TESORO CORP /NEW/
Form 10-Q
November 05, 2010

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

þ **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

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File Number 1-3473

TESORO CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**95-0862768**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

19100 Ridgewood Pkwy, San Antonio, Texas 78259-1828
(Address of principal executive offices) (Zip Code)

210-626-6000
(Registrant s telephone number, including area code)

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 þ No o

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 þ No o

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 definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

There were 143,160,349 shares of the registrant s Common Stock outstanding at November 1, 2010.

TESORO CORPORATION
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2010
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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

TESORO CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in millions except for par value)

	September 30, 2010 (Unaudited)	December 31, 2009
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 339	$ 413
Receivables, less allowance for doubtful accounts	1,045	1,116
Inventories	1,049	622
Prepayments and other	101	72
Total Current Assets	2,534	2,223
PROPERTY, PLANT AND EQUIPMENT		
Refining	5,934	5,789
Retail	654	647
Corporate and other	209	213
	6,797	6,649
Less accumulated depreciation and amortization expense	(1,620)	(1,459)
Net Property, Plant and Equipment	5,177	5,190
OTHER NONCURRENT ASSETS		
Acquired intangibles, net	250	255
Other, net	422	402
Total Other Noncurrent Assets	672	657
Total Assets	$ 8,383	$ 8,070
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 1,667	$ 1,441
Accrued liabilities	516	444
Current maturities of debt	3	4

Total Current Liabilities		2,186		1,889
DEFERRED INCOME TAXES		594		505
OTHER LIABILITIES		552		752
DEBT		1,844		1,837
COMMITMENTS AND CONTINGENCIES (Note H)				
STOCKHOLDERS EQUITY				
Common stock, par value $\$0.16^{2}/_{3}$; authorized 200,000,000 shares; 149,055,683 shares issued (147,295,424 in 2009)		25		24
Additional paid-in capital		964		947
Retained earnings		2,395		2,427
Treasury stock, 6,081,453 common shares (6,867,848 in 2009), at cost		(130)		(140)
Accumulated other comprehensive loss		(47)		(171)
Total Stockholders Equity		3,207		3,087
Total Liabilities and Stockholders Equity	$	8,383	$	8,070

The accompanying notes are an integral part of these condensed consolidated financial statements.

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TESORO CORPORATION
CONDENSED STATEMENTS OF CONSOLIDATED OPERATIONS
(Unaudited)
(Dollars in millions except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
REVENUES (a)	$ 5,320	$ 4,742	$ 15,070	$ 12,203
COSTS AND EXPENSES:				
Costs of sales (a)	4,647	4,125	13,386	10,435
Operating expenses	375	367	1,096	1,101
Selling, general and administrative expenses	56	55	165	162
Depreciation and amortization expense	106	102	314	315
Loss on asset disposals and impairments	7	4	39	25
OPERATING INCOME	129	89	70	165
Interest and financing costs	(40)	(35)	(114)	(94)
Interest income and other	4		4	3
Foreign currency exchange gain (loss)	1	(3)	2	(13)
EARNINGS (LOSS) BEFORE INCOME TAXES	94	51	(38)	61
Income tax provision (benefit)	38	18	(6)	22
NET EARNINGS (LOSS)	$ 56	$ 33	$ (32)	$ 39
NET EARNINGS (LOSS) PER SHARE:				
Basic	$ 0.40	$ 0.24	$ (0.23)	$ 0.28
Diluted	$ 0.39	$ 0.24	$ (0.23)	$ 0.28
WEIGHTED AVERAGE COMMON SHARES:				
Basic	140.9	138.2	140.3	138.0
Diluted	142.0	139.7	140.3	139.6
DIVIDENDS PER SHARE	$ 0.00	$ 0.10	$ 0.00	$ 0.30
SUPPLEMENTAL INFORMATION:				
(a) Includes excise taxes collected by our retail segment	$ 97	$ 72	$ 236	$ 213

The accompanying notes are an integral part of these condensed consolidated financial statements.

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TESORO CORPORATION
CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS
(Unaudited)
(Dollars in millions)

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
CASH FLOWS FROM (USED IN) OPERATING ACTIVITIES		
Net earnings (loss)	$ (32)	$ 39
Adjustments to reconcile net earnings (loss) to net cash from (used in) operating activities:		
Depreciation and amortization expense	314	315
Amortization of debt issuance costs and discounts	12	10
Loss on asset disposals and impairments	39	25
Stock-based compensation expense	28	33
Deferred income taxes		68
Provision for bad debts		7
Excess tax benefits from stock-based compensation arrangements	(2)	(1)
Other changes in non-current assets and liabilities	(123)	(71)
Changes in current assets and current liabilities:		
Receivables	72	(351)
Inventories	(427)	96
Prepayments and other	(28)	(2)
Accounts payable and accrued liabilities	302	501
Net cash from operating activities	155	669
CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES		
Capital expenditures	(228)	(326)
Proceeds from asset sales	2	1
Net cash used in investing activities	(226)	(325)
CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES		
Proceeds from debt offerings, net of discount of $12 million and issuance costs of $6 million		282
Borrowings under revolving credit agreement	66	418
Repayments on revolving credit agreement	(66)	(484)
Repayments of debt	(2)	(2)
Dividend payments		(41)
Proceeds from stock options exercised	4	1
Repurchases of common stock	(3)	(2)
Excess tax benefits from stock-based compensation arrangements	2	1
Financing costs and other	(4)	(3)
Net cash from (used in) financing activities	(3)	170

INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(74)	514
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	413	20
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 339	$ 534
SUPPLEMENTAL CASH FLOW DISCLOSURES		
Interest paid, net of capitalized interest	$ 53	$ 36
Income taxes paid (refunded)	$ (106)	$ 32
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING ACTIVITIES		
Capital expenditures in accounts payable and accrued liabilities at end of period	$ 25	$ 35

The accompanying notes are an integral part of these condensed consolidated financial statements.

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TESORO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE A BASIS OF PRESENTATION

As used in this report, the terms Tesoro, we, us, or our may refer to Tesoro Corporation, one or more if its consolidated subsidiaries or all of them taken as a whole.

The interim condensed consolidated financial statements and notes thereto of Tesoro Corporation and its subsidiaries have been prepared by management without audit according to the rules and regulations of the SEC. The accompanying condensed consolidated financial statements reflect all adjustments that, in the opinion of management, are necessary for a fair presentation of results for the periods presented. Such adjustments are of a normal recurring nature, unless otherwise disclosed. The consolidated balance sheet at December 31, 2009, has been condensed from the audited consolidated financial statements at that date. Certain information and notes normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) have been condensed or omitted pursuant to the SEC s rules and regulations. However, management believes that the disclosures presented herein are adequate to fairly present the information. The accompanying condensed consolidated financial statements and notes should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2009.

We prepare our condensed consolidated financial statements in conformity with U.S. GAAP that requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, to disclose contingent assets and liabilities at the date of the financial statements and to report revenues and expenses for the periods presented. We review our estimates on an ongoing basis using currently available information. Changes in facts and circumstances may result in revised estimates and actual results could differ from those estimates. The results of operations for any interim period are not necessarily indicative of results for the full year. Certain prior year balances have been disaggregated in order to conform to current year presentation.

NOTE B EARNINGS (LOSS) PER SHARE

We compute basic earnings (loss) per share by dividing net earnings (loss) by the weighted average number of common shares outstanding during the period. Diluted earnings (loss) per share include the effects of potentially dilutive shares, principally consisting of common stock options and unvested restricted stock outstanding during the period.

Share and per share calculations are presented below (in millions except per share amounts):

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Basic:				
Net earnings (loss)	$ 56	$ 33	$ (32)	$ 39
Weighted average common shares outstanding	140.9	138.2	140.3	138.0
Basic Earnings (Loss) Per Share	$ 0.40	$ 0.24	$ (0.23)	$ 0.28
Diluted:				
Net earnings (loss)	$ 56	$ 33	$ (32)	$ 39
Weighted average common shares outstanding	140.9	138.2	140.3	138.0
Common stock equivalents	1.1	1.5		1.6
Total diluted shares	142.0	139.7	140.3	139.6

Diluted Earnings (Loss) Per Share	$ 0.39	$ 0.24	$ (0.23)	$ 0.28

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TESORO CORPORATION
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(Unaudited)

Potentially dilutive common stock equivalents that were excluded from the calculation of diluted earnings (loss) per share, as the effect of including such securities would have been anti-dilutive, were as follows (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
Common stock equivalents (a)	¾	¾	1.5	¾
Stock options (b)	6.0	5.4	5.8	4.7

(a) For the nine months ended September 30, 2010, common stock equivalents, including stock options, were excluded as a result of the net loss reported during the period.

(b) Common stock options presented above were excluded as the exercise prices were greater than the average market price of the common stock during each respective reporting period.

NOTE C INVENTORIES

Components of inventories were as follows (in millions):

	September 30, 2010	December 31, 2009
Domestic crude oil and refined products	$ 747	$ 495
Foreign crude oil	184	12
Oxygenates and by-products	26	22

Merchandise		13		13
Materials and supplies		79		80
Total Inventories	$	1,049	$	622

We use the last-in, first-out (LIFO) cost method as the primary method to determine the carrying value of domestic crude oil and refined product inventories in our refining and retail segments. We determine the carrying value of inventories of foreign crude oil, oxygenates and by-products using the first-in, first-out (FIFO) cost method. The total carrying value of our crude oil and refined product inventories was less than replacement cost by approximately $1.2 billion and $1.1 billion at September 30, 2010, and December 31, 2009, respectively.

NOTE D FAIR VALUE MEASUREMENTS

We classify financial assets and financial liabilities into the following fair value hierarchy: level 1 quoted prices in active markets for identical assets and liabilities; level 2 quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability; and level 3 unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. When available, we measure fair value using level 1 inputs because they provide the most reliable evidence of fair value. Derivative instruments are our only financial assets and financial liabilities measured at fair value on a recurring basis using the market approach. See Note E for further information on the Company s derivative instruments.

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TESORO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Our derivative instruments consist primarily of options, exchange-traded futures (Futures Contracts), over-the-counter swaps and options (OTC Swap Contracts and OTC Option Contracts, respectively), and physical commodity forward purchase and sale contracts (Forward Contracts). Options are valued using quoted prices from the exchanges and are categorized in level 1 of the fair value hierarchy. Futures Contracts are valued based on quoted prices from exchanges and are categorized in level 1 or level 2 of the fair value hierarchy based on the liquidity of the instrument. OTC Swap Contracts, OTC Option Contracts and Forward Contracts are valued using third-party broker quotes, industry pricing services and exchange-traded curves, with consideration of counterparty credit risk and are categorized in level 2 of the fair value hierarchy. At September 30, 2010, and December 31, 2009, the fair values of our derivative instruments were immaterial to the condensed consolidated financial statements.

The fair values of our derivative assets and liabilities by level within the fair value hierarchy were as follows (in millions):

	September 30, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Derivatives				
Commodity Futures Contracts	$ 2	$	$ 2	$
Commodity OTC Swap Contracts	$ 2	$	$ 2	$
Liabilities:				
Derivatives				
Commodity Futures Contracts	$ 11	$ 11	$	$

	December 31, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Derivatives				
Commodity Futures Contracts	$ 6	$ 6	$	$
Liabilities:				
Derivatives				
Commodity Futures Contracts	$ 4	$ 3	$ 1	$

Certain of our derivative contracts, under master netting arrangements, include both asset and liability positions. We have elected to offset both the fair value amounts and any related cash collateral amounts recognized for multiple derivative instruments executed with the same counterparty.

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TESORO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The carrying value of our financial instruments, including cash and cash equivalents, receivables, accounts payable and certain accrued liabilities approximate fair value because of the short maturities of these instruments. The fair value of our debt was estimated primarily using quoted market prices. The carrying value and fair value of our debt at September 30, 2010, were approximately $1.8 billion and $1.9 billion, respectively. Both the carrying value and fair value of our debt at December 31, 2009, were approximately $1.8 billion.

The fair value of certain impaired nonfinancial assets, including property, plant and equipment, measured on a non-recurring basis as of and for the nine months ended September 30, 2010, was as follows (in millions):

	September 30, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Losses
Assets:					
Refining Equipment	$ 4	$	$	$ 4	$20

Due to the impact of the continuing weak economy on the refining industry, we continue to evaluate the recoverability of certain capital projects currently in progress. This evaluation resulted in an impairment charge of $20 million related to the deferral of a capital project at our Los Angeles refinery, recognized during the three months ended March 31, 2010. Equipment specifically manufactured and uniquely configured for this project was written down from a carrying value of $20 million to a fair value of $4 million for a loss of $16 million. The estimated recovery amounts were based on direct equipment cost recoverable if sold to an end user, in the principal or most advantageous market for the asset, in an orderly transaction. The amounts presented represent our estimates on unobservable inputs that require significant judgment, for which there is little or no market data. An additional $4 million loss was related to certain engineering costs that were determined to not be recoverable.

NOTE E DERIVATIVE INSTRUMENTS

The timing, direction and overall change in refined product prices versus crude oil prices impacts profit margins and has a significant impact on our earnings and cash flows. To manage these commodity price risks, we periodically use derivative instruments primarily associated with the purchase or sale of crude oil and refined products. We may also use derivative instruments to manage price risks associated with inventory quantities above or below our target levels. All derivative instruments are recorded in the condensed consolidated balance sheets at fair value. These derivative instruments typically involve options, Futures Contracts, OTC Swap Contracts, OTC Option Contracts, and Forward Contracts, all generally with maturity dates of less than one year. We believe that there is minimal credit risk with respect to our counterparties.

Option contracts provide the right, but not the obligation, to buy or sell the commodity at a specified price in the future. Futures Contracts include a requirement to buy or sell the commodity at a fixed price in the future. OTC Swap Contracts, OTC Option Contracts and Forward Contracts require cash settlement for the commodity based on the difference between a fixed or floating price and the market price on the settlement date. At September 30, 2010, we had open net short OTC Swap Contract positions of 0.3 million barrels, open net short Futures Contract positions of 2.9 million barrels, open net long Forward Contract positions of 1.0 million barrels and no open option positions. We also have OTC Swap contracts that require cash collateral if our liability position exceeds specified thresholds. At

September 30, 2010, we did not have any cash collateral outstanding.

TESORO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The following table presents the fair value and balance sheet classification of our non-hedging derivative instruments as of September 30, 2010, and December 31, 2009 (in millions). The fair value amounts below are presented on a gross basis and do not reflect the netting of asset and liability positions permitted under the terms of our master netting arrangements. We have elected to offset the recognized fair value amounts for multiple derivative instruments executed with the same counterparty in our financial statements. As a result, the asset and liability amounts below will not agree with the amounts presented in our condensed consolidated balance sheet, nor will they agree with the fair value information presented in Note D.

