

(Mark One)

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2004

OR

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from \_\_\_\_\_ to \_\_\_\_\_

SEMPRA ENERGY

(Exact name of registrant as specified in its charter)

CALIFORNIA 1-14201 33-0732627  
-----  
(State of incorporation (Commission (I.R.S. Employer  
or organization) File Number) Identification No.)  
101 ASH STREET, SAN DIEGO, CALIFORNIA 92101  
-----  
(Address of principal executive offices) (Zip Code)  
Registrant's telephone number, including area code (619)696-2000  
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SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of each class	Name of each exchange on which registered
Common stock, without par value	New York and Pacific
Mandatorily redeemable trust preferred securities	New York
Equity units, due 2007	New York

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: None

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Exhibit Index on page 49. Glossary on page 58.

Aggregate market value of the voting stock held by non-affiliates of the registrant as of January 31, 2005 was \$8.7 billion.

Registrant's common stock outstanding as of January 31, 2005 was 235,610,601 shares.

DOCUMENTS INCORPORATED BY REFERENCE:

Portions of the 2004 Annual Report to Shareholders are incorporated by reference into Parts I, II, and IV.

Portions of the Proxy Statement prepared for the April 2005 annual meeting of shareholders are incorporated by reference into Part III.

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## INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report contains statements that are not historical fact and constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words "estimates," "believes," "expects," "anticipates," "plans," "intends," "may," "could," "would" and "should" or similar expressions, or discussions of strategy or of plans are intended to identify forward-looking statements. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Future results may differ materially from those expressed in these forward-looking statements.

Forward-looking statements are necessarily based upon various assumptions involving judgments with respect to the future and other risks, including, among others, local, regional, national and international economic, competitive, political, legislative and regulatory conditions and developments; actions by the California Public Utilities Commission, the California State Legislature, the California Department of Water Resources, and the Federal Energy Regulatory Commission and other regulatory bodies in the United States and other countries; capital markets conditions, inflation rates, interest rates and exchange rates; energy and trading markets, including the timing and extent of changes in commodity prices; the availability of natural gas; weather conditions and conservation efforts; war and terrorist attacks; business, regulatory, environmental and legal decisions and requirements; the status of deregulation of retail natural gas and electricity delivery; the timing and success of business development efforts; and other uncertainties, all of which are difficult to predict and many of which are beyond the control of the company. Readers are cautioned not to rely unduly on any forward-looking statements and are urged to review and consider carefully the risks, uncertainties and other factors which affect the company's business described in this report and other reports filed by the company from time to time with the Securities and Exchange Commission.

## PART I

## ITEM 1. BUSINESS

## Description of Business

A description of Sempra Energy and its subsidiaries (the company) is given in "Management's Discussion and Analysis of Financial Condition and Results of Operations" of the 2004 Annual Report to Shareholders, which is incorporated by reference. The company has four separately managed reportable segments comprised of Southern California Gas Company (SoCalGas), San Diego Gas & Electric (SDG&E), Sempra Commodities and Sempra Generation. SoCalGas and SDG&E are collectively referred to as "the California Utilities."

## Company Website

The company's website address is <http://www.sempra.com/investor.htm>. The company makes available free of charge through its website its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission. The charters of the audit, compensation and corporate governance committees of the company's board of directors' (the board), the board's corporate governance guidelines, and the code of business conduct and ethics for directors and officers are posted on the company's website. Printed copies may be obtained by writing to the company's Corporate Secretary at Sempra Energy, 101 Ash Street, San Diego, CA 92101-3017.

## RISK FACTORS

The following risk factors and all other information contained in this report should be considered carefully when evaluating Sempra Energy and its subsidiaries. These risk factors could affect the actual results of Sempra Energy and its subsidiaries and cause such results to differ materially from those expressed in any forward-looking statements of, or made by or on behalf of, Sempra Energy or its subsidiaries. Other risks and uncertainties, in addition to those that are described below, may also impair their business operations. If any of the following risks occurs, Sempra Energy's business, cash flows, results of operations and financial condition could be seriously harmed. In addition, the trading price of its securities could decline due to the occurrence of any of these risks. These risk factors should be read in conjunction with the other detailed information concerning Sempra Energy and its subsidiaries set forth in the notes to Consolidated Financial Statements and in "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in the 2004 Annual Report to Shareholders, which is incorporated by reference in this report.

#### Risks Related to the California Utilities

The California Utilities are subject to extensive regulation by state, federal and local legislation and regulatory authorities, which may adversely affect the operations, performance and growth of their businesses.

The California Public Utilities Commission (CPUC), which consists of five commissioners appointed by the Governor of California for staggered six-year terms, regulates the California Utilities' rates (except electric transmission rates, which are regulated by the Federal Energy Regulatory Commission (FERC)) and conditions of service, sales of securities, rates of return, rates of depreciation, uniform systems of accounts, examination of records and long-term resource procurement. The CPUC conducts various reviews of utility performance (including reasonableness and prudence reviews) and affiliate relationships and conducts audits and investigations into various matters which may, from time to time, result in disallowances and penalties adversely affecting earnings and cash flows. Various proceedings involving the CPUC and relating to the California Utilities' rates, costs, incentive mechanisms, performance-based regulation and compliance with affiliate and holding company rules are discussed in the notes to Consolidated Financial Statements and in "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Periodically, the California Utilities' rates are approved by the CPUC based on forecasts of capital and operating costs. If the California Utilities' actual capital and operating costs were to exceed the amount included in its base rates approved by the CPUC, it would adversely affect earnings and cash flows.

To promote efficient operations and improved productivity and to move away from reasonableness reviews and disallowances, the CPUC adopted Performance-Based Regulation (PBR) for the California Utilities. Under PBR, regulators require future income potential to be tied to achieving or exceeding specific performance and productivity goals, rather than relying solely on expanding utility plant to increase earnings. The three areas that are eligible for PBR rewards are: operational incentives based on measurements of safety, reliability and customer satisfaction; energy efficiency rewards based on the effectiveness of the programs; and natural gas procurement rewards. Although the California Utilities have received significant PBR rewards in the past, there can be no assurance that the California Utilities will receive rewards at similar levels in the future, or at all. Additionally, if the California Utilities fail to achieve certain minimum performance levels established under the PBR mechanisms, they may be assessed financial disallowances or penalties which could adversely affect their earnings and cash flows.

The FERC regulates electric transmission rates, the transmission and wholesale sales of electricity in interstate commerce, transmission access and other similar matters involving SDG&E.

The California Utilities may be impacted by new regulations, decisions, orders or interpretations of the CPUC, FERC or other regulatory bodies. New legislation, regulations, decisions, orders or interpretations could change how the California Utilities operate, could affect their

ability to recover their various costs through rates or adjustment mechanisms, or could require the California Utilities to incur additional expenses.

SDG&E may incur substantial costs and liabilities as a result of its ownership of nuclear facilities.

SDG&E owns a 20% interest in the San Onofre Nuclear Generating Station (SONGS), a 2,150 megawatt nuclear generating facility near San Clemente, California. The Nuclear Regulatory Commission (NRC) has broad authority under federal law to impose licensing and safety-related requirements for the operation of nuclear generation facilities. SDG&E's ownership interest in SONGS subjects it to the risks of nuclear generation, which include:

- \* the potential harmful effects on the environment and human health resulting from the operation of nuclear facilities and the storage, handling and disposal of radioactive materials;
- \* limitations on the amounts and types of insurance commercially available to cover losses that might arise in connection with nuclear operations; and
- \* uncertainties with respect to the technological and financial aspects of decommissioning nuclear plants at the end of their licensed lives.

The California Utilities' future results of operations and financial condition may be materially adversely affected by the outcome of pending litigation against them.

The California energy crisis of 2000 and 2001 has generated numerous lawsuits, governmental investigations and regulatory proceedings involving many energy companies, including Sempra Energy and the California Utilities. They are the remaining defendants in class action and individual antitrust and unfair competition lawsuits scheduled for a jury trial to begin in September 2005 in which the plaintiffs have asserted that they are entitled to recover \$24 billion in damages. Additional lawsuits have been filed by the Attorney General of Nevada and by others. They are also responding to an ongoing investigation being conducted by the California Attorney General and an ongoing CPUC proceeding related to the increase in natural gas prices at the California-Arizona border in 2000-2001. The California Utilities have expended and continue to expend substantial amounts defending these lawsuits and in connection with related investigations and regulatory proceedings. If these matters are ultimately resolved unfavorably to the California Utilities, their results of operations and financial condition and those of Sempra Energy may be materially adversely affected.

These proceedings are discussed in the notes to Consolidated Financial Statements and in "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Risks Related to Sempra Energy's Electric Generation, Commodities Trading, Liquefied Natural Gas (LNG), Pipelines & Storage and Other Businesses

Sempra Energy's businesses are exposed to market risk, and its financial condition, results of operations, cash flows and liquidity may be adversely affected by fluctuations in commodity market prices that are beyond its control.

Sempra Commodities is a full-service trading company that markets and trades physical and financial commodity products. Its trading portfolios consist of physical and financial commodity contracts, including contracts for natural gas, electricity, petroleum products, base metals and other commodities that are settled by the delivery of the commodity or cash. Although Sempra Commodities generally seeks to structure its trading contracts so that a substantial majority of its trading revenues are realizable within 24 months and strives to maintain appropriate hedging mechanisms for its trading book, Sempra Commodities may have substantial unhedged trading positions in the market, resulting from the management of its trading portfolios or from its inability to hedge, in whole or in part, particular risks.

Sempra Generation generates electricity that it sells under long-term contracts and into the spot market or other competitive markets. It purchases fuel for its power plants, consisting of natural gas and coal, and may also purchase electricity in the open market to satisfy its contractual obligations.

Sempra Energy's sales and results of operations could be adversely affected if the prevailing market prices for electricity, natural gas, coal or other commodities, whether procured for power plants or to satisfy contractual obligations with trading counterparties or customers, in regional markets and other competitive markets in which the company competes, change in a direction or manner that it has not anticipated and for which it has not provided through purchase or sale commitments or other hedging transactions.

Unanticipated changes in market prices for energy-related and other commodities result from multiple factors, including: weather conditions; seasonality; changes in demand; transmission or transportation constraints or inefficiencies; availability of competitively priced alternative energy sources; commodity production levels; actions by the Organization of the Petroleum Exporting Countries with respect to the supply of crude oil; federal, state and foreign energy and environmental regulation and legislation; natural disasters, wars, embargoes and other catastrophic events; and expropriation of assets by foreign countries.

In 2001 the FERC, which has jurisdiction over wholesale power and transmission rates, independent system operators and other entities that control transmission facilities or that administer wholesale power sales in some of the markets in which the company operates, imposed price limitations which resulted in unexpected moves in electricity prices. The FERC may impose additional price limitations, bidding rules and other mechanisms or terminate existing price limitations from time to time in the future. Any such action by the FERC may result in prices for electricity changing in an unanticipated direction or manner, and may

have an adverse effect on Sempra Energy's sales and results of operations.

Sempra Energy and its subsidiaries cannot and do not attempt to fully hedge their assets or positions against changes in commodity prices, and their hedging procedures may not work as planned.

To reduce financial exposure related to commodity price fluctuations, Sempra Energy's subsidiaries routinely enter into contracts to hedge a substantial portion of their purchase and sale commitments and inventories of electricity, natural gas, coal, crude oil and refined petroleum products, base metals and other commodities. As part of this strategy, they routinely utilize fixed-price, forward, physical purchase and sales contracts, futures, financial swaps and option contracts traded in the over-the-counter markets or on exchanges. However, the company does not cover the entire exposure of its assets or its positions to market price volatility and the coverage will vary over time. To the extent Sempra Energy's subsidiaries have unhedged positions, or if their hedging positions do not work as planned, fluctuating commodity prices could have a material adverse effect on Sempra Energy's business, results of operations, cash flows and financial condition.

Risk management procedures may not prevent losses.

Although Sempra Energy and its subsidiaries have risk management systems and control systems in place that use advanced methodologies to quantify and manage risk, these systems may not always prevent material losses. Risk management procedures may not always be followed or may not always work as planned. In addition, daily value-at-risk and loss limits are derived from historic price movements. If prices significantly or persistently deviate from historic prices, the limits may not protect the company from significant losses. As a result of these and other factors, there can be no assurances that Sempra Energy's risk management procedures will prevent losses that would negatively affect its business, results of operations, cash flows and financial condition.

A downgrade in Sempra Energy's credit ratings could negatively affect its commodities trading and other non-utility businesses.

If Sempra Energy's credit ratings were to be downgraded, the business prospects of its commodities trading and other non-utility businesses, which generally rely on the credit-worthiness of Sempra Energy, would be adversely affected. Sempra Commodities would be required to comply with various margin or other credit enhancement obligations under its trading and marketing contracts, substantially all of which are guaranteed by Sempra Energy, and it may be unable to continue to trade or able to do so only on less-favorable terms. To meet liquidity requirements, Sempra Energy and its subsidiaries maintain substantial unused committed lines of credit for which borrowings are available without regard to credit ratings. However, a ratings downgrade could require Sempra Energy to divert to Sempra Commodities all or a portion of the liquidity that these lines would otherwise provide for the expansion of Sempra Energy's other non-utility businesses. In addition, if these lines were to become unavailable or to be inadequate to meet margin or other credit enhancement requirements, Sempra Commodities' trading partners could exercise other remedies such as liquidating and netting their exposures to Sempra Commodities, making it more difficult or impossible for Sempra

Commodities to manage effectively its remaining trading positions or to continue its trading business, and Sempra Energy and its subsidiaries may not have sufficient liquidity to meet their obligations.

Sempra Energy's businesses depend on counterparties, customers and suppliers performing in accordance with their agreements, and any failure by them to perform could require the company to incur substantial expenses and expose it to commodity price risk and volatility, which could adversely affect Sempra Energy's liquidity, cash flows and results of operations.

Sempra Energy's subsidiaries are exposed to the risk that counterparties, customers and suppliers that owe money or commodities as a result of market transactions or other long-term agreements will not perform their obligations under such agreements. Should they fail to perform, the company may be required to acquire alternative hedging arrangements or to honor the underlying commitment at then-current market prices. In such event, Sempra Energy's subsidiaries may incur additional losses to the extent of amounts already paid to such counterparties or suppliers. In addition, the subsidiaries often extend credit to counterparties and customers. While the company performs significant credit analyses prior to extending credit, Sempra Energy and its subsidiaries are exposed to the risk that they may not be able to collect amounts owed to them.

If the Department of Water Resources (DWR) were to succeed in setting aside, or were to fail to perform its obligations under its long-term power contract with Sempra Generation, Sempra Energy's business, results of operations and cash flows will be materially adversely affected.

In 2001, Sempra Generation entered into a 10-year power sales agreement with the DWR, to supply up to 1,900 megawatts to the state. Sempra Energy expects the contract with the DWR will be a source of significant revenue over the 10-year period. The validity of the power sales agreement with the DWR has been the subject of extensive litigation between the parties before the FERC and in California courts. Sempra Generation has prevailed in all of these challenges to date, but the plaintiffs have appealed several of these rulings. If the DWR were to succeed in setting aside its obligations under the contract, or if the DWR fails or is unable to meet its contractual obligations on a timely basis, it could have a material adverse effect on Sempra Energy's business, results of operations, cash flows and financial condition. These proceedings are described in the notes to Consolidated Financial Statements and in "Management's Discussion and Analysis of Financial Condition and Results of Operations."

In the future, Sempra Energy's subsidiaries may elect not to or may not be able to enter into long-term supply and sales agreements or long-term firm capacity agreements for their projects, which would subject their sales to increased volatility and its businesses to increased competition.

The electric generation and wholesale power sales industries have become highly competitive. As more plants are built and competitive pressures increase, wholesale electricity prices become more volatile. Without the benefit of long-term power sales agreements, such as the 10-year power sales agreement between Sempra Generation and the DWR, Sempra Energy's sales will be subject to increased price volatility, and it may be unable



to sell the power generated by Sempra Generation's facilities or operate those facilities profitably.

Sempra LNG does not intend to commence significant construction of its proposed LNG terminals without first obtaining long-term LNG supply agreements that substantially reduce its exposure to changes in natural gas prices (through corresponding natural gas sales agreements or supply prices tied to prevailing natural gas prices or long-term firm capacity agreements) for a substantial portion of the processing capacity of these facilities. However, if these plans were to change and the company were to construct its terminals without the benefit of such arrangements, its sales would be subject to increased price volatility, and it may be unable to sell the services of its LNG facilities or to operate the facilities profitably. If the counterparties, customers or suppliers to one or more of the key agreements for the LNG facilities were to fail or become unable to meet their contractual obligations on a timely basis, it could have a significant negative impact on Sempra Energy's business, results of operations, cash flows and financial condition.

Business development activities may not be successful and projects under construction may not commence operation as scheduled, which could increase Sempra Energy's costs and impair its ability to recover its investments.

The acquisition, development and construction of electric generating facilities, LNG receiving terminals, and natural gas pipelines and storage facilities involve numerous risks. Sempra Energy and its subsidiaries may be required to expend significant sums for preliminary engineering, permitting, fuel supply, resource exploration, legal and other expenses before it can be established whether a project is feasible, economically attractive or capable of being built. Sempra Energy's success in developing a particular project is contingent upon, among other things, negotiation of satisfactory engineering, procurement and construction agreements, fuel supply and power sales contracts (for generating facilities), supply and natural gas sales agreements or firm capacity service agreements (for LNG receiving terminals and natural gas pipelines and storage facilities), receipt of required governmental permits and timely implementation and satisfactory completion of construction and, successful completion of a particular project may be adversely affected by unforeseen engineering problems, construction delays and contractor performance shortfalls, work stoppages, adverse weather conditions, environmental and geological conditions, and other factors. If the company is unable to complete the development of a facility, it typically will not be able to recover its investment in the project.

The operation of these facilities also involves many risks, including the breakdown or failure of generation or regasification and storage facilities or other equipment or processes, labor disputes, fuel interruption and operating performance below expected levels. In addition, weather-related incidents and other natural disasters can disrupt generation, regasification, storage and transmission systems. The occurrence of any of these events could lead to operating power plants below expected capacity levels, which may result in lost revenues or increased expenses, including higher maintenance costs and penalties, and could adversely affect Sempra Energy's business, cash flows and results of operations.

Competition among developers and operators of LNG terminals is rapidly increasing, which may adversely affect the profitability of Sempra LNG's proposed LNG terminals.

Although there are only a limited number of LNG terminal facilities operating in North America today, many companies have announced plans to develop LNG facilities to serve the North American market. Some of these competitors have more operating experience, more development experience, larger staffs and greater financial resources than the company. Industry analysts have predicted that, if all of the proposed LNG facilities in North America that have been announced by developers are actually built, there will likely be substantial excess capacity for such terminals in the near future. Excess capacity is likely to lead to decreased prices for such services. Although its proposed LNG facilities in Mexico and Louisiana are more advanced in the siting, permitting and regulatory approval processes than the proposed projects of many of its competitors, there can be no assurance that Sempra Energy will be able to maintain that advantage.

Sempra Energy's subsidiaries rely on transportation assets that they do not own or control to deliver electricity and natural gas.

Sempra Energy's subsidiaries depend on electric transmission lines, natural gas pipelines and other transportation facilities owned and operated by third parties to deliver the electricity and natural gas they sell to wholesale markets, to supply natural gas and coal to their electric generation facilities, and to provide retail energy services to customers. Sempra LNG also will rely on specialized LNG ships to transport LNG to its proposed LNG facilities and on natural gas pipelines to transport natural gas for customers of the facilities. If transportation is disrupted, or if capacity is inadequate, the ability of Sempra Energy's subsidiaries to sell and deliver their products and services may be hindered. As a result, they may be responsible for damages incurred by their customers, such as the additional cost of acquiring alternative supply at then-current spot market rates.

Sempra Energy's businesses require numerous permits and other governmental approvals from various federal, state, local and foreign governmental agencies, and any failure to obtain or maintain required permits or approvals could cause Sempra Energy's sales to decline and/or its costs to increase.

The acquisition, ownership and operation of electric generation facilities, LNG receiving terminals, and natural gas pipelines and storage facilities require numerous permits, approvals and certificates from federal, state, local and foreign governmental agencies. All of the existing and planned development projects of Sempra Energy's subsidiaries require multiple permits. They may not be able to obtain or maintain all required regulatory approvals. If there is a delay in obtaining any required regulatory approvals or if the company fails to obtain any required approvals or to comply with any applicable laws or regulations, it may not be able to operate its facilities, or it may be forced to incur additional costs.

Sempra Energy's businesses are subject to complex government regulations and may be adversely affected by changes in these regulations or in their interpretation or implementation.

In recent years, the regulatory environment applicable to the electric power and natural gas industries has undergone significant changes, on both federal and state levels, which have affected the nature of these industries and the manner in which their participants conduct their businesses. These changes are ongoing, and Sempra Energy cannot predict the future course of changes in this regulatory environment or the ultimate affect that this changing regulatory environment will have on its businesses. Moreover, existing regulations may be revised or reinterpreted, and new laws and regulations may be adopted or become applicable to the company and its facilities. Future changes in laws and regulations may have a detrimental effect on Sempra Energy's business, cash flows, financial condition and results of operations.

Sempra Energy's energy and commodity trading operations are subject to affiliate rules relating to transactions with the California Utilities. These businesses could be adversely affected by changes in these rules or by additional CPUC or FERC rules' further restricting their ability to sell electricity or natural gas or to trade with the California Utilities. Affiliate transaction rules also could require these businesses to obtain the prior approval of the CPUC before entering into any such transactions with the California Utilities. Any such restrictions or approval requirements could adversely affect the electric generation plants, natural gas pipelines, LNG receiving terminals, or trading operations of the company's subsidiaries.

Various proceedings, inquiries and investigations relating to the business activities of Sempra Generation and Sempra Commodities are currently pending before the FERC. A description of such proceedings, inquiries and investigations is provided in the notes to Consolidated Financial Statements and in "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Sempra Energy's businesses have significant environmental compliance costs, and future environmental compliance costs could adversely affect Sempra Energy's profitability.

Sempra Energy's subsidiaries are subject to extensive federal, state, local and foreign statutes, rules and regulations relating to environmental protection. They are required to obtain numerous governmental permits, licenses and other approvals to construct and operate their businesses. Additionally, to comply with these legal requirements, they must spend significant sums on environmental monitoring, pollution control equipment and emissions fees. The company also is generally responsible for all on-site liabilities associated with the environmental condition of its electric generation facilities and other energy projects which it has acquired or developed, regardless of when the liabilities arose and whether they are known or unknown. If Sempra Energy's subsidiaries fail to comply with applicable environmental laws, they may be subject to penalties, fines and/or curtailments of their operations.

The scope and effect of any new environmental laws and regulations, including their affects on operations, are difficult to predict. However,

increasing national and international concerns regarding global warming and proposed regulations regarding mercury, nitrogen oxide and sulfur dioxide emissions could result in requirements for additional pollution control equipment or significant emissions fees or taxes, particularly with respect to coal-fired generation facilities, that could adversely affect Sempra Generation. In addition, existing environmental regulations could be revised or reinterpreted and other new laws and regulations could be adopted or become applicable to the company and its facilities.

Sempra Energy's international businesses are exposed to different local, regulatory and business risks and challenges, which could have a material adverse effect on Sempra Energy's financial condition, cash flows and results of operations.

Sempra Energy subsidiaries currently have interests in electricity generation, natural gas transmission and LNG terminal projects in Mexico, and also have trading, marketing and risk management operations in Canada, Europe and Asia. Sempra Pipelines & Storage also has ownership interests in electricity and natural gas distribution businesses in Argentina, Chile and Peru. Developing infrastructure projects, owning energy assets and operating businesses in foreign jurisdictions subject the company to significant political and financial risks which vary by country, including:

- \* changes in foreign laws and regulations, including tax and environmental laws and regulations;
- \* changes in U.S. laws and regulations, including tax and environmental laws and regulations, related to foreign operations;
- \* high rates of inflation;
- \* changes in government policies or personnel;
- \* trade restrictions;
- \* limitations on U.S. company ownership in foreign countries;
- \* permitting and regulatory compliance;
- \* changes in labor supply and labor relations in operations outside the U.S.;
- \* adverse rulings by foreign courts or tribunals and difficulty in enforcing contractual rights in foreign jurisdictions; and
- \* general political, economic and business conditions.

Sempra Energy's international businesses also are subject to foreign currency risks. These risks arise from both volatility in foreign currency exchange rates and devaluations of foreign currencies. In such cases, an appreciation of the U.S. dollar against a local currency could reduce the amount of cash and income received from those foreign

subsidiaries. For example, the devaluation of the Argentine peso against the U.S. dollar in recent years (as well as the Argentine government's unilateral, retroactive abrogation of utility agreements in early 2002) has had a material adverse effect on Sempra Pipelines & Storage's two unconsolidated subsidiaries in Argentina. On September 6, 2002, Sempra Pipelines & Storage initiated arbitration proceedings under the 1994 Bilateral Investment Treaty between the U.S. and Argentina for recovery of the diminution of the value of its investments that has resulted from Argentine governmental actions. Sempra Pipelines & Storage has claimed damages of at least \$258 million in these proceedings, which are continuing. A description of legal proceedings relating to Sempra Pipelines & Storage's business operations in Argentina is provided in the notes to Consolidated Financial Statements. While Sempra Pipelines & Storage believes that it has contracts and other measures in place to mitigate its most significant foreign currency exchange risks, it has some exposure that is not fully mitigated.

#### Other Risks Related to the Company

Sempra Energy's cash flows, ability to pay dividends and ability to meet its debt obligations largely depend on the performance of its subsidiaries.

Sempra Energy is a holding company and conducts its operations entirely through its subsidiaries. Sempra Energy's California Utilities are its major source of liquidity. Funding of other business units' capital expenditures is largely dependent on the California Utilities' paying sufficient dividends to Sempra Energy, which depends on the sufficiency of utility earnings and cash flows in excess of utility needs. In addition, Sempra Energy's cash flows, ability to meet its obligations to creditors and its ability to pay dividends on its common stock are largely dependent upon the earnings of the subsidiaries and the distribution of such earnings to Sempra Energy in the form of dividends. The subsidiaries are separate and distinct legal entities and could be precluded from making such distributions under certain circumstances, including as a result of legislation or regulation or in times of financial distress.

Natural disasters, catastrophic accidents or acts of terrorism could materially adversely affect Sempra Energy's business, earnings and cash flows.

Like other major industrial facilities, Sempra Energy's generation plants (including SONGS), electric transmission facilities, LNG receiving terminals and storage facilities, chartered oil and LNG tankers and natural gas pipelines and storage facilities may be damaged by natural disasters, catastrophic accidents or acts of terrorism. Any such incidents could result in severe business disruptions, significant decreases in revenues or significant additional costs to the company, which could have a material adverse effect on Sempra Energy's earnings and cash flows. Given the nature and location of these facilities, any such incidents also could cause fires, leaks, explosions, spills or other significant damage to natural resources or property belonging to third parties, or personal injuries, which could lead to significant claims against Sempra Energy and its subsidiaries. Insurance coverage may become unavailable for certain of these risks and the insurance proceeds received for any loss of or damage to any of its facilities, or for any

loss of or damage to natural resources or property or personal injuries caused by its operations, may be insufficient to cover the company's losses or liabilities without materially adversely affecting the company's financial condition, earnings and cash flows.

