

(c) "County" is the County of Orange.

(d) "State" is the State of California.

Section 1401. Oil Well Drilling.

No drilling for, exploration work of any kind, production or refining of, oil, gas or other hydrocarbon substances shall be permitted within that area of the City of Newport Beach as such limits exist as of the effective date of this Charter. The prohibitions shall include the City of Newport Beach.

This Section shall not prohibit the drilling for, production or refining of oil, gas or other hydrocarbon substances within any territory annexed to the City after the effective date of this Charter if such drilling, production or refining was being conducted in such territory at the date of the annexation thereof; but no such drilling, production or refining shall be permitted within any territory annexed to the City after the effective date of this Charter if such activities were not being conducted in such territory at the date of the annexation thereof.

This Section shall not prohibit the continuance of production of any well slant drilled under property within the City from a location outside the City and in existence at the time this Charter takes effect. Nor shall this section preclude the City Council from permitting the slant drilling of wells under the surface of property within the City from surface locations located either outside the City or within future annexations to the City wherein the drilling for and production of oil, gas and other hydrocarbon substances is permitted, provided that such slant drilling shall first be approved by a majority of the electors voting on such proposition at any special or general municipal election, and provided further that all of the following conditions shall be complied with:

(a) The holding of a public hearing upon any application for a permit to conduct such drilling;

(b) The requiring of the removal of all derricks and other surface structures used in the drilling of such well upon completion or abandonment of such well;

(c) The furnishing of a faithful performance surety bond and the maintenance of public liability and property damage insurance by the permittee in amounts deemed adequate by the City Council;

(d) The screening by landscaping and the beautification of any production and maintenance facilities used in the operation of any such well;

(e) Provisions for the payment to the City of such amounts as in the sound discretion of the Council are adequate amounts for the consideration or granting of such permit, the holding of such hearing, the making of initial and periodic inspections, the granting of easements under City property and for royalties or rentals;

(f) The requirement that no such well shall traverse any land under the area of the City wherein drilling is prohibited at a vertical depth of less than 400 feet from the surface of the ground; and

(g) Such other conditions as the City Council may prescribe by ordinance. (As amended effective April 23, 1958)

Restrictions on Oil Drilling
Charter Section 1401

STATEMENT OF THE ISSUE:

Oil well production and drilling activity have been on-going on City and County land on and in the immediate vicinity of Banning Ranch for over 50 years, and prior to enactment of the current City Charter. Over that period of time, many things have changed. The voters approved a new General Plan in 2006 that sets goals for the re-use of Banning Ranch as either fully or mostly open space, the achievement of which will require changes in current oil drilling activity. In addition, productivity of oil wells and methods of oil extraction have changed since the Charter was enacted. The original Charter language is ambiguous with regard to the scope of activities that are allowed to continue oil production from an existing oil extraction area. This makes it difficult for the City to move forward with consolidation of oil drilling on the Banning Ranch property to allow its reuse as called for in the General Plan or to implement new oil extraction techniques such as water injection on the City's own oil wells. Should the City modify Charter Section 1401 to clarify and simplify its provisions, to facilitate the achievement of General Plan goals and to allow current oil extraction activities to continue with greater efficiency and productivity, and on smaller areas of land?

RELEVANT BACKGROUND:

Charter Provisions:

Restrictions on oil drilling were part of City ordinances before enactment of the City's charter, at least as early as 1929. These restrictions comprised Charter Section 1401 when the charter was originally adopted by the voters on June 8, 1954.

Section 1401 of the charter prohibits drilling for, exploration and production or refining of oil, gas or other hydrocarbon substances within the City boundaries as of the effective date of the charter, January 7, 1955. (For the purposes of this white paper, the activities described in the charter will be referred to collectively as "oil drilling.") For territory annexed to the City after the charter's effective date, oil drilling is not prohibited, as long as that activity was occurring in the territory prior to the annexation. Section 1401 was amended by the voters on April 8, 1958 to add the sentence, "The prohibitions shall include the City of Newport Beach." The purpose of the amendment was to close what the Freeholders considered to be a loophole, which could allow the City Council to allow oil exploration without a vote of the people. In a letter received by the City Council on January 14, 1957, which started the amendment process, the Freeholders said that they had intended that Section 1401 should apply to both individuals and legislative bodies.