	Derivative Assets included in Prepayments and other		Derivative Liabilities included in Accrued liabilities	
	September 30, 2010	December 31, 2009	September 30, 2010	December 31, 2009
Commodity Future Contracts	$ 189	$ 68	$ (198)	$ (66)
Commodity OTC Swap Contracts	3	¾	(1)	¾
Commodity Forward Contracts	71	¾	(71)	¾
Total Derivative Instruments	$ 263	$ 68	$ (270)	$ (66)

Gains (Losses) for our non-hedging derivative instruments were as follows (in millions):

	Amount of Derivatives Gains (Losses) recognized in Cost of sales (a)			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Commodity Future Contracts	$ (3)	$ (2)	$ (5)	$ (50)
Commodity OTC Swap Contracts	¾	(4)	8	(11)
Commodity Forward Contracts	¾	¾	¾	¾
Total Derivative Instruments	$ (3)	$ (6)	$ 3	$ (61)

(a) Derivative gains (losses) are primarily included in Cost of sales in the condensed statements of consolidated operations. There are certain transactions that are included in Revenues in the condensed statements of consolidated operations. These amounts are not material for the three and nine months ended September 30, 2009 and 2010.

NOTE F DEBT

For additional information regarding our outstanding debt, see Capital Resources and Liquidity in Management s Discussion and Analysis of Financial Condition and Results of Operations in Item 2.

Tesoro Corporation Credit Agreement (Credit Agreement) Revolving Credit Facility

We amended our Credit Agreement in February 2010. The modifications included the following:

- the minimum tangible net worth requirement (as defined) was lowered;
- the purchase or sale of certain assets is no longer subject to the fixed charge coverage ratio;
- the covenant permitting additional unsecured indebtedness (as defined) increased from $75 million to $600 million;
- letters of credit allowed under separate letter of credit agreements, previously capped at $500 million, are no longer subject to a cap;
- the applicable margin (as defined) was adjusted; and
- the annual rate of commitment fees for the unused portion of the revolving credit facility was adjusted to 0.50% from 0.375%.

TESORO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

At September 30, 2010, our Credit Agreement provided for borrowings (including letters of credit) up to the lesser of the amount of a periodically adjusted borrowing base of approximately $1.5 billion (based upon an Alaska North Slope crude oil price of $72 per barrel), consisting of Tesoro s eligible cash and cash equivalents, receivables and petroleum inventories, net of the standard reserve as defined, or the agreement s total capacity of $1.86 billion. The total capacity can be further increased from $1.86 billion up to $2.0 billion. As of September 30, 2010, we had no borrowings and $669 million in letters of credit outstanding under the Credit Agreement, resulting in total unused credit availability of approximately $827 million or 55% of the eligible borrowing base.

Borrowings under the revolving credit facility bear interest at either a base rate (3.25% at September 30, 2010), or a Eurodollar rate (0.26% at September 30, 2010) plus an applicable margin. The applicable margin at September 30, 2010, was 2.25% in the case of the Eurodollar rate, but varies based upon our credit facility s credit availability and credit ratings. Letters of credit outstanding under the revolving credit facility incur fees at an annual rate tied to the applicable margin described above (2.25% at September 30, 2010). We also incur commitment fees for the unused portion of the revolving credit facility at an annual rate of 0.50% as of September 30, 2010. Our Credit Agreement expires in May 2012.

Lehman Commercial Paper Inc. (Lehman CPI) was one of the lenders under our Credit Agreement, representing a commitment of $50 million (less than 3% of our total Credit Agreement capacity). In October 2008, Lehman CPI filed for bankruptcy. Barclays Bank PLC assumed the $50 million commitment from Lehman CPI in April 2010. As a result, our capacity increased from $1.81 billion to $1.86 billion in April 2010 and remained $1.86 billion at September 30, 2010.

The Credit Agreement contains covenants and conditions that, among other things, limit our ability to pay cash dividends, incur indebtedness, create liens and make investments. Borrowing availability under the Credit Agreement is based on a minimum fixed charge coverage ratio. We have a default covenant, which requires us to maintain specified levels of tangible net worth. We were in compliance with the tangible net worth requirement for the three months ended September 30, 2010. The Credit Agreement is guaranteed by substantially all of Tesoro s active domestic subsidiaries. The Credit Agreement allows up to $100 million of restricted payments during any four quarter period subject to credit availability exceeding 20% of the borrowing base.

In October 2010, Tesoro Panama Company Sociedad Anonima (TPSA) entered into a revolving credit agreement (TPSA Credit Agreement) which provides for an uncommitted, secured revolving credit facility. The TPSA Credit Agreement is non-recourse to the Company, meaning only TPSA is liable for any borrowed amounts or interest. See Note M for additional information.

Letter of Credit Agreements

The Credit Agreement allows us to obtain letters of credit under separate letter of credit agreements for foreign crude oil purchases. At September 30, 2010, we had three separate letter of credit agreements with a total capacity of $550 million, of which $218 million was outstanding. Letters of credit outstanding under these agreements incur fees and are secured by the petroleum inventories for which they are issued. The letter of credit agreements may be terminated by either party, at any time.

NOTE G BENEFIT PLANS

Tesoro sponsors the following four defined benefit pension plans: the funded qualified employee retirement plan, the unfunded executive security plan, the unfunded non-employee director retirement plan and the unfunded restoration retirement plan. Although our funded qualified employee retirement plan fully meets all funding requirements under applicable laws and regulations, during the nine months ended September 30, 2010, we voluntarily contributed approximately $22 million to improve the funded status of the plan.

Tesoro provides health care benefits to retirees who met certain service requirements and were participating in our group health insurance program at retirement. In addition, Tesoro sponsors a thrift plan and retail savings plan

TESORO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

which provide for eligible employees to make contributions, subject to certain limitations, into designated investment funds with a matching contribution by Tesoro.

In June 2010, the Compensation Committee of the Board of Directors approved changes to certain retirement and postretirement benefits to be effective beginning January 1, 2011. The majority of our employees and retirees will be impacted by these changes subject to applicable collective bargaining and/or purchase and sale agreements.

Changes to retirement plans

The funded qualified employee retirement plan will change from a Final Average Pay based plan to a Cash Balance Account based plan. The Final Average Pay benefit will only incorporate service through December 31, 2010, but will continue to recognize changes in pay and age for determining retirement benefits. Employees will begin to earn a Cash Balance benefit for service on or after January 1, 2011. This change will reduce our future pension costs and funding obligations.

The unfunded restoration retirement plan will also be amended to reflect changes in the qualified employee retirement plan.

Changes to postretirement benefits

Postretirement medical insurance cost sharing for current and future retirees will change to reflect actual retiree claims experience rather than a blended premium cost (combination of active and retiree claim experience) effective January 1, 2011. The additional cost to the retiree will be phased in over three years. Beginning in 2014, the company contribution for retirees hired before January 1, 2006, will be capped and retirees will pay for any increases in costs.

Postretirement dental benefits for all current and future retirees will be eliminated effective January 1, 2011.

Postretirement medical coverage will be eliminated for retirees over the age of 65 as of January 1, 2014.

Postretirement life insurance will be eliminated for future retirees effective January 1, 2011.

Postretirement life insurance for current retirees will be reduced to $10,000 effective January 1, 2011, and eliminated entirely beginning January 1, 2016.

Changes to the thrift plan

Our present $1 for $1 match on 7% of pay (base pay, overtime and bonus) for our thrift plan will be reduced to a $1 for $1 match on 6% of pay (base pay only bonus and overtime excluded), effective January 1, 2011.

Pension Benefits Financial Information

The components of net periodic pension benefit expense included in the condensed statements of consolidated operations for the three and nine months ended September 30, 2010, and 2009, were (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
Service cost	$ 9	$ 10	$ 29	$ 27
Interest cost	7	7	21	20
Expected return on plan assets	(6)	(5)	(16)	(15)
Amortization of prior service cost	¾	1	2	3
Recognized net actuarial loss	3	4	10	11
Curtailments	¾	¾	4	¾

Net Periodic Benefit Expense	$ 13	$ 17	$ 50	$ 46

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TESORO CORPORATION
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(Unaudited)

There were no changes made to pension benefits during the 2010 third quarter.

Other Postretirement Benefits Financial Information

The components of other postretirement benefit expense included in the condensed statements of consolidated operations for the three and nine months ended September 30, 2010, and 2009, were (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
Service cost	$ 2	$ 3	$ 10	$ 12
Interest cost	1	4	12	15
Amortization of prior service cost	(9)		(9)	
Recognized net actuarial loss	3	(1)	4	1
Curtailment			(48)	
Net Periodic Benefit Expense (Income)	$ (3)	$ 6	$ (31)	$ 28

Measurement of Other Postretirement Benefits

As a result of the changes to other postretirement benefits during the 2010 second quarter, we remeasured our other postretirement obligations as of June 30, 2010. The discount rate used to determine these obligations as of June 30, 2010, and the related net periodic benefit costs for the six months ending December 31, 2010, is 4.64% compared to a discount rate of 6.36% used at December 31, 2009. There were no changes made to other postretirement benefits during the 2010 third quarter. There have been no significant changes to the funded status of our other postretirement benefits during the three months ended September 30, 2010.

Primarily as a result of the changes to the other postretirement benefits discussed above and the remeasurement of these obligations as of June 30, 2010, our projected benefit obligation and accumulated other comprehensive loss, net of tax, decreased by $240 million and $124 million, respectively, from December 31, 2009.

The assumed health care cost trend rates used to determine the projected postretirement benefit obligation for the remeasurement performed in the 2010 second quarter and as of December 31, 2009 are as follows:

	June 30, 2010	**December 31, 2009**
Health care cost trend rate assumed for future periods	8.50%	8.00%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	5.00%	5.00%
Year that the rate reaches the ultimate trend rate	2017	2015

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Changes in our projected benefit obligations, and the funded status for our other postretirement benefits as of September 30, 2010, and for the nine months then ended, were (in millions):

	September 30, 2010
Change in projected benefit obligation:	
Projected benefit obligations at beginning of year	$ (356)
Service cost	(10)
Interest cost	(12)
Net actuarial loss	(107)
Benefits paid	6
Plan amendments	317
Curtailment	46
Projected benefit obligation at period end	$ (116)
Changes in plan assets:	
Fair value of plan assets at beginning of year	$
Employer contributions	6
Benefits paid	(6)
Fair value of plan assets at period end	$
Funded status at period end	$ (116)

Comprehensive income for the three and nine months ended September 30, 2010, and 2009, was (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net Earnings (Loss)	$ 56	$ 33	$ (32)	$ 39
Other Comprehensive Income (Loss)	(3)		124	
Comprehensive Income	53	33	92	39

NOTE H COMMITMENTS AND CONTINGENCIES

Environmental and Tax Matters

We are a party to various litigation and contingent loss situations, including environmental and income tax matters, which arise in the ordinary course of business. Although we cannot predict the ultimate outcomes of these matters with certainty, we have accrued for the estimated liabilities when appropriate. We believe that the outcome of these matters will not materially impact our liquidity and consolidated financial position, although the resolution of certain of these matters could have a material impact on interim or annual results of operations. Additionally, if applicable, we accrue receivables for probable insurance or other third party recoveries.

We are subject to extensive federal, state and local environmental laws and regulations. These laws, which change frequently, regulate the discharge of materials into the environment and may require us to remove or mitigate the

environmental effects of the disposal or release of petroleum or chemical substances at various sites, install additional controls, or modify certain emission sources.
We are subject to extensive federal, state and local tax laws and regulations. Newly enacted tax laws and regulations, and changes in existing tax laws and regulations, could result in increased expenditures in the future.

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We are also subject to audits by federal, state and local taxing authorities in the normal course of business. It is possible that tax audits could result in claims against us in excess of recorded liabilities. We believe that resolution of any such claim(s) would not materially affect our consolidated financial position or results of operations. We believe it is possible that unrecognized tax benefits could decrease by as much as $11 million in the next twelve months through settlements or other conclusions, primarily regarding state tax issues.

Environmental Liabilities

We are, and expect to continue, incurring expenses for environmental liabilities at a number of currently and previously owned or operated refining, pipeline, terminal and retail station properties. We have accrued liabilities for these expenses and believe these accruals are adequate. At September 30, 2010, and December 31, 2009, our accruals for environmental expenditures totaled $107 million and $106 million, respectively. Our environmental accruals are based on estimates including engineering assessments, and it is possible that our estimates will change and additional costs will be recorded as more information becomes available.

We received $58.5 million in a settlement with a prior owner of our Golden Eagle refinery in 2007 in exchange for assuming responsibility for certain environmental liabilities arising from operations at the refinery prior to August 2000. These environmental liabilities totaled $63 million and $73 million at September 30, 2010, and December 31, 2009, respectively. We cannot presently determine the full extent of remedial activities that may be required at the Golden Eagle refinery. Therefore, it is possible that we will identify additional remediation costs as more information becomes available. We have filed insurance claims under environmental insurance policies that provide coverage up to $190 million for expenditures in excess of $50 million in self-insurance. Amounts recorded for environmental liabilities have not been reduced for possible insurance recoveries.

We are continuing to investigate conditions at certain active wastewater treatment units at our Golden Eagle refinery. This investigation is driven by an order from the San Francisco Bay Regional Water Quality Control Board that names us as well as two previous owners of the Golden Eagle refinery. Costs to investigate these conditions are included in our environmental accruals. We cannot currently estimate the amount of the ultimate resolution of the order but we believe it will not have a material adverse effect on our financial position or results of operations.

Washington Refinery Fire

On April 2, 2010, the naphtha hydrotreater unit at our Washington Refinery was involved in a fire, which fatally injured seven employees and rendered the unit inoperable. The Washington State Department of Labor & Industries (L&I), the U.S. Chemical Safety and Hazard Investigation Board (CSB) and the U.S. Environmental Protection Agency (EPA) initiated separate investigations of the fire. In October 2010, L&I completed its investigation, issued citations and assessed a $2.4 million fine. On October 22, 2010, we filed an appeal of the citations. The EPA and CSB investigations are ongoing. We have incurred $25 million in charges related to the incident.

Our business interruption insurance deductible is satisfied after we have exceeded both 60 days of operational disruption and $25 million in losses primarily based on the operating plan that existed prior to the incident. Our property damage insurance has a $10 million deductible. We have filed business interruption insurance claims and will be filing property damage claims related to this incident. Subsequent to September 30, 2010, we received $27 million in business interruption insurance recoveries. We have not recognized possible insurance recoveries in our financial statements as of and for the three and nine months ended September 30, 2010.

For additional information regarding this matter, see Capital Resources and Liquidity in Management s Discussion and Analysis of Financial Condition and Results of Operations in Item 2.