#### GOVERNMENT REGULATION

The most significant government regulation affecting Sempra Energy is that affecting its utility subsidiaries.

##### California Utility Regulation

The CPUC, which consists of five commissioners appointed by the Governor of California for staggered six-year terms, regulates SDG&E's and SoCalGas' rates and conditions of service, sales of securities, rate of return, rates of depreciation, uniform systems of accounts, examination of records, and long-term resource procurement. The CPUC conducts various reviews of utility performance and conducts investigations into various matters, such as deregulation, competition and the environment, to determine its future policies. The CPUC also regulates the relationship of utilities with their holding companies and is currently conducting an investigation into this relationship. This investigation is further discussed in Note 15 of the notes to Consolidated Financial Statements.

The California Energy Commission (CEC) has discretion over electric demand forecasts for the state and for specific service territories. Based upon these forecasts, the CEC determines the need for additional energy sources and for conservation programs. The CEC sponsors alternative-energy research and development projects, promotes energy conservation programs and maintains a state-wide plan of action in case of energy shortages. In addition, the CEC certifies power-plant sites and related facilities within California.

The CEC conducts a 20-year forecast of supply availability and prices for every market sector consuming natural gas in California. This forecast includes resource evaluation, pipeline capacity needs, natural gas demand and wellhead prices, and costs of transportation and distribution. This analysis is used to support long-term investment decisions.

##### United States Utility Regulation

The FERC regulates the interstate sale and transportation of natural gas, the transmission and wholesale sales of electricity in interstate commerce, transmission access, the uniform systems of accounts, rates of depreciation and electric rates involving sales for resale. Both the FERC and the CPUC are currently investigating prices charged to the California investor-owned utilities (IOUs) by various suppliers of natural gas and electricity. Further discussion is provided in Notes 14 and 15 of the notes to Consolidated Financial Statements.

The NRC oversees the licensing, construction and operation of nuclear facilities. NRC regulations require extensive review of the safety, radiological and environmental aspects of these facilities. Periodically, the NRC requires that newly developed data and techniques be used to re-analyze the design of a nuclear power plant and, as a result, requires plant modifications as a condition of continued operation in some cases.

##### Local Regulation

SoCalGas has natural gas franchises with the 240 legal jurisdictions in its service territory. These franchises allow SoCalGas to locate, operate and maintain facilities for the transmission and distribution of natural gas in streets and other public places. Some franchises have fixed terms, such as that for the city of Los Angeles, which expires in 2012. The range of expiration dates for the franchises with definite terms is 2005 to 2048. Most of the franchises do not have fixed terms and continue indefinitely.

SDG&E has electric franchises with the two counties and the 26 cities in its electric service territory, and natural gas franchises with the one county and the 18 cities in its natural gas service territory. These franchises allow SDG&E to locate, operate and maintain facilities for the transmission and distribution of electricity and/or natural gas in streets and other public places. The franchises do not have fixed terms, except for the electric and natural gas franchises with the cities of Encinitas (2012), San Diego (2021), Coronado (2028) and Chula Vista (2014), and the natural gas franchises with the city of Escondido (2036) and the county of San Diego (2030).

Sempra Pipelines & Storage's Mexican subsidiaries, Distribuidora de Gas Natural (DGN) de Mexicali, DGN de Chihuahua and DGN de La Laguna Durango, build and operate natural gas distribution systems in Mexicali, Chihuahua and the La Laguna-Durango zone in north-central Mexico, respectively. These companies are regulated by city and state government labor and environmental agencies. They are also regulated by the Mexican energy regulatory commission.

##### Other Regulation

Sempra Commodities has trading locations in North America, Europe and Asia that are subject to regulation as to operations and financial position. Among other things, its operations are subject to the New York Mercantile Exchange, the London Metals Exchange, the Commodity Futures Trading Commission, the FERC and the National Futures Association.

Sempra LNG has operations in the United States that are subject to regulation by the FERC and operations in Mexico that are subject to regulation by the Mexican energy regulatory commission.

Sempra Pipelines & Storage's affiliates have international operations in Argentina, Chile, Mexico and Peru that are subject to federal, local and other regulations of the countries and/or political subdivisions in which they are located. These regulatory bodies include but are not limited to Mexico's Comision Reguladora de Energia, Argentina's Ente Naal Regulator de Gas, Chile's Comision Nacional de Energia and Peru's Consejo Nacional de Energia.

Other subsidiaries are also subject to varying amounts of regulation by various governments, including various states in the United States.

#### Licenses and Permits

The California Utilities obtain numerous permits, authorizations and licenses in connection with the transmission and distribution of natural gas and electricity. They require periodic renewal, which results in continuing regulation by the granting agency.

The company's unregulated affiliates are also required to obtain numerous permits, authorizations and licenses in the normal course of business. Some of these permits, authorizations and licenses require periodic renewal. Sempra Generation and its subsidiaries obtain a number of permits, authorizations and licenses in connection with the construction and operation of power generation facilities. In addition, Sempra Generation obtains permits in connection with wholesale distribution of electricity. Sempra Pipelines & Storage's Mexican subsidiaries obtain construction permits for their distribution systems from the local governments where the service is provided. Sempra Pipelines & Storage and Sempra Commodities obtain licenses and permits for natural gas storage facilities. Sempra LNG obtains licenses and permits for construction and operations of LNG facilities.

Other regulatory matters are described in Notes 14 and 15 of the notes to Consolidated Financial Statements.

#### SOURCES OF REVENUE

Industry segment information is contained in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Note 17 of the notes to Consolidated Financial Statements. Various information concerning revenue and revenue recognition is provided in Note 1 of the notes to Consolidated Financial Statements.

#### NATURAL GAS UTILITY OPERATIONS

##### Resource Planning and Natural Gas Procurement and Transportation

The company is engaged in the purchase, sale, distribution, storage and transportation of natural gas through the California Utilities. The company's resource planning, power procurement, contractual commitments and related regulatory matters are discussed below and in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Notes 15 and 16 of the notes to Consolidated Financial Statements.

##### Customers

For regulatory purposes, customers are separated into core and noncore customers. Core customers are primarily residential and small commercial and industrial customers, without alternative fuel capability. Noncore customers consist primarily of electric generation, wholesale, large commercial, industrial and enhanced oil recovery customers.

Most core customers purchase natural gas directly from the California Utilities. Core customers are permitted to aggregate their natural gas requirement and purchase directly from brokers or producers. The California Utilities continue to be obligated to purchase reliable supplies of natural gas to serve the requirements of the core customers.

#### Natural Gas Procurement and Transportation

Most of the natural gas purchased and delivered by the California Utilities is produced outside of California, primarily in the southwestern U.S. and Canada. The California Utilities purchase natural gas under short-term and long-term contracts. Short-term purchases are primarily based on monthly spot-market prices.

To ensure the delivery of the natural gas supplies to the distribution system and to meet the seasonal and annual needs of customers, SoCalGas is committed to firm pipeline capacity contracts that require the payment of fixed reservation charges to reserve firm transportation entitlements. SoCalGas sells excess capacity, if any, on a short-term basis. Interstate pipeline companies, primarily El Paso Natural Gas Company and Transwestern Pipeline Company, provide transportation services into SoCalGas' intrastate transmission system for supplies purchased by SoCalGas or its transportation customers from outside of California. All of these contracts will have expired by 2007. The rates that interstate pipeline companies may charge for natural gas and transportation services are regulated by the FERC.

SDG&E has long-term natural gas transportation contracts with various interstate pipelines that expire on various dates between 2005 and 2023. SDG&E currently purchases natural gas on a spot basis to fill its long-term pipeline capacity and purchases additional spot market supplies delivered directly to California for its remaining requirements. SDG&E continues its ongoing assessment of its pipeline capacity portfolio, including the release of a portion of this capacity to third parties. In accordance with regulatory directives, SDG&E will reconfigure its pipeline capacity portfolio by November 2005 to secure firm transportation rights from a diverse mix of U.S. and Canadian supply sources for its projected core customer natural gas requirements. All of SDG&E's natural gas is delivered through SoCalGas' pipelines under a short-term transportation agreement. In addition, under a separate agreement expiring in March 2006, SoCalGas provides SDG&E eight billion cubic feet of storage capacity.

According to "Btu's Daily Gas Wire", the annual average spot price of natural gas at the California/Arizona border was \$5.53 per million British thermal unit (mmbtu) in 2004 (\$6.35 per mmbtu in December 2004), compared with \$5.10 per mmbtu in 2003 and \$3.14 per mmbtu in 2002. Prices for natural gas increased toward the end of 2002, 2003 and in 2004. The California Utilities' weighted average cost (including transportation charges) per mmbtu of natural gas was \$5.94 in 2004, \$5.06 in 2003 and \$3.12 in 2002.

With improved delivery capacity to California, the company expects adequate resources to be available at prices that generally will follow national natural gas pricing trends and volatility.

#### Natural Gas Storage

SoCalGas provides natural gas storage services for use by the core, noncore and off-system customers. Core customers are allocated a portion of SoCalGas storage capacity. Remaining customers, including SDG&E, can bid and negotiate the desired amount of storage on a contract basis. The



storage service program provides opportunities for customers to store natural gas, usually during the summer, to reduce winter purchases when natural gas costs are generally higher. This allows customers to select the level of service they desire to assist them in managing their fuel procurement and transportation needs.

#### Demand for Natural Gas

The California Utilities face competition in the residential and commercial customer markets based on the customers' preferences for natural gas compared with other energy products. The demand for natural gas by electric generators is influenced by a number of factors. In the short-term, natural gas use by electric generators is impacted by the availability of alternative sources of generation. The availability of hydroelectricity is highly dependent on precipitation in the western United States. In addition, natural gas use is impacted by the performance of other generation sources in the western United States, including nuclear and coal, and other natural gas facilities outside the service area. Natural gas use is also impacted by changes in end-use electricity demand. For example, natural gas use generally increases during summer heat waves. Over the long-term, natural gas use will be greatly influenced by additional factors such as the location of new power plant construction. More generation capacity currently is being constructed outside Southern California than within the California Utilities' service area. This new generation will likely displace the output of older, less efficient local generation, reducing use of natural gas for local electric generation.

Effective March 31, 1998, electric industry restructuring provided out-of-state producers the option to purchase energy for California utility customers. As a result, natural gas demand for electric generation within Southern California competes with electric power generated throughout the western United States. Although electric industry restructuring has no direct impact on the California Utilities' natural gas operations, future volumes of natural gas transported for electric generating plant customers may be significantly affected to the extent that regulatory changes divert electric generation from the California Utilities' service area.

Growth in the natural gas markets is largely dependent upon the health and expansion of the Southern California economy and prices of other energy products. External factors such as weather, the price of electricity, electric deregulation, the use of hydroelectric power, competing pipelines and general economic conditions can result in significant shifts in demand and market price. The California Utilities added 86,000 and 83,000 new natural gas customer meters in 2004 and 2003, respectively, representing growth rates of 1.4 percent in both cases. The California Utilities expect that their growth rate for 2005 will approximate that for 2004.

In the interruptible industrial market, customers are capable of burning a fuel other than natural gas. Fuel oil is the most significant competing energy alternative. The company's ability to maintain its industrial market share is largely dependent on price. The relationship between natural gas supply and demand has the greatest impact on the price of the company's product. With the reduction of natural gas production from domestic sources, the cost of natural gas from non-domestic sources may

play a greater role in the company's competitive position in the future. The price of oil depends upon a number of factors, including the relationship between world-wide supply and demand, and the policies of foreign and domestic governments.

The natural gas distribution business is seasonal in nature as variations in weather conditions generally result in greater revenues during the winter months when temperatures are colder. As is prevalent in the industry, the company injects natural gas into storage during the summer months (usually April through October) for withdrawal from storage during the winter months (usually November through March) when customer demand is higher.

#### ELECTRIC UTILITY OPERATIONS

##### Customers

At December 31, 2004, SDG&E had 1.3 million meters consisting of 1,170,000 residential, 139,000 commercial, 460 industrial, 1,940 street and highway lighting, and 7,700 direct access. The company's service area covers 4,100 square miles. The company added 22,000 new electric customer meters in 2004 and 18,000 in 2003, representing growth rates of 1.7% and 1.4% respectively.

##### Resource Planning and Power Procurement

SDG&E's resource planning, power procurement and related regulatory matters are discussed below and in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Notes 14, 15 and 16 of the notes to Consolidated Financial Statements.



Under the contract with PGE, SDG&E pays a capacity charge plus a charge based on the amount of energy received and/or PGE's non-fuel costs. Costs under the contracts with QFs are based on SDG&E's avoided cost. Charges under the remaining contracts are for firm and as-available energy and are based on the amount of energy received. The prices under these contracts are at the market value at the time the contracts were negotiated.

#### SONGS

SDG&E owns 20 percent of the three nuclear units at SONGS (located south of San Clemente, California). The cities of Riverside and Anaheim own a total of 5 percent of Units 2 and 3. Southern California Edison (Edison) owns the remaining interests and operates the units.

Unit 1 was removed from service in November 1992 when the CPUC issued a decision to permanently shut it down. Decommissioning of Unit 1 is now in progress and its spent nuclear fuel is being stored on site.

Units 2 and 3 began commercial operation in August 1983 and April 1984, respectively. SDG&E's share of the capacity is 214 MW of Unit 2 and 216 MW of Unit 3.

SDG&E had fully recovered its SONGS capital investment through December 31, 2003.

Additional information concerning the SONGS units and nuclear decommissioning is provided below and in "Environmental Matters" herein, and in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Notes 7, 14 and 16 of the notes to Consolidated Financial Statements.

#### Nuclear Fuel Supply

The nuclear-fuel cycle includes services performed by others under various contracts through 2008, including mining and milling of uranium concentrate, conversion of uranium concentrate to uranium hexafluoride, enrichment services, and fabrication of fuel assemblies.

Spent fuel from SONGS is being stored on site, where storage capacity is expected to be adequate at least through 2022, the expiration date of the NRC operating license. Pursuant to the Nuclear Waste Policy Act of 1982, SDG&E entered into a contract with the U.S. Department of Energy (DOE) for spent-fuel disposal. Under the agreement, the DOE is responsible for the ultimate disposal of spent fuel. SDG&E pays a disposal fee of approximately \$1.00 per megawatt-hour of net nuclear generation, or \$3 million per year. The DOE projects that it will not begin accepting spent fuel until 2010 at the earliest.

To the extent not currently provided by the contracts, the availability and the cost of the various components of the nuclear-fuel cycle for SDG&E's nuclear facilities cannot be estimated at this time.

Additional information concerning nuclear-fuel costs and the storage and movement of spent fuel is provided in Notes 16 and 14, respectively, of the notes to Consolidated Financial Statements.

#### Power Pools

SDG&E is a participant in the Western Systems Power Pool, which includes an electric-power and transmission-rate agreement with utilities and power agencies located throughout the United States and Canada. More than 280 investor-owned and municipal utilities, state and federal power agencies, energy brokers, and power marketers share power and information in order to increase efficiency and competition in the bulk power market. Participants are able to make power transactions on standardized terms that have been pre-approved by FERC.

#### Transmission Arrangements

The Pacific Intertie, consisting of AC and DC transmission lines, connects the Northwest with SDG&E, Pacific Gas & Electric, Edison and others under an agreement that expires in July 2007. SDG&E's share of the Pacific Intertie is 266 MW.

SDG&E's 500-kilovolt Southwest Powerlink transmission line, which is shared with Arizona Public Service Company and Imperial Irrigation District, extends from Palo Verde, Arizona to San Diego. SDG&E's share of the line is 970 MW, although it can be less, depending on specific system conditions.

Mexico's Baja California Norte system is connected to SDG&E's system via two 230-kilovolt interconnections with firm capability of 408 MW in the north to south direction and 800 MW in the south to north direction.

Due to electric-industry restructuring, discussed in "Transmission Access" below, the operating rights of SDG&E on these lines have been transferred to the Independent System Operator (ISO).

#### Transmission Access

The FERC has established rules to implement the transmission-access provisions of the National Energy Policy Act of 1992. These rules specify procedures for others' requests for transmission service. The FERC approved the California IOUs' transfer of operation and control of their transmission facilities to the ISO in 1998. Additional information regarding the FERC, ISO and transmission issues are provided in Note 15 of the notes to Consolidated Financial Statements.

#### SEMPRA GLOBAL

Sempra Global consists of most of the businesses of Sempra Energy other than the California Utilities, and serves a broad range of customers' energy and other needs. Sempra Global includes Sempra Commodities, Sempra Generation, Sempra LNG, Sempra Pipelines & Storage and several smaller business units. A discussion of each of these business units is provided below.

Additional information concerning these and other aspects of the operations of Sempra Global and also of Sempra Financial is provided under "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Notes 2, 3 and 17 of the notes to Consolidated Financial Statements.

#### Sempra Commodities

Sempra Commodities is a wholesale and retail trader of physical and financial products, including natural gas, power, crude oil and other commodities, a trader and wholesaler of metals and an owner of synthetic fuel facilities that generate Section 29 income tax credits. Sempra Commodities combines trading, risk-management and physical commodity expertise to provide innovative solutions to its customers worldwide.

Sempra Commodities owns the rights to develop Bluewater Gas Storage, LLC, a natural gas storage facility in Michigan, and to utilize its capacity to store natural gas for customers who buy, sell or transport natural gas in Michigan. The Bluewater Gas Storage facility commenced commercial operations in May 2004.

During 2002, Sempra Commodities completed acquisitions that added base metals trading and warehousing to its trading business. In February 2002, Sempra Commodities completed the acquisition of London-based Sempra Metals Limited, a leading metals trader on the London Metals Exchange. In April 2002, Sempra Commodities completed the acquisitions of the assets of New York-based Sempra Metals & Concentrates Corp., a leading global trader of copper, lead and zinc concentrates; and of Henry Bath & Sons Limited, which provides warehousing services for non-ferrous metals in Europe and Asia; and the assets of the U.S. warehousing business of Henry Bath, Inc.

#### Sempra Generation

Sempra Generation primarily acquires, develops and operates power plants for the competitive market. It also provides energy services and facilities management, and owns mineral rights in properties that produce petroleum and natural gas.

In May 2001, Sempra Generation entered into a ten-year agreement with the DWR to supply up to 1,900 MW of power to California. Sempra Generation may, but is not obligated to, deliver this electricity from its portfolio of natural gas-fired plants in the western United States and Baja California, Mexico. If and when Sempra Generation uses these plants to supply the entire 1,900 MW, those sales would comprise more than two-thirds of the plants' capacity. Subsequent to the state's signing of this contract and electricity-supply contracts with other vendors, various state officials have contended that the rates called for by the contracts are too high. Based on current natural gas prices, the price of power under the long-term contracts exceeds the current spot market price for electricity. Although the contract is subject to ongoing litigation and regulatory proceedings, both Sempra Generation and the State of California are performing under this contract. Information concerning litigation regarding this contract, the FERC's orders upholding this contract and the pending appeal is provided in Note 16 of the notes to Consolidated Financial Statements.

In July 2004, Topaz Power Partners (Topaz), a 50/50 joint venture between Sempra Energy Partners and Carlyle/Riverstone, acquired ten Texas power plants from American Electric Power (AEP), including the 632-MW coal-fired Coletto Creek Power Station. The transaction included the acquisition of six operating power plants with generating capacity of

1,950 MW and four inactive power plants capable of generating 1,863 MW. Topaz has entered into several power sales agreements for 572 MW of Coletto Creek Power Station's capacity. This is discussed further in Note 3 of the notes to Consolidated Financial Statements.

In August 2003, Sempra Generation obtained approvals by the California Energy Commission for the company's 550 MW Palomar power plant in Escondido, California. In June 2004, SDG&E received CPUC approval of its plans to purchase the Palomar plant from Sempra Generation after construction is completed in 2006. Construction of the project began in July 2004.

The 1,250 MW Mesquite Power plant, located near Phoenix, Arizona, provides electricity to wholesale energy markets in the Southwest. The first phase of commercial operations (50 percent of the plant's total capacity) began in June 2003 and the second phase of commercial operations (the remaining 50 percent) began in December 2003. Further discussion of this is provided under "New Accounting Standards" in Note 1 of the notes to Consolidated Financial Statements.

During 2003, construction was completed on Termoelectrica de Mexicali (TDM), a 625 MW power plant near Mexicali, and the Elk Hills Power Project (Elk Hills), both of which commenced commercial operations in July 2003. TDM and Elk Hills are discussed further in Note 2 and Note 3, respectively, of the notes to Consolidated Financial Statements.

In October 2002, Sempra Generation purchased the 305 MW, coal-fired Twin Oaks power plant for \$120 million. Sempra Generation sells substantially all of the output of the plant under a five-year contract expiring on October 1, 2007. In connection with the acquisition, Sempra Generation also assumed a contract that includes annual commitments to purchase lignite coal for the plant until an aggregate minimum volume has been achieved or through 2025.

#### Sempra LNG

Sempra LNG is developing receipt terminals for LNG and supplies natural gas to Mexico's state-owned electric utility.

In January 2005, Sempra LNG was awarded a 15-year natural gas supply contract by Mexico's state-owned electric utility, Comision Federal de Electricidad (CFE). The contract is estimated at \$1.4 billion over its life and supports the CFE's future energy needs in northern Baja California, including the Presidente Juarez power plant in Rosarito, and it is anticipated that it will use natural gas processed at Energia Costa Azul. Starting in 2008 and running through 2022, the agreement provides the CFE with an average of about 130 million cubic feet per day of natural gas.

In October 2004, Sempra LNG signed a sale and purchase agreement with British Petroleum for the supply of 500 million cubic feet of gas a day from Indonesia's Tangguh liquefaction facility to Sempra LNG's Energia Costa Azul regasification terminal. The terminal is expected to cost between \$900 million and \$1 billion, including related pipeline costs. The 20-year agreement provides for pricing tied to the Southern California border index for natural gas and will supply half the capacity of Energia Costa Azul.

Also in October 2004, Sempra LNG entered into an agreement with Shell International Gas Limited (Shell) by which Shell has contracted to purchase half of the initial capacity of Energia Costa Azul for an initial period of 20 years. In December 2004, Sempra LNG entered into two additional contracts: one for the construction of the terminal and one for the construction of the project's breakwater.

In April 2004, Sempra LNG announced plans to develop and construct a new \$600 million LNG receiving terminal near Port Arthur, Texas. The terminal would be capable of processing 1.5 billion cubic feet (bcf) of natural gas per day and could be expanded to 3 bcf per day. The company is currently in the process of obtaining FERC approval for the construction of the terminal. The project is expected to begin construction in 2006, with start-up slated for 2009.

In April 2003, Sempra LNG completed its acquisition of the proposed Cameron LNG project in Hackberry, Louisiana from a subsidiary of Dynegey, Inc. The total cost of the project is expected to be \$700 million. The terminal is currently designed to supply 1.5 bcf of natural gas per day. The FERC approved the construction and operation of the project in September 2003. Construction is expected to begin in 2005 and commercial operations are expected to begin in 2008.

Additional discussion concerning these projects is provided in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Notes 2 and 16 of the notes to Consolidated Financial Statements.

#### Sempra Pipelines & Storage

Sempra Pipelines & Storage engages in energy-infrastructure projects in North and South America. It holds interests in companies that provide natural gas or electricity services to over 2.8 million customers in Argentina, Chile, Mexico and Peru; develops natural gas storage facilities; and owns two small natural gas distribution utilities in the eastern United States.

In July 2004, the company acquired the rights to develop a salt-cavern natural gas storage facility located in Calcasieu Parish, Louisiana. This facility, operating as Liberty Gas Storage (Liberty) is expected to have capacity of 17 bcf. Liberty is estimated to cost \$150 million and to begin operation in 2006.

In April 2004, the company acquired land and associated rights for the development of a salt-cavern natural gas storage facility in Evangeline Parish, Louisiana. This facility, operating as the Pine Prairie Energy Center, will consist of three salt caverns with a total capacity of 24 bcf of natural gas and is expected to cost \$175 million and to begin operations in 2006. The company is negotiating contracts to sell the capacity of this facility. FERC has issued a certificate of public convenience and necessity for the project and authorized Pine Prairie to charge market-based rates.

Also in April 2004, Sempra Pipelines & Storage and PSEG sold a portion of their interests in Luz del Sur S.A.A. (Luz Del Sur), a Peruvian electric utility. Each party had a 44-percent interest in Luz del Sur prior to the



sale and a 38-percent interest after the sale was completed. Sempra Pipelines & Storage recognized an after-tax gain of \$5 million as a result of the sale.

During the third quarter of 2003, Sempra Pipelines & Storage recorded a \$77 million before-tax write-down of the carrying value of the assets of Frontier Energy, a small North Carolina utility subsidiary, as a result of reductions in actual and previously anticipated sales of natural gas by the utility.

Sempra Pipelines & Storage's Mexican subsidiaries build and operate natural gas distribution systems in Mexicali, Chihuahua and the La Laguna-Durango zone in north-central Mexico. In February 2003, Sempra Pipelines & Storage purchased the remaining minority interests in its Mexican subsidiaries.

In 2002, Sempra Pipelines & Storage completed construction of the 140-mile Gasoducto Bajanorte Pipeline that connects the Rosarito Pipeline south of Tijuana, Mexico with a TransCanada pipeline that connects to Arizona. Sempra Pipelines & Storage continues to incur costs for the development of a spur line connecting the Energia Costa Azul terminal to Gasoducto Bajanorte and for the expansion of the pipeline.

Additional discussion concerning these projects is provided in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Notes 2, 3 and 16 of the notes to Consolidated Financial Statements.

#### Sempra Financial

Sempra Financial invests as a limited partner in affordable-housing properties. Its portfolio includes 1,300 properties throughout the U.S. that are expected to provide income tax benefits (primarily from income tax credits) over 10-year periods.

In July 2004, Sempra Financial sold its investment in an enterprise that earns Section 29 income tax credits. That investment comprised one-third of Sempra Energy's Section 29 participation, the rest being held by Sempra Commodities, and was sold because the company's alternative minimum tax position defers utilization of the credits in the determination of income taxes currently payable. The transaction has been accounted for under the cost-recovery method, whereby future proceeds in excess of the carrying value of the investment will be recorded as income when they are received. As a result of this sale, Sempra Financial will not be receiving Section 29 income tax credits in the future.

#### RATES AND REGULATION -- CALIFORNIA UTILITIES

Information concerning rates and regulations applicable to the California Utilities is provided in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Notes 1, 14 and 15 of the notes to Consolidated Financial Statements.

## ENVIRONMENTAL MATTERS

Discussions about environmental issues affecting the company are included in Note 16 of the notes to Consolidated Financial Statements. The following additional information should be read in conjunction with those discussions.

## Hazardous Substances

In 1994, the CPUC approved the Hazardous Waste Collaborative Memorandum account, allowing California's IOUs to recover their hazardous waste cleanup costs, including those related to Superfund sites or similar sites requiring cleanup. Cleanup costs at sites related to electric generation were specifically excluded from the collaborative by the CPUC. Recovery of 90 percent of hazardous waste cleanup costs and related third-party litigation costs, and 70 percent of the related insurance-litigation expenses is permitted. In addition, the company has the opportunity to retain a percentage of any insurance recoveries to offset the 10 percent of costs not recovered in rates.

