EXHIBIT B

PRC 2839.1
E-412.1

Replacement Lease for

GAS STORAGE LEASE PRC 2839.1

MCDONALD ISLAND GAS FIELD

San Joaquin County, California

THIS LEASE is made and entered into on _____, by and between the STATE OF CALIFORNIA, acting through the STATE LANDS COMMISSION, hereafter sometimes referred to as the "STATE" and PACIFIC GAS AND ELECTRIC COMPANY, a corporation organized and existing under the laws of the State of California, hereafter sometimes referred to as the "COMPANY."

W I T N E S S E T H:

WHEREAS, for the purposes of this Lease the following terms shall have the following meanings:

McDonald Island Gas Field: That certain gas field located in Sections 19, 30, 31 and 32, Township 2 North, Range 5 East, MDB&M, and Sections 23, 24, 25, 26 and 36, Township 2 North, Range 4 East, MDB&M, County of San Joaquin, State of California.

McDonald Island Sand: Those certain gas sands in the McDonald Island Gas Field shown by the electric log of well "Weyl-Zuckerman" No. 2, within the interval between the measured depth of 5,160 feet, which depth is 75 feet above the main sand body, and measured depth of 5,390 feet, which is the top of a shale section.

1 Storage Reservoir: That portion of the McDonald Island Sand in the McDonald
2 Island Gas Field shown on the attached map marked Exhibit "A."
3 Native Gas: Natural or other gaseous hydrocarbons present in the McDonald
4 Island Sand on March 16, 1958, when the average static surface pressure of
5 wells completed in the Storage Reservoir was 459 p.s.i.g. and prior to the
6 commencement of injection by the Company of gas produced from other lands.
7 WHEREAS, commencing in 1935, Standard Oil Company of California entered
8 into certain oil and gas leases of lands in the McDonald Island Gas Field, acquired
9 mineral interests in these lands and entered upon these lands and explored for,
10 discovered and developed natural gas.
11 WHEREAS, by agreement dated March 1, 1940, the State entered into
12 Compensatory Agreement Easement 412.1 with Standard Oil Company of California for
13 the payment of compensation to the State for drainage of State lands by gas produced
14 from wells drilled in the McDonald Island Gas Field.
15 WHEREAS, Standard Oil Company of California assigned its interests under
16 Compensatory Agreement Easement 412.1 dated March 1, 1940, as amended by an
17 agreement effective June 1, 1950, to the Natural Gas Corporation of California on
18 January 29, 1959, and then the Natural Gas Corporation of California assigned these
19 interests to Pacific Gas and Electric Company on March 17, 1960.
20 WHEREAS, it was the purpose of the Company in acquiring the mineral interests
21 to convert a part of the McDonald Island Gas Field to a facility for the underground
22 storage of gas.

1 WHEREAS, the Company paid the State on March 29, 1962, the lump sum of
2 $127,420.74 as full compensation for the State's share of the Native Gas.
3 WHEREAS, the State approved Gas Storage Lease PRC 2839.1 McDonald
4 Island Gas Field dated January 25, 1962, for a fifteen (15) year period commencing
5 March 1, 1962 and ending March 1, 1977. This lease provided the Company with a
6 preferential right of renewal for two successive periods of 15 years each upon
7 reasonable terms and conditions as prescribed by the State. The first lease renewal
8 period was from March 1, 1977 to March 1, 1992. The second lease renewal period
9 was from March 1, 1992 to March 1, 2007. Beginning September 1, 1995, the parties
10 modified the State's ownership share of the Storage Reservoir from 12.193% to 9.6%.
11 WHEREAS, the second lease renewal provided the Company with the right to
12 renew the lease for a third 15-year period from March 1, 2007 to March 1, 2022.
13 However, Title 2, California Code of Regulations, Section 2004 limits the terms for
14 general leases and permits, including any optional renewal periods, to no longer than
15 necessary to accomplish the intended use or purpose, and not to exceed forty-nine (49)
16 years. In accordance with this provision, the third renewal of Gas Storage Lease PRC
17 2839.1 would have to expire by law at 7:00 a.m. on March 1, 2011.
18 NOW, THEREFORE, in consideration of the mutual covenants and agreements
19 herein set forth, the parties agree as follows:
20 1. The Company has purchased and paid for all Native Gas in the McDonald
21 Island Gas Field and has the right at any time to extract, produce, remove, market, use
22 or dispose of native gas in the McDonald Island Sand free of any claim or demand by
23 the State.

