

MINUTE ITEM

This Calendar Item No. C78 was approved as
Minute Item No. 78 by the California State Lands
Commission by a vote of 3 to 0 at its
4-26-05 meeting.

CALENDAR ITEM

C78

A 1

S 2

04/26/05
PRC 8556.2
J. Adams

**CONSIDER APPROVAL OF THE AMENDMENT OF
STATE GEOTHERMAL RESOURCES LEASE NO. PRC 8556.2
TO PROVIDE FOR THE LEASING OF ADDITIONAL LANDS
AND THE DRILLING OF GEOTHERMAL WELLS,
THE GEYSERS GEOTHERMAL FIELD,
SONOMA AND MENDOCINO COUNTIES**

LESSEE:

Geysers Power Company, LLC
Attn: Mr. Kevin Talkington
10350 Socrates Mine Road
Middletown, CA 95461

AREA, LAND TYPE, AND LOCATION:

Approximately 1,881.43 acres of State 100 percent (100%) reserved mineral interest School Lands at The Geysers Geothermal Field, Sonoma and Mendocino Counties, as described in Exhibit A, attached hereto.

BACKGROUND:

State Geothermal Resources Lease No. PRC 8556.2 (Lease) was issued to WHR, Inc., owner of the surface estate, then assigned to Geysers Power Company, LLC (Lessee), both actions effective September 1, 2004. Lessee holds six of the State's seven geothermal leases at The Geysers. A related company, Silverado Geothermal Resources, Inc., holds the seventh lease. Both entities are wholly-owned subsidiaries of Calpine Corporation. The two subsidiaries utilize geothermal resources from State, Federal, and private leaseholds to generate approximately 1,000 megawatts of electricity. The seven State leases cover 6,635 acres and yield more than \$4 million per year in royalty and net profit revenue. Pursuant to Public Resources Code section 6217.5, revenue derived from State School Lands benefits the State Teachers' Retirement Fund.

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The Lease was granted for a primary term of seven (7) years, subject to the requirement that the Lessee commence drilling operations within the first three (3) years of the term in order to maintain the Lease in effect. The Lease presently includes 1,657.43 acres of State reserved mineral interest lands subdivided into three parcels, as shown on Exhibit B, attached hereto. The parcels are identified as Parcel 1, Parcel 2, and Parcel 3. The leased land was subdivided to prevent all three discontinuous tracts of land from being held beyond the primary term by virtue of a single commercial well on one tract. If any of the three Parcels is not producing, or is not capable of producing, at the end of the primary term, then the Lease expires with respect to that Parcel. As issued, the Lease authorizes the drilling of three exploratory wells, with any subsequent development drilling or utilization of geothermal resources subject to Commission approval.

ADJACENT STATE LANDS:

In addition to Parcels 1, 2, and 3 of the Lease, there is another tract of State reserved mineral interest land shown on Exhibit B, attached hereto. It is located immediately west of Parcel 2 and covers 224.00 acres. The State's mineral interest in the property is not currently under lease, although it was under lease twice during the last twenty-five years. Portions of the property were included in two former State leases issued in 1980 and 1982 following competitive bid lease sales. Both leases were quitclaimed in 1986 without being explored. The same lands were offered for lease again in 1993 through another competitive bid sale, but no bids were received. In 1994, the lands in the 224-acre tract were leased through negotiation as State Geothermal Resources Lease No. PRC 7810.2, a no surface occupancy lease that Lessee planned to develop to supplement geothermal resources on an adjacent private leasehold for use at its Aidlin Geothermal Power Plant. However, Lessee did not drill a well into Lease PRC 7810.2 until 2002. That well failed to encounter geothermal resources and was plugged. No other attempts were made to establish commercial production, so Lease PRC 7810.2 expired in 2004 at the end of its primary term.

APPLICATION FOR AMENDMENT:

Lessee has submitted an application to lease the 224 acres of State reserved mineral interest lands adjacent to Parcel 2 of the Lease by adding the lands as a "Parcel 4" to the Lease. Lessee's application also requests approval to drill into Parcel 4 from existing drill sites on adjacent private lands controlled by Lessee, and then utilize geothermal resources from the added lands at its Aidlin Power Plant.

