

MINUTE ITEM

This Calendar Item No. C44 was approved as Minute Item No. 44 by the California State Lands Commission by a vote of 3 to 0 at its 12/9/04 meeting.

**CALENDAR ITEM
C44**

A 67
S 35

12/9/04
W 25306
J. Trout
A. Reid
P. Griggs

CONSIDER APPROVAL OF AN AGREEMENT TO COMPENSATE AERA ENERGY LLC FOR IMPACTS TO ITS OIL AND GAS OPERATIONS FROM THE CONSTRUCTION OF THE PACIFIC COAST HIGHWAY BRIDGE AS PART OF THE BOLSA CHICA LOWLANDS RESTORATION PROJECT AND AUTHORIZE THE EXECUTIVE OFFICER TO SIGN AND IMPLEMENT THE AGREEMENT

PARTIES:

California State Lands Commission, in its Capacity as the Kapiloff Land Bank Trustee

Aera Energy LLC
10000 Ming Ave.
P.O. Box 11164
Bakersfield, Ca 93389-1164

BACKGROUND: As part of the Bolsa Chica Lowlands Restoration Project (Project) that was approved by the State Lands Commission (Commission) on January 30, 2002 (Calendar Item 49), it will be necessary to construct a tidal inlet channel with rock jetties and to construct a bridge over the inlet channel for Pacific Coast Highway (PCH) (State Route 1). During the construction of the bridge, a detour will be constructed to provide for traffic on PCH. Bridge construction is expected to be completed within a period of 9 months, but could take longer. In fulfillment of the Interagency Agreement approved by the Commission on August 21, 1996 (Calendar Item 90), between the California State Lands Commission, the U.S. Environmental Protection Agency, the California Department of Fish and Game, the U.S. Fish and Wildlife Service, the State Coastal Conservancy, the National Marine Fisheries Service, the California Resources Agency, and the U.S. Army Corps of Engineers, the U.S. Fish and Wildlife Service awarded the construction contract on September 1, 2004, and is overseeing the construction effort.

Immediately adjacent to PCH are numerous oil wells operated by Aera Energy LLC (Aera). The oil wells have been directionally drilled from surface locations on upland sites into the State's tide and submerged lands leased pursuant to Oil and Gas Leases

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PRC 163 and 426 (Whipstock wells). The upland sites are part of the lands acquired by the State Lands Commission (SLC) for the Project. The land acquisition was approved by the Commission on February 12, 1997 (Calendar Item 90). The SLC acquired the property subject to pre-existing lease obligations connected with oil and gas operations. The Bolsa Surface Use Agreement, dated September 2, 1971, as amended (BSUA), governs the relationship between the fee owner (SLC) and the oil and gas lessee (now Aera) by allowing for the development of the surface of the Project lands, subject to an obligation on the part of the fee owner to compensate the oil and gas lessee for resulting disruption of the lessee's oil and gas operations.

In furtherance of the Project, the SLC and Aera's predecessor in interest signed the Operating Assurances Agreement (OAA) on February 13, 1997, in recognition of the plans to restore the Bolsa Chica property as wetlands and the financial obligations of the SLC on behalf of the Project under the BSUA. Under the OAA and subsequent implementing agreements, the SLC agreed to pay the costs to abandon 39 wells and for production lost due to the premature abandonment of these wells. The payment for lost production was set at \$4,620,000, and the abandonment costs were estimated at \$5,180,000. The abandonment effort is nearly complete.

At the time the costs for abandonment and lost production were negotiated, the construction design for the PCH bridge was not complete. As a result, potential impacts to Aera's operation of the Whipstock wells was not recognized. Although there is room to construct the PCH detour and install concrete barriers between the existing PCH and the Whipstock wells, there will be a temporary loss of critical access space surrounding the wellheads that will preclude the use of a standard workover rig on thirteen of the wells should any of them require maintenance during the time the detour is in place. Even with good oilfield practices, maintenance is required from time to time when well equipment breaks down. Additionally, construction of the bridge, especially the pile-driving activities, may cause well equipment to fail because of the impacts from the extreme vibration.

