This Calendar Item No. 13
was approved as Minute Item
No. 13 by the State Lands
Commission by a vote of 3
to 0 at its 1-25-79
meeting.

CALENDAR ITEM

13.

1/79
W 9738.1
Willard

APPROVAL OF CHEVRON USA, INC. AND SHELL OIL COMPANY
GAS SALES AGREEMENTS WITH
PACIFIC GAS AND ELECTRIC COMPANY

Chevron USA, Inc. and Shell have negotiated price increases under their gas sales contracts with Pacific Gas and Electric Company (PG&E) covering gas produced under State leases and gas allocated to State lands under compensatory agreements. Copies of the letter agreements dated July 1, 1978 modifying the price provisions of the sales contracts have been filed with the Commission. The price modification covers a 2-year period commencing July 1, 1978. The new price for gas delivered at 33-1/3% load factor and having a heating value of 1,000 Btu per cubic foot is $1.70 per Mcf for the period of July 1, 1978 through June 30, 1979, and $1.78 per Mcf for the period of July 1, 1979 through June 30, 1980 (the previous price was $1.20 per Mcf).

The State leases subject to these modified sales contracts include Easement 415.1 in the Rio Vista Gas Field, Oil and Gas Leases PRC 3743.1 and PRC 3896.1 in the Ryer Island Field (jointly held by Chevron and Shell) and Gas Leases PRC 714.1 and PRC 729.1 in the River Island Field. Each of these agreements provides that the Commission shall approve any sales contract or other arrangement by which the lessee disposes of the gas produced under the lease. The Rio Vista and Ryer Island leases, but not the River Island leases, permit the Commission to determine the reasonable market value or current market price of the gas for purposes of determining the State's royalty.

The Natural Gas Policy Act of 1978 was signed into law on November 9, 1978, and provided for the regulation of intrastate gas sales as well as interstate gas sales. Natural gas is separated into defined categories with each category having a different price ceiling. The price ceiling applicable to sales under existing intrastate contracts, which is the present classification of the gas sold under the State leases, is the lower of:

> "(A) the price under the terms of the existing contract, to which such natural gas was subject on the date of the enactment of this Act (November 9, 1978), as such contract was in effect on such date; or

A 5, 9, 10, 12

S 4, 5, 7

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"(B) the maximum lawful price, per million Btu's, computed for such month under Section 102 (relating to new natural gas)."

The new gas price for November 1978 computed under the Act is $2.060 per MMBtu. The contract price in effect on November 9, 1978, under the Chevron and Shell sales contracts with PG&E is $1 70 per MMBtu. The new gas price will escalate monthly by an inflation adjustment factor. The contract price will increase to $1.78 per MMBtu on July 1, 1979. Therefore, the contract price will always be lower than the new gas price with the result that the contract price will be the ceiling price through June 30, 1980.

It is understood that essentially all of the Northern California gas producers have agreed to sales contracts with PG&E at prices indentical to those in the Chevron and Shell contracts. Therefore, gas selling in the intrastate market in Northern California cannot be sold at a price higher than the PG&E contract price unless it were determined to come within another category which has a higher lawful price. Such categories include new gas, gas from new onshore wells, high-cost natural gas and stripper well natural gas. While it is unlikely that any of the gas produced under the State leases would qualify for such higher ceiling prices, such prices would be a ceiling only. Nothing in the federal law or any other law requires PG&E or any other purchaser to pay the ceiling price.

Subsequent to June 30, 1980, the gas sales contracts will roll over and gas produced from the State leases will be subject to a different and higher ceiling price. Under this category the maximum lawful price is the higher of:

"(A)(i) the maximum price paid under the expired contract, per million Btu's, in the case of the month in which the effective date of such rollover contract occurs; and

"(ii) in the case of any month thereafter, the maximum lawful price, per million Btu's, prescribed under this subparagraph for the preceding month multiplied by the monthly equivalent of the annual inflation adjustment factor applicable for such month; or

"(B)(i) $1.00 per million Btu's, in the case of April 1977; and "(ii) in the case of any month thereafter, the maximum lawful price, per million Btu's, presribed under this subparagraph for the preceding month multiplied by the monthly equivalent of the annual adjustment factor applicable for such month."

