MINUTE ITEM
This Calendar Item No. C61 was approved as Minute Item No. 61 by the California State Lands Commission by a vote of 3 to 0 at its 12-16-02 meeting.

CALENDAR ITEM
C61

A 17

S 5

12/16/02
PRC 2839.1
M. Hamilton

CONSIDER APPROVAL OF THE AMENDMENT OF GAS STORAGE LEASE PRC 2839.1 MCDONALD ISLAND GAS STORAGE FACILITY, SAN JOAQUIN COUNTY

OPERATOR:

Pacific Gas and Electric Company
Attn.: Mr. Loren Loo
77 Beale Street
San Francisco, CA 94105

AREA, LAND TYPE, AND LOCATION:

Sovereign State lands underlying Whisky Slough on McDonald Island, located about 10 miles west of the city of Stockton in San Joaquin County.

BACKGROUND:

On April 4, 1940, the California State Lands Commission (Commission) and Standard Oil Company of California entered into Compensatory Agreement E-412 dated March 1, 1940, to compensate the State for gas withdrawn from sovereign State lands (Whiskey Slough) located within the McDonald Island Gas Field (Exhibit A, attached hereto). In March 1958, after producing over 150 billion cubic feet of natural gas, the field was shut-in and no more gas originally in place was produced.

On March 17, 1960, through Commission approved assignments, Pacific Gas and Electric Company (PG&E) acquired Agreement E-412. On February 27, 1962, the Commission issued Gas Storage Lease PRC 2839.1 to PG&E for a 15-year period commencing March 1, 1962. The lease covers only the Eocene series McDonald Island Sand (the gas storage reservoir) while Agreement E-412 covers the remaining strata.

Under the terms of Lease PRC 2839.1, PG&E received the preferential right to renew Lease PRC 2839.1 for two successive 15-year periods upon such reasonable terms and conditions as may be prescribed by the State. Lease PRC 2839.1 was amended and renewed on August 19, 1977, for the first 15-year renewal term beginning March 1, 1977, and ending March 1, 1992. PG&E has requested the renewal of Lease PRC 2839.1 for the second 15-year period beginning March 1, 1992, and ending on March 1, 2007. Annual rental in the amount of $226,627.25, as provided under the Amendment for the lease year March 1, 2002, through February 2003, has been paid by PG&E. The incremental gas fee, discussed in greater detail below, is set at $0.06774 per Mcf for the March 1, 2002, through February 2003 lease year.

PROPOSED LEASE TERMS:

The Amendment (attached hereto as Exhibit B) provides for PG&E to make annual lease payments at a rate which is the higher of: (1) annual rental; or (2) an incremental gas fee based upon the total volume of gas injected into the storage reservoir during the lease year (March through February), multiplied by the State's percentage share of ownership of the reservoir. The annual rental and the incremental gas fee are based upon the previous year's rental and fees. Annual rental and gas fees are escalated at the rate of five percent (5%) per year. The annual rental and incremental gas fee for the lease year, March 1, 1992, through February 1993, has been determined to be $176,708.92 and $0.04158 per Mcf, respectively.

The Amendment provides that the State's ownership of the storage reservoir will be 12.193 percent (12.193%) for the period March 1, 1992, to September 1, 1995. Beginning September 1, 1995, the State's ownership of the storage reservoir will be reduced to 9.6 percent (9.6%). The reduction in the percentage of the State's ownership of the storage reservoir affects both the amount of annual rental under the lease and the calculation of the percentage of gas injected into the reservoir during the lease year that is attributable to the State lease for purposes of determining the incremental gas fee. In 1995, the year the reduction is implemented pursuant to the Amendment, annual rental on the lease drops from $194,821.60 to $161,059.76. As stated above, due to the effect of the five percent (5%) escalator, annual rental under the proposed amendment has risen to $226,627.25 for the current lease year.