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SURFACE OWNER RIGHTS:

Public Resources Code section 6912(a) provides that the owner of lands which have been sold by the State, subject to a reservation of the geothermal resources, shall be notified of any applications for a permit or lease covering those lands, and may, within four months from the date of service of such notice, file an application for a permit or lease. The code section further provides that if the surface owner files an application and is qualified to hold a lease, and if the Commission determines that the leasing of the lands is in the best interests of the State, the owner's application shall be granted, subject to all the provisions of Article 5.5 of the Public Resources Code.

WHR, Inc., owns the surface estate covering Parcels 1, 2, 3 of the Lease as well as Parcel 4, the lands proposed for addition to the Lease. Pursuant to Public Resources Code section 6912(a), Commission staff notified WHR, Inc., and supplied it with a copy of Lessee's application. WHR, Inc., responded that it would not exercise its right to submit an application.

JUSTIFICATION FOR A NEGOTIATED LEASE:

Adding State lands to an existing lease is, in effect, equivalent to issuing a new lease through negotiation. Public Resources Code section 6919 provides that the Commission may issue negotiated geothermal leases, in lieu of a competitive bid procedure, if any of the following conditions exist: (a) wells drilled upon private or public lands, including State-owned lands, are draining or may drain geothermal resources from State-owned lands; (b) the lands are determined to be unsuitable for competitive bidding because of such factors as their small size or irregular configuration, or their inaccessibility from surface drill sites reasonably available or obtainable; (c) the State owns a fractional interest in the lands; or (d) the lease or agreement is determined by the Commission to be in the best interests of the State.

Commission staff believe the first two of these conditions apply to the 224-acre parcel of State reserved mineral interest land, namely drainage and unsuitability due to size and accessibility limitations, and that leasing is in the best interest of the State. The bottom-hole locations of two or more producing geothermal wells associated with Lessee's Aidlin Power Plant are sufficiently close to the boundary of the parcel that drainage of geothermal resources may be occurring now or may occur in the future. Moreover, the parcel is considered too small, irregular, and lacking in accessibility to be developed by any company other than Lessee. Lessee holds lease rights on adjacent lands and surface access rights on the State's reserved mineral interest lands, and is the only company with a

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land position that affords access to the geothermal resources beneath the parcel. In addition, Lessee has existing facilities that could immediately utilize newly-developed geothermal resources. The leasing and subsequent development of the parcel will increase the revenue derived from State School Lands, and help achieve California's goal of increasing electrical generation from renewable sources. Therefore, Commission staff believe it is in the best interests of the State to enter into a negotiated geothermal resources lease with Lessee with respect to this 224-acre parcel through an amendment to the Lease.

AMENDMENT TERMS:

The amendment to State Geothermal Resources Lease No. PRC 8556.2 will contain the following terms and conditions:

1. The 224 acres of State reserved mineral interest lands described in Exhibit A, attached hereto, shall be added to the Land Description of the Lease and designated as Parcel 4.
2. The annual rent applicable to Parcel 4 shall be set at \$50.00 per acre until production is established from Parcel 4, whereupon it will be \$10.00 per acre, which is the rent applicable to Parcels 1, 2, and 3.
3. Lessee may drill wells into Parcel 4 from approved drill sites on adjacent non-State lands controlled by Lessee and may utilize geothermal resources from Parcel 4 at the Aidlin Power Plant in accordance with the terms and limitations of Sonoma County Use Permit 94-760.

All other material terms and conditions of the Lease will be unchanged.

STATUTORY AND OTHER REFERENCES:

- A. Public Resources Code sections: Division 6, Parts 1 and 2; Division 13.
- B. California Code of Regulations, sections: Title 2, Division 3; Title 14.

