



Carbon Asset Risk Hess Corporation Annual Meeting: May 2, 2015, Houston, TX

RESOLUTION

RESOLVED:

Shareholders request Hess to prepare a scenario analysis report by September 2015, omitting proprietary information, on the Company's strategy to address the risk of stranded assets presented by global climate change and associated demand reductions for oil and gas, including analysis of long and short term financial and operational risks to the company.

SUPPORTING STATEMENT:

We recommend the report:

- Evaluate a range of low-carbon, low-demand scenarios, including a scenario in which two thirds of reserves cannot be monetized;
- Provide an assessment of different capital allocation strategies for the low-demand scenarios including diversifying capital investment or returning capital to shareholders;
- Provide information on carbon price and crude oil price assumptions used in each scenario.

GUIDELINES – Guidelines suggest a recommendation in favor of resolutions requesting a company to disclose information on the impact of climate change on its operations and investments, considering whether a company already provides current, publicly available information on the impacts climate change may have on the company, as well as associated company policies and procedures to address related risks and/opportunities.

In applying these guidelines, investors and analysts should make a distinction between the different impacts that climate change can have on a company, and whether a company has provided information on the type of climate change impact requested by shareowners. Climate change impacts can broadly be assessed in three categories: (1) Risks to physical assets and operations, including climate change's potential to harm company assets such as plant, property and equipment. This may include damage caused by intense storms that shut down drilling platforms or hurricanes that limit the ability to ship product or supplies. (2) Risk associated with reputational damage to brand and goodwill from climate change denial activities, or undermining reasonable environmental policy. (3) Carbon asset risk, i.e., the risk that a company's fossil fuel reserves and associated infrastructure will be devalued such that the assets become stranded and are subject to premature write downs or devaluations. Stranded assets can result from climate-related demand reductions associated with climate change regulations, and from product substitution in response to the need to respond to climate change, among others.

Thus, risks from climate change result from differing causes, affect different parts of a business, and entail different solutions. For example, a solution to physical risk might be to develop infrastructure that can withstand hurricane-level winds or a sea level rise. Whereas a solution to stranded asset risk might be to assess how to avoid production and development of reserves that are uneconomic, diversifying capital expenditures into new energy sources, or returning capital to investors. Similarly, adopting greenhouse gas targets to reduce a company's own carbon pollution, while important, is distinct from addressing stranded asset risk. Simply put, one solution to a given climate change risk does not necessarily solve another. Both shareowners and companies must exercise care to differentiate climate change risks and the respective solutions to reduce those risks.

SHAREHOLDER CAMPAIGN

A shareholder initiative was begun in September 2013, which has been adopted by the Global Investor Coalition, in which shareholders representing \$23 trillion in assets under management have asked 45 coal, oil and gas, and utility companies for increased disclosure about whether they are addressing carbon related asset risk, the impact of companies' capital expenditure decisions in light of these growing risks, and how the companies are prepared to manage risks under these scenarios.

RATIONALE FOR A YES VOTE

Summary: This proposal asks Hess Corporation to analyze certain risks associated with an increasingly carbon-constrained energy market, including scenarios for low probability, but high impact events such as global government adoption of rigorous climate change regulations, and high probability, high impact events such as disruptive, low-carbon technologies leading to large-scale adoption of cleaner energy sources. These scenarios will result in decreased demand for fossil fuels and lower fossil fuel prices, creating risk of stranding of certain high cost or high carbon assets.

Despite the increasing potential for carbon associated asset risk, oil and gas companies continue to spend hundreds of billions of dollars each year on finding and developing high-cost fossil resources. Further, industry production costs – and risk -- are rising as companies invest in more remote and difficult to extract carbon reserves. Kepler Cheuvreux has declared this trend a “capex crisis,” noting that, since 2005, annual upstream investment for oil has increased by 100 percent, while crude oil supply has increased by only three percent. Given the generally high production costs of the newest sources of oil (including deep water and those that require hydraulic fracturing,¹) proponents are concerned that the industry in general, and Hess in particular, is vulnerable to scenarios in which demand for oil and gas declines along with prices.