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Other Matters

In the ordinary course of business, we become party to lawsuits, administrative proceedings and governmental investigations, including environmental, regulatory and other matters. Large, and sometimes unspecified, damages or penalties may be sought from us in some matters for which the likelihood of loss may be possible but the amount of loss is not currently estimable. As a result, we have not established accruals for these matters. On the basis of existing information, we believe that the resolution of these matters, individually or in the aggregate, will not have a material adverse effect on our financial position or results of operations.

On February 5, 2010, the EPA filed suit against us alleging violations of the Clean Air Act and corresponding regulatory requirements concerning the testing and reporting of transportation fuels and fuel additives. In February 2009, we received a Notice of Violation (NOV) from the EPA for alleged violations arising from a compliance review conducted by the EPA in 2006 for the years 2003 through the time of the review in 2006. We are discussing the alleged violations contained in the suit with the EPA and the U.S. Department of Justice and have not established an accrual for this matter. On the basis of existing information, we believe that the resolution of this matter will not have a material adverse effect on our financial position or results of operations.

During 2009, Chevron filed a lawsuit against us claiming they are entitled to a share of the refunds we received in 2008 from the owners of the Trans Alaska Pipeline System (TAPS). We received $50 million in 2008, net of contingent legal fees, for excessive intrastate rates charged by TAPS during 1997 through 2000, and the period of 2001 through June 2003. Chevron is asserting that it is entitled to a share of its portion of the refunds for retroactive price adjustments under our previous crude oil contracts with them. In September 2010, the trial court judge granted Chevron s motion for summary judgment and awarded them $16 million. We disagree with the trial court and intend to appeal the decision to the Alaska Supreme Court. We believe that the outcome of this matter will not materially impact our liquidity and consolidated financial position, although the resolution of this matter could have a material impact on interim or annual results of operations.

NOTE I STOCKHOLDERS EQUITY

Cash Dividends

In February 2010, our Board of Directors suspended indefinitely our quarterly cash dividend on common stock.

Treasury Stock

We purchase shares of our common stock in open market transactions to meet our obligations under employee benefit plans. We also purchase shares of our common stock in connection with the exercise of stock options, the vesting of restricted stock and to fulfill other stock compensation requirements.

The Company entered into an employment agreement with our CEO (the CEO Agreement) on March 30, 2010, effective May 1, 2010. Inducement awards were granted based on the terms of this agreement and were issued from treasury stock subject to certain vesting and employment restrictions. The annual award grant to our CEO, excluding performance unit awards, was granted from treasury stock.

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NOTE J STOCK-BASED COMPENSATION

Stock-based compensation expense included in our condensed statements of consolidated operations was as follows (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Restricted common stock	$ 3	$ 4	$ 10	$ 10
Stock options	1	2	5	9
Restricted stock units			1	
Stock appreciation rights	6	5	7	9
Phantom stock	3	3	4	5
Performance units	1		1	
Total Stock-Based Compensation Expense	$ 14	$ 14	$ 28	$ 33

The income tax benefit from tax deductions associated with stock-based compensation totaled $5 million and $2 million for the nine months ended September 30, 2010, and 2009, respectively.

Stock Options

During the nine months ended September 30, 2010, we granted stock options to certain officers and other key employees. The fair value of each option is estimated on the grant date using the Black-Scholes option-pricing model. The estimated fair value of these stock options is amortized over the vesting period using the straight-line method. The estimated weighted-average grant-date fair value per share of options granted was $7.36. These awards generally will become exercisable after one year in 33% annual increments and expire ten years from the date of grant. Stock options granted in connection with the inducement awards of the CEO Agreement will vest 30% on each of the first two anniversaries of the grant date and 40% on the third anniversary of the grant date. Total unrecognized compensation cost related to non-vested stock options totaled $6 million as of September 30, 2010. This cost is expected to be recognized over a weighted average period of 2.1 years. A summary of our stock option activity and changes during the nine months ended September 30, 2010, is presented below (shares in thousands):

	Number of Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2010	7,931	$ 21.91	5.3 years	$
Granted	679	$ 12.97		
Exercised	(757)	$ 5.16		
Forfeited or expired	(81)	$ 19.38		
Outstanding at September 30, 2010	7,772	$ 22.78	5.3 years	$
Vested or expected to vest at September 30, 2010	7,740	$ 22.83	5.3 years	$
Exercisable at September 30, 2010	6,655	$ 23.93	4.7 years	$

Restricted Common Stock

During the nine months ended September 30, 2010, we granted restricted common stock to certain officers and key employees. The fair value of each restricted share on the grant date is equal to the market price of our common stock on that date. The estimated fair value of our restricted stock is amortized over the vesting period using the straight-line method. These awards generally vest in annual increments ratably over three years. Restricted stock granted in connection with the inducement awards of the CEO Agreement will vest 100% on May 1, 2011.

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Unrecognized compensation cost related to our non-vested restricted stock totaled $19 million as of September 30, 2010. This cost is expected to be recognized over a weighted-average period of 2.0 years. The fair value of non-vested restricted common stock as of September 30, 2010, totaled $25 million.

A summary of our restricted stock activity for the nine months ended September 30, 2010, is set forth below (shares in thousands):

	Number of Restricted Shares	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2010	1,370	$ 21.66
Granted	1,181	$ 12.94
Vested	(595)	$ 24.59
Forfeited	(91)	$ 16.95
Nonvested at September 30, 2010	1,865	$ 15.44

Restricted Stock Units

In May 2010, we granted restricted stock units in connection with the inducement awards of the CEO Agreement. The fair value of each restricted stock unit on the grant date is equal to the market price of our common stock on that date. The estimated fair value of the restricted stock units is amortized over the vesting period using the straight-line method. These restricted stock units vest in annual increments ratably over two years. Unrecognized compensation cost related to our non-vested units totaled $3 million as of September 30, 2010. This cost is expected to be recognized over a weighted-average period of 1.6 years. The fair value of non-vested restricted stock units as of September 30, 2010, totaled $3 million. A summary of our restricted stock unit activity for the nine months ended September 30, 2010, is set forth below:

	Number of Restricted Units	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2010		$
Granted	256,223	$ 13.66
Nonvested at September 30, 2010	256,223	$ 13.66

Stock Appreciation Rights

A stock appreciation right (SAR) entitles a holder to receive cash in an amount equal to the excess of the fair market value of one share of common stock on the date of exercise over the grant price of the SAR. The fair value of each SAR is estimated at the end of each reporting period using the Black-Scholes option-pricing model. The SARs granted during the nine months ended September 30, 2010, vest ratably over three years following the date of grant and expire seven years from the grant date. The liability associated with our SARs totaled $21 million and $13 million at September 30, 2010, and December 31, 2009, respectively. A summary of SARs activity for the nine months ended September 30, 2010, is set forth below (shares in thousands):

	Weighted-	Weighted-Average

	Number of SARs	Average Exercise Price	Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2010	7,486	$ 22.65	5.5 years	$
Granted	483	$ 12.93		
Forfeited	(347)	$ 18.87		
Outstanding at September 30, 2010	7,622	$ 22.21	4.9 years	$
Vested or expected to vest at September 30, 2010	7,611	$ 22.22	4.9 years	$
Exercisable at September 30, 2010	3,775	$ 28.68	4.3 years	$

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Performance Unit Awards

During the nine months ended September 30, 2010, we granted 5.4 million performance unit awards to certain officers and other key employees. These performance unit awards represent the right to receive a cash payment at the end of the performance period depending on Tesoro s achievement of pre-established performance measures and will vest at the end of a 33 month performance period. The value of the award ultimately paid will be based on our relative total shareholder return against the performance peer group and the S&P 500 index as well as the absolute total shareholder return of Tesoro s common stock over the performance period. The performance unit awards are settled in cash and can range from 0% to 200% of targeted award value. The fair value of each performance unit award is estimated at the end of each reporting period using a Monte Carlo simulation. As of September 30, 2010, the fair value of each outstanding non-vested performance unit award was approximately $0.42.

Phantom Stock Options

We did not grant phantom stock options during the nine months ended September 30, 2010. As of September 30, 2010, we had 1.5 million executive phantom stock options outstanding. The fair value of each phantom stock option is estimated at the end of each reporting period using the Black-Scholes option-pricing model. The phantom stock options vest ratably over three years following the date of grant and expire ten years from the date of grant. The liability associated with executive phantom stock awards totaled $9 million and $6 million at September 30, 2010, and December 31, 2009, respectively.

NOTE K OPERATING SEGMENTS

The Company s revenues are derived from two operating segments, refining and retail. We own and operate seven petroleum refineries located in California, Washington, Alaska, Hawaii, North Dakota and Utah. These refineries manufacture gasoline and gasoline blendstocks, jet fuel, diesel fuel, residual fuel oils and other refined products. We sell these refined products, together with refined products purchased from third parties, at wholesale through terminal facilities and other locations. Our refining segment also sells refined products to unbranded marketers and occasionally exports refined products to foreign markets. Our retail segment sells gasoline, diesel fuel and convenience store items through company-operated retail stations and branded jobber/dealers in 15 states from Minnesota to Alaska and Hawaii.

We evaluate the performance of our segments based primarily on segment operating income. Segment operating income includes those revenues and expenses that are directly attributable to management of the respective segment. Intersegment sales from refining to retail are made at prices that approximate market. Income taxes, other income, foreign currency exchange gain (loss), interest and financing costs, interest income, corporate depreciation and corporate general and administrative expenses are excluded from segment operating income. Identifiable assets are those utilized by the segments, whereas corporate assets are principally cash and other assets that are not associated with a specific operating segment.

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Segment information is as follows (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenues				
Refining:				
Refined products	$ 4,907	$ 4,489	$ 13,813	$ 11,310
Crude oil resales and other	275	91	863	526
Retail:				
Fuel (a)	947	863	2,647	2,182
Merchandise and other	61	63	171	178
Intersegment Sales from Refining to Retail	(870)	(764)	(2,424)	(1,993)
Total Revenues	$ 5,320	$ 4,742	$ 15,070	$ 12,203
Segment Operating Income				
Refining (b) (c)	$ 146	$ 84	$ 127	$ 268
Retail	32	53	86	42
Total Segment Operating Income	178	137	213	310
Corporate and unallocated costs	(49)	(48)	(143)	(145)
Operating Income (d)	129	89	70	165
Interest and financing costs	(40)	(35)	(114)	(94)
Interest Income and other	4		4	3
Foreign currency exchange gain (loss)	1	(3)	2	(13)
Earnings (Loss) Before Income Taxes	$ 94	$ 51	$ (38)	$ 61
Depreciation and Amortization Expense				
Refining	$ 92	$ 86	$ 270	$ 263
Retail	10	10	30	29
Corporate	4	6	14	23
Total Depreciation and Amortization Expense	$ 106	$ 102	$ 314	$ 315
Capital Expenditures				
Refining	$ 67	$ 91	$ 207	$ 250
Retail	8	1	12	10
Corporate		4		31
Total Capital Expenditures	$ 75	$ 96	$ 219	$ 291

(a) Federal and state motor fuel taxes on sales by our retail segment are included in both Revenues and Costs of sales in our condensed statements of consolidated operations. These taxes totaled $97 million and $72 million for the three months ended September 30, 2010, and 2009, respectively, and $236 million and $213 million for the nine months ended September 30, 2010, and 2009, respectively.

(b) Includes impairment charges related to our Los Angeles refinery of $20 million and $12 million for the nine months ended September 30, 2010, and 2009, respectively. The loss on asset disposals and impairments is included in refining segment operating income but excluded from the regional operating costs per barrel.

(c) Includes additional costs of $23 million and $36 million at our Washington refinery for the three and nine months ended September 30, 2010, respectively. Approximately $12 million and $25 million of the costs during the three and nine months ended September 30, 2010, respectively, were directly related to the April 2, 2010, incident. The remaining $11 million of the costs during the same periods was a result of maintenance work performed while the refinery was shut down.

(d) Includes a $43 million net gain for the nine months ended September 30, 2010, primarily

from the
elimination of
postretirement
life insurance
benefits for
current and
future retirees.

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	September 30, 2010	December 31, 2009
Identifiable Assets		
Refining	$ 7,228	$ 6,690
Retail	620	656
Corporate	535	724
Total Assets	$ 8,383	$ 8,070

NOTE L NEW ACCOUNTING STANDARDS

Fair Value Measurements

We adopted a standard on January 1, 2009, that expanded the framework and disclosures for measuring the fair value of nonfinancial assets and nonfinancial liabilities, including:

acquired or impaired goodwill;

the initial recognition of asset retirement obligations; and

impaired property, plant and equipment.

The adoption of this standard did not impact our financial position or results of operations.

In January 2010, the FASB amended the standard covering fair value measurements to require additional disclosures, including transfers in and out of levels 1 and 2 fair value measurements, the gross basis presentation of the reconciliation of level 3 fair value measurements, and fair value measurement disclosure at the class level, as opposed to category level, as previously required. This guidance is effective for interim and annual reporting periods beginning after December 15, 2009, except for disclosures related to level 3 fair value measurements, which are effective for fiscal years beginning after December 15, 2010 (including interim periods). The adoption of the amendment did not impact our financial position or results of operations.

Variable Interest Entities

The FASB issued a standard in June 2009 that amends previous guidance on variable interest entities. The standard modifies the criteria for determining whether an entity is a variable interest entity and requires ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity and an analysis to determine whether the enterprise s variable interest(s) give it a controlling financial interest in a variable interest entity. This standard became effective January 1, 2010, and did not impact our financial position or results of operations.

NOTE M SUBSEQUENT EVENTS

On October 18, 2010, TPSA, a directly and wholly owned subsidiary of the Company, entered into an uncommitted, secured revolving credit agreement. TPSA is an excluded and unrestricted subsidiary (as defined) from the Company s Fourth Amended and Restated Credit Agreement and outstanding indentures. The TPSA Credit Agreement is non-recourse to the Company. The TPSA Credit Agreement includes two uncommitted facilities, which provide for revolving loans, swing line loans, daylight overdraft loans and letters of credit. At closing, the combined facility maximum was $350 million consisting of $245 million under the first facility and $105 million under the second facility. The total facilities can be further increased up to $700 million.

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Under the TPSA Credit Agreement, each extension of credit will bear interest, at the following rates per annum:

- TPSA may select between an Eurodollar Rate plus an Applicable Margin (as defined), or an Alternative Base Rate (as defined), for borrowings under the revolving credit facility;
- the Applicable Margin (as defined) for letters of credit will be 1.75% for both facilities; and
- for loans the Alternative Base Rate (as defined) plus the Applicable Margin (as defined) plus 0.50% per annum.

