Responses Submitted by Chevron to Follow-up Questions from the March 14, 2006 Hearing by the United States Senate Committee on the Judiciary

QUESTIONS FOR THE RECORD
SENATOR SPECTER

1. Please provide an analysis of the draft bill, the "Petroleum Industry Antitrust Act of 2006," which was submitted to the Congressional Record earlier this month.

Answer: Chevron believes that passage of one or more of the draft provisions could severely undermine U.S. oil and gas companies' efforts to remain competitive in what is an increasingly global market for fuel products. The company's concerns about each of the bill's sections are discussed in more detail in Attachment 1.

2. What steps can be taken to decrease consumption of oil and natural gas?

Answer: The U.S. government should encourage continuous improvement in the responsible use of energy. It should expand its efforts to educate consumers about the value of conservation, a message included in Chevron's ongoing advertising. As a large consumer of energy, the U.S. government should lead the way in becoming more energy efficient and continue to support its Energy Savings Performance Contracting Program. The energy bill enacted last year also provided some strong provisions on energy efficiency/conservation for the states and government agencies. Finally, the U.S. government should support research and development on advanced energy-saving technologies.

3. Please provide an analysis of the incentives offered to petroleum companies by the federal government that explains what the incentives are intended to do, which incentives are important to you, and why they should be maintained.

Answer: We believe incentives should encourage investment to strengthen the nation's energy security and economic health. Energy projects are risky investments and typically require extensive lead times before they result in actual energy production. Therefore, maintaining a stable fiscal and regulatory regime is critical to this industry which commits to significant long-term investments based on the rules in place at that time. Moving forward, we believe any new incentive(s) would need to be evaluated on their own merits.

4. In the two weeks prior to March 14, 2006, the price of oil decreased seven cents per gallon, while the price of gasoline increased by eleven cents per gallon. Why would gasoline become more expensive during this period, despite a decrease in the cost of crude oil?

Answer: The markets for crude oil and gasoline are separate markets, and snapshots of either market can be misleading. Over the long term, crude oil is the most significant factor influencing the price of gasoline as evidenced by the trends in historical price data. However, in the short term, there are many factors that can influence gasoline prices in a local market – gasoline supply, consumer demand, taxes, etc. Prices for both gasoline and crude oil are set by the market, and although they will trend together over the long

term, they will not necessarily move in correlation at any point in time. Figure 1 below shows the prices for WTI crude oil and U.S. retail gasoline since January of 2005.

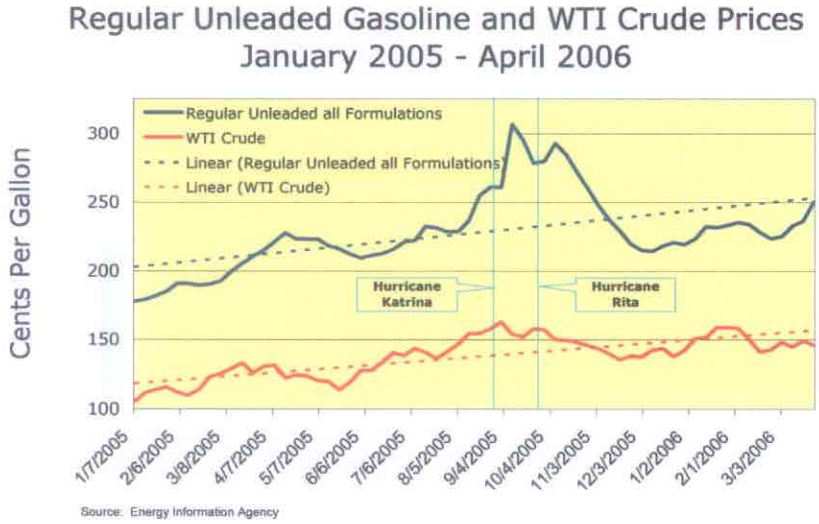


Figure 1. U.S. Gasoline and WTI Crude Prices

5. With respect to the large mergers that your companies have engaged in over the past decade, what efficiencies have they produced that have benefited consumers, particularly in downstream markets?

