

13. (OIL AND GAS LEASE AUTHORIZATION, SUMMERLAND AREA, SANTA BARBARA COUNTY - W. O. 2046.) The following report was presented to the Commission:

"On April 12, 1956 (Minute Item 3, pages 2593-97) the Commission deferred consideration of the form of oil and gas lease to be utilized in the offering of 500 acres of tide and submerged lands in the Summerland area, Santa Barbara County. The lease proposed for consideration at this prior meeting had been approved as to form by the Office of the Attorney General and had been reviewed by participants in the public hearing held at Santa Barbara January 11, 1956, without developing any statement of objection. Non-objection to the utilization of the lease form was also reported by the State Department of Natural Resources. Additional proposals relative to lease terms submitted by the Public Lands Committee, Western Oil and Gas Association, have been considered and incorporated for the purpose of clarification and elimination of possible ambiguities. The resultant amended form of lease proposed for use under the subject lease offer has now been reported as acceptable by the Public Lands Committee, Western Oil and Gas Association."

Mr. Paul K. Home stated that he had been requested by the Chairman of the Public Lands Committee of the Western Oil and Gas Association, which committee was in charge of considering revisions of the lease, to discuss the provisions of the lease with the Executive Officer and his staff, and he believed that in the main the provisions were satisfactory to the Association. However, he further believed that it was essential for clarification that the points previously made by Mr. Ruble about removable structures (Minute Item 12) be considered in connection with Paragraphs 6 and 14. He indicated that the ambiguity in Paragraph 6 probably had been corrected, but stated that Paragraph 14 probably needed further clarification, and suggested that the language to be used be substantially the same as that adopted in connection with the changes to the Commission's rules and regulations. The Executive Officer indicated that this was satisfactory.

Mr. Kirkwood asked if the necessary action had been taken to protect the recreational and residential areas involved, in accordance with the Commission's previous resolution at its meeting of February 9, 1956 (Minute pages 2576-2578).

Mr. Milton L. Duncan of the Summerland Citizens Association informed the Commission that while the Commission had been working conscientiously to protect his association's interests, he wished to know whether these terms were the same as those previously reviewed. The Executive Officer assured him that they were the same.

In response to Mr. Kirkwood's question, Mr. Rountree indicated that the Commission had discretion under the provisions of Section 6873.2 of the Public Resources Code with regard to the conditions under which the proposed lease could be issued. This section states in part:

"Within thirty (30) days after such hearing the commission shall determine to offer the land for lease, as provided under Sections 6871.3, 6872 and 6872.1, unless the commission shall determine that the issuance of a lease as to all or a part of such land would result in an impairment or interference with the developed shore line recreational or residential areas adjacent to the proposed leased acreage, or the commission may determine to offer such land for lease as to all or a part thereof and include in the offer for lease such reasonable rules and regulations which, in the opinion of the commission, are necessary for the exploration, development, and operation of said lease in a manner which will not impair or interfere with said developed shore line recreational or residential areas;"

In the light of the foregoing, Mr. Rountree suggested that in the action taken with respect to the issuance of the lease the Commission make a finding under the foregoing portion of Section 6873.2. Assemblyman Miller asked whether this particular lease of 500 acres was in a known geological structure of a producing oil and gas field, and was informed by the Executive Officer that the Commission had determined that it was in such a structure. Mr. Miller then asked if the 500 acres covered the entire field, and was told that it did not.

Mr. Miller then questioned the royalty rate of 16-2/3 percent minimum, with a ceiling of 50 percent, following which Assemblyman Bruce Allen asked why these rates should apply when production reaches 500 barrels per day per well, and why on that kind of production the State's royalty should be limited to 50 percent. The Executive Officer pointed out that the State has several leases which produce a much higher royalty, but that it was felt that it was neither fair to potential lessees nor proper for the State to demand too high a royalty, for under such circumstances the State could reach the point of diminishing returns where the lessee could loaf and not produce to full capacity.

Assemblyman Allen then referred to the oil wells in Long Beach, on which large royalties have been received, and indicated that there was something wrong with the State's leases if the lessees could produce less than the maximum of which the wells were capable, whereupon he was informed by the Executive Officer that if the lessees do "lay down" the State can require them to go to the maximum efficiency rate. Answering the remark about the higher figures quoted on Long Beach leases, the Executive Officer pointed out that Long Beach does not issue leases, but rather works on a contract basis, and is responsible for certain costs, whereas the State takes no risk with respect to costs of production, all risks being taken by the lessees. Under the present law it is not believed that the State is authorized to enter into contracts such as Long Beach does.

Assemblyman Allen remarked that limitation of the State's royalties to 50 percent on production of over 500 barrels a day per well does not appear reasonable, on the basis of past experience and that of the City of Long Beach, and questioned if in this instance the State was securing the best possible royalties and actual returns from its oil, stating that it did not appear to be reasonable and in the public interest of the State to do otherwise. The Executive Officer explained that the higher the royalty rate was set the lower the bonus would be that the State would receive; that it was a question of the Commission feeling its way on the new law until the best combination can be determined.