STAFF REPORT: Although the number of well workovers needed during the time the detour is in place is unknown, studies suggest that six well workovers may be expected. The actual number could be higher or lower. Aera and SLC staff have determined that a special type of workover rig, a Hydraulic Workover Rig (HWR), would be able to fit in the limited space available during the time the detour is in place. The HWR is more expensive to use and takes longer to operate than a standard rig. Use of the HWR may be economically justified, however, depending on a particular well's production rate and the expected remaining duration of the detour.

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The proposed agreement (Agreement) (Exhibit A), provides for SLC to compensate Aera for the incremental costs to use the HWR over a standard rig for workovers and for lost and/or deferred production attributable to the Project. Decisions on whether to conduct maintenance requiring the HWR will be made jointly by Aera and SLC based on an economic analysis of the potential return.

To minimize potential costs, proactive well workovers are being conducted on three wells that would most likely require maintenance during the time the detour is in place. Aera would not have conducted these well workovers at this time except for the impending detour. The Agreement provides for a 50/50 split of the costs associated with this proactive work, estimated to cost the Project less than \$50,000.

To further minimize potential costs related to well downtime, advance engineering preparations to implement and mobilize the HWR will be undertaken immediately, in anticipation that one or more wells will require maintenance. These costs are not expected to exceed \$400,000 and will be borne exclusively by the Project. The proactive well workovers and the preparations for the HWR could substantially reduce overall costs to the Project because they will likely reduce the amount of well downtime and resulting lost and/or deferred production for which the Project might have to compensate Aera.

Because of the urgent need to conduct the proactive well workovers and begin the advance engineering preparations for the HWR before the Detour is in place, The Bolsa Chica Wetlands Steering Committee approved these expenditures and requests ratification by the Commission.

Total compensation and/or reimbursement under the proposed Agreement is capped at \$2.5 million. This represents the parties' best estimate of the financial impacts caused by the PCH detour. It is only an estimate, however, and impacts could greatly exceed this amount. Should impacts exceed the cap, additional authorization may be sought from the Commission to increase the \$2.5 million cap under the Agreement. In such event, the State Lands Commission may elect to increase the cap, or require Aera to seek such additional compensation as it may be entitled to pursuant to the terms of the BUSA and OAA.

The State's royalty interest in the Whipstock wells is 25 percent at current oil prices. Any payments made to Aera on account of lost and/or deferred oil and gas production, shall be subject to the obligation to pay the State the royalty percentage attributable to such production. Royalty payments to the State made under the Agreement will be treated as a "subsidy" or "extra payment" under Paragraph 2 of each of the Oil and Gas Leases PRC 163 and 426. No amendment of the leases is required.

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It is expected that the Bolsa Chica Wetlands Steering Committee will approve a recommendation that the State Lands Commission approve the Agreement before the State Lands Commission considers this Calendar Item. Compensation under the proposed Agreement will be paid from mitigation funds for the Bolsa Chica Lowlands Restoration Project held in trust in the Kapiloff Land Bank Fund for that purpose.

If the Commission does not authorize the Agreement, Aera would almost certainly claim the incremental costs of well workovers and lost and/or deferred production under pre-existing agreements, including the BSUA and OAA. Staff believes that compensation under such circumstances would likely expose the Project to greater expense than the proposed Agreement provides.

Additional Funding: The funds available to complete the Bolsa Chica Lowlands Restoration Project are inadequate to pay the projected expenses of the Project. The construction contract awarded by the U.S. Fish and Wildlife Service on behalf of the Project is for approximately \$64 million. With the funds currently available, there is an estimated deficiency of \$5 to 10 million, depending on contracting change orders resulting from unexpected conditions. Expenses incurred under the proposed Agreement with Aera will contribute to that deficiency. Efforts are underway by all members of the Steering Committee to identify and obtain this needed funding.