The TPSA Credit Agreement contains the following default financial covenants, as they relate to TPSA financial results:

- maximum Leverage Ratio (as defined);
- Minimum Adjusted Tangible Net Worth (as defined), based on the Combined Facility Maximum Amount (as defined);
- Minimum Adjusted Net Working Capital (as defined), based on the Combined Facility Maximum Amount (as defined); and
- maximum inventory levels below certain thresholds depending on the Combined Facility Maximum Amount (as defined).

For additional information regarding the TPSA Credit Agreement, see Capital Resources and Liquidity on page 40.

NOTE N CONDENSED CONSOLIDATING FINANCIAL INFORMATION

Separate condensed consolidating financial information of Tesoro Corporation, subsidiary guarantors and non-guarantors are presented below. Tesoro and certain subsidiary guarantors have fully and unconditionally guaranteed our 6 1/4% senior notes due 2012, 6 1/2% senior notes due 2015, 6 1/2% senior notes due 2017, and 9 3/4% senior notes due 2019. As a result of these guarantee arrangements, we are required to present the following condensed consolidating financial information. The following condensed consolidating financial information should be read in conjunction with the accompanying condensed consolidated financial statements and notes. The following condensed consolidating financial information is provided as an alternative to providing separate financial statements for guarantor subsidiaries. Separate financial statements of Tesoro s subsidiary guarantors are not included because the guarantees are full and unconditional and these subsidiary guarantors are 100% owned and jointly and severally liable for Tesoro s outstanding senior notes. The information is presented using the equity method of accounting for investments in subsidiaries.

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Condensed Consolidating Balance Sheet as of September 30, 2010
(in millions)

	Tesoro Corporation	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Current Assets					
Cash and cash equivalents	$	$ 335	$ 4	$	$ 339
Receivables, less allowance for doubtful accounts	9	896	140		1,045
Inventories		865	184		1,049
Prepayments and other	37	64			101
Total Current Assets	46	2,160	328		2,534
Net Property, Plant and Equipment		5,012	165		5,177
Investment in Subsidiaries	3,970	(120)	(5)	(3,845)	
Long-Term Receivables from Affiliates	2,075			(2,075)	
Other Noncurrent Assets	35	636	1		672
Total Assets	$ 6,126	$ 7,688	$ 489	$ (5,920)	$ 8,383
LIABILITIES AND STOCKHOLDERS EQUITY					
Current Liabilities					
Accounts payable and accrued liabilities	$ 97	$ 1,862	$ 224	$	$ 2,183
Current maturities of debt		3			3
Total Current Liabilities	97	1,865	224		2,186
Long-Term Payables to Affiliates		1,948	127	(2,075)	
Debt	1,821	23			1,844
Other Noncurrent Liabilities	1,001	144	1		1,146
Stockholders Equity	3,207	3,708	137	(3,845)	3,207
Total Liabilities and Stockholders Equity	$ 6,126	$ 7,688	$ 489	$ (5,920)	$ 8,383

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Condensed Consolidating Balance Sheet as of December 31, 2009
(in millions)

	Tesoro Corporation	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Current Assets					
Cash and cash equivalents	$	$ 411	$ 2	$	$ 413
Receivables, less allowance for doubtful accounts	114	760	242		1,116
Inventories		610	12		622
Prepayments and other	28	43	1		72
Total Current Assets	142	1,824	257		2,223
Net Property, Plant and Equipment		5,019	171		5,190
Investment in Subsidiaries	3,999	(102)	(5)	(3,892)	
Long-Term Receivables from Affiliates	1,878		83	(1,961)	
Other Noncurrent Assets	42	615			657
Total Assets	$ 6,061	$ 7,356	$ 506	$ (5,853)	$ 8,070
LIABILITIES AND STOCKHOLDERS EQUITY					
Current Liabilities					
Accounts payable and accrued liabilities	$ 88	$ 1,428	$ 369	$	$ 1,885
Current maturities of debt		4			4
Total Current Liabilities	88	1,432	369		1,889
Long-Term Payables to Affiliates		1,961		(1,961)	
Debt	1,814	23			1,837
Other Noncurrent Liabilities	1,072	183	2		1,257
Stockholders Equity	3,087	3,757	135	(3,892)	3,087
Total Liabilities and Stockholders Equity	$ 6,061	$ 7,356	$ 506	$ (5,853)	$ 8,070

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TESORO CORPORATION
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(Unaudited)
Condensed Consolidating Statement of Operations for the Three Months Ended September 30, 2010
(in millions)

	Tesoro Corporation	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
REVENUES	$	$ 6,746	$ 797	$ (2,223)	$ 5,320
Costs and expenses	2	6,617	795	(2,223)	5,191
OPERATING INCOME (LOSS)	(2)	129	2		129
Equity in earnings (loss) of subsidiaries	58	(4)		(54)	
Other expense		(35)			(35)
EARNINGS (LOSS) BEFORE INCOME TAXES	56	90	2	(54)	94
Income tax provision (a)		37	1		38
NET EARNINGS (LOSS)	$ 56	$ 53	$ 1	$ (54)	$ 56

(a) The income tax provision reflected in each column does not include any tax effect of the equity in earnings from subsidiaries.

Condensed Consolidating Statement of Operations for the Three Months Ended September 30, 2009
(in millions)

	Tesoro Corporation	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
REVENUES	$	$ 5,921	$ 533	$ (1,712)	$ 4,742
Costs and expenses	2	5,831	532	(1,712)	4,653
OPERATING INCOME (LOSS)	(2)	90	1		89
Equity in earnings (loss) of subsidiaries	35	(1)		(34)	
Other expense		(38)			(38)
EARNINGS (LOSS) BEFORE INCOME TAXES	33	51	1	(34)	51

Income tax provision (a)				18						18
NET EARNINGS (LOSS)	$	33	$	33	$	1	$	(34)	$	33

(a) The income tax provision reflected in each column does not include any tax effect of the equity in earnings from subsidiaries.

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TESORO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
Condensed Consolidating Statement of Operations for the Nine Months Ended September 30, 2010
(in millions)

	Tesoro Corporation	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
REVENUES	$	$ 19,227	$ 1,882	$ (6,039)	$ 15,070
Costs and expenses	5	19,157	1,877	(6,039)	15,000
OPERATING INCOME (LOSS)	(5)	70	5		70
Equity in earnings (loss) of subsidiaries	(29)	(18)		47	
Other expense		(108)			(108)
EARNINGS (LOSS) BEFORE INCOME TAXES	(34)	(56)	5	47	(38)
Income tax provision (benefit) (a)	(2)	(7)	3		(6)
NET EARNINGS (LOSS)	$ (32)	$ (49)	$ 2	$ 47	$ (32)

(a) The income tax provision (benefit) reflected in each column does not include any tax effect of the equity in earnings from subsidiaries.

Condensed Consolidating Statement of Operations for the Nine Months Ended September 30, 2009
(in millions)

	Tesoro Corporation	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
REVENUES	$	$ 14,663	$ 1,395	$ (3,855)	$ 12,203
Costs and expenses	5	14,494	1,394	(3,855)	12,038
OPERATING INCOME (LOSS)	(5)	169	1		165
Equity in earnings (loss) of subsidiaries	43	(31)	(3)	(9)	
Other expense		(104)			(104)
EARNINGS (LOSS) BEFORE INCOME TAXES	38	34	(2)	(9)	61

Income tax provision (benefit) (a)	(1)	23			22
NET EARNINGS (LOSS)	$ 39	$ 11	$ (2)	$ (9)	$ 39

(a) The income tax provision (benefit) reflected in each column does not include any tax effect of the equity in earnings from subsidiaries.

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TESORO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
Condensed Consolidating Statement of Cash Flows for the Nine Months Ended September 30, 2010
(in millions)

	Tesoro Corporation	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
CASH FLOWS FROM (USED IN) OPERATING ACTIVITIES					
Net cash from (used in) operating activities	$ 7	$ 354	$ (206)	$	$ 155
CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES					
Capital expenditures		(227)	(1)		(228)
Intercompany notes, net	(4)			4	
Proceeds from asset sales		2			2
Net cash from (used in) investing activities	(4)	(225)	(1)	4	(226)
CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES					
Borrowings under revolving Credit Agreement	66				66
Repayments on revolving Credit Agreement	(66)				(66)
Repayments of debt		(2)			(2)
Proceeds from stock options exercised	4				4
Repurchase of common stock	(3)				(3)
Excess tax benefits from stock-based compensation arrangements		2			2
Financing costs and other	(4)				(4)
Net intercompany borrowings (repayments)		(205)	209	(4)	
Net cash from (used in) financing activities	(3)	(205)	209	(4)	(3)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		(76)	2		(74)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD		411	2		413
CASH AND CASH EQUIVALENTS, END OF PERIOD	$	$ 335	$ 4	$	$ 339

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TESORO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
Condensed Consolidating Statement of Cash Flows for the Nine Months Ended September 30, 2009
(in millions)

	Tesoro Corporation	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
CASH FLOWS FROM OPERATING ACTIVITIES					
Net cash from operating activities	$	$ 607	$ 62	$	$ 669
CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES					
Capital expenditures		(293)	(33)		(326)
Intercompany notes, net	(171)			171	
Proceeds from asset sales		1			1
Net cash from (used in) investing activities	(171)	(292)	(33)	171	(325)
CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES					
Proceeds from debt borrowings, net of discount of $12 million and issuance costs of $6 million	282				282
Borrowings under revolving Credit Agreement	418				418
Repayments on revolving Credit Agreement	(484)				(484)
Repurchase of common stock	(2)				(2)
Dividend payments	(41)				(41)
Repayments of debt		(2)			(2)
Financing costs and other	(3)				(3)
Proceeds from stock options exercised	1				1
Excess tax benefits from stock-based compensation arrangements		1			1
Net intercompany borrowings (repayments)		199	(28)	(171)	
Net cash from (used in) financing activities	171	198	(28)	(171)	170
INCREASE IN CASH AND CASH EQUIVALENTS		513	1		514
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD		20			20
CASH AND CASH EQUIVALENTS, END OF PERIOD	$	$ 533	$ 1	$	$ 534

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Those statements in this section that are not historical in nature should be deemed forward-looking statements that are inherently uncertain. See Important Information Regarding Forward-Looking Statements on page 49 for a discussion of the factors that could cause actual results to differ materially from those projected in these statements. This section should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2009.

BUSINESS STRATEGY AND OVERVIEW

Strategy and Goals

Our refining and marketing business strategy is to create shareholder value in a global market with competitive returns in any economic environment through:

- operating our facilities in a safe, reliable and environmentally responsible way;
- achieving greater operational and administrative efficiencies; and
- using cash flows from operations to create further shareholder value.

We expect industry fundamentals, namely lower refined product demand and excess refining capacity, to continue throughout 2010. Our value creation plan is designed to optimize our cash flows from operations by:

- improving our capture of available margins;
- lowering our break-even costs;
- lowering our energy and maintenance costs; and
- devoting capital to income improvement projects.

We continue to benefit from prior years capital programs that allow us to run less expensive crude oil and further reduce refinery operating expenses. We plan to further improve our capture of available margins and operating profit in 2010 by:

- reducing logistics costs;
- further increasing flexibility in our slate of crude oil feedstocks;
- matching production to demand;
- optimizing profitability by responding to changes in relative product values and crude costs; and
- reducing operating expenses through energy and maintenance efficiency programs.

We have identified approximately 300 high-return projects that we can implement quickly to improve our economic position and create incremental shareholder value. These projects focus on lowering our feedstock costs, improving clean product yields and reducing operating costs, which includes improving energy efficiency at all of our refineries. The majority of these projects will cost less than $1 million. We have reduced our planned 2010 spending for these projects from $50 million to $40 million in an effort to focus our resources at the Washington refinery. We spent $18 million on these projects during the first nine months of 2010.

Tesoro Panama Company Sociedad Anonima (TPSA)

In September 2007, Castor Petroleum (Castor) entered into a Transportation and Storage Agreement (TSA) with Petroterminal de Panama, S.A. (PTP). Concurrent with the execution of the TSA, TPSA entered into a Transportation and Storage Agreement (the TPSA Agreement) with Castor. The TSA provides Castor the use of the Trans-Panama pipeline and several tanks at the Atlantic and Pacific terminals for a seven-year period. The Trans-Panama pipeline (Pipeline) is 81 miles long, with a capacity exceeding 860 thousand barrels per day

(Mbpd). The Pipeline runs across Panama near the Costa Rican border from Port Charco Azul on the Pacific coast to Port Chiriqui Grande, Bocas del Toro on the Caribbean.

As part of our business strategy, we formed TPSA to further utilize the pipeline and tank facilities in Panama by enhancing strategic partnerships, developing economies of scale around freight and storage opportunities, providing discretionary crude oil trading, expanding global commercial relationships and evaluating opportunities to source crude from alternative supply markets. The TPSA Agreement allocates and delegates a portion of Castor s rights, duties, and obligations set forth in the TSA to TPSA. TPSA has access to, and is obligated for, pipeline capacity of more than 100 Mbpd and tank capacity of approximately 4.4 million barrels. TPSA is:

- a directly and wholly consolidated subsidiary of Tesoro Corporation;
- not a subsidiary guarantor of our senior notes;
- an excluded subsidiary (as defined) in the Fourth Amended and Restated Credit Agreement (financing and credit obtained by TPSA will not be guaranteed by Tesoro Corporation); and
- an unrestricted subsidiary and will not be subject to the restrictive covenants in the indentures.

In October 2010, TPSA entered into a revolving credit agreement which provides for an uncommitted, secured revolving credit facility (TPSA Credit Agreement). The TPSA Credit Agreement is non-recourse to the Company, meaning only TPSA is liable for any borrowed amounts or interest. For additional information regarding this agreement, see Capital Resources and Liquidity on page 40.

Industry Overview

Our profitability is heavily influenced by the cost of crude oil and the aggregate value of the products we make from that crude oil and is affected by changes in economic conditions. Product values and crude oil costs are set by the market and are outside of the control of independent refiners.

Crude Oil and Product Price Analysis

Average Key Commodity Prices and Differentials

(Dollars per barrel)

The overall U.S. economy, including that of the West Coast, has shown signs of improvement, though these improvements have not consistently translated into stronger demand for refined products. Measures of commercial activity that are correlated with oil demand continued to show improvement in the third quarter. West Coast port container traffic recovered to its 2007 level in August 2010 and third quarter self-reported available seat miles at the largest U.S.-flagged air carriers were 2.5% higher than the previous year, compared to just 0.6% growth in the 2010 second quarter.

Improved West Coast petroleum product supply and demand fundamentals led to improved product margins in the 2010 third quarter over the 2010 first and second quarters. West Coast gasoline margins improved in the 2010 third quarter approximately 54% over the 2010 first quarter and 2% over the 2010 second quarter, due to seasonal demand increases and several industry-wide unplanned refinery outages. During the same periods, U.S. West Coast benchmark diesel fuel margins increased by approximately 77% and 4%, respectively, from refinery outages and strengthening commercial activity.