Answer: Chevron's merger and acquisition activity over the last decade has been driven primarily to gain strategic scale and efficiencies in our global upstream operations. The major synergy benefits of an upstream-driven merger are operating expense reductions, optimization of capital and exploratory expenditures and having greater technical, financial and other resources available to most efficiently pursue large project development to bring new energy supplies to market in a manner that benefits both stockholders and consumers.

Prior to the merger with Chevron, Texaco had entered into a joint venture of its U.S. refining and marketing operations with those of Shell in the mid '90s. However, as a consequence of Chevron's merger with Texaco, the FTC required the divestiture of Texaco's refining and marketing interests, which were sold to Shell. In 2005, Chevron acquired Unocal, which had no refining and marketing assets.

QUESTIONS FOR THE RECORD
SENATOR SCHUMER

1. Would you please clarify which income figures your company reported to the internal revenue service last year for tax purposes, as well as the basis for those figures? Are these the same income figures reported to your shareholders? If different figures were used, what were they, what was their basis, and what is the rationale for this decision?

Answer: Chevron's annual consolidated statement of income, which is provided to the company's stockholders and is included in the company's Annual Report on SEC Form 10-K, is prepared in conformity with accounting principles generally accepted in the United States (commonly referred to as GAAP). Taxable income reported to the Internal Revenue Service is based on the GAAP income statement adjusted to conform to the rules of the Internal Revenue Code.

2. Based on your written testimony, it appears that your company has put at most 5% of annual investment toward developing alternative energy technologies like hydrogen fuel cells, wind, solar, and others. What is the rationale for this investment strategy? Have you decided that investment in these energy sources is not in the interest of your shareholders?

Answer: Chevron has an active program with a broad R&D portfolio for the development of alternative energy and advanced technologies. Most alternative fuels and alternative energy technologies are in the R&D and demonstration/pilot stage and constitute a substantial component of our technology development budget (see response below). Our direct commercial investments are increasing as alternative energy technology and markets develop, but at this point are much smaller than our commercial investments in conventional oil and gas resource development. Very large investments are required to maintain and develop the oil and gas infrastructure and resources for providing reliable supplies to consumers today.

We believe our current investments in technology development are at an appropriate level. Our approach is founded on the belief that such investments must be economically sound to compete in the context of the company's broader energy technology development objectives and strategies. In considering any investments – including long-term opportunities such as alternative energy – Chevron seeks to protect and further shareholder interest, and to ensure that the investments we undertake offer the potential to provide acceptable returns in an appropriate timeframe.

In addition to investing in the development of alternative energy technologies, Chevron installs solar and fuel cell energy systems for public and institutional customers through our Chevron Energy Solutions subsidiary. Chevron Energy Solutions is among the five largest energy services companies in the United States that provide these kinds of systems. Chevron is also demonstrating the application of very large-scale solar power systems for oil field co-generation. Finally, Chevron has developed more than a quarter of the world's geothermal energy and is currently the world's largest geothermal energy producer.

3. How much royalty relief have you received from the Department of Interior for exploration on public lands? Which public lands specifically? At what price threshold have you predicted internally that you would not need royalty relief to make exploration viable?

Answer: Since 2001, Chevron (Chevron, Texaco and Unocal) received an estimated $72 million of royalty relief on properties subject to Deep Water Royalty Relief and an estimated $20 million of royalty relief on properties subject to Shallow Water Deep Gas Royalty Relief. Within that same time frame, Chevron paid a total of approximately $2.8 billion in royalties to the federal government attributable to production from federal lands, both offshore and onshore. This $2.8 billion figure understates the total value of royalties paid by Chevron because it excludes the value of the large volumes of oil and gas delivered to the Government as royalty-in-kind.