OTHER PERTINENT INFORMATION:

1. Authority to enter into the Agreement: The Commission certified the Bolsa Chica Lowlands Restoration Project (Project) Final Environmental Impact Report/Environmental Impact Report/Environmental Impact Statement, adopted Findings, adopted a Mitigation Monitoring Program, and adopted a Statement of Overriding Considerations, and approved the Project on January 30, 2002. The NEPA lead agencies issued the Record of Decision in the second quarter of 2002.

Public Resources Code section 8613(b) provides that "Moneys deposited in the [Land Bank] fund pursuant to subdivision (b) or (c) of Section 8625 shall be available for expenditure by the trustee for management and improvement of real property held by the trustee to provide open space, habitat for plants and animals, and public access."

2. 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

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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.

EXHIBIT:

- A. Bolsa Chica Lowlands Restoration Project Pacific Coast Highway Detour Impacts Reimbursement Agreement

RECOMMENDED ACTION:

IT IS RECOMMENDED THAT THE COMMISSION:

AUTHORIZATION:

1. FIND THAT THE COMMISSION IS ACTING IN ITS CAPACITY AS LAND BANK TRUSTEE UNDER THE KAPILOFF LAND BANK ACT, PUBLIC RESOURCES CODE SECTIONS 8600 *ET SEQ.*
2. FIND THAT THESE ACTIVITIES ARE EXEMPT FROM THE REQUIREMENTS OF CEQA PURSUANT TO TITLE 14 CALIFORNIA CODE OF REGULATIONS, SECTION 15060(c)(3) BECAUSE THESE ACTIVITIES ARE NOT PROJECTS AS DEFINED BY PUBLIC RESOURCES CODE SECTION 21065 AND TITLE 14 CALIFORNIA CODE OF REGULATIONS, SECTION 15378.
3. RATIFY THE EXPENDITURE OF AN AMOUNT NOT TO EXCEED \$50,000 FOR THE PROACTIVE WELL WORKOVERS AND AN AMOUNT NOT TO EXCEED \$400,000 FOR THE ADVANCE ENGINEERING WORK FOR THE HYDRAULIC WORKOVER RIG, BOTH AS DESCRIBED HEREIN.
4. AUTHORIZE THE EXECUTIVE OFFICER TO EXECUTE THE AGREEMENT ATTACHED HERETO IN SUBSTANTIVELY THE SAME FORM AS EXHIBIT A, AND TO EXECUTE ALL OTHER DOCUMENTS AND TO TAKE SUCH OTHER ACTIONS AS ARE REASONABLY NECESSARY TO COMPLETE THE RESTORATION.
5. AUTHORIZE THE EXECUTIVE OFFICER OR HIS DESIGNEE TO IMPLEMENT THE AGREEMENT AND APPROVE THE

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EXPENDITURE PURSUANT TO THE AGREEMENT IN AN AMOUNT NOT TO EXCEED \$2.5 MILLION (INCLUDING THE AMOUNTS BEING RATIFIED) OF MITIGATION FUNDS HELD IN TRUST IN THE KAPILOFF LAND BANK FUND FOR THE BOLSA CHICA LOWLANDS RESTORATION PROJECT.

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**Bolsa Chica Lowlands Restoration Project
Pacific Coast Highway Detour Impacts
Reimbursement Agreement**

This Bolsa Chica Lowlands Project Reimbursement Agreement (“Reimbursement Agreement”) is made and entered into by and between the California State Lands Commission (the “SLC”) and Aera Energy LLC (“Aera”) (successor to CalResources LLC), collectively referred to as the “Parties”, and it shall be effective _____, 2004.