The Amendment will grant PG&E the right to renew the Lease for one additional 15-year period at the end of the current renewal term (March 1, 2007). The Amendment, if approved by the Commission, will be retroactive to March 1,

1992. All other terms and conditions of the Lease will remain unchanged and in full force and effect.

STATUTORY AND OTHER REFERENCES:

A. Gas Storage Lease PRC 2839.1, Paragraph 12 (amendment)

OTHER PERTINENT INFORMATION:

1. Since March 1992, PG&E has been making rental payments based on the escalating rental schedule of the previous lease, the same rental schedule currently proposed in the Amendment. These payments may be adjusted when a final determination has been made between PG&E and the Commission regarding the annual rental and incremental gas fee for the new lease. Currently, all rentals have been paid in full.

2. Based on data from a well drilled on private property adjacent to and west of the McDonald Island Gas Storage facility, PG&E and staff have determined that the storage reservoir is larger than originally estimated, which reduces the State's proportionate share of the storage facility. Therefore, both parties have agreed that beginning September 1, 1995, the State's ownership share of the storage reservoir will be reduced from 12.193 percent (12.193%) to 9.6 percent (9.6%). Since September 1, 1995, the rental payments that were made have been adjusted to reflect the reduced ownership share.

3. The California Department of General Services (CDGS) had expressed an interest in using the State's ownership share of the storage reservoir to store its gas. However, after reevaluating its needs, the CDGS has determined that it is not presently interested in using the State's ownership share of the storage reservoir.

4. Pursuant to the Commission's delegation of authority and the State CEQA Guidelines [Title 14, California Code of Regulations, section 15060(c)(3)], the staff has determined that this activity is not subject to the provisions of the CEQA because it is not a "project" as defined by the CEQA and the State CEQA Guidelines.

   Authority: Public Resources Code section 21065 and Title 14, California Code of Regulations, sections 15060(c)(3) and 15378.

EXHIBITS:

A. Location Map
B. Amendment to Gas Storage Lease PRC 2839.1

PERMIT STREAMLINING ACT DEADLINE:

N/A

RECOMMENDED ACTION:

IT IS RECOMMENDED THAT THE COMMISSION:

CEQA FINDINGS:

FIND THAT THE ACTIVITY IS NOT SUBJECT TO THE REQUIREMENTS OF THE CEQA PURSUANT TO TITLE 14, CALIFORNIA CODE OF REGULATIONS, SECTION 15060(c)(3) BECAUSE THE ACTIVITY IS NOT A PROJECT AS DEFINED BY PUBLIC RESOURCES CODE SECTION 21065 AND TITLE 14, CALIFORNIA CODE REGULATIONS, SECTION 15378.

