

MINUTE ITEM

This Calendar Item No. C22 was approved as Minute Item No. 22 by the California State Lands Commission by a vote of 3 to 0 at its 02-09-06 meeting.

CALENDAR ITEM
C22

A 33
S 15

02/09/06
PRC 1390.1
J. Brown

GENERAL LEASE - INDUSTRIAL USE AND CONDITIONAL ASSIGNMENT

APPLICANTS:

Duke Energy Morro Bay LLC
1290 Embarcadero Road
Morro Bay, CA 93442

LS Power Generation, LLC
Two Tower Center, 11th Floor
East Brunswick, NJ 08816

AREA, LAND TYPE, AND LOCATION:

5.23 acres, more or less, of sovereign lands in the Pacific Ocean, Estero Bay, San Luis Obispo County.

AUTHORIZED USE:

Continued maintenance of existing offshore marine terminal facilities in caretaker status.

LEASE TERM:

Two years, beginning February 2, 2006.

CONSIDERATION:

\$14,570 per year with the State reserving the right to fix a different rent periodically during the lease term, as provided in the lease.

SPECIFIC LEASE PROVISIONS:

Insurance:

Liability insurance in the amount of \$1,000,000 per occurrence for bodily injury and \$5,000,000 for property damage.

Financial Security in a form approved by staff:

\$5,000,000

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Operation:

The existing facilities may not be operated as a marine terminal as defined under Public Resources Code section 8750.

Assignment:

Conditional assignment to LS Power Generation, LLC under the following conditions:

- a) close of the sale and transfer of Duke Energy Morro Bay LLC to LS Power Generation, LLC, on or before June 1, 2006; and,
- b) receipt of an unconditional Guaranty from LS Power Generation, LLC, as surety for performance of all obligations under the lease.

Guaranty:

LS Power Generation, LLC, to provide an unconditional guaranty of DEMB's faithful performance of all the terms, covenants and obligations under lease PRC 1390.1.

OTHER PERTINENT INFORMATION:

1. Applicant owns or has the right to use the uplands adjoining the lease premises.
2. The original 49-year lease (Lease PRC 1390.1) for the offshore marine terminal facilities was issued to Pacific Gas and Electric Company (PG&E) effective May 26, 1954. The marine terminal facilities were constructed to transfer fuel oil from vessels to onshore tanks for use at the upland Morro Bay Power Plant. The offshore marine terminal and a portion of the pipelines extending from the terminal are located on ungranted sovereign lands under the Commission's jurisdiction. The pipelines continue across sovereign lands that have been legislatively granted to the city of Morro Bay, pursuant to Chapter 1076, Statutes of 1947.
3. In the early 1990s, the power plant was converted to natural gas fuel. Some of the facilities appurtenant to the marine terminal were removed, the pipelines were cleaned, and the marine terminal was officially placed in caretaker status, which status remains today.
4. In 1998, the Commission authorized the assignment of Lease PRC 1390.1 from PG&E to the Duke Energy Morro Bay LLC, (DEMB) in conjunction with its acquisition of the Morro Bay Power Plant.
5. The marine terminal has been subject to review of cathodic protection reports by staff of the Commission's Marine Facilities Division.

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6. The original 49-year lease expired on May 25, 2003, and was in holdover status until February 2, 2004, when the Commission authorized a two-year lease to allow DEMB to continue to maintain the remaining marine terminal facilities in caretaker status and to evaluate options and develop a plan for the future use or disposition of the remaining facilities.
7. On October 1, 2004, DEMB submitted an application to consider the decommissioning of the remaining marine terminal improvements. The Commission is the lead agency for CEQA and is in the process of preparing an environmental document for the final disposition of the remaining marine terminal facilities. There is no restriction on public use of the water area over the existing facilities.
8. On February 1, 2006, Lease PRC 1390.1 expired. The Applicants have submitted an application for issuance of a new lease for a term that will allow for completion of the environmental documentation regarding the disposition of the remaining facilities, which is presently scheduled for the fall of 2006.
9. As a condition of the Lease, DEMB will provide a Letter of Credit or similar financial security of no less than \$5,000,000 as a surety for performance of all obligations under Lease PRC 1390.1.
10. LS Power Generation, LLC (LSPG) has signed an agreement with Duke Energy Corporation to purchase certain Duke assets, including DEMB. The lease is the subject of a proposed change of ownership, which will result from the purchase of the assets of Duke Energy Morro Bay LLC, a subsidiary of Duke Energy Corporation, by LS Power Generation, LLC. Under the terms of the proposed lease with DEMB, the purchase by LSPG is considered an assignment of the lease because it will result in a transfer of controlling interest. However, once the purchase has been completed, DEMB will remain the State's lessee.
11. Upon completion of the purchase transaction, anticipated to be late March 2006, LSPG would hold a controlling interest in DEMB. The proposed issuance of Lease PRC 1390.1 includes special conditions that will be required as a condition of the assignment of PRC 1390.1 to LS Power Generation, LLC. The conditions are: a) close of the sale and transfer of Duke Energy Morro Bay LLC to LS Power Generation, LLC, on or before

