

MINUTE ITEM

This Calendar Item No. 25
was approved as Minute Item
No. 25 by the State Lands
Commission by a vote of 2
to 0 at its 11/20/86
meeting.

CALENDAR ITEM

A 4, 10, 11, 26

25

S 2, 5, 7

11/20/86
LSE E-415
PRC 714
PRC 729
PRC 2966
PRC 3743
PRC 3896
PRC 6498
W 9738
Hamilton

**AMENDMENT OF GAS PURCHASE AND SALES AGREEMENTS TO PERMIT
STATE PARTICIPATION IN PACIFIC GAS AND ELECTRIC COMPANY'S
NEW CALIFORNIA GAS MARKET RETENTION PROGRAM**

LESSEE AND OPERATOR:

Chevron U.S.A., Inc.
Attn: Hilman P. Walker
P. O. Box 5050
San Ramon, California 94583-0905

LEASE INFORMATION:

Chevron U.S.A. Inc. (Chevron) is lessee and operator of State oil and gas Leases LSE E-415, PRC's 714, 729, 3743, 3896 and 6498 and Compensatory Royalty Agreement PRC 2966 which are located in Contra Costa, Sacramento, San Joaquin and Solano Counties. Leases PRC 3743 and 3896 are jointly held by Chevron and Shell California Production Inc. Shell's 50 percent share of the gas produced from these two leases is used by Shell at its Bay Area refinery with the State's royalty based upon the price Chevron receives from its sales of gas to Pacific Gas and Electric Company (PG&E). The State leases require that the Commission approve all sales contracts including any amendments which affect the disposition of the State's royalty share of production from the State leased lands.

BACKGROUND AND SUMMARY:

Chevron is presently selling all, except Shell's share, of the gas produced from the State leases (including the State's royalty share) to PG&E. As a result of a drop in world oil and

-1-

(PAGES 76-76.6 ADDED 11/12/86)
(NON-SUBSTANTIVE REVISION 12/01/86)

CALENDAR PAGE	76
MINUTE PAGE	3826

CALENDAR ITEM NO. 25 (CONT'D)

natural gas prices, the Commission approved on July 24, 1986 five price adjustments to permit Chevron to sell the State's royalty share of produced gas at the reduced preferential sequencing price of \$2.23 per MMBtu (from \$2.50 per MMBtu) retroactive to April 1, 1986. This price reduction permitted the seller (Chevron and the State) an opportunity to maintain its preferential sequencing position, as set forth by the CPUC in its Gas Purchase Sequencing Policy (CPUC Decision No. 84-12-067), currently in effect for preferentially sequenced gas purchases.

On June 30, 1986, El Paso Natural Gas Company, one of PG&E's out-of-state gas suppliers, filed with the Federal Energy Regulatory Commission a request to reduce its commodity price for gas entering PG&E's system effective July 1, 1986. This drop in price by El Paso reflects current market conditions which have created the need for California gas producers to lower their price to compete with low-cost spot and discount priced gas available to PG&E. Therefore, PG&E again has notified its California producers that they must lower their wellhead price to \$2.05 per MMBtu effective August 1, 1986, if they are to maintain a preferential position in PG&E's gas purchase sequencing; PG&E's take of preferentially sequenced priced gas has been less than 50 percent for the months of August, September and October 1986, inclusive.

As an alternative to the CPUC mandated sequencing program, PG&E has offered California gas producers, selectively by contract, the option to participate in its new California Gas Market Retention Program (MRP). The MRP offers the California gas producer an opportunity to maximize its gas deliveries by matching PG&E's average gas cost on a monthly basis in which spot and discount gas is purchased. The contract period for this program will be from August 1, 1986 through October 31, 1986. The MRP prices for the months of August, September and October 1986 are \$1.89, \$1.88 and \$1.87 per MMBTU, respectively; PG&E's take of MRP priced gas is 100 percent for the contract period. PG&E has offered this MRP option to Chevron for the contracts covering the State leases. At the end of the MRP it is anticipated that the price for natural gas will revert to the CPUC mandated sequencing program. It is understood that PG&E's MRP will not be continued beyond October 31, 1986 because spot prices during the winter months are expected to exceed the sequencing price.

(ADDED 11/12/86)

-1-

CALENDAR PAGE	76.1
MINUTE PAGE	3827

CALENDAR ITEM NO. 25 (CONT'D)

On August 1, 1986, Chevron amended its gas purchase and sales agreements and accepted PG&E's price reduction in order to participate in PG&E's new MRP, to maximize deliverabilities and production and increase income including royalty income. Since Chevron cannot sell the State's gas royalty under the MRP without first obtaining Commission approval, Chevron has requested that the Commission also elect to participate in PG&E's new MRP.