A special rule provides that the even higher ceiling for new natural gas is to be applicable to first sales under intrastate rollover contracts which constitute "a State government's or Indian tribe's natural gas production, or royalty share or other interest...in natural gas production, from real property (inlcuding subsurface mineral interests) owned on the date of enactment of this Act by such State government or Indian tribe."

These maximum lawful prices for intrastate rollover contracts, like those for existing intrastate contracts, are merely price ceilings. There is nothing in the Act requiring PG&E to pay these prices at the time these ceilings become applicable. The ceilings merely set the upper limit on any price that PG&E, Shell and Chevron may agree upon to be effective after June 30, 1980.

EXHIBIT: A. Location Map.

IT IS RECOMMENDED THAT THE COMMISSION:

1. APPROVE THE LETTER AGREEMENT MODIFICATIONS DATED JULY 1, 1978, TO GAS SALES AGREEMENTS BETWEEN CHEVRON USA, INC. AND PACIFIC GAS AND ELECTRIC COMPANY AS A BASIS FOR THE SALE AND DELIVERY BY CHEVRON OF THEIR SHARE OF THE GAS PRODUCED UNDER GAS LEASE EASEMENT 415.1, GAS LEASES PRC 714.1 AND PRC 729.1, AND OIL AND GAS LEASES PRC 3743.1 AND PRC 3896.1.

2. APPROVE THE LETTER AGREEMENT MODIFICATIONS DATED JULY 1, 1978, TO GAS SALES AGREEMENTS BETWEEN SHELL OIL COMPANY AND PACIFIC GAS AND ELECTRIC COMPANY AS A BASIS FOR THE SALE AND DELIVERY BY SHELL OF THEIR SHARE OF THE GAS PRODUCED UNDER OIL AND GAS LEASES PRC 3743.1 AND PRC 3896.1.

3. STIPULATE THAT THE APPROVALS ARE SUBJECT TO THE EXPRESS CONDITION THAT THEY SHALL NOT BE CONSTRUED TO MODIFY OR TO AFFECT IN ANY MANNER ANY OF THE LEASE TERMS, INCLUDING FULL COMPLIANCE BY THE LESSEE WITH ALL THE TERMS AND CONDITIONS OF THE LEASES, AND THE RULES AND REGULATIONS OF THE COMMISSION.

4. FURTHER STIPULATE THAT THE APPROVAL SHALL BE OF NO FORCE AND EFFECT SHOULD THOSE PORTIONS OF THE NATURAL GAS POLICY ACT OF 1978 IMPOSE PRICE CEILINGS ON THE SALES OF ROYALTY GAS FROM THE STATE LEASES BE DECLARED UNCONSTITUTIONAL IN ANY JUDICIAL PROCEEDING INCLUDING BUT NOT LIMITED TO THE PRESENTLY PENDING CASE FILED ON NOVEMBER 20, 1978 IN THE UNITED STATES DISTRICT COURT, FOR THE WESTERN DISTRICT OF OKLAHOMA ENTITLED OKLAHOMA, TEXAS AND LOUISIANA V. FEDERAL ENERGY REGISTRY COMMISSION.

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(Added 1/24/79)

