

EXHIBIT 2  
PRELIMINARY TRACT SELECTION

CALENDAR PAGE 01.115  
MINUTE PAGE 3505

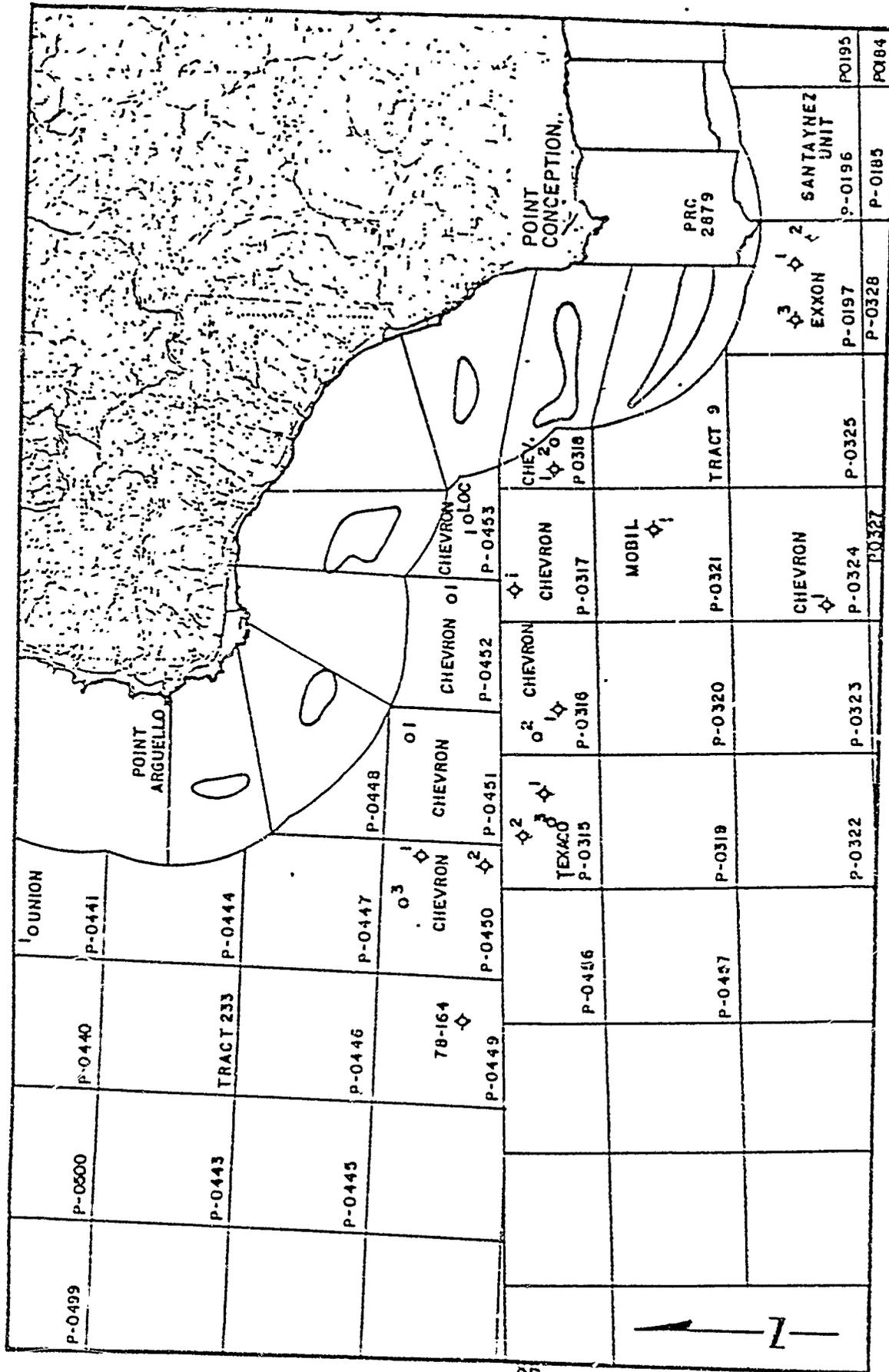


EXHIBIT 3  
RECOMMENDED TRACT SELECTION

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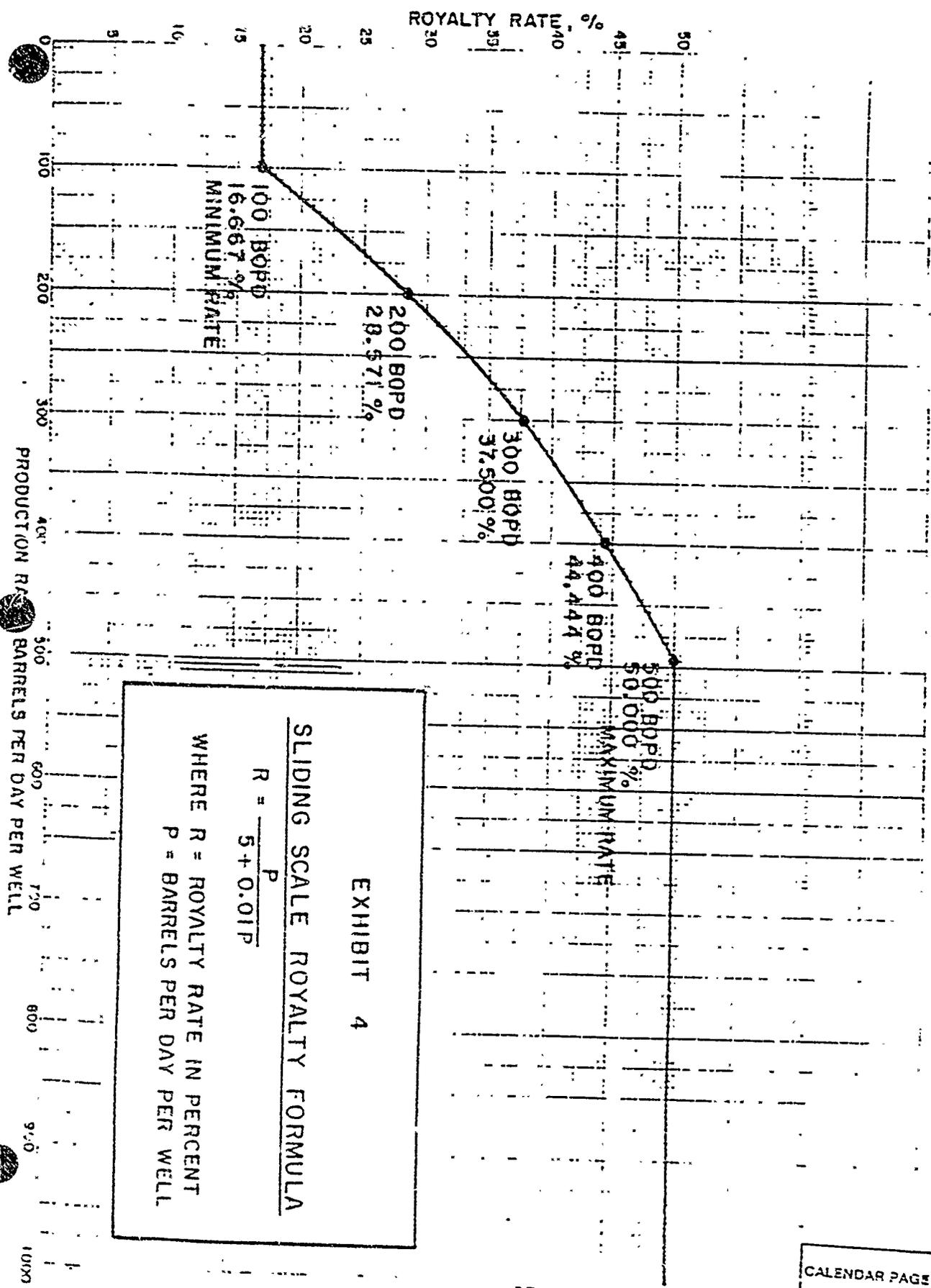


EXHIBIT 4

SLIDING SCALE ROYALTY FORMULA

$$R = \frac{P}{5 + 0.01P}$$

WHERE R = ROYALTY RATE IN PERCENT  
 P = BARRELS PER DAY PER WELL

EXHIBIT 5

DRAFT

POINT CONCEPTION  
SLIDING-SCALE ROYALTY  
DRAFT  
11-19-82

STATE LANDS COMMISSION

State of California

Oil and Gas Lease

(Sliding-Scale Royalty)

This Oil and Gas Lease is entered into this \_\_\_\_\_  
day of \_\_\_\_\_, 19\_\_\_\_, pursuant to Division 6 of the  
Public Resources Code, and is between the State of  
California, acting through the State Lands Commission, which  
will be referred to as the State, and \_\_\_\_\_,  
which will be referred to as the Lessee.