Assemblyman Unruh stated he also was interested in the question of the maximum 50 percent royalty, and pointed out that it had been mentioned that one reason for the limitation of 50 percent on the royalty was to assure maximum production, whereas the Executive Officer had stated that the Commission had power under its leasing arrangements to assure the maximum and most efficient rate of production, and he asked why a limitation on the royalty was necessary to assure maximum production if the Commission had the power to force the maximum rate of production.

Mr. Hortig explained that the Commission is invariably faced with the necessity of balancing all factors going into the sum total; that if there is higher specified royalty rate, even if only prospective and never actually realized in practice, the mere specification of a higher royalty rate would necessitate that any future bidder write insurance against that higher royalty rate in terms of a lower bonus; in other words, the maximum to accrue to the State is not the 50 percent royalty only but also what is expected to be a substantial cash bonus, which bonus is now required under the Cunningham-Shell Act. The previous higher royalty rates were without any bonus, and will now be offset by the cash bonus.

Assemblyman Unruh asked if there was any way of predicting the size of a pool. Mr. Hortig stated that it could be determined how much area there was within a known geological structure. Assemblyman Unruh further asked if it could be determined how much the State should get as a bonus. Mr. Hortig indicated that this could not be determined precisely, but that a reasonable estimate could be arrived at of maximum potential production from the area being offered for lease, what the value of that production was going to be, and what a prudent operator could afford to pay for that amount of oil, which would give a yardstick to work from in deciding how much to expect from royalty and from cash bonuses.

The Executive Officer explained that this was not the final action taken by the Commission, but that after bids are taken they are evaluated and the staff formulates a recommendation as to whether, in the interests of the State, all bids should be rejected.

Assemblyman Unruh then referred to the staff's statement about now having one area of 500 acres which it was prepared to offer for lease, and another parcel of 5500 acres not yet known, and asked if it could be determined that the 5500 acres was in a known geological structure. The Executive Officer stated

that this would be subject to an investigation which had not yet been made - that the Commission may have the necessary information available in the office. Mr. Unruh then asked if this information was available anywhere, and was informed by the Executive Officer that the area had been explored by several companies in the past, but that such information obtained was not available to the Commission. Mr. Unruh went on to say that he was attempting to bring out that he was mistaken in his impression on the 5500 acres, and suggested that if this area is to be classified as a known geological structure, it might be well to wait a while to see what the royalty provisions of this 500-acre lease would be, before offering further leases in that area.

Mr. Kirkwood mentioned that for the Huntington Beach leases issued last summer he understood the maximum royalty was 60 percent, and he asked the reason for bringing this rate down to 50 percent. Mr. Hortig explained that economic studies indicated that the areas offered at Huntington Beach at that time were expected to have a better potential than the 500 acres currently being considered - that it was the normal expectation that the wells on the lease in the Santa Barbara area would be smaller producers than the Huntington Beach wells. In response to a query by Mr. Kirkwood as to whether it was anticipated that any of the wells would exceed 500 barrels, Mr. Hortig replied that this was not expected.

UPON MOTION DULY MADE AND UNANIMOUSLY CARRIED, IT WAS RESOLVED AS FOLLOWS:

THE COMMISSION FINDS AND DETERMINES THAT THE ISSUANCE OF THIS LEASE IN THE MODIFIED FORM SUBMITTED, AS TO THE LAND DESCRIBED THEREIN, WILL NOT RESULT IN IMPAIRMENT OF OR INTERFERENCE WITH THE DEVELOPED SHORE LINE RECREATIONAL AREAS ADJACENT TO THE PROPOSED LEASE ACREAGE. THE EXECUTIVE OFFICER IS AUTHORIZED TO UTILIZE THE FORM OF OIL AND GAS LEASE WHICH WAS SUBMITTED TO THE COMMISSION WITH THE CALENDAR OF MAY 18, 1956, WITH PARAGRAPH 14 MODIFIED WITH RESPECT TO REMOVAL OF EQUIPMENT, WHICH FORM OF LEASE IS MADE A PART OF THIS RESOLUTION BY REFERENCE, AND TO OFFER FOR LEASE, PURSUANT TO SECTION 6872 OF THE PUBLIC RESOURCES CODE, THE MOST LANDWARD 500 ACRES OF TIDE AND SUBMERGED LANDS UNDER CONSIDERATION UNDER WORK ORDER 2046.

14. (CONSULTING SERVICES FOR REVIEW OF PROPOSED OIL AND GAS LEASES - W. O. 2049-D.) The following report was presented to the Commission:

"On August 16, 1955 (Minute Item 5, pages 2413-14) the Commission authorized the Executive Officer to negotiate and enter into contracts with the firm of Stanley & Stolz, and with Dr. P. T. Homan, and Mr. Charles B. Bennett for consulting services and for preparation of reports on problems related to tide and submerged land oil and gas leases by the State Lands Commission during the budget year 1955-56, pursuant to Chapter 1724, Statutes of 1955, at a total cost not to exceed \$50,000. Total consulting services to date under the contracts authorized have cost \$602.20. Due to the incompatibility of other consulting commitments, the firm of Stanley & Stolz did not enter into a contract and, therefore, it has become necessary to retain another consulting geologist to perform the scope of work originally proposed to be contracted with Stanley & Stolz."