¹ <http://www.npr.org/2014/11/04/361204786/falling-oil-make-fracking-less-lucrative>

These concerns are amplified in a market with already falling oil and gas prices. Proponents recognize Hess' vulnerability to scenarios in which demand for its resources decline, potentially precipitously and ask Hess to: evaluate a range of low-carbon, low demand scenarios; provide an assessment of different capital allocation strategies, including diversifying capital investment or returning capital to shareholders; and provide information on critical assumptions used in such analysis, including price assumptions. Investors need to know more about Hess' planning for adverse market conditions, and the basic assumptions Hess uses to predict future demand and market prices. It is only with these disclosures that investors can understand and assess the risk of Hess' reserves becoming uneconomic to produce over short, medium, and long-term price horizons.

Hess Is Particularly Exposed To Carbon Asset Risk

Proponents and third parties recognize that Hess is particularly exposed to scenarios in which demand for oil and gas resources decline. In order to sustain shareholder returns in a low price, low demand market, companies' focus is best directed at low cost projects, deferring or cancelling projects with high breakeven costs.² Hess' 2014, \$5.8 billion exploration and production budget was invested approximately 50% in unconventional shale resources and 20% in deep water development.³ Shareholders are concerned that high cost, deep water and unconventional shale projects could prove to be low return assets in a low-demand scenario. Shareholders have asked Hess to analyze a range of such scenarios to assess whether deferring or cancelling some range of these projects might better protect shareholder returns. Analysts at Morningstar have noted that Hess' 2008-13 capital efficiency (arguably the most important metric in oil and gas, given its high capital intensity) was one of the worst of its peer group."⁴ The company itself notes that "...our initiatives are positioned to make 5% to 8% compound average annual production growth through 2017, off of our 2012 pro forma base, and to generate free cash flow post 2014 based upon \$100 Brent."⁵ Shareowners' question to Hess is what will happen to the company in a lower-priced market.

CHANGING MARKETS

Falling Demand for Fossil Fuels – In developed nations, demand for oil has fallen since 2005 as a result of more efficient vehicles and demographic trends that have seen car ownership and car use peak.⁶ A March 2013 Citi report cites to a number of trends indicating that "oil demand is approaching a tipping point" and that it may occur sooner than predicted, potentially leveling off by 2020.⁷ Chief among such factors is increased fuel efficiency, which has an outsized impact because transportation accounts for 60

² Carbon Tracker Initiative, *Oil & Gas Majors Fact Sheet*, p. 1, <http://www.carbontracker.org/wp-content/uploads/2014/09/CTI-Oil-Gas-Majors-Company-Factsheets-August-2014-FULL.pdf>.

³ Hess Corporation. *Hess Corporation Announces 2014 Capital and Exploratory Budget* (Jan, 2014).

<http://phx.corporate-ir.net/phoenix.zhtml?c=101801&p=irol-newsArticle&ID=1893181&highlight>

⁴ Morningstar. Hess Corp: Investment Thesis. (August 2014).

<http://analysisreport.morningstar.com/stock/research?t=HES®ion=usa&culture=en-US>

⁵ : Hess Corp. (HES) Q1 2014 Earnings Call Corrected Transcript: Apr 30, 2014

<http://www.thestreet.com/story/12695327/1/hess-corp-hes-q1-2014-earnings-call.html>

⁶ *Yesterday's fuel*, The Economist, <http://www.economist.com/news/leaders/21582516-worlds-thirst-oil-could-be-nearing-peak-bad-news-producers-excellent>;

⁷ <http://www.bloomberg.com/bw/articles/2013-05-01/peak-oil-is-back-but-this-time-its-a-peak-in-demand>

percent of global oil use. Other factors include emerging alternatives to gasoline including natural-gas powered trucks and plug-in-electric vehicles. The IEA⁸ and Deutsche Bank forecast global oil demand could peak in the next ten to fifteen years.