Outlook

The current global economic weakness and high unemployment in the U.S. are expected to continue to depress demand for refined products. The impact of low demand has been further compounded by excess global refining capacity and historically high inventory levels. These conditions are expected to continue to put pressure on refined product margins. We expect margins to be negatively impacted until the economy improves further and unemployment declines.

Several refineries in North America and Europe have been temporarily or permanently shut down in response to falling demand and excess refining capacity. We will continue to assess our refineries to determine if a complete or partial shutdown of one or more of the facilities is appropriate.

In addition to current market conditions, there are long-term factors that may impact the supply and demand of refined products in the U.S. These factors include:

- the increased fuel efficiency standards for vehicles;
- the mandated renewable fuels standards;
- potential and enacted climate change legislation;
- the EPA regulation of greenhouse gas emissions under the Clean Air Act; and
- competing refineries being built overseas.

Global Financial Markets

While there are signs of improvement in global financial markets, we remain attentive to the current condition of these markets, including limits to credit availability. While our ability to finance operations has not been impaired, there can be no assurance that there will not be a further deterioration in financial markets and confidence in major economies that could negatively impact us.

Washington Refinery

On April 2, 2010, the naphtha hydrotreater unit at our Washington Refinery was involved in a fire, which fatally injured seven employees and rendered the unit inoperable. Subsequent to the incident, refinery processing was temporarily shut down until after the unit reconstruction was completed. The Washington refinery began to restart certain units during the month of October 2010. We do not believe that this tragic incident will have a material adverse effect on our financial position or results of operations.

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RESULTS OF OPERATIONS THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2010, COMPARED WITH THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2009

A discussion and analysis of the factors contributing to our results of operations is presented below. The accompanying condensed consolidated financial statements, together with the following information, are intended to provide investors with a reasonable basis for assessing our historical operations, but should not serve as the only criteria for predicting our future performance.

Summary

Our net earnings were $56 million ($0.39 per diluted share) for the three months ended September 30, 2010 (2010 Quarter), compared with net earnings of $33 million ($0.24 per diluted share) for the three months ended September 30, 2009 (2009 Quarter). The $23 million increase in net earnings during the 2010 Quarter was primarily due to the following:

- higher industry distillate margins primarily due to strong exports and improvements in manufacturing activity nationwide;
- higher gross refining margins at our Mid-Continent refineries due to downtime at other refineries in the region; and
- higher gross refining margins at our California refineries due to improved product yields and increased throughput of discounted foreign heavy crudes.

The following factors negatively impacted the 2010 Quarter compared to the 2009 Quarter, partially offsetting the increase in net earnings:

- lower refining throughput primarily as a result of the temporary shut-down of processing at the Washington refinery and completion of a planned turnaround at our Hawaii refinery;
- additional costs of $23 million at the Washington refinery, of which $12 million is related to the April 2, 2010, incident and $11 million to maintenance work performed while the refinery was shut down;
- a $4 million one-time charge related to the sublease of office space at our Corporate headquarters; and
- a last-in-first-out (LIFO) liquidation benefit during the 2009 Quarter resulting in a reduction to costs of sales of $12 million.

For the year-to-date periods, our net loss was $32 million ($0.23 per diluted share) for the nine months ended September 30, 2010 (2010 Period), compared with net earnings of $39 million ($0.28 per diluted share) for the nine months ended September 30, 2009 (2009 Period). The $71 million decrease in net earnings during the 2010 Period was primarily due to the following:

- lower refining throughput primarily as a result of the temporary shut-down of processing at the Washington refinery and completion of scheduled refinery turnarounds;
- additional costs of $36 million at the Washington refinery, of which $25 million is related to the April 2, 2010, incident and $11 million to maintenance work performed while the refinery was shut down;
- higher incentive compensation costs of $16 million;
- charges totaling $9 million for preexisting obligations related to the retirement of certain Company officers; and
- a LIFO liquidation benefit during the 2009 Period resulting in a reduction to costs of sales of $12 million.

The following factors positively impacted the 2010 Period compared to the 2009 Period, partially offsetting the decrease in net earnings:

gains on our commodity derivative instruments of $3 million as compared to losses of $61 million during the 2009 Period; and

a $43 million net gain primarily from the elimination of postretirement life insurance benefits for current and future retirees.

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Refining Segment (Dollars in millions except per barrel amounts)	**Three Months Ended September 30, 2010**	**2009**	**Nine Months Ended September 30, 2010**	**2009**
Revenues (a)				
Refined products	$ 4,907	$ 4,489	$ 13,813	$ 11,310
Crude oil resales and other	275	91	863	526
Total Revenues	$ 5,182	$ 4,580	$ 14,676	$ 11,836
Throughput (thousand barrels per day)				
Heavy crude oil (b)	191	162	184	176
Light crude oil	251	361	259	342
Other feedstocks	30	41	29	37
Total Refining Throughput	472	564	472	555
% Heavy Crude Oil of Total Refining Throughput (b)	40%	29%	39%	32%
Yield (thousand barrels per day)				
Gasoline and gasoline blendstocks	238	289	231	278
Jet fuel	63	79	66	70
Diesel fuel	104	113	100	115
Heavy oils, residual products, internally produced fuel and other	95	115	103	124
Total Yield	500	596	500	587
Gross refining margin ($/throughput barrel) (c)	$ 13.28	$ 9.59	$ 10.87	$ 10.04
Manufacturing Cost before Depreciation and Amortization Expense ($/throughput bbl) (c)	$ 6.14	$ 4.79	$ 5.94	$ 4.90

(a) Refined products sales include intersegment sales to our retail segment at prices, which approximate market of $870 million and $764 million for the three months ended September 30, 2010, and 2009, respectively, and $2.4 billion and $2.0 billion for the nine months ended September 30, 2010, and 2009, respectively.

(b) We define heavy crude oil as crude oil with an American Petroleum Institute gravity of 24 degrees or less.

(c) Management uses gross refining margin per barrel to evaluate performance and compare profitability to other companies in the industry. There are a variety of ways to calculate gross refining margin per barrel; different companies may calculate it in different ways. We calculate gross refining margin per barrel by dividing gross refining margin (revenue less costs of feedstocks, purchased refined products, transportation and distribution) by total refining throughput. Management uses manufacturing costs per barrel to evaluate the efficiency of refining operations. There are a variety of ways to calculate manufacturing costs per barrel; different companies may calculate it in different ways. We calculate manufacturing costs per barrel by dividing manufacturing costs by total refining throughput. Investors and analysts use these financial measures to help analyze and compare companies in the industry on the basis of operating performance. These financial measures should not be considered alternatives to segment operating income, revenues, costs of sales and operating expenses or any other measure of financial performance presented in accordance with accounting principles generally accepted in the United States of America.

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Refining Segment	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions except per barrel amounts)	**2010**	**2009**	**2010**	**2009**
Segment Operating Income				
Gross refining margin (d)	$ 577	$ 498	$ 1,402	$ 1,521
Expenses				
Manufacturing costs	266	248	766	743
Other operating expenses	60	69	182	205
Selling, general and administrative expenses	6	7	22	19
Depreciation and amortization expense (e)	92	86	270	263
Loss on asset disposals and impairments (f)	7	4	35	23
Segment Operating Income (g)	$ 146	$ 84	$ 127	$ 268
Refined Product Sales (thousand barrels per day) (h)				
Gasoline and gasoline blendstocks	294	309	285	311
Jet fuel	92	92	93	83
Diesel fuel	131	129	114	123
Heavy oils, residual products and other	72	81	75	85
Total Refined Product Sales	589	611	567	602
Refined Product Sales Margin ($/barrel) (h)				
Average sales price	$ 88.81	$ 83.71	$ 88.95	$ 70.17
Average costs of sales	78.95	76.47	81.20	61.72
Refined Product Sales Margin	$ 9.86	$ 7.24	$ 7.75	$ 8.45

(d) Consolidated gross refining margin combines gross refining margin for each of our regions adjusted for other costs not directly attributable to a specific region. Other costs resulted in a decrease of $3 million for the three months ended September 30, 2009. Gross refining margin includes the effect of intersegment sales to the retail segment at prices, which approximate market. Gross refining margin approximates total refining throughput times gross refining margin per barrel.

(e) Includes manufacturing depreciation and amortization expense per throughput barrel of approximately \$2.01 and \$1.57 for the three months ended September 30, 2010, and 2009, respectively, and \$1.98 and \$1.63 for the nine months ended September 30, 2010, and 2009, respectively.

(f) Includes impairment charges related to our Los Angeles refinery of \$20 million and \$12 million for the nine months ended September 30, 2010, and 2009, respectively.

The nine months ended September 30, 2010, also includes a $4 million charge related to the Washington refinery incident. The loss on asset disposals and impairments is included in refining segment operating income but excluded from the regional operating costs per barrel.

(g) Includes a $36 million net gain for the nine months ended September 30, 2010, primarily from the elimination of postretirement life insurance benefits for current and future retirees.

(h) Sources of total refined product sales includes refined products manufactured at our refineries and refined products purchased from third parties. Total refined product sales margins include margins on sales

of manufactured
and purchased
refined
products.

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Refining Data by Region

(Dollars in millions except per barrel amounts)	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
California (Golden Eagle and Los Angeles)				
Refining throughput (thousand barrels per day) (i)	241	235	223	245
Gross refining margin	$ 305	$ 250	$ 730	$ 771
Gross refining margin ($/throughput barrel) (c)	$13.74	$11.54	$11.97	$11.54
Manufacturing cost before depreciation and amortization expense (c) ($/throughput bbl)	$ 7.02	$ 7.02	$ 7.53	$ 6.72
Pacific Northwest (Alaska and Washington)				
Refining throughput (thousand barrels per day) (i)	64	155	90	136
Gross refining margin	$ 68	$ 129	$ 230	$ 335
Gross refining margin ($/throughput barrel) (c)	$11.68	$ 9.08	$ 9.40	$ 9.04
Manufacturing cost before depreciation and amortization expense (c) ($/throughput bbl)	$10.23	$ 3.04	$ 6.27	$ 3.74
Mid-Pacific (Hawaii)				
Refining throughput (thousand barrels per day) (i)	53	66	62	68
Gross refining margin	$ 25	$ 7	$ 58	$ 78
Gross refining margin ($/throughput barrel) (c)	$ 5.00	$ 1.05	$ 3.39	$ 4.17
Manufacturing cost before depreciation and amortization expense (c) ($/throughput bbl)	$ 3.93	$ 3.26	$ 3.16	$ 3.07
Mid-Continent (North Dakota and Utah)				
Refining throughput (thousand barrels per day) (i)	114	108	97	106
Gross refining margin	$ 179	$ 115	$ 384	$ 337
Gross refining margin ($/throughput barrel) (c)	$17.16	$11.50	$14.52	$11.64
Manufacturing cost before depreciation and amortization expense (c) ($/throughput bbl)	$ 3.04	$ 3.37	$ 3.78	$ 3.39

(i) We experienced reduced throughput due to scheduled turnarounds at our Hawaii refinery during the 2010 Quarter and North Dakota, Golden Eagle and Utah refineries in the 2010 Period. We temporarily shut-down processing at the Washington refinery beginning in April 2010. We experienced reduced throughput due to scheduled turnarounds at our Alaska and Golden Eagle refineries and scheduled maintenance at our Washington refinery during the 2009 Period.

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Three Months Ended September 30, 2010, Compared with Three Months Ended September 30, 2009

Overview. Operating income for our refining segment increased by $62 million during the 2010 Quarter primarily due to higher gross refining margins. The significantly higher gross refining margin per barrel positively impacted total gross refining margins by $79 million during the 2010 Quarter.

Gross Refining Margins. Our gross refining margin per barrel increased to $13.28 per barrel in the 2010 Quarter compared to $9.59 per barrel in the 2009 Quarter reflecting higher industry diesel fuel margins. Industry diesel fuel margins in the U.S. West Coast and Mid-Continent regions increased, primarily due to strong exports and improvements in manufacturing activity nationwide.

Gross refining margins for our California region were positively impacted by improved product yields and increased throughput of discounted foreign heavy crudes. Our California refineries run a high proportion of the heavy, less expensive crude oils (73% of our total California region refining throughput during the 2010 Quarter). Gross refining margins for our Mid-Continent region increased due to lower regional refining production from scheduled and unscheduled downtime at certain refineries during the 2010 Quarter.

We periodically use derivative instruments, primarily to manage exposure to commodity price risks associated with the purchase or sale of crude oil and finished products. We may also use commodity derivative instruments to manage price risks associated with inventories above or below our target levels. Gains or losses associated with our commodity derivative instruments are included in gross refining margin. Losses totaled $3 million during the 2010 Quarter versus losses of $6 million during the 2009 Quarter.

Refining Throughput. Total refining throughput decreased 92 Mbpd during the 2010 Quarter, primarily due to the temporary shut-down of processing at the Washington refinery subsequent to the April 2, 2010, naphtha hydrotreater fire and our scheduled turnaround activity at the Hawaii refinery.

Refined Products Sales. Revenues from sales of refined products increased 9% to $4.9 billion in the 2010 Quarter as compared to the 2009 Quarter, primarily due to higher refined product sales prices, partially offset by a decrease in refined product sales volume. Our average product sales price increased 6% to $88.81 per barrel in the 2010 Quarter as higher crude oil prices put upward pressure on product prices. Total refined product sales volumes decreased 4% or 22 Mbpd from the 2009 Quarter, primarily reflecting reduced throughput.

Costs of Sales and Expenses. Our average costs of sales increased 3% to $78.95 per barrel during the 2010 Quarter reflecting higher crude oil prices. Manufacturing and other operating expenses increased to $326 million in the 2010 Quarter, compared to $317 million in the 2009 Quarter primarily from increased operating expenses at the Washington refinery related to the April 2, 2010, incident, maintenance work performed at the Washington refinery while it was shut down and higher natural gas costs primarily at our California refineries.

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Nine Months Ended September 30, 2010, Compared with Nine Months Ended September 30, 2009

Overview. Operating income for our refining segment decreased by $141 million during the 2010 Period primarily due to significantly reduced refining throughputs. Total gross refining margins decreased by $119 million and were substantially impacted by a 15% decline in throughputs. The 2010 Period included $36 million in costs at the Washington refinery and an $8 million increase in charges at the Los Angeles refinery, partially offset by a $36 million net gain primarily from the elimination of postretirement life insurance benefits. The 2009 Period included a LIFO liquidation benefit resulting in a reduction to costs of sales of $12 million.