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June 1, 2006; and, b) receipt of an unconditional Guaranty from LS Power Generation, LLC, as surety for performance of all obligations under the lease.

12. DEMB will remain responsible and liable, after close of the purchase transaction, for all existing marine terminal improvements, including, but not limited to, removal (as determined through the CEQA process and subsequent Commission consideration), and environmental and public safety liability arising from removal/abandonment of such marine terminal improvements.
13. Pursuant to the Commission's delegation of authority and the State CEQA Guidelines (Title 14, California Code of Regulations, section 15061), the staff has determined that this activity is exempt from the requirements of the CEQA as a categorically exempt project. The project is exempt under Class 1, Existing Facilities; Title 2, California Code of Regulations, section 2905 (a)(2).

Authority: Public Resources Code section 21084 and Title 14, California Code of Regulations, section 15300 and Title 2, California Code of Regulations, section 2905.

14. This activity involves lands identified as possessing significant environmental values pursuant to Public Resources Code sections 6370, et seq. Based upon the staff's consultation with the persons nominating such lands and through the CEQA review process, it is the staff's opinion that the project, as proposed, is consistent with its use classification.

EXHIBITS:

- A. Location and Site Map
- B. Land Description

RECOMMENDED ACTION:

IT IS RECOMMENDED THAT THE COMMISSION:

CEQA FINDING:

FIND THAT THE ACTIVITY IS EXEMPT FROM THE REQUIREMENTS OF THE CEQA PURSUANT TO TITLE 14, CALIFORNIA CODE OF REGULATIONS, SECTION 15061 AS A CATEGORICALLY EXEMPT

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PROJECT, CLASS 1, EXISTING FACILITIES; TITLE 2, CALIFORNIA CODE OF REGULATIONS, SECTION 2905 (a)(2).

SIGNIFICANT LANDS INVENTORY FINDING:

FIND THAT THIS ACTIVITY IS CONSISTENT WITH THE USE CLASSIFICATION DESIGNATED BY THE COMMISSION FOR THE LAND PURSUANT TO PUBLIC RESOURCES CODE SECTIONS 6370, ET SEQ.

AUTHORIZATION:

1. AUTHORIZE ISSUANCE TO DUKE ENERGY MORRO BAY LLC OF A GENERAL LEASE - INDUSTRIAL USE, BEGINNING FEBRUARY 2, 2006, FOR A TERM OF TWO YEARS, FOR CONTINUED MAINTENANCE OF THE OFFSHORE MARINE TERMINAL FACILITIES IN CARETAKER STATUS ON THE LAND DESCRIBED ON EXHIBIT B ATTACHED AND BY THIS REFERENCE MADE A PART HEREOF; ANNUAL RENT IN THE AMOUNT OF \$14,570, WITH THE STATE RESERVING THE RIGHT TO FIX A DIFFERENT RENT PERIODICALLY DURING THE LEASE TERM, AS PROVIDED IN THE LEASE; FINANCIAL SECURITY IN THE AMOUNT OF \$5,000,000 IN A FORM APPROVED BY STAFF; LIABILITY INSURANCE IN THE AMOUNT OF \$1,000,000 PER OCCURRENCE FOR BODILY INJURY AND \$5,000,000 FOR PROPERTY DAMAGE.