1 2. The Company shall have the exclusive right during the term of this Lease
2 to inject and store gas (with any water vapors absorbed), whether produced from
3 State's lands or from other lands, in and withdraw such injected gas (with any water
4 vapors absorbed) from the Storage Reservoir, together with the right to select, subject
5 to the approval of the State as to location, and to use without charge all necessary
6 rights of way and easements required by the Company for operation of the Storage
7 Reservoir, with the right of ingress and egress, over any and all property owned or
8 controlled by the State in the McDonald Island Gas Field lying within the productive
9 limits line shown on Exhibit "A." All rights of way and easements through the State's
10 lands granted to the Company shall be under such regulations as to location,
11 application and use as may be prescribed by the State.
12 3. The State reserves from the operation of this Lease all crude oil, natural
13 gasoline and other liquid hydrocarbons and natural gas other than gas in the McDonald
14 Island Sand in any of the State's lands. These substances shall remain the sole
15 property of the State, and no rights to them are granted to the Company by this Lease.
16 The State further reserves the right to grant easements or rights of way in, upon and
17 under the State lands. Nothing in this Lease shall be construed as limiting the power of
18 the State to lease, convey or otherwise transfer or encumber any or all of the State
19 lands for any purpose that will not interfere with the rights or privileges granted to the
20 Company by this Lease.
21 4. The Company shall pay to the State the higher of (1) an annual rental **or**
22 (2) an incremental gas fee on all gas injected into the State's ownership share of the
23 Storage Reservoir (specified in Paragraph 5 of this Lease) 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 this Lease with the right to exercise any legal or equitable remedy that the State might otherwise have.

(a) The annual rental shall be based on the State's ownership share of the Storage Reservoir (specified in Paragraph 5 of this Lease). Beginning March 1, 2007, the annual rental shall be $289,240.19 and shall be increased each year by five percent (5%) of the previous year's annual rental. The annual rental shall be due and payable in advance by March 1 of each year.

(b) The incremental gas fee shall be based on the total gas injected for storage (Mcf) into the State's ownership share of the Storage Reservoir (specified in Paragraph 5 of this Lease) during the lease year (March through February). Beginning March 1, 2007, the incremental gas fee factor shall be $0.08646 per Mcf and shall be increased each year by five percent (5%) of the previous year's incremental gas fee factor as listed on Exhibit "B" (Incremental Gas Fee Factor Schedule). By April 25 of each year, the Company shall submit to the State a written statement showing the total gas injected for storage (Mcf) for the immediately preceding lease year. The Company shall pay to the State on the date of the submission of the written statement, 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 written statement. The records and accounts of the Company

supporting the written statement shall be subject to audit by the State at all reasonable times.

(c) All late rental and incremental gas fee payments are subject to interest and penalty charges as specified in Title 2, California Code of Regulations, Section 1911.

5. 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" to this Lease 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 agreed to by the State and the Company.