WHEREAS, the SLC, in cooperation with seven other state and federal agencies is undertaking a project (the “Project”) to restore the wetlands and habitat areas found on portions of the Bolsa Chica Lowlands and the Bolsa Chica Ecological Reserve; the SLC owns the restoration Project lands and administers Project funds; and the U.S. Fish and Wildlife Service (“FWS”) is responsible for construction of the restoration Project; and

WHEREAS, Aera operates the overlying oil field facilities pursuant to certain oil and gas leases; and

WHEREAS, pursuant to that certain “Agreement Implementing Provisions of the Bolsa Surface Use Agreement and the Operating Assurances Agreement Concerning Acquisition of Surface Rights; Lost Production; and Plugging and Abandonment at Bolsa Chica, Orange County, California,” effective August 13, 2003 (“Agreement”) Aera will abandon 56 of Aera’s wells in the Full Tidal Area of the Signal Lowlands portion of the Bolsa Chica and relinquish the Aera surface rights in exchange for a lost production payment and certain cost reimbursement; and

WHEREAS, in addition to the abandonment work to be performed and the cost to be reimbursed under the Agreement, Aera will be impacted due to construction of the Pacific Coast Highway (“PCH”) bridge, which requires a detour of PCH (“Detour”), onto property owned by the State and under the jurisdiction of the SLC, containing oil wells (Whipstock wells) that have been directionally drilled into the State’s tide and submerged lands leased to Aera pursuant to Oil and Gas Leases PRC 163 and 426. The Detour will result in limiting access to wells for the purpose of well workover with conventional workover rig equipment. In addition, it is anticipated that certain construction activity may impact the ability to operate certain wells, and that there may be resulting production impacts; and

WHEREAS, the SLC acquired the property subject to pre-existing lease obligations connected with oil and gas operations, including the Bolsa Surface Use Agreement, dated September 2, 1971, as amended (“BSUA”) that governs the relationship between the fee owner (SLC) and the oil and gas lessee (now Aera) by allowing for the development of the surface of the Project lands, subject to an obligation on the part of the fee owner to compensate the oil and gas lessee for certain resulting disruption of the lessee’s oil and gas operations; and

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WHEREAS, in furtherance of the Project, the SLC and Aera's predecessor in interest signed the Operating Assurances Agreement (OAA), dated February 13, 1997, providing in Article 12 that "[t]he SLC agrees that the surface of the entire Whipstock Area shall be owned and managed by the SLC to support oil operations for the duration of oil operations there, subject, however, to the construction, operation, and maintenance of the Tidal Inlet in accordance with the Bolsa Chica Lowlands Project Agreement;" and

WHEREAS, the OAA also provides in Article 13 (C) that "[d]uring the construction of the Project, and in the operation and maintenance of the Project, the SLC shall plan and coordinate all work with CalResources [now Aera] in a manner that minimizes production downtime. Likewise, CalResources will, in good faith, cooperate with the SLC and any third party which is managing the construction, operation, and maintenance of the Project;" and

WHEREAS, the Parties desire to enter into this Reimbursement Agreement to provide for reimbursement and/or compensation by the SLC for the incremental costs associated with servicing and maintaining the wells with limited access, for fixed costs agreed upon to develop an alternate well workover solution, and for impacted oil production below the mutually agreed upon decline curve, due to the Detour and to accommodate the restoration of the Bolsa Chica Lowlands as a full tidal wetland and wildlife habitat; and

WHEREAS, reimbursement and/or compensation by the SLC for such costs incurred by Aera, and its engineering support contractors, will be paid from money deposited into the Kapiloff Land Bank Fund as mitigation funds to be used for the Project and administered by SLC for that purpose;

NOW THEREFORE, in consideration of the terms and conditions of this Reimbursement Agreement, as well as the relevant terms and conditions of the Agreement, OAA, and the BSUA, the Parties agree as follows:

