

MINUTE ITEM

This Calendar Item No. 33
was approved as Minute Item
No. 33 by the State Lands
Commission by a vote of 3
to 0 at its 3/27/90
meeting.

CALENDAR ITEM

A 2, 8

33

03/27/90

S 5, 4

PRC 5820

PRC 5821

Willard

**DETERMINATION THAT GEOTHERMAL RESOURCES
ARE BEING DRAINED FROM LEASED LANDS
PRC 5820 AND PRC 5821, SONOMA COUNTY**

LESSEE: GRI Exploration Corporation
1825 South Grant Street, Suite 900
San Mateo, CA 94402
Attn: Mr. Peter A. Hansen

AREA, TYPE OF LAND AND LOCATION.

Approximately 240 acres (PRC 5820 - 40 acres
and PRC 5821 - 200 acres) of reserved mineral
interest land in the northwestern portion of
The Geysers Geothermal Steam Field, Sonoma
County.

BACKGROUND:

PRC 5820 and PRC 5821 were issued by competitive bidding in
1980. Lease PRC 5820 was issued to Geothermal Power
Corporation as highest bidder with a net profit bid of 72.5
percent. Lease PRC 5821 was issued to the surface owner, Squaw
Creek Investment Company, for a net profit bid of 76.1
percent. Both leases were assigned to Aminoil USA, Inc. and
then assigned to GRI Exploration Corporation (GRIE). On
February 9, 1982, the Commission approved the pooling of Lease
PRC 5820 (40 acres) with PRC 5821 (200 acres) so that the
parcels could be developed jointly under a single drilling
obligation and for purposes of royalties and net profits
calculations production would be allocated to the respective
leases in the proportion that the acreage in the lease bears to
the total acreage in the pool.

PERTINENT INFORMATION:

There has been no production from leases 5820 and 5821. In January 1984, a single well was completed and shut in on lease PRC 5821. The well is not connected with any steam plant and there is no likelihood that it will be in the near future. The well is therefore not generating any income to the State.

Last May, the Commission determined that the lessee was in breach of certain lease provisions, including three provisions relating to timely development and marketing of the steam from the leased lands. These breaches involved failure to drill additional wells on the leased property, failure to develop a market for the geothermal resources on these leases, and failure to prepare and submit, to the Commission for approval, annual plans of development and operation. None of these breaches has been cured.

On June 23, 1989, the lessee and three affiliated corporations filed for reorganization under Chapter 11 of the federal bankruptcy law. Those proceedings are still pending in the bankruptcy court.

Immediately to the east of leases PRC 5820 and PRC 5821 is Plant Area A-2. It and Plant Area A-1 to the southeast have been designated by the California Energy Commission as the Plant Areas that are to provide steam to the Coldwater Creek power plant, which is operated by the Central California Power Agency (CCPA). GRIE, the Commission's lessee here, also holds, leasehold rights in the producing wells on Plant Area A-2 that are supplying steam to the Coldwater Creek plant. Wells on Plant Area A-2 have been supplying steam to the Coldwater Creek Plant since March 25, 1988.

Staff has recently confirmed, based on information from Lawrence Berkeley Laboratory, that these other wells operated by GRIE on Plant Area A-2 have drained steam from beneath leases PRC 5820 and PRC 5821. Through December 31, 1989, the amount of steam lost from leases PRC 5820 and PRC 5821 to lands in adjacent Plant Area A-2 is estimated at 2,020,000,000 pounds. Calculated under the pricing provisions of the steam sales contract for the Coldwater Creek project dated March 31, 1983, which was approved by the Commission on March 22, 1984, the estimated royalty lost by the State is \$386,426.

(REVISED 03/27/90)

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Paragraph 15 of the leases contemplates three prospective remedies for drainage situations: (1) drilling offset wells to capture the steam that would otherwise be drained away; (2) unitizing or pooling with the draining wells so that the State may receive its equitable share of the royalties accruing from the steam production that is occurring on the adjacent lands; (3) paying the State a compensatory royalty for the steam that will be lost by drainage.

