

CHEVRON CORP  
Form 10-Q  
November 05, 2010

**Table of Contents**

**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 quarterly period ended September 30, 2010**
- or**
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934**

**Commission file number 001-00368**

**Chevron Corporation**

*(Exact name of registrant as specified in its charter)*

**Delaware**

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

**6001 Bollinger Canyon Road,**

**San Ramon, California**

*(Address of principal executive offices)*

**94-0890210**

*(I.R.S. Employer  
Identification No.)*

**94583-2324**

*(Zip Code)*

**Registrant's telephone number, including area code: (925) 842-1000**

**NONE**

**(Former name, former address and former fiscal year, if changed since last report.)**

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). 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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

<b>Class</b>	<b>Outstanding as of September 30, 2010</b>
Common stock, \$.75 par value	2,012,428,494

---

**INDEX**

	<b>Page No.</b>
<u>Cautionary Statements Relevant to Forward-Looking Information for the Purpose of Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995</u>	2
 <b><u>PART I</u></b> <b><u>FINANCIAL INFORMATION</u></b>	
<u>Item 1. Consolidated Financial Statements</u>	
<u>Consolidated Statement of Income for the Three and Nine Months Ended September 30, 2010, and 2009</u>	3
<u>Consolidated Statement of Comprehensive Income for the Three and Nine Months Ended September 30, 2010, and 2009</u>	4
<u>Consolidated Balance Sheet at September 30, 2010, and December 31, 2009</u>	5
<u>Consolidated Statement of Cash Flows for the Nine Months Ended September 30, 2010, and 2009</u>	6
<u>Notes to Consolidated Financial Statements</u>	7-23
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	24-41
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	41
<u>Item 4. Controls and Procedures</u>	41
 <b><u>PART II</u></b> <b><u>OTHER INFORMATION</u></b>	
<u>Item 1. Legal Proceedings</u>	42-43
<u>Item 1A. Risk Factors</u>	43
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	44
<u>Item 5. Other Information</u>	45
<u>Item 6. Exhibits</u>	46
<u>Signature</u>	47
<u>Exhibits: Computation of Ratio of Earnings to Fixed Charges</u>	49
<u>Rule 13a-14(a)/15d-14(a) Certifications</u>	50-51
<u>Section 1350 Certifications</u>	52-53
<u>EX-12.1</u>	
<u>EX-31.1</u>	
<u>EX-31.2</u>	
<u>EX-32.1</u>	
<u>EX-32.2</u>	
<u>EX-101 INSTANCE DOCUMENT</u>	
<u>EX-101 SCHEMA DOCUMENT</u>	
<u>EX-101 CALCULATION LINKBASE DOCUMENT</u>	
<u>EX-101 LABELS LINKBASE DOCUMENT</u>	
<u>EX-101 PRESENTATION LINKBASE DOCUMENT</u>	
<u>EX-101 DEFINITION LINKBASE DOCUMENT</u>	

**Table of Contents**

**CAUTIONARY STATEMENT RELEVANT TO FORWARD-LOOKING INFORMATION  
FOR THE PURPOSE OF SAFE HARBOR PROVISIONS OF THE  
PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995**

This quarterly report on Form 10-Q of Chevron Corporation contains forward-looking statements relating to Chevron's operations that are based on management's current expectations, estimates and projections about the petroleum, chemicals and other energy-related industries. Words such as anticipates, expects, intends, plans, targets, projects, believes, seeks, schedules, estimates, budgets and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and are subject to certain risks, uncertainties and other factors, some of which are beyond the company's control and are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. The reader should not place undue reliance on these forward-looking statements, which speak only as of the date of this report. Unless legally required, Chevron undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

Among the important factors that could cause actual results to differ materially from those in the forward-looking statements are: changing crude oil and natural gas prices; changing refining, marketing and chemical margins; actions of competitors or regulators; timing of exploration expenses; timing of crude oil liftings; the competitiveness of alternate-energy sources or product substitutes; technological developments; the results of operations and financial condition of equity affiliates; the inability or failure of the company's joint-venture partners to fund their share of operations and development activities; the potential failure to achieve expected net production from existing and future crude oil and natural gas development projects; potential delays in the development, construction or start-up of planned projects; the potential disruption or interruption of the company's net production or manufacturing facilities or delivery/transportation networks due to war, accidents, political events, civil unrest, severe weather or crude oil production quotas that might be imposed by the Organization of Petroleum Exporting Countries; the potential liability for remedial actions or assessments under existing or future environmental regulations and litigation; significant investment or product changes under existing or future environmental statutes, regulations and litigation; the potential liability resulting from other pending or future litigation; the company's future acquisition or disposition of assets and gains and losses from asset dispositions or impairments; government-mandated sales, divestitures, recapitalizations, industry-specific taxes, changes in fiscal terms or restrictions on scope of company operations; foreign currency movements compared with the U.S. dollar; the effects of changed accounting rules under generally accepted accounting principles promulgated by rule-setting bodies; and the factors set forth under the heading "Risk Factors" on pages 30 through 32 of the company's 2009 Annual Report on Form 10-K. In addition, such statements could be affected by general domestic and international economic and political conditions. Unpredictable or unknown factors not discussed in this report could also have material adverse effects on forward-looking statements.

Table of Contents**PART I.****FINANCIAL INFORMATION****Item 1. Consolidated Financial Statements****CHEVRON CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF INCOME  
(Unaudited)**

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars, except per-share amounts)</b>			
<b>Revenues and Other Income</b>				
Sales and other operating revenues*	\$ 48,554	\$ 45,180	\$ 146,346	\$ 119,814
Income from equity affiliates	1,242	1,072	4,127	2,418
Other (loss) income	(78)	373	428	728
<b>Total Revenues and Other Income</b>	<b>49,718</b>	<b>46,625</b>	<b>150,901</b>	<b>122,960</b>
<b>Costs and Other Deductions</b>				
Purchased crude oil and products	28,610	26,969	86,358	71,047
Operating expenses	4,665	4,403	13,845	12,958
Selling, general and administrative expenses	1,181	1,177	3,359	3,197
Exploration expenses	420	242	812	1,061
Depreciation, depletion and amortization	3,401	2,988	9,624	8,954
Taxes other than on income*	4,559	4,644	13,568	13,008
Interest and debt expense	9	14	46	28
<b>Total Costs and Other Deductions</b>	<b>42,845</b>	<b>40,437</b>	<b>127,612</b>	<b>110,253</b>
<b>Income Before Income Tax Expense</b>	<b>6,873</b>	<b>6,188</b>	<b>23,289</b>	<b>12,707</b>
<b>Income Tax Expense</b>	<b>3,081</b>	<b>2,342</b>	<b>9,473</b>	<b>5,246</b>
<b>Net Income</b>	<b>3,792</b>	<b>3,846</b>	<b>13,816</b>	<b>7,461</b>
Less: Net income attributable to noncontrolling interests	24	15	87	48
<b>Net Income Attributable to Chevron Corporation</b>	<b>\$ 3,768</b>	<b>\$ 3,831</b>	<b>\$ 13,729</b>	<b>\$ 7,413</b>
<b>Per Share of Common Stock:</b>				
<b>Net Income Attributable to Chevron Corporation</b>				
Basic	\$ 1.89	\$ 1.92	\$ 6.88	\$ 3.72

Edgar Filing: CHEVRON CORP - Form 10-Q

<b>Diluted</b>	\$	<b>1.87</b>	\$	1.92	\$	<b>6.84</b>	\$	3.71
<b>Dividends</b>	\$	<b>0.72</b>	\$	0.68	\$	<b>2.12</b>	\$	1.98
<b>Weighted Average Number of Shares Outstanding</b>								
<b>(000s)</b>								
<b>Basic</b>		<b>1,997,721</b>		1,992,452		<b>1,996,376</b>		1,991,733
<b>Diluted</b>		<b>2,006,785</b>		2,000,586		<b>2,005,677</b>		1,999,925
* Includes excise, value-added and similar taxes:	\$	<b>2,182</b>	\$	2,079	\$	<b>6,455</b>	\$	6,023

See accompanying notes to consolidated financial statements.

Table of Contents**CHEVRON CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME  
(Unaudited)**

	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
	(Millions of dollars)			
<b>Net Income</b>	<b>\$3,792</b>	\$3,846	<b>\$13,816</b>	\$7,461
Currency translation adjustment	46	31	33	44
Unrealized holding loss on securities:				
Net gain (loss) arising during period	3	8	(1)	3
Derivatives:				
Net derivatives gain (loss) on hedge transactions	43	7	67	(65)
Reclassification to net income of net realized loss (gain)	4	(9)	7	(25)
Income taxes on derivatives transactions	(16)	1	(26)	31
Total	31	(1)	48	(59)
Defined benefit plans:				
Actuarial loss:				
Amortization to net income of net actuarial loss	165	136	497	451
Prior service cost:				
Amortization to net income of net prior service credits	(15)	(15)	(45)	(49)
Defined benefit plans sponsored by equity affiliates	8	5	22	10
Income taxes on defined benefit plans	(52)	(45)	(173)	(152)
Total	106	81	301	260
<b>Other Comprehensive Gain, Net of Tax</b>	<b>186</b>	119	<b>381</b>	248
<b>Comprehensive Income</b>	<b>3,978</b>	3,965	<b>14,197</b>	7,709
Comprehensive income attributable to noncontrolling interests	(24)	(15)	(87)	(48)
<b>Comprehensive Income Attributable to Chevron Corporation</b>	<b>\$3,954</b>	\$3,950	<b>\$14,110</b>	\$7,661

See accompanying notes to consolidated financial statements.