In consideration of the bonus, rental and royalty  
to be paid and the covenants, conditions, agreements and  
stipulations contained in this lease, the State leases to  
the Lessee certain lands, which will be referred to as the  
leased lands, situate in Santa Barbara County, California,  
identified on the attached map that is marked Exhibit "A"  
and described as follows:

\* \* \* \* \*

1.

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1. TERM AND PURPOSE OF LEASE

This lease shall be for a primary term of twenty (20) years, and for so long thereafter as oil or gas is produced in paying quantities from the leased lands, or so long as Lessee is diligently conducting producing, drilling, deepening, repairing, redrilling or other necessary lease or well maintenance operations on the leased lands. The Lessee shall have the exclusive right to prospect for, drill for, produce and take only oil, gas and other hydrocarbon substances from the leased lands. This right includes the right to conduct geological and geophysical surveys on the leased lands for the purpose of determining subsurface conditions. However, the State may permit others to conduct geological or geophysical surveys on the leased lands as provided in sections 6212.2 and 6826 of the Public Resources Code and the applicable regulations of the State. This lease does not give the Lessee the privilege or right to store gas within the geological zones underlying the leased lands nor any other privilege or right not expressly stated. Within the drilling term of three (3) years from the date of this lease, or a later date determined pursuant to paragraph 24(b), the Lessee shall commence operations for the drilling of a well for oil or gas. If the Lessee fails to commence such operations before or to prosecute them diligently after the expiration of the three (3) year term, or any extension thereof, this lease

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shall terminate. Whenever the leased lands cease to produce oil or gas, the lease will continue in force if within six months after production ceases, or such longer period as the State may authorize, the Lessee commences and prosecutes with reasonable diligence, drilling, deepening, repairing, redrilling or other operations for restoring production of oil or gas from the leased lands.

2. EXPLORATION AND DEVELOPMENT OBLIGATIONS  
AND DRILLING REQUIREMENTS

Within one hundred twenty (120) days after the effective date of this lease, the Lessee shall submit to the State for approval an exploration plan for the leased lands, which plan shall provide at least for the drilling of one (1) well. After the completion of the site-specific environmental review, the Lessee shall commence within the three (3) year drilling term and diligently prosecute exploratory operations in accordance with the approved exploration plan, which shall include whatever measures are necessary to mitigate adverse environmental effects. No later than one (1) year after a commercial discovery, the Lessee shall submit to the State for approval a development plan for the discovered pool or pools. Upon completion of the environmental review, the Lessee shall commence and diligently prosecute development operations in accordance with the approved development plan, which shall include whatever measures are necessary to mitigate adverse

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environmental effects. Development plans for later discovered pools capable of commercial production shall be submitted to the State for approval within one (1) year of discovery. The Lessee shall diligently pursue the acquisition of all permits necessary for the conduct of drilling and production operations on the leased lands and for the construction of structures and facilities on and off the leased lands required for the conduct of drilling and production operations. All drilling operations shall be conducted in accordance with the requirements in Exhibit "B".

### 3. RENTAL

The Lessee shall pay to the State, annually in advance, rental of \$ \_\_\_\_\_ per acre per year. If any portion of the leased lands is quitclaimed as to all zones, the annual rental shall be reduced \$ \_\_\_\_\_ for each acre quitclaimed. This reduction shall become effective on the lease anniversary date next following the date of quitclaim.

### 4. ROYALTY

(a) In addition to the rental provided in paragraph 3, the Lessee shall account for and pay to the State in money as royalty on oil, a percentage, determined in accordance with Exhibit "D" which is attached and made a part of this lease, of the current market price of all oil production removed or sold from the leased lands. The current market price shall be determined by the State and

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shall include any premium or bonus paid for the oil. The current market price shall never be less than the highest price in the nearest field at which oil of like gravity and quality is being sold in substantial quantities. Money royalty on oil shall be due not later than the twenty-fifth day of the calendar month following the calendar month in which the oil is produced.

(b) At the State's option, exercised upon sixty (60) days' written notice, and in lieu of money royalty on oil production, the Lessee shall deliver to the State in kind a percentage, determined in accordance with Exhibit "D", of all oil production removed or sold from the leased lands. If the State elects to take in kind its royalty share of oil produced from the leased lands, the State may require the Lessee to provide at the Lessee's shipping tanks, without charge to the State, tankage of sufficient capacity to store the State's royalty share of oil produced from the leased lands during any continuous forty-eight (48) hours.

(c) In addition to the rental provided in paragraph 3, the Lessee shall account for and pay to the State in money as royalty on non-oil production, which consists of dry gas, including vented and flared gas (except during testing with approval of the State), natural gasoline, and other products extracted and saved from the gas produced from the leased lands, except gas used for lease

operations or reinjected into the leased lands, twenty percent (20%) of the current market price of all such production removed or sold from the leased lands. The current market price shall be determined by the State and shall include any premium or bonus paid for the non-oil production. The current market price never shall be less than the higher of the highest price in the nearest field at which non-oil production of like quality is being sold in substantial quantities or the net proceeds or exchange value derived by the Lessee from the non-oil production removed or sold from the leased lands. Money royalty on non-oil production shall be due not later than the twenty-fifth day of the calendar month following the calendar month in which the non-oil production is produced.

(d) At the State's option, exercised upon sixty (60) days' written notice and in lieu of money royalty on non-oil production, the Lessee shall deliver to the State in kind, twenty percent (20%) of all non-oil production removed or sold from the leased lands.

(e) If the State elects to take in kind its royalty share or shares of oil or non-oil production, or both, it may elect thereafter, upon sixty (60) days' written notice, to take its royalty share or shares in money, and upon like notice at any time thereafter, may elect to take its royalty share or shares either in kind or in money.

5. TRANSFER OF LEASE

(a) Subject to approval by the State, this lease may be assigned, transferred or sublet to any person, association of persons or corporation who at the time of the proposed assignment, transfer or sublease possesses the qualifications provided in section 6801 of the Public Resources Code. Any assignment, transfer or sublease may involve all or any part of the leased lands or any separate or distinct zone or geological horizon or portion of such zone or horizon. Any assignment, transfer or sublease shall take effect on the first day of the month following its approval by the State and the filing with the State of an executed counterpart thereof, together with any required bond and proof of the qualifications of the assignee, transferee or sublessee to hold this lease or any interest in it. Unless approved by the State, no assignment, transfer or sublease shall be of any effect. Upon approval of any assignment, transfer or sublease, the assignee, transferee or sublessee shall be bound by the terms of this lease to the same extent as if such assignee, transferee or sublessee were the original lessee, any conditions in the assignment, transfer or sublease to the contrary notwithstanding.

(b) Any assignment or transfer of a separate portion of this lease or of a separate or distinct zone or geological horizon, or portion thereof, shall segregate the

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assigned or transferred portion from the retained portion. The approval of the assignment or transfer shall release the assignor or transferor from all obligations thereafter accruing under this lease with respect to the assigned or transferred lands or zones or horizons. The lease on any segregated portion of the lands or zones or horizons shall continue in force for the primary term of this lease, but for not less than two (2) years after the date of discovery of oil or gas in paying quantities upon any of the lands or zones or horizons originally subject to this lease, and so long thereafter as oil or gas is produced in paying quantities from such segregated portion.