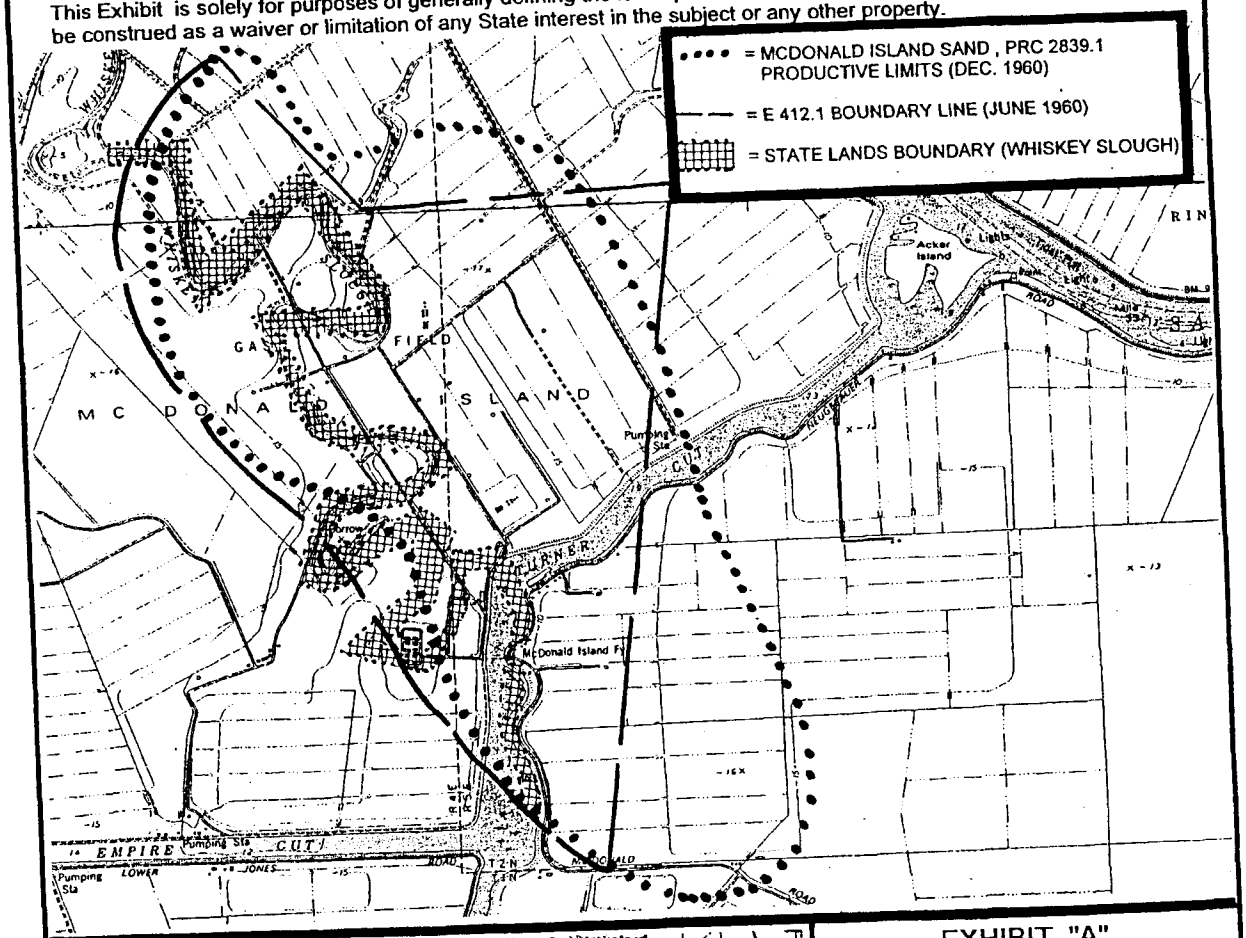
AUTHORIZATION:

1. CONSENT TO THE RENEWAL AND AMENDMENT OF GAS STORAGE LEASE PRC 2839.1; AND GRANT TO THE LESSEE THE RIGHT TO RENEW THE LEASE FOR ONE ADDITIONAL FIFTEEN (15) YEAR PERIOD, COMMENCING MARCH 1, 2007, UPON SUCH REASONABLE TERMS AND CONDITIONS AS THE STATE MAY PRESCRIBE; EACH AS MORE PARTICULARLY SET FORTH IN EXHIBIT B, ATTACHED.

2. AUTHORIZE THE EXECUTIVE OFFICER OR HIS DESIGNEE TO EXECUTE ALL DOCUMENTS NECESSARY OR CONVENIENT TO FULLY IMPLEMENT THE COMMISSION'S ACTION.

EXHIBIT A

This Exhibit is solely for purposes of generally defining the lease premises and is not intended to be, nor shall it be construed as a waiver or limitation of any State interest in the subject or any other property.