**Table of Contents****CHEVRON CORPORATION AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEET****(Unaudited)**

	<b>At September 30 2010</b>	<b>At December 31 2009</b>
	<b>(Millions of dollars, except per-share amounts)</b>	
<b>ASSETS</b>		
Cash and cash equivalents	\$ 10,995	\$ 8,716
Time deposits	3,473	
Marketable securities	66	106
Accounts and notes receivable, net	17,994	17,703
Inventories:		
Crude oil and petroleum products	4,147	3,680
Chemicals	436	383
Materials, supplies and other	1,554	1,466
Total inventories	6,137	5,529
Prepaid expenses and other current assets	5,818	5,162
<b>Total Current Assets</b>	<b>44,483</b>	<b>37,216</b>
Long-term receivables, net	2,147	2,282
Investments and advances	21,764	21,158
Properties, plant and equipment, at cost	202,108	188,288
Less: Accumulated depreciation, depletion and amortization	100,376	91,820
Properties, plant and equipment, net	101,732	96,468
Deferred charges and other assets	2,455	2,879
Goodwill	4,618	4,618
<b>Total Assets</b>	<b>\$177,199</b>	<b>\$164,621</b>
<b>LIABILITIES AND EQUITY</b>		
Short-term debt	\$ 170	\$ 384
Accounts payable	17,237	16,437
Accrued liabilities	5,405	5,375
Federal and other taxes on income	2,588	2,624
Other taxes payable	1,450	1,391
<b>Total Current Liabilities</b>	<b>26,850</b>	<b>26,211</b>
Long-term debt	10,143	9,829
Capital lease obligations	306	301
Deferred credits and other noncurrent obligations	18,409	17,390
Noncurrent deferred income taxes	12,204	11,521

Edgar Filing: CHEVRON CORP - Form 10-Q

Reserves for employee benefit plans	<b>6,322</b>	6,808
<b>Total Liabilities</b>	<b>74,234</b>	72,060
Preferred stock (authorized 100,000,000 shares, \$1.00 par value, none issued)		
Common stock (authorized 6,000,000,000 shares, \$.75 par value, 2,442,676,580 shares issued at September 30, 2010, and December 31, 2009)	<b>1,832</b>	1,832
Capital in excess of par value	<b>14,767</b>	14,631
Retained earnings	<b>115,784</b>	106,289
Accumulated other comprehensive loss	<b>(3,940)</b>	(4,321)
Deferred compensation and benefit plan trust	<b>(312)</b>	(349)
Treasury stock, at cost (430,248,086 and 434,954,774 shares at September 30, 2010, and December 31, 2009, respectively)	<b>(25,888)</b>	(26,168)
<b>Total Chevron Corporation Stockholders Equity</b>	<b>102,243</b>	91,914
Noncontrolling interests	<b>722</b>	647
<b>Total Equity</b>	<b>102,965</b>	92,561
<b>Total Liabilities and Equity</b>	<b>\$177,199</b>	\$164,621

See accompanying notes to consolidated financial statements.

**Table of Contents**

**CHEVRON CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**  
**(Unaudited)**

	<b>Nine Months Ended</b>	
	<b>September 30</b>	
	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>	
<b>Operating Activities</b>		
Net Income	\$ 13,816	\$ 7,461
Adjustments		
Depreciation, depletion and amortization	9,624	8,954
Dry hole expense	381	481
Distributions less than income from equity affiliates	(153)	(510)
Net before-tax gains on asset retirements and sales	(359)	(1,083)
Net foreign currency effects	203	481
Deferred income tax provision	(60)	335
Net increase in operating working capital	(132)	(2,993)
Increase in long-term receivables	(47)	(288)
Decrease in other deferred charges	48	131
Cash contributions to employee pension plans	(895)	(860)
Other	676	244
<b>Net Cash Provided by Operating Activities</b>	<b>23,102</b>	<b>12,353</b>
<b>Investing Activities</b>		
Capital expenditures	(14,108)	(14,488)
Proceeds and deposits related to asset sales	543	2,132
Net purchases of time deposits	(3,473)	
Net sales of marketable securities	41	113
Repayment of loans by equity affiliates	169	167
Net (purchases) sales of other short-term investments	(63)	153
<b>Net Cash Used for Investing Activities</b>	<b>(16,891)</b>	<b>(11,923)</b>
<b>Financing Activities</b>		
Net payments of short-term obligations	(169)	(3,258)
Proceeds from issuance of long-term debt	350	5,339
Repayments of long-term debt and other financing obligations	(107)	(461)
Cash dividends	(4,233)	(3,945)
Distributions to noncontrolling interests	(56)	(37)
Net sales of treasury shares	245	86
<b>Net Cash Used for Financing Activities</b>	<b>(3,970)</b>	<b>(2,276)</b>
<b>Effect of Exchange Rate Changes on Cash and Cash Equivalents</b>	<b>38</b>	<b>67</b>

<b>Net Change in Cash and Cash Equivalents</b>	<b>2,279</b>	<b>(1,779)</b>
<b>Cash and Cash Equivalents at January 1</b>	<b>8,716</b>	<b>9,347</b>
<b>Cash and Cash Equivalents at September 30</b>	<b>\$ 10,995</b>	<b>\$ 7,568</b>

See accompanying notes to consolidated financial statements.

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****Note 1. Interim Financial Statements**

The accompanying consolidated financial statements of Chevron Corporation and its subsidiaries (the company) have not been audited by an independent registered public accounting firm. In the opinion of the company's management, the interim data include all adjustments necessary for a fair statement of the results for the interim periods. These adjustments were of a normal recurring nature. The results for the three- and nine-month periods ended September 30, 2010, are not necessarily indicative of future financial results. The term "earnings" is defined as net income attributable to Chevron Corporation.

Effective January 1, 2010, Chevron's segment reporting reflects the reclassification of certain businesses. Prior period information was revised to conform to the 2010 presentation. Refer to Note 5. Operating Segments and Geographic Data, beginning on page 9, for a discussion of the changes.

Certain notes and other information have been condensed or omitted from the interim financial statements presented in this Quarterly Report on Form 10-Q. Therefore, these financial statements should be read in conjunction with the company's 2009 Annual Report on Form 10-K.

Earnings for the first nine months of 2010 included after-tax charges of \$175 million associated with employee reductions in the downstream businesses and corporate staffs. Refer to Note 16. Restructuring and Reorganization Costs, beginning on page 22, for further discussion.

Earnings for the third quarter 2009 included \$400 million of after-tax gains from asset sales and tax items related to an upstream project in Australia. Earnings for the first nine months of 2009 also included \$540 million of after-tax gains reported on sales of marketing businesses outside the United States.

**Note 2. Time Deposits**

In the first quarter 2010, the company began investing in bank time deposits with maturities greater than 90 days. The company believes that the investment in longer-term bank time deposits is consistent with its cash management strategy to preserve principal, maintain high levels of liquidity and earn a competitive return.

**Note 3. Noncontrolling Interests**

Ownership interests in the company's subsidiaries held by parties other than the parent are presented separately from the parent's equity on the Consolidated Balance Sheet. The amounts of consolidated net income attributable to the parent and the noncontrolling interests are both presented on the face of the Consolidated Statement of Income. Activity for the equity attributable to noncontrolling interests for the first nine months of 2010 and 2009 is presented in the following table:

2010			2009		
Chevron Corporation Stockholders Equity	Noncontrolling Interest	Total Equity	Chevron Corporation Stockholders Equity	Noncontrolling Interest	Total Equity
(Millions of dollars)					

Edgar Filing: CHEVRON CORP - Form 10-Q

Balance at January 1	<b>\$ 91,914</b>	<b>\$647</b>	<b>\$ 92,561</b>	\$86,648	\$469	\$87,117
Net income	<b>13,729</b>	<b>87</b>	<b>13,816</b>	7,413	48	7,461
Dividends	<b>(4,233)</b>		<b>(4,233)</b>	(3,945)		(3,945)
Distributions to noncontrolling interests		<b>(56)</b>	<b>(56)</b>		(37)	(37)
Treasury shares, net	<b>280</b>		<b>280</b>	121		121
Other changes, net*	<b>553</b>	<b>44</b>	<b>597</b>	409	96	505
Balance at September 30	<b>\$102,243</b>	<b>\$722</b>	<b>\$102,965</b>	\$90,646	\$576	\$91,222

\* Includes components of comprehensive income, which are disclosed separately in the Consolidated Statement of Comprehensive Income.

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Note 4. Information Relating to the Consolidated Statement of Cash Flows**

The Net increase in operating working capital was composed of the following operating changes:

	<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>	
Increase in accounts and notes receivable	<b>\$ (13)</b>	<b>\$ (877)</b>
(Increase) decrease in inventories	<b>(608)</b>	<b>356</b>
Increase in prepaid expenses and other current assets	<b>(646)</b>	<b>(216)</b>
Increase (decrease) in accounts payable and accrued liabilities	<b>718</b>	<b>(1,597)</b>
Increase (decrease) in income and other taxes payable	<b>417</b>	<b>(659)</b>
Net increase in operating working capital	<b>\$(132)</b>	<b>\$(2,993)</b>

The Net increase in operating working capital includes reductions of \$37 million and \$11 million for excess income tax benefits associated with stock options exercised during the nine months ended September 30, 2010, and 2009, respectively. These amounts are offset by an equal amount in Net sales of treasury shares.