COST REIMBURSEMENT

1. Aera staff time, engineering support contractor's time, and contractor's time and materials, will be directly chargeable as described below and as shown on the attached Exhibit A. Except for the proactive well workovers described in 4E and the advance engineering preparations to implement and mobilize the HWR described in paragraphs 4A and 6, liability for reimbursement and/or compensation under this Reimbursement Agreement will begin when the wells listed in Exhibit __ are physically inaccessible to a conventional workover rig due to the Detour. Liability will cease to accrue upon the removal of the Detour's physical barriers, and/or restoration of accessibility to said wells by a conventional workover rig, whichever first occurs. Aera shall establish and use a system of accounting that will account for all costs to be reimbursed under section 4. All such costs to be reimbursed shall be commercially reasonable.

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2. The Parties acknowledge and agree that there are other wells in the Whipstock area that may be idle, injection, or producing, that shall not be entitled to receive any reimbursement and/or compensation under this Reimbursement Agreement because of limited access caused by the Detour. Only the wells listed in Exhibit ___ shall be entitled to reimbursement and/or compensation due to limited access caused by the Detour. Changes and/or additions to the scope of work, not identified on Exhibit A, shall be reimbursed only if Aera has submitted such changes and/or additions to the SLC and has received express written authorization from the SLC to proceed. Such changes and/or additions shall be documented on a Change Order Management Log, and be tracked against the amounts allocated as shown on Exhibit A.

3. Aera shall not obligate or use the contingency funds shown on Exhibit A unless it has received written authorization from the SLC to obligate or use said funds. Such authorization will not be unreasonably withheld by the SLC.

4. The total amount of reimbursable funds provided for under this Reimbursement Agreement is \$2,500,000.00, composed of the following elements:

A. Reimbursement of all costs associated with implementation and mobilization of a Hydraulic Workover Rig (“HWR”), for the purpose of performing maintenance activities on certain wells listed in Exhibit ___ that cannot be accessed with a conventional well workover rig. The cost estimate for implementation and mobilization of the HWR is \$177,600, plus Aera’s administrative overhead of 15%, \$26,640, totaling approximately \$204,240 for this element.

B. Reimbursement of all costs associated with Stand-by rental charges for the HWR, when not being used, based on the proposed daily rig rental rate. The stand-by rig rental is a strategic decision to minimize well downtime and associated production impacts, associated with high mobilization/demobilization costs and mobilization turnaround times from Contractor’s base of operations out of state. The cost estimate for this element is approximately \$230,000, assuming a nine-month Detour. Aera’s Administrative Overhead for this element shall be 0% (zero).

C. Reimbursement of all incremental costs, associated with performing well workover maintenance. Incremental costs shall be defined as Total Cost, minus Base Cost. Neither Total Cost nor Base Cost shall include any downhole “Equipment Costs”, (i.e.; tubulars, pump, cable, etc. For the purposes of this agreement, “Base Cost” is defined as the average well workover cost for this set of wells, normalized for well depth (see Exhibit B – Base Costs by Well). The estimated incremental costs on a per well basis are approximately \$120,000 per well. Based upon an estimate of six well workovers to be performed during the Detour, the incremental costs would be \$720,000, plus Aera’s administrative overhead of 15%, \$108,000, totaling \$828,000 for this element.

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(i). Aera will notify SLC of a well problem within 24 hours of Aera verifying that a failure or a significant problem exists, excluding weekends.

(ii). Economic analysis will be performed utilizing a mutually agreeable tool, to determine whether the incremental costs associated with servicing the well are offset by the impacted production revenues, based on Detour duration remaining, individual well production, oil price of the day, and other variables.

(iii). The decision to work on any individual well subject to this Reimbursement Agreement will be a joint decision made between Aera and SLC.

(iv). Cost reconciliation and Aera's request for reimbursement shall be completed at the end of each well workover.