(c) With the approval of the State, assignments or transfers may be made of parts of this lease which are on their extended term because of production. The lease on any segregated portion containing only undeveloped lands or zones or horizons shall continue in force for two (2) years and so long thereafter as oil or gas is produced in paying quantities from such segregated portion.

#### 6. QUITCLAIM

The Lessee at any time may make a written quitclaim of all rights under this lease or of any portion of the leased lands comprising a ten-acre parcel or multiple thereof in a compact form, or of any separate or distinct zone or geological horizon or portion thereof underlying a ten-acre parcel or multiple thereof. The quitclaim shall be

effective when it is filed with the State, provided that the Lessee and its surety shall be subject to the continued obligation to pay all accrued rentals and royalties and to abandon all wells drilled into the lands or in the zones or horizons to be quitclaimed in accordance with the terms of this lease and the regulations of the State. At the option of the State, the Lessee may be required to place all such wells in condition for suspension instead of abandoning them. The Lessee shall then be released from all obligations thereafter accruing under the lease with respect to the lands, zones or horizons quitclaimed. The quitclaim shall not release the Lessee or its surety from any liability for breach of any obligation of this lease with respect to which the Lessee is in default at the time of the filing of the quitclaim.

#### 7. CANCELLATION

If the Lessee fails to exercise due diligence and care in the prosecution of the exploratory or development work in accordance with the terms and conditions of this lease prior to the discovery of oil or gas in paying quantities and if such default continues after thirty (30) days' written notice to the Lessee, the State may cancel this lease. After discovery of oil or gas in paying quantities, this lease may be canceled upon failure of the Lessee, after ninety (90) days' written notice, to comply with the provisions of this lease or applicable statutes or

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regulations. In the event of cancellation, the Lessee shall have the right to retain any drilling or producing wells as to which no default exists, together with such rights of way into or through the leased lands as may be reasonably necessary to enable the Lessee to drill and operate the retained well or wells. In the event of any termination of this lease in whole or in part, the Lessee shall have a reasonable time to remove any property, equipment and facilities used by the Lessee in operations under the terminated portion of this lease.

#### 8. RESERVATIONS TO STATE

The State reserves the right to grant, upon its own terms, joint or several easements or rights of way upon, through or in the leased lands as may be necessary or appropriate, and the right to allow, upon its own terms, the continued use of any existing easement or right of way upon, through or in the leased lands. The State also reserves the right to lease, sell or otherwise dispose of whatever transferable interest it may have in the surface of the leased lands, subject to the reasonable use by the Lessee of the surface for operations under this lease.

#### 9. PREVENTION OF WASTE

The Lessee shall use all reasonable precautions to prevent waste of oil and gas in the leased lands and to prevent the entrance of water through wells drilled to the oil or gas-bearing strata that may destroy or injure the oil or gas deposits.

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10. COMPLIANCE WITH LAWS AND OTHER  
OPERATIONAL CONTROLS

The Lessee shall comply with all valid laws and ordinances of the United States and of the State of California and its political subdivisions applicable to the Lessee's operations, including, but not limited to, the applicable provisions of Divisions 3 and 6 of the Public Resources Code and the regulations of the Division of Oil and Gas and State Lands Commission. The Lessee shall also comply with the special operating requirements set forth in Exhibit "C".

11. FORCE MAJEURE

The obligations imposed upon the Lessee by this lease may be suspended whenever the Lessee is prevented from complying with them by wars, strikes, riots, acute and unusual labor or material shortages, acts of God, laws, rules and regulations of any federal, state, county or municipal agency or by other unusual conditions that are beyond the control of the Lessee. In order for any obligation imposed upon the Lessee to be suspended, the Lessee must notify the State in writing as soon as possible that a condition warranting suspension has arisen. The notification shall state the nature of the condition, an estimate of the condition's duration and the steps to be taken by the Lessee to eliminate the condition. The Lessee shall use its best efforts to eliminate the condition and

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notify the State in writing as soon as the condition no longer exists.

12. OPERATIONAL STANDARDS

The Lessee shall exercise reasonable diligence in the operation of the wells while their products can be obtained in paying quantities and shall not unreasonably or unnecessarily suspend operations. All operations shall be conducted in a proper and workerlike manner, in accordance with generally accepted good oil field practice and with regard for the protection of the safety and health of workers.

13. LIABILITY AND INDEMNIFICATION

The Lessee shall be liable to the State for all damage to any reservoir underlying the leased lands and any loss of oil, gas or other hydrocarbon substances to the extent that they are caused by the negligence of, or the breach of any provision of this lease by, or noncompliance with any applicable statutes or regulations by the Lessee, its employees, servants, agents or contractors. Nothing in this lease shall diminish any other rights or remedies which the State may have in connection with any such negligence or breach. The Lessee shall indemnify the State of California, its officers, agents and employees against all claims, demands, causes of action or liabilities of any kind which may be asserted against or imposed upon the State of California, its officers, agents or employees, by any third

person or entity arising out of or connected with the issuance of this lease, operations hereunder, or the use by Lessee, its agents, employees or contractors of the leased lands.

14. BONDS

The Lessee shall furnish upon execution of this lease and maintain a bond in favor of the State of California in the sum of \$\_\_\_\_\_ to guarantee the faithful performance by the Lessee of all provisions of this lease, Division 6 of the Public Resources Code and the regulations promulgated thereunder, including, but not limited to, immediate elimination of any contamination or pollution caused by or resulting from operations under this lease. If the Lessee places platforms or other fixed or floating structures on the leased lands, the Lessee shall file at the commencement of such placement and maintain an additional bond in favor of the State of California in a reasonable amount as specified by the State, but not exceeding fifty percent (50%) of the replacement cost of the structures, to guarantee the faithful performance by the Lessee of the placement of the structures, their maintenance and their removal at the State's request upon the expiration or sooner termination of this lease. All bonds shall require the surety to give at least ninety (90) days' written notice of its intention to cease acting as guarantor. If a surety gives notice of its intention to

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cease acting as guarantor, the Lessee shall provide to the State within sixty (60) days of such notice a replacement bond of equal value to become effective upon the expiration of the existing bond. Failure to provide such a replacement bond within the required time shall constitute a default entitling the State to levy against the entire amount of the existing bond.

15. SURRENDER OF PREMISES

At the expiration of this lease or upon its sooner termination, the Lessee shall surrender the leased lands and all improvements on them in good condition, or the State may provide that the Lessee shall remove some or all of the structures and other fixtures placed upon the leased lands and restore the lands, in whole or in part, to their natural condition at no cost to the State. The Lessee shall not be denied the right to remove any drilling, development and production equipment having a reuse or salvage value.

16. DAMAGES TO THIRD PERSONS AND PROPERTY

(a) The Lessee shall furnish upon execution of this lease a certificate showing that at all times throughout the life of this lease, the Lessee is insured against damages to third persons and their property resulting from an oil spill or other pollution caused by operations under this lease. The insurance shall be for an amount not less than ten million dollars (\$10,000,000) for each occurrence. The minimum amount may be raised by the

State if economic conditions change. The certificate of insurance shall indicate that the Lessee has obtained from a responsible insurance company doing business in California the required insurance coverage which shall include the State of California as a named insured, or shall demonstrate to the satisfaction of the State that the Lessee is capable of self-insuring the risk. The certificate of insurance shall remain in effect at all times throughout the life of the lease. A new certificate of insurance meeting the above requirements may be substituted by the Lessee with the State's approval.

(b) Should an oil spill or other polluting event occur which the State determines will result in the filing of a substantial number of claims against the Lessee, the Lessee shall open or cause to be opened within ten (10) days of such event a claims office in the City of Santa Barbara staffed with personnel sufficient to process all claims and having authority to settle all uncontested claims. Barring unusual circumstances, all claims shall be processed and all uncontested claims shall be settled within sixty (60) days of their filing. To facilitate settlement of contested claims, the Lessee shall agree to arbitration of claims of five thousand dollars (\$5,000) or less and mediation of claims in excess of five thousand dollars (\$5,000). The arbitration and mediation shall be conducted pursuant to agreements prepared by the State at or before

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the time of the invitation for bids.