Net Cash Provided by Operating Activities included the following cash payments for interest on debt and for income taxes:

	<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>	
Interest on debt (net of capitalized interest)	<b>\$ 92</b>	<b>\$ 11</b>
Income taxes	<b>9,014</b>	<b>4,825</b>

The Net purchases of time deposits consisted of the following gross amounts:

	<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>	
Time deposits purchased	<b>\$(4,868)</b>	<b>\$</b>
Time deposits matured	<b>1,395</b>	<b>\$</b>
Net purchases of time deposits	<b>\$(3,473)</b>	<b>\$</b>



The Net sales of marketable securities consisted of the following gross amounts:

	<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>	
Marketable securities purchased	<b>\$</b>	<b>\$ (24)</b>
Marketable securities sold	<b>41</b>	<b>137</b>
Net sales of marketable securities	<b>\$41</b>	<b>\$113</b>

The Net sales of treasury shares represents the cost of common shares acquired less the cost of shares issued for share-based compensation plans. Net sales totaled \$245 million and \$86 million in the first nine months of 2010 and 2009, respectively. No purchases were made under the company's stock repurchase program in the 2010 and 2009 periods.

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The major components of Capital expenditures and the reconciliation of this amount to the capital and exploratory expenditures, including equity affiliates, are as follows:

	<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>	
Additions to properties, plant and equipment	<b>\$13,242</b>	\$11,542
Additions to investments	<b>617</b>	793
Current year dry hole expenditures	<b>348</b>	399
Payments for other liabilities and assets, net	<b>(99)</b>	1,754
Capital expenditures	<b>14,108</b>	14,488
Expensed exploration expenditures	<b>431</b>	580
Assets acquired through capital lease obligations	<b>56</b>	20
Capital and exploratory expenditures, excluding equity affiliates	<b>14,595</b>	15,088
Company's share of expenditures by equity affiliates	<b>942</b>	923
Capital and exploratory expenditures, including equity affiliates	<b>\$15,537</b>	\$16,011

Payments for other liabilities and assets, net in the 2009 period include \$2 billion for a cash payment related to an accrual recorded in 2008 for the extension of an upstream operating agreement outside the United States.

**Note 5. Operating Segments and Geographic Data**

Although each subsidiary of Chevron is responsible for its own affairs, Chevron Corporation manages its investments in these subsidiaries and their affiliates. The investments are grouped into two business segments, Upstream and Downstream, representing the company's reportable segments and operating segments as defined in accounting standards for segment reporting (ASC 280). Upstream operations consist primarily of exploring for, developing and producing crude oil and natural gas; processing, liquefaction, transportation and regasification associated with liquefied natural gas (LNG); transporting crude oil by major international oil export pipelines; transporting, storage and marketing of natural gas; and a gas-to-liquids project. Downstream operations consist primarily of refining of crude oil into petroleum products; marketing of crude oil and refined products; transporting crude oil and refined products by pipeline, marine vessel, motor equipment and rail car; and manufacturing and marketing of commodity petrochemicals, plastics for industrial uses and fuel and lubricant additives. All Other activities of the company include mining operations, power generation businesses, worldwide cash management and debt financing activities, corporate administrative functions, insurance operations, real estate activities, energy services, alternative fuels and technology.

The segments are separately managed for investment purposes under a structure that includes segment managers who report to the company's chief operating decision maker (CODM) (terms as defined in the accounting standards). The CODM is the company's Executive Committee (EXCOM), a committee of senior officers that includes the Chief Executive Officer, and EXCOM reports to the Board of Directors of Chevron Corporation.

The operating segments represent components of the company as described in the accounting standards that engage in activities (a) from which revenues are earned and expenses are incurred; (b) whose operating results are regularly reviewed by the CODM, which makes decisions about resources to be allocated to the segments and assesses their performance; and (c) for which discrete financial information is available.

Segment managers for the reportable segments are directly accountable to and maintain regular contact with the company's CODM to discuss the segments' operating activities and financial performance. The CODM approves annual capital and exploratory budgets at the reportable segment level, as well as reviews capital and exploratory funding for major projects and approves major changes to the annual capital and exploratory budgets. However, business unit managers within the operating segments are directly responsible for decisions relating to project

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

implementation and all other matters connected with daily operations. Company officers who are members of EXCOM also have individual management responsibilities and participate in other committees for purposes other than acting as the CODM.

The activities reported in Chevron's upstream and downstream operating segments have changed effective January 1, 2010. Chemicals businesses are now reported as part of the downstream segment. In addition, the company's significant upstream-enabling operations, primarily a gas-to-liquids project and major international export pipelines, have been reclassified from the downstream segment to the upstream segment. Prior period information in this report has been revised to conform to the 2010 presentation.

The company's primary country of operation is the United States of America, its country of domicile. Other components of the company's operations are reported as International (outside the United States).

*Segment Earnings* The company evaluates the performance of its operating segments on an after-tax basis, without considering the effects of debt financing interest expense or investment interest income, both of which are managed by the company on a worldwide basis. Corporate administrative costs and assets are not allocated to the operating segments. However, operating segments are billed for the direct use of corporate services. Nonbillable costs remain at the corporate level in All Other. Earnings by major operating area for the three- and nine-month periods ended September 30, 2010 and 2009 are presented in the following table:

**Segment Earnings**

	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>			
<b>Upstream</b>				
United States	\$ 946	\$ 889	\$ 3,192	\$ 1,196
International	2,618	2,847	9,638	5,575
<b>Total Upstream</b>	<b>3,564</b>	<b>3,736</b>	<b>12,830</b>	<b>6,771</b>
<b>Downstream</b>				
United States	349	127	864	212
International	216	135	872	934
<b>Total Downstream</b>	<b>565</b>	<b>262</b>	<b>1,736</b>	<b>1,146</b>
<b>Total Segment Earnings</b>	<b>4,129</b>	<b>3,998</b>	<b>14,566</b>	<b>7,917</b>
<b>All Other</b>				
Interest Expense	(7)	(11)	(37)	(22)
Interest Income	16	10	49	36
Other	(370)	(166)	(849)	(518)

<b>Net Income Attributable to Chevron Corporation</b>	<b>\$ 3,768</b>	\$ 3,831	<b>\$ 13,729</b>	\$ 7,413
---	-----------------	----------	------------------	----------

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Segment Assets* Segment assets do not include intercompany investments or intercompany receivables. All Other assets consist primarily of worldwide cash, cash equivalents, time deposits and marketable securities; real estate; information systems; mining operations; power generation businesses; alternative fuels; technology companies; and assets of the corporate administrative functions. Segment assets at September 30, 2010, and December 31, 2009, are as follows:

**Segment Assets**

	<b>At September 30 2010</b>	<b>At December 31 2009</b>
	<b>(Millions of dollars)</b>	
<b>Upstream</b>		
United States	\$ 25,700	\$ 25,478
International	86,532	81,209
Goodwill	4,617	4,618
<b>Total Upstream</b>	<b>116,849</b>	111,305
<b>Downstream</b>		
United States	20,365	20,317
International	20,376	19,618
<b>Total Downstream</b>	<b>40,741</b>	39,935
<b>Total Segment Assets</b>	<b>157,590</b>	151,240
<b>All Other</b>		
United States	9,620	7,125
International	9,989	6,256
<b>Total All Other</b>	<b>19,609</b>	13,381
<b>Total Assets</b> <b>United States</b>	<b>55,685</b>	52,920
<b>Total Assets</b> <b>International</b>	<b>116,897</b>	107,083
<b>Goodwill</b>	<b>4,617</b>	4,618
<b>Total Assets</b>	<b>\$177,199</b>	\$164,621

*Segment Sales and Other Operating Revenues* Segment sales and other operating revenues, including internal transfers, for the three- and nine-month periods ended September 30, 2010 and 2009, are presented in the following table. Products are transferred between operating segments at internal product values that approximate market prices. Revenues for the upstream segment are derived primarily from the production and sale of crude oil and natural gas, as well as the sale of third-party production of natural gas. Revenues for the downstream segment are derived from the

refining and marketing of petroleum products such as gasoline, jet fuel, gas oils, lubricants, residual fuel oils and other products derived from crude oil. This segment also generates revenues from the manufacture and sale of fuel and lubricant additives and the transportation and trading of refined products and crude oil. All Other activities include revenues from mining operations, power generation businesses, insurance operations, real estate activities and technology companies.