During the early 1900s, the California Utilities and their predecessors manufactured gas from coal or oil. The manufactured-gas plants (MGPs) often have become contaminated with the hazardous residual by-products of the process. SoCalGas has identified 42 such sites at which it (together with other users as to 21 of these sites) may have cleanup obligations. At a minimum, preliminary investigations have been completed on 41 of the sites. As of December 31, 2004, 27 of these sites have been remediated, of which 22 have received certification from the California Environmental Protection Agency. At December 31, 2004, SoCalGas' estimated remaining investigation and remediation liability for the MGPs is \$40.5 million. SDG&E identified three former MGPs, two of which were remediated in 1998 and 2000, with closure letters being received. The estimated remaining remediation liability on the third site is \$1.8 million.

SDG&E sold its fossil-fuel generating facilities in 1999. As a part of its due diligence for the sale, SDG&E conducted a thorough environmental assessment of the facilities. Pursuant to the sale agreements for such facilities, SDG&E and the buyers have apportioned responsibility for such environmental conditions generally based on contamination existing at the time of transfer and the cleanup level necessary for the continued use of the sites as industrial sites. While the sites are relatively clean, the assessments identified some instances of significant contamination, principally resulting from hydrocarbon releases, for which SDG&E has a cleanup obligation under the agreement. Estimated costs to perform the necessary remediation are \$11 million. These costs were offset against the sales price for the facilities, together with other appropriate costs, and the remaining net proceeds were included in the calculation of customer rates. Remediation of the plants commenced in early 2001. During 2002, cleanup was completed at several minor sites at a cost of \$0.4 million. In late 2002, additional assessments were started at the primary sites, where cleanup commenced in 2003 and is expected to be completed during 2005. In 2003, cleanup was completed at the Encina power plant site at a cost of \$0.8 million. In 2004, cleanup was completed at two combustion turbine sites at a cost of \$0.7 million.

The California Utilities lawfully dispose of wastes at permitted facilities owned and operated by other entities. Operations at these

facilities may result in actual or threatened risks to the environment or public health. Under California law, businesses that arrange for legal disposal of wastes at a permitted facility from which wastes are later released, or threaten to be released, can be held financially responsible for corrective actions at the facility.

The company and certain subsidiaries are named as potentially responsible parties (PRPs) for one landfill site and two industrial waste disposal sites, from which releases have occurred.

Remedial actions and negotiations with other PRPs and the United States Environmental Protection Agency have been in progress since 1993 for the Casmalia landfill site. The company's share of costs to remediate this site is estimated to be \$1.3 million, of which \$0.9 million has been spent.

In December 1999, SoCalGas was notified that it is a PRP at a waste treatment facility in Bakersfield, California. SoCalGas is working with other PRPs in order to remove from the site certain liquid wastes that threaten to be released. SoCalGas' share of total site cleanup costs is estimated at \$0.7 million, of which \$0.2 million has been spent.

The company and 10 other entities have been named PRPs by the Department of Toxic Substance Control (DTSC) as liable for any required corrective action regarding contamination at an industrial waste disposal site in Pico Rivera, California. DTSC has taken this action because SDG&E and others sold used transformers to the site's owner. SDG&E and the other PRPs have entered into a cost-sharing agreement to provide funding for the implementation of a consent order between DTSC and the site owner for the development of a cleanup plan. SDG&E's interim share under the agreement is 10 percent, subject to adjustment based on allocations of responsibility. The total estimate for all PRPs is \$1 million for the development of the cleanup plan and \$2 million to \$8 million for the actual cleanup. Since inception, SDG&E's share of the cleanup expenses and plan development was \$0.2 million. Cleanup is expected to commence in 2005.

At December 31, 2004, the company's estimated remaining investigation and remediation liability related to hazardous waste sites, including the MGPs, was \$44.6 million, of which 90 percent is authorized to be recovered through the Hazardous Waste Collaborative mechanism. This estimated cost excludes remediation costs associated with SDG&E's former fossil-fuel power plants. The company believes that any costs not ultimately recovered through rates, insurance or other means will not have a material adverse effect on the company's consolidated results of operations or financial position.

Estimated liabilities for environmental remediation are recorded when amounts are probable and estimable. Amounts authorized to be recovered in rates under the Hazardous Waste Collaborative mechanism are recorded as a regulatory asset.

#### Electric and Magnetic Fields (EMFs)

Although scientists continue to research the possibility that exposure to EMFs causes adverse health effects, science has not demonstrated a cause-and-effect relationship between exposure to the type of EMFs emitted by

power lines and other electrical facilities and adverse health effects. Some laboratory studies suggest that such exposure creates biological effects, but those effects have not been shown to be harmful. The studies that have most concerned the public are epidemiological studies, some of which have reported a weak correlation between the proximity of homes to certain power lines and equipment and childhood leukemia. Other epidemiological studies found no correlation between estimated exposure and any disease. Scientists cannot explain why some studies using estimates of past exposure report correlations between estimated EMF levels and disease, while others do not.

To respond to public concerns, the CPUC has directed California IOUs to adopt a low-cost EMF-reduction policy that requires reasonable design changes to achieve noticeable reduction of EMF levels that are anticipated from new projects. However, consistent with the major scientific reviews of the available research literature, the CPUC has indicated that no health risk has been identified. During 2004, the CPUC instituted a rulemaking to re-examine its policies related to EMFs and determine whether the current mitigation policies and utility directives should be updated in light of science that has developed over the last decade.

#### Air and Water Quality

California's air quality standards are more restrictive than federal standards. However, as a result of the sale of the company's fossil-fuel generating facilities, the company's primary air-quality issue, compliance with these standards now has had less significance to the company's operation. That is changing as Sempra Generation operates more generating facilities.

The transmission and distribution of natural gas require the operation of compressor stations, which are subject to increasingly stringent air-quality standards. Costs to comply with these standards are recovered in rates.

In connection with the issuance of operating permits, SDG&E and the other owners of SONGS previously reached agreement with the California Coastal Commission to mitigate the environmental damage to the marine environment attributed to the cooling-water discharge from SONGS Units 2 and 3. This mitigation program includes an enhanced fish-protection system, a 150-acre artificial kelp reef and restoration of 150 acres of coastal wetlands. In addition, the owners must deposit \$3.6 million with the state for the enhancement of fish hatchery programs and pay for monitoring and oversight of the mitigation projects. SDG&E's share of the cost is estimated to be \$34 million. These mitigation projects are expected to be completed in 2008. Through December 31, 2003, SONGS mitigation costs were recovered through the Incremental Cost Incentive Pricing mechanism. SONGS mitigation costs incurred after December 31, 2003, are being capitalized and recovered from ratepayers over the remaining life of the SONGS units, subject to CPUC approval in the Edison rate case. Additional information on SONGS cost recovery is provided in Note 14 of the notes to Consolidated Financial Statements.

## OTHER MATTERS

## Research, Development and Demonstration (RD&amp;D)

The SoCalGas RD&D portfolio is focused in five major areas: operations, utilization systems, power generation, public interest and transportation. Each of these activities provides benefits to customers and society by providing more cost-effective, efficient natural gas equipment with lower emissions, increased safety and reduced operating costs. The CPUC has authorized SoCalGas to recover its operating costs associated with RD&D. SoCalGas' annual RD&D costs have averaged \$8.2 million over the past three years.

For 2004, the CPUC authorized SDG&E to fund \$1.2 million and \$5.7 million for its natural gas and electric RD&D programs, respectively, including \$5.7 million to the CEC for its PIER (Public Interest Energy Research) Program. SDG&E's annual RD&D costs have averaged \$6.5 million over the past three years.

## Employees of Registrant

As of December 31, 2004, the company had 13,381 employees, compared to 12,807 at December 31, 2003.

## Labor Relations

Field, technical and most clerical employees at SoCalGas are represented by the Utility Workers' Union of America (UWUA) or the International Chemical Workers' Union Council (ICWUC). The collective bargaining agreement for field, technical and most clerical employees at SoCalGas covering wages, hours, working conditions, medical and various benefit plans was in effect through December 31, 2004. SoCalGas has signed with UWUA and ICWUC a new collective bargaining agreement that will be in effect from January 1, 2005 through September 30, 2008.

Certain employees at SDG&E are represented by the Local 465 International Brotherhood of Electrical Workers. The current contract is in effect through August 31, 2008.

At some of its field job sites, Sempra Generation employs mechanics who are represented by the International Union of Operating Engineers, Local 501. One collective bargaining agreement is through November 1, 2006, and the other through July 7, 2007.

## ITEM 2. PROPERTIES

## Electric Properties - SDG&amp;E

SDG&E's interest in SONGS is described in "Electric Resources" herein. At December 31, 2004, SDG&E's electric transmission and distribution facilities included substations, and overhead and underground lines. The electric facilities are located in San Diego, Imperial and Orange counties and in Arizona, and consist of 1,814 miles of transmission lines and 21,433 miles of distribution lines. Periodically, various areas of the service territory require expansion to accommodate customer growth.

## Natural Gas Properties - California Utilities

At December 31, 2004, the California Utilities' natural gas facilities included 2,996 miles of transmission and storage pipeline, 55,276 miles of distribution pipeline and 52,109 miles of service piping. They also included 13 transmission compressor stations and 4 underground storage reservoirs, with a combined working capacity of 122 bcf.

## Energy Properties - Other

At December 31, 2004, Sempra Generation operated power plants in California, Arizona, Texas, Nevada and Mexico with total capacity of 3,670 MW. Additional information is provided in Notes 2 and 3 of the notes to Consolidated Financial Statements.

At December 31, 2004, Sempra Pipelines & Storage's operations in Mexico included 1,704 miles of distribution pipeline, 165 miles of transmission pipeline and one compressor station.

At December 31, 2004, the company's two small natural gas utilities, Frontier Energy and Bangor Gas, located in North Carolina and Maine, respectively, owned 147 miles of transmission lines and 230 miles of distribution lines.

## Other Properties

The 21-story corporate headquarters building at 101 Ash Street, San Diego is occupied pursuant to a capital lease that expires in 2015. The lease has two separate five-year renewal options.

SoCalGas leases approximately half of a 52-story office building in downtown Los Angeles through 2011. The lease has six separate five-year renewal options.

SDG&E occupies an office complex in San Diego pursuant to an operating lease ending in 2007. The lease can be renewed for two five-year periods.

Sempra Global leases office facilities at various locations in the U.S., Mexico and Europe with the leases ending from 2005 to 2027. Sempra LNG owns land to develop an LNG receiving terminal in Baja California, Mexico. Sempra LNG also has a land lease to develop an LNG receiving terminal in Hackberry, Louisiana. In December 2004, Sempra LNG renewed the land lease for another five-year period. In April 2004, the company acquired land and associated rights to develop a natural gas storage facility in Evangeline Parish, Louisiana that is part of Sempra Pipelines & Storage. In addition, Sempra Commodities owns the rights to develop a natural gas storage facility in St. Clair, Michigan.

The company owns or leases other offices, operating and maintenance centers, shops, service facilities and equipment necessary in the conduct of its business.

## ITEM 3. LEGAL PROCEEDINGS

SDG&E and the County of San Diego are continuing to negotiate the remaining terms of a settlement relating to alleged environmental law violations by SDG&E and its contractors in connection with the abatement of asbestos-containing materials during the demolition of a natural gas storage facility in 2001. SDG&E expects that any settlement with the County would involve payments by SDG&E of less than \$750,000. In January 2005, Sempra Energy and SDG&E received a grand jury subpoena from the United States Attorney's Office in San Diego seeking documents related to this matter. The companies are fully cooperating with the investigation.

Except for the matters described above, in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and in Notes 14, 15 and 16 of the notes to Consolidated Financial Statements, neither the company nor its subsidiaries are party to, nor is their property the subject of, any material pending legal proceedings other than routine litigation incidental to their businesses.

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Sempra Energy common stock is traded on the New York and Pacific stock exchanges. In addition to the shares held by intermediaries, there were 57,000 holders of record of the company's common stock at January 31, 2005. The quarterly common stock information required by Item 5 is included in the schedule of Quarterly Financial Data of the 2004 Annual Report to Shareholders.

## EQUITY COMPENSATION PLANS

The company's 1998 Long Term Incentive Plan and Employee Stock Incentive Plan permit the compensation committee of the board of directors to grant to officers and key employees a wide variety of equity and equity-based incentive awards relating to common stock. At December 31, 2004, outstanding awards consisted of stock options and restricted stock held by 344 employees.

The company's Non-employee Directors Stock Plan also provides for annual automatic grants to non-employee directors of options to purchase common stock.

The following table sets forth information regarding these plans at December 31, 2004.

Equity Compensation Plan Information

	Number of shares to be issued upon exercise of outstanding options (A)	Weighted- average exercise price of outstanding options	Number of additional shares remaining available for future issuance
-----			
Equity compensation plans approved by shareholders:			
-----			
1998 Long Term Incentive Plan	11,998,342	\$ 23.92	5,321,240 (B) (C) (D)
Non-employee Directors Stock Plan	570,000	\$ 25.54	876,360
Equity compensation plans not approved by shareholders:			
-----			
Employee Stock Incentive Plan	506,375	\$ 24.38	8,161,030 (B) (C)
-----			

(A) Consists solely of options to purchase common stock, all of which were granted at an exercise price of 100% of the grant date fair market value of the shares subject to the option.

(B) Excludes shares subject to outstanding stock options and those subject to other outstanding awards, consisting of unvested shares of restricted stock which total 2,051,800 shares for the 1998 Long Term Incentive Plan and 767,900 shares for the Employee Stock Incentive Plan.

(C) The number of shares available for future issuance is increased by the number of shares received in payment of the exercise price or withheld to satisfy related tax withholding obligations relating to awards and by the number of shares subject to awards that lapse, expire or are otherwise terminated or settled other than by the issuance of shares.

(D) The number of shares available for future issuance also is increased at the beginning of each year by 1.5% of the total number of shares of common stock then outstanding.



## ITEM 6. SELECTED FINANCIAL DATA

(Dollars in millions, except per share data)  
At December 31, or for the years then ended -

	2004	2003	2002	2001	2000
<b>Income Statement Data:</b>					
Operating revenues	\$ 9,410	\$ 7,887	\$ 6,048	\$ 7,720	\$ 6,760
Operating income	\$ 1,272	\$ 939	\$ 987	\$ 997	\$ 884
Income from continuing operations before extraordinary item and cumulative effect of changes in accounting principles	\$ 926	\$ 695	\$ 575	\$ 518	\$ 429
Net income	\$ 649	\$ 591	\$ 518	\$ 429	\$ 429
<b>Balance Sheet Data: Total assets</b>					
	\$23,643	\$21,900	\$20,242	\$17,378	\$17,850
Long-term debt	\$ 4,192	\$ 3,841	\$ 4,083	\$ 3,436	\$ 3,260
Short-term debt (a)	\$ 903	\$ 1,461	\$ 851	\$ 1,117	\$ 926
Trust preferred securities	\$ 200	\$ 200	\$ 200	\$ 200	\$ 200
Shareholders' equity	\$ 4,865	\$ 3,890	\$ 2,825	\$ 2,692	\$ 2,494
<b>Per Common Share Data:</b>					
Income from continuing operations before extraordinary item and cumulative effect of changes in accounting principles	\$ 4.03	\$ 3.29	\$ 2.80	\$ 2.54	\$ 2.06
Diluted	\$ 3.03	\$ 3.24	\$ 2.79	\$ 2.52	\$ 2.06
Net income	\$ 3.02	\$ 3.07	\$ 2.88	\$ 2.54	\$ 2.06
Diluted	\$ 2.82	\$ 3.03	\$ 2.87	\$ 2.52	\$ 2.06
Dividends declared	\$ 1.00	\$ 1.00	\$ 1.00	\$ 1.00	\$ 1.00
Book value	\$ 20.77	\$ 17.17	\$ 13.79	\$ 13.16	\$ 12.35

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

~~(a)  
includes  
long term  
debt due  
within one  
year.†  
Amount has  
been  
reclassified  
to Due to  
Unconsolidated  
Affiliates  
effective in  
2003.~~

This data should be read in conjunction with the Consolidated Financial Statements and the notes to Consolidated Financial Statements.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The information required by Item 7 is incorporated by reference from pages 1 through 32 of the 2004 Annual Report to Shareholders.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information required by Item 7A is incorporated by reference from pages 24 through 27 of the 2004 Annual Report to Shareholders.

## ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The information required by Item 8 is incorporated by reference from pages 37 through 112 of the 2004 Annual Report to Shareholders. Item 15(a)1 includes a listing of financial statements included in the 2004 Annual Report to Shareholders.

## ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES

None.

## ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures - Management has established disclosure controls and procedures to ensure that material information relating to the company and its consolidated subsidiaries is made known to the officers who certify the company's financial reports and to other members of senior management and the Board of Directors. In designing and evaluating these controls and procedures, management recognizes that any system of controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired objectives and necessarily applies judgment in evaluating the cost-benefit relationship of other possible controls and procedures.

Based on their evaluation as of December 31, 2004, the principal executive officer and principal financial officer of the company have concluded that the company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) are effective, at the reasonable assurance level, to ensure that the information required to be disclosed by the company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified by SEC rules and forms.

Management's Report on Internal Control Over Financial Reporting - Company management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Exchange Act Rule 13a-15(f). Under the supervision and with the participation of company management, including the principal executive officer and principal financial officer, the company conducted an evaluation of the effectiveness of its internal control over financial reporting based on the framework in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on the company's evaluation under the framework in Internal Control - Integrated Framework, management concluded that the company's internal control over financial reporting was effective as of December 31, 2004. Management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2004 has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in its report, which is included herein.

## ITEM 9B. OTHER INFORMATION

In February 2005, Sempra Energy entered into a severance pay agreement with each of its executive officers (other than Stephen L. Baum, Donald E. Felsing and Neal E. Schmale whose continuing employment and employment-related agreements have been previously filed with the Securities and Exchange Commission) to replace the previously reported agreements. The agreements are for an initial term of three years and are subject to automatic one year extensions on each anniversary of the effective date (commencing with the second anniversary) unless Sempra Energy or the executive elects not to extend the term.

The agreements provide severance benefits to the executive in the event that Sempra Energy or its subsidiaries terminates the executive's employment (other than for cause, death or disability) or the executive does so for good reason.

Severance benefits under the agreements vary with the executive's position and include (i) a lump sum cash severance payment varying from 50% to 100% of the sum of the executive's annual base salary plus the greater of the executive's average annual bonus or average annual target bonus for the two years prior to termination; (ii) continuation of health insurance benefits for a period varying from six months to one year; and (iii) financial planning and outplacement services for a period varying from 18 months to two years. If the termination were to occur within two years after a change in control of the company, (i) the lump sum cash severance payment would be multiplied by two; (ii) an additional lump sum payment would be paid equal to the pro rata portion for the year of termination of the target amount payable under any annual incentive compensation award for that year or, if greater, the average of the three highest gross annual bonus awards paid to the executive in the five years preceding the year of termination; (iii) all equity-based incentive compensation awards would immediately vest and become exercisable or payable and any restrictions on the awards would automatically lapse; (iv) a lump sum cash payment would be made equal to the present value of the executive's benefits under supplemental executive retirement plans calculated on the basis of the greater of actual years of service or years of service that would have been completed upon attaining age 62 and applying certain early retirement factors; (v) life, disability, accident and health insurance benefits would be continued for a period varying from one year to two years; and (vi) financial planning and outplacement services would be provided for a period varying from two years to three years.

The agreements also provide that if the terminated executive agrees to provide consulting services for two years and abide by certain covenants regarding non-solicitation of employees and information confidentiality, the executive would receive (i) an additional lump sum payment equal to the executive's annual base salary and the greater of the executive's target bonus for the year of termination or the average of the two or three highest gross annual bonus awards paid to the executive in the five years prior to termination and (ii) health insurance benefits would be continued for an additional one year.

The agreements also provide for a gross-up payment to offset the effects of any excise tax imposed on the executive under Section 4999 of the Internal Revenue Code.

Good reason is defined in the agreements to include the assignment to the executive of duties materially inconsistent with those appropriate to a senior executive of Sempra Energy and its subsidiaries; a material reduction in the executive's overall standing and responsibilities within Sempra Energy and its subsidiaries; and a material reduction in the executive's annualized compensation and benefit opportunities other than across-the-board reductions affecting all similarly situated executives of comparable rank. Following a change in control, good reason is defined to include an adverse change in the executive's title, authority, duties, responsibilities or reporting lines; reduction in the executive's annualized compensation opportunities other than across-the-board reductions of less than 10% similarly affecting all similarly situated executives of comparable rank; relocation of the executive's principal place of employment by more than 30 miles; and a substantial increase in business travel obligations. A change in control is defined to include the acquisition by one person or group of 20% or more of the voting power of Sempra Energy's shares; the election of a new majority of the board of Sempra Energy comprised of individuals who are not recommended for election by two-thirds of the current directors or successors to the current directors who were so recommended for election; certain mergers, consolidations or sales of assets that result in the shareholders of Sempra Energy owning less than 60% of the voting power of Sempra Energy or of the surviving entity or its parent; and approval by shareholders of the liquidation or dissolution of the company.

## PART III

## ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information required on Identification of Directors is incorporated by reference from "Election of Directors" in the Proxy Statement prepared for the April 2005 annual meeting of shareholders. The information required on the company's executive officers is provided below.

## EXECUTIVE OFFICERS OF THE REGISTRANT

Name	Age*	Position
Stephen L. Baum	63	Chairman and Chief Executive Officer
Donald E. Felsingner	57	President and Chief Operating Officer
Edwin A. Guiles	55	Group President, Sempra Energy Utilities
Mark A. Snell	48	Group President, Sempra Global Enterprises
M. Javade Chaudhri	52	Executive Vice President and General Counsel
Neal E. Schmale	58	Executive Vice President and Chief Financial Officer
Frank H. Ault	60	Senior Vice President and Controller
G. Joyce Rowland	50	Senior Vice President, Human Resources

\* As of December 31, 2004.

Each Executive Officer has been an officer of the company or one of its subsidiaries for more than five years, with the exception of Mr. Chaudhri. Prior to joining the company in 2003, Mr. Chaudhri was Senior Vice President and General Counsel of Gateway, Inc.

In June 2004, the company announced a succession plan whereby Donald E. Felsingner became president and chief operating officer, effective June 9, 2004, and will become chairman and chief executive officer in January 2006, when Steven L. Baum retires. At that time, Neal E. Schmale, currently the company's chief financial officer, will become president and chief operating officer.

## ITEM 11. EXECUTIVE COMPENSATION

The information required by Item 11 is incorporated by reference from "Election of Directors" and "Executive Compensation" in the Proxy Statement prepared for the April 2005 annual meeting of shareholders.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT  
AND RELATED STOCKHOLDER MATTERS

Securities Authorized for Issuance Under Equity Compensation Plans

Information regarding securities authorized for issuance under equity compensation plans is set forth in Item 5 herein.

Additional discussion of stock-based compensation is provided in Note 10 of the notes to Consolidated Financial Statements.

Security Ownership of Certain Beneficial Owners

The security ownership information required by Item 12 is incorporated by reference from "Share Ownership" in the Proxy Statement prepared for the April 2005 annual meeting of shareholders.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

None.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Information regarding principal accountant fees and services as required by Item 14 is incorporated by reference from "Proposal 3: Ratification of Independent Auditors" in the Proxy Statement prepared for the April 2005 annual meeting of shareholders.

## PART IV

## ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) The following documents are filed as part of this report:

## 1. Financial statements

	Page in Annual Report*
Management's Responsibility for Financial Statements . . .	33
Management's Report on Internal Control Over Financial Reporting . . . . .	33
Reports of Independent Registered Public Accounting Firm .	34
Statements of Consolidated Income for the years ended December 31, 2004, 2003 and 2002 . . . . .	37
Consolidated Balance Sheets at December 31, 2004 and 2003. . . . .	38
Statements of Consolidated Cash Flows for the years ended December 31, 2004, 2003 and 2002 . . . . .	40
Statements of Consolidated Changes in Shareholders' Equity for the years ended December 31, 2004, 2003 and 2002 . . . . .	42
Notes to Consolidated Financial Statements . . . . .	43

\*Incorporated by reference from the indicated pages of the 2004 Annual Report to Shareholders.

## 2. Financial statement schedules

The following document may be found in this report at the indicated page number.

Schedule I--Condensed Financial Information of Parent. . . 44

Any other schedules for which provision is made in Regulation S-X are not required under the instructions contained therein or are inapplicable.



### 3. Exhibits

See Exhibit Index on page 49 of this report.

#### (b) Reports on Form 8-K

The following reports on Form 8-K were filed after September 30, 2004:

Current Report on Form 8-K filed October 27, 2004, discussing the current status of the California Utilities' Cost of Service Proceedings and the Border Price Investigation.

Current Report on Form 8-K filed November 4, 2004, filing as an exhibit Sempra Energy's press release of November 4, 2004, giving the financial results for the quarter ended September 30, 2004.

Current Report on Form 8-K filed November 5, 2004, discussing the current status of the California Utilities' Cost of Service Proceedings, including a proposed decision and an alternate proposed decision issued by CPUC commissioners on November 4, 2004.

Current Report on Form 8-K filed November 17, 2004, discussing the current status of the Border Price Investigation, including the proposed decision issued by the CPUC Administrative Law Judge on November 16, 2004.

Current Report on Form 8-K filed December 3, 2004, discussing the current status of the California Utilities' Cost of Service Proceedings, including the CPUC decision issued on December 2, 2004.

Current Report on Form 8-K filed December 7, 2004, discussing and filing as an exhibit the 2005 Deferred Compensation Plan and announcing the impending retirement of directors Hyla H. Berteau and Herbert L. Carter.

Current Report on Form 8-K filed December 17, 2004, discussing the Sempra Energy/Sempra Energy LNG \$1.25 billion five-year credit agreement and discussing the current status of the Border Price Investigation.

Current Report on Form 8-K filed January 11, 2005, discussing the current status of energy crisis litigation.

Current Report on Form 8-K filed January 18, 2005, discussing the current status of energy crisis litigation.

Current Report on Form 8-K filed February 8, 2005, announcing that Sempra Energy had raised its earnings-per-share estimate for 2004 to approximately \$3.80, from its previous guidance of \$3.15 to \$3.25, filing as an exhibit Sempra Energy's press release of February 8, 2005.

Current Report on Form 8-K filed February 23, 2005, filing as an exhibit Sempra Energy's press release of February 23, 2005, giving the financial results for the three months ended December 31, 2004.

## CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM AND REPORT ON SCHEDULES

To the Board of Directors and Shareholders of Sempra Energy:

We consent to the incorporation by reference in Registration Statement Numbers 333-51309, 333-52192, 333-70640 and 333-103588 on Form S-3 and Registration Statement Numbers 333-56161, 333-50806, 333-49732 and 333-121073 on Form S-8 of Sempra Energy of our reports dated February 22, 2005 (which reports express an unqualified opinion and include an explanatory paragraph relating to the Company's adoption of Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations, effective January 1, 2003, and Financial Accounting Standards Board Interpretation No. 46, Consolidation of Variable Interest Entities an Interpretation of ARB No. 51, effective December 31, 2003) relating to the financial statements of Sempra Energy and management's report on the effectiveness of internal control over financial reporting, incorporated by reference in this Annual Report on Form 10-K of Sempra Energy for the year ended December 31, 2004.