17. SALES CONTRACTS AND EXCHANGE AGREEMENTS

The Lessee shall file with the State copies, certified by the Lessee to be true, of all contracts and other agreements for the sale, exchange or other disposition of oil, gas, natural gasoline and other substances produced from the leased lands. If the State elects to take its royalty share of production in money instead of in kind, the Lessee shall not sell or otherwise dispose of the royalty share of the production except in accordance with sales contracts or other methods first approved in writing by the State.

18. ROYALTY STATEMENTS

The Lessee shall furnish monthly true royalty statements in whatever form the State prescribes. The statements shall show for the preceding calendar month the amount, gravity and market price of all oil produced, saved and sold, the amount and gross value of gas produced, vented and flared (except during testing), saved, used and sold and the amount and gross value of natural gasoline or other products produced from the leased lands. The statement also shall show the number of days each well is on production.

19. EXAMINATION OF RECORDS AND INSPECTION OF PREMISES

Insofar as it has the right to do so, the Lessee consents to an examination by any person authorized by the

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State of the books and records of any individual, association or corporation which has transported for or received from the Lessee any oil, gas, natural gasoline or other products produced from the leased lands. The Lessee also consents to the inspection at all times by any person authorized by the State of its operations on the leased lands, including wells, improvements, machinery and fixtures used in connection with those operations.

20. SUBMISSION AND USE OF DATA

The Lessee shall file promptly with the State true copies of all geophysical data covering the leased lands and all logs (including electric logs), surveys, drilling records, well histories, core records, formation tests and related information as measured and recorded in the course of drilling, for the wells drilled into the leased lands. All data and information filed by the Lessee with the Division of Oil and Gas in connection with this lease, whether or not held in confidential status by the Division of Oil and Gas, shall be submitted to the State for its use in enforcing compliance with the terms of this lease and regulations of the State. All data and information supplied in confidence of the Lessee under this paragraph shall be kept confidential by the State and shall not be disclosed to any person or agency without the written consent of the Lessee or unless their disclosure is required by law. Notwithstanding the above, the State may

disclose any data or information filed by the Lessee to any governmental agency needing the data or information to regulate the leased lands or adjacent lands, provided that the disclosure is made pursuant to an agreement with the governmental agency specifying the purposes for which the data and information may be used and requiring the data and information to be kept confidential.

21. FACILITIES AND MEASUREMENT  
OF PRODUCTION

The Lessee shall furnish to the State for its approval detailed plats, drawings and other pertinent data concerning the oil and gas facilities and pipelines to be used for the production, processing, measurement and transportation of the oil, gas and other hydrocarbon substances from the leased lands. Any changes, including emergency changes, in the facilities and pipelines shall be approved by the State. The Lessee shall install whatever sampling and measuring equipment the State deems necessary for the sampling and measuring of the oil, gas and other hydrocarbon substances. The Lessee shall measure and account for all oil, gas and other hydrocarbon substances produced from, used on or transported from the leased lands in accordance with the terms of this lease and the regulations of the State. The State shall have the right at all times to witness the measurement and sampling of all oil, gas and other hydrocarbon substances. The State may

elect to measure and sample the oil, gas and other hydrocarbon substances in the presence of a representative of the Lessee. The Lessee shall furnish samples of oil, gas and other hydrocarbon substances that are required by the State for laboratory tests. The Lessee shall be given the opportunity to witness the tests conducted by the State, and the readings and results of those tests shall be binding on the Lessee.

22. STATE'S RIGHTS TO DETERMINE WELL SPACING AND RATES OF DRILLING AND PRODUCTION

The State shall have the right to determine the spacing of wells and the rate of drilling and rate of production of wells to prevent the waste of oil and gas and promote the maximum economic recovery of oil or gas from, and the conservation of reservoir energy in, each zone or separate underground source of supply of oil or gas covered in whole or in part by this lease.

23. UNITIZATION

If the State determines that the ultimate recovery of oil or gas will be increased, oil or gas will be protected from unreasonable waste, land subsidence may be arrested or ameliorated, or adjacent landowners will be protected, the Lessee shall unite with other lessees of the State or with others owning or operating lands not belonging to the State, including lands belonging to the United States, in operating under a cooperative or unit plan of

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development or operation for the pool or field or any part thereof. The State, with the consent of the Lessee, may establish, change or revoke any drilling and production requirements of this lease, may permit apportionment of production, and may make such regulations concerning the institution and operation of any cooperative or unit plan that the State deems necessary or proper for the protection of its interests.

24. OFFSHORE STRUCTURES

(a) Subject to the provisions of Exhibit "B", each well may be drilled or slant-drilled to and into the subsurface of the leased lands from platforms or other fixed or floating structures in, on or over the tide and submerged lands covered by the lease or otherwise available to the Lessee.

(b) If the Lessee proposes to drill one or more wells from platforms or other fixed or floating structures and if permission from any federal or state agency is legally required for construction of such structures, the Lessee shall be allowed a reasonable time following the execution of the lease to secure the necessary permission from such federal or state agencies and, upon securing such permission, a further reasonable time, determined with regard to the nature of the structure or structures to be constructed, to commence drilling operations on such well or wells. The State shall extend

the drilling term of the lease by a period equal to the reasonable time necessary to secure the permission and, if necessary, to the date to which the time to commence drilling operations on such well or wells has been extended.

(c) Any platforms or other fixed or floating structures shall conform to the regulations of the State in effect at the time of the invitation for bids.

25. POLLUTION AND CONTAMINATION OF WATERS PROHIBITED

Pollution and contamination of state waters, impairment of and interference with bathing, fishing or navigation in state waters, and impairment of and interference with developed shoreline recreational or residential areas are prohibited. No oil, tar, residuary product of oil or any refuse of any kind from any well or works shall be deposited on or allowed to pass into state waters. The permission given in section 6873(b) of the Public Resources Code to the deposition in state waters of water not containing any hydrocarbons or vegetable or animal matter and drill cuttings and drilling mud which are free of oil and materials that are deleterious to marine life, shall not supersede any restrictions on the deposition of such substances which are contained in this lease, which includes the exhibits.

\* \* \* \* \*

21.

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26. SOLVENCY

If the Lessee at any time makes a general assignment for the benefit of its creditors, or a receiver is appointed over or an attachment is levied and permitted to remain for any unreasonable length of time upon or against the interest of the Lessee in any oil, gas, natural gasoline or other products produced from the wells drilled into the leased lands, the State may terminate this lease by giving written notice to the Lessee.

27. USE OF PRODUCTION FOR LEASE OPERATIONS

With the approval of the State, the Lessee may use oil produced from the Lessee's wells drilled into the leased lands for lease operations only. Oil so used shall be reported to the State monthly. Such oil shall not be included in computing for royalty purposes the total production or oil removed or sold from the leased lands during the month, nor in computing for royalty purposes the current market price of such production, but shall be used in computing the average production of oil per well per day for the purpose of determining the royalty rate as provided in Exhibit "D". With the approval of the State, the Lessee may also use gas produced from the Lessee's wells drilled into the leased lands, or gas received currently in exchange for gas so produced, for the following purposes only: fuel, gas lift, injection into oil sands from which the well or wells may be producing and reinjection into the leased

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lands. Gas so used, or gas given in exchange for gas so used, shall be reported to the State monthly, but shall not be included in computing for royalty purposes the total production removed or sold from the leased lands during the month, nor in computing for royalty purposes the current market price of such production. The State may take, free of cost to it and at no expense to the Lessee, all produced surplus gas which cannot be marketed or beneficially utilized by the Lessee. The surplus gas taken by the State shall be for the use of the State of California. The existence of this option shall not relieve Lessee of the obligation to pay royalty on gas vented or flared at times other than during testing.

28. LESSEE'S DISPOSITION OF STATE'S ROYALTY

The Lessee shall be empowered to convey good title to the State's royalty share of oil, gas, natural gasoline and other products produced and saved, if and when such rules have been approved in writing by the State. The proceeds from the royalty share of oil, gas, gasoline or any other products produced from the leased lands shall be held by the Lessee in trust for the State until the Lessee makes the full royalty payment to the State.