Table of Contents

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Sales and Other Operating Revenues

		Three Months Ended September 30		Nine Months Ended September 30	
		2010	2009	2010	2009
(Millions of dollars)					
<b>Upstream</b>					
United States		\$ 5,892	\$ 4,985	\$ 18,207	\$ 13,657
International		9,984	8,335	29,642	22,297
Subtotal		15,876	13,320	47,849	35,954
Intersegment Elimination	United States	(3,299)	(3,014)	(10,142)	(6,925)
Intersegment Elimination	International	(5,623)	(4,866)	(17,141)	(12,696)
<b>Total Upstream</b>		<b>6,954</b>	<b>5,440</b>	<b>20,566</b>	<b>16,333</b>
<b>Downstream</b>					
United States		18,438	18,025	55,378	44,699
International		23,042	21,557	70,102	58,389
Subtotal		41,480	39,582	125,480	103,088
Intersegment Elimination	United States	(31)	(19)	(80)	(76)
Intersegment Elimination	International	(27)	(25)	(75)	(59)
<b>Total Downstream</b>		<b>41,422</b>	<b>39,538</b>	<b>125,325</b>	<b>102,953</b>
<b>All Other</b>					
United States		413	473	1,088	1,180
International		13	19	46	48
Subtotal		426	492	1,134	1,228
Intersegment Elimination	United States	(239)	(281)	(652)	(679)
Intersegment Elimination	International	(9)	(9)	(27)	(21)
<b>Total All Other</b>		<b>178</b>	<b>202</b>	<b>455</b>	<b>528</b>
<b>Sales and Other Operating Revenues</b>					
United States		24,743	23,483	74,673	59,536
International		33,039	29,911	99,790	80,734
Subtotal		57,782	53,394	174,463	140,270
Intersegment Elimination	United States	(3,569)	(3,314)	(10,874)	(7,680)
Intersegment Elimination	International	(5,659)	(4,900)	(17,243)	(12,776)
<b>Total Sales and Other Operating Revenues</b>		<b>\$48,554</b>	<b>\$45,180</b>	<b>\$146,346</b>	<b>\$119,814</b>





Table of Contents**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Note 6. Summarized Financial Data Chevron U.S.A. Inc.**

Chevron U.S.A. Inc. (CUSA) is a major subsidiary of Chevron Corporation. CUSA and its subsidiaries manage and operate most of Chevron's U.S. businesses. Assets include those related to the exploration and production of crude oil, natural gas and natural gas liquids and those associated with refining, marketing, and supply and distribution of products derived from petroleum, excluding most of the regulated pipeline operations of Chevron. CUSA also holds the company's investment in the Chevron Phillips Chemical Company LLC joint venture, which is accounted for using the equity method. The summarized financial information for CUSA and its consolidated subsidiaries is as follows:

	<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>	
Sales and other operating revenues	<b>\$107,595</b>	\$86,522
Costs and other deductions	<b>103,433</b>	85,461
Net income attributable to CUSA	<b>3,130</b>	852

	<b>At September 30</b>	<b>At December 31</b>
	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>	
Current assets	<b>\$25,546</b>	\$23,286
Other assets	<b>33,653</b>	32,827
Current liabilities	<b>14,952</b>	16,098
Other liabilities	<b>15,681</b>	14,625
Total CUSA net equity	<b>\$28,566</b>	\$25,390
Memo: Total debt	<b>\$ 7,327</b>	\$ 6,999

**Note 7. Summarized Financial Data Chevron Transport Corporation**

Chevron Transport Corporation Limited (CTC), incorporated in Bermuda, is an indirect, wholly owned subsidiary of Chevron Corporation. CTC is the principal operator of Chevron's international tanker fleet and is engaged in the marine transportation of crude oil and refined petroleum products. Most of CTC's shipping revenue is derived by providing transportation services to other Chevron companies. Chevron Corporation has fully and unconditionally guaranteed this subsidiary's obligations in connection with certain debt securities issued by a third party. Summarized financial information for CTC and its consolidated subsidiaries is as follows:

	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>			

Sales and other operating revenues	<b>\$ 200</b>	\$ 153	<b>\$ 694</b>	\$ 492
Costs and other deductions	<b>228</b>	186	<b>755</b>	565
Net loss attributable to CTC	<b>(28)</b>	(34)	<b>(54)</b>	(73)

	<b>At September 30 2010</b>	<b>At December 31 2009</b>
	(Millions of dollars)	
Current assets	<b>\$265</b>	\$377
Other assets	<b>201</b>	173
Current liabilities	<b>96</b>	115
Other liabilities	<b>74</b>	90
Total CTC net equity	<b>\$296</b>	\$345

There were no restrictions on CTC's ability to pay dividends or make loans or advances at September 30, 2010.

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Note 8. Income Taxes**

Taxes on income for the third quarter and first nine months of 2010 were \$3.1 billion and \$9.5 billion, respectively, compared with \$2.3 billion and \$5.2 billion for the corresponding periods in 2009. The associated effective tax rates (calculated as the amount of Income Tax Expense divided by Income Before Income Tax Expense) for the third quarters of 2010 and 2009 were 45 percent and 38 percent, respectively. For the comparative nine-month periods, the effective tax rates were 41 percent for both periods.

The increase in the effective tax rate in the quarterly comparison was primarily due to the effect of one-time tax benefits in 2009 that were significantly higher than those generated in the comparable 2010 period. Additionally, foreign currency translation losses were greater in the 2010 quarter, resulting in a larger reduction in Income Before Income Tax Expense, with no corresponding impact on Income Tax Expense. Partially offsetting these items was the increased utilization of tax credits resulting from higher profits in certain foreign tax jurisdictions in the 2010 period. For the comparative nine-month periods, greater one-time tax benefits were generated in 2009 than in 2010. This effect was essentially offset by increased tax credit utilization in foreign tax jurisdictions in 2010 and by foreign currency translation impacts.

Tax positions for Chevron and its subsidiaries and affiliates are subject to income tax audits by many tax jurisdictions throughout the world. For the company's major tax jurisdictions, examinations of tax returns for certain prior tax years had not been completed as of September 30, 2010. For these jurisdictions, the latest years for which income tax examinations had been finalized were as follows: United States 2005, Nigeria 1994, Angola 2001 and Saudi Arabia 2003.

The company engages in ongoing discussions with tax authorities regarding the resolution of tax matters in the various jurisdictions. Both the outcome of these tax matters and the timing of resolution and/or closure of the tax audits are highly uncertain. However, it is reasonably possible that developments on tax matters in certain tax jurisdictions may result in significant increases or decreases in the company's total unrecognized tax benefits within the next 12 months. Given the number of years that still remain subject to examination and the number of matters being examined in the various tax jurisdictions, we are unable to estimate the range of possible adjustments to the balance of unrecognized tax benefits.

**Note 9. Employee Benefits**

Chevron has defined benefit pension plans for many employees. The company typically prefunds defined benefit plans as required by local regulations or in certain situations where prefunding provides economic advantages. In the United States, all qualified plans are subject to the Employee Retirement Income Security Act (ERISA) minimum funding standard. The company does not typically fund U.S. nonqualified pension plans that are not subject to funding requirements under laws and regulations because contributions to these pension plans may be less economic and investment returns may be less attractive than the company's other investment alternatives.

The company also sponsors other postretirement (OPEB) plans that provide medical and dental benefits, as well as life insurance for some active and qualifying retired employees. The plans are unfunded, and the company and the retirees share the costs. Medical coverage for Medicare-eligible retirees in the company's main U.S. medical plan is secondary to Medicare (including Part D) and the increase to the company contribution for retiree medical coverage is limited to no more than 4 percent each year. Certain life insurance benefits are paid by the company.



**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The components of net periodic benefit costs for 2010 and 2009 are as follows:

	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
	(Millions of dollars)			
<b>Pension Benefits</b>				
<b>United States</b>				
Service cost	\$ 85	\$ 66	\$ 253	\$ 199
Interest cost	121	121	364	361
Expected return on plan assets	(135)	(99)	(404)	(296)
Amortization of prior-service credits	(1)	(1)	(5)	(5)
Amortization of actuarial losses	79	74	238	223
Settlement losses	55	25	165	126
<b>Total United States</b>	<b>204</b>	186	<b>611</b>	608
<b>International</b>				
Service cost	38	31	114	90
Interest cost	78	76	230	215
Expected return on plan assets	(60)	(52)	(180)	(148)
Amortization of prior-service costs	5	6	16	17
Amortization of actuarial losses	24	30	74	81
<b>Total International</b>	<b>85</b>	91	<b>254</b>	255
<b>Net Periodic Pension Benefit Costs</b>	<b>\$ 289</b>	\$277	<b>\$ 865</b>	\$ 863
<b>Other Benefits*</b>				
Service cost	\$ 10	\$ 9	\$ 29	\$ 25
Interest cost	45	45	131	134
Amortization of prior-service credits	(19)	(20)	(56)	(61)
Amortization of actuarial losses	7	6	20	20
Curtailement gains				(5)
<b>Net Periodic Other Benefit Costs</b>	<b>\$ 43</b>	\$ 40	<b>\$ 124</b>	\$ 113

\* Includes costs for U.S. and international OPEB plans. Obligations for plans outside the U.S. are not significant relative to the company's total OPEB obligation.

At the end of 2009, the company estimated it would contribute \$900 million to employee pension plans during 2010 (composed of \$600 million for the U.S. plans and \$300 million for the international plans). Through September 30,

2010, a total of \$895 million was contributed (including \$790 million to the U.S. plans). Total contributions for the full year are currently estimated to be \$1.5 billion (\$1.2 billion for the U.S. plans and \$300 million for the international plans). Actual contribution amounts are dependent upon investment returns, changes in pension obligations, regulatory environments and other economic factors. Additional funding may ultimately be required if investment returns are insufficient to offset increases in plan obligations.

During the first nine months of 2010, the company contributed \$138 million to its OPEB plans. The company anticipates contributing about \$70 million during the remainder of 2010.