Our audits of the financial statements referred to in our aforementioned report also included the financial statement schedule of Sempra Energy, listed in Item 15. This financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion based on our audits. In our opinion, such financial statement schedule, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects, the information set forth therein.

/S/ DELOITTE & TOUCHE LLP

San Diego, California  
February 22, 2005

## Schedule I -- CONDENSED FINANCIAL INFORMATION OF PARENT

## SEMPRA ENERGY

Condensed Statements of Income  
(Dollars in millions, except per share amounts)

Years ended December 31, 2004 2003 2002 ----- -----
Interest income \$ 166 \$ 122 \$ 53
Interest expense (202) (187) (134) Trust preferred distributions (9) (10)
Operating expenses and other (52) (17) (15)
Income tax benefits 92 57 28
-----
Loss before subsidiary earnings 7 (34) (76)
Subsidiary earnings before extraordinary item and cumulative effect of changes in accounting principles 913 729 651
-----
Income from continuing operations 929 695 575
Loss from discontinued operations and disposal of discontinued operations (25)
-----
Income before extraordinary item and cumulative effect of changes in accounting principles 905 695 575
Extraordinary item, net of tax 16
-----
Income before cumulative effect of changes in accounting principles 905 695 591
Cumulative effect of changes in accounting principles, net of tax (46)
-----
Net income \$ 895 \$ 649 \$ 591 -----
-----
Basic earnings per share:
Income from continuing operations \$ 4.83 \$ 3.29 \$ 2.80
Discontinued operations, net of tax (0.11)
Extraordinary item, net of tax
0.00
Cumulative effect of changes in

accounting  
principles,  
net of tax  
(0.22)

Net income \$  
2.92 \$ 3.07  
\$ 2.88

Weighted  
average  
number of  
shares  
outstanding  
(thousands)  
228,271  
211,740  
208,003

Diluted  
earnings per  
share  
Income from  
continuing  
operations \$  
0.93 \$ 3.24  
\$ 2.79

Discontinued  
operations,  
net of tax  
(0.10)

Extraordinary  
item, net of  
tax  
0.00

Cumulative  
effect of  
changes in  
accounting  
principles,  
net of tax  
(0.21)

Net income \$  
2.83 \$ 3.03  
\$ 2.87

Weighted  
average  
number of  
shares  
outstanding  
(thousands)  
223,852  
214,482  
206,062

## SEMPRA ENERGY

Condensed Balance Sheets  
(Dollars in millions)December 31,  
2004 2003 --

-----	
--- Assets:	
Cash and	
cash	
equivalents	
9,220	9,510
Due from	
affiliates	
116,521	116,521
Other	
current	
assets	
25,413	
-----	
Total	
current	
assets	
164,154	
Investments	
in	
subsidiaries	
6,320	5,510
Due from	
affiliates	
2,701	2,521
Other assets	
813,462	
-----	
Total	
assets	
\$	
10,000	\$
9,655	
-----	

-----	
Liabilities	
and	
Shareholders'	
Equity:	
Current	
portion of	
long term	
debt	
\$	\$
301	301
Income	
taxes	
payable	
524	524
Due to	
affiliates	
288	288
Other	
current	
liabilities	
1,623	1,403
-----	
Total	
current	
liabilities	
2,664	2,394
Long term	
debt	
2,224	2,224
Due to	
affiliate	
1,000	1,000
Other	
long term	
liabilities	
255	271
Shareholders'	
equity	
4,065	3,890
-----	

-----	
Total	
liabilities	
and	
shareholders'	
equity	
\$	
10,000	\$
9,655	
-----	

## SEMPRA ENERGY

Condensed Statements of Cash Flows  
(Dollars in millions)

Years ended December 31, 2004 2003 2002 ----- -----		
	<del>Net cash</del>	
	provided by (used	
	in) operating	
	activities \$ (71)	
	\$ (60) \$ 145	
	-----	
	Dividends	
	received from	
	subsidiaries 200	
	250 100	
	Expenditures for	
	property, plant	
	and equipment	
	(10) (4) (12)	
	Increase in	
	investments and	
	other assets (2)	
	(3) (20)	
	-----	
	Cash provided by	
	investing	
	activities 100	
	243 60	
	-----	
	Common stock	
	dividends paid	
	(195) (192) (201)	
	Repurchase of	
	common stock (5)	
	(7) (17)	
	Issuances of	
	common stock 110	
	505 0	
	Issuances	
	of long term debt	
	625 400 600	
	Payment on long	
	term debt (511)	
	(26) Loans to	
	affiliates net	
	(174) (829) (620)	
	Other (3) (4)	
	(19)	
	-----	
	Cash used in	
	financing	
	activities (153)	
	(127) (262)	
	-----	
	Increase (decrease)	
	in cash and cash	
	equivalents (26)	
	56 (69) Cash and	
	cash equivalents,	
	January 1 59 3 72	
	-----	
	Cash and	
	cash equivalents,	
	December 31 \$ 23	
	\$ 59 \$ 3	
	-----	

SEMPRA ENERGY  
 Note to Condensed Financial Statements

Long-term Debt

(Dollars in millions)	December 31,	
	2004	2003
Other long-term debt		
5.60% equity units May 17, 2007*	\$ 600	\$ 600
7.95% notes March 1, 2010	200	500
Notes at variable rates after fixed-to-floating swap March 1, 2010 (5.97% at December 31, 2004)	300	--
6.95% notes December 1, 2005	300	300
6.0% notes due February 1, 2013	400	400
4.75% notes due May 15, 2009	300	--
Notes at variable rates (2.82% at December 31, 2004) May 21, 2008 Employee Stock Ownership Plan	300	--
Bonds at 4.213% November 1, 2014	82	82
Bonds at variable rates (3.00% at December 31, 2004) November 1, 2014	33	19
Notes payable at variable rates after a fixed-to-floating rate swap July 1, 2004	--	500
Capitalized leases	1	3
Market value adjustments for interest rate swaps - net (expires March 1, 2010)	11	23
Total	2,527	2,427
Less:		
Current portion of long-term debt	(301)	(525)
Unamortized discount on long-term debt	(2)	(2)
Total	\$2,224	\$1,900

\*4.62% after remarketing in February 2005.

Excluding capital leases and market value adjustments for interest-rate swaps, maturities of long-term debt are \$300 million in 2005, \$600 million in 2007, \$300 million in 2008, \$300 million 2009 and \$1 billion thereafter.

Additional information on Sempra Energy's long-term debt is provided in Note 6 of the notes to Consolidated Financial Statements.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, hereunto duly authorized.

SEMPRA ENERGY

By: /s/ Stephen L. Baum

Stephen L. Baum  
Chairman and  
Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report is signed below by the following persons on behalf of the Registrant in the capacities and on the dates indicated.

Name/Title	Signature	Date
Principal Executive Officer	Stephen L. Baum	February 10, 2005
Chairman and Chief Executive Officer	/s/ Stephen L. Baum	February 10, 2005
Principal Financial Officer	Neal E. Schmale	February 10, 2005
Vice President and Chief Financial Officer	/s/ Neal E. Schmale	February 10, 2005
Principal Accounting Officer	Frank H. Ault	February 10, 2005
Vice President and Controller	/s/ Frank H. Ault	February 10, 2005
Director	Stephen L. Baum	February 10, 2005
Chairman	/s/ Stephen L. Baum	February 10, 2005
Director	Hyle H. Bertea	February 10, 2005
Director	/s/ Hyle H. Bertea	February 10, 2005
Director	James G. Brocksmith	February 10, 2005
Director	/s/ James G. Brocksmith	February 10, 2005
Director	Herbert L. Carter	February 10, 2005
Director	/s/ Herbert L. Carter	February 10, 2005
Director	Richard A. Collato	February 10, 2005
Director	/s/ Richard A. Collato	February 10, 2005
Director	Donald E. Felsing	February 10, 2005
Director	/s/ Donald E. Felsing	February 10, 2005
Director	Denise K. Fletcher	February 10, 2005



Director  
/s/ Denise  
Kr  
Fletcher  
February  
10, 2005  
Wilford D.  
Gedbold,  
Jr.,  
Director  
/s/  
Wilford D.  
Gedbold,  
Jr.,  
February  
10, 2005  
William D.  
Jones,  
Director  
/s/  
William D.  
Jones  
February  
10, 2005  
Richard C.  
Newman,  
Director  
/s/  
Richard C.  
Newman  
February  
10, 2005  
William C.  
Ouchi,  
Director  
/s/  
William C.  
Ouchi  
February  
10, 2005  
William C.  
Ruonaek,  
Director  
/s/  
William C.  
Ruonaek  
February  
10, 2005  
William F.  
Rutledge,  
Director  
/s/  
William F.  
Rutledge  
February  
10, 2005  
Neal E.  
Schmale,  
Director  
/s/ Neal  
E. Schmale  
February  
10, 2005

## EXHIBIT INDEX

The Forms 8, 8-B/A, 8-K, S-4, 10-K and 10-Q referred to herein were filed under Commission File Number 1-14201 (Sempra Energy), Commission File Number 1-40 (Pacific Enterprises), Commission File Number 1-3779 (San Diego Gas & Electric), Commission File Number 1-1402 (Southern California Gas Company), Commission File Number 1-11439 (Enova Corporation) and/or Commission File Number 333-30761 (SDG&E Funding LLC).

3.a The following exhibits relate to Sempra Energy and its subsidiaries

Exhibit 1 -- Underwriting Agreements

Enova Corporation and San Diego Gas & Electric Company

1.01 Underwriting Agreement dated December 4, 1997 (Incorporated by reference from Form 8-K filed by SDG&E Funding LLC on December 23, 1997, Exhibit 1.1).

Exhibit 3 -- Bylaws and Articles of Incorporation

Bylaws

Sempra Energy

3.01 Amended and Restated Bylaws of Sempra Energy effective May 26, 1998 (Incorporated by reference from the Registration Statement on Form S-8 Sempra Energy Registration No. 333-56161 dated June 5, 1998 (Exhibit 3.2)).

Articles of Incorporation

Sempra Energy

3.02 Amended and Restated Articles of Incorporation of Sempra Energy (Incorporated by reference to the Registration Statement on Form S-3 File No. 333-51309 dated April 29, 1998, Exhibit 3.1).

Exhibit 4 -- Instruments Defining the Rights of Security Holders, Including Indentures

The company agrees to furnish a copy of each such instrument to the Commission upon request.

Enova Corporation and San Diego Gas & Electric Company

4.01 Mortgage and Deed of Trust dated July 1, 1940. (Incorporated by reference from SDG&E Registration No. 2-49810, Exhibit 2A.)

4.02 Second Supplemental Indenture dated as of March 1, 1948. (Incorporated by reference from SDG&E Registration No. 2-49810, Exhibit 2C.)

4.03 Ninth Supplemental Indenture dated as of August 1, 1968.

(Incorporated by reference from SDG&E Registration No. 2-68420, Exhibit 2D.)

- 4.04 Tenth Supplemental Indenture dated as of December 1, 1968.  
(Incorporated by reference from SDG&E Registration No. 2-36042, Exhibit 2K.)
- 4.05 Sixteenth Supplemental Indenture dated August 28, 1975.  
(Incorporated by reference from SDG&E Registration No. 2-68420, Exhibit 2E.)
- 4.06 Thirtieth Supplemental Indenture dated September 28, 1983.  
(Incorporated by reference from SDG&E Registration No. 33-34017, Exhibit 4.3.)
- 4.07 Forty-Ninth Supplemental Indenture dated June 1, 2004.

Pacific Enterprises and Southern California Gas

- 4.08 First Mortgage Indenture of Southern California Gas Company to American Trust Company dated as of October 1, 1940 (Registration Statement No. 2-4504 filed by Southern California Gas Company on September 16, 1940, Exhibit B-4).
- 4.09 Supplemental Indenture of Southern California Gas Company to American Trust Company dated as of July 1, 1947 (Registration Statement No. 2-7072 filed by Southern California Gas Company on March 15, 1947, Exhibit B-5).
- 4.10 Supplemental Indenture of Southern California Gas Company to American Trust Company dated as of August 1, 1955 (Registration Statement No. 2-11997 filed by Pacific Lighting Corporation on October 26, 1955, Exhibit 4.07).
- 4.11 Supplemental Indenture of Southern California Gas Company to American Trust Company dated as of June 1, 1956 (Registration Statement No. 2-12456 filed by Southern California Gas Company on April 23, 1956, Exhibit 2.08).
- 4.12 Supplemental Indenture of Southern California Gas Company to Wells Fargo Bank, National Association dated as of August 1, 1972 (Registration Statement No. 2-59832 filed by Southern California Gas Company on September 6, 1977, Exhibit 2.19).
- 4.13 Supplemental Indenture of Southern California Gas Company to Wells Fargo Bank, National Association dated as of May 1, 1976 (Registration Statement No. 2-56034 filed by Southern California Gas Company on April 14, 1976, Exhibit 2.20).
- 4.14 Supplemental Indenture of Southern California Gas Company to Wells Fargo Bank, National Association dated as of September 15, 1981 (Pacific Enterprises 1981 Form 10-K, Exhibit 4.25).
- 4.15 Supplemental Indenture of Southern California Gas Company to Manufacturers Hanover Trust Company of California, successor to Wells Fargo Bank, National Association, and Crocker National Bank

as Successor Trustee dated as of May 18, 1984 (Southern California Gas Company 1984 Form 10-K, Exhibit 4.29).

- 4.16 Supplemental Indenture of Southern California Gas Company to Bankers Trust Company of California, N.A., successor to Wells Fargo Bank, National Association dated as of January 15, 1988 (Pacific Enterprises 1987 Form 10-K, Exhibit 4.11).
- 4.17 Supplemental Indenture of Southern California Gas Company to First Trust of California, National Association, successor to Bankers Trust Company of California, N.A. dated as of August 15, 1992 (Registration Statement No. 33-50826 filed by Southern California Gas Company on August 13, 1992, Exhibit 4.37).
- 4.18 Supplemental Indenture of Southern California Gas Company to U.S. Bank, N.A., successor to First Trust of California, N.A., dated as of October 1, 2002. (Sempra Energy 2002 Form 10-K, Exhibit 4.17).
- 4.19 Supplemental Indenture of Southern California Gas Company to U.S. Bank, N.A., successor to First Trust of California, N.A., dated as of October 17, 2003.
- 4.20 Supplemental Indenture of Southern California Gas Company to U.S. Bank, N.A., successor to First Trust of California, N.A., Dated as of December 15, 2003.
- 4.21 Supplemental Indenture of Southern California gas Company to U.S. Bank, N.A., successor to First Trust of California, N.A., Dated as of December 10, 2004.

Exhibit 10 -- Material Contracts (Previously filed exhibits are incorporated by reference from Forms 8-K, S-4, 10-K or 10-Q as referenced below).

Sempra Energy

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- 10.01 Energy Purchase Agreement between Sempra Energy Resources and the California Department of Water Resources, executed May 4, 2001 (2001 Form 10-K, Exhibit 10.01).
- 10.02 Form of Employment Agreement between Sempra Energy and Stephen L. Baum (September 30, 2002 Form 10-Q, Exhibit 10.1).
- 10.03 Amendment to Employment Agreement, effective December 1, 1998 (Employment agreement, dated as of October 12, 1996 between Mineral Energy Company and Stephen L. Baum (Enova 8-K filed October 15, 1996, Exhibit 10.2)) (1998 Form 10-K, Exhibit 10.01).
- 10.04 Form of Employment Agreement between Sempra Energy and Donald E. Felsing (September 30, 2002 Form 10-Q, Exhibit 10.2).
- 10.05 Amendment to Employment Agreement effective December 1, 1998 (Employment contract, dated as of October 12, 1996 between Mineral Energy Company and Donald E. Felsing (Enova 8-K filed

October 15, 1996, Exhibit 10.4)) (1998 Form 10-K, Exhibit 10.03).

Enova Corporation and San Diego Gas & Electric Company

- 
- 10.06 Operating Agreement between San Diego Gas & Electric and the California Department of Water Resources dated April 17, 2003 (Sempra Energy 2003 10-K, Exhibit 10.06).
  - 10.07 Servicing Agreement between San Diego Gas & Electric and the California Department of Water Resources dated December 19, 2002 (Sempra Energy 2003 10-K, Exhibit 10.07).
  - 10.08 Transition Property Purchase and Sale Agreement dated December 16, 1997 (Incorporated by reference from Form 8-K filed by SDG&E Funding LLC on December 23, 1997, Exhibit 10.1).
  - 10.09 Transition Property Servicing Agreement dated December 16, 1997 (Incorporated by reference from Form 8-K filed by SDG&E Funding LLC on December 23, 1997, Exhibit 10.2).

Compensation

Sempra Energy

- 
- 10.10 Form of Sempra Energy Severance Pay Agreement.
  - 10.11 Sempra Energy 2005 Deferred Compensation Plan (8-K filed on December 07, 2004, Exhibit 10.1).
  - 10.12 Sempra Energy Employee Stock Incentive Plan (September 30, 2004 Form 10-Q, Exhibit 10.1).
  - 10.13 Sempra Energy Amended and Restated Executive Life Insurance Plan (September 30, 2004 Form 10-Q, Exhibit 10.2).
  - 10.14 Sempra Energy Excess Cash Balance Plan (September 30, 2004 Form 10-Q, Exhibit 10.3).
  - 10.15 Form of Sempra Energy 1998 Long Term Incentive Plan Performance-Based Restricted Stock Award (September 30, 2004 Form 10-Q, Exhibit 10.4).
  - 10.16 Form of Sempra Energy 1998 Long Term Incentive Plan Nonqualified Stock Option Agreement (September 30, 2004 Form 10-Q, Exhibit 10.5).
  - 10.17 Form of Sempra Energy 1998 Non-Employee Directors' Stock Plan Nonqualified Stock Option Agreement (September 30, 2004 Form 10-Q, Exhibit 10.6).
  - 10.18 Sempra Energy Supplemental Executive Retirement Plan (September 30, 2004 Form 10-Q, Exhibit 10.7).
  - 10.19 Neal Schmale Restricted Stock Award Agreement (September 30, 2004 Form 10-Q, Exhibit 10.8).
  - 10.20 Severance Pay Agreement between Sempra Energy and

Donald E. Felsing (September 30, 2004 Form 10-Q, Exhibit 10.9).

- 10.21 Severance Pay Agreement between Sempra Energy and Neal Schmale (September 30, 2004 Form 10-Q, Exhibit 10.10).
- 10.22 Sempra Energy Executive Personal Financial Planning Program Policy Document (September 30, 2004 Form 10-Q, Exhibit 10.11).
- 10.23 2003 Sempra Energy Executive Incentive Plan B. (2003 Form 10-K, Exhibit 10.10).
- 10.24 2003 Executive Incentive Plan (June 30, 2003 Form 10-Q, Exhibit 10.1).
- 10.25 Amended 1998 Long-Term Incentive Plan (June 30, 2003 Form 10-Q, Exhibit 10.2).
- 10.26 Sempra Energy Executive Incentive Plan effective January 1, 2003 (2002 Form 10-K, Exhibit 10.09).
- 10.27 Amended Sempra Energy Retirement Plan for Directors (2002 Form 10-K, Exhibit 10.10).
- 10.28 Amended and Restated Sempra Energy Deferred Compensation and Excess Savings Plan (September 30, 2002 Form 10-Q, Exhibit 10.3).
- 10.29 Form of Sempra Energy Severance Pay Agreement for Executives (2001 Form 10-K, Exhibit 10.07).
- 10.30 Sempra Energy Executive Security Bonus Plan effective January 1, 2001 (2001 Form 10-K, Exhibit 10.08).
- 10.31 Sempra Energy Deferred Compensation and Excess Savings Plan effective January 1, 2000 (2000 Form 10-K, Exhibit 10.07).
- 10.32 Sempra Energy 1998 Long Term Incentive Plan (Incorporated by reference from the Registration Statement on Form S-8 Sempra Energy Registration No. 333-56161 dated June 5, 1998, Exhibit 4.1).
- 10.33 Sempra Energy 1998 Non-Employee Directors' Stock Plan (Incorporated by reference from the Registration Statement on Form S-8 Sempra Energy Registration No. 333-56161 dated June 5, 1998, Exhibit 4.2).

#### Financing

##### Enova Corporation and San Diego Gas & Electric

-----

- 10.34 Loan agreement with the City of Chula Vista in connection with the issuance of \$25 million of Industrial Development Bonds, dated as of October 1, 1997 (Enova 1997 Form 10-K, Exhibit 10.34).
- 10.35 Loan agreement with the City of Chula Vista in connection

with the issuance of \$38.9 million of Industrial Development Bonds, dated as of August 1, 1996 (Enova 1996 Form 10-K, Exhibit 10.31).

- 10.36 Loan agreement with the City of Chula Vista in connection with the issuance of \$60 million of Industrial Development Bonds, dated as of November 1, 1996 (Enova 1996 Form 10-K, Exhibit 10.32).
- 10.37 Loan agreement with the City of San Diego in connection with the issuance of \$92.9 million of Industrial Development Bonds 1993 Series C dated as of July 1, 1993 (June 30, 1993 SDG&E Form 10-Q, Exhibit 10.2).
- 10.38 Loan agreement with the City of San Diego in connection with the issuance of \$70.8 million of Industrial Development Bonds 1993 Series A dated as of April 1, 1993 (March 31, 1993 SDG&E Form 10-Q, Exhibit 10.3).
- 10.39 Loan agreement with the City of Chula Vista in connection with the issuance of \$250 million of Industrial Development Bonds, dated as of December 1, 1992 (1992 SDG&E Form 10-K, Exhibit 10.5).
- 10.40 Loan agreement with the California Pollution Control Financing Authority in connection with the issuance of \$129.82 million of Pollution Control Bonds, dated as of June 1, 1996 (Enova 1996 Form 10-K, Exhibit 10.41).
- 10.41 Loan agreement with the California Pollution Control Financing Authority in connection with the issuance of \$60 million of Pollution Control Bonds, dated as of June 1, 1993 (June 30, 1993 SDG&E Form 10-Q, Exhibit 10.1).
- 10.42 Loan agreement with the California Pollution Control Financing Authority, dated as of December 1, 1991, in connection with the issuance of \$14.4 million of Pollution Control Bonds (1991 SDG&E Form 10-K, Exhibit 10.11).
- 10.43 Loan agreement with the City of Chula Vista in connection with the issuance of \$251.3 million of Industrial Revenue Refunding Bonds, dated as of June 1, 2004.

#### Natural Gas Transportation

##### Enova Corporation and San Diego Gas & Electric

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- 10.44 Amendment to Firm Transportation Service Agreement, dated December 2, 1996, between Pacific Gas and Electric Company and San Diego Gas & Electric Company (1997 Enova Corporation Form 10-K, Exhibit 10.58).
- 10.45 Firm Transportation Service Agreement, dated December 31, 1991 between Pacific Gas and Electric Company and San Diego Gas & Electric Company (1991 SDG&E Form 10-K, Exhibit 10.7).

- 10.46 Firm Transportation Service Agreement, dated October 13, 1994 between Pacific Gas Transmission Company and San Diego Gas & Electric Company (1997 Enova Corporation Form 10-K, Exhibit 10.60).

## Nuclear

## Enova Corporation and San Diego Gas &amp; Electric

- 
- 10.47 Nuclear Facilities Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station, approved November 25, 1987 (1992 SDG&E Form 10-K, Exhibit 10.7).
- 10.48 Amendment No. 1 to the Qualified CPUC Decommissioning Master Trust Agreement dated September 22, 1994 (see Exhibit 10.47 herein) (1994 SDG&E Form 10-K, Exhibit 10.56).
- 10.49 Second Amendment to the San Diego Gas & Electric Company Nuclear Facilities Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station (see Exhibit 10.47 herein) (1994 SDG&E Form 10-K, Exhibit 10.57).
- 10.50 Third Amendment to the San Diego Gas & Electric Company Nuclear Facilities Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station (see Exhibit 10.47 herein) (1996 SDG&E Form 10-K, Exhibit 10.59).
- 10.51 Fourth Amendment to the San Diego Gas & Electric Company Nuclear Facilities Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station (see Exhibit 10.47 herein) (1996 SDG&E Form 10-K, Exhibit 10.60).
- 10.52 Fifth Amendment to the San Diego Gas & Electric Company Nuclear Facilities Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generation Station (see Exhibit 10.47 herein) (1999 SDG&E Form 10-K, Exhibit 10.26).
- 10.53 Sixth Amendment to the San Diego Gas & Electric Company Nuclear Facilities Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station (see Exhibit 10.47 herein) (1999 SDG&E Form 10-K, Exhibit 10.27).
- 10.54 Seventh Amendment to the San Diego Gas & Electric Company Nuclear Facilities Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station dated December 24, 2003 (see Exhibit 10.47 herein) (2003 Form 10-K, Exhibit 10.42).
- 10.55 Nuclear Facilities Non-Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station, approved November 25, 1987 (1992 SDG&E Form 10-K, Exhibit 10.8).
- 10.56 First Amendment to the San Diego Gas & Electric Company Nuclear Facilities Non-Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station (see Exhibit 10.55 herein) (1996 Form 10-K, Exhibit 10.62).



- 10.57 Second Amendment to the San Diego Gas & Electric Company Nuclear Facilities Non-Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station (see Exhibit 10.55 herein) (1996 Form 10-K, Exhibit 10.63).
- 10.58 Third Amendment to the San Diego Gas & Electric Company Nuclear Facilities Non-Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station (see Exhibit 10.55 herein) (1999 SDG&E Form 10-K, Exhibit 10.31).
- 10.59 Fourth Amendment to the San Diego Gas & Electric Company Nuclear Facilities Non-Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station (see Exhibit 10.55 herein) (1999 SDG&E Form 10-K, Exhibit 10.32).
- 10.60 Fifth Amendment to the San Diego Gas & Electric Company Nuclear Facilities Non-Qualified CPUC Decommissioning Master Trust Agreement for San Onofre Nuclear Generating Station dated December 24, 2003 (see Exhibit 10.55 herein) (2003 Form 10-K, Exhibit 10.48).
- 10.61 Second Amended San Onofre Operating Agreement among Southern California Edison Company, SDG&E, the City of Anaheim and the City of Riverside, dated February 26, 1987 (1990 SDG&E Form 10-K, Exhibit 10.6).
- 10.62 U. S. Department of Energy contract for disposal of spent nuclear fuel and/or high-level radioactive waste, entered into between the DOE and Southern California Edison Company, as agent for SDG&E and others; Contract DE-CR01-83NE44418, dated June 10, 1983 (1988 SDG&E Form 10-K, Exhibit 10N).

Exhibit 12 -- Statement re: Computation of Ratios

- 12.01 Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividends for the years ended December 31, 2004, 2003, 2002, 2001 and 2000.

Exhibit 13 -- Annual Report to Security Holders

- 13.01 Sempra Energy 2004 Annual Report to Shareholders. (Such report, except for the portions thereof which are expressly incorporated by reference in this Annual Report, is furnished for the information of the Securities and Exchange Commission and is not to be deemed "filed" as part of this Annual Report).

Exhibit 21 -- Subsidiaries

- 21.01 Schedule of Significant Subsidiaries at December 31, 2004.

Exhibit 23 -- Consent of Independent Registered Public Accounting Firm and Report on Schedules, page 43.