There are additional provisions in the charter that apply to slant drilling under property within the City boundaries from a drill location outside the City boundaries. Slant drilling is a process whereby the drill shaft travels vertically from the surface for a distance, and then travels at an angle (or slants) to reach oil resources under property other than the location of the surface well, including locations

under the ocean floor. Slant drilling that was occurring prior to the effective date of the charter is allowed to continue. The City Council may permit new slant drilling under property within the City boundaries from drill locations outside the City or within future annexations to the City, only if that slant drilling is first approved by the voters. Additional conditions for new slant drilling include the holding of a public hearing, the removal of all surface structures upon abandonment of wells, the screening of oil facilities, payment to the City for the permit process, inspections and easements under City property, maintaining a minimum well distance of 400 feet below the surface, and other requirements established by ordinance. However, it is unclear how the City could enforce these conditions when the only activity that occurs on the surface, the drilling itself, occurs outside City boundaries and City jurisdiction.

City Wells:

The City owns and operates 16 oil wells that were drilled between 1953 and 1958. Fourteen are operating today, with one used for water injection to increase productivity from other wells, and one completely out of service. The well heads are located on two sites in unincorporated County territory along West Coast Highway (See Exhibit A), and the wells are slant drilled under property within the City, into the area under the ocean which is called the West Newport Offshore Oil Field.

Oil production has declined since the 1980's (when the City acquired the wells) from approximately 60,000 barrels per year to 30,000 barrels per year in 2009. Oil revenue generated is influenced by the price volatility of the oil commodity market. Oil prices have ranged from a low of \$9.05 in 1999 to a high of \$85.92 in 2008. Since 1990, the City has collected approximately \$19.9 million in oil and gas revenue, with operation and maintenance expenditures of \$9.2 million. (Oil and gas revenue is deposited into the Tidelands Fund because the source of the oil is the tidelands area that the City holds in trust for the people of California. The Tidelands Fund may be used only for eligible expenditures that support and maintain the tidelands, such as improvements to tidelands property including dredging Lower Newport Bay, lifeguards, beach cleaning, etc.) Net oil income to the Tidelands Fund since 1990 amounts to \$10.7 million. Since 2007, over \$1 million of net income has been generated per year due to the dramatic increase in oil commodity prices, even with the declining oil production.

The City has been advised that the productivity of its wells will continue to decline unless new oil extraction techniques are used. These techniques may include reconditioning of existing oil wells, converting existing oil wells to water injection wells, drilling new water injection wells or drilling new oil wells. Charter Section 1401 requires a vote of the people for slant drilling new oil wells under property within City boundaries, but there is an exemption for activities that comprise the "continuance of production." It is unclear what "continuance of production" includes and how expansively or limited it may be interpreted.

Banning Ranch Wells:

Over 460 producing/potentially producing and abandoned oil wells are located on the Banning Ranch property, in the County unincorporated area comprising roughly 360 acres of the total of 402-acre

Banning Ranch property, as shown on Exhibit B. The wells are a combination of vertical and slant drilled. The mineral rights and the surface rights on this property are owned by different parties, and there are agreements between the parties regarding use of the surface for oil extraction, drilling new wells, and consolidation of oil operations if the property is developed as allowed in the City's General Plan.