Natural gas price volatility – As of January of this year, natural gas prices had dropped to their lowest levels since September 2012, reflecting domestic overproduction and inventory buildup.⁹ Future demand for natural gas is also unclear; natural gas is threatened by the same market forces as those that affect oil and coal, and the impacts of hydraulic fracturing are subject to particular scrutiny. Natural gas has also been forecast to peak by 2020,¹⁰ and many gas plays have been overestimated, and or are being exhausted ahead of schedule.¹¹

Global Movement Toward Renewable Resources – Low carbon solutions have been adopted by consumers at a higher rate than most analysts predicted, and costs have come down faster than predicted. Renewable energy adoption levels have been unprecedented, putting the transition to a low carbon economy six years ahead of schedule.¹² Bloomberg's 2030 Market Analysis predicts that, "[b]y 2030, the world's power mix will have transformed: from today's system with two-thirds fossil fuels to one with over half from zero-emission energy sources."¹³ Deutsche Bank predicts that that solar systems will be at grid parity in up to 80 per cent of the global market within 2 years.¹⁴ As prices of renewable energy become equal to or less than fossil fuels, an aggressive shift to these forms of energy is likely to occur due to benefits including low and predictable fuel and power costs, ease of scalability and distribution, reduced regulatory risk, and environmental and public health benefits.

Growing Carbon Constraints - The International Energy Agency, in its 2012 World Energy Outlook, recognized that no more than one-third of proven reserves of fossil fuels can be consumed prior to 2050 if the world is to have a chance at limiting warming to 2 degree Celsius, the level beyond which severe consequences occur for economies, market participants, and the environment. Global governments have acknowledged this limit as a policy goal, and are amidst negotiations to achieve it. The principal means to halt, mitigate, or slow climate change is to reduce carbon emissions which are caused primarily by fossil fuel use. Thus, laws and regulations adopted to limit carbon emissions and stave off climate change impacts will have the effect of reducing fossil fuel use, affecting producer competition,

⁸ See "Oil's Black Swans on the Horizon," WSJ (<http://www.wsj.com/articles/oils-black-swans-on-the-horizon-1424108038>)

⁹ <http://www.eia.gov/todayinenergy/detail.cfm?id=19751>

¹⁰ "US natural gas production could peak in 2020; Research project forecasts much less production than government estimates," ARS Technica, Dec. 4, 2014

<http://arstechnica.com/science/2014/12/us-natural-gas-production-could-peak-in-2020/>; see also "Who to Believe: U.S. Natural Gas may Peak in 2040. Or 2020," Money Beat (Dec. 4, 2014).

<http://blogs.wsj.com/moneybeat/2014/12/04/who-to-believe-u-s-natural-gas-may-peak-in-2040-or-2020/>

¹¹ See "Natural Gas: The Fracking Fallacy: The United States is banking on decades of abundant natural gas to power its economic resurgence. That may be wishful thinking," Nature (Dec. 3, 2014).

¹² <http://www.bloombergvew.com/articles/2015-04-08/clean-energy-revolution-is-way-ahead-of-schedule>

¹³ 2030 Market Outlook, Bloomberg New Energy Finance,

<http://bnf.foliohack.com/document/v71ve0nkr8e0/who42hnkr8fo>

¹⁴ See <http://cleantechnica.com/2015/01/14/deutsche-bank-predicts-solar-grid-parity-80-global-market-2017/>

commodity prices, and raising the cost of doing business. These effects are likely to leave the vast majority of fossil fuel companies with significant stranded assets in the form of uneconomic reserves and underused infrastructure.

Taken together, these fundamental changes in energy markets suggest that demand for oil and gas will decrease over time, reducing commodity prices, and increasing the risks and uncertainties around investing shareholder capital in developing new fossil fuel assets. Shareowners ask the Company to evaluate a range of low-carbon, low-demand scenarios and describe how the Company is positioned to address these coming changes in energy markets.