2. AUTHORIZE THE CONDITIONAL ASSIGNMENT OF LEASE NO. PRC 1390.1, A GENERAL LEASE - INDUSTRIAL USE OF SOVEREIGN LANDS AS SHOWN ON EXHIBIT A ATTACHED AND BY THIS REFERENCE MADE A PART HEREOF, FROM DUKE ENERGY MORRO BAY LLC TO LS POWER GENERATION, LLC; SUCH AUTHORIZATION TO BE EFFECTIVE UPON THE TIMELY OCCURANCE OF THE FOLLOWING CONDITIONS:
 - A. THE CLOSING OF THE SALE AND TRANSFER OF DUKE ENERGY MORRO BAY LLC TO LS POWER GENERATION, LLC, ON OR BEFORE JUNE 1, 2006.

 - B. RECEIPT OF AN UNCONDITIONAL GUARANTEE FROM LS POWER GENERATION, LLC.

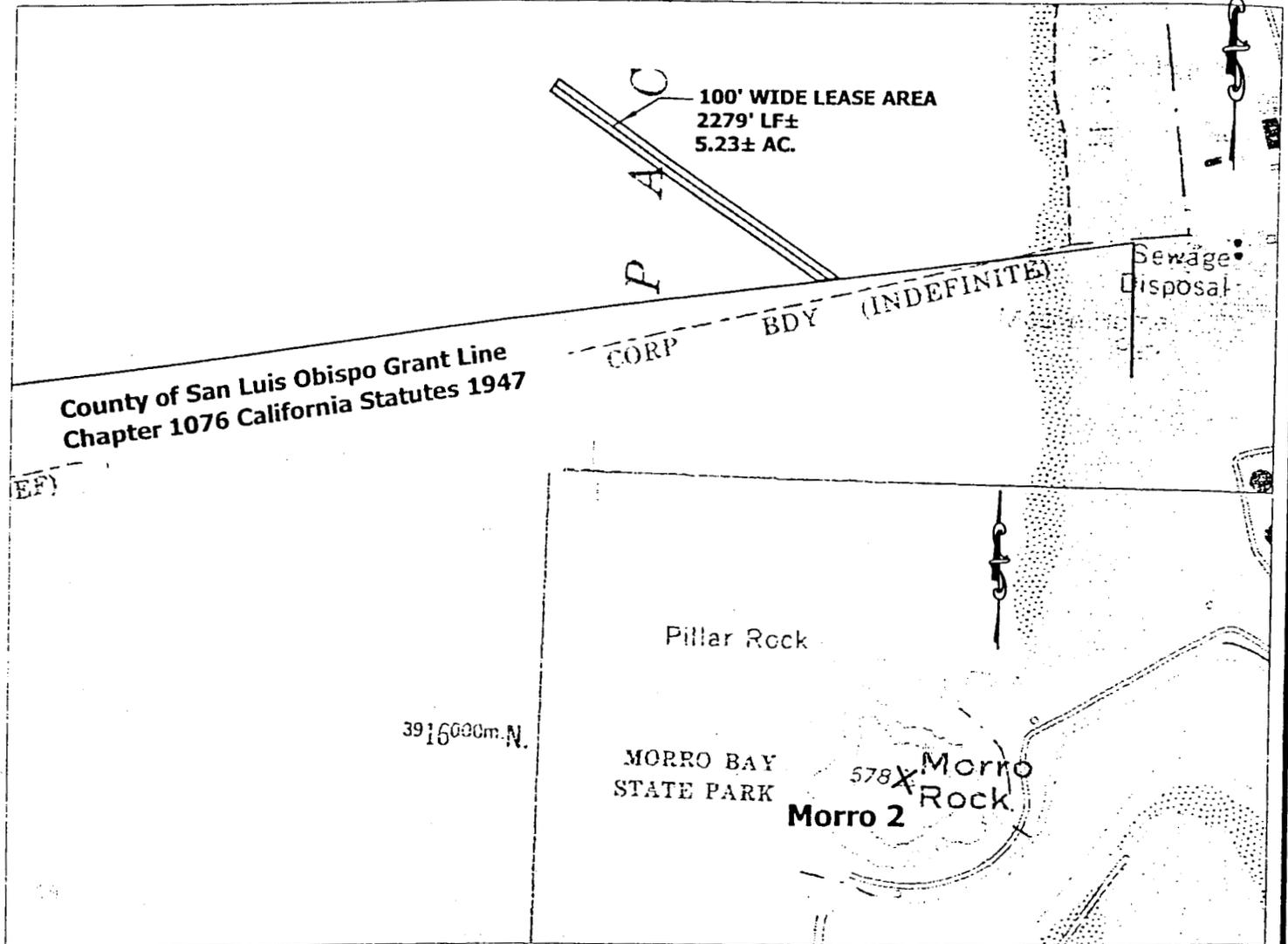
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PROVIDED HOWEVER, THE EXECUTIVE OFFICER, IN HIS SOLE DISCRETION, MAY EXTEND THE DEADLINE FOR FULFILLING EITHER OF THE CONDITIONS SET FORTH IN PARAGRAPHS A AND B ABOVE BY A PERIOD NOT TO EXCEED 60 DAYS UPON A SHOWING THAT THE AFFECTED CONDITON WILL LIKELY BE FULFILLED WITHIN THE PERIOD OF THE EXTENSION.