Gross Refining Margins. Our gross refining margin per barrel increased to $10.87 per barrel in the 2010 Period, compared to $10.04 per barrel in the 2009 Period reflecting higher industry distillate margins. Industry gasoline margins substantially decreased reflecting poor global demand and higher inventories resulting from high domestic unemployment rates.

Gross refining margins were most significantly impacted by substantially lower throughputs. The decrease in gross refining margins was partially offset by an increase in our Mid-Continent region. The increase is primarily due to lower regional refining production caused by scheduled and unscheduled downtime in the 2010 Period at other refineries in the Mid-Continent region.

We periodically use derivative instruments, primarily to manage exposure to commodity price risks associated with the purchase or sale of crude oil and finished products. We may also use commodity derivative instruments to manage price risks associated with inventories above or below our target levels. Gains or losses associated with our commodity derivative instruments are included in gross refining margin. Gains totaled $3 million during the 2010 Period versus losses of $61 million during the 2009 Period. Crude prices increased significantly during the 2009 Period compared to marginal increases during the 2010 Period. This pricing difference and lower price volatility impacted derivative results during the 2010 Period.

Our policy is to test for goodwill impairment annually, or more frequently if indications of impairment exist. We evaluated current economic conditions and events, and did not identify any triggering events or indicators of impairment within our reporting units during the quarter. It is possible that future economic changes or changes in our estimates could have a material effect on the carrying amount of goodwill. We will perform our annual impairment test in the fourth quarter.

Refining Throughput. Total refining throughput decreased 83 Mbpd during the 2010 Period. The significant decrease in throughput was primarily caused by the temporary shut-down of processing at the Washington refinery subsequent to the April 2, 2010, naphtha hydrotreater fire. Additionally, scheduled turnarounds at the Utah refinery, North Dakota refinery and Hawaii refinery, and our efforts to match production with decreased product demand in the 2010 Period lowered our refining throughputs.

Refined Products Sales. Revenues from sales of refined products increased 22% to $13.8 billion in the 2010 Period as compared to the 2009 Period, primarily due to higher average refined product sales prices partially offset by lower refined product sales volumes. Our average product sales price increased 27% to $88.95 per barrel in the 2010 Period as significantly higher average crude oil prices placed upward pressure on product prices. Total refined product sales volumes decreased 6% or 35 Mbpd, primarily reflecting lower product demand.

Costs of Sales and Expenses. Our average costs of sales increased 32% to $81.20 per barrel during the 2010 Period reflecting significantly higher average crude oil prices. Manufacturing and other operating expenses were consistent during the 2010 and 2009 Periods. The 2010 Period included increased operating expenses at the Washington refinery related to the April 2, 2010, incident, maintenance work performed at the Washington refinery while it was shut down and higher natural gas costs primarily at our California refineries. Additionally, there were significantly higher natural gas costs at both of our California refineries.

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Retail Segment

(Dollars in millions except per gallon amounts)	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Revenues				
Fuel	$ 947	$ 863	$ 2,647	$ 2,182
Merchandise and other	61	63	171	178
Total Revenues	$ 1,008	$ 926	$ 2,818	$ 2,360
Fuel Sales (millions of gallons)	351	345	1,000	1,004
Fuel Margin ($/gallon) (a)	$ 0.22	$ 0.28	$ 0.22	$ 0.19
Merchandise Margin (in millions)	$ 14	$ 14	$ 40	$ 39
Merchandise Margin (percent of sales)	26%	25%	26%	25%
Average Number of Stations (during the period)				
Company-operated	383	388	384	388
Branded jobber/dealer	497	483	499	487
Total Average Retail Stations	880	871	883	875
Segment Operating Income (Loss)				
Gross Margin				
Fuel (b)	$ 76	$ 98	$ 223	$ 189
Merchandise and other non-fuel margin	20	21	59	58
Total Gross Margin	96	119	282	247
Expenses				
Operating expenses	49	51	148	153
Selling, general and administrative expenses	5	5	14	21
Depreciation and amortization expense	10	10	30	29
Loss on asset disposals and impairments			4	2
Segment Operating Income	$ 32	$ 53	$ 86	$ 42

(a) Management uses fuel margin per gallon to compare profitability to other companies in the industry. There are a variety of ways to calculate fuel margin per gallon; different companies may calculate it in different ways. We calculate fuel margin per gallon by dividing fuel margin by fuel sales volumes. Investors and analysts use fuel margin per gallon to help analyze and compare companies in the industry on the basis of operating performance. This financial measure should not be considered an alternative to segment operating income and revenues or any other measure of financial performance presented in accordance with accounting principles generally accepted in the United States of America.

(b) Includes the effect of intersegment purchases from our refining segment at prices, which approximate market.

Three Months Ended September 30, 2010, Compared with Three Months Ended September 30, 2009

Revenues on fuel sales increased to $947 million in the 2010 Quarter, from $863 million in the 2009 Quarter, reflecting higher retail fuel sales prices, and costs of sales increased due to higher prices for purchased fuel. Operating income for our retail segment decreased by $21 million to $32 million in the 2010 Quarter reflecting significantly lower fuel margins. Fuel margin per gallon decreased 21% from the 2009 Quarter.

Nine Months Ended September 30, 2010, Compared with Nine Months Ended September 30, 2009

Revenues on fuel sales increased to $2.6 billion in the 2010 Period, from $2.2 billion in the 2009 Period, reflecting higher retail sales prices, and costs of sales increased due to higher prices for purchased fuel. Operating income for our retail segment increased by $44 million in the 2010 Period reflecting higher fuel margins and decreased expenses. Fuel margin per gallon increased 16% from the 2009 Period.

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Consolidated Results of Operations

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased by $1 million and $3 million during the 2010 Quarter and 2010 Period, respectively. During the 2010 Period, we incurred increased incentive compensation expenses that were offset by a net gain recognized primarily from the elimination of postretirement life insurance for current and future retirees.

Interest and Financing Costs

Interest and financing costs increased by $5 million and $20 million during the 2010 Quarter and 2010 Period, respectively. The increase was primarily due to additional interest expense recognized during the 2010 Period as a result of increases in 2010 letter of credit fees from the February 2010 amendment to our Credit Agreement, partially offset by a $5 million reduction in estimated interest from the settlement of a state tax audit.

Foreign Currency Exchange Gain (Loss)

In the 2010 Quarter and 2010 Period, we had foreign currency gains of $1 million and $2 million, respectively, compared to foreign currency losses of $3 million and $13 million in the 2009 Quarter and 2009 Period, respectively. The improved results are due to efforts to manage exchange rate risk in foreign currency.

Income Tax Provision (Benefit)

Our income tax provision totaled $38 million for the 2010 Quarter versus $18 million in the 2009 Quarter. In the 2010 Period, the income tax benefit totaled $6 million versus a tax provision of $22 million in the 2009 Period. The 2010 and 2009 Periods included non-recurring tax expenses of $8 million primarily related to recent health care legislation and $1 million of non-recurring tax benefits, respectively.

CAPITAL RESOURCES AND LIQUIDITY

Overview

We operate in an environment where our capital resources and liquidity are impacted by a variety of factors beyond our control, including changes in the price of crude oil and refined products, availability of trade credit, market uncertainty, the level of consumer demand for transportation fuels, weather conditions, fluctuations in seasonal demand, governmental regulations, geo-political conditions and overall market and global economic conditions. See Important Information Regarding Forward-Looking Statements on page 49 for further information related to risks and other factors. Future capital expenditures, as well as borrowings under our credit agreement and other sources of capital, may be affected by these conditions.

Our primary sources of liquidity have been cash flows from operations and borrowing availability under revolving lines of credit. We ended the 2010 Quarter with $339 million of cash and cash equivalents, no borrowings under our revolver, and approximately $827 million in available borrowing capacity under our credit agreement after $669 million in outstanding letters of credit. At September 30, 2010, we also had three separate letter of credit agreements with a total capacity of $550 million, of which we had $332 million available after $218 million in outstanding letters of credit. Our total capacity of $1.86 billion under the credit agreement can be increased up to a total capacity of $2.0 billion. We can also increase the capacity of our separate letter of credit agreements.

Our credit agreement and senior notes impose various restrictions and covenants that could potentially limit our ability to respond to market conditions, raise additional debt or equity capital, pay cash dividends, or repurchase stock. The indentures for our senior notes contain covenants and restrictions which are customary for notes of this nature. These covenants and restrictions limit, among other things, our ability to:

- pay dividends and other distributions with respect to our capital stock and purchase, redeem or retire our capital stock;
- incur additional indebtedness and issue preferred stock;
- sell assets unless the proceeds from those sales are used to repay debt or are reinvested in our business;
- incur liens on assets to secure certain debt;
- engage in certain business activities;
- engage in certain merger or consolidations and transfers of assets; and
- enter into transactions with affiliates.

The indentures also limit our subsidiaries ability to make certain payments and distributions.

Tesoro Corporation Credit Agreement (Credit Agreement) Revolving Credit Facility

We amended our Credit Agreement in February 2010. The modifications included the following:

- the minimum tangible net worth requirement (as defined) was lowered;
- the purchase or sale of certain assets is no longer subject to the fixed charge coverage ratio;
- the covenant permitting additional unsecured indebtedness (as defined) increased from $75 million to $600 million;
- letters of credit allowed under separate letter of credit agreements, previously capped at $500 million, are no longer subject to a cap;
- the applicable margin (as defined) was adjusted; and
- the annual rate of commitment fees for the unused portion of the revolving credit facility was adjusted to 0.50% from 0.375%.

At September 30, 2010, our Credit Agreement provided for borrowings (including letters of credit) up to the lesser of the amount of a periodically adjusted borrowing base of approximately $1.5 billion (based upon an Alaska North Slope crude oil price of $72 per barrel), consisting of Tesoro s eligible cash and cash equivalents, receivables and petroleum inventories, net of the standard reserve as defined, or the agreement s total capacity of $1.86 billion.

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The total capacity can be further increased from $1.86 billion up to $2.0 billion. As of September 30, 2010, we had no borrowings and $669 million in letters of credit outstanding under the Credit Agreement, resulting in total unused credit availability of approximately $827 million or 55% of the eligible borrowing base.

Borrowings under the revolving credit facility bear interest at either a base rate (3.25% at September 30, 2010), or a Eurodollar rate (0.26% at September 30, 2010) plus an applicable margin. The applicable margin at September 30, 2010, was 2.25% in the case of the Eurodollar rate, but varies based upon our credit facility s credit availability and credit ratings. Letters of credit outstanding under the revolving credit facility incur fees at an annual rate tied to the applicable margin described above (2.25% at September 30, 2010). We also incur commitment fees for the unused portion of the revolving credit facility at an annual rate of 0.50% as of September 30, 2010. Our Credit Agreement expires in May 2012.

Lehman Commercial Paper Inc. (Lehman CPI) was one of the lenders under our Credit Agreement, representing a commitment of $50 million (less than 3% of our total Credit Agreement capacity). In October 2008, Lehman CPI filed for bankruptcy. Barclays Bank PLC assumed the $50 million commitment from Lehman CPI in April 2010. As a result, our capacity increased from $1.81 billion to $1.86 billion in April 2010 and remained $1.86 billion at September 30, 2010.

The Credit Agreement contains covenants and conditions that, among other things, limit our ability to pay cash dividends, incur indebtedness, create liens and make investments. Borrowing availability under the Credit Agreement is based on a minimum fixed charge coverage ratio. We have a default covenant, which requires us to maintain specified levels of tangible net worth. We were in compliance with the tangible net worth requirement for the three months ended September 30, 2010. The Credit Agreement is guaranteed by substantially all of Tesoro s active domestic subsidiaries. The Credit Agreement allows up to $100 million of restricted payments during any four quarter period subject to credit availability exceeding 20% of the borrowing base.

We believe available capital resources will be adequate to meet our capital expenditure, working capital and debt service requirements. Due to the current unfavorable economic conditions in the refining industry, we continue to focus on maximizing our available cash through the management of working capital, capital expenditures and operating expenses. However, if industry refining margins remain depressed for an extended period of time, we may be required to materially alter our operations which could include continuing to defer capital expenditures, selling assets or temporarily idling one or more of our refineries.

Tesoro Panama Company Sociedad Anonima (TPSA) Credit Agreement

As part of our business strategy, we formed TPSA to further utilize the pipeline and tank facilities in Panama by enhancing strategic partnerships, developing economies of scale around freight and storage opportunities, providing discretionary crude oil trading, expanding global commercial relationships and evaluating opportunities to source crude from alternative supply markets. TPSA is:

- a directly and wholly consolidated subsidiary of Tesoro Corporation;
- not a subsidiary guarantor of our senior notes;
- an excluded subsidiary (as defined) in the Fourth Amended and Restated Credit Agreement (financing and credit obtained by TPSA will not be guaranteed by Tesoro Corporation); and
- an unrestricted subsidiary and will not be subject to the restrictive covenants in the indentures.

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On October 18, 2010, TPSA entered into an uncommitted revolving credit agreement that is non-recourse to the Company. The TPSA Credit Agreement will provide for:

- up to $260 million in an uncommitted, secured revolving credit facility available for revolving loans, swing line loans, daylight overdraft loans and the issuance on an uncommitted basis of letters of credit. This facility will be used for advances in connection with the purchase, storage and sale of crude oil inventories and for related hedging and working capital requirements;
- up to $150 million uncommitted, secured facility available for letters of credit and advances. This facility will be used to finance TPSA s purchase of crude oil from suppliers through the issuance of letters of credit;
- both facilities are available on an uncommitted basis subject to the applicable maximums (at closing, the combined facility maximum was $350 million consisting of $245 million under the first facility and $105 million under the second facility), and
- the facilities can be further increased up to $700 million provided facilities maximum amounts do not exceed $550 million and $350 million, respectively.

Under the TPSA Credit Agreement, each extension of credit will bear interest, at the following rates per annum:

- TPSA may select between an Eurodollar Rate plus an Applicable Margin (as defined), or an Alternative Base Rate (as defined), for borrowings under the revolving credit facility;
- the Applicable Margin (as defined) for letters of credit will be 1.75% for both facilities; and
- for loans the Alternative Base Rate (as defined) plus the Applicable Margin (as defined) plus 0.50% per annum.

The TPSA Credit Agreement contains the following default financial covenants, as they relate to TPSA financial results:

- maximum Leverage Ratio (as defined);
- Minimum Adjusted Tangible Net Worth (as defined), based on the Combined Facility Maximum Amount (as defined);
- Minimum Adjusted Net Working Capital (as defined), based on the Combined Facility Maximum Amount (as defined); and
- maximum inventory levels below certain thresholds depending on the Combined Facility Maximum Amount (as defined).

Cash Dividends

In February 2010, we suspended our quarterly cash dividend indefinitely to preserve cash and maintain a strong balance sheet as we expect further refining margin volatility. This action also provides us flexibility to allocate capital to our quick-return projects, which we believe will deliver the highest shareholder return in a low margin environment.