Inadequate Discussion of Stranded Asset Risks by Hess

Hess has generally noted in its 10K, website, and other reporting that “climate change initiatives may result in significant operational changes and expenditures, reduced demand for our products and adversely affect our business” and other similar statements. Hess has also adopted greenhouse gas emission reduction measures and other climate-change related policies. Yet, neither these disclosures, nor the greenhouse gas reductions measures Hess has undertaken are responsive to this Proposal.

While Hess acknowledges the risks raised in the Proposal, including risks associated with climate change regulations, shifting demand, and competition from renewables, Hess provides no quantification of likely impact, no analysis of the extent to which such regulations/risks could affect the company’s value, or whether or how the company plans to address such risks. *Mere statements that “these agreements and measures may require significant equipment modifications, operational changes...” and other actions does not substitute for rigorous analysis of whether the company is prepared to adjust its operations accordingly.* Given the likelihood that these identified risks have the potential to dramatically affect shareholder value, especially given Hess’ investment in high-cost unconventional and deep water reserves, shareholders are asking Hess to undertake the requested scenario and related analysis.

Knowing that the company has evaluated these potentially low likelihood, but high impact events, such as a 2 degree carbon regulation, or the more likely carbon-related reductions in demand, and assessed how these events may impact the company’s business, is important to shareholders. Companies that have undertaken such analysis, using a range of demand and price scenarios, and that have developed plans to address the impacts are more likely to survive and remain profitable. Moreover, this analysis is likely to shed light on the future value of investing additional capital in high cost resources versus investing in alternative activities, or returning shareholder to investors. Shareholders also seek disclosure of the range of assumptions underlying this scenario analysis, including for instance carbon price, breakeven price, and other assumptions critical to this type of scenario planning.

RESPONSE TO HESS ARGUMENTS

Hess’ Opposition Arguments are as follows:

- 1) The company recognizes the importance of addressing the environmental, social and business impacts of carbon emissions and climate change and publishing annual sustainability reports

including a discussion of the company's policies and goals in addressing the risks and opportunities for the company presented by climate change and the changing market for energy products and services.

The company's 2013 CSR provides details of the company's achievements in regard to its climate change strategy and introduces goals for 2014 including; "refresh our climate change strategy," "reduce our flaring rate at the wellhead in North Dakota to 10 percent no later than 2017" and "reassess our Scope 3 emissions inventory and material Scope 3 categories for reporting in 2014." Many of Hess' goals address climate change and greenhouse gas emission concerns, and are therefore important. Emission reduction goals and statements recognizing risk and opportunities do not, however, substitute for the scenario planning and financial risk analysis requested by this proposal. Proponents are seeking more than mere statements.

- 2) In its 2013 sustainability report, the company cites to a variety of forecasts from which it concludes that there is not a substantial risk that its reserves will not be monetized, and that markets are currently valuing carbon assets rationally.

While this information clarifies the company's position on the likelihood that a 2 degree regulatory limit will be imposed, the company has failed to prepare an analysis of this event or other low demand, low price scenarios associated with carbon-related demand reduction drivers and the impact these changes would have on the company if they occurred. For instance, even though the IEA predicts fossil fuels would comprise 60% of world energy use under the 2 degree scenario, a 40% reduction of demand compared to a business as usual scenario would likely have dramatic effects on global supply and selling price, particularly for higher cost reserves, thus creating ramifications across the entire industry and greatly effecting this company's performance.

The Proposal asks for the requested assessment even if the company believes such an outcome is unlikely. The precipitous and generally unpredicted drop in oil prices over the past year has demonstrated that price declines can occur suddenly and will adversely affect companies.

The report requested will provide information to investors as to whether or not Hess' strategic investment decisions have made carbon asset risk a non-substantial concern. Additionally, as noted above, many investors, including long term institutional investors, understand carbon asset risk to be an important factor to consider, reflecting an increased prioritization on climate-associated risks. The Bank of England has publically addressed carbon asset risk and the potential for stranded fossil fuel assets in its *One Bank Research Agenda* noting that climate change presents "for central banks to consider, including the potential for carbon intensive assets becoming 'stranded.'"