Chevron received royalty relief on deepwater and shallow water Gulf of Mexico lease blocks. Since 2001, Chevron received Deep Water Royalty Relief on the following leases: Green Canyon Block 282 (off production since September 2005 due to hurricane damage); Mississippi Canyon Block 661 (off production since March 2005); Mississippi Canyon Block 705; Green Canyon Block 236 (off production since August 2004); Green Canyon Block 237 (off production since September 2005 due to hurricane damage); East Breaks Block 205; Garden Banks Block 409; Green Canyon Block 782; Green Canyon Blocks 562/563; and East Breaks Block 114 (off production since September 2002).

Since 2001, Chevron received Shallow Water Deep Gas Royalty Relief on the following leases: Grand Isle Block 90; South Marsh Island Block 217 (royalty relief volume limit reached in September 2005, royalties being paid since then); South Timbalier Block 136; South Timbalier Block 200; South Timbalier Block 35; West Cameron Block 54 Well; High Island Block 37 and West Cameron Block 48 (royalty suspension supplement received for drilling dry hole in excess of 18,000 feet true vertical depth).

Two other royalty relief programs may also apply to Gulf of Mexico leases. These are marginal property royalty relief and special case royalty relief. Our research to date indicates that Chevron has not participated in either of these programs.

Note that this response does not include information related to royalty rate reduction programs administered by MMS that are applicable to onshore public lands. These programs, which terminate this year, relate to the production of heavy crude oil and crude produced from "stripper wells."

While Chevron believes that current prices generally provide adequate incentive for today's deepwater exploration, we have not made any predictions around particular price thresholds. Chevron has always relied on the terms of its leases, including royalty relief where it applies, in evaluating project economics. Of course, individual exploration project viability and risk involve a complex set of economic, geologic, and other factors. We believe that the existing royalty relief program, which is limited to select leases, volumes and price thresholds, has worked well in achieving the purposes which Congress intended, namely to incent resource development on leases that may have otherwise gone undeveloped under economic conditions present at the time the royalty provisions were initially constructed. In fact, MMS has recently reported to Congress the success of its Deepwater Royalty Relief Program relative to increases in lease bonuses and drilling activity.

QUESTIONS FOR THE RECORD
SENATOR DEWINE

1. At our last hearing, we heard testimony that some of the gasoline price spikes can be attributed to regulations that create multiple grades of gasoline to comply with different environmental standards – so called "boutique fuels." What can we do to reduce the number of boutique fuels? What would be the effect of just requiring everyone in the industry to comply with the highest standard, and have just one fuel available?

Answer: It is important to bring fuel specifications into alignment with the regional manufacturing, supply and distribution systems. As a good initial step, legislation passed last year by the House of Representatives contains provisions that would limit the number of boutique fuels to a specific slate of 4 choices for gasoline and 2 for diesel fuel. Also, granting EPA more authority to temporarily waive and pre-empt state fuel requirements in situations like we experienced during the hurricanes last year will result in quicker response to such emergencies.

We do not believe having just one fuel at the highest standard throughout the U.S. is feasible, necessary or cost effective. Having one fuel of the highest standard would mean requiring the use of California Reformulated Gasoline Phase 3 throughout the U.S. Given the number of areas that are attaining air quality standards, it does not appear necessary or appropriate to impose that formulation everywhere when one considers the significantly higher costs involved with making it.

2. In the last couple of months most of the oil industry has announced record-breaking profits for the last fiscal year. How much is your company investing annually in exploration, production and refining, and when will we see those investments pay off? And perhaps most important, what are you investing in alternative energy sources so we can help reduce domestic dependence on foreign oil?

Answer: Over the past four years Chevron earned $36 billion and reinvested $36 billion in the business. Last year, Chevron had net reported earnings of $14.1 billion. Chevron's worldwide investment program for 2006 is $14.8 billion – 34% higher than 2005 spending.