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Capitalization

Our capital structure at September 30, 2010, was comprised of the following (in millions):

Debt, including current maturities:	
Credit Agreement Revolving Credit Facility	$
$6^1/_4$% Senior Notes Due 2012	450
$6^5/_8$% Senior Notes Due 2015	450
$6^1/_2$% Senior Notes Due 2017	500
9 $^3/4$% Senior Notes Due 2019, net of unamortized discount of $11 million	289
Junior subordinated notes due 2012, net of unamortized discount of $18 million	132
Capital lease obligations and other	26
Total debt	1,847
Stockholders equity	3,207
Total Capitalization	$ 5,054

At September 30, 2010, and December 31, 2009, our debt to capitalization ratio was 37%.

Cash Flow Summary

Components of our cash flows are set forth below (in millions):

	Nine Months Ended September 30,	
	2010	**2009**
Cash Flows From (Used In):		
Operating Activities	$ 155	$ 669
Investing Activities	(226)	(325)
Financing Activities	(3)	170
Increase (Decrease) in Cash and Cash Equivalents	$ (74)	$ 514

Net cash from operating activities during the 2010 Period totaled $155 million compared to net cash from operating activities of $669 million in the 2009 Period. The decrease in net cash from operating activities of $514 million was primarily due to lower net earnings and increased working capital levels, which was partially offset by income tax refunds received in the 2010 Period. Net cash used in investing activities of $226 million was primarily related to capital expenditures. Net cash used in financing activities during the 2010 Period totaled $3 million, compared to net cash from financing activities of $170 million in the 2009 Period. The decrease primarily reflects the net proceeds from our senior notes issuance in June 2009 partially offset by repayments on our revolver and dividend payments.

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Capital Expenditures

Our 2011 capital budget is $380 million. During 2010, we expect to spend approximately $320 million, which is below our 2010 capital budget of $450 million. The decrease in capital spending is generally a result of increased efficiencies in our current capital program, identification of lower than previously expected materials and labor costs and deferral of non-essential capital projects. Capital spending during the 2010 Quarter and 2010 Period was $75 million and $219 million, respectively. Our capital budgets and spending amounts are comprised of the following project categories at September 30, 2010:

Project Category	Percent of 2011 Capital Budget	Percent of 2010 Expected Capital Spending	Percent of 2010 Quarter Capital Spending	Percent of 2010 Period Capital Spending
Regulatory	40%	60%	54%	60%
Sustaining	30%	30%	39%	32%
Income Improvement	30%	10%	7%	8%

The increase in the percentage of income improvement projects from 2010 to 2011 is consistent with our strategy to focus a portion of capital spending on high-return projects that we can implement quickly to improve our economic position and create incremental shareholder return.

See Business Strategy and Overview and Environmental Capital Expenditures for additional information.

Refinery Turnaround Spending

Our 2011 budget is $165 million for refinery turnarounds primarily at our Golden Eagle and Los Angeles refineries. We spent $130 million for refinery turnarounds and catalysts during the 2010 Period primarily at our Utah, Golden Eagle, North Dakota and Hawaii refineries, including $35 million in the 2010 Quarter primarily at our Hawaii refinery. During the remainder of 2010, we expect to spend an additional $21 million primarily at our Los Angeles and Golden Eagle refineries. Refining throughput and yields were affected by the scheduled turnaround at our Hawaii refinery during the third quarter.

Off-Balance Sheet Arrangements

We have not entered into any transactions, agreements or other contractual arrangements that would result in off-balance sheet liabilities.

Environmental and Other Matters

We are a party to various litigation and contingent loss situations, including environmental and income tax matters, which arise in the ordinary course of business. Although we cannot predict the ultimate outcomes of these matters with certainty, we have accrued for the estimated liabilities when appropriate. We believe that the outcome of these matters will not materially impact our liquidity and consolidated financial position, although the resolution of certain of these matters could have a material impact on interim or annual results of operations. Additionally, if applicable, we accrue receivables for probable insurance or other third party recoveries.

We are subject to extensive federal, state and local environmental laws and regulations. These laws, which change frequently, regulate the discharge of materials into the environment and may require us to remove or mitigate the environmental effects of the disposal or release of petroleum or chemical substances at various sites, install additional controls, or modify certain emission sources.

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Future expenditures may be required to comply with the Clean Air Act and other federal, state and local requirements for our various sites, including our refineries, tank farms, pipelines, operating retail stations, closed retail stations, operating refined-products terminals and closed refined products terminals. The impact of legislative and regulatory developments, including any greenhouse gas cap-and-trade program or low carbon fuel standards, could result in increased compliance costs, additional operating restrictions on our business and an increase in the cost of the products we manufacture, which could have an adverse impact on our financial position, results of operations and liquidity.

In December 2007, the U.S. Congress passed the Energy Independence and Security Act that created a second Renewable Fuels Standard (RFS2). This standard requires the total volume of renewable transportation fuels (including ethanol and advanced biofuels) sold or introduced in the U.S. to reach 12.95 billion gallons in 2010 and rise to 36 billion gallons by 2022. The requirements could reduce future demand for petroleum products that we manufacture. In the near term, the RFS2 presents production and logistics challenges for the ethanol, alternative fuel and refining and marketing industries. Additional expenditures could be required to logistically accommodate the increased use of renewable transportation fuels.

In California, Assembly Bill 32 (AB 32), created a statewide cap on greenhouse gas emissions and requires that the state return to 1990 emissions levels by 2020. AB 32 focuses on using market mechanisms, such as a cap-and-trade program and a Low Carbon Fuel Standard (LCFS) to achieve emissions reduction targets. The LCFS became effective in January 2010 and requires a 10% reduction in the carbon intensity of gasoline and diesel fuel by 2020. Final regulations for all other aspects of AB 32, including cap-and-trade requirements, are being developed by the California Air Resources Board, will take effect in 2012 and will be fully implemented by 2020. The implementation and implications of AB 32 will take many years to realize, and we cannot currently predict its impact on our financial position, results of operations and liquidity.

In 2009, the U.S. Environmental Protection Agency proposed regulating greenhouse gas emissions under the Clean Air Act. The first of these regulations, finalized on April 1, 2010, sets standards for the control of greenhouse gas emissions from light trucks and cars. It could reduce the demand for our manufactured transportation fuels. In addition, other proposed regulations include permitting requirements for stationary sources that emit greenhouse gases above a certain threshold. The resulting permitting requirements could impose emission controls that increase required capital expenditures at our refineries.

We are subject to extensive federal, state and local tax laws and regulations. Newly enacted tax laws and regulations, and changes in existing tax laws and regulations, could result in increased expenditures in the future.

We are also subject to audits by federal, state and local taxing authorities in the normal course of business. It is possible that tax audits could result in claims against us in excess of recorded liabilities. We believe that resolution of any such claim(s) would not materially affect our consolidated financial position or results of operations. We believe it is possible that unrecognized tax benefits could decrease by as much as $11 million in the next twelve months through settlements or other conclusions, primarily regarding state tax issues.

Environmental Liabilities

We are, and expect to continue, incurring expenses for environmental liabilities at a number of currently and previously owned or operated refining, pipeline, terminal and retail station properties. We have accrued liabilities for these expenses and believe these accruals are adequate. At September 30, 2010, and December 31, 2009, our accruals for environmental expenditures totaled $107 million and $106 million, respectively. Our environmental accruals are based on estimates including engineering assessments, and it is possible that our estimates will change and additional costs will be recorded as more information becomes available.

We received $58.5 million in a settlement with a prior owner of our Golden Eagle refinery in 2007 in exchange for assuming responsibility for certain environmental liabilities arising from operations at the refinery prior to August 2000. These environmental liabilities totaled $63 million and $73 million at September 30, 2010, and December 31, 2009, respectively. We cannot presently determine the full extent of remedial activities that may be required at the Golden Eagle refinery. Therefore, it is possible that we will identify additional remediation costs as more

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information becomes available. We have filed insurance claims under environmental insurance policies that provide coverage up to $190 million for expenditures in excess of $50 million in self-insurance. Amounts recorded for environmental liabilities have not been reduced for possible insurance recoveries.

We are continuing to investigate conditions at certain active wastewater treatment units at our Golden Eagle refinery. This investigation is driven by an order from the San Francisco Bay Regional Water Quality Control Board that names us as well as two previous owners of the Golden Eagle refinery. Costs to investigate these conditions are included in our environmental accruals. We cannot currently estimate the amount of the ultimate resolution of the order but we believe it will not have a material adverse effect on our financial position or results of operations.

Other Matters

In the ordinary course of business, we become party to lawsuits, administrative proceedings and governmental investigations, including environmental, regulatory and other matters. Large, and sometimes unspecified, damages or penalties may be sought from us in some matters for which the likelihood of loss may be possible but the amount of loss is not currently estimable. As a result, we have not established accruals for these matters. On the basis of existing information, we believe that the resolution of these matters, individually or in the aggregate, will not have a material adverse effect on our financial position or results of operations.

On April 2, 2010, the naphtha hydrotreater unit at our Washington Refinery was involved in a fire, which fatally injured seven employees and rendered the unit inoperable. Subsequent to the incident, refinery processing was temporarily shut down until after the unit reconstruction was completed. The Washington refinery began to restart certain units during the month of October 2010. We have incurred $25 million in charges related to the incident. We do not believe that this tragic incident will have a material adverse effect on our financial position or results of operations.

We maintain comprehensive property (including business interruption), workers compensation, and general liability insurance policies with significant loss limits. Our business interruption insurance deductible is satisfied after we have exceeded both 60 days of operational disruption and $25 million in losses primarily based on the operating plan that existed prior to the incident. Our property damage insurance has a $10 million deductible. We have filed business interruption insurance claims and will be filing property damage claims related to this incident. Subsequent to September 30, 2010, we received $27 million in business interruption insurance recoveries. We have not recognized possible insurance recoveries in our financial statements as of and for the three and nine months ended September 30, 2010.

On February 5, 2010, the EPA filed suit against us alleging violations of the Clean Air Act and corresponding regulatory requirements concerning the testing and reporting of transportation fuels and fuel additives. In February 2009, we received a Notice of Violation (NOV) from the EPA for alleged violations arising from a compliance review conducted by the EPA in 2006 for the years 2003 through the time of the review in 2006. We are discussing the alleged violations contained in the suit with the EPA and the U.S. Department of Justice and have not established an accrual for this matter. On the basis of existing information, we believe that the resolution of this matter will not have a material adverse effect on our financial position or results of operations.

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We are a defendant, along with other manufacturing, supply and marketing defendants, in six lawsuits alleging MTBE contamination in groundwater. We were served with the sixth lawsuit on April 22, 2010. The defendants are being sued for having manufactured MTBE and having manufactured, supplied and distributed gasoline containing MTBE. The plaintiffs in the six cases, all in California, are municipalities and governmental authorities. The plaintiffs allege, in part, that the defendants are liable for manufacturing or distributing a defective product. The suits generally seek individual, unquantified compensatory and punitive damages and attorney s fees. We intend to vigorously assert our defenses against these claims.

Prior to this year, we received two NOVs from the EPA for the Washington refinery alleging that, prior to our acquisition of the refinery, certain modifications were made to the fluid catalytic cracking unit in violation of the Clean Air Act. We have investigated the allegations and believe we have defenses to the allegations and intend to vigorously defend ourselves.

Prior to this year, we received a NOV from the EPA concerning our Utah refinery alleging certain violations of the Clean Air Act at the refinery beginning in 2004. We have investigated the allegations contained in the NOV and sent the EPA additional information in 2009.

During 2009, Chevron filed a lawsuit against us claiming they are entitled to a share of the refunds we received in 2008 from the owners of the Trans Alaska Pipeline System (TAPS). We received $50 million in 2008, net of contingent legal fees, for excessive intrastate rates charged by TAPS during 1997 through 2000, and the period of 2001 through June 2003. Chevron is asserting that it is entitled to a share of its portion of the refunds for retroactive price adjustments under our previous crude oil contracts with them. In September 2010, the trial court judge granted Chevron s motion for summary judgment and awarded them $16 million. We disagree with the trial court and intend to appeal the decision to the Alaska Supreme Court. We believe that the outcome of this matter will not materially impact our liquidity and consolidated financial position, although the resolution of this matter could have a material impact on interim or annual results of operations.

On July 21, 2010, the President signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act, also known as the Financial Reform Act of 2010. The key provisions of the Financial Reform Act require that standardized swaps be cleared through a registered clearinghouse and executed on a registered trading platform with specific margin requirements. The requirements in the Financial Reform Act could make these products more complicated or costly by creating new regulatory risks and increasing reporting, capital, and administrative requirements for companies that use derivatives for hedging and trading activities. Final rules on provisions in the legislation will be established and will not take effect until twelve months after the date of enactment. Although we cannot predict the ultimate outcome of this legislation, new regulations in this area may result in increased hedging costs and cash collateral requirements, and ultimately affect liquidity and working capital requirements.

Environmental Capital Expenditures

The EPA issued regulations in February 2007 that require the reduction of benzene in gasoline. We expect to spend approximately $166 million in 2010 through 2012 at five of our refineries to comply with the regulations, including $50 million spent in the 2010 Period. Our California refineries will not require capital spending to meet the benzene reduction standards.

Regulations issued by California s South Coast Air Quality Management District require the emission of nitrogen oxides to be reduced through 2011 at our Los Angeles refinery. Currently, we plan to meet this requirement by implementing operational changes, small capital projects and the continued management of our offsetting emissions credits.

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Other projects at our Los Angeles refinery include replacing underground pipelines with above-ground pipelines to comply with an order from the California Regional Water Quality Control Board. We expect to spend approximately $39 million from 2010 through 2015 to complete the project.

We completed installing equipment at our Golden Eagle refinery during the 2010 first quarter with spending in the 2010 Period of $12 million, to eliminate the use of atmospheric blowdown towers as emergency relief systems.

We expect to spend approximately $17 million through 2013 to reconfigure and replace above-ground storage tank systems at our Golden Eagle refinery including $8 million spent in the 2010 Period.

We have evaluated alternative projects for wharves at our Golden Eagle refinery to meet engineering and maintenance standards issued by the State of California in February 2006 and expect certain commercial transactions could significantly reduce our capital spending. We are currently working with counterparties on these agreements. Based on the updated alternative, we expect to spend $20 million in 2011 through 2013. The timing of these projects is under evaluation and is subject to change.

We are required under a consent decree with the EPA to reduce air emissions at our North Dakota and Utah refineries. We expect to spend approximately $6 million in 2010. We have spent $5 million in 2010 to install emission controls for nitrogen oxides on boilers and heaters at these refineries and expect to complete these projects this year.

The cost estimates for the environmental projects described above are subject to further review and analysis and include estimates for capitalized interest and labor costs.