- 3) Hess states that "[t]wo of Hess' key enterprise processes, Enterprise Risk Management (ERM) and Value Assurance (VA), incorporate non-technical risk considerations, including climate change risk, and account for the cost of carbon in the VA process for major new projects.

Shareholders appreciate that Hess utilizes an asset-level risk assessment process and value assurance process, but this has not resulted in the assessment requested here. Hess specifically responds with “no” to the CDP question, “Do you conduct any scenario analysis based on a low-carbon scenario consistent with reducing GHG emissions by 80% by 2050 to achieve the 2°C goal...?” Hess also leaves questions unanswered in the CDP report which are relevant to disclosing risks of stranded assets, such as details of capital expenditures and the total expected return on capital allocation in such scenarios. If Hess had performed other low demand analyses, it fails to disclose to shareowners the results, or its key planning assumptions which are necessary for shareholders to assess the extent to which the company has minimized risk associated with low demand scenarios. Moreover, Hess fails to provide requested information regarding its capital allocation process and whether it would continue to invest in high cost deep water and unconventional resources given a low-demand scenario. In sum, despite its standard planning processes, Hess provides shareholders with no detailed information on the short and long-term financial risks associated with low demand scenarios and does not give information on the ability to economically monetize assets in these scenarios.

- 4) Hess also argues that the requested analysis would be speculative and risk confusing and misleading investors about the company’s actual performance.

The scenarios requested are widely acknowledged as possible. Although reaching a global agreement to avoid global temperature rise may appear to be a remote possibility, its impact on fossil fuel energy companies would be high, as would demand reductions associated with carbon-related technologies and increasingly low cost renewables. The Proposal does not require that Hess merely speculate about these possibilities. Multiple recent studies have assessed the magnitude of stranded asset risk and the impacts to the value of coal, oil, and gas assets of not burning 2/3 of worldwide fossil fuel reserves, as well as other low demand scenarios. Far from being speculative, this proposal asks Hess to undertake an analysis of a scenario that has been considered and studied by many scientists and policy makers; including the IPCC, IEA, UN, while assessing the specific impact on the company.

The analysis and planning called for by this resolution is a reasonable undertaking. Proponents acknowledge that there is no certainty on this issue, but the lack of certainty does not excuse inaction. The company is fully equipped to provide a range of reduced demand/usage scenarios, to describe how each scenario would financially affect the company, and to provide information regarding how, or whether, the company plans to address those risks and in what circumstances.

Further, studies and information exist to assist the company in projecting these types of scenarios such as the demand-by-fuel-type included in the 2014 World Energy Outlook prepared by the IEA. Bloomberg also provides a tool that can assist companies in predicting carbon asset risk. In sum, proponents are not asking Hess to randomly speculate or to accurately predict the future, but to use its planning teams to assess risks and to provide shareholders with information about how the company is prepared to withstand or make use of opportunities related to carbon constrained, low demand scenarios. This information, if appropriately discussed as a scenario analysis, is not likely to mislead shareholders.

PEER COMPARISON

In 2014, ExxonMobil publicly agreed to issue a report on carbon asset risk. Although this report only met shareholder requests on the margins, it was the first company to undertake the task. Shell and BP have made public statements that they are supporting similar shareholder proposals addressing the financial risk and investment strategies associated with low demand scenarios.

CONCLUSION

The information requested in this proposal is important to shareholders. In order to effectively manage risks associated with the potential for stranding of reserves and associated assets due to climate change drivers, shareholders need to be fully informed of if, or how, the company is planning for a carbon constrained future and whether it is addressing the risk of stranded reserves. This valuable information will enable investors to analyze how the company is positioned to address climate change and carbon restrictions and to make reasonable judgments about the benefits or risks associated with investing in this company.