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Note 10. Accounting for Suspended Exploratory Wells**

Accounting standards for the costs of exploratory wells (ASC 932) provide that exploratory well costs continue to be capitalized after the completion of drilling when (a) the well has found a sufficient quantity of reserves to justify its completion as a producing well and (b) the entity is making sufficient progress assessing the reserves and the economic and operating viability of the project. If either condition is not met or if an entity obtains information that raises substantial doubt about the economic or operational viability of the project, the exploratory well would be assumed to be impaired, and its costs, net of any salvage value, would be charged to expense. (Note that an entity is not required to complete the exploratory or exploratory-type stratigraphic well as a producing well.) The company's capitalized cost of suspended wells at September 30, 2010, was \$2.6 billion, an increase of \$191 million from year-end 2009, primarily due to drilling activities in Australia. For the category of exploratory well costs at year-end 2009 that were suspended more than one year, a total of \$15 million was expensed in the first nine months of 2010.

**Note 11. Litigation**

*MTBE* Chevron and many other companies in the petroleum industry have used methyl tertiary butyl ether (MTBE) as a gasoline additive. Chevron is a party to 19 pending lawsuits and claims, the majority of which involve numerous other petroleum marketers and refiners. Resolution of these lawsuits and claims may ultimately require the company to correct or ameliorate the alleged effects on the environment of prior release of MTBE by the company or other parties. Additional lawsuits and claims related to the use of MTBE, including personal-injury claims, may be filed in the future. The company's ultimate exposure related to pending lawsuits and claims is not determinable, but could be material to net income in any one period. The company no longer uses MTBE in the manufacture of gasoline in the United States.

*Ecuador* Chevron is a defendant in a civil lawsuit before the Superior Court of Nueva Loja in Lago Agrio, Ecuador, brought in May 2003 by plaintiffs who claim to be representatives of certain residents of an area where an oil production consortium formerly had operations. The lawsuit alleges damage to the environment from the oil exploration and production operations and seeks unspecified damages to fund environmental remediation and restoration of the alleged environmental harm, plus a health monitoring program. Until 1992, Texaco Petroleum Company (Texpet), a subsidiary of Texaco Inc., was a minority member of this consortium with Petroecuador, the Ecuadorian state-owned oil company, as the majority partner; since 1990, the operations have been conducted solely by Petroecuador. At the conclusion of the consortium and following an independent third-party environmental audit of the concession area, Texpet entered into a formal agreement with the Republic of Ecuador and Petroecuador for Texpet to remediate specific sites assigned by the government in proportion to Texpet's ownership share of the consortium. Pursuant to that agreement, Texpet conducted a three-year remediation program at a cost of \$40 million. After certifying that the sites were properly remediated, the government granted Texpet and all related corporate entities a full release from any and all environmental liability arising from the consortium operations.

Based on the history described above, Chevron believes that this lawsuit lacks legal or factual merit. As to matters of law, the company believes first, that the court lacks jurisdiction over Chevron; second, that the law under which plaintiffs bring the action, enacted in 1999, cannot be applied retroactively; third, that the claims are barred by the statute of limitations in Ecuador; and, fourth, that the lawsuit is also barred by the releases from liability previously given to Texpet by the Republic of Ecuador and Petroecuador and by the pertinent provincial and municipal governments. With regard to the facts, the company believes that the evidence confirms that Texpet's remediation was properly conducted and that the remaining environmental damage reflects Petroecuador's failure to timely fulfill its legal obligations and Petroecuador's further conduct since assuming full control over the operations.



In 2008, a mining engineer appointed by the court to identify and determine the cause of environmental damage, and to specify steps needed to remediate it, issued a report recommending that the court assess \$18.9 billion, which would, according to the engineer, provide financial compensation for purported damages, including wrongful death claims, and pay for, among other items, environmental remediation, health care systems and additional infrastructure for Petroecuador. The engineer's report also asserted that an additional \$8.4 billion could be

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

assessed against Chevron for unjust enrichment. In 2009, following the disclosure by Chevron of evidence that the judge participated in meetings in which businesspeople and individuals holding themselves out as government officials discussed the case and its likely outcome, the judge presiding over the case was recused. In 2010, Chevron moved to strike the mining engineer's report and to dismiss the case based on evidence obtained through discovery in the United States indicating that the report was prepared by consultants for the plaintiffs before being presented as the mining engineer's independent and impartial work and showing further evidence of misconduct. In August 2010, the judge issued an order stating that he was not bound by the mining engineer's report and requiring the parties to provide their positions on damages within 45 days. Chevron subsequently petitioned for recusal of the judge, claiming that he had disregarded evidence of fraud and misconduct and that he had failed to rule on a number of motions within the statutory time requirement.

In September 2010, Chevron submitted its position on damages, asserting that no amount should be assessed against it. The plaintiffs' submission, which relied in part on the mining engineer's report, took the position that damages are between approximately \$16 billion and \$76 billion and that unjust enrichment should be assessed in an amount between approximately \$5 billion and \$38 billion. The next day, the judge issued an order closing the evidentiary phase of the case and notifying the parties that he had requested the case file so that he could prepare a judgment. Chevron petitioned to have that order declared a nullity in light of Chevron's prior recusal petition, and because procedural and evidentiary matters remain unresolved. In October 2010, Chevron's motion to recuse the judge was granted. A new judge has taken charge of the case, and that judge has revoked the prior judge's order closing the evidentiary phase of the case.

Chevron cannot predict the timing or content of future developments in the Lago Agrio litigation, and a judgment could be entered at any time. Chevron will continue a vigorous defense of any attempted imposition of liability. In the event of an adverse trial court judgment, Chevron would expect to pursue its appeals in Ecuador. Because Chevron has no substantial assets in Ecuador, Chevron would expect enforcement actions following any adverse judgment to be brought in other jurisdictions. Chevron would expect to contest any such actions. The ultimate outcome, including any financial effect on Chevron, remains uncertain.

Management does not believe an estimate of a reasonably possible loss (or a range of loss) can be made in this case. Due to the defects associated with the 2008 engineer's report and the September 2010 plaintiffs' submission, management does not believe those documents have any utility in calculating a reasonably possible loss (or a range of loss). Moreover, the highly uncertain legal environment surrounding the case provides no basis for management to estimate a reasonably possible loss (or a range of loss).

**Note 12. Other Contingencies and Commitments**

*Guarantees* The company and its subsidiaries have certain other contingent liabilities with respect to guarantees, direct or indirect, of debt of affiliated companies or third parties. Under the terms of the guarantee arrangements, generally the company would be required to perform should the affiliated company or third party fail to fulfill its obligations under the arrangements. In some cases, the guarantee arrangements may have recourse provisions that would enable the company to recover any payments made under the terms of the guarantees from assets provided as collateral.

*Off-Balance-Sheet Obligations* The company and its subsidiaries have certain other contingent liabilities relating to long-term unconditional purchase obligations and commitments, including throughput and take-or-pay agreements, some of which relate to suppliers' financing arrangements. The agreements typically provide goods and services, such as pipeline and storage capacity, drilling rigs, utilities, and petroleum products, to be used or sold in the ordinary

course of the company's business.

*Indemnifications* The company provided certain indemnities of contingent liabilities of Equilon and Motiva to Shell and Saudi Refining, Inc., in connection with the February 2002 sale of the company's interests in those investments. The company would be required to perform if the indemnified liabilities become actual losses. Were that to occur, the company could be required to make future payments up to \$300 million. Through September 2010, the company

**Table of Contents**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

paid \$48 million under these indemnities and continues to be obligated for possible additional indemnification payments in the future.

The company has also provided indemnities relating to contingent environmental liabilities related to assets originally contributed by Texaco to the Equilon and Motiva joint ventures and environmental conditions that existed prior to the formation of Equilon and Motiva or that occurred during the period of Texaco's ownership interest in the joint ventures. In general, the environmental conditions or events that are subject to these indemnities must have arisen prior to December 2001. Claims had to be asserted by February 2009 for Equilon indemnities and must be asserted no later than February 2012 for Motiva indemnities. Under the terms of these indemnities, there is no maximum limit on the amount of potential future payments. In February 2009, Shell delivered a letter to the company purporting to preserve unmaturing claims for certain Equilon indemnities. The letter itself provides no estimate of the ultimate claim amount. Management does not believe this letter or any other information provides a basis to estimate the amount, if any, of a range of loss or potential range of loss with respect to either the Equilon or the Motiva indemnities. The company posts no assets as collateral and has made no payments under the indemnities.

The amounts payable for the indemnities described in the preceding paragraph are to be net of amounts recovered from insurance carriers and others and net of liabilities recorded by Equilon or Motiva prior to September 30, 2001, for any applicable incident.

In the acquisition of Unocal, the company assumed certain indemnities relating to contingent environmental liabilities associated with assets that were sold in 1997. The acquirer of those assets shared in certain environmental remediation costs up to a maximum obligation of \$200 million, which had been reached at December 31, 2009. Under the indemnification agreement, after reaching the \$200 million obligation, Chevron is solely responsible until April 2022, when the indemnification expires. The environmental conditions or events that are subject to these indemnities must have arisen prior to the sale of the assets in 1997.

Although the company has provided for known obligations under this indemnity that are probable and reasonably estimable, the amount of additional future costs may be material to results of operations in the period in which they are recognized. The company does not expect these costs will have a material effect on its consolidated financial position or liquidity.