In this situation, staff believes that neither of the first two remedies offers a timely, economically practicable, and effective solution to the substantial revenue loss to the State that is occurring by virtue of the continuous loss of the State's steam to lessee's other wells to the east. It would be quite costly to drill the necessary offset wells on the State's two leases. More importantly, there is no power plant outside of Plant Areas A-1 and A-2 to which such wells could be connected, so no production could occur from them. Accordingly, the drainage would continue unabated. For unitizing or pooling to work as a prospective remedy, not only would the assent of the other property owners in Plant Area A-2 be necessary, but approval to expand the boundaries of Plant Area A-2 would have to be obtained from both CCPA and the California Energy Commission. These approvals are problematic and would take considerable time, in any case.

The Commission is entitled to payment of compensatory royalty from GRIE to cover the revenue loss to the State from the steam lost by drainage until such time as lessee has fully complied with the provisions of paragraph 15 of the leases concerning prospective relief from drainage.

AB 884: N/A.

OTHER PERTINENT INFORMATION:

1. Pursuant to the Commission's delegation of authority and the State CEQA Guidelines (14 Cal. Code Regs. 15061), staff has determined that this activity is exempt from the requirements of CEQA because the activity is not a "project" as defined by CEQA and the State CEQA Guidelines.

Authority: P.R.C. 6804, P.R.C. 21065 and 14 Cal. Code Regs. 15378.

EXHIBIT: A. Site Map.

IT IS RECOMMENDED THAT THE COMMISSION:

1. FIND THAT THE ACTIVITY IS EXEMPT FROM THE REQUIREMENTS OF THE CEQA PURSUANT TO 14 CAL. ADM. CODE REGS. 15061 BECAUSE THE ACTIVITY IS NOT A PROJECT AS DEFINED BY P.R.C. 21056 AND 14 CAL. CODE REGS. 15378
2. DETERMINE THAT WELLS ON PLANT AREA A-2 ARE PRODUCING GEOTHERMAL RESOURCES IN COMMERCIAL QUANTITIES, AND THAT THOSE WELLS HAVE BEEN AND ARE DRAINING GEOTHERMAL RESOURCES FROM LEASES PRC 5820 AND PRC 5821.
3. AUTHORIZE THE EXECUTIVE OFFICER TO REQUEST COMPLIANCE BY GRI EXPLORATION CORPORATION WITH THE PROVISIONS OF PARAGRAPH 15 OF THE LEASES, WITH DIRECTION TO PURSUE THE PAYMENT OF COMPENSATORY ROYALTY AS THE MOST TIMELY, ECONOMICALLY PRACTICABLE, AND EFFECTIVE SOLUTION TO THE PROBLEM OF CONTINUED DRAINAGE.
4. AUTHORIZE THE EXECUTIVE OFFICER TO DEMAND PAYMENT OF COMPENSATORY ROYALTY BY GRI EXPLORATION CORPORATION FOR ALL DRAINAGE THAT HAS OCCURRED (\$386,426 AS OF DECEMBER 31, 1989) AND ALL CONTINUING DRAINAGE UNTIL SUCH TIME AS THE LESSEE HAS FULLY COMPLIED WITH THE PROVISIONS OF PARAGRAPH 15 OF THE LEASES.
5. AUTHORIZE THE EXECUTIVE OFFICER TO NOTIFY GRI EXPLORATION CORPORATION THAT, IF IT HAS NOT COMPLIED WITH PARAGRAPH 15 OF THE LEASES AND, IN ADDITION, PAID COMPENSATORY ROYALTY FOR PAST DRAINAGE WITHIN A PERIOD OF 120 DAYS FROM SUCH NOTIFICATION, THEN IT SHALL BE CONSIDERED IN DEFAULT OF ITS LEASE OBLIGATIONS UNDER THE TERMS OF PARAGRAPH 33 OF THE LEASES.
6. AUTHORIZE STAFF OF THE COMMISSION AND THE OFFICE OF THE ATTORNEY GENERAL TO TAKE ALL APPROPRIATE ACTION, INCLUDING LITIGATION, TO OBTAIN ALL REMEDIES AVAILABLE TO THE STATE FOR THESE AND THE PREVIOUSLY IDENTIFIED BREACHES OF LEASES PRC 5820 AND 5821.