For 2006, $11.3 billion of Chevron's total spending program is targeted for investment in exploration, production and natural gas-related projects, including $3.3 billion in the United States. About $2.8 billion of total spending is targeted for refining, marketing and transportation, of which $1 billion is in the United States.

The oil and gas business is very capital-intensive. For example, in our upstream business we currently have over 20 projects, each with net total capital costs exceeding $1 billion and 45 projects with net total capital costs exceeding $500 million. Most of Chevron's

major capital projects are large long-term investments that will take many years to reach payout. For example, it may take 7 to 10 years to bring significant new sources online, from discovery to production.

Chevron is working on developing many forms of alternative and renewable fuels and energy sources and investing the amount necessary to pursue those endeavors practically. Since 2000, Chevron has spent more than $1 billion to develop alternative and renewable energy technologies and deliver energy efficiency solutions. In the near term, energy efficiency or conservation is the cheapest and most reliable "new' source of energy. Chevron is spending more than $300 million each year to test and develop alternatives and renewable forms of energy, including hydrogen, geothermal, advanced hybrid batteries, wind, solar and biofuels.

QUESTIONS FOR THE RECORD
SENATOR FEINGOLD

1. The President mentioned in his state of the union address that America is "addicted to oil", and outlined several steps - including increasing investments in alternative fuels - to end the addiction. What percentage of your R&D is dedicated to alternatives? In your response, please indicate how your company defines alternatives. In addition to your R&D, what are your companies doing, as corporate citizens, to move away from fossil fuels?

Answer: Chevron concurs with the projections of the Department of Energy and others that conventional hydrocarbons, which include oil, natural gas, and coal, will continue to provide the vast majority of energy supplies for the next few decades. However Chevron supports the diversification and the development of alternative energy supplies and more efficient use of energy to reduce projected demand. Chevron defines "alternative fuels and renewables" to include: hydrogen, bio-fuels (ethanol and bio-diesel), power generated from geothermal, wind, solar, stationary fuel cells, and advanced battery storage. Approximately 1/3 of our total R&D expenditures in 2005 were directed to alternative fuels and alternative energy (excluding geothermal). The remaining 2/3rds of our total R&D expenditures were focused on promoting technology advancements and efficiencies for conventional hydrocarbons, which as noted, remain our current, and immediate future, energy sources.

QUESTIONS FOR THE RECORD
SENATOR KOHL

1. An independent study by the consumers group Public Citizen found that from 1999 to 2004 U.S. oil refiners increased their profits they made on each gallon of gas refined by 79%. Don't these statistics show that it is not merely the rising worldwide cost of crude oil that accounts for high prices and other petroleum products? And does the success of your industry in passing along rising crude oil prices to consumers demonstrate that your companies have gained market power and that there is a failure of competition in this market?

Answer: The answer is no to both questions. The oil industry competes in a global marketplace and is intensely competitive, as confirmed by numerous government investigations and studies. Consolidation has allowed the oil industry to improve its efficiency and to compete in this global marketplace, where economies of scale and large size are needed to make the enormous capital investments required. Recent merger activity occurred in the last two decades when oil prices were lower, and finding additional efficiencies and deploying capital most effectively was critical to remaining competitive. Chevron's share of U.S. refining capacity has decreased from 6.8% in 1995, to a 5.4% share in 2005.

In addition, it should be noted the statement by Public Citizens referring to refiners' profits is not accurate. The statement relies on statistics published by the Energy Information Administration ("EIA") showing the difference between average refinery costs to acquire crude oil and average prices at which refineries sell gasoline to resellers. This is a "gross margin; " it does not represent refinery profits because other costs associated with manufacturing products (e.g. the cost of fuel to operate the refinery, catalyst costs, manpower costs, etc.) are not included in that particular calculation.