29. NOTICES

All notices to be given under this lease shall be deemed to have been fully given when made in writing and deposited in the United States mail, registered and postage

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prepaid, and addressed as follows:

To the State:

To the Lessee:

The addresses to which the notices shall be mailed may be changed by written notice given by one party to the other as provided above. Nothing contained in this paragraph shall preclude the giving of any notice by personal service to the Lessee or its officer or agent. All payments specified in this lease shall be made to the State at the address provided for notices to the State.

30. TAXES

The Lessee shall pay timely all taxes or assessments levied under the laws of any state, county, city or the United States of America against Lessee's interest in the leased lands, against improvements placed on the leased lands by the Lessee and against all oil, gas and other products produced from the leased lands. There shall be no deduction from the royalties payable to the State by reason of any charges levied against the Lessee pursuant to sections 3400 et seq. of the Public Resources Code and any successor statute. Notwithstanding the above, any state severance tax or windfall profit tax enacted by the

California Legislature after the notice of invitation for bids and applicable to the State's royalty share of production, shall be paid by the State to the extent only of its applicability to the State's royalty share.

31. FAILURE TO ENFORCE

The failure of the State to enforce any provision of this lease, which includes the exhibits, shall not constitute a waiver by the State of that or any other provision.

STATE LANDS COMMISSION OF THE  
STATE OF CALIFORNIA

By:

\_\_\_\_\_  
Executive Officer

LESSEE:

ATTEST

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

EXHIBIT "A"  
MAP

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EXHIBIT "B"

DRILLING REQUIREMENTS

1. All operations shall be conducted in accordance with generally accepted good oil field practices.

2. An oil or gas zone is defined as any sequence of strata containing oil, gas or other hydrocarbon substances, where the reservoir characteristics, such as pressure, temperature, specific gravity, viscosity, permeability, and porosity, are similar and whenever such sequence of strata is separated from dissimilar producing strata by a competent layer of shale or other impervious rock.

3. Within one hundred twenty (120) days after the date of the cessation of drilling operations in the first well, the Lessee shall commence operations for the drilling of the next well. Operations for the drilling of each succeeding well shall commence within one hundred twenty (120) days after the cessation of drilling operations in the preceding well. The term "drilling operations" as used in this paragraph 3 shall include any of the following: actual drilling in the ground, logging or surveying the well bore, coring, sidewall sampling or coring, drill stem or formation testing, carrying on fishing operations, running and cementing protection or production casing, running tubing, perforating casing, milling casing, reaming, setting whipstock for redrilling, operations to stop lost

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circulation, and actual plugging and abandonment of the well. The term "cessation of drilling operations" as used in this paragraph 3 shall not include a temporary stoppage of drilling operations of less than seventy-two (72) hours relating to the resumption of drilling operations in the same well or a similar stoppage of longer duration which has been approved by the State. Irrespective of the requirements of this paragraph 3, the Lessee may suspend and resume drilling operations at any time during the drilling term of three (3) years or any extension of it. After oil or gas is discovered in commercial quantities in any oil or gas zone in the leased lands, wells shall be drilled to each commercially productive oil or gas zone, if it is mechanically practicable to do so, as follows:

- a. At least one (1) well for the production of oil into each twenty (20) acres of the area contained in the leased lands where the bottom of the productive interval of the well as completed for production is at a vertical depth of less than 6,000 feet.
- b. At least one (1) well for the production of oil into each forty (40) acres of the area contained in the leased lands where the bottom of the productive interval of the well as completed for production is at a vertical depth in excess of 6,000 feet.

c. At least one (1) well for the production of gas or gas condensate from any zone which produces gas or gas condensate into each one hundred-sixty (160) acres, or major fraction thereof, of the area contained in the leased lands.

The drilling requirements set forth in subparagraphs a, b, and c of this paragraph 3 are required for and are applicable to each separate commercially productive oil or gas zone. With the approval of the State, a well may be completed in more than one zone and shall be considered a well for each zone into which it is completed and producing for the purpose of satisfying the drilling requirements of sub-paragraphs a, b, and c of this paragraph. The zones shall be segregated within the well bore and produced through separate tubing strings. The Lessee shall not be required to operate more than one (1) drilling string at any time, unless the operation of more than one (1) drilling string at any time is necessary in order to commence an offset well within the time required by paragraph 5 of this exhibit.

4. Any well drilled in accordance with the provisions of this lease shall be drilled only from a surface location and on a course and to an objective approved in writing by the State prior to the commencement of drilling. The Lessee shall submit a detailed well drilling program to the State for its review and approval

prior to commencement of drilling. Any significant changes in the approved drilling program, such as altering the casing program or redrilling, deepening or abandoning a well, shall require advance approval by the State.

5. if any well producing in commercial quantities only gas and/or gas condensate has been, is or shall be completed on other than State lands, with any part of its producing interval within fourteen hundred eighty-nine (1489) feet from the exterior boundary of this lease, or if any well producing in commercial quantities oil and gas has been, is or shall be completed on other than State lands, with any part of its producing interval within five hundred (500) feet from the exterior boundary of this lease, the State may notify the Lessee in writing to drill an offset well. Within the time specified in the notice, which shall be a reasonable time, taking into account the availability, type and location of facilities required, and which in no event shall be less than one hundred-twenty (120) days from the date of the notice, the Lessee shall commence operations for the drilling of an offset well on the leased lands to the same zone as that zone from which such well is producing, or is capable of producing, oil or gas. For the purpose of this paragraph, an offset well for the production of only gas and/or gas condensate shall mean a well, the midpoint of the producing interval of which is situated at a location in the leased lands not more than fourteen hundred

eighty-nine (1489) feet from the point on the boundary of the lease nearest to the producing interval of the well to be offset. For the purpose of this paragraph, an offset well for the production of oil and gas shall mean a well, the midpoint of the producing interval of which is situated at a location in the leased lands not more than five hundred (500) feet from the point on the boundary of the lease nearest to the producing interval of the well to be offset.

6. An electric log or logs shall be made of all formations penetrated to the drilled depth of each well or to such depth as is mechanically possible. At least one oriented core or dipmeter record shall be made during the drilling of the first well to each zone if it is mechanically practicable to do so, or during the drilling of the earliest subsequent well in which it is mechanically practicable to make such core or record. True copies of all electric logs, surveys, paleontological reports, dipmeter records, oriented core records, rock core records, and all other drilling, test and production data taken by Lessee or its agents shall immediately be available to the representatives of the State. State representatives also shall have ready access to all rock cores and samples which may be obtained during the drilling of each well.

7. Each well drilled landward of the ordinary high water mark shall be completed in such manner that all production equipment and facilities are recessed, covered or

otherwise screened from view to the satisfaction of the State.

8. The State reserves the right, upon receipt of any evidence of subsidence of the surface of either the leased or adjacent lands, to determine that any or all further operations under this lease would or might cause or aggravate subsidence in or cause damage to the leased lands or other properties. In the event of such determination, the State may notify the Lessee in writing to suspend, in the manner and to the extent specified in the notice, its operations under this lease within thirty (30) days of the notice, and the Lessee shall suspend its operations within the time, in the manner and to the extent specified.

Exercise of either or both of the foregoing rights by the State is subject to the following:

(a) The determination may be made by the State at any time during the term of this lease but only at a meeting of the State Lands Commission at least thirty (30) days after written notice to Lessee that the State has received evidence of subsidence and proposes to determine whether any or all further operations under this lease would or might cause or aggravate subsidence in or cause damage to the leased lands or other properties. At this meeting, Lessee may present facts and arguments relevant to such determination.

(b) At least thirty (30) days prior to the

meeting, the State, to the best of its ability and to the extent permitted by law, shall make available to the Lessee for study, any written or graphic information or opinions received by or prepared for the State relative to subsidence of the surface of the leased and adjacent lands.

(c) Operations under this lease that have been suspended pursuant to this paragraph 8 may be resumed by the Lessee only in the manner and to the extent provided and subject to conditions contained in a program designed to alleviate or prevent further subsidence that has been agreed to by the State and the Lessee.