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IMPORTANT INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (including information incorporated by reference) includes and references forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements relate to, among other things, expectations regarding refining margins, revenues, cash flows, capital expenditures, turnaround expenses, and other financial items. These statements also relate to our business strategy, goals and expectations concerning our market position, future operations, margins and profitability. We have used the words anticipate , believe , could , estimate , expect , intend , may , plan , predict , project , will , w and phrases to identify forward-looking statements in this Quarterly Report on Form 10-Q, which speak only as of the date the statements were made.

Although we believe the assumptions upon which these forward-looking statements are based are reasonable, any of these assumptions could prove to be inaccurate and the forward-looking statements based on these assumptions could be incorrect.

The matters discussed in these forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and trends to differ materially from those made, projected, or implied in or by the forward-looking statements depending on a variety of uncertainties or other factors including, but not limited to:

- changes in global economic conditions and the effects of the global economic downturn on our business and the business of our suppliers, customers, business partners and lenders;
- disruptions due to equipment interruption or failure at our facilities or third-party facilities; the timing and extent of changes in commodity prices and demand for our refined products;
- operational hazards inherent in refining operations and in transporting and storing crude oil and refined products; changes in our cash flow from operations; actions of customers and competitors;
- state and federal environmental, economic, health and safety, energy and other policies and regulations, any changes therein, and any legal or regulatory investigations, delays or other factors beyond our control;
- risks related to labor relations and workplace safety;
- adverse rulings, judgments, or settlements in litigation or other legal or tax matters, including unexpected environmental remediation costs in excess of any accruals;
- changes in capital requirements or in execution of planned capital projects;
- direct or indirect effects on our business resulting from actual or threatened terrorist incidents or acts of war;
- political developments;
- changes in our inventory levels and carrying costs;
- seasonal variations in demand for refined products;
- changes in fuel and utility costs for our facilities; changes in insurance markets impacting costs and the level and types of coverage available;
- the availability and costs of crude oil, other refinery feedstocks and refined products;
- changes in the cost or availability of third-party vessels, pipelines and other means of transporting crude oil, feedstocks and refined products;
- weather conditions affecting our operations or the areas in which our refined products are marketed; and
- earthquakes or other natural disasters affecting operations.

Many of these factors are described in greater detail in our filings with the SEC. All future written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the previous statements. We undertake no obligation to update any information contained herein or to publicly release the results of any revisions to any forward-looking statements that may be made to reflect events or circumstances that occur, or that we become aware of, after the date of this Quarterly Report on Form 10-Q.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our primary source of market risk is the difference between prices received from the sale of refined products and the prices paid for crude oil and other feedstocks. We have a risk management committee whose responsibilities include reviewing a quarterly assessment of risks to the corporation and presenting a quarterly risk report to executive management for consideration.

Commodity Price Risks

Our earnings and cash flows from operations depend on the margin at which we are able to sell refined products relative to our fixed and variable expenses (including the costs of crude oil and other feedstocks). The prices of crude oil and refined products have fluctuated substantially in recent years and depend on many factors. These factors include the global supply and demand for crude oil, diesel fuel and other refined products. This demand is impacted by changes in the global economy, the level of foreign and domestic production of crude oil and refined products, geo-political conditions, the availability of imports of crude oil and refined products, the relative strength of the U.S. dollar, the marketing of alternative and competing fuels and the impact of government regulations. The prices we sell our refined products for are also affected by local factors such as local market conditions and the level of operations of other suppliers in our markets.

Prices for refined products are influenced by the price of crude oil. Generally, an increase or decrease in the price of crude oil results in a corresponding increase or decrease in the price of gasoline and other refined products. The timing, direction and the overall change in refined product prices versus crude oil prices will impact profit margins and could have a significant impact on our earnings and cash flows. Assuming all other factors remained constant, a $1 per barrel change in average gross refining margins, based on our 2010 Period average throughput of 472 Mbpd, would change annualized pretax operating income by approximately $172 million.

We maintain inventories of crude oil and intermediate and finished refined products, the values of which are subject to fluctuations in market prices. Our inventories of refinery feedstocks and refined products totaled 26 million barrels and 20 million barrels at September 30, 2010, and December 31, 2009, respectively. The average cost of our refinery feedstocks and refined products at September 30, 2010, was approximately $36 per barrel on a LIFO basis, compared to market prices of approximately $86 per barrel. If market prices decline to a level below the cost of these inventories, we would be required to write down the value of our inventory to market.

We periodically use non-trading derivative instruments, primarily to manage exposure to commodity price risks associated with the purchase or sale of crude oil and finished refined products. We may also use derivative instruments to manage price risks associated with inventories above or below our target levels. These derivative instruments typically involve exchange-traded futures, over-the-counter (OTC) swaps and options and physical commodity forward purchase and sale contracts, generally with durations of less than one year.

We formed Tesoro Panama Company Sociedad Anonima (TPSA) to further utilize our pipeline and tank facilities in Panama to provide discretionary crude oil trading through a global infrastructure. We maintain inventories of crude oil on a FIFO basis which have exposure to commodity price risk. We periodically use derivative instruments, primarily to manage these exposures. These derivative instruments include, but are not limited to, options, exchange traded futures, OTC swaps and options, or physical commodity forwards. All TPSA transactions are conducted in accordance with Tesoro s risk policies and procedures.

We elected not to designate our derivative instruments as cash flow or fair value hedges during the first nine months of 2010 and 2009. Therefore, we mark-to-market our derivative instruments and recognize the changes in their fair value. Accordingly, no change in the value of the related underlying physical commodity is recorded.

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Net earnings during the 2010 and 2009 third quarters included derivative instrument losses of $3 million and $6 million, respectively. The losses (in millions) and volumes (in millions) were comprised of the following:

	September 30,			
	2010		2009	
	Contract Volumes	Net Gain (Loss)	Contract Volumes	Net Gain (Loss)
Unrealized gain carried on open derivative positions from prior quarter	3	$ 5	2	$ 13
Realized gain (loss) on settled derivative positions	103	1	69	(19)
Unrealized loss on open derivative positions	2	(9)	1	
Net loss		$ (3)		$ (6)

We have prepared a sensitivity analysis to quantify our exposure to market risk associated with our derivative instruments. This analysis is based on our open derivative positions of 2.2 million barrels at September 30, 2010, which expire at various times, primarily in 2010, and on the fair value of each derivative instrument at quoted market prices. If all other factors remain constant, a $1 per-barrel change in quoted market prices of our derivative instruments would change the fair value of our derivative instruments and pretax operating income by approximately $2.2 million.

Trading Activities

The above table includes 1.0 million barrels in open derivative positions at September 30, 2010, entered into to manage exposure to commodity price risks associated with our trading activities. Unrealized gains or losses are not material to the consolidated financial statements for the three months ended September 30, 2010.

Counterparty Credit Risk

We have exposure to concentrations of credit risk related to the ability of our counterparties to meet their contractual payment obligations, and the potential non-performance of counterparties to deliver contracted commodities or services at the contracted price. We have risk management policies in place, and continue to monitor closely the status of our counterparties. We perform ongoing credit evaluations of our customers credit worthiness, and in certain circumstances, require prepayments, letters of credit or other collateral arrangements.

Foreign Currency Risk

We are exposed to exchange rate fluctuations on our monthly purchases of Canadian crude oil. Beginning in August 2009, we have entered into forward contracts of Canadian dollars to manage any monthly exchange rate fluctuations. We had a $2.2 million gain related to these transactions for the three months ended September 30, 2010. As of September 30, 2010, we had a forward contract to purchase 53 million Canadian dollars that matured on October 25, 2010.

ITEM 4. CONTROLS AND PROCEDURES

We carried out an evaluation required by the Securities Exchange Act of 1934, as amended (the Exchange Act), under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15(b) under the Exchange Act as of the end of the period. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective. During the quarter ended September 30, 2010, there have been no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In the ordinary course of business, we become party to lawsuits, administrative proceedings and governmental investigations, including environmental, regulatory and other matters. Large, and sometimes unspecified, damages or penalties may be sought from us in some matters and some matters may require years to resolve. Although we cannot provide assurance, we believe that an adverse resolution of these matters described below will not have a material adverse effect on our financial position or results of operations.

In October 2010, the Washington State Department of Labor & Industries (L&I) issued citations to us and assessed a penalty of $2.4 million for alleged violations of state health and safety regulations related to the fire that occurred at our Washington refinery on April 2, 2010. On October 22, 2010, we filed an appeal of the citations. The U.S. Chemical Safety and Hazard Investigation Board (CSB) and the U.S. Environmental Protection Agency (EPA) are also conducting investigations concerning the fire. As a result of the fire, seven employees were fatally injured. We cannot predict with certainty the ultimate resolution the appeal of the L&I citations and are unable to predict the CSB s findings or estimate what actions the EPA may require or what penalties they might assess.

During 2009, Chevron filed a lawsuit against us claiming they are entitled to a share of the refunds we received in 2008 from the owners of the Trans Alaska Pipeline System (TAPS). We received $50 million in 2008, net of contingent legal fees, for excessive intrastate rates charged by TAPS during 1997 through 2000, and the period of 2001 through June 2003. Chevron is asserting that it is entitled to a share of its portion of the refunds for retroactive price adjustments under our previous crude oil contracts with them. In September 2010, the trial court judge granted Chevron s motion for summary judgment and awarded them $16 million. We disagree with the trial court and intend to appeal the decision to the Alaska Supreme Court. We believe that the outcome of this matter will not materially impact our liquidity and consolidated financial position, although the resolution of this matter could have a material impact on interim or annual results of operations.

We are a defendant, along with other manufacturing, supply and marketing defendants, in six lawsuits alleging MTBE contamination in groundwater. We were served with the sixth lawsuit on April 22, 2010. The defendants are being sued for having manufactured MTBE and having manufactured, supplied and distributed gasoline containing MTBE. The plaintiffs in the six cases, all in California, are municipalities and governmental authorities. The plaintiffs allege, in part, that the defendants are liable for manufacturing or distributing a defective product. The suits generally seek individual, unquantified compensatory and punitive damages and attorney s fees. We intend to vigorously assert our defenses against these claims.

On February 5, 2010, the EPA filed suit against us alleging violations of the Clean Air Act and corresponding regulatory requirements concerning the testing and reporting of transportation fuels and fuel additives. In February 2009, we received a Notice of Violation (NOV) from the EPA for alleged violations arising from a compliance review conducted by the EPA in 2006 for the years 2003 through the time of the review in 2006. We are discussing the alleged violations contained in the suit with the EPA and the U.S. Department of Justice and have not established an accrual for this matter. On the basis of existing information, we believe that the resolution of this matter will not have a material adverse effect on our financial position or results of operations.

In June 2010, we settled an enforcement action brought by the Alaska Department of Environmental Conservation (ADEC) related to the grounding of a vessel in the Alaska Cook Inlet on February 2, 2006. We settled this matter for a total of $265,000. The ADEC had alleged that two vessels chartered by us violated provisions of our Cook Inlet Vessel Oil Prevention and Contingency Plan from December 2004 to February 2006.

In June 2010, we accepted a settlement offer from the Bay Area Air Quality Management District (the District) to settle 44 NOVs. The NOVs were issued from May 2006 to April 2008 and allege violations of air quality regulations at our Golden Eagle refinery.

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On July 1, 2010, we received an offer from the District to settle 46 NOVs for $620,000. The NOVs were issued from June 2006 to September 2009 and allege violations of air quality regulations at our Golden Eagle refinery. We are evaluating the allegations contained in the settlement offer and will seek to negotiate a settlement of the NOVs with the District. The resolution of this matter will not have a material adverse effect on our financial position or results of operations.

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ITEM 1A. RISK FACTORS

There have been no significant changes from the risk factors previously disclosed in Item 1A of our 2009 Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Purchases of unregistered equity securities during the three-months ended September 30, 2010

The table below provides a summary of all repurchases by Tesoro of its common stock during the three-month period ended September 30, 2010.

Period	Total Number of Shares Purchased	Average Price Paid per Share
July 2010		$
August 2010	256*	$ 11.60
September 2010		$ ¾
Total	256	

* All of these shares acquired were surrendered to Tesoro to satisfy tax withholding obligations in connection with the vesting of restricted stock issued to certain employees. These shares were not acquired under a stock repurchase program.

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ITEM 6. EXHIBITS

(a) Exhibits

10.1 Amendment to the Fourth Amended and Restated Credit Agreement, dated as of February 23, 2010, among the Company, JP Morgan Chase Bank, NA as administrative agent and a syndicate of banks, financial institutions and other entities (incorporated by reference herein to Exhibit 10.4 to the Company s Annual Report on Form 10-K for the year ended December 31, 2009, File No. 1-3473).

10.2 Separation and Waiver of Liability Agreement between Tesoro Corporation and William J. Finnerty dated March 18, 2010 (incorporated by reference herein to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on March 23, 2010, File No. 1-3473).

10.3 Amended and Restated Employment Agreement between Tesoro Corporation and Everett D. Lewis dated March 18, 2010 (incorporated by reference herein to Exhibit 10.2 to the Company s Current Report on Form 8-K filed on March 23, 2010, File No. 1-3473).

10.4 Employment Agreement between Tesoro and Gregory J. Goff dated as of March 30, 2010 (incorporated by reference herein to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on April 5, 2010, File No. 1-3473).

10.5 Retention Employment Agreement between Tesoro and Everett D. Lewis dated as of June 9, 2010 (incorporated by reference herein to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on June 10, 2010, File No. 1-3473).

10.6 Uncommitted Revolving Credit Agreement dated as of October 18, 2010, among Tesoro Panama Company, S.A. as Borrower, certain lenders listed on the signature pages, as Lenders, and BNP Paribas, as Administrative Agent, Collateral Agent, Letter of Credit Issuer, Swing Line Lender and Daylight Overdraft Bank (incorporated by reference herein to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on October 22, 2010, File No. 1-3473).

31.1 Certification by Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification by Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification by Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification by Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

*101 The following materials from Tesoro Corporation s Form 10-Q for the quarter ended September 30, 2010, formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Cash Flows, and (iv) Notes to Condensed Consolidated Financial Statements, tagged as blocks of text.

* Submitted electronically herewith.

In accordance with Rule 402 of Regulation S-T, the XBRL information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed to be filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (Exchange Act), or otherwise subject to the liability of that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

TESORO CORPORATION

Date: November 5, 2010	/s/ GREGORY J. GOFF Gregory J. Goff President and Chief Executive Officer (Principal Executive Officer)
Date: November 5, 2010	/s/ G. SCOTT SPENDLOVE G. Scott Spendlove Senior Vice President, Chief Financial Officer and Treasurer (Principal Financial Officer)

EXHIBIT INDEX

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