2. In most competitive industries, when there are high prices, high profits to be made, and soaring consumer demand, we would expect to see an expansion of capacity to meet this demand. Yet in the oil industry this has not happened. Instead of opening new refineries, the industry has closed more than half of all that existed 25 years ago. In 1981, there were 324 refineries operating in the United States – today there are 149. According the Department of Energy, in the period from 1981 to 2004 overall national refining capacity has declined by more than 9% while demand for gasoline rose by 37%. Oil industry critics suggest that this decline in refining capacity is no accident – that oil companies actually prefer to keep supplies tight in order to be able to gain market power to raise price. Indeed, many economists believe this is a central reason why gas prices are so high.

So why hasn't your industry opened new refineries while closing so many existing ones? Does the failure of the oil industry to open new refineries suggest an effort to keep supplies tight or something anti-competitive going on?

Answer: During the 1980s and early 1990s, the industry had spare refining capacity and was faced with the requirement to invest significant amounts of capital to comply with more stringent environmental regulations. In certain cases, it was uneconomic to make those incremental investments, which resulted in the closure of some refineries.

While it is true that the number of refineries has steadily decreased, total U.S. refining capacity has, in fact, increased (see Attachment D in Chevron's Written Testimony to the Judiciary Committee). Although no new refineries have been built for some time, many existing refineries have become larger, more efficient, and more complex (better equipped to handle less desirable but more readily available heavy and sour crude slates). A combination of the high cost to build a new refinery (billions of dollars), economic and regulatory uncertainty, lengthy and convoluted permitting processes, and lack of

acceptance from neighbors, all create significant disincentives for constructing new refineries and at times limit expansion of existing facilities.

3. In the last 15 years there has been a tremendous amount of consolidation in the oil industry – the GAO counts 2600 mergers and acquisitions in this industry since the 1990s alone. Indeed, almost all the companies represented here today are a product of these mergers. During this time, the FTC has approved most of the oil industry mergers it has reviewed, including the gigantic ones like Exxon/Mobil, Chevron/Texaco, and Conoco/Phillips. While each one of these mergers may not have seemed problematic when reviewed, taken as a whole these mergers have greatly increased concentration in the industry. And the GAO has concluded that these mergers have raised gasoline prices.

(3a) What is your view of the effects of these mergers on competition in your industry and the price of petroleum products?

Answer: We believe that the referenced mergers as approved by the FTC with associated mandated divestitures were not injurious to competition. Industry structure varies greatly from industry to industry, and depends upon the costs of entry, capital intensity, technology, economies of scale, historical developments, the regulatory environment, and many other factors. The true level of competition in an industry often depends more upon these factors than on the number of mergers or on formal industry concentration measures. In fact, many industries, including automobile manufacturing, aircraft manufacturing, and home center retailing, are more concentrated than the petroleum industry.

The petroleum industry is very capital intensive and the leading companies operate globally; hence, they are very large in size, but their shares of market within regional and local distributive areas in the U.S. are well within competitive norms.

The market price of petroleum products derives from the price of crude oil and other inputs to the refining process and the supply of and demand for petroleum products. Chevron mergers have resulted in operating expense reductions, optimization of capital and exploratory expenditures, and having greater technical, financial and other resources available to most efficiently pursue large project development to bring new energy supplies to market in a manner that benefits both stockholders and consumers. Also as noted in Chevron's written and oral testimony – despite periods of volatility – gasoline prices have increased at a lower rate than many other consumer goods and services over the past 35 years.

(3b) Are we likely to see even more consolidation in the years ahead? If so, what will this mean for competition in this industry?

Answer: It is impossible to predict whether we will see more consolidation. Many capital intensive industries have tended to consolidate over time, but technological developments, changing economics and divestitures have created new competitors. We are now in a period of great change in the energy sector. With significant investment needed to provide new energy

supplies and to develop new technologies and alternative fuels, it is likely the industry will continue to evolve, which may include additional merger activity.