OTHER PERTINENT INFORMATION:

1. A Mitigated Negative Declaration was prepared and adopted for this project by the Sonoma County Permit and Resource Management Department. The California State Lands Commission's staff has reviewed such document.
2. A Mitigation Monitoring Program was not adopted by the Sonoma County Permit and Resource Management Department.

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3. This activity involves land which have NOT been identified as possessing significant environmental values pursuant to Public Resources Code sections 6370, et seq. However, the Commission has declared that all state school lands and submerged lands are "significant" by nature of their public ownership (as opposed to "environmentally significant"). Since such declaration of significance is not based upon the requirements and criteria of Public Resources Code sections 6370, et seq., use classifications for such lands have not been designated. Therefore, the finding of the project's consistency with the use classification as required by Title 2, California Code of Regulations, section 2954 is not applicable.

EXHIBITS:

- A. Land Description
- B. Location Map

PERMIT STREAMLINING ACT DEADLINE:

August 9, 2005

RECOMMENDED ACTION:

IT IS RECOMMENDED THAT THE COMMISSION:

CEQA FINDING:

1. FIND THAT A MITIGATED NEGATIVE DECLARATION WAS PREPARED AND ADOPTED FOR THIS PROJECT BY THE SONOMA COUNTY PERMIT AND RESOURCE MANAGEMENT DEPARTMENT AND THAT THE COMMISSION HAS REVIEWED AND CONSIDERED THE INFORMATION CONTAINED THEREIN.

OTHER FINDINGS:

1. FIND THAT CONDITIONS EXIST FOR THE ISSUANCE OF A NEGOTIATED GEOTHERMAL RESOURCES LEASE PURSUANT TO PUBLIC RESOURCES CODE SECTION 6919(a), IN THAT GEOTHERMAL RESOURCES ARE BEING DRAINED OR MAY BE DRAINED FROM THE LEASED LANDS, AND SECTION 6919(b), IN THAT LIMITATIONS DUE TO SIZE, CONFIGURATION, AND ACCESSIBILITY MAKE THE LANDS UNSUITABLE FOR COMPETITIVE BIDDING.

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2. FIND THAT A NEGOTIATED GEOTHERMAL RESOURCES LEASE PURSUANT TO PUBLIC RESOURCES CODE SECTION 6919(d) IS IN THE BEST INTERESTS OF THE STATE

AUTHORIZATION:

1. AUTHORIZE THE AMENDMENT OF STATE GEOTHERMAL RESOURCES LEASE NO. PRC 8556.2 UPON THE TERMS AND CONDITIONS OUTLINED IN THIS CALENDAR ITEM AND IN FORM ON FILE IN THE OFFICES OF THE COMMISSION, THE AMENDMENT TO PROVIDE FOR: 1) THE LEASING OF AN ADDITIONAL 224.00 ACRES, MORE OR LESS, DESCRIBED IN EXHIBIT A, ATTACHED HERETO; AND 2) APPROVAL OF THE DRILLING OF GEOTHERMAL WELLS INTO PARCEL 4 FROM APPROVED DRILL SITES ON ADJACENT NON-STATE LANDS CONTROLLED BY LESSEE.
2. AUTHORIZE THE EXECUTIVE OFFICER OR HIS DESIGNEE TO EXECUTE ANY DOCUMENTS NECESSARY TO IMPLEMENT THE COMMISSION'S ACTION.

EXHIBIT A

PRC 8556.2

LAND DESCRIPTION

LANDS ORIGINALLY INCLUDED:

Parcel 1: Lots 1, 2, 3, 4, 5, 6, 7, 8, 11, and 12 of Section 1, Township 11 North, Range 9 West, Mount Diablo Base and Meridian, Sonoma County, containing 394.46 acres, more or less; and Lot 8 of Section 2, Township 11 North, Range 9 West, Mount Diablo Base and Meridian, Sonoma County, containing 39.70 acres, more or less.