(d) Notwithstanding any agreement by the State to any such program, the State, upon receipt of evidence of further subsidence occurring after the resumption of operations under such program, may notify the Lessee again to suspend operations in accordance with the provisions of this paragraph, and Lessee shall so suspend operations.

During any period of suspension pursuant to this paragraph 8, the drilling, offset and production obligations of Lessee shall likewise be suspended only to the extent that the performance of such drilling, offset and production obligations is rendered impracticable or unreasonable as a result of the notice to suspend issued by the State pursuant to this paragraph 8.

The rights reserved by the State under this paragraph 8 shall be exercisable to the extent that such exercise is permitted by law.

EXHIBIT "C"

SPECIAL OPERATING REQUIREMENTS

1. SUBSEA COMPLETIONS

In preparing a development plan, the Lessee shall give the same consideration to the use of subsea completions as it does to fixed platforms. When approving a development plan, the State may require the use of subsea completions in those cases where it determines that economics, technical feasibility, environmental impacts, compatibility with commercial fishing operations and the religious beliefs of Native Americans, considered together rather than separately, indicate that subsea completions would be preferable to fixed platforms. When subsea completions are used, the Lessee shall promptly prepare and continually update maps showing the exact location of every subsea installation and shall make such maps available to commercial fisherman and other members of the public.

2. PIPELINE FEASIBILITY

(a) Pipelines will be required by the State for the transportation of produced oil, gas and other hydrocarbons if pipeline rights-of-way can be obtained and the State, acting upon information supplied by affected parties and responsible governmental agencies, determines that the laying of pipelines is economically and technologically feasible and environmentally preferable to other methods of transportation. The State reserves the

right to require the placement of any pipeline in certain designated pipeline corridors.

(b) Following the completion of a pipeline, no hydrocarbons produced from the leased lands shall be transported by surface vessel from offshore production sites, except in cases of emergency as determined by the State.

(c) Where the criteria in subparagraph (a) above are not met and surface transportation must be employed, all vessels used for transporting produced hydrocarbons shall conform with all standards established for such vessels under the Port and Tanker Safety Act of 1978 (33 U.S.C. sections 1221 et seq.).

(d) The State shall not approve any development or production plan which proposes the use of tankers or barges to transport produced hydrocarbons unless the Lessee, in cooperation with the State, has performed a study which demonstrates to the satisfaction of the State that a pipeline cannot meet the criteria in subparagraph (a) above.

(e) If the State determines that a pipeline cannot meet the criteria in subparagraph (a) above, the Lessee shall use the safest available transport vessels. The use of oil barges will be permitted only if the Lessee demonstrates to the satisfaction of the State that barging is environmentally preferable to tankering.

### 3. POTENTIAL GEOHAZARDS

Drilling operations shall not be conducted and seafloor wellheads and fixed structures for the production, transportation or storage of oil, gas or other hydrocarbons shall not be placed within geologically unstable portions of the leased lands such as potentially unstable sediments, areas of mass movement, submarine canyons or channels, shallow gas zones and areas near active faulting or surface ruptures unless the Lessee has demonstrated to the satisfaction of the State that such operations can be conducted and such wellheads and such structures can be designed and placed so as to withstand the maximum probable effects of the identified geohazards. Site-specific surveys shall be conducted prior to exploration and development operations to determine the potential for unstable bottom conductions and other geologic hazards. Extension of these surveys outside the leased lands may be required where necessary to evaluate the magnitude and significance of the hazard. All potentially unstable areas, including fault zones, must be mapped before any seafloor wellheads or fixed structures are installed. The State may require site-specific soil testing before exploration and development operations are allowed.

### 4. MANDATORY BIOLOGICAL AND MARINE MAMMAL SURVEYS

(a) Prior to the commencement of any drilling operations and prior to the commencement of construction or

placement of any structure, including pipelines, on the leased lands, the Lessee shall conduct site-specific biological and marine mammal surveys as specified by the State after consulting with the Department of Fish and Game, the United States Fish and Wildlife Service, the Minerals Management Service and the National Marine Fisheries Service. The site-specific biological and marine mammal surveys shall determine whether the site contains areas of special biological significance that may be adversely affected, either directly or indirectly, by drilling operations or the placement of structures on the leased lands. The surveys shall also determine whether adjacent areas of special biological significance may be similarly affected. Areas of special biological significance include, but are not limited to: (1) existing or potential critical habitats for rare, threatened or endangered species, including but not limited to the California sea otter and the California gray whale; (2) areas used by rare, threatened or endangered species for breeding or migrating; (3) areas containing very unusual or rare ecosystems or ecotones; (4) areas with large numbers or high diversity of species; and (5) areas containing species of limited regional distribution due to natural range or significantly reduced populations.

(b) The biological surveys shall include a characterization of (1) the area within a one (1) kilometer

radius of the development site (and within three hundred (300) meters of pipelines) and (2) areas potentially affected by the development by on-site observations of a marine biologist using a submersible device for deep water or scuba equipment for shallow water. A remote camera survey (video and/or film) may suffice in soft bottom areas. Observations shall be accompanied by photodocumentation and the taking of samples. Box core samples shall be taken on soft bottoms. Rocks, portions of rocks or organisms living on rocks shall be taken from hard bottoms. Sampling and observations shall be most intense within three hundred (300) meters of the development site and within one hundred (100) meters of pipelines. Sample species collected shall be identified to the lowest possible taxonomic level.

(c) The marine mammal surveys shall be performed by a qualified mammologist and shall consist of systematic observations which accurately describe mammal occurrences in and uses of the project area, including an on-site census and behavioral observations of feeding, breeding and migration. The surveys shall also indicate the relationship of project area observations to known data on sea otter and other marine mammal population, size, dynamics, structure and movements in adjacent present or potential habitats.

(d) If the results of site-specific biological and surveys show the existence of a special biological

resource marine mammal that may be adversely affected by lease operations, the Lessee shall (1) pursue feasible alternatives which will not have a significant adverse effect upon the resource identified or employ mitigation measures, (2) establish through submissions to the State of such documents as an oil spill contingency plan and critical operation and curtailment plan, that operations will not have a significant adverse effect upon the resource identified, or (3) establish that it is in the best interests of the State to permit the project even though no feasible alternatives or mitigation measures exist. The State will review all data submitted and after consultation with the Department of Fish and Game, the United States Fish and Wildlife Service and the National Marine Fisheries Service and preparation of a project specific environmental impact report, will determine in writing whether a special biological resource exists and whether it may be significantly affected by lease operations. No lease operations may be commenced until the State has approved the project and has given the Lessee written directions on how to proceed and the Lessee has obtained all necessary governmental approvals and permits. Any mitigation measures provided in the State's written directive shall be based on laws and regulations of the State governing offshore oil and gas activities on State lands and shall be made in consultation with the Department of Fish and Game, the United States Fish and Wildlife

Service and the National Marine Fisheries Service.

(e) If any area of biologically significant resources should be endangered during the conduct of any lease operations, the Lessee shall immediately report such occurrence to the State and take every reasonable effort to protect the resource.

5. FISHERIES TRAINING PROGRAM

The Lessee shall include in its exploration and development plans a proposed fisheries training program. The training program shall be subject to approval by the State after consultation with the Department of Fish and Game and the National Marine Fisheries Service. The training program shall be for the personnel involved in operating vessels used in carrying out lease operations and platform and shore-based supervisors. The purpose of the training program shall be to familiarize persons working on the leased lands of the value of the commercial fishing industry, methods of offshore fishing operations and potential hazards, conflicts and impacts resulting from offshore oil and gas activities. The training program shall be formulated and implemented by qualified instructors.

6. SUSPENSION OF OPERATIONS AND  
EVACUATION OF AND SHELTER FOR PERSONNEL

(a) Before the Lessee operates or causes to be operated on its behalf boat or aircraft traffic into individual, designated warning areas, the Lessee shall

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coordinate and comply with instructions from the Commander, Western Space and Missile Center (WSMC) or other appropriate military agency. Such control and instruction will provide for positive control of boats and aircraft operating in the warning areas at all times.