Exhibit 31 -- Section 302 Certifications

- 31.1 Statement of Registrant's Chief Executive Officer pursuant

to Rules 13a-14 and 15d-14 of the Securities Exchange Act of 1934.

31.2 Statement of Registrant's Chief Financial Officer pursuant to Rules 13a-14 and 15d-14 of the Securities Exchange Act of 1934.

Exhibit 32 -- Section 906 Certifications

32.1 Statement of Registrant's Chief Executive Officer pursuant to 18 U.S.C. Sec. 1350.

32.2 Statement of Registrant's Chief Financial Officer pursuant to 18 U.S.C. Sec. 1350.

## GLOSSARY

AB	California Assembly Bill
AEG	Atlantic Electric & Gas
AEP	American Electric Power
AFUDC	Allowance for Funds Used During Construction
ALJ	Administrative Law Judge
APBO	Accounting Principles Board Opinion
ARB	Accounting Research Bulletin
ECAP	Biennial Cost Allocation Proceeding
Bcf	One Billion Cubic Feet (of natural gas)
California Utilities	Southern California Gas Company and San Diego Gas & Electric
CEC	California Energy Commission
CEMA	Catastrophic Event Memorandum Account
CFE	Comision Federal de Electricidad
CPUC	California Public Utilities Commission
DGN	Distribuidora de Gas Natural
DOE	Department of Energy
DSM	Demand Side Management
DTSC	Department of Toxic Substance Control
DWR	Department of Water Resources
Edison	Southern California Edison Company
EITF	Emerging Issues Task Force
El Paso	El Paso Natural Gas Company
Elk Hills	Elk Hills Power
EMFs	Electric and Magnetic Fields
EPS	Earnings per Share
ERMG	Energy Risk Management Group
ERMOC	Energy Risk Management Oversight Committee

ESOP	Employee Stock Ownership Plan
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
FIN	FASB Interpretation Number
FSP	FASB Staff Position
GCIM	Gas Cost Incentive Mechanism
GIR	Gas Industry Restructuring
ICIP	Incremental Cost Incentive Pricing
ICWUC	International Chemical Workers' Union Council
IOUs	Investor-Owned Utilities
IRS	Internal Revenue Service
ISO	Independent System Operator
ISFSI	Independent Spent Fuel Storage Facility
Liberty	Liberty Gas Storage
LIBOR	London Interbank Offered Rate
LIFO	Last In First Out inventory costing method
LNG	Liquefied Natural Gas
Luz del Sur	Luz del Sur S.A.A.
MGP	Manufactured-Gas Plants
mmbtu	Million British Thermal Units (of natural gas)
MW	Megawatt
NRC	Nuclear Regulatory Commission
OIR	Order Instituting Ratemaking
ORA	Office of Ratepayer Advocates
OTC	Over-the-counter
PBR	Performance-Based Ratemaking/Regulation
PE	Pacific Enterprises
PGE	Portland General Electric Company

PIER	Public Interest Energy Research
PRP	Potentially Responsible Party
PSEG	Public Service Enterprise Group
PX	Power Exchange
QF	Qualifying Facility
QUIPS	Quarterly Income Preferred Securities
RD&D	Research, Development and Demonstration
ROE	Return on Equity
ROR	Return on Ratebase
SDG&E	San Diego Gas & Electric Company
SFAS	Statement of Financial Accounting Standards
Shell	Shell International Gas Limited
SoCalGas	Southern California Gas Company
SONGS	San Onofre Nuclear Generating Station
SWPL	Southwest Powerlink, a transmission line connecting San Diego to Phoenix and intermediate points.
Sunat	Peruvian tax authorities
TDM	Termoelectrica de Mexicali
Topaz	Topaz Power Partners
Trust	ESOP Trust
UCAN	Utility Consumers Action Network
UWUA	Utility Workers' Union of America
VaR	Value at Risk
VIE	Variable Interest Entity

**Ex. 4.07**

13RECORDING REQUESTED BY RECORDED MAIL TO:  
U.S. BANK NATIONAL ASSOCIATION  
633 W. FIFTH STREET, 24<sup>TH</sup> FLOOR  
LOS ANGELES, CA 90071  
ATTN: CORPORATE TRUST SERVICES

**Index as a UCC Filing and an Indenture  
This is a Security Agreement and a Mortgage of Chattels  
as well as a Mortgage of Real Estate and Other Property**

**FORTY-NINTH SUPPLEMENTAL INDENTURE**

**FROM**

**SAN DIEGO GAS & ELECTRIC COMPANY**

**TO**

**U.S. BANK NATIONAL ASSOCIATION**

\*\*\*\*\*

Dated as of June 1, 2004

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**THIS FORTY-NINTH SUPPLEMENTAL INDENTURE IS A SECURITY  
AGREEMENT AND A MORTGAGE OF CHATTELS AS WELL AS  
A MORTGAGE OF REAL ESTATE AND OTHER PROPERTY**

THIS FORTY-NINTH SUPPLEMENTAL INDENTURE, dated as of the first day of June, 2004, by and between SAN DIEGO GAS & ELECTRIC COMPANY, a corporation duly organized and existing under and by virtue of the laws of the State of California, having its principal office in that State in the City of San Diego (the "Company"), and U.S. BANK NATIONAL ASSOCIATION, a banking association duly organized under an act known as the "National Bank Act", of the United States of America, having a corporate trust office in the City of Los Angeles, State of California, as Trustee (the "Trustee").

WHEREAS, the Company executed and delivered a Mortgage and Deed of Trust (the "Original Indenture"), dated July 1, 1940, to The Bank of California, National Association, as predecessor trustee to Bankers Trust Company of California, National Association, as predecessor trustee to First Trust of California, National Association, (subsequently renamed U.S. Bank Trust National Association) as predecessor trustee to the Trustee, to secure payment of the principal of and the interest on all bonds of the Company at any time outstanding thereunder according to their tenor and effect, and to provide the terms and provisions with respect to its First Mortgage Bonds, 3 3/8% Series due July 1, 1970, issued in the aggregate principal amount of \$16,000,000 and heretofore retired; and

WHEREAS, the Company executed and delivered to the then current trustee, a First Supplemental Indenture dated as of December 1, 1946, a Second Supplemental Indenture dated as of Much 1, 1948, a Third Supplemental Indenture dated as of April 1, 1952, a Fourth Supplemental Indenture dated as of April 1, 1954, a Fifth Supplemental Indenture dated as of October 1, 1955, a Sixth Supplemental Indenture dated as of October 1, 1957, a Seventh Supplemental Indenture dated as of October 1, 1960, an Eighth Supplemental Indenture dated as of March 1, 1967, a Tenth Supplemental Indenture dated as of December 1, 1968, an Eleventh Supplemental Indenture dated as of February 1, 1970, a Twelfth Supplemental Indenture dated as of September 1, 1971, a Thirteenth Supplemental Indenture dated as of January 15, 1974, a Fourteenth Supplemental Indenture dated as of December 15, 1974, a Fifteenth Supplemental Indenture dated as of May 1, 1975, a Seventeenth Supplemental Indenture dated as of July 15, 1976, an Eighteenth Supplemental Indenture dated as of March 15, 1977, a Nineteenth Supplemental Indenture dated as of May 1, 1978, a Twentieth Supplemental Indenture dated as of March 15, 1980, a Twenty-First Supplemental Indenture dated as of August 1, 1980, a Twenty-Second Supplemental Indenture dated as of July 15, 1981, a Twenty-Third Supplemental Indenture dated as of January 15, 1982, a Twenty-Fourth Supplemental Indenture dated as of August 16, 1982, a Twenty-Fifth Supplemental Indenture dated as of August 16, 1982, a Twenty-Sixth Supplemental Indenture dated as of August 16, 1982, a Twenty-Seventh Supplemental Indenture dated as of June 1, 1983, a Twenty-Eighth Supplemental Indenture dated as of July 15, 1983, a Twenty-Ninth Supplemental Indenture dated as of September 1, 1983, a Thirty-First, Supplemental Indenture dated as of May 1, 1984, a Thirty-Second Supplemental Indenture dated as of December 1984, a Thirty-Third Supplemental Indenture dated as of September 1, 1985, a Thirty-Fourth Supplemental Indenture dated as of December 1, 1985, a Third-Fifth Supplemental Indenture dated as of July 1, 1986, a Thirty-Sixth Supplemental Indenture dated as of December 1, 1986, a Thirty-Seventh Supplemental Indenture dated as of September 1, 1987, a Thirty-Eighth Supplemental Indenture dated as of April 15, 1990, a Thirty-Ninth Supplemental Indenture dated as of December 1, 1991, a Fortieth Supplemental Indenture dated as of April 1, 1992, a Forty-First Supplemental Indenture dated as of June 15, 1992, a Forty-Second Supplemental Indenture dated as of September 1, 1992, a Forty-Third Supplemental Indenture dated as of December 1, 1992, a Forty-Fourth Supplemental Indenture dated as of April 1, 1993, a Forty-Fifth Supplemental Indenture dated as of June 1, 1993, a Forty-Sixth Supplemental Indenture dated as of July 1, 1993, a Forty-Seventh Supplemental Indenture dated as of June 1, 1995 and a Forty-Eighth Supplemental Indenture dated as of June 1, 1995, whereby, among other things, the Company set forth certain of the particulars of the Bonds of series designated "First Mortgage Bonds, 2 3/4% Series due December 1, 1981" issued in the aggregate principal amount of \$2,800,000; "First Mortgage Bonds, Series C due 1978" issued in the aggregate principal amount of \$10,000,000; "First Mortgage Bonds, Series D due 1982" issued in the aggregate principal amount of \$512,000,000; "First Mortgage Bonds, Series E due 1984" issued in the aggregate principal amount of \$17,000,000; "First Mortgage Bonds, Series F due 1985" issued in the aggregate principal amount of \$18,000,000; "First Mortgage Bonds, Series G due 1987" issued in the aggregate principal amount of \$12,000,000; "First Mortgage Bonds, Series H due 1990" issued in the aggregate principal amount of \$30,000,000; "First Mortgage Bonds, Series I due 1997" issued in the aggregate principal amount of \$25,000,000; "First Mortgage Bonds, Series J due 1998" issued in the aggregate principal amount of \$35,000,000; "First Mortgage Bonds, Series K due 2000" issued in the aggregate principal amount of \$40,000,000; "First Mortgage Bonds, Series L due 2001" issued in the aggregate principal amount of \$45,000,000; "First Mortgage Bonds, Series M due 2004" issued in the aggregate principal amount of \$75,000,000; "First Mortgage Bonds, Series N due 1979" issued in the aggregate principal amount of \$50,000,000; "First Mortgage Bonds, Series O due 1982" issued in the aggregate principal amount of \$40,000,000; "First Mortgage Bonds, Series P due 2006" issued in the aggregate principal amount of \$45,000,000; "First Mortgage Bonds, Series Q due 2007" issued in the aggregate principal amount of \$50,000,000; "First Mortgage Bonds, Series R due 2008" issued in the aggregate principal amount of \$50,000,000; "First Mortgage Bonds, Series S due 2010" issued in the aggregate principal amount of \$50,000,000; "First Mortgage Bonds, Series T due 2010" issued in the aggregate principal amount of \$75,000,000; "First Mortgage Bonds, Series U-1 due 1984, and U-2 due 1994" issued in the aggregate principal amount of \$6,567,000 for Series U-1 and \$13,268,000 for Series U-2, "First Mortgage Bonds, Series V due 2011" issued in the aggregate principal amount of \$50,000,000, "First Mortgage Bonds, Series W due 1988" issued in the aggregate principal amount of \$40,000,000; "First Mortgage Bonds, Series X due 1987" issued in the aggregate principal amount of \$20,000,000; "First Mortgage Bonds, Series Y due 1987" issued in the aggregate principal amount of \$15,000,000; "First Mortgage Bonds, Series Z, due 2013" issued in the aggregate principal amount of \$65,000,000; "First Mortgage Bonds, Series AA, due 2018" issued in the aggregate principal amount of \$150,000,000; "First Mortgage Bonds, Series BB, due 2018" issued in the aggregate principal amount of \$150,000,000; "First Mortgage Bonds, Series CC, due 2008" issued in the aggregate principal amount of \$53,000,000; "First Mortgage Bonds Series DD, due 2008" issued in the aggregate principal amount of \$27,000,000; "First Mortgage Bonds, Series EE, due 2015" issued in the aggregate principal amount of \$100,000,000; "First Mortgage Bonds, Series FF, due 2007" issued in the aggregate principal amount of \$35,000,000; "First Mortgage Bonds, Series GG, due 2021" issued in the aggregate principal amount of \$44,250,000; "First Mortgage Bonds, Series HH, due 2021" issued in the aggregate principal amount of \$381,350,000; "First Mortgage Bonds, Series II due 2023" issued in the aggregate principal amount of \$25,000,000; "First Mortgage Bonds, Series JJ, due 2015" issued in the aggregate principal amount of \$100,000,000; "First Mortgage Bonds, Series KK, due 2015" issued in the aggregate principal amount of \$14,400,000; "First Mortgage Bonds, Series LL, due 2022" issued in the aggregate principal amount of \$60,000,000, "First Mortgage Bonds, Series MM due 2002" issued in the aggregate principal amount of \$80,000,000; "First Mortgage Bonds, Series NN", issued in the aggregate principal amount of \$118,615,000; "First Mortgage Bonds, Series OO", issued in the aggregate principal amount of \$250,000,000; "First Mortgage Bonds, Series PP, due 2018" issued in the aggregate principal amount of \$70,795,000; "First Mortgage Bonds, Series QQ, due 2018" issued in the aggregate principal amount of \$14,915,000; "First Mortgage Bonds, Series RR, due 2021" issued in the aggregate principal amount of \$60,000,000, and "First Mortgage Bonds, Series SS, due 2018" issued in the aggregate principal amount of \$92,945,000, "First Mortgage Bonds, Series TT due 2020" issued in the aggregate principal amount of \$57,650,000 and "First Mortgage Bonds, Series UU due 2020" issued in the aggregate principal amount of \$16,700,000, respectively, all of which First Mortgage Bonds are presently issued and outstanding, except the 2 3/4% Series due 1981, the Series C due 1978, the Series D due 1982, the Series E due 1984, the Series F due 1985, the Series G due 1987, the Series H due 1990, the Series I due 1997, the Series J due 1998, the Series K due 2000, the Series L due 2001, the Series M due 2004, the Series N due 1979, the Series O due 1982, the Series P due 2006, the Series Q due 2007, the Series R due 2008, the Series S due 2010, the Series T due 2010, the Series U-1 due 1984, the Series U-2 due 1994, the Series V due 2011, the Series W due 1988, the Series X due 1987, the Series Y due 1987, the Series Z due 2013, the Series AA due 2018, the Series BB due 2018, the Series CC due 2008, the Series DD due 2008, the Series EE due 2015, the Series FF due 2007, the Series GG due 2021, the Series HH due 2021, the Series II due 2023, the Series JJ due 2015, the Series LL due 2022, the Series MM due 2022, the Series QQ due 2018 and the Series UU due 2020, which have heretofore been retired or redeemed; and

WHEREAS, certain of the provisions of the Original Indenture have been amended by the aforesaid Second and Tenth Supplemental Indentures, a Ninth Supplemental Indenture dated as of August 1, 1968, a Sixteenth Supplemental Indenture dated August 28, 1975, and a Thirtieth Supplemental Indenture dated September 23, 1983; and

WHEREAS, the Original Indenture and each of said Supplemental Indentures have been recorded in the Official Records of the Recorders of the Counties of San Diego, Orange, Riverside, and Imperial in the State of California and the Counties, Yuma and Maricopa in the State of Arizona, as follows:

Document	Official Records	Counties of			
		San Diego	Orange	Riverside	Imperial
Original Indenture	Book Page Date 1087 1 Oct. 10, 1940	1062 300 Oct. 10, 1940	1765 364 July 13, 1955	1369 232 Nov. 22, 1974	
First Supplemental Indenture	Book Page Date 2321 48 Jan. 2, 1947	1506 472 Jan. 9, 1947	1765 499 July 13, 1955	1369 332 Nov. 22, 1974	
Second Supplemental Indenture	Book Page Date 2537 363 Mar. 16, 1948	1616 190 Mar. 15, 1948	1765 448 July 13, 1955	1369 343 Nov. 22, 1974	
Third Supplemental Indenture	Book 4424 535 Apr. 3, 1952	2311	1765 475 July 13, 1955	1369	

	Page Date		116 Apr. 3, 1952		370 Nov. 22, 1974
Fourth Supplemental Indenture	Book Page Date	5193 217 Apr. 2, 1954	2701 153 Apr. 2, 1954	1765 336 July 13, 1955	1369 409 Nov. 22, 1974
Fifth Supplemental Indenture	Book Page Date	5893 291 Dec. 5, 1955	3304 205 Dec. 5, 1955	1829 3 Dec. 5, 1955	2369 456 Nov. 22, 1974
Sixth Supplemental Indenture	Book Page Date	6829 390 Nov. 12, 1957	4099 109 Nov. 12, 1957	2175 538 Nov. 12, 1957	1369 492 Nov. 22, 1974
Seventh Supplemental Indenture	Book Page Date	1960 Series 1 File No. 202061 Oct. 10, 1960	5455 385 Oct. 10, 1960	2780 3 Oct. 10, 1960	1369 541 Nov. 22, 1974
Eighth Supplemental Indenture	Book Page Date	1967 Series 8 File No. 33860 Mar. 13, 1967	8197 129 Mar. 13, 1967	Endorsement No. 20925 Mar. 13, 1967	1369 618 Nov. 22, 1974
Ninth Supplemental Indenture	Book Page Doc. No. Date	1968 Series 9 138926 Aug. 14, 1968	8691 69 9816 Aug. 14, 1968	78781 Aug. 14, 1968	1369 694 Nov. 22, 1974
Tenth Supplemental Indenture	Book Page Doc. No. Date	1968 Series 9 215131 Dec. 9, 1968	8810 375 Dec. 9, 1968	Endorsement No. 119982 Dec. 9, 1968	1369 706 Nov. 22, 1974
Eleventh Supplemental Indenture	Book Page Doc. No. Date	1970 27782 Feb. 16, 1970	9217 516 Feb. 16, 1970	Endorsement No. 14780 Feb. 16, 1970	1369 725 Nov. 22, 1974
Twelfth Supplemental Indenture	Book Page Date	File/Page No. 212688 Sept. 20, 1971	9810 539 Sept. 20, 1971	Endorsement No. 106508 Sept. 20, 1971	1369 744 Nov. 22, 1974
Thirteenth Supplemental Indenture	Book Page Date	File/Page No. 74-006878 Jan. 10, 1974	11055 1 Jan. 10, 1974	Endorsement No. 3853 Jan. 10, 1974	1369 763 Nov. 22, 1974
Fourteenth Supplemental Indenture	Book Page Date	File/Page No. 74-322156 Dec. 11, 1974	11303 458 Dec. 11, 1974	Endorsement No. 157219 Dec. 11, 1974	1369 1689 Dec. 11, 1974
Fifteenth Supplemental Indenture	Book Page Date	File/Page No. 755-108612 May 7, 1975	11395 1879 May 7, 1975	Instrument No. 52617 May 7, 1975	1374 809 May 7, 1975

Document	Official Records	Counties of			
		San Diego	Orange	Riverside	Imperial
Sixteenth Supplemental Indenture	Book Page Date	File/Page No. 75-235624 Sept. 2, 1975	11500 1620 Sept. 2, 1975	Instrument No. 107732 Sept. 3, 1975	1378 952 Sept. 2, 1975
Seventeenth Supplemental Indenture	Book Page Date	File/Page No. 76-224493 July 16, 1976	11815 640 July 16, 1976	Instrument No. 103484 July 16, 1976	1389 687 July 16, 1976
Eighteenth Supplemental Indenture	Book Page Date	File/Page No. 77-100483 Mar. 18, 1977	12110 58 Mar. 18, 1977	Instrument No. 45619 Mar. 18, 1977	1398 1675 Mar. 18, 1977
Nineteenth Supplemental Indenture	Book Page Date	File/ Page No. 78-194210 May 12, 1978	12672 1803-1822 May 12, 1978	Instrument No. 94450 May 12, 1978	1415 1638 May 12, 1978
Twentieth Supplemental Indenture	Book Page Date	File/Page No. 80-082569 Mar. 11, 1980	13530 722 Mar. 11, 1980	Instrument No. 47195 Mar. 11, 1980	1448 1221 Mar. 11, 1980
Twenty-First Supplemental Indenture	Book Page Date	File/Page No. 80-245100 Aug. 1, 1980	13687 349 Aug. 1, 1980	Instrument No. 139349 Aug. 1, 1980	1455 1660 Aug. 1, 1980
Twenty-Second Supplemental Indenture	Book Page Date	File/Page No. 81-22576 July 17, 1981	Instrument No. 24605 July 17, 1981	Instrument No. 135815 July 17, 1981	1472 508 July 17, 1981



Twenty-Third Supplemental Indenture	Book Page Date	File/Page No. 82-02387 Jan. 27, 1982	Instrument No. 82-031423 Jan. 27, 1982	Instrument No. 16093 Jan. 27, 1982	1479 1714 Jan. 27, 1982
Twenty-Fourth Supplemental Indenture	Book Page Date	File/Page No. 82-257258 Aug. 19, 1982	File/Page No. 82-291894 Aug. 19, 1982	File/Page No. 82/143370212 Aug. 19, 1982	1489 Aug. 19, 1982
Twenty-Fifth Supplemental Indenture	Book Page Date	File/Page No. 82-257259 Aug. 19, 1982	File/Page No. 82-291895 Aug. 19, 1982	File/Page No. 82-143371 Aug. 19, 1982	1489 236 Aug. 19, 1982
Twenty-Sixth Supplemental Indenture	Book Page Date	File/Page No. 82-257260 Aug. 19, 1982	File/Page No. 82-291896 Aug. 19, 1982	File/Page No. 82/143372260 Aug. 19, 1982	1489 Aug. 19, 1982
Twenty-Seventh Supplemental Indenture	Book Page Date	File/Page No. 83-200545 June 15, 1983	File/Page No. 83-253901 June 15, 1983	File/Page No. 118670 June 15, 1983	1503 743 June 15, 1983
Twenty-Eighth Supplemental Indenture	Book Page Date	File/Page No. 83-252396 July 22, 1983	File/Page No. 83-316224 July 22, 1983	File/Page No. 147671 July 22, 1983	1505 583 July 22, 1983
Twenty-Ninth Supplemental Indenture	Book Page Date	File/Page No. 83-339007 Sept. 22, 1983	File/Page No. 83-417956 Sept. 22, 1983	File/Page No. 194083 Sept. 22, 1983	1508 1425 Sept. 22, 1983

		Counties of	
		Yuma	Maricopa
Thirtieth Supplemental Indenture Consisting of Original and Twenty-Nine Supplemental Indentures thereto	Book Page Date	Docket 1352 272-1002 Docket 1353 1-264 Sept. 28, 1983	File No. 83-399354 Oct. 3, 1983

Document	Official Records	Counties of					
		San Diego	Orange	Riverside	Imperial	Yuma	Maricopa
Thirty-First Supplemental Indenture	Book Page Date	File/Page 84-161897 5/2/84	File/Page 84-180870 5/2/84	File/Page 92011 5/2/84	1520 1552 4/30/84	Docket 1382 743-761 4/30/84	File No. 84-186813 5/2/84
Thirty-Second Supplemental Indenture	Book Page Date	File/Page 84-466428 12/14/84	File/Page 84-517843 12/14/84	File/Page 267452 12/14/84	1533 753 12/14/84	Docket 1413 216-235 12/14/84	File No. 84-537706 12/14/84
Thirty-Third Supplemental Indenture	Book Page Date	File/Page 85-323210 9/4/85	File/Page 85-333505 9/4/85	File/Page 198810 9/4/85	1546 708 9/4/85	Docket 1450 816 9/4/85	File No. 85-418309 9/4/85
Thirty-Fourth Supplemental Indenture	Book Page Date	File/Page 85-42465 12/2/85	File/Page 85-481794 12/2/85	File/Page 270136 12/2/85	1550 1573 12/3/85	Docket 1463 215 12/3/85	File No. 85-568874 12/2/85
Thirty-Fifth Supplemental Indenture	Book Page Date	File/Page 86-279922 7/8/86	File/Page 86-290957 7/8/86	File/Page 158161 7/8/86	1562 549 7/8/86	Docket 1491 639-657 7/8/86	File No. 86-347412 7/8/86
Thirty-Sixth Supplemental Indenture	Book Page Date	File/Page 86-576027 12/10/86	File/Page 86-606666 12/10/86	File/Page 314771 12/10/86	1571 240 12/10/86	Docket 1512 5-24 12/10/86	File/Page 86-680502 12/10/86
Thirty-Seventh Supplemental Indenture	Book Page Date	File/Page 87-532270 9/21/87	File/Page 87-530266 9/21/87	File/Page 273181 9/21/87	1588 844 9/21/87	Docket 1555 844 9/21/87	File/Page 87-585903 9/21/87
Thirty-Eighth Supplemental Indenture	Book Page Date	File/Page 90-217585 4/23/90	File/Page 90-212277 14679,1 4/23/90	File/Page 146794 4/23/90	1646 1280 4/23/90	Docket 1686 92-120 4/23/90	File/Page 88-176460 4/23/90
Thirty-Ninth Supplemental Indenture	Book Page Date	File/Page 91-632073 12/09/91	File/Page 91-674397 12/09/91	File/Page 425578 12/09/91	1687 743 12/09/91	Docket 1771 711-728 12/09/91	File/Page 91-0574751 12/09/91
Fortieth Supplemental Indenture	Book Page Date	File/Page 92-185636 4/1/92	File/Page 92-202372 4/1/92	File/Page 115201 4/1/92	Book/Page 92-06577 4/1/92	Docket 1790 954-970 4/1/92	File/Page 92-0169646 4/1/92
Forty-First		File/Page	File/Page			Docket 1804	File/Page

Supplemental Indenture	Book Page Date	92-0363471 6/11/92	92-393790 6/11/92	File/Page 214904 6/11/92	Book/Page 92-011833 6/11/92	73-88 6/11/92	92-0317072 6/11/92
Forty-Second Supplemental Indenture	Book Page Date	File/Page 92-0650893 10/13/92	File/Page 92-692066 10/13/92	File/Page 384167 10/13/92	Book/Page 92-21988 10/13/92	Docket 1824 670-689 10/13/92	File/Page 92-0575062 10/13/92
Forty-Third Supplemental Indenture	Book Page Date	File/Page 92-0788665 12/9/92	File/Page 92-845626 12/10/92	File/Page 471625 12/10/92	Book/Page 92-27082 12/9/92	Docket 1834 187-206 12/9/92	File/Page 92-0700568 12/9/92
Forty-Fourth Supplemental Indenture	Book Page Date	File/Page 93-0257065 4/27/93	File/Page 93-0277892 4/27/93	File/Page 153382 4/27/93	Book/Page 93-009487 4/27/93	Docket 1859 Fee 09300 4/27/93	File/Page 93-0246725 4/26/93
Forty-Fifth Supplemental Indenture	Book Page Date	File/Page 93-0395609 6/23/93	File/Page 93-0420127 6/23/93	File/Page 239922 6/23/93	Book/Page 93-14224 6/23/93	Docket Fee 14413 6/23/93	File/Page 93-0403060 6/23/93

Document	Official Records	Counties of					
		San Diego	Orange	Riverside	Imperial	Yuma	Maricopa
Forty-Sixth Supplemental Indenture	Book Page Date	File/Page 93-0474705 7/26/93	File/Page 93-0496100 7/26/93	File/Page 288868 7/27/93	Book/Page 93-17399 7/27/93	Docket Fee 17163 7/27/93	File/Page 93-0487598 7/27/93
Forty-Seventh Supplemental Indenture	Book Page Date	File/Page 95-0230457 6/01/95	File/Page 95-0232951 6/01/95	File/Page 175604 6/01/95	Book/Page 95-11739 6/01/95	Docket 246-264 6/01/95	File/Page 95-0313576 6/01/95
Forty-Eighth Supplemental Indenture	Book Page Date	File/Page 95-0230458 6/01/95	File/Page 95-0232952 6/01/95	File/Page 175605 6/01/95	Book/Page 95-11740 6/01/95	Docket 265-284 6/01/95	File/Page 95-0343577 6/01/95

WHEREAS, the Board of Directors of the Company has duly authorized the creation of six additional series of bonds to be designated "First Mortgage Bonds, Series VV, due 2034," "First Mortgage Bonds, Series WW, due 2034," "First Mortgage Bonds, Series XX, due 2034," "First Mortgage Bonds, Series YY, due 2034," "First Mortgage Bonds, Series ZZ, due 2034," and "First Mortgage Bonds, Series AAA, due 2039," as hereinafter set forth in this Forty-Ninth Supplemental Indenture; and

WHEREAS, the execution and delivery of this Forty-Ninth Supplemental Indenture has been duly authorized by resolution of the Board of Directors of the Company; and

WHEREAS, all the conditions and requirements necessary to make this Forty-Ninth Supplemental Indenture a valid, binding and legal instrument in accordance with its terms and for the purposes herein expressed have been performed and fulfilled and the execution and delivery hereof have been in all respects duly authorized.