Parcel 2: Lots 4, 6, and 11 of Section 2, Township 11 North, Range 9 West, Mount Diablo Base and Meridian, Sonoma County, containing 119.18 acres, more or less; and Lots 1, 2, 3, 4, and 5, the Southeast Quarter, the South Half of the Northeast Quarter, the Northwest Quarter of the Northwest Quarter, the South Half of the Northwest Quarter, and the East Half of the Southwest Quarter of Section 3, Township 11 North, Range 9 West, Mount Diablo Base and Meridian, Sonoma County, containing 624.09 acres, more or less;

Parcel 3: The South Half of the South Half of Section 26, Township 12 North, Range 9 West, Mount Diablo Base and Meridian, Mendocino County, containing 160.00 acres, more or less; and the South Half of the Southeast Quarter of Section 27, Township 12 North, Range 9 West, Mount Diablo Base and Meridian, Mendocino County, containing 80.00 acres, more or less; and the Northeast Quarter of the Northeast Quarter and the Northeast Quarter of the Southeast Quarter of Section 34, Township 12 North, Range 9 West, Mount Diablo Base and Meridian, Sonoma County, containing 80.00 acres, more or less; and the North Half of the North Half of Section 35, Township 12 North, Range 9 West, Mount Diablo Base and Meridian, Sonoma County, containing 160.00 acres, more or less.

LANDS TO BE ADDED THROUGH AMENDMENT:

Parcel 4: Lots 6, 7, 8, and 9, and the Southeast Quarter of the Northeast Quarter, and the North Half of the Northeast Quarter, all in Section 4, Township 11 North, Range 9 West, Mount Diablo Base and Meridian, Sonoma County, containing 224.00 acres, more or less, based upon the Mitchell & Heryford Record of Survey filed in the office of the County Recorder, County of Sonoma, on March 2, 1991, in Book 470 of Maps at Pages 37 and 38, and the Mitchell & Heryford acreage compilation map on May 13, 1994 on file in the office of the State Lands Commission.

Total acreage in Parcels 1, 2, 3, and 4 is 1,881.43 acres, more or less.