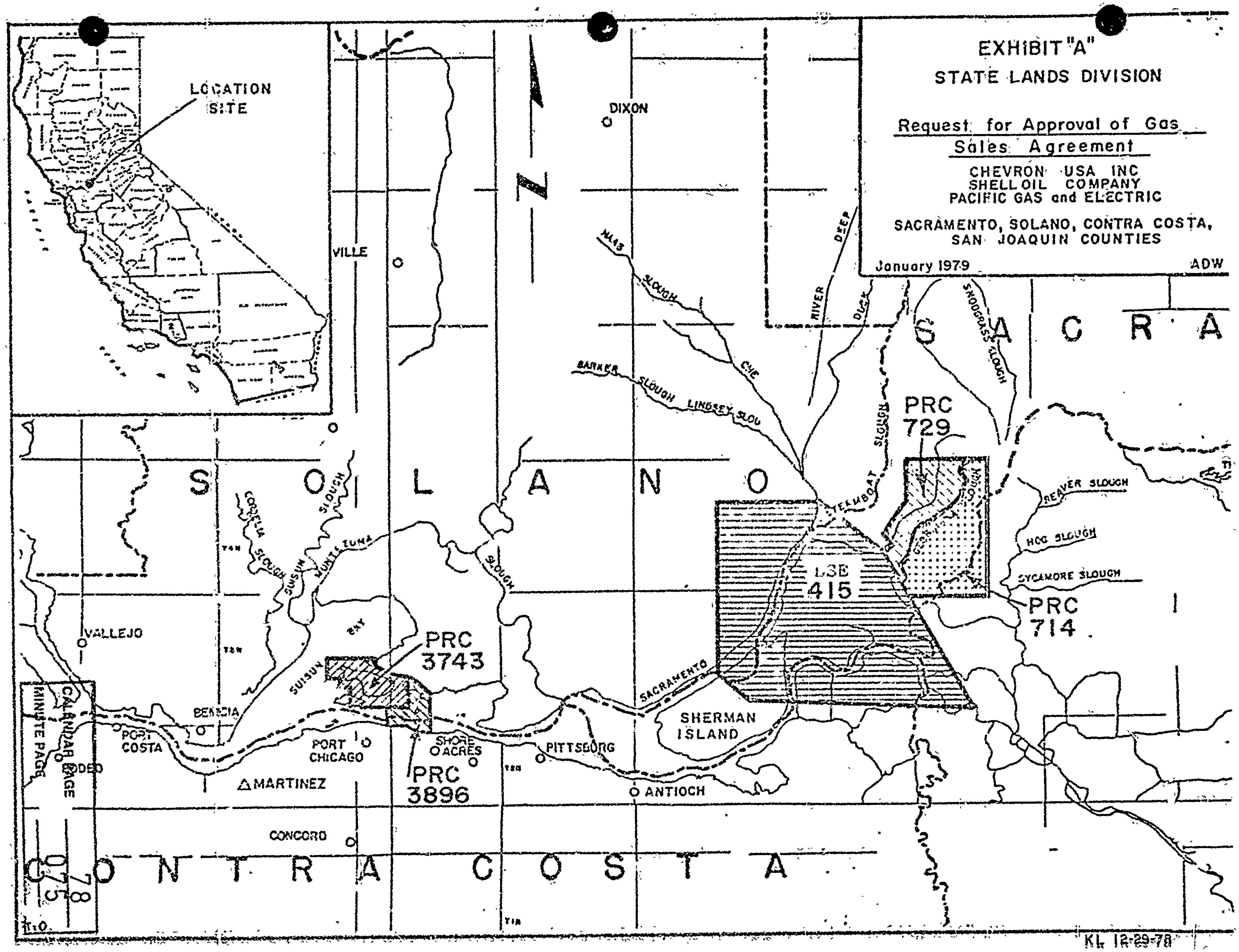
EXHIBIT "A"
STATE LANDS DIVISION
Request for Approval of Gas Sales Agreement
CHEVRON USA INC
SHELL OIL COMPANY
PACIFIC GAS and ELECTRIC
SACRAMENTO, SOLANO, CONTRA COSTA, SAN JOAQUIN COUNTIES
January 1979
ADW
LOCATION SITE
DIXON
VILLE
S O L A N O
S A C R A
C O N T R A C O S T A
PRC 729
PRC 714
PRC 3743
PRC 3896
LSE 415
SHERMAN ISLAND
VALLEJO
BENICIA
PORT COSTA
RODEO
PORT CHICAGO
MARTINEZ
SHORE ACRES
PITTSBURG
ANTIOCH
CONCORD
SUISUN BAY
SACRAMENTO
BARKER SLOUGH
LINDSEY SLOUGH
BEAVER SLOUGH
HOG SLOUGH
SYCAMORE SLOUGH
SNODGRASS SLOUGH
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