6. All equipment, devices and materials required to measure the volume of gas injected into and withdrawn from the Storage Reservoir shall be installed, maintained, operated or furnished by the Company at the Company's expense. The unit of volume for purposes of measurement shall be one (1) cubic foot of gas at a temperature of sixty degrees (60°) Fahrenheit and at the pressure of fourteen and seventy-three one-hundredths (14.73) pounds per square inch absolute. The volumes of gas injected into the Storage Reservoir and withdrawn from the Storage Reservoir shall be metered by one or more ultrasonic meters installed and maintained, and

volumes shall be measured in accordance with the methods prescribed in American Gas Association (AGA) Report No. 9 Measurement of Gas by Multipath Ultrasonic Meters (2007) and any subsequent revision acceptable to the Company. Flow computer calculations shall be governed by the equations described in AGA Report No. 7, Measurement of Natural Gas by Turbine Meters (2006). To determine gas energy content and factors for deviation from perfect gas laws a state approved gas chromatograph shall make quantitative analysis of the gas at reasonable intervals. The State by its duly authorized representative shall have the right to check and inspect measuring equipment installed or furnished by the Company and measurement data at all times during business hours, but the reading, calibration and adjustment of such equipment and collecting of data shall be done only by the Company. A Company representative shall be present when any such check or inspection is made by the State.

7. The Company shall pay when due any and all taxes lawfully assessed and levied under the laws of the United States of America, the State of California or any of its political subdivisions, upon improvements installed or maintained on, or gas or other hydrocarbon substances injected into or produced from State lands in, the McDonald Island Gas Field pursuant to the provisions of this Lease.

8. At the time of execution of this Lease, the Company shall furnish to the State and throughout the term of this Lease maintain a good and sufficient bond in the amount of Fifty Thousand Dollars ($50,000.00) in favor of the State guaranteeing faithful performance by the Company of the terms, covenants and conditions of this Lease.

9. The Company shall not assign this Lease without the prior written consent of the State.

10. The Company shall exercise reasonable diligence in the operation of the lands used as a Storage Reservoir for natural gas and carry on all operations under this Lease in a good and worker-like manner in accordance with approved methods, having due regard for the health and safety of workers and employees. The Company shall hold the State, its officers, agents and employees, at all times, free and harmless from all claims and liabilities on account of any negligent maintenance or operation on the part of the Company or its officers, agents or employees.

11. This Lease may be terminated and any provisions of it may be modified or amended by written agreement of the parties.

12. If the Company assigns this Lease without the consent of the State, fails to comply with the applicable provisions of Division 6 of the Public Resources Code, or defaults in the performance or observance of any of the terms, covenants and conditions of this Lease or of any applicable rules and regulations, now or hereafter promulgated by the State, or any agency having jurisdiction over the activities under this Lease, and such default continues for at least thirty (30) days after written notice to the Company and no steps shall have been taken within that time to remedy the default, then State shall have the right to cancel this Lease, provided that any termination for failure to pay any adjusted rate and/or minimum annual rental shall be governed by the provisions of paragraph 4 of this Lease. This provision shall not be construed to prevent the exercise by the State of any legal or equitable remedy which the State might otherwise have. The waiver or failure of the State to act upon any particular violation

1 shall not prevent the termination of this Lease for any other cause or for the same cause
2 occurring at another time.
3 13. This Lease shall be effective at 7:00 a.m. on March 1, 2007, and shall
4 continue in effect for a term of fifteen (15) years until 7:00 a.m. on March 1, 2022. The
5 Company shall have the right to renew the Lease for two (2) successive terms of fifteen
6 (15) years each upon such reasonable terms and conditions as may be prescribed by
7 the State, unless applicable law in effect at the time of the expiration of the Lease
8 prevents such renewal. If this Lease is terminated pursuant to the provisions of
9 Paragraphs 4, 11 or 12 of this Lease, the Company shall have the right for a period of
10 five (5) years after any such termination to withdraw from the Storage Reservoir all gas
11 injected by the Company and all Native Gas. If the Company exercises this right, it
12 shall continue to be responsible for payment to the State of the higher of the annual
13 rental or incremental gas fee through the end of the lease year in which the Lease is
14 terminated. While the Lease is in effect, including any extension or renewal of the
15 Lease, the State shall not drill or produce or permit others to drill or produce any well for
16 the production of gas within any zones and horizons of the McDonald Island Gas Field.
17 14. Within sixty (60) days after full execution of this Lease, the Company shall
18 provide to the State a quitclaim of all of its rights in Compensatory Agreement
19 Easement 412.1 issued March 1, 1940, as amended by an agreement effective June 1,
20 1950. The acceptance of this quitclaim by the State shall constitute a termination of
21 Compensatory Agreement Easement 412.1 pursuant to paragraph 15 of that
22 Agreement.