D. Reimbursement for all impacted production that falls below the historical decline curve of 10.0%, based on an allocated oil production for specified quarterly periods starting 12/1/04. Allocated oil production targets have been set for each quarterly period (see Exhibit C – Quarterly Oil Production). Actual oil production which falls below the target for each quarterly period shall be reimbursable, at the average oil price postings for the given period, adjusted for API Gravity and Aera Operating Cost, of \$9.03 per barrel of oil. Aera's administrative overhead for this paragraph 4D shall be 5%. Costs under this paragraph 4D have the potential to be significantly higher than the estimate shown in Exhibit _____. Total reimbursable costs for impacted production shall not exceed \$1 million, without written approval from SLC. Total reimbursable costs under this Reimbursement Agreement above the \$2.5 million cap specified in paragraph 8 will be treated as provided in paragraph 8.

(i). Quarterly periods shall be as follows; 12/1/04 – 2/28/05, 3/1/05 – 5/31/05, 6/1/05 – 8/31/05, and 9/1/05 – 11/30/05. In the event that the Detour takes longer than 9 months, and additional quarterly periods are required, they shall be as follows; 12/1/05 – 2/28/06, 3/1/06 – 5/31/06, 6/1/06 – 8/31/06, and 9/1/06 – 11/31/06.

(ii). Aera shall be responsible to initiate workover operations on an identified well within a reasonable timeframe, using sound oilfield practices, when scheduling well work and rig availability. This may be impacted by HWR availability during the first months of the Detour, and when the HWR is already working on a well previously selected for workover maintenance.

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(iii). Aera and SLC will meet on a quarterly basis to reconcile actual production versus decline curve production in order to determine a quarterly invoice amount, if any. All production which falls below the agreed upon decline curve for the quarter shall be paid at the average quarterly price as determined by using the current pricing formula basis paid to the SLC by Aera for other SLC royalty at the Huntington Beach Field, for the specific period, plus Aera's administrative overhead of 5%. Reimbursable costs under this paragraph 4D will be normalized in Barrels in order to ensure proper payment by Aera to all royalty owners of said Barrels.

(iv). Final reconciliation of impacted production, below the decline curve, over the life of the Detour will be conducted within 60 days of the removal of the Detour, and/or restoration of all rig accessibility, whichever first occurs. Final reconciliation will be the difference between all targeted production versus all actual production, rounded to the nearest month. Production volumes above the decline curve shall be used as an offset to volumes below the decline curve only. If the reconciliation shows that there were no net oil production impacts that fall below the decline curve, for the duration of the Detour, the reimbursable amount would be zero.

(v). Any sums paid to Aera for impacted production pursuant to paragraph 4D of this Reimbursement Agreement from wells producing from State Leases PRC 163 and 426 shall be treated as a "subsidy" or "extra payment" under paragraph 2 of said leases, for which royalty shall be payable to the State according to the terms of said leases.

E. Proactive Well Workovers to minimize Project risks of well downtime during the Detour. - Due to the impending Detour and the high cost of workover during the Detour, Aera has chosen to conduct proactive well workovers on three wells, in order to minimize risks of downtime. As this proactive well work is primarily to benefit the Project, by minimizing the risk of a well going down during the Detour, Aera and the SLC agree the cost shall be shared 50/50, by each party. Aera estimates that this cost will be approximately \$87,000, whereby SLC shall be liable for \$43,500, plus Aera's administrative overhead of 5%, \$2,175, totaling \$45,675 for this activity. Aera shall charge the SLC one time for charges under this paragraph 4E, as per the applicable shared cost.