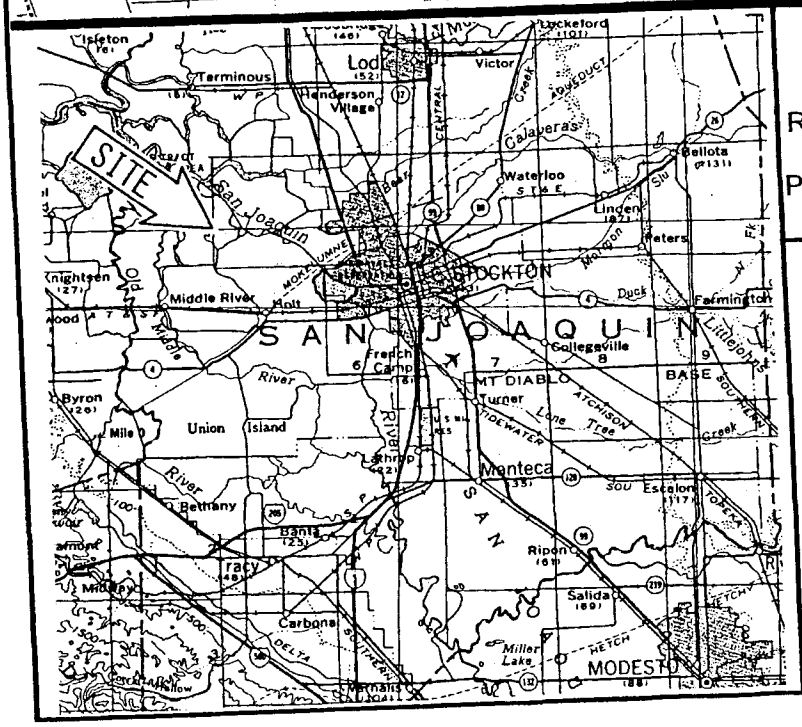


EXHIBIT "A"
LOCATION MAP
PRC 2839.1
RENEWAL OF GAS STORAGE LEASE
PACIFIC GAS & ELECTRIC CO.
SAN JOAQUIN COUNTY, CA.

CNP 98

STATE LANDS COMMISSION
GAS STORAGE LEASE PRC 2839.1

- AMENDMENT -

This Amendment to Gas Storage Lease PRC 2839.1 ("Lease") is made and entered into on _____ by and between the State of California acting through the State Lands Commission ("State") and Pacific Gas and Electric Company, a California corporation ("Company").

Recitals

The Lease was originally entered into between the State and the Company on January 25, 1962 for a period of fifteen (15) years. The Lease gave the Company a preferential right of renewal for two (2) successive periods of fifteen (15) years each upon such reasonable terms and conditions as may be prescribed by the State. The Lease was renewed and amended on August 19, 1977 for a fifteen (15) year term beginning March 1, 1977 and ending March 1, 1992. The Company seeks to renew the Lease for a second fifteen (15) year period beginning March 1, 1992.

The State and the Company wish to make additional amendments to the Lease to be effective for the second fifteen (15) year term.

Renewal and Amendment

1. Acting pursuant to Paragraph 14 of the Lease and in consideration of the sums provided for and the covenants, conditions and agreements below, the State renews the Lease for a period of fifteen (15) years, beginning at 7:00 a.m. on March 1, 1992 and ending at 7:00 a.m. on March 1, 2007.

2. Paragraph 5 of the Lease shall be deleted and the following substituted in its place:

5. The Company shall pay to the State the higher of (1) an annual rental, or (2) an incremental gas fee on all gas injected for storage during the lease year (March through February). If the Company fails to pay the appropriate annual rental or incremental gas fee for any lease year, the State may terminate this Lease upon giving ninety (90) days notice to the Company, or may continue the Lease with the right to exercise any legal or equitable remedy that the State might otherwise have.

(a). All annual rentals shall be based on the State's ownership share of the storage reservoir as specified in Paragraph 6 of the Lease. For the period March 1, 1992 to September 1, 1995, the rentals are based on the State's ownership of 12.193% of the storage reservoir as specified in Paragraph 6 of the Lease. Beginning on September 1, 1995 and running through the end of the fifteen (15) year lease term, the annual rentals shall be based on the State's ownership of 9.6% of the storage reservoir as specified in Paragraph 6 of the Lease.