*Environmental* The company is subject to loss contingencies pursuant to laws, regulations, private claims and legal proceedings related to environmental matters that are subject to legal settlements or that in the future may require the company to take action to correct or ameliorate the effects on the environment of prior release of chemicals or petroleum substances, including MTBE, by the company or other parties. Such contingencies may exist for various sites, including, but not limited to, federal Superfund sites and analogous sites under state laws, refineries, crude oil fields, service stations, terminals, land development areas, and mining operations, whether operating, closed or divested. These future costs are not fully determinable due to such factors as the unknown magnitude of possible contamination, the unknown timing and extent of the corrective actions that may be required, the determination of the company's liability in proportion to other responsible parties, and the extent to which such costs are recoverable from third parties.

Although the company has provided for known environmental obligations that are probable and reasonably estimable, the amount of additional future costs may be material to results of operations in the period in which they are recognized. The company does not expect these costs will have a material effect on its consolidated financial position or liquidity. Also, the company does not believe its obligations to make such expenditures have had, or will have, any significant impact on the company's competitive position relative to other U.S. or international petroleum or chemical

companies.

*Financial Instruments* The company believes it has no material market or credit risks to its operations, financial position or liquidity as a result of its commodities and other derivative activities.

*Equity Redetermination* For crude oil and natural gas producing operations, ownership agreements may provide for periodic reassessments of equity interests in estimated crude oil and natural gas reserves. These activities, individually or together, may result in gains or losses that could be material to earnings in any given period.

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

One such equity redetermination process has been under way since 1996 for Chevron's interests in four producing zones at the Naval Petroleum Reserve at Elk Hills, California, for the time when the remaining interests in these zones were owned by the U.S. Department of Energy. A wide range remains for a possible net settlement amount for the four zones. For this range of settlement, Chevron estimates its maximum possible net before-tax liability at approximately \$200 million, and the possible maximum net amount that could be owed to Chevron is estimated at about \$150 million. The timing of the settlement and the exact amount within this range of estimates are uncertain.

*Other Contingencies* On April 26, 2010, a California appeals court issued a ruling related to the adequacy of an Environmental Impact Report (EIR) supporting the issuance of certain permits by the city of Richmond, California, to replace and upgrade certain facilities at Chevron's refinery in Richmond. The parties to the case have stipulated that entry of final judgment by the trial court be postponed pending on-going settlement discussions. The company continues to evaluate its options going forward, which may include settlement, requesting the city to revise the EIR to address the issues identified by the Court of Appeal or other actions. Management believes the outcomes associated with the potential options for the project are uncertain. Due to the uncertainty of the company's future course of action, or potential outcomes of any action or combination of actions, management does not believe an estimate of the financial effects, if any, of the ruling can be made at this time. However, the company's ultimate exposure may be significant to net income in any one future period.

Chevron receives claims from and submits claims to customers; trading partners; U.S. federal, state and local regulatory bodies; governments; contractors; insurers; and suppliers. The amounts of these claims, individually and in the aggregate, may be significant and take lengthy periods to resolve.

The company and its affiliates also continue to review and analyze their operations and may close, abandon, sell, exchange, acquire or restructure assets to achieve operational or strategic benefits and to improve competitiveness and profitability. These activities, individually or together, may result in gains or losses in future periods.

**Note 13. Fair Value Measurements**

Accounting standards for fair value measurement (ASC 820) establish a framework for measuring fair value and stipulate disclosures about fair value measurements. The standards apply to recurring and nonrecurring financial and nonfinancial assets and liabilities that require or permit fair value measurements. Among the required disclosures is the fair value hierarchy of inputs the company uses to value an asset or a liability. The three levels of the fair value hierarchy are described as follows:

Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities. For the company, Level 1 inputs include exchange-traded futures contracts for which the parties are willing to transact at the exchange-quoted price and marketable securities that are actively traded.

Level 2: Inputs other than Level 1 that are observable, either directly or indirectly. For the company, Level 2 inputs include quoted prices for similar assets or liabilities, prices obtained through third-party broker quotes and prices that can be corroborated with other observable inputs for substantially the complete term of a contract.

Level 3: Unobservable inputs. The company does not use Level 3 inputs for any of its recurring fair value measurements. Level 3 inputs may be required for the determination of fair value associated with certain nonrecurring measurements of nonfinancial assets and liabilities.



**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The fair value hierarchy for recurring assets and liabilities measured at fair value at September 30, 2010 and December 31, 2009, is as follows:

**Assets and Liabilities Measured at Fair Value on a Recurring Basis**

	At September 30, 2010	Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	At December 31, 2009	Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
	(Millions of dollars)							
<b>Assets</b>								
Marketable Securities	\$ 66	\$ 66	\$	\$	\$106	\$106	\$	\$
Derivatives	154	21	133		127	14	113	
<b>Total Recurring Assets at Fair Value</b>	<b>\$220</b>	<b>\$ 87</b>	<b>\$133</b>	<b>\$</b>	<b>\$233</b>	<b>\$120</b>	<b>\$113</b>	<b>\$</b>
<b>Liabilities</b>								
Derivatives	\$175	\$143	\$ 32	\$	\$101	\$ 20	\$ 81	\$
<b>Total Recurring Liabilities at Fair Value</b>	<b>\$175</b>	<b>\$143</b>	<b>\$ 32</b>	<b>\$</b>	<b>\$101</b>	<b>\$ 20</b>	<b>\$ 81</b>	<b>\$</b>

*Marketable Securities* The company calculates fair value for its marketable securities based on quoted market prices for identical assets and liabilities. The fair values reflect the cash that would have been received if the instruments were sold at September 30, 2010.

*Derivatives* The company records its derivative instruments other than any commodity derivative contracts that are designated as normal purchase and normal sale on the Consolidated Balance Sheet at fair value, with virtually all the offsetting amount to the Consolidated Statement of Income. For derivatives with identical or similar provisions as contracts that are publicly traded on a regular basis, the company uses the market values of the publicly traded instruments as an input for fair value calculations.

The company's derivative instruments principally include crude oil, natural gas and refined product futures, swaps, options and forward contracts. Derivatives classified as Level 1 include futures, swaps and options contracts traded in active markets such as the New York Mercantile Exchange.



Derivatives classified as Level 2 include swaps, options, and forward contracts principally with financial institutions and other oil and gas companies, the fair values for which are obtained from third-party broker quotes, industry pricing services and exchanges. The company obtains multiple sources of pricing information for the Level 2 instruments. Since this pricing information is generated from observable market data, it has historically been very consistent. The company does not materially adjust this information. The company incorporates internal review, evaluation and assessment procedures, including a comparison of Level 2 fair values derived from the company's internally developed forward curves (on a sample basis) with the pricing information to document reasonable, logical and supportable fair value determinations and proper level of classification.

*Impairments of Properties, plant and equipment* Assets measured at fair value on a nonrecurring basis were not material to the company's financial position, results of operations or liquidity in the three- and nine-month periods of 2010. Before-tax losses associated with the impairment of property, plant and equipment held and used and held for sale in the third quarter 2009 were \$93 million and nil, respectively, and for the nine months ended September 30, 2009, were \$358 million and \$92 million, respectively. The losses in 2009 were the result of fair values determined both from internal cash flow models, using discount rates consistent with those used by the company to evaluate cash flows of other assets of a similar nature, and from bids received from prospective buyers of assets held for sale.

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Assets and Liabilities not Required to be Measured at Fair Value* The company holds cash equivalents and bank time deposits in U.S. and non-U.S. portfolios. The instruments classified as cash equivalents are primarily bank time deposits with maturities of 90 days or less and money market funds. Cash and cash equivalents had carrying/fair values of \$11.0 billion and \$8.7 billion at September 30, 2010 and December 31, 2009, respectively. The instruments held in Time deposits are bank time deposits with maturities greater than 90 days, and had carrying/fair values of \$3.5 billion at September 30, 2010. The fair values of cash, cash equivalents and bank time deposits reflect the cash that would have been received or paid if the instruments were settled at September 30, 2010.

Cash and cash equivalents does not include investments with a carrying/fair value of \$186 million and \$123 million at September 30, 2010 and December 31, 2009, respectively. These investments are restricted funds related to an international upstream development project and Pascagoula Refinery projects, which are reported in Deferred charges and other assets on the Consolidated Balance Sheet. Long-term debt of \$5.6 billion and \$5.7 billion had estimated fair values of \$6.5 billion and \$6.2 billion at September 30, 2010 and December 31, 2009, respectively.

Fair values of other financial instruments at September 30, 2010 were not material.

**Note 14. Derivative Instruments and Hedging Activities**

The company's derivative instruments principally include crude oil, natural gas and refined product futures, swaps, options and forward contracts. None of the company's derivative instruments are designated as a hedging instrument, although certain of the company's affiliates make such designation. The company's derivatives are not material to the company's financial position, results of operations or liquidity. The company believes it has no material market or credit risks to its operations, financial position or liquidity as a result of its commodities and other derivatives activities.