NOW, THEREFORE, in order further to secure the payment of the principal of and interest on all of the bonds of the Company at any time outstanding under the Original Indenture, as from time to time amended and supplemented (the "Indenture") and to secure the performance and observance of each and every of the covenants and agreements of the Indenture, as from time to time amended and supplemented, and for and in consideration of the premises, and of the sum of One Dollar (\$1.00) to the Company duly paid by the Trustee (the receipt whereof is hereby acknowledged), the Company has executed and delivered this Forty-Ninth Supplemental Indenture and has granted, bargained, sold, warranted, released, conveyed, assigned, transferred, mortgaged, pledged, hypothecated, granted a security interest in, set over and confirmed, and by these presents does grant, bargain, sell, warrant, release, convey, assign, transfer, mortgage, pledge, hypothecate, grant a security interest in, set over and confirm unto O. S. Bank National Association, as Trustee, and to its respective successors in said trust forever, with power of sale, all property, real, personal and mixed, now owned or hereafter acquired or to be acquired by the Company, and whosoever situated (except such property as is expressly excepted or excluded from the lien and security interest of the Indenture, and property of a successor corporation or corporations excluded from the lien and security interest thereof by the provisions of Section 3 of Article XIV thereof) subject to the rights reserved by the Company in and by other provisions of the Indenture, including in the property subject and to be subject to the lien and security interest thereof and hereof (without in any manner limiting or impairing by the enumeration of the same scope and intent of the foregoing or of any general description contained in the Original Indenture or in this or any other supplemental indenture) all lands, rights-of-way, other land rights, flowage and other water rights, power houses, dams, reservoirs, docks, roads, and buildings, structures and other land improvements; steam, and other electric generating plants, including buildings and other structures, turbines, generators, exciters, boilers and other boiler plant equipment, condensing equipment, and all auxiliary equipment; stations and substations; electric transmission and distribution systems, including structures, poles, towers, fixtures, conduits, insulators, wires, cables, transformers, services and meters; steam heating plants and systems, including mains and equipment, gas plants, transmission and distribution systems, including pipe lines, structures, tanks, mains, compressor stations, purifier stations, pressure holders, governors, services and meters; communication systems, office, shop and other buildings and structures, and equipment; apparatus and equipment and materials and supplies of all other kinds and descriptions; and all municipal and other franchises, leaseholds, licenses, permits, and privilege s;

TOGETHER WITH all and singular the tenements, hereditaments and appurtenances belonging or in any wise appertaining to the aforesaid property or any part thereof with the reversion and reversions, remainder and remainders, tolls, rents and revenues, issues, income, proceeds, product and profits thereof, and all the estate, right, title and interest and claim whatsoever, at law as well as in equity, which the Company now has or may hereafter acquire in and to the aforesaid property and every part and parcel thereof (except such property as is expressly excepted or excluded from the lien and security interest of the Indenture, and property of a successor corporation or corporations excluded from the lien and security interest thereof by the provisions of Section 3 of Article XIV thereof), subject to the rights reserved by the Company in and by other provisions of the Indenture;

It is hereby agreed by the Company that, except as aforesaid, all the property, rights, and franchises acquired by the Company after the date hereof shall be as fully embraced within the lien and security interest hereof as if such property were now owned by the Company and were specifically described herein and conveyed and a security interest therein granted hereby;

SAVING AND EXCEPTING, HOWEVER, anything to the contrary notwithstanding contained herein or in the granting clauses of the Original Indenture and said Supplemental Indentures (a) such property described or referred to in any of such granting clauses as has been from time to time, released or sold free from the lien and security interest of the Original Indenture (or the Original Indenture, as supplemented) in accordance and compliance with the provisions thereof (or of the Original Indenture, as supplemented, as the case may be) and (b) all of the following property (whether now owned by the Company or hereafter acquired by it): (1) all gas, electric energy and steam produced, purchased or otherwise acquired; (2) all contracts, chosen in action, shares of stock, bonds, notes, evidences of indebtedness, and other securities, other than any of the foregoing which may be required to be deposited from time to time with the Trustee in accordance with the provisions of the Indenture or are required by some express provision thereof to be deposited with the Trustee; (3) merchandise and appliances at any time acquired for the purpose of sale or lease to customers and others and contracts for the sale of merchandise and appliances; (4) motor vehicles; (5) timber on land owned by the Company; (6) minerals or mineral rights in lands owned by the Company; (7) oil, coal or gas, or oil, coal or gas rights in land owned by the Company or gas wells or oil wells or equipment therefor or coal mines or equipment therefor; (8) fuel and other personal property which are consumable in their use in the operation of the properties of the Company; (9) bills and accounts receivable; (10) cash on hand and in banks other than such cash as may be deposited from time to time with the Trustee in accordance with the provisions of the Indenture or as is required by some express provision thereof to be deposited with the Trustee; and (11) the last day of the term of each leasehold estate now or hereafter enjoyed by the Company. The Company may, however, expressly subject to the lien and security interest and operation of the Original Indenture and all indentures supplemental thereto all or any part of the property of the character described in clause (b) of this paragraph;

TO HAVE AND TO HOLD all said properties, real, personal and mixed, mortgaged, pledged, or conveyed and in which a security interest has been granted by the Company as aforesaid, or intended so to be, unto the Trustee and its successors and assigns forever, subject, however, to Permitted Liens as defined in the Indenture;

IN TRUST NEVERTHELESS, for the equal pro rata benefit and security as provided in the Original Indenture and all indentures supplemental thereto of all and every of the bonds issued and to be issued in accordance with the provisions of the Original Indenture and all indentures supplemental thereto, without preference priority or distinction as to lien or security interest of any over the others by reason of priority in time of the issue, negotiation or maturity thereof, subject, however, to the provisions of the Original Indenture and all indentures supplemental thereto relating to any sinking fund or similar fund for the benefit of the bonds of any particular series;

The Company does further covenant and agree with the Trustee as follows:

#### ARTICLE I SERIES VV BONDS

**Section 1:** There is hereby created, for issuance under the Original Indenture as supplemented by the said Supplemental Indentures (including this Forty-Ninth Supplemental Indenture), a series of bonds designated Series VV, due 2034, each of which shall bear the descriptive title "First Mortgage Bonds, Series VV, due 2034," (herein sometimes referred to as "Series VV Bonds"), and the form thereof shall contain suitable provisions with respect to the matters hereinafter in this Section specified. All of the Series VV Bonds shall be registered bonds without coupons, and shall be substantially of the tenor and purport hereinafter recited. The Series VV Bonds shall mature on February 15, 2034 and shall be issued in denominations of either \$5,000 or \$100,000 and any multiple thereof as the Company may from time to time execute and deliver. The Series VV Bonds shall bear interest from the date of delivery at rates and shall be payable on payment dates which shall correspond exactly to the rate of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series A issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee. Both the principal and interest on the Series VV Bonds shall be payable at the office of the Trustee in St. Paul, Minnesota. The Series VV Bonds shall be dated as in Section 9 of Article II of the Original Indenture provided with respect to registered bonds without coupons.

The Series VV Bonds shall be redeemable as provided in the Form of Reverse of Bond of Series VV, due 2034.

The Series VV Bonds shall be exchangeable for bonds of other authorized denominations and shall be transferable as provided in the Form of Reverse of Bond of Series VV, due 2034.

The Series VV Bonds shall otherwise be of such terms, provisions, tenor and form as provided in this Forty-Ninth Supplemental Indenture.

**Section 2:** The Series VV Bonds and the Trustee's certificate on said Bonds, are to be substantially in the following forms, respectively:

(Form of Face of Bond of Series VV, due 2034)

**THE SERIES VV BONDS REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, AND MAY NOT BE OFFERED OR SOLD IN CONTRAVENTION OF SAID ACT, NOR MAY THEY BE TRANSFERRED EXCEPT TO A TRUSTEE PURSUANT TO THE PROVISIONS OF THAT CERTAIN LOAN AGREEMENT DATED AS OF JUNE 1, 2004, BETWEEN THE CITY OF CHULA VISTA AND SAN DIEGO GAS & ELECTRIC COMPANY.**

SAN DIEGO GAS & ELECTRIC COMPANY  
(INCORPORATED UNDER THE LAWS OF THE STATE OF CALIFORNIA)

FIRST MORTGAGE BOND  
SERIES VV, DUE 2034

No. \_\_\_\_\_ \$ \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY, a corporation organized and existing under the laws of the State of California (hereinafter called the "Company"), for value received, hereby promises to pay to \_\_\_\_\_, or registered assigns, the sum of \_\_\_\_\_ Dollars in lawful money of the United States of America, on the fifteenth day of February, 2034, at the office of U.S. BANK NATIONAL ASSOCIATION as Trustee under the Indenture, as amended, or its successor thereunder, in St. Paul, Minnesota, and to pay to the registered owner hereof interest thereon from the date of delivery hereof until said principal sum shall be paid, at interest rates and on payment dates which shall correspond exactly to the rates of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series A issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee.

The provisions of this bond are continued on the reverse hereof and such continued provisions shall for all purposes have the same effect as though fully set forth at this place.

This bond shall not be valid or become obligatory for any purpose unless and until U.S. BANK NATIONAL ASSOCIATION, as Trustee under the Indenture, as amended, or its successor thereunder, shall have signed the certificate of authentication endorsed hereon.

IN WITNESS WHEREOF, SAN DIEGO GAS & ELECTRIC COMPANY has caused this instrument to be executed in its name by the signature or facsimile signature of its President or any Vice President and its corporate seal, or a facsimile thereof to be hereto affixed and attested by the signature or facsimile signature of its Secretary or any Assistant Secretary.

Dated: \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY

Attest:

\_\_\_\_\_  
By: \_\_\_\_\_

Secretary or Assistant Secretary President or Vice President

(Form of Reverse of Bond of Series VV, due 2034)

This bond is one of a duly authorized issue of bonds of the Company, known as its First Mortgage Bonds, of the series and designation indicated on the face hereof, which issue of bonds consists or may consist, of several series of varying denominations, dates and tenor, all issued and to be issued under and equally secured (except insofar as a sinking fund, or similar fund, established in accordance with the provisions of the Indenture may afford additional security for the bonds of any specific series) by a Mortgage and Deed of Trust dated July 1, 1940, and indentures supplemental thereto, including the Forty-Ninth Supplemental Indenture dated as of June 1, 2004 (which Mortgage and Deed of Trust, as so supplemented, is herein called the "Indenture") executed by the Company to U.S. Bank National Association, as Trustee (herein called the "Trustee"), to which Indenture reference is hereby made for a description of the property mortgaged, pledged, hypothecated and in which a security interest was granted, the nature and extent of the security, the rights of the holders of the bonds and appurtenant coupons as to such security, and the terms and conditions upon which the bonds may be issued under the Indenture and are secured. The principal hereof may be declared or may become due on the conditions, in the manner and at the time set forth in the Indenture, upon the happening of a completed default as in the Indenture provided.

With the consent of the Company and to the extent permitted by and as provided in the Indenture, the rights and obligations of the Company or of the holders of the bonds or coupons, or the terms and provisions of the Indenture or of any indentures supplemental thereto, may be modified or altered by the affirmative vote of the holders of the percentage of principal amount of bonds required by the Indenture; provided, however, that without the consent of the holder hereof no such modification or alteration shall permit the reduction of the principal or the extension of the maturity of the principal of this, bond, or the reduction of the rate of interest hereon, or any other modification of the terms of payment of such principal or interest.

The Company, the Trustee, any paying agent, any registrar, and any depository may deem and treat the person in whose name this bond is registered as the absolute owner hereof for the purpose of receiving payment of or on account of the principal hereof and interest hereon and for all other purposes and shall not be affected by any notice to the contrary.

The Series VV Bonds shall be redeemable, in whole or in part, to the same extent that redemption may be, or is required to be, made of the City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series A as set forth in Section 4.01 of the indenture pursuant to which such bonds were issued. The Series VV Bonds shall also be redeemable, in whole, at a redemption price of 100% of the principal amount, plus accrued interest, if any, on the date the above 2004 Series A Bonds become due and payable upon acceleration or otherwise.

As more fully provided in and subject to the provisions of the Indenture, the Series VV Bonds are also subject to redemption on any date, under certain circumstances specified in Section 13 of Article XI of the Indenture, upon not less than thirty (30) nor more than sixty (60) days' prior notice, given as aforesaid, in case of the disposition of certain properties of the Company, at 100% of the principal amount thereof, together with accrued interest thereon.

If this bond shall be called for redemption and payment duly provided therefor, as specified in the Indenture, interest shall cease to accrue hereon from and after the date fixed for redemption.

This bond is transferable as prescribed in the Indenture by the registered owner hereof in person, or by his duly authorized attorney, at the office of the Trustee in St. Paul, Minnesota, upon surrender and cancellation of this bond and thereupon a new registered bond of the same series and principal amount will be issued to the transferee in exchange therefor as provided in the Indenture, upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such transfer.

The registered owner of any bond or bonds of the Series VV, at the option of such holder, may surrender the same, accompanied by a written instrument of transfer in form approved by the Company duly executed by the registered owner, at the office of the Trustee in St. Paul, Minnesota, for cancellation in exchange for another or other registered bonds of the said series of higher or lower authorized denominations of an aggregate principal amount equal to the aggregate principal amount of the bond or bonds so surrendered and bearing interest as provided in Section 9 of Article II of the Indenture, and upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such exchange and subject to the terms and conditions specified in the Indenture, thereupon the Company shall execute and deliver to the Trustee and the Trustee shall authenticate and deliver such other bonds to such registered owner at its office or at such agency of the Company, at the option of such registered owner.

No recourse shall be had for the payment of the principal of (or premium, if any) or the interest on this bond, or any part thereof, or of any claim based herein or in respect hereof or of said Indenture, against any incorporator, or any past, or future stockholder, officer or director, as such, of the Company or of any predecessor or successor corporation, either directly or through the Company, or through any such predecessor or successor corporation, or through any receiver or a trustee in bankruptcy, whether, by virtue of any constitution, statute or rule of law or by the enforcement of any assessment or penalty or otherwise, all such liability being, by the acceptance hereof and as part of the consideration for the issue hereof expressly waived and released, as more fully provided in the Indenture

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(Form of Trustee's Certificate)

This bond is one of the bonds of the Series designated therein, described in the within-mentioned Indenture

U.S. BANK NATIONAL ASSOCIATION,

As Trustee,

By \_\_\_\_\_

Authorized Officer

**Section 3:** The Series VV Bonds shall be executed, authenticated and delivered in accordance with the provisions and shall be entitled to the protection and security, of the Original Indenture supplemented by this Forty-Ninth Supplemental Indenture and the other supplemental indentures, and shall be subject to all of the terms, conditions and covenants and limitations thereof. The aggregate principal amount of the Series VV Bonds, which may be executed by the Company and authenticated and delivered by the Trustee and secured by the Indenture as from time to time in effect, is limited only to the extent provided in Section 1 of Article II of the Original Indenture.

ARTICLE II  
SERIES WW BONDS

**Section 1:** There is hereby created, for issuance under the Original Indenture as supplemented by the said Supplemental Indentures (including this Forty-Ninth Supplemental Indenture), a series of bonds designated Series WW, due 2034, each of which shall bear the descriptive title "First Mortgage, Bonds Series WW, due 2034," (herein sometimes referred to as "Series WW Bonds"), and the form thereof shall contain suitable provisions with respect to the matters hereinafter in this Section specified. All of the Series WW Bonds shall be registered bonds without coupons, and shall be substantially of the tenor and purport hereinafter recited. The Series WW Bonds shall mature on February 15, 2034 and shall be issued in denominations of either \$5,000 or \$100,000 and any multiple thereof as the Company may from time to time execute and deliver. The Series WW Bonds shall bear interest from the date of delivery at rates and shall be payable on payment dates which shall correspond exactly to the rates of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series B issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee. Both the principal and interest on the Series WW Bonds shall be payable at the office of the Trustee in St. Paul, Minnesota. The Series WW Bonds shall be dated as in Section 9 of Article II of the Original Indenture provided with respect to registered bonds without coupons.

The Series WW Bonds shall be redeemable as provided in the Form of Reverse of Bond of Series WW, due 2034.

The Series WW Bonds shall be exchangeable for bonds of other authorized denominations and shall be transferable as provided in the Form of Reverse of Bond of Series WW, due 2034.

The Series WW Bonds shall otherwise be of such terms, provisions, tenor and form as provided in this Forty-Ninth Supplemental Indenture.

**Section 2:** The Series WW Bonds and the Trustee's certificate on said Bonds, are to be substantially in the following forms, respectively:

(Form of Face of Bond of Series WW, due 2034)

**THE SERIES WW BONDS REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, AND MAY NOT BE OFFERED OR SOLD IN CONTRAVENTION OF SAID ACT, NOR MAY THEY BE TRANSFERRED EXCEPT TO A TRUSTEE PURSUANT TO THE PROVISIONS OF THAT CERTAIN LOAN AGREEMENT DATED AS OF JUNE 1, 2004, BETWEEN THE CITY OF CHULA VISTA AND SAN DIEGO GAS & ELECTRIC COMPANY.**

SAN DIEGO GAS & ELECTRIC COMPANY  
(INCORPORATED UNDER THE LAWS OF THE STATE OF CALIFORNIA)

FIRST MORTGAGE BOND  
SERIES WW, DUE 2034

No. \_\_\_\_\_ \$ \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY, a corporation organized and existing under the laws of the State of California (hereinafter called the "Company"), for value received, hereby promises to pay to \_\_\_\_\_, or registered assigns, the sum of \_\_\_\_\_ Dollars in lawful money of the United States of America, on the fifteenth day of February, 2034, at the office of U.S. BANK NATIONAL ASSOCIATION as Trustee under the Indenture, as amended, or its successor thereunder, in St. Paul, Minnesota, and to pay to the registered owner hereof interest thereon from the date of delivery hereof until said principal sum shall be paid, at interest rates and on payment dates which shall correspond exactly to the rates of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series B issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee.

The provisions of this bond are continued on the reverse hereof and such continued provisions shall for all purposes have the same effect as though fully set forth at this place.

This bond shall not be valid or become obligatory for any purpose unless and until U.S. BANK NATIONAL ASSOCIATION, as Trustee under the Indenture, as amended, or its successor thereunder, shall have signed the certificate of authentication endorsed hereon.

IN WITNESS WHEREOF, SAN DIEGO GAS & ELECTRIC COMPANY has caused this instrument to be executed in its name by the signature or facsimile signature of its President or any Vice President and its corporate seal, or a facsimile thereof to be hereto affixed and attested by the signature or facsimile signature of its Secretary or any Assistant Secretary.

Dated: \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY

Attest:

\_\_\_\_\_  
By: \_\_\_\_\_

Secretary or Assistant Secretary President or Vice President

(Form of Reverse of Bond of Series WW, due 2034)

This bond is one of a duly authorized issue of bonds of the Company, known as its First Mortgage Bonds, of the series and designation indicated on the face hereof, which issue of bonds consists or may consist, of several series of varying denominations, dates and tenor, all issued and to be issued under and equally secured (except insofar as a sinking fund, or similar fund, established in accordance with the provisions of the Indenture may afford additional security for the bonds of any specific series) by a Mortgage and Deed of Trust dated July 1, 1940, and indentures supplemental thereto, including the Forty-Ninth Supplemental Indenture dated as of June 1, 2004 (which Mortgage and Deed of Trust, as so supplemented, is herein called the "Indenture") executed by the Company to U.S. Bank National Association, as Trustee (herein called the "Trustee"), to which Indenture reference is hereby made for a description of the property mortgaged, pledged, hypothecated and in which a security interest was granted, the nature and extent of the security, the rights of the holders of the bonds and appurtenant coupons as to such security, and the terms and conditions upon which the bonds may be issued under the Indenture and are secured. The principal hereof may be declared or may become due on the conditions, in the manner and at the time set forth in the Indenture, upon the happening of a completed default as in the Indenture provided.

With the consent of the Company and to the extent permitted by and as provided in the Indenture, the rights and obligations of the Company or of the holders of the bonds or coupons, or the terms and provisions of the Indenture or of any indentures supplemental thereto, may be modified or altered by the affirmative vote of the holders of the percentage of principal amount of bonds required by the Indenture; provided, however, that without the consent of the holder hereof no such modification or alteration shall permit the reduction of the principal or the extension of the maturity of the principal of this, bond, or the reduction of the rate of interest hereon, or any other modification of the terms of payment of such principal or interest.

The Company, the Trustee, any paying agent, any registrar, and any depository may deem and treat the person in whose name this bond is registered as the absolute owner hereof for the purpose of receiving payment of or on account of the principal hereof and interest hereon and for all other purposes and shall not be affected by any notice to the contrary.

The Series WW Bonds shall be redeemable, in whole or in part, to the same extent that redemption may be, or is required to be, made of the City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series B as set forth in Section 4.01 of the indenture pursuant to which such bonds were issued. The Series WW Bonds shall also be redeemable, in whole, at a redemption price of 100% of the principal amount, plus accrued interest, if any, on the date the above 2004 Series B Bonds become due and payable upon acceleration or otherwise.

As more fully provided in and subject to the provisions of the Indenture, Series WW are also subject to redemption on any date, under certain circumstances specified in Section 13 of Article XI of the Indenture, upon not less than thirty (30) nor more than sixty (60) days' prior notice, given as aforesaid, in case of the disposition of certain properties of the Company, at 100% of the principal amount thereof, together with accrued interest thereon.

If this bond shall be called for redemption and payment duly provided therefor, as specified in the Indenture, interest shall cease to accrue hereon from and after the date fixed for redemption.

This bond is transferable as prescribed in the Indenture by the registered owner hereof in person, or by his duly authorized attorney, at the office of the Trustee in St. Paul, Minnesota, upon surrender and cancellation of this bond and thereupon a new registered bond of the same series and principal amount will be issued to the transferee in exchange therefor as provided in the Indenture, upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such transfer.

The registered owner of any bond or bonds of the Series WW at the option of such holder, may surrender the same, accompanied by a written instrument of transfer in form approved by the Company duly executed by the registered owner, at the office of the Trustee in St. Paul, Minnesota, for cancellation in exchange for another or other registered bonds of the said series of higher or lower authorized denominations of an aggregate principal amount equal to the aggregate principal amount of the bond or bonds so surrendered and bearing interest as provided in Section 9 of Article II of the Indenture, and upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such exchange and subject to the terms and conditions specified in the Indenture, thereupon the Company shall execute and deliver to the Trustee and the Trustee shall authenticate and deliver such other bonds to such registered owner at its office or at such agency of the Company, at the option of such registered owner.

No recourse shall be had for the payment of the principal of (or premium, if any) or the interest on this bond, or any part thereof, or of any claim based herein or in respect hereof or of said Indenture, against any incorporator, or any past, or future stockholder, officer or director, as such, of the Company or of any predecessor or successor corporation, either directly or through the Company, or through any such predecessor or successor corporation, or through any receiver or a trustee in bankruptcy, whether, by virtue of any constitution, statute or rule of law or by the enforcement of any assessment or penalty or otherwise, all such liability being, by the acceptance hereof and as part of the consideration for the issue hereof expressly waived and released, as more fully provided in the Indenture

\*\*\*\*\*

(Form of Trustee's Certificate)

This bond is one of the bonds of the Series designated therein, described in the within-mentioned Indenture

U.S. BANK NATIONAL ASSOCIATION,

As Trustee,

By \_\_\_\_\_

Authorized Officer

**Section 3:** The Series WW Bonds shall be executed, authenticated and delivered in accordance with the provisions and shall be entitled to the protection and security, of the Original Indenture supplemented by this Forty-Ninth Supplemental Indenture and the other supplemental indentures, and shall be subject to all of the terms, conditions and covenants and limitations thereof. The aggregate principal amount of the Series WW Bonds, which may be executed by the Company and authenticated and delivered by the Trustee and secured by the Indenture as from time to time in effect, is limited only to the extent provided in Section 1 of Article II of the Original Indenture.

**ARTICLE III  
SERIES XX BONDS**

**Section 1:** There is hereby created, for issuance under the Original Indenture as supplemented by the said Supplemental Indenture (including this Forty-Ninth Supplemental Indenture), a series of bonds designated Series XX, due 2034, each of which shall bear the descriptive title "First Mortgage, Bonds Series XX, due 2034," (herein sometimes referred to as "Series XX Bonds"), and the form thereof shall contain suitable provisions with respect to the matters hereinafter in this Section specified. All of the Series XX Bonds shall be registered bonds without coupons, and shall be substantially of the tenor and purport hereinafter recited. The Series XX Bonds shall mature on February 15, 2034 and shall be issued in denominations of either \$5,000 or \$100,000 and any multiple thereof as the Company may from time to time execute and deliver. The Series XX Bonds shall bear interest from the date of delivery at rates and shall be payable on payment dates which shall correspond exactly to the rate s of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series C issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee. Both the principal and interest on the Series XX Bonds shall be payable at the office of the Trustee in St. Paul, Minnesota. The Series XX Bonds shall be dated as in Section 9 of Article II of the Original Indenture provided with respect to registered bonds without coupons.

The Series XX Bonds shall be redeemable as provided in the Form of Reverse of Bond of Series XX due 2034.

The Series XX Bonds shall be exchangeable for bonds of other authorized denominations and shall be transferable as provided in the Form of Reverse of Bond of Series XX due 2034.

