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Comment Letter No. 698

HESS CORPORATION

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International Accounting Standards Board
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Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: **Proposed Accounting Standards Update- Leases (Topic 840)**

Dear IASB/FASB Board members:

Hess Corporation (Hess or the Corporation) appreciates the opportunity to comment on the Proposed Accounting Standards Update on Leases (Topic 840) "ASU". Hess is a global integrated energy company primarily engaged in the exploration for and production of crude oil and natural gas, the manufacturing of refined petroleum products and the purchasing, trading and marketing of refined petroleum products, natural gas and electricity. The Corporation is supportive of developing a converged lease accounting standard for both IFRS and U.S. GAAP; however, we believe that there are still additional clarifications and outstanding issues that need to be resolved in order for the proposal to be operational. We have not provided responses to all of the questions set out by the Board, but directed our comments to specific sections of the ASU that would likely have the most significant impact on the Corporation.

1. Definition of a lease and distinguishing leases from service contracts

We believe that the definition of a lease as currently described in the proposal requires additional clarification. An area of particular concern is understanding how to distinguish a lease from a service contract. We believe that the criteria currently set forth in paragraphs B1 through B4 of the proposed ASU would be difficult to practically apply to service arrangements that are common in our industry. These types of third party service contracts are typically used to deliver commodity products to customers (through the use of pipelines or tankers) and for drilling oil and gas wells.

Product transportation service agreements may contain both fixed and variable cost elements. For example, a pipeline agreement could include a fixed fee representing a right to transport a certain volume of product through a pipeline within a specified time period and additional variable costs that are incurred only when the capacity is utilized. In general, the volume

associated with the fixed fee under the agreement does not represent a significant portion of the total capacity of the pipeline. Furthermore, we do not control or operate the pipeline asset under the terms of these third-party service arrangements. Based on our interpretation of the criteria set forth in paragraphs B1 through B4 of the proposed ASU, we believe that most product transportation service arrangements would be accounted for as service agreements instead of leases, which in our view is consistent with the underlying business purpose of obtaining a service to deliver a product to a customer. However, we believe that without additional clarification there is a significant risk of diversity in practice when making the distinction between a lease and service contract.

We note the scope exclusion provided for leases to "explore for or use minerals, oil, natural gas and similar non-regenerative resources". However, it is not entirely clear whether this exclusion applies solely to leases for mineral rights or whether it also extends to other arrangements such as drilling rig service contracts. If drilling rig service arrangements are within the scope of this proposed ASU, it would conflict with the existing accounting requirements for oil and gas activities required by ASC 932 (formerly FAS 19). Under these existing requirements, undiscounted daily rig costs (the "day rate") are initially capitalized as suspended well costs during drilling. The well costs are then assessed under the successful efforts method and either continue to be capitalized as part of an oil and gas discovery or are expensed as a dry hole. If the drilling rig service contract is capitalized as an asset on a discounted basis at the inception of the agreement under the proposed ASU, we believe there will be unnecessary complexity and the potential for diversity in practice in attributing drilling rig costs to wells as they are drilled. We believe the final ASU should either specify the required accounting treatment when the proposal conflicts with industry specific accounting requirements or clarify that the accounting for a capitalized lease asset should fall under the scope of industry specific standards if different from the proposed ASU.

In addition, drilling rig service arrangements typically vary depending on the type and location of the well being drilled. Under certain arrangements a drilling rig might be specifically identified in the agreement while in other arrangements only general technical specifications of the drilling rig would be included and substitution would be permitted. This could lead to different accounting depending on the type of drilling rig service arrangement. Because of the specialized nature of extractive industry accounting, the potential for diversity in practice and the unintended consequences which may result from the proposed ASU, we believe the scope exception for leases to explore for or use oil or natural gas should be extended to drilling rig contracts.

An additional area of confusion is identifying the appropriate unit of account for assessing the right to use an asset. An asset can have multiple sub-components, some of which could be controlled by a single lessee while the asset in its entirety, may not. A simple example would be in a typical office lease arrangement. If a lessee rented one floor of a fifty story office building, they would have control of their floor, but would not control the building as a whole, nor would they likely have more than an insignificant portion of the output or utility of the building. Therefore, would the asset be defined as the leased floor or the entire building? We recommend that this issue be addressed in the final ASU.

2. Lease term, contingent rentals and expected payments

We believe that the determination of a lease term should be based on the longest possible period that is probable (rather than "more likely than not") of occurring at the inception of a lease and should be subsequently modified if and when that assumption changes. With regard to

contingent rentals and term option penalties, the Corporation believes that they should only be recorded when either earned by a lessor or incurred by a lessee. The proposed expected outcome technique is complex, requires an extensive use of estimates and judgment that could vary significantly by entity. For these reasons, we believe that the measurements resulting from this proposed technique would not be considered useful information by our financial statement users due to the uncertainty of the assumptions on which they are based and would not be justified from a cost-benefit perspective.

3. Reassessment

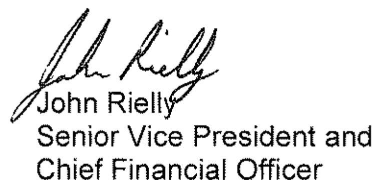
Hess believes that the proposed continuous reassessment requirement would be an overly burdensome undertaking that would require an extensive amount of time, incremental resources and likely require major systems modifications. Similar to the above, we question the cost-benefit justification for a continuous reassessment. We believe that a more simplified and practical approach is warranted especially given the condensed quarterly reporting timeframe that large accelerated public companies like Hess are now operating within. In our opinion, it is not reasonable to expect an entity to make a complete quarterly reassessment for each individual lease. The Corporation believes that an annual reassessment is a more reasonable approach and that interim adjustments would only be recorded when material changes have occurred based on known external factors (such as inflation indexed rent escalations) or significant contractual modifications.

4. Implementation issues

The Corporation does not believe that retrospective adoption of this proposal is the most practical transition option. We believe that prospective adoption is the more appropriate approach. A prospective transition method would more clearly highlight to a financial statement reader the impact of adoption on the face of the financial statements given the new line items that would be required under this proposed ASU. In addition, we believe that to adjust prior periods for leases which potentially could have expired or have been modified, would not be meaningful information to a financial statement user and would add an additional layer of complexity. It would also place a further strain on valuable resources and we question whether the benefits of a retrospective adoption would outweigh the incremental impact to the already anticipated significant implementation costs.

Thank you for the opportunity to provide comments on this proposed ASU. I would be pleased to discuss our views with you at your convenience.

Sincerely yours,



John Rielly
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