(b) Recognizing that mineral exploration, exploitation and recovery operations on the leased lands can impede tactical military operations, the Lessee acknowledges and agrees that the United States reserves and has the right to suspend temporarily lease operations in the interest of national security requirement. Such temporary suspension of operations, including the evacuation of personnel and appropriate sheltering of personnel not evacuated (an appropriate shelter shall mean the protection of all personnel engaged in operations on the lease for the duration of any Department of Defense activity from flying or falling objects or substances), will become effective upon the order of the Commander, WSMC, other appropriate military agency or higher authority when national security interests necessitate such action. Any temporary suspension of operations for national security may not exceed seventy two (72) hours, provided that any such suspension may be extended by order of the appropriate authority. Equipment may remain in place during periods of suspension.

(c) The Lessee shall control its own electromagnetic emissions and those of its agents,

employees, invitees, independent contractors and subcontractors emanating from individual, designated defense warning areas in accordance with requirements specified by the Commander, WSMC or other appropriate military agency, to the degree necessary to prevent damage to, or unacceptable interference with, Department of Defense flight, testing or operational activities conducted within individual, designated warning areas. Necessary monitoring, control and coordination with the Lessee, its agents, employees, invitees, independent contractors and subcontractors, will be effected by the Commander of the appropriate onshore military installation conducting operations in the particular warning area, provided that control of such electromagnetic emissions shall permit at least one (1) continuous channel of communication between the Lessee, its agents, employees, invitees, independent contractors or subcontractors, and onshore facilities.

7. ASSUMPTION OF RISK AND HOLD HARMLESS

Whether or not compensation for damage or injury might be due under a theory of strict or absolute liability or otherwise, the Lessee assumes all risks of injury or damage to persons or property which occurs in, on or above the leased lands to any person or any property of any person who is an agent, employee or invitee of the Lessee, or its agents, independent contractors or subcontractors, in connection with any activities being

performed by or for the Lessee in, on or above the leased lands, if such injury or damage to such person or property occurs by reason of the activities of any agency of the United States, its contractors or subcontractors, or any of their officers, agents or employees, being conducted as a part of, or in connection with, the programs and activities of the WSMC or other appropriate military agency.

Notwithstanding any limitations of the Lessee's liability in this lease, the Lessee assumes the risk that such injury or damage is caused in whole or in part by any act or omission, regardless of negligence or fault, of the United States, its contractors or subcontractors, or any of their officers, agents or employees. The Lessee shall indemnify and save harmless the United States against all claims for loss, damage or injury to the Lessee and to the agents, employees and invitees of the Lessee, its agents, independent contractors and subcontractors, in connection with the programs and activities of the aforementioned military installations and agencies, whether the same be caused in whole or in part by the negligence or fault of the United States, its contractors or subcontractors, or any of their officers, agents or employees, and whether such claims might be sustained under theories of strict or absolute liability or otherwise.

\* \* \* \* \*

8. LABOR REQUIREMENT

(a) During exploration, development and production activities on the leased lands, all vessels, rigs, platforms and other vehicles or structures under the control of the Lessee must be manned by citizens of the United States or aliens lawfully admitted to the United States for permanent residence.

b) The requirements of subparagraph (a) do not apply if the Lessee files with the State and the Department of Industrial Relations a report, deemed adequate by these agencies, showing that there is an insufficient number of qualified citizens of the United States, or aliens lawfully admitted to the United States for permanent residence, available for such work.

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EXHIBIT "D"

SLIDING-SCALE ROYALTY FORMULA

The oil royalty shall be calculated according to the following formula:

$$R = \frac{P}{5 + 0.01P}$$

Where R is the royalty rate in percent, and P is the average production of oil per well per day under the lease determined by dividing the total lease production in barrels for the month by the total number of well-production days of 24 hours each.

In no event shall the Lessee pay an oil royalty rate of less than sixteen and two-thirds percent (16-2/3%) or more than fifty percent (50%).

For purposes of applying this formula, a multiple completion well shall be deemed a separate well for each zone into which it is completed and producing where the average daily production from each zone is separately measured and the production from each zone is produced through a separate string of tubing or through casing which is not in communication with any other zone. No well shall be deemed a producing well for inclusion in the formula in any month unless for that month the well produces an amount of oil or gas sufficient to pay for its direct lifting costs as determined by the State.

EXHIBIT 6

DRAFT

POINT CONCEPTION  
NET PROFITS SHARE  
DRAFT  
11-19-82

STATE LANDS COMMISSION  
State of California  
Oil and Gas Lease  
(Net Profits Share)

This Oil and Gas Lease is entered into this \_\_\_\_\_  
day of \_\_\_\_\_, 19\_\_\_\_, pursuant to Division 6 of the  
Public Resources Code, and is between the State of  
California, acting through the State Lands Commission, which  
will be referred to as the State, and \_\_\_\_\_,  
which will be referred to as the Lessee.

In consideration of the rental and share of net  
profits to be paid and the covenants, conditions, agreements  
and stipulations contained in this lease, the State leases  
to the Lessee certain lands, which will be referred to as  
the leased lands, situate in Santa Barbara County,  
California, identified on the attached map that is marked  
Exhibit "A" and described as follows:

\* \* \* \* \*

1.

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1. TERM AND PURPOSE OF LEASE

This lease shall be for a primary term of twenty (20) years, and for so long thereafter as oil or gas is produced in paying quantities from the leased lands, or so long as Lessee is diligently conducting producing, drilling, deepening, repairing, re-drilling or other necessary lease or well maintenance operations on the leased lands. The Lessee shall have the exclusive right to prospect for, drill for, produce and take only oil, gas and other hydrocarbon substances from the leased lands. This right includes the right to conduct geological and geophysical surveys on the leased lands for the purpose of determining subsurface conditions. However, the State may permit others to conduct geological or geophysical surveys on the leased lands as provided in sections 6212.2 and 6826 of the Public Resources Code and the applicable regulations of the State. This lease does not give the Lessee the privilege or right to store gas within the geological zones underlying the leased lands nor any other privilege or right not expressly stated. Within the drilling term of three (3) years from the date of this lease, or a later date determined pursuant to paragraph 24(b), the Lessee shall commence operations for the drilling of a well for oil or gas. If the Lessee fails to commence such operations before or to prosecute them diligently after the expiration of the three (3) year term, or any extension thereof, this lease

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shall terminate. Whenever the leased lands cease to produce oil or gas, the lease will continue in force if within six months after production ceases, or such longer period as the State may authorize, the Lessee commences and prosecutes with reasonable diligence, drilling, deepening, repairing, redrilling or other operations for restoring production of oil or gas from the leased lands.

2. EXPLORATION AND DEVELOPMENT OBLIGATIONS  
AND DRILLING REQUIREMENTS

Within one hundred twenty (120) days after the effective date of this lease, the Lessee shall submit to the State for approval an exploration plan for the leased lands, which plan shall provide at least for the drilling of one (1) well. After the completion of the site-specific environmental review, the Lessee shall commence within the three (3) year drilling term and diligently prosecute exploratory operations in accordance with the approved exploration plan, which shall include whatever measures are necessary to mitigate adverse environmental effects. No later than one (1) year after a commercial discovery, the Lessee shall submit to the State for approval a development plan for the discovered pool or pools. Upon completion of the environmental review, the Lessee shall commence and diligently prosecute development operations in accordance with the approved development plan, which shall include whatever measures are necessary to mitigate adverse

3.

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environmental effects. Development plans for later discovered pools capable of commercial production shall be submitted to the State for approval within one (1) year of discovery. The Lessee shall diligently pursue the acquisition of all permits necessary for the conduct of drilling and production operations on the leased lands and for the construction of structures and facilities on and off the leased lands required for the conduct of drilling and production operations. All drilling operations shall be conducted in accordance with the requirements in Exhibit "B".