F. Other items not covered above by section 4, paragraphs A through E. In the event there are issues raised by either party that cannot be agreed upon then such issues shall be resolved by the arbitration process in Exhibit C of the "Agreement Implementing Provisions of the Bolsa Surface Use Agreement and the Operating Assurances Agreement Concerning Acquisition of Surface Rights; Lost Production; and Plugging and Abandonment at Bolsa Chica, Orange County,

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California,” dated August 13, 2003, incorporated herein by reference. Examples of issues that may fall under paragraph 4F include, but shall not be limited to, loss of water injection support, abnormal well failure requiring extended engineering time, permitting, and damage to surface equipment due to pile-driving activities. Notwithstanding anything to the contrary, Aera shall not be entitled to reimbursement for any costs of operations or loss of or delay in production that would have been incurred or suffered if construction of the Project had not occurred, excluding normal operating upsets and well downtime that are already built into the historical decline curve as referenced in paragraph 4D.

5. SLC or its duly authorized representative shall have reasonable access during normal business hours to review and copy the accounting records and other documents maintained by Aera which relate to charges under this Reimbursement Agreement. Aera agrees to maintain such records for possible audit for a period of four years after final payment.

6. Subject to the terms and conditions of this Reimbursement Agreement, Aera shall work in coordination with SLC on completing all items with relation to the implementation and mobilization planning for the HWR, noting that the Detour is likely to be in place, on or about 11/25/04, and there will be a time period that the Project is exposed to more risk of impacted production, due to not having these items completed. Aera agrees that all items referred to in paragraph 4A necessary to mobilize the HWR will be completed within 60 days of the effective date of this agreement. In the event that the SLC has previously agreed to approval and/or release of funds for the purpose of expediting the Engineering work and associated preparation work for the HWR, those funds shall be bound by the terms, as set forth in this agreement.

7. Aera will invoice the SLC, in arrears, not more often than monthly, for the work and services to be reimbursed under this Reimbursement Agreement. All invoices shall be accompanied by a statement of charges detailing costs incurred. If any payment is not made within 60 days after receipt of invoice by the SLC, the unpaid balance shall bear interest at the rate provided for under California Government Code section 926.10.

8. The Parties have agreed that the maximum amount of reimbursement and/or compensation recoverable against the SLC under the terms of this Reimbursement Agreement shall be capped at \$2.5 million. Reimbursement and/or compensation in excess of \$2.5 million (“Excess Charges”) that Aera claims it is entitled to recover against SLC, shall be submitted under the provisions of this Reimbursement Agreement. The State Lands Commission, may in its sole discretion, increase the cap to cover all or any portion of Excess Costs. The Bolsa Chica Wetlands Steering Committee will provide its recommendation to the State Lands Commission concerning any Excess Costs. Any Excess Charges not approved for payment shall be treated for all purposes as outside the scope of this Reimbursement Agreement and Aera may seek reimbursement and/or compensation pursuant to terms of the OAA and the BUSA, to the extent such Excess Charges are allowable. Aera shall promptly notify the SLC as soon as reimbursement

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and/or compensation covered by this Reimbursement Agreement reaches ninety percent (90%), \$2,250,000, or more, of \$2.5 million.

9. Aera shall exercise reasonable diligence in the operation of the wells subject to this Reimbursement Agreement, and shall not unreasonably or unnecessarily suspend continuous operations except with the consent of the SLC. Aera shall conduct its operations to ensure production at the “maximum efficient rate,” defined as the maximum sustainable daily oil or gas rate from a reservoir that will permit economic development and depletion of that reservoir without detriment to the ultimate recovery.

10. Aera shall defend, indemnify, and hold harmless the State Lands Commission, the members of the Bolsa Chica Wetlands Steering Committee, their respective Commissioners, Directors, officers, employees, contractors, agents, and assigns from and against any and all suits, liabilities, losses, damages, penalties, claims, costs, charges, and expenses, including all reasonable costs of defense and litigation (“Liabilities”) as follows:

A. Liabilities arising from any third party claim, including, but not limited to, working interest owners and/or royalty interest owners, for damages or compensation for the loss or delay of any portion of the production from wells impacted by the Project, or the loss or delay of revenue for which reimbursement and/or compensation is payable to Aera under this Reimbursement Agreement.