The Series XX Bonds shall otherwise be of such terms, provisions, tenor and form as provided in this Forty-Ninth Supplemental Indenture.

**Section 2:** The Series XX Bonds and the Trustee's certificate on said Bonds, are to be substantially in the following forms, respectively:

(Form of Face of Bond of Series XX, due 2034)

**THE SERIES XX BONDS REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, AND MAY NOT BE OFFERED OR SOLD IN CONTRAVENTION OF SAID ACT, NOR MAY THEY BE TRANSFERRED EXCEPT TO A TRUSTEE PURSUANT TO THE PROVISIONS OF THAT CERTAIN LOAN AGREEMENT DATED AS OF JUNE 1, 2004, BETWEEN THE CITY OF CHULA VISTA AND SAN DIEGO GAS & ELECTRIC COMPANY.**

SAN DIEGO GAS & ELECTRIC COMPANY  
(INCORPORATED UNDER THE LAWS OF THE STATE OF CALIFORNIA)

FIRST MORTGAGE BOND  
SERIES XX, DUE 2034

No. \_\_\_\_\_ \$ \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY, a corporation organized and existing under the laws of the State of California (hereinafter called the "Company"), for value received, hereby promises to pay to \_\_\_\_\_, or registered assigns, the sum of \_\_\_\_\_ Dollars in lawful money of the United States of America, on the fifteenth day of February, 2034, at the office of U.S. BANK NATIONAL ASSOCIATION as Trustee under the Indenture, as amended, or its successor thereunder, in St. Paul, Minnesota, and to pay to the registered owner hereof interest thereon from the date of delivery hereof until said principal sum shall be paid, at interest rates and on payment dates which shall correspond exactly to the rates of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series C issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee.

The provisions of this bond on the reverse hereof and such continued provisions shall for all purposes have the same effect as though fully set forth at this place.

This bond shall not be valid or become obligatory for any purpose unless and until U.S. BANK NATIONAL ASSOCIATION, as Trustee under the Indenture, as amended, or its successor thereunder, shall have signed the certificate of authentication endorsed hereon.

IN WITNESS WHEREOF, SAN DIEGO GAS & ELECTRIC COMPANY has caused this instrument to be executed in its name by the signature or facsimile signature of its President or any Vice President and its corporate seal, or a facsimile thereof to be hereto affixed and attested by the signature or facsimile signature of its Secretary or any Assistant Secretary.

Dated: \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY

Attest:

\_\_\_\_\_ By: \_\_\_\_\_

Secretary or Assistant Secretary President or Vice President

(Form of Reverse of Bond of Series XX, due 2034)

This bond is one of a duly authorized issue of bonds of the Company, known as its First Mortgage Bonds, of the series and designation indicated on the face hereof, which issue of bonds consists or may consist, of several series of varying denominations, dates and tenor, all issued and to be issued under and equally secured (except insofar as a sinking fund, or similar fund, established in accordance with the provisions of the Indenture may afford additional security for the bonds of any specific series) by a Mortgage and Deed of Trust dated July 1, 1940, and indentures supplemental thereto, including the Forty-Ninth Supplemental Indenture dated as of June 1, 2004 (which Mortgage and Deed of Trust, as so supplemented, is herein called the "Indenture") executed by the Company to U.S. Bank National Association, as Trustee (herein called the "Trustee"), to which Indenture reference is hereby made for a description of the property mortgaged, pledged, hypothecated and in which a security interest was granted, the nature and extent of the security, the rights of the holders of the bonds and appurtenant coupons as to such security, and the terms and conditions upon which the bonds may be issued under the Indenture and are secured. The principal hereof may be declared or may become due on the conditions, in the manner and at the time set forth in the Indenture, upon the happening of a completed default as in the Indenture provided.

With the consent of the Company and to the extent permitted by and as provided in the Indenture, the rights and obligations of the Company or of the holders of the bonds or coupons, or the terms and provisions of the Indenture or of any indentures supplemental thereto, may be modified or altered by the affirmative vote of the holders of the percentage of principal amount of bonds required by the Indenture; provided, however, that without the consent of the holder hereof no such modification or alteration shall permit the reduction of the principal or the extension of the maturity of the principal of this, bond, or the reduction of the rate of interest hereon, or any other modification of the terms of payment of such principal or interest.

The Company, the Trustee, any paying agent, any registrar, and any depository may deem and treat the person in whose name this bond is registered as the absolute owner hereof for the purpose of receiving payment of or on account of the principal hereof and interest hereon and for all other purposes and shall not be affected by any notice to the contrary.

The Series XX Bonds shall be redeemable, in whole or in part, to the same extent that redemption may be, or is required to be, made of the City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series C as set forth in Section 4.01 of the indenture pursuant to which such bonds were issued. The Series XX Bonds shall also be redeemable, in whole, at a redemption price of 100% of the principal amount, plus accrued interest, if any, on the date the above 2004 Series C Bonds become due and payable upon acceleration or otherwise.

As more fully provided in and subject to the provisions of the Indenture, the Series XX are also subject to redemption on any date, under certain circumstances specified in Section 13 of Article XI of the Indenture, upon not less than thirty (30) nor more than sixty (60) days' prior notice, given as aforesaid, in case of the disposition of certain properties of the Company, at 100% of the principal amount thereof, together with accrued interest thereon.

If this bond shall be called for redemption and payment duly provided therefor, as specified in the Indenture, interest shall cease to accrue hereon from and after the date fixed for redemption.

This bond is transferable as prescribed in the Indenture by the registered owner hereof in person, or by his duly authorized attorney, at the office of the Trustee in St. Paul, Minnesota, upon surrender and cancellation of this bond and thereupon a new registered bond of the same series and principal amount will be issued to the transferee in exchange therefor as provided in the Indenture, upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such transfer.

The registered owner of any bond or bonds of the Series XX at the option of such holder, may surrender the same, accompanied by a written instrument of transfer in form approved by the Company duly executed by the registered owner, at the office of the Trustee in St. Paul, Minnesota, for cancellation in exchange for another or other registered bonds of the said series of higher or lower authorized denominations of an aggregate principal amount equal to the aggregate principal amount of the bond or bonds so surrendered and bearing interest as provided in Section 9 of Article II of the Indenture, and upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such exchange and subject to the terms and conditions specified in the Indenture, thereupon the Company shall execute and deliver to the Trustee and the Trustee shall authenticate and deliver such other bonds to such registered owner at its office or at such agency of the Company, at the option of such registered owner.

No recourse shall be had for the payment of the principal of (or premium, if any) or the interest on this bond, or any part thereof, or of any claim based herein or in respect hereof or of said Indenture, against any incorporator, or any past, or future stockholder, officer or director, as such, of the Company or of any predecessor or successor corporation, either directly or through the Company, or through any such predecessor or successor corporation, or through any receiver or a trustee in bankruptcy, whether, by virtue of any constitution, statute or rule of law or by the enforcement of any assessment or penalty or otherwise, all such liability being, by the acceptance hereof and as part of the consideration for the issue hereof expressly waived and released, as more fully provided in the Indenture

\*\*\*\*\*

(Form of Trustee's Certificate)

This bond is one of the bonds of the Series designated therein, described in the within-mentioned Indenture

U.S. BANK NATIONAL ASSOCIATION,

As Trustee,

By \_\_\_\_\_

Authorized Officer

**Section 3:** The Series XX Bonds shall be executed, authenticated and delivered in accordance with the provisions and shall be entitled to the protection and security, of the Original Indenture supplemented by this Forty-Ninth Supplemental Indenture and the other supplemental indentures, and shall be subject to all of the terms, conditions and covenants and limitations thereof. The aggregate principal amount of the Series XX Bonds, which may be executed by the Company and authenticated and delivered by the Trustee and secured by the Indenture as from time to time in effect, is limited only to the extent provided in Section 1 of Article II of the Original Indenture.

**ARTICLE IV  
SERIES YY BONDS**

**Section 1:** There is hereby created, for issuance under the Original Indenture as supplemented by the said Supplemental Indenture (including this Forty-Ninth Supplemental Indenture), a series of bonds designated Series YY, due 2034, each of which shall bear the descriptive title "First Mortgage, Bonds Series YY, due 2034," (herein sometimes referred to as "Series YY Bonds"), and the form thereof shall contain suitable provisions with respect to the matters hereinafter in this Section specified. All of the Series YY Bonds shall be registered bonds without coupons, and shall be substantially of the tenor and purport hereinafter recited. The Series YY Bonds shall mature on January 1, 2034 and shall be issued in denominations of either \$5,000 or \$100,000 and any multiple thereof as the Company may from time to time execute and deliver. The Series YY Bonds shall bear interest from the date of delivery at rates and shall be payable on payment dates which shall correspond exactly to the rates of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series D issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee. Both the principal and interest on the Series YY Bonds shall be payable at the office of the Trustee in St. Paul, Minnesota. The Series YY Bonds shall be dated as in Section 9 of Article II of the Original Indenture provided with respect to registered bonds without coupons.

The Trustee will rely on the Company for the calculation of interest payable on the Series YY Bonds. In the event that the Company fails to provide the Trustee with such calculations, the Trustee shall be under no obligation to make or cause to be made such calculations.

The Series YY Bonds shall be redeemable as provided in the Form of Reverse of Bond of Series YY, due 2034.

The Series YY Bonds shall be exchangeable for bonds of other authorized denominations and shall be transferable as provided in the Form of Reverse of Bond of Series YY, due 2034.

The Series YY Bonds shall otherwise be of such terms, provisions, tenor and form as provided in this Forty-Ninth Supplemental Indenture.

**Section 2:** The Series YY Bonds and the Trustee's certificate on said Bonds, are to be substantially in the following forms, respectively:

(Form of Face of Bond of Series YY, due 2034)

**THE SERIES YY BONDS REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, AND MAY NOT BE OFFERED OR SOLD IN CONTRAVENTION OF SAID ACT, NOR MAY THEY BE TRANSFERRED EXCEPT TO A TRUSTEE PURSUANT TO THE PROVISIONS OF THAT CERTAIN LOAN AGREEMENT DATED AS OF JUNE 1, 2004, BETWEEN THE CITY OF CHULA VISTA AND SAN DIEGO GAS & ELECTRIC COMPANY.**

SAN DIEGO GAS & ELECTRIC COMPANY  
(INCORPORATED UNDER THE LAWS OF THE STATE OF CALIFORNIA)

FIRST MORTGAGE BOND  
SERIES YY, DUE 2034

No. \_\_\_\_\_ \$ \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY, a corporation organized and existing under the laws of the State of California (hereinafter called the "Company"), for value received, hereby promises to pay to \_\_\_\_\_, or registered assigns, the sum of \_\_\_\_\_ Dollars in lawful money of the United States of America, on the first day of January, 2034, at the office of U.S. BANK NATIONAL ASSOCIATION as Trustee under the Indenture, as amended, or its successor thereunder, in St. Paul, Minnesota, and to pay to the registered owner hereof interest thereon from the date of delivery hereof until said principal sum shall be paid, at interest rates and on payment dates which shall correspond exactly to the rates of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series D issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee.

The provisions of this bond are continued on the reverse hereof and such continued provisions shall for all purposes have the same effect as though fully set forth at this place.

This bond shall not be valid or become obligatory for any purpose unless and until U.S. BANK NATIONAL ASSOCIATION, as Trustee under the Indenture, as amended, or its successor thereunder, shall have signed the certificate of authentication endorsed hereon.

IN WITNESS WHEREOF, SAN DIEGO GAS & ELECTRIC COMPANY has caused this instrument to be executed in its name by the signature or facsimile signature of its President or any Vice President and its corporate seal, or a facsimile thereof to be hereto affixed and attested by the signature or facsimile signature of its Secretary or any Assistant Secretary.

Dated: \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY

Attest:

\_\_\_\_\_  
By: \_\_\_\_\_

Secretary or Assistant Secretary President or Vice President

(Form of Reverse of Bond of Series YY, due 2034)

This bond is one of a duly authorized issue of bonds of the Company, known as its First Mortgage Bonds, of the series and designation indicated on the face hereof, which issue of bonds consists or may consist, of several series of varying denominations, dates and tenor, all issued and to be issued under and equally secured (except insofar as a sinking fund, or similar fund, established in accordance with the provisions of the Indenture may afford additional security for the bonds of any specific series) by a Mortgage and Deed of Trust dated July 1, 1940, and indentures supplemental thereto, including the Forty-Ninth Supplemental Indenture dated as of June 1, 2004 (which Mortgage and Deed of Trust, as so supplemented, is herein called the "Indenture") executed by the Company to U.S. Bank National Association, as Trustee (herein called the "Trustee"), to which Indenture reference is hereby made for a description of the property mortgaged, pledged, hypothecated and in which a security interest was granted, the nature and extent of the security, the rights of the holders of the bonds and appurtenant coupons as to such security, and the terms and conditions upon which the bonds may be issued under the Indenture and are secured. The principal hereof may be declared or may become due on the conditions, in the manner and at the time set forth in the Indenture, upon the happening of a completed default as in the Indenture provided.

With the consent of the Company and to the extent permitted by and as provided in the Indenture, the rights and obligations of the Company or of the holders of the bonds or coupons, or the terms and provisions of the Indenture or of any indentures supplemental thereto, may be modified or altered by the affirmative vote of the holders of the percentage of principal amount of bonds required by the Indenture; provided, however, that without the consent of the holder hereof no such modification or alteration shall permit the reduction of the principal or the extension of the maturity of the principal of this, bond, or the reduction of the rate of interest hereon, or any other modification of the terms of payment of such principal or interest.

The Company, the Trustee, any paying agent, any registrar, and any depository may deem and treat the person in whose name this bond is registered as the absolute owner hereof for the purpose of receiving payment of or on account of the principal hereof and interest hereon and for all other purposes and shall not be affected by any notice to the contrary.

The Series YY Bonds shall be redeemable, in whole or in part, to the same extent that redemption may be, or is required to be, made of the City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series D as set forth in Section 4.01 of the indenture pursuant to which such bonds were issued. The Series YY Bonds shall also be redeemable, in whole, at a redemption price of 100% of the principal amount, plus accrued interest, if any, on the date the above 2004 Series D Bonds become due and payable upon acceleration or otherwise.

As more fully provided in and subject to the provisions of the Indenture, the Series YY are also subject to redemption on any date, under certain circumstances specified in Section 13 of Article XI of the Indenture, upon not less than thirty (30) nor more than sixty (60) days' prior notice, given as aforesaid, in case of the disposition of certain properties of the Company, at 100% of the principal amount thereof, together with accrued interest thereon.

If this bond shall be called for redemption and payment duly provided therefor, as specified in the Indenture, interest shall cease to accrue hereon from and after the date fixed for redemption.

This bond is transferable as prescribed in the Indenture by the registered owner hereof in person, or by his duly authorized attorney, at the office of the Trustee in St. Paul, Minnesota, upon surrender and cancellation of this bond and thereupon a new registered bond of the same series and principal amount will be issued to the transferee in exchange therefor as provided in the Indenture, upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such transfer.

The registered owner of any bond or bonds of the Series YY at the option of such holder, may surrender the same, accompanied by a written instrument of transfer in form approved by the Company duly executed by the registered owner, at the office of the Trustee in St. Paul, Minnesota, for cancellation in exchange for another or other registered bonds of the said series of higher or lower authorized denominations of an aggregate principal amount equal to the aggregate principal amount of the, bond or bonds so surrendered and bearing interest as provided in Section 9 of Article II of the Indenture, and upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such exchange and subject to the terms and conditions specified in the Indenture, thereupon the Company shall execute and deliver to the Trustee and the Trustee shall authenticate and deliver such other bonds to such registered owner at its office or at such agency of the Company, at the option of such registered owner.

No recourse shall be had for the payment of the principal of (or premium, if any) or the interest on this bond, or any part thereof, or of any claim based herein or in respect hereof or of said Indenture, against any incorporator, or any past, or future stockholder, officer or director, as such, of the Company or of any predecessor or successor corporation, either directly or through the Company, or through any such predecessor or successor corporation, or through any receiver or a

trustee in bankruptcy, whether, by virtue of any constitution, statute or rule of law or by the enforcement of any assessment or penalty or otherwise, all such liability being, by the acceptance hereof and as part of the consideration for the issue hereof expressly waived and released, as more fully provided in the Indenture

\*\*\*\*\*

(Form of Trustee's Certificate)

This bond is one of the bonds of the Series designated therein, described in the within-mentioned Indenture

U.S. BANK NATIONAL ASSOCIATION,

As Trustee,

By \_\_\_\_\_

Authorized Officer

**Section 3:** The Series YY Bonds shall be executed, authenticated and delivered in accordance with the provisions and shall be entitled to the protection and security, of the Original Indenture supplemented by this Forty-Ninth Supplemental Indenture and the other supplemental indentures, and shall be subject to all of the terms, conditions and covenants and limitations thereof. The aggregate principal amount of the Series YY Bonds, which may be executed by the Company and authenticated and delivered by the Trustee and secured by the Indenture as from time to time in effect, is limited only to the extent provided in Section 1 of Article II of the Original Indenture.

**ARTICLE V  
SERIES ZZ BONDS**

**Section 1:** There is hereby created, for issuance under the Original Indenture as supplemented by the said Supplemental Indenture (including this Forty-Ninth Supplemental Indenture), a series of bonds designated Series ZZ, due 2034, each of which shall bear the descriptive title "First Mortgage, Bonds Series ZZ, due 2034," (herein sometimes referred to as "Series ZZ Bonds"), and the form thereof shall contain suitable provisions with respect to the matters hereinafter in this Section specified. All of the Series ZZ Bonds shall be registered bonds without coupons, and shall be substantially of the tenor and purport hereinafter recited. The Series ZZ Bonds shall mature on January 1, 2034 and shall be issued in denominations of either \$5,000 or \$100,000 and any multiple thereof as the Company may from time to time execute and deliver. The Series ZZ Bonds shall bear interest from the date of delivery at rates and shall be payable on payment dates which shall correspond exactly to the rates of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series E issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee. Both the principal and interest on the Series ZZ Bonds shall be payable at the office of the Trustee in St. Paul, Minnesota. The Series ZZ Bonds shall be dated as in Section 9 of Article II of the Original Indenture provided with respect to registered bonds without coupons.

The Trustee will rely on the Company for the calculation of interest payable on the Series ZZ Bonds. In the event that the Company fails to provide the Trustee with such calculations, the Trustee shall be under no obligation to make or cause to be made such calculations.

The Series ZZ Bonds shall be redeemable as provided in the Form of Reverse of Bond of Series ZZ, due 2034.

The Series ZZ Bonds shall be exchangeable for bonds of other authorized denominations and shall be transferable as provided in the Form of Reverse of Bond of Series ZZ, due 2034.

The Series ZZ Bonds shall otherwise be of such terms, provisions, tenor and form as provided in this Forty-Ninth Supplemental Indenture.

**Section 2:** The Series ZZ Bonds and the Trustee's certificate on said Bonds, are to be substantially in the following forms, respectively:

(Form of Face of Bond of Series ZZ, due 2034)

**THE SERIES ZZ BONDS REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, AND MAY NOT BE OFFERED OR SOLD IN CONTRAVENTION OF SAID ACT, NOR MAY THEY BE TRANSFERRED EXCEPT TO A TRUSTEE PURSUANT TO THE PROVISIONS OF THAT CERTAIN LOAN AGREEMENT DATED AS OF JUNE 1, 2004, BETWEEN THE CITY OF CHULA VISTA AND SAN DIEGO GAS & ELECTRIC COMPANY.**

SAN DIEGO GAS & ELECTRIC COMPANY  
(INCORPORATED UNDER THE LAWS OF THE STATE OF CALIFORNIA)

FIRST MORTGAGE BOND  
SERIES ZZ, DUE 2034

No. \_\_\_\_\_ \$ \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY, a corporation organized and existing under the laws of the State of California (hereinafter called the "Company"), for value received, hereby promises to pay to \_\_\_\_\_, or registered assigns, the sum of \_\_\_\_\_ Dollars in lawful money of the United States of America, on the first day of January, 2034, at the office of U.S. BANK NATIONAL ASSOCIATION as Trustee under the Indenture, as amended, or its successor thereunder, in St. Paul, Minnesota, and to pay to the registered owner hereof interest thereon from the date of delivery hereof until said principal sum shall be paid, at interest rates and shall be payable on payment dates which shall correspond exactly to the rates of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series E issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee.

The provisions of this bond are continued on the reverse hereof and such continued provisions shall for all purposes have the same effect as though fully set forth at this place.

This bond shall not be valid or become obligatory for any purpose unless and until U.S. BANK NATIONAL ASSOCIATION, as Trustee under the Indenture, as amended, or its successor thereunder, shall have signed the certificate of authentication endorsed hereon.

IN WITNESS WHEREOF, SAN DIEGO GAS & ELECTRIC COMPANY has caused this instrument to be executed in its name by the signature or facsimile signature of its President or any Vice President and its corporate seal, or a facsimile thereof to be hereto affixed and attested by the signature or facsimile signature of its Secretary or any Assistant Secretary.

Dated: \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY

Attest:

By: \_\_\_\_\_

Secretary or Assistant Secretary President or Vice President

(Form of Reverse of Bond of Series ZZ, due 2034)

This bond is one of a duly authorized issue of bonds of the Company, known as its First Mortgage Bonds, of the series and designation indicated on the face hereof, which issue of bonds consists or may consist, of several series of varying denominations, dates and tenor, all issued and to be issued under and equally secured (except insofar as a sinking fund, or similar fund, established in accordance with the provisions of the Indenture may afford additional security for the bonds of any specific series) by a Mortgage and Deed of Trust dated July 1, 1940, and indentures supplemental thereto, including the Forty-Ninth Supplemental Indenture dated as of June 1, 2004 (which Mortgage and Deed of Trust, as so supplemented, is herein called the "Indenture") executed by the Company to U.S. Bank National Association, as Trustee (herein called the "Trustee"), to which Indenture reference is hereby made for a description of the property mortgaged, pledged, hypothecated and in which a security interest was granted, the nature and extent of the security, the rights of the holders of the bonds and appurtenant coupons as to such security, and the terms and conditions upon which the bonds may be issued under the Indenture and are secured. The principal hereof may be declared or may become due on the conditions, in the manner and at the time set forth in the Indenture, upon the happening of a completed default as in the Indenture provided.

With the consent of the Company and to the extent permitted by and as provided in the Indenture, the rights and obligations of the Company or of the holders of the bonds or coupons, or the terms and provisions of the Indenture or of any indentures supplemental thereto, may be modified or altered by the affirmative vote of the holders of the percentage of principal amount of bonds required by the Indenture; provided, however, that without the consent of the holder hereof no such modification or alteration shall permit the reduction of the principal or the extension of the maturity of the principal of this, bond, or the reduction of the rate of interest hereon, or any other modification of the terms of payment of such principal or interest.

The Company, the Trustee, any paying agent, any registrar, and any depository may deem and treat the person in whose name this bond is registered as the absolute owner hereof for the purpose of receiving payment of or on account of the principal hereof and interest hereon and for all other purposes and shall not be affected by any notice to the contrary.

The Series ZZ Bonds shall be redeemable, in whole or in part, to the same extent that redemption may be, or is required to be, made of the City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series E as set forth in Section 4.01 of the indenture pursuant to which such bonds were issued. The Series ZZ Bonds shall also be redeemable, in whole, at a redemption price of 100% of the principal amount, plus accrued interest, if any, on the date the above 2004 Series E Bonds become due and payable upon acceleration or otherwise.

As more fully provided in and subject to the provisions of the Indenture, the Series ZZ are also subject to redemption on any date, under certain circumstances specified in Section 13 of Article XI of the Indenture, upon not less than thirty (30) nor more than sixty (60) days' prior notice, given as aforesaid, in case of the disposition of certain properties of the Company, at 100% of the principal amount thereof, together with accrued interest thereon.

If this bond shall be called for redemption and payment duly provided therefor, as specified in the Indenture, interest shall cease to accrue hereon from and after the date fixed for redemption.

This bond is transferable as prescribed in the Indenture by the registered owner hereof in person, or by his duly authorized attorney, at the office of the Trustee in St. Paul, Minnesota, upon surrender and cancellation of this bond and thereupon a new registered bond of the same series and principal amount will be issued to the transferee in exchange therefor as provided in the Indenture, upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such transfer.

The registered owner of any bond or bonds of the Series ZZ at the option of such holder, may surrender the same, accompanied by a written instrument of transfer in form approved by the Company duly executed by the registered owner, at the office of the Trustee in St. Paul, Minnesota, for cancellation in exchange for another or other registered bonds of the said series of higher or lower authorized denominations of an aggregate principal amount equal to the aggregate principal amount of the, bond or bonds so surrendered and bearing interest as provided in Section 9 of Article II of the Indenture, and upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such exchange and subject to the terms and conditions specified in the Indenture, thereupon the Company shall execute and deliver to the Trustee and the Trustee shall authenticate and deliver such other bonds to such registered owner at its office or at such agency of the Company, at the option of such registered owner.

No recourse shall be had for the payment of the principal of (or premium, if any) or the interest on this bond, or any part thereof, or of any claim based herein or in respect hereof or of said Indenture, against any incorporator, or any past, or future stockholder, officer or director, as such, of the Company or of any predecessor or successor corporation, either directly or through the Company, or through any such predecessor or successor corporation, or through any receiver or a trustee in bankruptcy, whether, by virtue of any constitution, statute or rule of law or by the enforcement of any assessment or penalty or otherwise, all such liability being, by the acceptance hereof and as part of the consideration for the issue hereof expressly waived and released, as more fully provided in the Indenture

\*\*\*\*\*  
(Form of Trustee's Certificate)

This bond is one of the bonds of the Series designated therein, described in the within-mentioned Indenture

U.S. BANK NATIONAL ASSOCIATION,

As Trustee,

By \_\_\_\_\_  
Authorized Officer

**Section 3:** The Series ZZ Bonds shall be executed, authenticated and delivered in accordance with the provisions and shall be entitled to the protection and security, of the Original Indenture supplemented by this Forty-Ninth Supplemental Indenture and the other supplemental indentures, and shall be subject to all of the terms, conditions and covenants and limitations thereof. The aggregate principal amount of the Series ZZ Bonds, which may be executed by the Company and authenticated and delivered by the Trustee and secured by the Indenture as from time to time in effect, is limited only to the extent provided in Section 1 of Article II of the Original Indenture.

**ARTICLE VI  
SERIES AAA BONDS**

**Section 1:** There is hereby created, for issuance under the Original Indenture as supplemented by the said Supplemental Indenture (including this Forty-Ninth Supplemental Indenture), a series of bonds designated Series AAA, due 2039, each of which shall bear the descriptive title "First Mortgage, Bonds Series AAA, due 2039," (herein sometimes referred to as "Series AAA Bonds"), and the form thereof shall contain suitable provisions with respect to the matters hereinafter in this Section specified. All of the Series AAA Bonds shall be registered bonds without coupons, and shall be substantially of the tenor and purport hereinafter recited. The Series AAA Bonds shall mature on May 1, 2039 and shall be issued in denominations of either \$5,000 or \$100,000 and any multiple thereof as the Company may from time to time execute and deliver. The Series AAA Bonds shall bear interest from the date of delivery at rates and shall be payable on payment dates which shall correspond exactly to the rate s of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series F issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee. Both the principal and interest on the Series AAA Bonds shall be payable at the office of the Trustee in St. Paul, Minnesota. The Series AAA Bonds shall be dated as in Section 9 of Article II of the Original Indenture provided with respect to registered bonds without coupons.