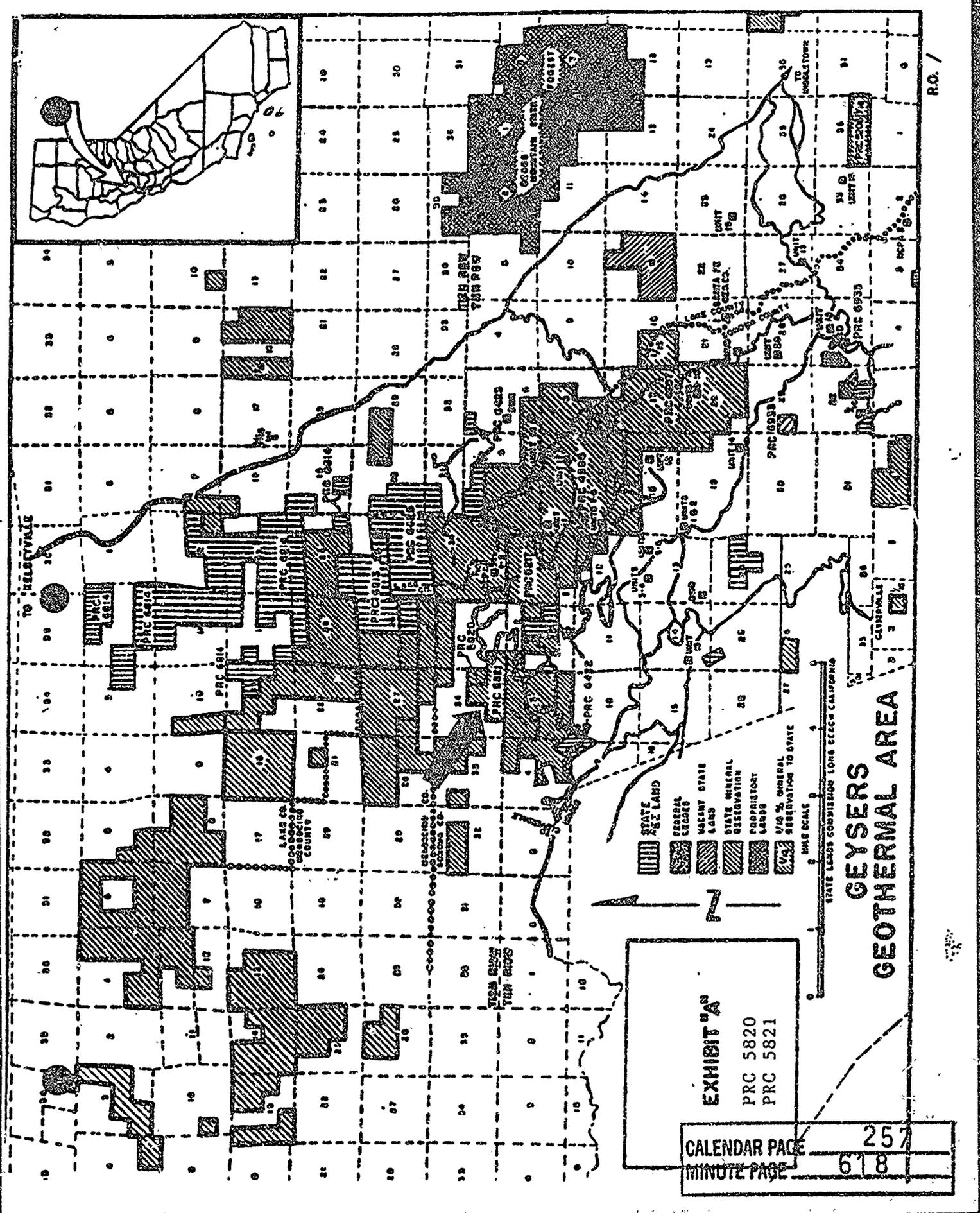


EXHIBIT "A"
 PRC 5820
 PRC 5821

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**GEYSERS
 GEOTHERMAL AREA**

R.O. 7

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