The annual rental for the lease year beginning on March 1, 1992 shall be $176,708.92, shall be increased each year by five percent (5%) of the previous year's annual rental and shall be subject to adjustment as provided in Paragraph 6 of the Lease. The annual rental shall be due and payable in advance by March 1 of each year.

(b) All incremental gas fees shall be based on the State's ownership share of the storage reservoir as specified in Paragraph 6 of the Lease. For the period March 1, 1992 to September 1, 1995, the incremental gas fees shall be based on the State's ownership of 12.193% of the storage reservoir as specified in Paragraph 6 of the Lease. Beginning on September 1, 1995 and running through the end of the fifteen (15) year term, the incremental gas fees shall be based on the State's ownership of 9.6% of the storage reservoir as specified in Paragraph 6 of the Lease.

The incremental gas fee shall be based on all gas injected for storage. The incremental gas fee for the lease year beginning on March 1, 1992 shall be $0.04158 per Mcf, shall be increased each year by five percent (5%) of the previous year's annual incremental gas fee and shall be subject to adjustment as provided in Paragraph 6 of the Lease. By March 25 of each year, the Company shall submit to the State a written statement showing for the immediately preceding lease year the total quantity of gas injected for storage and the Company shall pay to the State the difference between the incremental gas fee and the annual rental for the previous lease year if the former exceeds the latter. The State's acceptance of any payment representing the incremental gas fee shall not be deemed a waiver of the State's right to object to the aforementioned statement. The records and accounts of the Company supporting the statement shall be subject to audit by the State at all reasonable times.

All late rental and incremental gas fee payments are subject to interest and penalty charges as specified in Title 14, California Code of Regulations, section 1911.

3. Paragraph 6 of the Lease shall be deleted and the following substituted in its place:

6. The State's ownership share of the storage reservoir has been determined to be 12.193% for the period March 1, 1992 to September 1, 1995. The State and the

Company have determined that beginning September 1, 1995 the State's ownership share of the storage reservoir shall be 9.6%. The State's ownership share of the storage reservoir has been determined according to the best judgment of the State and the Company based upon currently available geological data. Should it be determined by the State and the Company based on subsequently acquired geological data that the area of the storage reservoir or the State's ownership share of the storage reservoir is greater or smaller than herein specified, then an appropriate adjustment shall be made in the State's ownership interest and Exhibit "A" attached hereto shall be modified accordingly. Any such adjustment shall be effective at 7:00 a.m. of the first day of the calendar month in which the adjustment is determined and agreed to by the State and the Company.

4. Paragraph 14 of the Lease shall be deleted and the following substituted in its place:

14. The Lease shall be effective on January 25, 1962 and shall continue in effect until 7:00 a.m. on March 1, 2007. The Company shall have the right to renew the Lease for one (1) additional period of fifteen (15) years at the expiration of the present period upon such reasonable terms and conditions as may be prescribed by the State, unless applicable law in effect at the time of the expiration of the Lease prevents such renewal. If the Lease is terminated pursuant to the provisions of Paragraph 5, 12 or 13 of the Lease, the Company shall have the right for a period of five (5) years after any such termination to withdraw from the storage reservoir all gas injected by the Company and all native gas for which the Company has paid the State its share pursuant to Paragraph 1 of the Lease. If the Company exercises this right, it shall continue to be responsible for payment to the State of the higher of the annual rental or incremental gas fee through the end of the lease year in which the Lease is terminated.

This Amendment shall be effective retroactively to March 1, 1992. All other terms and conditions of the Lease shall remain unchanged and in full force and effect.

Pacific Gas and Electric Company	**State Lands Commission**
By: _____	By: _____
Name: _____	Name: _____
Title: _____	Title: _____
Date: _____	Date: _____

All signatures must be acknowledged.