TESTIMONY OF JOHN S. CHALSTY
CHAIRMAN, EXECUTIVE COMPENSATION
AND HUMAN RESOURCES COMMITTEE OF THE
BOARD OF DIRECTORS OF OCCIDENTAL PETROLEUM CORPORATION,
BEFORE THE U.S. SENATE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

Chairman Levin, Ranking Member Coleman, and Members of the Subcommittee:

Thank you for inviting me to participate in today's hearing. I look forward to a constructive dialogue about these issues.

My name is John S. Chalsty. I have spent most of my professional career working in investment banking and finance. From 1986 to 1996, I served as President and Chief Executive Officer of Donaldson, Lufkin & Jenrette, Inc., and I served as Chairman of that firm from 1996 to 2000. Since 2003, I have been Chairman of Muirfield Capital Management LLC, an asset management firm. Since 1996, I have served on the Board of Directors of Occidental Petroleum Corporation, and I currently serve on the Board of Directors of several other companies in a variety of industries. In connection with my service on the Board of Directors of Occidental Petroleum Corporation, I currently serve as Chairman of Occidental's Executive Compensation and Human Resources Committee, generally referred to as the Compensation Committee.

Introduction

Before discussing generally Occidental Petroleum Corporation's policies and procedures regarding stock options, I would like to emphasize two important points. First, the Compensation Committee only grants stock options pursuant to plans that have been approved by Occidental's stockholders, and the company fully discloses to its stockholders the granting of such stock options as required by law and regulation. The granting of stock options to officers and employees of Occidental Petroleum Corporation is a longstanding practice that is well-understood by the company's stockholders, who have seen the company's management transform and re-focus Occidental from 1990 to 2006. During that period, the company has increased core profits from $191 million to more than $4.3 billion, reduced debt by 65% from more than $8 billion to less than $3 billion, and increased its stock market value by 650% to $41 billion. Occidental's transformation increased the oil and gas sales from 17% of total sales in 1990 to 72% in 2006. The use of stock options as a part of the company's compensation program is not a surprise to our stockholders, the investment community, regulators, or the public.

Second, throughout this period the company's treatment of stock options for both tax and accounting purposes complied fully with all applicable laws, rules, and regulations – and no one has contended otherwise. Prior to the adoption of Statement of Financial Accounting Standard ("FAS") No. 123R on July 1, 2005, Occidental Petroleum Corporation accounted for stock awards pursuant to APB 25. Because all stock options awarded by Occidental are granted "at the money," there was no "intrinsic value" to record as expense at the time of the grant. Beginning on July 1, 2005, Occidental Petroleum Corporation accounted for stock awards, as all companies are now required to do, pursuant to FAS 123R and reported their "fair value" as expense in its publicly available financial statements. No stock options were ever backdated, and no restated SEC financial statement filings have been required in the last 15 years.

Likewise, Occidental Petroleum Corporation has complied fully with all federal, state, local and foreign tax laws and has deducted from its tax returns only those amounts related to employee stock option exercises as is permitted by law. The result of this compliance with the law has been that over the past five years, from 2002 to 2006, Occidental has paid more than $4 billion in corporate income taxes in the United States. In sum, Occidental Petroleum Corporation is a successful United States company that complies with the law and pays substantial taxes. Again, no one has contended to the contrary.

Occidental's Policies and Procedures for Granting Stock Options

As the Subcommittee has requested, I would like to provide a brief overview of Occidental Petroleum Corporation's policies and procedures for granting stock options to its executives. Stock options are granted by the Compensation Committee of the Board of Directors. Pursuant to its written charter, the Compensation Committee is made up entirely of independent directors. Among other things, the Compensation Committee makes recommendations to the Board of Directors with respect to incentive-compensation plans and equity-based plans and administers the stock-based compensation plans of the Corporation that have been adopted by the Board from time to time. The Compensation Committee performs many tasks in connection with this role, including, but not limited to, selecting participants, making grants and awards, setting performance targets, and interpreting the terms and provisions of the Plans. The Compensation Committee, as it deems appropriate, may engage special legal or other consultants to report directly to the Committee.