Staff has reviewed the Letter Agreement between Chevron and PG&E dated July 22, 1986, that allows Chevron to participate in PG&E's new MRP and finds that it is in the State's best interest to permit Chevron to include the State's royalty share in the sale of gas produced from the State leases.

OTHER INFORMATION:

1. Pursuant to the Commission's delegation of authority and the State CEQA Guidelines (14 Cal. Adm. Code 15061), the staff has determined that this activity is exempt from the requirements of the CEQA because the activity is not a "project" as defined by CEQA and the State CEQA Guidelines.

Authority: P.R.C. 21065 and 14 Cal. Adm. Code 15378.

AB 884: N/A.

EXHIBIT: A. Letter Agreement dated July 22, 1986.

IT IS RECOMMENDED THAT THE COMMISSION:

1. FIND THAT THE ACTIVITY IS EXEMPT FROM THE REQUIREMENTS OF THE CEQA PURSUANT TO 14 CAL. ADM. CODE 15061 BECAUSE IT IS NOT A PROJECT AS DEFINED BY P.R.C. 21065 and 14 CAL. ADM. CODE 15378.
2. APPROVE THE LETTER AGREEMENT DATED JULY 22, 1986, WHICH AMENDS CERTAIN GAS PURCHASE AND SALES AGREEMENTS BETWEEN CHEVRON U.S.A., INC. AND PACIFIC GAS AND ELECTRIC COMPANY AND PERMITS CHEVRON U.S.A., INC. TO SELL THE STATE'S ROYALTY SHARE OF THE GAS PRODUCED FROM STATE OIL AND GAS LEASES LSE E-415, PRC'S 714, 729, 3743, 3896 AND 6498 AND COMPENSATORY ROYALTY AGREEMENT PRC 2966 AT PACIFIC GAS AND ELECTRIC COMPANY'S NEW CALIFORNIA GAS MARKET RETENTION PROGRAM PRICE FOR THE MONTHS OF AUGUST, SEPTEMBER AND OCTOBER 1986, INCLUSIVE, EFFECTIVE AUGUST 1, 1986.

EXHIBIT "A"

PACIFIC GAS AND ELECTRIC COMPANY

PG&E + 245 MARKET STREET • SAN FRANCISCO, CALIFORNIA 94106 • (415) 972-6500 • TWX 910-372-6587

GENE SATRAP
MANAGER
GAS SUPPLY MANAGEMENT

July 22, 1986

Chevron U.S.A. Inc.
Room E1094
P.O. Box 5043
San Ramon, CA 94583-0943

Gentlemen:

Please refer to that certain Gas Purchase and Sales Agreement(s), as amended, (Agreement) between Chevron U.S.A. Inc. (Seller) and Pacific Gas and Electric Company (Buyer) as listed on the attached Exhibit A, and specifically to the PRICE paragraph therein.

Buyer's continuing purchases of large volumes of low-cost SPOT and discount-priced gas have significantly reduced the average delivered cost to Buyer for its out-of-state gas supplies. Such purchase opportunities, coupled with current end-user alternative fuel and gas market competition in Buyer's service territory, now require Seller to adjust the cost for its higher-priced California gas to compete with Buyer's gas purchase opportunities for available lower-cost gas. Buyer proposes that, rather than Buyer reducing purchases of Seller's gas production volumes to favor out-of-state lower-cost gas purchases, Buyer is willing to offer to Seller the opportunity to maximize its gas deliveries by meeting Buyer's market price target.

To provide Seller such a market opportunity to maximize its gas production from its gas well(s) covered by the Agreement on a selective basis, Buyer offers to Seller the option to participate in the California Gas Market Retention Program (Program). Such Program participation is at Seller's sole and complete discretion.

Please be advised that this is not a request from Buyer to Seller to redetermine the Fair Market Value gas purchase price in the Agreement between us.

Therefore, be it understood that:

"The price Buyer agrees to pay and Seller agrees to accept as payment in full, pursuant to the terms of the Agreement, as amended herein, for Seller's share of gas

(ADDED 11/12/86)

CALENDAR PAGE	76.3
MINUTE PAGE	3829

produced and sold to Buyer from well(s) covered by the Agreement for the months of August, September and October 1986, inclusive, shall be determined as follows:

As a Program participant, from the fifteenth (15th) day through the twenty-fifth (25th) day of July 1986, from the fifteenth (15th) day through the twentieth (20th) day of August 1986 and from the fifteenth (15th) day through the nineteenth (19th) day of September 1986, Seller shall have the option to contact Buyer during normal business hours of 8:00 a.m. to 5:00 p.m., P.D.T., Monday through Friday at the telephone numbers listed below, and Buyer shall be obligated to provide its PRELIMINARY PRICE for the next succeeding month: (415) 972-2690; (415) 972-7075; or (415) 972-6598.