### 3. RENTAL

The Lessee shall pay to the State, annually in advance, rental of \$ \_\_\_\_\_ per acre per year through the year in which production in paying quantities is first obtained. Thereafter, rental shall be \$ \_\_\_\_\_ per acre per year and shall be payable annually in advance. If any portion of the leased lands is quitclaimed as to all zones, the annual rental shall be reduced \$ \_\_\_\_\_ for each acre quitclaimed. This reduction shall become effective on the lease anniversary date next following the date of quitclaim.

### 4. NET PROFITS

The Lessee shall pay to the State \_\_\_\_\_ percent (\_\_\_\_%) of the net profits from the operations under this lease. Net profits shall be determined as provided and paid in the manner prescribed in the net profits accounting

procedure, which is Exhibit "D" to this lease.

5. IN-KIND SHARE

From time to time the State may elect to take in kind up to twenty percent (20%) of the oil, gas and/or other hydrocarbon substances removed or sold from the leased lands. The State shall make this election by giving at least sixty (60) days' written notice to the Lessee. In the notice, the State shall specify which hydrocarbon or hydrocarbons it elects to take in kind, the percentage, up to twenty percent (20%), of each hydrocarbon it elects to take in kind and the date it wishes to begin receiving in kind the hydrocarbon or hydrocarbons. If the State elects to take in kind a percentage of the oil removed or sold from the leased lands, the State may require the Lessee to provide at the Lessee's shipping tanks, without charge to the State, tankage of sufficient capacity to store the State's in kind of oil produced during any continuous forty-eight (48) hours. Whenever the State exercises its right to take in kind a share of any hydrocarbon, the value of such hydrocarbon determined in accordance with Exhibit "D" shall be credited to the net profits account. However, any additional value received by the State in a sale or other disposition of any hydrocarbon taken in kind shall not be credited to the net profits account. Upon sixty (60) days' written notice to the Lessee, the State may elect to stop receiving in kind any or all hydrocarbons or any

portion of any or all hydrocarbons taken in kind. The State may exercise its right under this paragraph to take hydrocarbons in kind at any time it is not taking the full twenty percent (20%) of all hydrocarbons removed or sold from the leased lands.

6. TRANSFER OF LEASE

(a) Subject to approval by the State, this lease may be assigned, transferred or sublet to any person, association of persons or corporation who at the time of the proposed assignment, transfer or sublease possesses the qualifications provided in section 6801 of the Public Resources Code. Any assignment, transfer or sublease may involve all or any part of the leased lands or any separate or distinct zone or geological horizon or portion of such zone or horizon. Any assignment, transfer or sublease shall take effect on the first day of the month following its approval by the State and the filing with the State of an executed counterpart thereof, together with any required bond and proof of the qualifications of the assignee, transferee or sublessee to hold this lease or any interest in it. Unless approved by the State, no assignment, transfer or sublease shall be of any effect. Upon approval of any assignment, transfer or sublease, the assignee, transferee or sublessee shall be deemed to have accepted the terms and conditions of this lease.

assignment, transfer or sublease to the contrary notwithstanding.

(b) Any assignment or transfer of a separate portion of this lease or of a separate or distinct zone or geological horizon, or portion thereof, shall segregate the assigned or transferred portion from the retained portion. The approval of the assignment or transfer shall release the assignor or transferor from all obligations thereafter accruing under this lease with respect to the assigned or transferred lands or zones or horizons. The lease on any segregated portion of the lands or zones or horizons shall continue in force for the primary term of this lease, but for not less than two (2) years after the date of discovery of oil or gas in paying quantities upon any of the lands or zones or horizons originally subject to this lease, and so long thereafter as oil or gas is produced in paying quantities from such segregated portion.

(c) With the approval of the State, assignments or transfers may be made of parts of this lease which are on their extended term because of production. The lease on any segregated portion containing only undeveloped lands or zones or horizons shall continue in force for two (2) years and so long thereafter as oil or gas is produced in paying quantities from such segregated portion.

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#### 7. QUITCLAIM

The Lessee at any time may make a written quitclaim of all rights under this lease or of any portion of the leased lands comprising a ten-acre parcel or multiple thereof in a compact form, or of any separate or distinct zone or geological horizon or portion thereof underlying a ten-acre parcel or multiple thereof. The quitclaim shall be effective when it is filed with the State, provided that the Lessee and its surety shall be subject to the continued obligation to pay all accrued rentals and net profits and to abandon all wells drilled into the lands or in the zones or horizons to be quitclaimed in accordance with the terms of this lease and the regulations of the State. At the option of the State, the Lessee may be required to place all such wells in condition for suspension instead of abandoning them. The Lessee shall then be released from all obligations thereafter accruing under the lease with respect to the lands, zones or horizons quitclaimed. The quitclaim shall not release the Lessee or its surety from any liability for breach of any obligation of this lease with respect to which the Lessee is in default at the time of the filing of the quitclaim.

#### 8. CANCELLATION

If the Lessee fails to exercise due diligence and care in the prosecution of the exploratory or development work in accordance with the terms and conditions of this

lease prior to the discovery of oil or gas in paying quantities and if such default continues after thirty (30) days' written notice to the Lessee, the State may cancel this lease. After discovery of oil or gas in paying quantities, this lease may be canceled upon failure of the Lessee, after ninety (90) days' written notice, to comply with the provisions of this lease or applicable statutes or regulations. In the event of cancellation, the Lessee shall have the right to retain any drilling or producing wells as to which no default exists, together with such rights of way into or through the leased lands as may be reasonably necessary to enable the Lessee to drill and operate the retained well or wells. In the event of any termination of this lease in whole or in part, the Lessee shall have a reasonable time to remove any property, equipment and facilities used by the Lessee in operations under the terminated portion of this lease.

9. RESERVATIONS TO STATE

The State reserves the right to grant, upon its own terms, joint or several easements or rights of way upon, through or in the leased lands as may be necessary or appropriate, and the right to allow, upon its own terms, the continued use of any existing easement or right of way upon, through or in the leased lands. The State also reserves the right to lease, sell or otherwise dispose of whatever transferable interest it may have in the surface of the

leased lands, subject to the reasonable use by the Lessee of the surface for operations under this lease.

10. PREVENTION OF WASTE

The Lessee shall use all reasonable precautions to prevent waste of oil and gas in the leased lands and to prevent the entrance of water through wells drilled to the oil or gas-bearing strata that may destroy or injure the oil or gas deposits.

11. COMPLIANCE WITH LAWS AND OTHER OPERATIONAL CONTROLS

The Lessee shall comply with all valid laws and ordinances of the United States and of the State of California and its political subdivisions applicable to the Lessee's operations, including, but not limited to, the applicable provisions of Divisions 3 and 6 of the Public Resources Code and the regulations of the Division of Oil and Gas and State Lands Commission. The Lessee shall also comply with the special operating requirements set forth in Exhibit "C".

12. FORCE MAJEURE

The obligations imposed upon the Lessee by this lease may be suspended whenever the Lessee is prevented from complying with them by wars, strikes, riots, acute and unusual labor or material shortages, acts of God, laws, rules and regulations of a federal, state, county or municipal agency or by other unusual conditions that are

beyond the control of the Lessee. In order for any obligation imposed upon the Lessee to be suspended, the Lessee must notify the State in writing as soon as possible that a condition warranting suspension has arisen. The notification shall state the nature of the condition, an estimate of the condition's duration and the steps to be taken by the Lessee to eliminate the condition. The Lessee shall use its best efforts to eliminate the condition and notify the State in writing as soon as the condition no longer exists.

### 13. OPERATIONAL STANDARDS

The Lessee shall exercise reasonable diligence in the operation of the wells while their products can be obtained in paying quantities and shall not unreasonably or unnecessarily suspend operations. All operations shall be conducted in a proper and workerlike manner, in accordance with generally accepted good oil field practice and with regard for the protection of the safety and health of workers.

### 14. LIABILITY AND INDEMNIFICATION

The Lessee shall be liable to the State for all damage to any reservoir underlying the leased lands and any loss of oil, gas or other hydrocarbon substances to the extent that they are caused by the negligence of, or the breach of any provision of this lease by, or noncompliance with any applicable statutes or regulations by the Lessee,

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