15. The address of each party for the purpose of service of notices provided under this Lease, until changed by either party by written notice to the other, is:

Pacific Gas and Electric Company	**State Lands Commission**
77 Beale Street, Room 1612	200 Oceangate 12th Floor
San Francisco CA 94105	Long Beach CA 90802-4331

With a copy to:

Manager, Land Asset Management
PG&E Technical and Land Services
P.O. Box 770000, Mail Code N10A
San Francisco, CA 94177

IN WITNESS WHEREOF, the parties have executed, or caused this Lease to be executed, by their duly authorized officers. This Lease shall be effective March 1, 2007.

Pacific Gas and Electric Company	**State Lands Commission**
By:	By:
Name: Richard A. Gigliotti	Name:
Title: Manager, Land Energy Delivery, T&LS	Title:
Date: 11.07.08	Date:

All signatures must be acknowledged.

ACKNOWLEDGMENT

State of California
County of San Francisco)

On November 7, 2008 before me, Jennifer Ann LesCallett, Notary Public
(insert name and title of the officer)

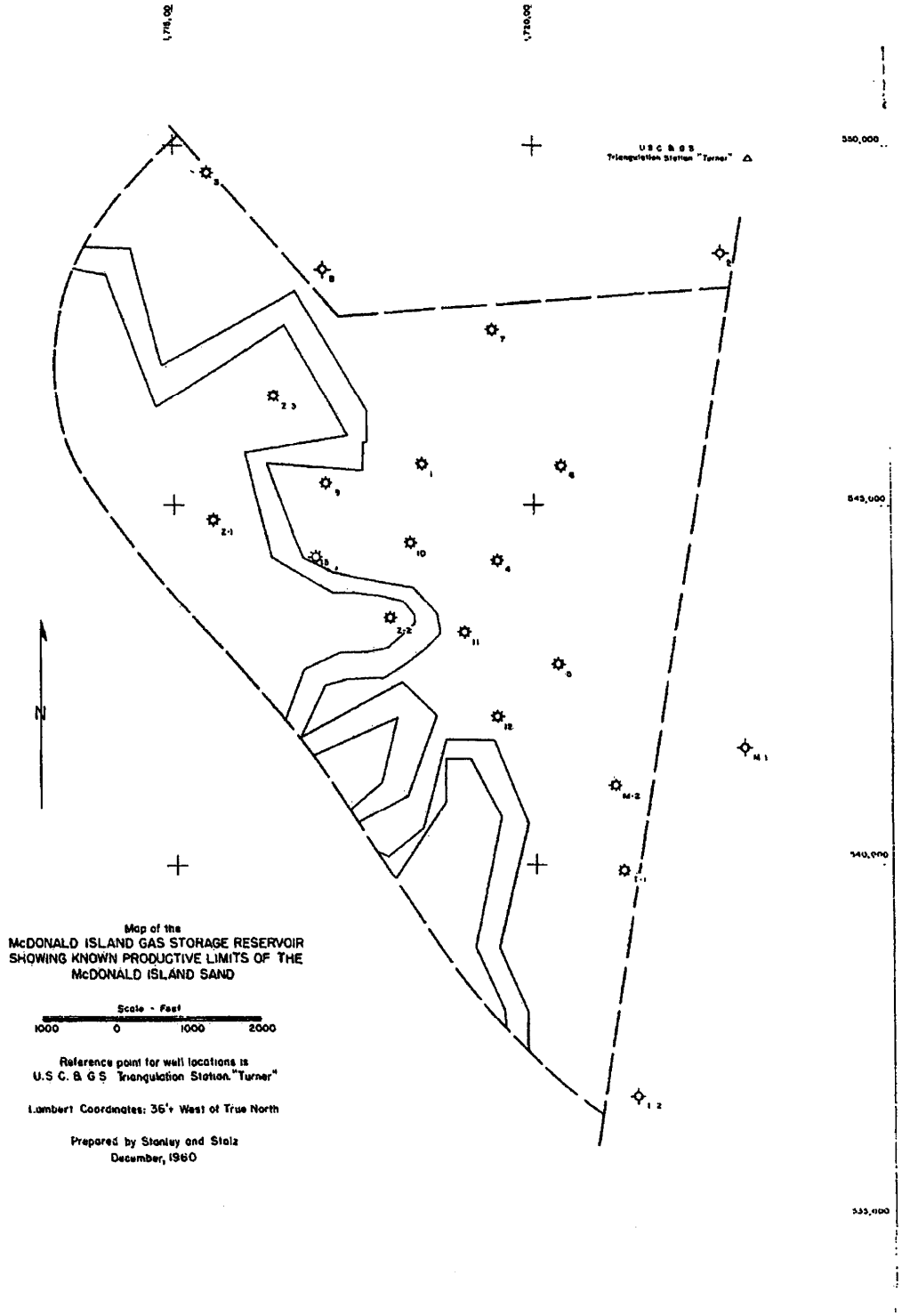
personally appeared Richard A. Gigliotti,
who proved to me on the basis of satisfactory evidence to be the person(s) whose name(s) is/are subscribed to the within instrument and acknowledged to me that he/she/they executed the same in his/her/their authorized capacity(ies), and that by his/her/their signature(s) on the instrument the person(s), or the entity upon behalf of which the person(s) acted, executed the instrument.