All new stock plans and amendments to existing stock plans must be reviewed by the Compensation Committee before being submitted to Occidental's Board of Directors for approval. In making its recommendation to the Board of Directors, the Compensation Committee takes into consideration the potential dilutive effect of such awards, as well as changes in compensation practices. New stock plans and any material amendments to existing stock plans must be approved by Occidental Petroleum Corporation's stockholders before they can be implemented.

Occidental's Compensation Committee grants stock awards, including stock option awards, at regularly scheduled meetings normally held the day before regularly scheduled Board meetings. The Board's regularly scheduled meeting dates are set in the prior year. For approximately the past ten years, stock option grants have been made at the Compensation Committee's July meeting. As I mentioned earlier, no stock options granted by Occidental have been backdated.

Accordingly, the exercise price for stock options is determined using the closing price on the New York Stock Exchange on the date the award is made by the Compensation Committee. As such, the intrinsic value of the options on the date of the grant is zero. Occidental's stock plans do not permit re-pricing of options without the approval of stockholders, and Occidental has not re-priced options. The stock options granted by Occidental Petroleum Corporation vest one-third each year over a three year vesting period. The options are exercisable for a ten-year term and are subject to forfeiture in certain events, such as termination of employment for cause. In making grants to the executive officers named in the proxy statement, the Compensation

Committee considers personal performance, industry practices, prior award levels, outstanding awards, and overall Occidental stock ownership in an effort to foster a performance-oriented culture and to align the interests of executive officers with the long-term interests of the company and its stockholders. Grants to other employees are reviewed and approved by the Compensation Committee taking into consideration management's recommendations.

Differences Between Treatment of Stock Options Under the Accounting and Tax Rules

As I mentioned at the beginning of my testimony, Occidental Petroleum Corporation complies fully with both the accounting and tax rules with respect to stock options. From an accounting perspective, pursuant to FAS 123R, on July 1, 2005, Occidental began recognizing fair value compensation expense for stock options. Compensation is measured on the grant date using the Black Scholes option valuation method, and the expense is recognized for accounting purposes on a straight-line basis over the requisite service period, which is generally the option's vesting period.

With respect to Occidental's federal tax returns, in accordance with IRS regulations, Occidental reported deductions in its corporate tax returns for non-qualified stock options in the year they were exercised. For non-qualified stock options, the amount of Occidental's corporate tax deduction in the year of the option's exercise is the same as the amount included in taxable income by the exercising executives on their individual federal income tax returns, that is, the difference between the fair market value at exercise and the option exercise or strike price.

Occidental recognizes stock option compensation expense in its financial statements in accordance with the applicable Generally Accepted Accounting Principles in effect at the time the financial statements are prepared. Likewise, Occidental reports the tax treatment of stock option compensation expenses in accordance with the applicable tax laws and regulations in effect when the tax returns are prepared. Any variations in the expenses recognized in the financial statements and the deductions reported in the tax returns are a result of the differences between the applicable accounting and tax regulations.

The accounting rules and the tax rules are designed to pursue different objectives using different approaches with frequently different results. The accounting rules are based on the matching principle where in this case the value of the options is expensed over the service period. The tax rules defer the value of the stock options until the date that the employee realizes the benefit of the option by exercising them. These different perspectives, not surprisingly, produce different results for different purposes. I cannot say that one is "right" and the other "wrong." What I can say with certainty is that Occidental has complied, and will comply, with whatever accounting and tax regulations the respective accounting and tax standard-setters apply to the granting and exercising of stock option awards.

Conclusion

Thank you again for the opportunity to testify at today's hearing. I would be happy to answer to the best of my ability any questions that you may have.