Derivative instruments measured at fair value at September 30, 2010 and December 31, 2009, and their classification on the Consolidated Balance Sheet and Consolidated Statement of Income are as follows:

**Consolidated Balance Sheet:  
Fair Value of Derivatives Not Designated as Hedging Instruments**

Type of Derivative Contract	Balance Sheet Classification	Asset Derivatives Fair Value		(Millions of Dollars)	Liability Derivatives Fair Value	
		At September 30 2010	At December 31 2009		At September 30 2010	At December 31 2009
Commodity	Accounts and notes receivable, net	\$ 85	\$ 99	Accounts payable	\$125	\$ 73
Commodity	Long-term receivables, net	69	28	Deferred credits and other noncurrent obligations	50	28
		\$154	\$127		\$175	\$101

**Consolidated Statement of Income:  
The Effect of Derivatives Not Designated as Hedging Instruments**

Type of Derivative Contract	Statement of Income Classification	Gain/(Loss) Three Months Ended September 30		Gain/(Loss) Nine Months Ended September 30	
		2010	2009	2010	2009
		(Millions of dollars)			
Foreign Exchange	Other income	\$	\$ 8	\$	\$ 26
Commodity	Sales and other operating revenues	(58)	32	94	(63)
Commodity	Purchased crude oil and products	(12)	(18)	(38)	(295)
Commodity	Other income	7	8	(2)	1
		<b>\$(63)</b>	<b>\$ 30</b>	<b>\$ 54</b>	<b>\$(331)</b>

**Table of Contents**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 15. New Accounting Standards**

*Transfers and Servicing (ASC 860), Accounting for Transfers of Financial Assets (ASU 2009-16)* The FASB issued ASU 2009-16 in December 2009. This standard became effective for the company on January 1, 2010. ASU 2009-16 changes how companies account for transfers of financial assets and eliminates the concept of qualifying special-purpose entities. Adoption of the guidance did not have an effect on the company's results of operations, financial position or liquidity.

*Consolidation (ASC 810), Improvements to Financial Reporting by Enterprises Involved With Variable Interest Entities (ASU 2009-17)* The FASB issued ASU 2009-17 in December 2009. This standard became effective for the company on January 1, 2010. ASU 2009-17 requires the enterprise to qualitatively assess if it is the primary beneficiary of a variable-interest entity (VIE), and, if so, the VIE must be consolidated. Adoption of the standard did not have an impact on the company's results of operations, financial position or liquidity.

*Receivables (ASC 310), Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses (ASU 2010-20)* In July 2010, the FASB issued ASU 2010-20, which becomes effective with the company's reporting at December 31, 2010. This standard amends and expands disclosure requirements about the credit quality of financing receivables and the related allowance for credit losses. As a result of these amendments, companies are required to disaggregate, by portfolio segment or class of financing receivable, certain existing disclosures and provide certain new disclosures about financing receivables and related allowance for credit losses. The company does not anticipate changes to its existing disclosures when the standard becomes effective.

**Note 16. Restructuring and Reorganization Costs**

In the first quarter 2010, the company announced employee reduction programs related to the restructuring and reorganization of its downstream businesses and corporate staffs. As originally announced, approximately 3,200 employees in the refining, marketing, and supply and trading operations, and 600 employees from corporate staffs, were expected to be terminated under the programs. Due to redeployment efforts within the company, total employee terminations under the programs are expected to be reduced from approximately 3,800 employees to approximately 3,600 employees. About 1,700 of the affected positions are located in the United States. It is anticipated that 2,400 employees of the total covered under the programs will be terminated during 2010, and the programs are expected to be completed by the end of 2011. About 600 employees have been terminated to date.

A before-tax charge of \$244 million (\$175 million after-tax) was recorded in the first quarter 2010, with \$191 million reported as Operating expenses and \$53 million as Selling, general and administrative expenses on the Consolidated Statement of Income. The accrued liability is classified as current on the Consolidated Balance Sheet. Approximately \$80 million (\$50 million after-tax) is associated with terminations in the U.S. Downstream, \$127 million (\$100 million after-tax) in International Downstream and \$37 million (\$25 million after-tax) in All Other.

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

During the second and third quarters of 2010, the company made payments of \$35 million associated with these liabilities. The majority of the payments were in Downstream.

	<b>Amounts Before Tax (Millions of dollars)</b>
Balance at January 1, 2010	\$
Accruals	<b>244</b>
Adjustments	<b>(3)</b>
Payments	<b>(35)</b>
Balance at September 30, 2010	<b>\$206</b>

**Note 17. Asset Retirement Obligations**

At September 30, 2010, the company's liability for asset retirement obligations calculated in accordance with accounting standards for asset retirement obligations (ASC 410) was approximately \$11.4 billion, compared with \$10.2 billion at year-end 2009. The \$1.2 billion net increase reflects increasing costs to abandon wells, equipment and facilities.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations****Third Quarter 2010 Compared with Third Quarter 2009  
And Nine Months 2010 Compared with Nine Months 2009****Key Financial Results****Earnings by Business Segment**

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
	<b>(Millions of dollars)</b>			
<b>Upstream(1)</b>				
United States	\$ 946	\$ 889	\$ 3,192	\$1,196
International	2,618	2,847	9,638	5,575
<b>Total Upstream</b>	<b>3,564</b>	<b>3,736</b>	<b>12,830</b>	<b>6,771</b>
<b>Downstream(1)</b>				
United States	349	127	864	212
International	216	135	872	934
<b>Total Downstream</b>	<b>565</b>	<b>262</b>	<b>1,736</b>	<b>1,146</b>
<b>Total Segment Earnings</b>	<b>4,129</b>	<b>3,998</b>	<b>14,566</b>	<b>7,917</b>
<b>All Other</b>	<b>(361)</b>	<b>(167)</b>	<b>(837)</b>	<b>(504)</b>
<b>Net Income Attributable to Chevron Corporation(2)(3)</b>	<b>\$3,768</b>	<b>\$3,831</b>	<b>\$13,729</b>	<b>\$7,413</b>

(1) 2009 information has been revised to conform with the 2010 segment presentation.

(2) Includes foreign currency effects

(3) Also referred to as earnings in the discussions that follow.

*Net income attributable to Chevron Corporation* for the third quarter 2010 was \$3.77 billion (\$1.87 per share diluted), compared with \$3.83 billion (\$1.92 per share diluted) in the corresponding 2009 period. Net income attributable to Chevron Corporation for the first nine months of 2010 was \$13.73 billion (\$6.84 per share diluted), versus \$7.41 billion (\$3.71 per share diluted) in the first nine months of 2009.

The activities reported in Chevron's upstream and downstream operating segments have changed effective January 1, 2010. Results for the chemicals businesses are now reported as part of the downstream segment. In addition, the company's significant upstream-enabling operations, primarily a gas-to-liquids project and major international export pipelines, have been reclassified from the downstream segment to the upstream segment. Prior period information in this report has been revised to conform to the 2010 presentation.

*Upstream* earnings in the third quarter 2010 were \$3.56 billion, compared with \$3.74 billion in the 2009 quarter. The decrease was primarily associated with the absence of gains on asset sales and tax items related to Gorgon project in Australia in the third quarter of 2009. Earnings for the first nine months of 2010 were \$12.83 billion, versus \$6.77 billion a year earlier. The increase between periods was mainly due to higher prices for crude oil and natural gas and increased production of crude oil.

*Downstream* earnings were \$565 million in the third quarter 2010, compared with \$262 million in the year-earlier period. Earnings for the first nine months of 2010 were \$1.74 billion, versus \$1.15 billion in the corresponding 2009 period. The increase between both comparative periods was mainly associated with improved margins on refined products, and higher earnings from chemicals operations largely from the 50 percent-owned Chevron Phillips Chemical Company LLC. Also contributing to the increase in the 2010 nine-month period was a favorable swing in

**Table of Contents**

mark-to-market effects on derivative instruments. Earnings for the first nine months of 2009 included \$540 million of gains on sales of marketing businesses outside the United States.

Refer to pages 29 through 32 for additional discussion of results by business segment and All Other activities for the third quarter and first nine months of 2010 versus the same periods in 2009.

***Business Environment and Outlook***

Chevron is a global energy company with significant business activities in the following countries: Angola, Argentina, Australia, Azerbaijan, Bangladesh, Brazil, Cambodia, Canada, Chad, China, Colombia, Democratic Republic of the Congo, Denmark, Indonesia, Kazakhstan, Myanmar, the Netherlands, Nigeria, Norway, the Partitioned Zone between Saudi Arabia and Kuwait, the Philippines, Republic of the Congo, Singapore, South Africa, South Korea, Thailand, Trinidad and Tobago, the United Kingdom, the United States, Venezuela, and Vietnam.

Earnings of the company depend largely on the profitability of its upstream and downstream business segments. The single biggest factor that affects the results of operations for both segments is movement in the price of crude oil. In the downstream business, crude oil is the largest cost component of refined products. The overall trend in earnings is typically less affected by results from the company's other activities and investments. Earnings for the company in any period may also be influenced by events or transactions that are infrequent or unusual in nature.

The company's operations, especially upstream, can also be affected by changing economic, regulatory and political environments in the various countries in which it operates, including the United States. Civil unrest, acts of violence or strained relations between a government and the company or other governments may impact the company's operations or investments. Those developments have at times significantly affected the company's operations and results and are carefully considered by management when evaluating the level of current and future activity in such countries.

To sustain its long-term competitive position in the upstream business, the company must develop and replenish an inventory of projects that offer attractive financial returns for the investment required. Identifying promising areas for exploration, acquiring the necessary rights to explore for and to produce crude oil and natural gas, drilling successfully, and handling the many technical and operational details in a safe and cost-effective manner are all important factors in this effort. Projects often require long lead times and large capital commitments. From time to time, certain governments have sought to renegotiate contracts or impose additional costs on the company. Governments may attempt to do so in the future. The company will continue to monitor these developments, take them into account in evaluating future investment opportunities, and otherwise seek to mitigate any risks to the company's current operations or future prospects.