The General Plan includes two alternatives for reuse of the Banning Ranch property: restored open space, and a residential village with the majority of the land preserved as open space. The City is currently reviewing an application for the residential village alternative. The proposed development plan includes the consolidation of Banning Ranch's oil operations on two sites comprising roughly 20 acres, significantly less land than is currently occupied by oil wells (See Exhibit C). To remediate areas planned for open space preservation or development, new wells are proposed to be drilled at the consolidation sites to replace wells removed from larger areas proposed for development and open space preservation. Although it is not known whether the open space preservation (without development) option would require the same oil drilling consolidation, it is likely that consolidation would be desired by the property owners before sale to an open space owner to ensure proper remediation and indemnification; and equally desired by the open space owner to maximize the amount of area and safety associated with public access to the land.

Both proposed consolidation sites are in unincorporated County territory, and both sites currently have oil wells., The City currently has no ability to restrict drilling of new vertical wells on Banning Ranch, and Charter Section 1401 would allow oil operations existing at the time of annexation to continue at those sites after annexation. Because Charter Section 1401 is not clear regarding the scope of activities that are allowed without a vote of the people for the "continuance of production," it is possible that new wells slant drilled under land in the City for consolidation purposes could require a vote of the people, if they are drilled after annexation of the land to Newport Beach.

The property owners have agreed to City review and approval of their development application for the entire property, even though the majority of the site is not within City boundaries; and their application includes a Pre-Annexation and Development Agreement. This agreement is intended to provide for annexation of the entire County portion of the property in one action, thereby ensuring that the City of Newport Beach would be the land use and permitting authority for all development.

The uncertainty regarding the need for a vote on oil drilling for consolidation could affect the property owner's decision to annex the property prior to remediation for open space preservation and/or development. This would result in the County, rather than the City, being the land use and permitting authority. Annexation after development would mean the City may be accepting the responsibility to maintain and serve an area developed under County standards, and annexation after occupancy of the development would require a vote of the residents.

ALTERNATIVES:

The Commission has the following alternatives identified by staff:

Alternative 1: Recommend no change.

This alternative would continue to require a vote of the people for new slant drilling under property within existing City boundaries or newly annexed areas. The existing ambiguity with regard to the need for a vote on activities to continue existing production would remain. This would make it difficult for the City to achieve its General Plan goals for the Banning Ranch property, or to use new oil extraction techniques such as water injection to preserve or enhance oil revenues available to Tidelands areas such as Newport Harbor.

Alternative 2: Recommend deletion of Section 1401.

Without the charter provisions regulating oil drilling, it is certain that a vote of the people would not be required for drilling new City wells, drilling Banning Ranch replacement wells, or drilling in other locations if oil resources were discovered.

Alternative 3: Recommend that Section 1401 be amended to define geographic areas in which oil drilling may occur after the areas are annexed to Newport Beach. The recommended areas are the two City sites (Exhibit A) and the two consolidation sites proposed for Banning Ranch (Exhibit C).

This alternative would clarify the charter by simplifying its provisions and eliminating the existing ambiguity with regard to the need for a vote on activities that comprise “continuance of production.” At the same time, the charter’s environmental protections against proliferation of oil wells would be preserved. The land area on which oil drilling could occur would be reduced from roughly 360 acres in use today to roughly 20 acres, ensuring that visual and noise impacts from oil drilling would be minimized. This alternative would facilitate the City’s achievement of its General Plan goals for Banning Ranch, and would provide greater flexibility for current oil extraction activities to continue with greater efficiency and productivity and to change as new oil extraction methods are developed in the future. Finally, it would provide the City with the opportunity to increase revenue from its oil resources, which by law are dedicated to tidelands uses, including the maintenance and improvement of Newport Harbor.