On or after the twenty-fifth (25th) day of July, the twenty-seventh (27th) day of August and the twenty-fifth (25th) day of September 1986, inclusive, Seller shall have the option of contacting Buyer at the above-listed telephone numbers during the listed business hours and Buyer shall be obligated to inform Seller of the Program price in effect for the current or succeeding month, as appropriate. Said Program price shall not vary from the PRELIMINARY PRICE, as previously committed to, by more than plus or minus five percent (5%) and shall be rounded to the nearest whole one cent. Buyer shall confirm in writing such Program price in effect for the succeeding or current month, as requested.

From the first day following execution of this Amendment between the parties through the nineteenth (19th) day of September 1986, inclusive, excluding the period of August 20 through 31, 1986, inclusive, Seller shall retain the unilateral right to terminate this Amendment by giving Buyer written notice, as provided for in the NOTICE section of the Agreement, stating Seller's intent to terminate its participation in the Program and, therefore, terminate this Amendment, effective 7:00 a.m., P.D.T., on the first (1st) day of the next succeeding month. Seller understands that once Seller gives such written notice to terminate its participation in the Program, Seller cannot re-enter the Program.

Seller and Buyer further agree that the prices agreed to herein do not constitute a redetermination of the Fair Market Value gas purchase price under the PRICE paragraph of the Agreement. Seller understands that

(ADDED 11/12/86)

CALENDAR PAGE	764
MINUTE PAGE	3830

EXHIBIT A

Attached to and made part of that certain Letter Agreement
between Chevron U.S.A. Inc. and Pacific Gas and Electric Company
dated July 22, 1986

<u>Field</u>	<u>Contract Date</u>	<u>PGandE Contract Number</u>
Arbuckle	September 1, 1957	205
Beehive Bend - Willows	January 20, 1985	844
Bounde Creek	September 1, 1983	1022
Buckeye Kirk	January 1, 1982	297
Cache Slough	October 12, 1978	654
Compton Landing	October 12, 1978	655
Compton Landing	September 16, 1980	708
Crossroads	July 1, 1978	648
Durham	January 1, 1968	460
Dutch Slough	January 1, 1986	-
Grimes	July 21, 1964	373
Grimes	June 15, 1979	683
Grimes	June 23, 1980	1050
Grimes	June 3, 1981	1021
Lathrop	March 30, 1962	329
Rio Vista Deep	September 22, 1967	451
Rio Vista Deep, State Lands	September 22, 1967	453
Rio Vista State Lands	May 16, 1940	100
Rio Vista	January 1, 1956	239
River Islands Winters Zone	January 10, 1968	458
River Islands - Isleton	January 20, 1985	845
Ryer Island	November 26, 1968	480
Sherman Island	June 30, 1967	449
Stockton	August 19, 1985	874
Sugarfield	May 31, 1979	677
Van Sickle Island	October 23, 1969	493
West Grimes	August 11, 1961	295
West Thornton	July 18, 1957	214
Zamora	July 1, 1978	640

(ADDED 11/12/86)

CALENDAR PAGE	76.5
MINUTE PAGE	3831

July 22, 1986

gas tendered for sale at the prices to be offered by Buyer herein will be purchased by Buyer on a discretionary basis at its sole judgement when Buyer is capable of accepting such gas into its system subject to constraints imposed by contracts or operating requirements.

The term of this Amendment shall be from the date of execution through October 31, 1986, inclusive, unless earlier terminated by Seller pursuant to the terms herein. Seller and Buyer further agree that, except as appearing in this Amendment to the Agreement, all other terms and conditions of the Agreement shall remain in full force and effect."

If Seller agrees to the foregoing, please execute and return both copies to Buyer for execution on behalf of Buyer. A fully executed copy will be returned to Seller.

Sincerely,

PACIFIC GAS AND ELECTRIC COMPANY

By _____
Manager, Gas Supply Management
Department

Date _____

ACCEPTED AND AGREED TO:

CHEVRON U.S.A. INC.

By H.P. Walke
Assistant Secretary

Date August 1, 1986

(ADDED 11/12/86)

CALENDAR PAGE	76.6
MINUTE PAGE	3832