I certify under PENALTY OF PERJURY under the laws of the State of California that the foregoing paragraph is true and correct.

WITNESS my hand and official seal.

JENNIFER ANN LESCALLETT
COMM. #1621312
Notary Public - California
San Francisco County
My Comm. Expires Nov. 14, 2009
NRO1

Signature Jennifer Ann LesCallett (Seal)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Map of the
McDONALD ISLAND GAS STORAGE RESERVOIR
SHOWING KNOWN PRODUCTIVE LIMITS OF THE
McDONALD ISLAND SAND
Scale - Feet
1000 0 1000 2000
Reference point for well locations is
U.S.C. & G.S. Triangulation Station "Turner"
Lambert Coordinates: 36'+ West of True North
Prepared by Stanley and Stolz
December, 1960

EXHIBIT A

EXHIBIT "B"

INCREMENTAL GAS FEE FACTOR SCHEDULE					
YEAR	LEASE PERIOD			Incremental Gas Fee Factor	
1	March 1, 2007	to	March 1, 2008	$0.08646	per Mcf
2	March 1, 2008	to	March 1, 2009	$0.09078	per Mcf
3	March 1, 2009	to	March 1, 2010	$0.09532	per Mcf
4	March 1, 2010	to	March 1, 2011	$0.10009	per Mcf
5	March 1, 2011	to	March 1, 2012	$0.10509	per Mcf
6	March 1, 2012	to	March 1, 2013	$0.11035	per Mcf
7	March 1, 2013	to	March 1, 2014	$0.11586	per Mcf
8	March 1, 2014	to	March 1, 2015	$0.12166	per Mcf
9	March 1, 2015	to	March 1, 2016	$0.12774	per Mcf
10	March 1, 2016	to	March 1, 2017	$0.13413	per Mcf
11	March 1, 2017	to	March 1, 2018	$0.14083	per Mcf
12	March 1, 2018	to	March 1, 2019	$0.14788	per Mcf
13	March 1, 2019	to	March 1, 2020	$0.15527	per Mcf
14	March 1, 2020	to	March 1, 2021	$0.16303	per Mcf
15	March 1, 2021	to	March 1, 2022	$0.17118	per Mcf