXECUTIVE OFFICER

By /s/ John P. Rielly
JOHN P. RIELLY
SENIOR VICE PRESIDENT AND
CHIEF FINANCIAL OFFICER

Date: November 6, 2008