Attachments: Exhibit A: City Oil Well Locations
Exhibit B: Banning Ranch Oil Well Locations
Exhibit C: Banning Ranch Proposed Land Use Plan

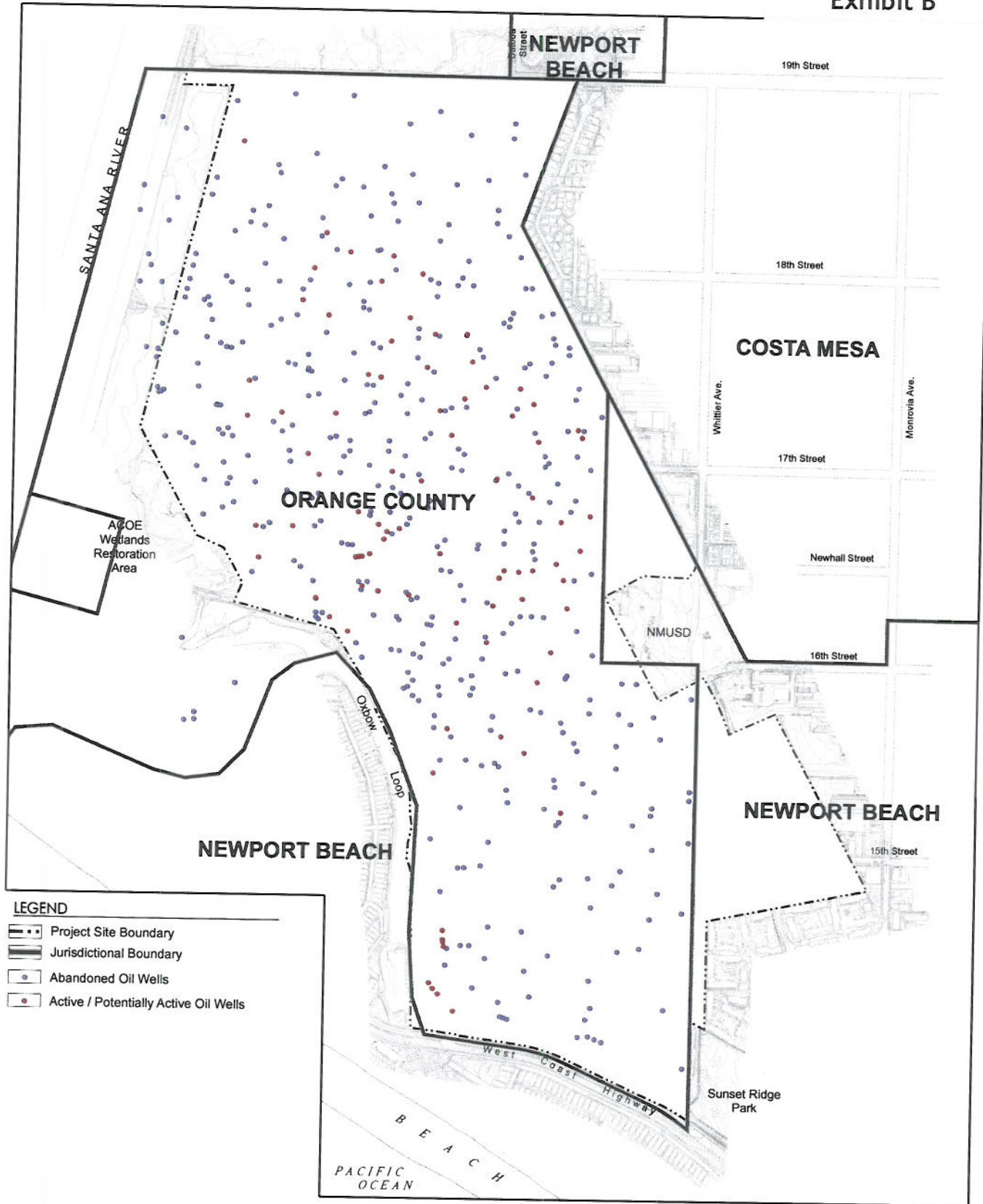



City of Newport Beach
Utilities Department Oil Field

West Coast Highway



0 150 300 600
Feet



- LEGEND**
- Project Site Boundary
 - Jurisdictional Boundary
 - Abandoned Oil Wells
 - Active / Potentially Active Oil Wells



Existing Oil Wells Inventory Map

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