B. Consistent with paragraph 10 of the BSUA, Aera agrees to be solely responsible for its operations hereunder and agrees to indemnify and save the SLC harmless from any liability or damages which may result from its operations. SLC agrees to be solely responsible for its operations hereunder and agrees to indemnify and save Aera harmless from any liability or damages that may result from its operations.

11. Force Majeure. Neither party shall be responsible for losses or delays caused by force majeure events. Force majeure, for the purposes of this Reimbursement Agreement, is defined as any event arising from causes beyond the control of a Party, or one of its contractors, that delays or prevents the performance of any obligation under this Reimbursement Agreement despite that Party’s best efforts to fulfill that obligation, including, but not limited to, labor disputes, strikes, war, riots, insurrection, civil commotion, fire, flood, accident, storm or any act of God, delays in issuance of permits, or delays due to the presence of endangered species on the Site. “Best efforts to fulfill that obligation” includes using best efforts to anticipate any potential force majeure event and best efforts to address the effects of such an event both as it is occurring and after it has occurred, such that the delay is minimized to the greatest extent possible. Force majeure does not include financial inability to complete any required actions pursuant to this Reimbursement Agreement.

12. A. All notices or other communications between the Parties regarding this Reimbursement Agreement shall be in writing and shall be given in the manner set forth

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below, addressed to the Party to be served at the address set forth below, or at such other address for which that party may have given notice under the provisions of this paragraph. Any notice or other communication given by (a) overnight common carrier courier service shall be deemed to be given on the business day immediately following the date it was deposited with such common carrier which has been reasonably approved by the Parties (Federal Express, UPS, and DHL Worldwide Express being deemed approved by the Parties), postage prepaid; or (b) delivery in person or by messenger shall be deemed to have been given upon delivery in person or by messenger; or (c) fax shall be deemed given on the date sent or the next business day if not sent on a business day if a hard copy is thereafter delivered under (a) or (b) above.

To SLC:
Executive Officer
California State Lands Commission
100 Howe Avenue, Suite 100-South
Sacramento, CA 95825-8202

To Aera:
Aera Energy LLC
Attn: Vice President, Coastal Asset
P.O. Box 11164
Bakersfield, CA 93389-1164

Telecopier: (916) 574-1810

Telecopier: (661) 665-5973

B. To facilitate communication between Aera and SLC regarding reimbursement matters, the lead contact persons are:

Aera	SLC
Tony Devito	Jim Trout
(714) 969-3270	(916) 574-1396

C. To facilitate communication between Aera and FWS regarding design review and construction coordination matters, the lead contact persons are:

Aera Design Engineer	FWS Project Manager or
Don McElhaney	Jack Fancher
(714) 969-3349	(760) 431-9440 x215

13. This Reimbursement Agreement is binding upon, and shall inure to the benefit of, the Parties and their respective legal representatives, successors and assigns.

14. This Reimbursement Agreement may only be modified by mutual written consent of the Parties. This Agreement supplements but does not supersede or replace the OAA, the BSUA, the Agreement, or any other agreement between the Parties with respect to the subject matter hereof.

15. This Reimbursable Agreement will terminate when the work identified in Exhibits A, B, C and D has been completed and reimbursement has been made pursuant to this Reimbursement Agreement, or by mutual written consent of the Parties, or by SLC on 30 days written notice without any further obligation other than to pay for non-cancelable costs incurred prior to the date of notice to terminate and for services already provided, provided that the wells listed in Exhibit ___ are made physically accessible by a conventional workover rig by the termination date.

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16. This Reimbursement Agreement shall be governed by and construed in accordance with the laws of the State of California.

The Parties have executed this Reimbursement Agreement on the dates shown below.

California State Lands Commission,
for itself and in its capacity as Kapiloff
Land Bank Trustee

Aera Energy LLC

By: _____

By: _____

Its: _____

Its: _____

Date: _____

Date: _____