FAILURE OF EITHER OF THE FOREGOING CONDITIONS TO OCCUR WITHIN THE TIMEFRAME PROVIDED ABOVE SHALL RENDER THE AUTHORIZATION TO ASSIGN GRANTED BY THE COMMISSION'S ACTION IN THIS MATTER TO BE OF NO FORCE AND EFFECT.

NO SCALE

SITE



DUKE ENERGY MORRO BAY LLC

NO SCALE

LOCATION

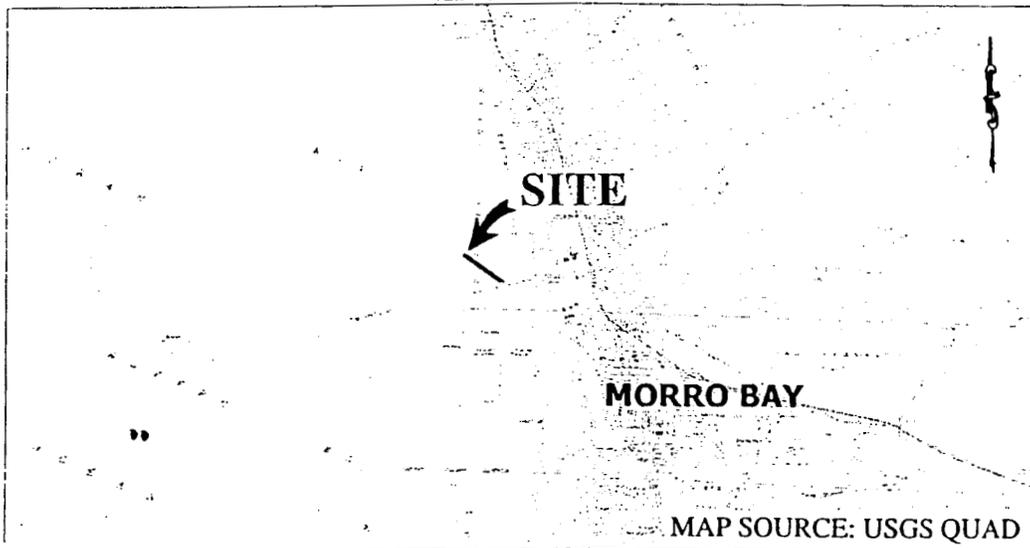


Exhibit A

WP 1390
 Duke Energy Morro Bay LLC
 INDUSTRIAL USE
 ESTERO BAY
 SAN LUIS OBISPO CO.



This Exhibit is solely for purposes of generally defining the lease premises, is based on unverified information provided by the Lessee or other parties 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"**LAND DESCRIPTION**

A strip of submerged land 100 feet wide, in the bed of Estero Bay, County of San Luis Obispo, California, said strip laying 50 feet on each side of the following described centerline:

BEGINNING at a point from which the U.S.C. & G.S. triangulation station "Morro 2", having California Coordinate System 1927, Zone 5 coordinates of $X=1,145,458.88$ and $Y=692,530.27$, bears South $27^{\circ}44'05''$ East, 5272.99 feet; thence South $55^{\circ}42'58''$ East, 2279.37 feet to a point in the northerly boundary line of the Grant to the County of San Luis Obispo as described in Chapter 1076, California Statutes 1947, amended by Statutes 1957 Chapter 1874, and as shown on the map recorded in Book 1 of Misc. Maps at page 2, San Luis Obispo County Records; the side lines of said strip of land shall be lengthened or shortened at the southeasterly termini thereof so as to terminate in said northerly boundary line.

END OF DESCRIPTION

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