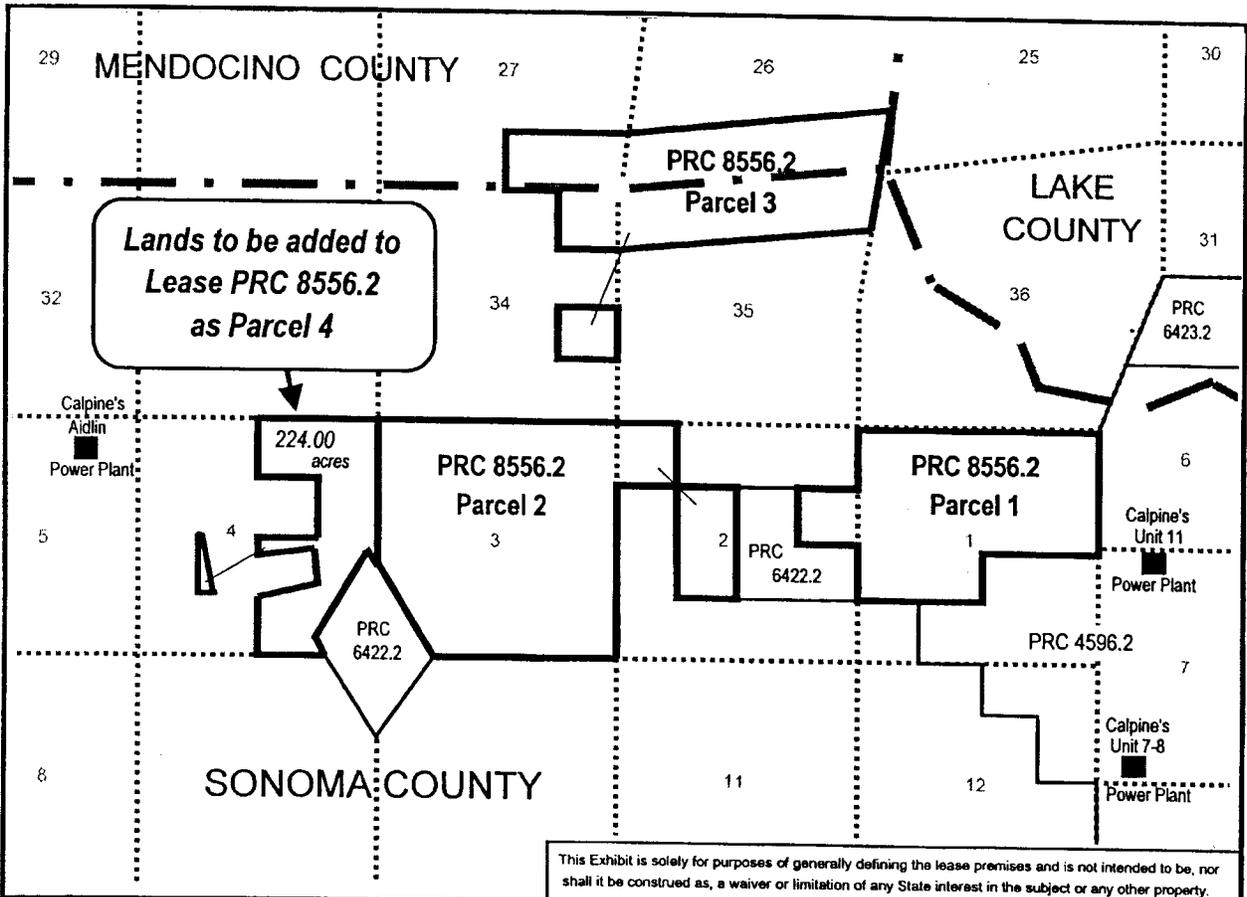
END OF DESCRIPTION

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CALENDAR PAGE

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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.

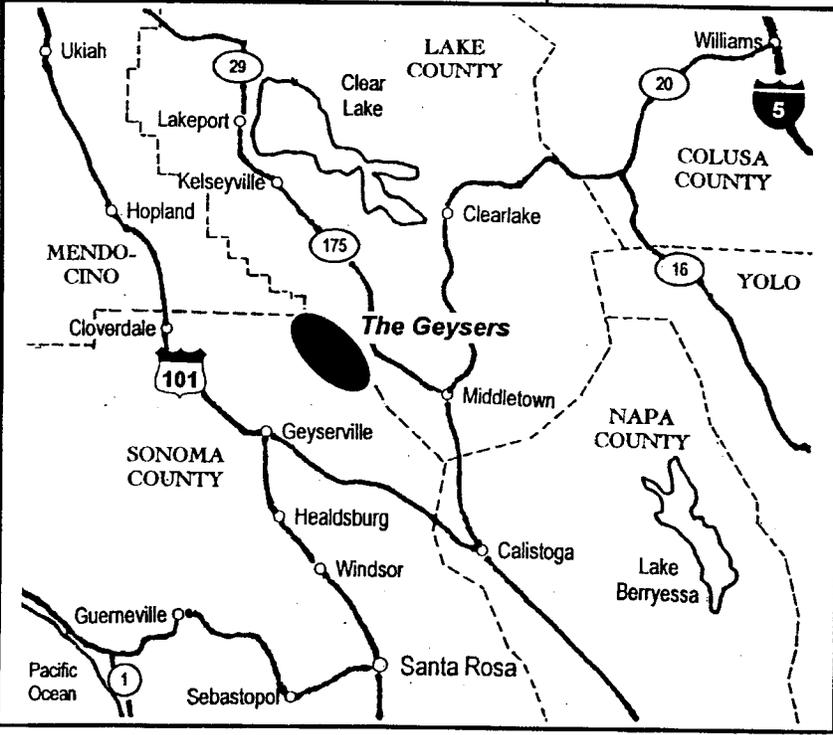


EXHIBIT B
PRC 8556.2

LOCATION MAP
The Geysers Geothermal Field
SONOMA, LAKE, and
MENDOCINO COUNTIES

JWA, 2004