The company also continually evaluates opportunities to dispose of assets that are not expected to provide sufficient long-term value or to acquire assets or operations complementary to its asset base to help augment the company's financial performance and growth. Asset dispositions and restructurings may also occur in future periods and could result in significant gains or losses.

In recent years, Chevron and the oil and gas industry generally experienced an increase in certain costs that exceeded the general trend of inflation in many areas of the world. This increase in costs affected the company's operating expenses and capital programs for all business segments, but particularly for upstream. Softening of these cost pressures started in late 2008 and continued through most of 2009. Industry costs began to level out in the fourth quarter 2009 and rose slightly in 2010. The company continues to actively manage its schedule of work, contracting, procurement and supply-chain activities to effectively manage costs. (Refer to the Upstream section below for a discussion of the trend in crude oil prices.)



The company closely monitors developments in the financial and credit markets, the level of worldwide economic activity and the implications to the company of movements in prices for crude oil and natural gas. Management takes these developments into account in the conduct of daily operations and for business planning. The company remains confident of its underlying financial strength to address potential challenges presented in the current environment. (Refer also to the Liquidity and Capital Resources section beginning on page 36.)

**Table of Contents**

Comments related to earnings trends for the company's major business areas are as follows:

**Upstream** Earnings for the upstream segment are closely aligned with industry price levels for crude oil and natural gas. Crude oil and natural gas prices are subject to external factors over which the company has no control, including product demand connected with global economic conditions, industry inventory levels, production quotas imposed by the Organization of Petroleum Exporting Countries (OPEC), weather-related damage and disruptions, competing fuel prices, and regional supply interruptions or fears thereof that may be caused by military conflicts, civil unrest or political uncertainty. Moreover, any of these factors could also inhibit the company's production capacity in an affected region. The company monitors developments closely in the countries in which it operates and holds investments, and attempts to manage risks in operating its facilities and businesses. Besides the impact of the fluctuation in prices for crude oil and natural gas, the longer-term trend in earnings for the upstream segment is also a function of other factors, including the company's ability to find or acquire and efficiently produce crude oil and natural gas, changes in fiscal terms of contracts and changes in tax laws and regulations.

Price levels for capital and exploratory costs and operating expenses associated with the production of crude oil and natural gas can also be subject to external factors beyond the company's control. External factors include not only the general level of inflation but also commodity prices and prices charged by the industry's material and service providers, which can be affected by the volatility of the industry's own supply-and-demand conditions for such materials and services. Capital and exploratory expenditures and operating expenses also can be affected by damage to production facilities caused by severe weather or civil unrest.

The chart below shows the trend in benchmark prices for West Texas Intermediate (WTI) crude oil and U.S. Henry Hub natural gas. During 2009, industry price levels for WTI ranged from \$34 to \$81 per barrel and finished the year at \$79 per barrel. The WTI price in the first nine months of 2010 averaged \$78 and ended October at \$81.

A differential in crude oil prices exists between high quality (high-gravity, low-sulfur) crudes and those of lower quality (low-gravity, high-sulfur). The amount of the differential in any period is associated with the supply of heavy crude available versus the demand, which is a function of the number of refineries that are able to process this lower quality feedstock into light products (motor gasoline, jet fuel, aviation gasoline and diesel fuel). The differential widened in the first nine months of 2010 primarily due to greater availability of lower quality crudes. Chevron produces or shares in the production of heavy crude oil in California, Chad, Indonesia, the Partitioned Zone between Saudi Arabia and Kuwait, Venezuela and in certain fields in Angola, China and the United Kingdom sector of the North Sea. (See page 35 for the company's average U.S. and international crude oil realizations.)

In contrast to price movements in the global market for crude oil, price changes for natural gas in many regional markets are more closely aligned with supply-and-demand conditions in those markets. In the United States, prices at Henry Hub averaged about \$4.60 per thousand cubic feet (MCF) in the first nine months of 2010, compared with about \$3.50 during the first nine months of 2009. At the end of October 2010, the Henry Hub spot price was about \$3.40 per MCF. Fluctuations in the price for natural gas in the United States are closely associated with customer demand relative to the volumes produced in North America and the level of inventory in underground storage.

Certain international natural gas markets in which the company operates have different supply, demand and regulatory circumstances, which historically have resulted in lower average sales prices for the company's production of natural gas in these locations. Chevron continues to invest in long-term projects in these locations to install infrastructure to produce and liquefy natural gas for transport by tanker to other markets where greater demand results in higher prices. International natural gas realizations averaged about \$4.60 per MCF during the first nine months of 2010, compared with about \$4.00 in the same period last year. (See page 35 for the company's average natural gas realizations for the U.S. and international regions.)

**Table of Contents**

The company's worldwide net oil-equivalent production in the first nine months of 2010 averaged 2.755 million barrels per day. During the period, about one-fifth of the company's net oil-equivalent production occurred in the OPEC-member countries of Angola, Nigeria and Venezuela and in the Partitioned Zone between Saudi Arabia and Kuwait. OPEC quotas had no effect on the company's net crude oil production for the first nine months of 2010, while production during the first nine months of 2009 was reduced by approximately 27,000 barrels per day due to quota limitations. Curtailments by OPEC did not constrain the company's production in the third quarter 2009. At the most recent meeting in October 2010, members of OPEC supported maintaining production quotas in effect since December 2008.

The full-year outlook for oil-equivalent production based on the nine-month 2010 average price of \$78 per barrel is estimated at 2.75 million barrels per day. This estimate is subject to many factors and uncertainties, including additional quotas that may be imposed by OPEC, price effects on production volumes calculated under production-sharing and variable-royalty provisions of certain agreements, changes in fiscal terms or restrictions on the scope of company operations, delays in project startups, fluctuations in demand for natural gas in various markets, weather conditions that may shut in production, civil unrest, changing geopolitics, delays in completion of maintenance turnarounds, greater-than-expected declines in production from mature fields, or other disruptions to operations. The outlook for future production levels is also affected by the size and number of economic investment opportunities and, for new large-scale projects, the time lag between initial exploration and the beginning of production. Investments in upstream projects generally begin well in advance of the start of the associated crude oil and natural gas production. A significant majority of Chevron's upstream investment is made outside the United States.

*Gulf of Mexico Update* In April 2010, an accident occurred on the Transocean Deepwater Horizon, a deepwater drilling rig in the Gulf of Mexico, resulting in loss of life, the sinking of the rig and a significant oil spill. The rig was drilling an exploratory well at the BP-operated Macondo prospect. Chevron was not a participant in the well. Subsequent to the event, the U.S. Department of the Interior suspended drilling of wells using subsea blowout preventers (BOPs) or surface BOPs on a floating facility in the Gulf of Mexico and the Pacific regions. On October 12, 2010, the Secretary of the Interior lifted the suspension on deepwater drilling activity, provided that operators certify compliance with all rules and requirements, including availability of adequate blowout containment resources.

The suspension has created delays in shallow water permitting and delayed the drilling of some exploratory deepwater wells as well as impacted development drilling at the recently commissioned, nonoperated Perdido project. The company does not expect there to be a material impact on production for the full year 2010. The company has submitted one deepwater drilling permit application and plans to submit several additional applications over the next few months. Two deepwater drilling rigs are on stand-by, pending issuance of permits from the U.S. Bureau of Ocean Energy Management (BOEM), Regulation, and Enforcement to drill wells in the Gulf of Mexico. A third deepwater drill rig has received a permit to drill a water injection well at the Tahiti Field. The future effects of this incident, including any new or additional regulations that may be adopted in response, are not fully known at this time. Chevron remains committed to deepwater exploration and development in the Gulf of Mexico and other deepwater basins around the world.

As previously announced, Chevron and several other companies plan to build and deploy a rapid response system that will be available to capture and contain crude oil in the event of a future well blowout in the deepwater Gulf of Mexico. The new system will be engineered to be used in water depths up to 10,000 feet and designed to have initial capacity to contain 100,000 barrels per day, with potential for expansion. The companies committed to equally fund the initial \$1 billion investment in the system. There will be additional ongoing costs for operations and maintenance of the system components. An initial agreement to secure underwater well containment equipment for industry use has been announced, and other equipment is expected to be secured and available in the coming months with the new system targeted for completion within 18 months. The companies intend to form a non-profit organization, the Marine

Well Containment Company, to operate and maintain this system. Other companies will be invited and encouraged to participate in this organization.

Refer to the Results of Operations section on pages 29-31 for additional discussion of the company's upstream business.

**Table of Contents**

***Downstream*** Earnings for the downstream segment are closely tied to margins on the refining, manufacturing and marketing of products that include gasoline, diesel, jet fuel, lubricants, fuel oil, fuel and lubricant additives, and petrochemicals. Industry margins are sometimes volatile and can be affected by the global and regional supply-and-demand balance for refined products and petrochemicals and by changes in the price of refinery crude oil feedstocks, petrochemical feedstocks and fuel costs. Industry margins can also be influenced by inventory levels, geopolitical events, cost of materials and services, refinery or chemical plant capacity utilization, maintenance programs and disruptions at refineries or chemical plants resulting from unplanned outages due to severe weather, fires or other operational events.

Other factors affecting profitability for downstream operations include the reliability and efficiency of the company's refining and marketing network, the effectiveness of the crude oil and product-supply functions and the volatility of tanker-c