Attachment 1
Comments on Draft Bill "Petroleum Industry Antitrust Act of 2006"

Section 2: Unilateral Supply Decisions: The bill could outlaw legitimate, efficiency-enhancing decisions that are appropriate responses to supply and demand conditions through its intent-based standard for establishing antitrust violations. For example, if this legislation had been in effect in 2005, a company would have exposed itself to the risk of liability if it had chosen to move supplies from the Pacific Northwest and Northeast to Hurricane-impacted areas of the U.S., where prices might have been higher due to supply disruptions. That is because the draft bill provides that an illegal intent to violate the antitrust laws can be demonstrated if the price a supplier obtains from moving product is greater than the price obtained where the existing supplies are located. This form of antitrust regulation, which seeks to define "intent" with reference to cost and price variables, is subject to gross misinterpretation. It runs counter to the general direction of antitrust law, which has come to focus on market power and competitive effects.

Sections 3 and 4: Merger Review: The overall goal of the draft merger provision is to reduce the burden of proof with respect to merger prosecutions from "substantially lessen competition" to "appreciably diminish competition." The phrase "substantially lessen competition" benefits from more than 50 years of Supreme Court precedents, as well as the well-established enforcement practices of the federal agencies under the economic tests of the Merger Guidelines. While the new language obviously must be intended to mean something different, it would take years of litigation to transform this ambiguous language into something that could be effectively and fairly applied by courts.

Moreover, industry-specific rules, particularly those dealing with mergers and acquisitions, tend to strand capital, distort investment incentives, and disadvantage U.S. competitors relative to international firms. Existing antitrust laws have proven to be sufficiently broad and flexible enough to address competitive problems across the full range of industry settings. These laws, including the procedures for premerger notification and review, have served our country well, and the U.S. model has been widely adopted around the world as a best practice. A recent Federal Trade Commission study of oil and gas mergers concluded that in applying the "substantially lessen competition" standard federal agencies have been more stringent in the oil industry than in most other industries – i.e., they have tended to challenge oil and gas industry mergers resulting in lower levels of concentration than in other industries. Competition remains intense, and mergers have helped firms like Chevron remain competitive in an increasingly global marketplace, where we compete against larger and increasingly aggressive foreign -- including many state-owned -- oil companies.

Section 5: Information Exchanges: The draft bill proposed to create a joint federal and state task force to review the scope of information exchanges occurring among industry participants. Chevron will comply with any obligations the company

may have regarding any information requests if a task force is formed, but it is not clear to us why a task force is necessary. In general, markets with more transparent information flows function more efficiently, encourage competition, and prevent distortions. By contrast, a lack of information can result in a poorly functioning market or facilitate market manipulation. Most commonly, firms might share information with a competitor that is related to a joint venture, joint production arrangement, or other legitimate collaborative activity in which both are involved. This is both normal and necessary in an industry that depends heavily on joint venture activity of various kinds to develop energy resources.

Information exchange within the oil and gas industry has been frequently investigated by federal and state antitrust authorities with virtually no meaningful enforcement actions. Thus, this feature of the bill seeks to address what has proven to be a non-issue. The costs of further investigations will simply increase industry compliance costs with no corresponding public benefit.

Section 6: NOPEC: Chevron has concerns that, as drafted, the legislation could outlaw legitimate joint venture and other collaborative activities between Chevron and national oil companies. The bill prohibits any joint action "to set or maintain the price" of petroleum products, but as the Supreme Court recognized in its recent *Dagher* decision, a joint venture must set the prices of the products it produces and sells. Thus, while Chevron certainly applauds the desire to improve the competitiveness of the world crude market, it is not clear to us that this will actually accomplish that purpose without some unforeseen and presumably unintended consequences. The relationships between the United States and the OPEC nations are complex, encompassing a broad range of security, geopolitical, economic and other foreign policy considerations. The draft legislation addresses only one dimension of that relationship. As a private company, Chevron is not privy to the facts that might influence those relationships and thus would not opine as to whether such legislation would be in the best interest of the United States. Ultimately, Chevron believes it is important for the United States government to constructively engage other governments, to ensure access to resources and to help open up the additional sources of energy the world needs.