The Trustee will rely on the Company for the calculation of interest payable on the Series AAA Bonds. In the event that the Company fails to provide the Trustee with such calculations, the Trustee shall be under no obligation to make or cause to be made such calculations.

The Series AAA Bonds shall be redeemable as provided in the Form of Reverse of Bond of Series AAA, due 2039.

The Series AAA Bonds shall be exchangeable for bonds of other authorized denominations and shall be transferable as provided in the Form of Reverse of Bond of Series AAA, due 2039.

The Series AAA Bonds shall otherwise be of such terms, provisions, tenor and form as provided in this Forty-Ninth Supplemental Indenture.

**Section 2:** The Series AAA Bonds and the Trustee's certificate on said Bonds, are to be substantially in the following forms, respectively:

(Form of Face of Bond of Series AAA, due 2039)

**THE SERIES AAA BONDS REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, AND MAY NOT BE OFFERED OR SOLD IN CONTRAVENTION OF SAID ACT, NOR MAY THEY BE TRANSFERRED EXCEPT TO A TRUSTEE PURSUANT TO THE PROVISIONS OF THAT CERTAIN LOAN AGREEMENT DATED AS OF JUNE 1, 2004, BETWEEN THE CITY OF CHULA VISTA AND SAN DIEGO GAS & ELECTRIC COMPANY.**

SAN DIEGO GAS & ELECTRIC COMPANY  
(INCORPORATED UNDER THE LAWS OF THE STATE OF CALIFORNIA)

FIRST MORTGAGE BOND  
SERIES AAA, DUE 2039

No. \_\_\_\_\_ \$ \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY, a corporation organized and existing under the laws of the State of California (hereinafter called the "Company"), for value received, hereby promises to pay to \_\_\_\_\_, or registered assigns, the sum of \_\_\_\_\_ Dollars in lawful money of the United States of America, on the first day of May, 2039, at the office of U.S. BANK NATIONAL ASSOCIATION as Trustee under the Indenture, as amended, or its successor thereunder, in St. Paul, Minnesota, and to pay to the registered owner hereof interest thereon from the date of delivery hereof until said principal sum shall be paid, at interest rates and on payment dates which shall correspond exactly to the rates of interest and payment dates on the corresponding City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series F issued pursuant to the terms of the Indenture of Trust dated as of June 1, 2004 between the City of Chula Vista and U.S. Bank National Association, as trustee.

The provisions of this bond are continued on the reverse hereof and such continued provisions shall for all purposes have the same effect as though fully set forth at this place.

This bond shall not be valid or become obligatory for any purpose unless and until U.S. BANK NATIONAL ASSOCIATION, as Trustee under the Indenture, as amended, or its successor thereunder, shall have signed the certificate of authentication endorsed hereon.

IN WITNESS WHEREOF, SAN DIEGO GAS & ELECTRIC COMPANY has caused this instrument to be executed in its name by the signature or facsimile signature of its President or any Vice President and its corporate seal, or a facsimile thereof to be hereto affixed and attested by the signature or facsimile signature of its Secretary or any Assistant Secretary.

Dated: \_\_\_\_\_

SAN DIEGO GAS & ELECTRIC COMPANY

Attest:

By: \_\_\_\_\_

Secretary or Assistant Secretary President or Vice President

(Form of Reverse of Bond of Series AAA, due 2039)

This bond is one of a duly authorized issue of bonds of the Company, known as its First Mortgage Bonds, of the series and designation indicated on the face hereof, which issue of bonds consists or may consist, of several series of varying denominations, dates and tenor, all issued and to be issued under and equally secured (except insofar as a sinking fund, or similar fund, established in accordance with the provisions of the Indenture may afford additional security for the bonds of any specific series) by a Mortgage and Deed of Trust dated July 1, 1940, and indentures supplemental thereto, including the Forty-Ninth Supplemental Indenture dated as of June 1, 2004 (which Mortgage and Deed of Trust, as so supplemented, is herein called the "Indenture") executed by the Company to U.S. Bank National Association, as Trustee (herein called the "Trustee"), to which Indenture reference is hereby made for a description of the property mortgaged, pledged, hypothecated and in which a security interest was granted, the nature and extent of the security, the rights of the holders of the bonds and appurtenant coupons as to such security, and the terms and conditions upon which the bonds may be issued under the Indenture and are secured. The principal hereof may be declared or may become due on the conditions, in the manner and at the time set forth in the Indenture, upon the happening of a completed default as in the Indenture provided.

With the consent of the Company and to the extent permitted by and as provided in the Indenture, the rights and obligations of the Company or of the holders of the bonds or coupons, or the terms and provisions of the Indenture or of any indentures supplemental thereto, may be modified or altered by the affirmative vote of the holders of the percentage of principal amount of bonds required by the Indenture; provided, however, that without the consent of the holder hereof no such modification or alteration shall permit the reduction of the principal or the extension of the maturity of the principal of this, bond, or the reduction of the rate of interest hereon, or any other modification of the terms of payment of such principal or interest.



The Company, the Trustee, any paying agent, any registrar, and any depository may deem and treat the person in whose name this bond is registered as the absolute owner hereof for the purpose of receiving payment of or on account of the principal hereof and interest hereon and for all other purposes and shall not be affected by any notice to the contrary.

The Series AAA Bonds shall be redeemable, in whole or in part, to the same extent that redemption may be, or is required to be, made of the City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series F as set forth in Section 4.01 of the indenture pursuant to which such bonds were issued. The Series AAA Bonds shall also be redeemable, in whole, at a redemption price of 100% of the principal amount, plus accrued interest, if any, on the date the above 2004 Series F Bonds become due and payable upon acceleration or otherwise.

As more fully provided in and subject to the provisions of the Indenture, the Series AAA are also subject to redemption on any date, under certain circumstances specified in Section 13 of Article XI of the Indenture, upon not less than thirty (30) nor more than sixty (60) days' prior notice, given as aforesaid, in case of the disposition of certain properties of the Company, at 100% of the principal amount thereof, together with accrued interest thereon.

If this bond shall be called for redemption and payment duly provided therefor, as specified in the Indenture, interest shall cease to accrue hereon from and after the date fixed for redemption.

This bond is transferable as prescribed in the Indenture by the registered owner hereof in person, or by his duly authorized attorney, at the office of the Trustee in St. Paul, Minnesota, upon surrender and cancellation of this bond and thereupon a new registered bond of the same series and principal amount will be issued to the transferee in exchange therefor as provided in the Indenture, upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such transfer.

The registered owner of any bond or bonds of the Series AAA at the option of such holder, may surrender the same, accompanied by a written instrument of transfer in form approved by the Company duly executed by the registered owner, at the office of the Trustee in St. Paul, Minnesota, for cancellation in exchange for another or other registered bonds of the said series of higher or lower authorized denominations of an aggregate principal amount equal to the aggregate principal amount of the, bond or bonds so surrendered and bearing interest as provided in Section 9 of Article II of the Indenture, and upon payment of any tax or taxes or other governmental charges required to be paid by the Company by reason of such exchange and subject to the terms and conditions specified in the Indenture, thereupon the Company shall execute and deliver to the Trustee and the Trustee shall authenticate and deliver such other bonds to such registered owner at its office or at such agency of the Company, at the option of such registered owner.

No recourse shall be had for the payment of the principal of (or premium, if any) or the interest on this bond, or any part thereof, or of any claim based herein or in respect hereof or of said Indenture, against any incorporator, or any past, or future stockholder, officer or director, as such, of the Company or of any predecessor or successor corporation, either directly or through the Company, or through any such predecessor or successor corporation, or through any receiver or a trustee in bankruptcy, whether, by virtue of any constitution, statute or rule of law or by the enforcement of any assessment or penalty or otherwise, all such liability being, by the acceptance hereof and as part of the consideration for the issue hereof expressly waived and released, as more fully provided in the Indenture

\*\*\*\*\*

(Form of Trustee's Certificate)

This bond is one of the bonds of the Series designated therein, described in the within-mentioned Indenture

U.S. BANK NATIONAL ASSOCIATION,

As Trustee,

By \_\_\_\_\_

Authorized Officer

**Section 3:** The Series AAA Bonds shall be executed, authenticated and delivered in accordance with the provisions and shall be entitled to the protection and security, of the Original Indenture supplemented by this Forty-Ninth Supplemental Indenture and the other supplemental indentures, and shall be subject to all of the terms, conditions and covenants and limitations thereof. The aggregate principal amount of the Series AAA Bonds, which may be executed by the Company and authenticated and delivered by the Trustee and secured by the Indenture as from time to time in effect, is limited only to the extent provided in Section I of Article II of the Original Indenture.

#### ARTICLE VII MISCELLANEOUS PROVISIONS

**Section 1:** This instrument is executed and shall be construed as an indenture supplemental to the Original Indenture and shall form a part thereof and, as supplemented by this Forty-Ninth Supplemental Indenture, the Original Indenture as heretofore supplemented and amended is hereby confirmed.

All terms used in this Forty-Ninth Supplemental Indenture shall be taken to have meaning as in the Original Indenture, as heretofore supplemented and amended, except terms which may be otherwise expressly defined herein and in cases where the context clearly indicates otherwise.

In order to facilitate the filing of this Forty-Ninth Supplemental Indenture the same may be executed in several counterparts each of which, when so executed, shall be deemed to be an original, but such counterparts shall constitute but one and the same instrument.

**Section 2:** This Forty-Ninth Supplemental Indenture is dated for convenience June , 2004, although executed and delivered on the date of the acknowledgment hereof by the Trustee and the same shall be effective from the date on which it is so executed and delivered.

**Section 3:** All of the covenants, stipulations, promises and agreements in this Forty-Ninth Supplemental Indenture by or on behalf of the Company shall bind its successors and assigns, whether so expressed or not.

IN WITNESS WHEREOF, SAN DIEGO GAS & ELECTRIC COMPANY has caused this Forty-Ninth Supplemental Indenture to be signed in its name and behalf by its duly authorized officer and its corporate seal to be hereunto affixed duly attested by its Secretary or one of its Assistant Secretaries, and U.S. BANK NATIONAL ASSOCIATION, to evidence its acceptance of the trusts hereby created, has caused this Forty-Ninth Supplemental Indenture to be signed in its name and behalf by its duly authorized officer as of the day and year first above written.

SAN DIEGO GAS & ELECTRIC COMPANY

By: /S/TERRY M. FLESKES

Name: Terry M. Fleskes

Title: Vice President and Treasurer

Attest:

By: /S/THOMAS C. SANGER

Name: Thomas C. Sanger

Title: Secretary

U.S. BANK NATIONAL ASSOCIATION, AS TRUSTEE

By: /S/FONDA HALL

Name: Fonda Hall

Title: Vice President

STATE OF CALIFORNIA

COUNTY OF SAN DIEGO

On June \_\_\_\_, 2004, before me, \_\_\_\_\_, a Notary Public, in and for said County and State, personally appeared Terry M. Fleskes, a Vice President and the Treasurer, and Thomas C. Sanger, the Secretary, of SAN DIEGO GAS & ELECTRIC COMPANY, personally known to me (or proved to me on the basis of satisfactory evidence) to be the persons whose names are subscribed to the within instrument and acknowledged to me that they executed the same in their authorized capacities, and that by their signatures on the instrument the entity upon behalf of which they acted, executed the instrument.

WITNESS my hand and official seal.

STATE OF CALIFORNIA

COUNTY OF LOS ANGELES

On June \_\_\_\_, 2004, before me, \_\_\_\_\_, a Notary Public in and for said County and State, personally appeared \_\_\_\_\_ of U.S. BANK NATIONAL ASSOCIATION, personally known to me (or proved to me on the basis of satisfactory evidence to be the person whose name is subscribed to the within instrument and acknowledged to me that he/she executed the same in his/her authorized capacities, and that by his/her signature on the instrument the entity upon behalf of which he/she acted, executed the instrument.

WITNESS my hand and official seal.

# SOUTHERN CALIFORNIA GAS

## COMPANY

TO

## U.S. BANK NATIONAL ASSOCIATION

(successor by merger to U.S. Bank Trust National Association,  
formerly known as First Trust of California, National Association)

TRUSTEE

SUPPLEMENTAL INDENTURE

To Base Indenture dated October 1, 1940

*Dated as of October 17, 2003*

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THIS SUPPLEMENTAL INDENTURE, dated as of October 17, 2003 (this "Supplemental Indenture"), is made and entered into in the City of Los Angeles, State of California by and between SOUTHERN CALIFORNIA GAS COMPANY, a corporation duly organized and existing under the laws of the State of California, and having its principal place of business in the City of Los Angeles, State of California (hereinafter sometimes called the "Corporation") and U.S. BANK NATIONAL ASSOCIATION (successor by merger to U.S. Bank Trust National Association, formerly known as First Trust of California, National Association), an association duly organized and existing under the laws of the United States of America and having a corporate trust office in the City and County of Los Angeles, State of California (hereinafter, together with its predecessors as trustees under the Indenture referred to below, sometimes called the "Trustee").

**WITNESSETH:**

WHEREAS, the Corporation has executed and delivered to the Trustee a certain Indenture (hereinafter referred to as the "Base Indenture") dated October 1, 1940, to secure bonds of the Corporation designated generally as its "First Mortgage Bonds" to be issued from time to time in one or more series, any of which series may vary from any other as to certain particulars specified in Section 2.01 of the Base Indenture, and the Corporation has executed and delivered to the Trustee supplemental indentures dated, respectively, as of July 1, 1947, May 1, 1948, June 1, 1950, April 1, 1952, August 1, 1955, June 1, 1956, December 1, 1956, July 1, 1957, October 1, 1959, July 1, 1963, September 1, 1964, June 1, 1965, December 1, 1966, October 1, 1970, August 1, 1972, September 1, 1972, October 1, 1974, May 1, 1976, October 1, 1977, November 1, 1979, February 1, 1981, September 15, 1981, April 1, 1982, August 15, 1983, May 18, 1984, December 16, 1985, March 1, 1986, November 15, 1986, December 1, 1986, January 15, 1988, June 15, 1988, November 1, 1988, December 1, 1990, October 1, 1991, August 15, 1992, December 15, 1992, March 1, 1993, June 15, 1993, November 1, 1993, November 15, 1993 and October 1, 2002 supplementing and amending the Base Indenture (each, a "Prior Supplemental Indenture," and the Base Indenture together with all Prior Supplemental Indentures and this Supplemental Indenture being herein collectively referred to as the "Indenture"); and

WHEREAS, the Base Indenture and the Prior Supplemental Indentures dated, respectively, as of July 1, 1947, May 1, 1948, June 1, 1950, April 1, 1952 and August 1, 1955, are recorded in the office of the County Recorder of each of the Counties listed below in the Official Records thereof, as stated in the Prior Supplemental Indenture dated as of June 1, 1956; the Prior Supplemental Indentures dated, respectively, as of June 1, 1956 and December 1, 1956, are so recorded as stated in the Prior Supplemental Indenture dated as of July 1, 1957; the Prior Supplemental Indenture dated as of July 1, 1957 and each subsequently dated Prior Supplemental Indenture (other than the Prior Supplemental Indenture dated October 1, 2002) is so recorded as stated in the Prior Supplemental Indenture dated as of the next succeeding date; and the Prior Supplemental Indenture dated as of October 1, 2002 is recorded in the offices of the County Recorders in the Counties of the State of California, as follows:

County	Reference	Date
Fresno	Official Records, Document 02-0181136	October 14, 2002
Imperial	Official Records, Document 02-026619	October 17, 2002
Kern	Official Records, Document 02-02170190	October 11, 2002
Kings	Official Records, Document 02-22771	October 14, 2002
Los Angeles	Official Records, Document 02-2379242	October 9, 2002
Orange	Official Records, Document 02-0883135	October 11, 2002
Riverside	Official Records, Document 02-568597	October 11, 2002
San Bernardino	Official Records, Document 02-0541056	October 10, 2002
San Diego	Official Records, Document 02-0878743	October 10, 2002
San Luis Obispo	Official Records, Document 02-107564	December 9, 2002
Santa Barbara	Official Records, Document 02-0102671	October 11, 2002
Tulare		

WHEREAS, bonds of the Corporation of three (3) series designated, respectively, as its "First Mortgage Bonds, Series EE, due 2025," "First Mortgage Bonds, Series FF, due 2003" and "First Mortgage Bonds, Series GG, Due 2012" are outstanding as a part of the First Mortgage Bonds referred to in the Indenture, each such series of bonds, unless and until the taking of further appropriate action by the Board of Directors of the Corporation, being without limitation as to aggregate authorized principal amount; and

WHEREAS, pursuant to the provisions of Sections 2.01 and 2.02 of the Indenture, the Board of Directors has, by resolution duly adopted and delivered to the Trustee, created, as a part of the First Mortgage Bonds referred to in the Indenture, a new series of bonds designated "First Mortgage Bonds, Series HH, due 2018" (the "Series HH Bonds"), to be of the form, terms and provisions provided in that resolution and herein, which new series of bonds, unless and until the taking of further appropriate action by the Board of Directors, is to be without limitation as to aggregate authorized principal amount and of which series of bonds in the aggregate principal amount of \$250,000,000 are to be presently issued; and

WHEREAS, it is provided in the Indenture that all the business, franchises and properties, real, personal, and mixed, of every kind and nature whatsoever and wheresoever situated, which might thereafter be acquired by the Corporation, shall be as fully embraced within the lien thereof as if said properties were owned by the Corporation at the date of the Base Indenture and were particularly described therein and specifically conveyed thereby, excepting certain properties expressly excepted by the provisions of the Indenture; and

WHEREAS, subsequent to the execution of the most recently recorded Prior Supplemental Indenture identifying after acquired property, the Corporation has acquired properties hereinafter mentioned or referred to, all of which properties, upon the acquisition thereof by the Corporation, became and now are subject to the lien, operation and effect of the Indenture by virtue of the after-acquired property clause or other clauses thereof; the Corporation, nevertheless, desires to execute, acknowledge, deliver and cause to be recorded this Supplemental Indenture for the purposes, among others, of expressly and specifically subjecting such after-acquired properties to the lien of the Indenture and of further assuring and confirming the lien of the Indenture on all of the properties of every kind and character, whether real or

personal and regardless of the date of acquisition thereof by the Corporation, intended to be subjected to the lien thereof; and

WHEREAS, under the provisions of Sections 2.02 and 16.01 of the Indenture, the Corporation and the Trustee may execute and deliver a Supplemental Indenture (i) to set forth the particulars, permitted by Section 2.01 of the Indenture, as to which the Series HH Bonds may vary from the bonds of the other series of the First Mortgage Bonds, and (ii) for any purpose not inconsistent with the terms of the Indenture; and

WHEREAS, the making, executing, delivering and recording of this Supplemental Indenture have been duly authorized by proper corporate action of the Corporation; and

WHEREAS, the issuance of the Series HH Bonds and the encumbrances of the Corporation's property to secure the Series HH Bonds pursuant to this Supplemental Indenture have been authorized by the Public Utilities Commission of the State of California:

NOW, THEREFORE, in consideration of the foregoing premises and of other good and valuable consideration, receipt of which is hereby acknowledged, and in order: (a) to set forth or specify (i) the form of the fully registered Series HH Bonds, and the form of the certificate to be endorsed on all Series HH Bonds, and (ii) the terms and provisions of the Series HH Bonds, including the particulars thereof which vary from the bonds of the other series of the First Mortgage Bonds; and (b) further to secure the payment of both the principal of and interest on the bonds of the Corporation now or at any time hereafter outstanding under the Indenture, including specifically, but without limitation, all of the First Mortgage Bonds now outstanding and the \$250,000,000 aggregate principal amount of Series HH Bonds and further to secure the observance and performance of all of the covenants, agreements and conditions contained in the Indenture, and without in any way limiting the generality or effect of the Indenture insofar as by any provision thereof any of the property therein or hereafter described or referred to is now subject or intended to be subject to the lien and operation thereof, but to such extent confirming such lien and operation, the Corporation has executed and delivered this Supplemental Indenture and has granted, bargained, sold, released, conveyed, mortgaged, assigned, transferred, pledged, set over and confirmed, and does hereby grant, bargain, sell, release, convey, mortgage, assign, transfer, pledge, set over and confirm unto U.S. Bank National Association, the Trustee, and to its successors or successors in the trust created by the Indenture, and to its and their assigns, forever, with power of sale, subject, to the extent applicable by the terms of the Indenture to any of the properties hereinafter referred to or described, to the exceptions (other than as expressly provided in the granting clauses of the Prior Supplemental Indentures dated respectively as of June 1, 1956, July 1, 1957, October 1, 1959, July 1, 1963, September 1, 1964 and December 1, 1966 with respect to exception (f) set forth on page 67 of the Base Indenture and reading as follows: "(f) Any gas and/or oil acreage, gas and/or oil wells, gas and/or oil reserves, or gas and/or oil leaseholds hereafter acquired by the Corporation, or any property or equipment now or hereafter owned by the Corporation and used for the development of gas and/or oil acreage or for the drilling for or production of gas and/or oil from such acreage;" which exception (f) is by said granting clauses expressly made inapplicable to certain therein specified parcels of property), reservations, conditions, terms and provisions provided in the Indenture with respect to properties subject or intended to be subject thereto, all of the properties and assets of the Corporation, real, personal and mixed, of every kind and character, whether now or hereafter

owned by the Corporation and wheresoever situated, including, without in any way limiting or modifying the generality or effect of the foregoing, all and singular, the following properties:

FIRST: All of the lots, pieces and parcels of land and rights or interests in real property situated in the Counties in the State of California, specifically described and mentioned or enumerated in Schedule A attached hereto, to which reference is hereby made and the same is made a part hereof with the same force and effect as if the same were here set forth at length.

SECOND: All and singular the plants, properties, equipment, real and personal property, estates, interests, goodwill, generating, transmission, feeding, storing, and distribution systems, and utilities of the Corporation situated in the Counties of Fresno, Imperial, Kern, Kings, Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Luis Obispo, Santa Barbara, Tulare and Ventura, and elsewhere, in the State of California, with all and singular the franchises, ordinances, grants, easements, licenses, powers, immunities, permits, privileges, appurtenances, tenements and other rights and property thereunto appertaining or belonging, as the same now exist and as the same and any and all parts thereof may hereafter exist or be improved, added to, enlarged, extended or acquired in said counties or elsewhere in said state or any other state or states.

THIRD: All other property, real, personal and mixed, of every kind, nature and description (including, without in any way limiting the effect or the generality hereof, all facilities; all stocks, bonds and other securities from time to time conveyed, assigned, transferred, mortgaged or pledged on behalf of the Corporation, or with its consent, to the Trustee in the manner and for the purposes as provided in the Indenture; all gas manufacturing plants, boilers, engines, compressors, motors, pumps, generators, gasholders, tanks, appliances, oil storage facilities, gas storage facilities, wells, buildings, structures, plants, works and other improvements; all gas transmission and distributing lines and systems; all meters and regulators and all other apparatus, machinery, appliances, tools, furniture, fixtures, supplies, facilities and utilities and other personal property; or any right or interest in any thereof; all business and goodwill, rights, consents, franchises, ordinances, license s, agreements, contracts, permits, easements, rights of way, leases and leasehold interests; powers, grants, privileges and immunities to construct, operate and maintain lines and other facilities or properties for conveying gas or other commodity or utility for any purpose or purposes through, under and over public streets or highways, or public or private places or property; all reversions, remainders, tolls, incomes, revenues, earnings, rents, issues and profits of any property, real, personal and mixed; and all other classes and types of property described or referred to in the Indenture), now or hereafter owned, held, possessed, acquired or enjoyed by or in any manner conferred upon or appertaining to the Corporation, including the interest of the Corporation in all leases now or hereafter owned by it, together with all and singular the tenements, hereditaments, and appurtenances belonging or in any way appertaining to each and every part of any and all property subject or intended to be subject to the lien and operation of the Indenture, and the reversion and reversions, remainder and remainders, tolls, incomes, revenues, earnings, rents, issues and profits thereof.

SAVING AND EXCEPTING, however, from the property hereby mortgaged, conveyed in trust and/or pledged, all property, whether now owned by the Corporation or hereafter acquired by it, expressly saved and excepted from the lien of the Indenture and therein referred

to as the "excepted property" (except as otherwise expressly provided in any Prior Supplemental Indenture hereinabove mentioned with respect to exception (f) of said "excepted property"), unless and until, upon the occurrence of an event of default under the Indenture, the Trustee, or any receiver appointed thereunder, shall take possession of any or all of such excepted property.

TO HAVE AND TO HOLD in trust with power of sale for the equal and proportionate benefit and security of all holders of bonds of the Corporation, now or hereafter outstanding under the Indenture as from time to time in effect, and for the enforcement and payment of said bonds and interest thereon when payable, and the performance of and compliance with the covenants and conditions of the Indenture as from time to time in effect, without any preference, distinction or priority as to lien or otherwise of any of said bonds over any others thereof by reason of the difference in the time of the actual issue, sale or negotiation thereof, or for any other reason whatsoever, except as otherwise expressly provided in the Indenture as from time to time in effect, so that each and every such bond shall have the same lien and so that the principal and interest of every such bond shall, subject to the terms thereof, be equally and proportionately secured by said lien, as if such bond had been made, executed, delivered, sold and negotiated simultaneously with the execution and delivery of the Base Indenture.

IT IS HEREBY COVENANTED, DECLARED, AND AGREED by and between the parties hereto that all such bonds are issued, authenticated and delivered, or are to be issued, authenticated and delivered, and that all property subject, or to become subject, to the Indenture is to be held, subject to the covenants, conditions, uses and trusts therein set forth.

#### ARTICLE I

#### AMOUNT, FORM, NUMBERING, DENOMINATION, TRANSFER AND EXCHANGE OF SERIES HH BONDS, DUE 2018

Section 1.01. The Series HH Bonds may be issued at any time or from time to time upon and subject to the terms and provisions of the Indenture. Unless and until the taking of further appropriate action by the Board of Directors of the Corporation the Series HH Bonds shall be without limitation as to aggregate authorized principal amount.

Section 1.02. The Series HH Bonds shall be issued only as fully registered bonds without coupons. In addition, the Series HH Bonds may be issuable in whole or in part in the form of one or more securities that evidences all or part of the bonds of such series which is issued to a depository or a nominee thereof for such series (a "Global Security") and, in such case, the Board of Directors shall appoint a clearing agency registered under the Exchange Act of 1934, as amended (the "Exchange Act"), designated to act as depository (a "depository") for such Global Securities.

Section 1.03. In the event the Series HH Bonds are issued as a Global Security the following provisions, in addition to the provisions of the Indenture, shall apply:

(a) Each Global Security authenticated under the Indenture shall be registered in the name of the depository designated for such Global Security or a nominee thereof

and delivered to such depository or a nominee thereof or custodian therefor, and each such Global Security shall constitute a single bond for all purposes of this Supplemental Indenture.

(b) Notwithstanding any other provision in this Supplemental Indenture, no Global Security may be exchanged in whole or in part for bonds registered, and no transfer of a Global Security in whole or in part may be registered, in the name of any person other than the depository for such Global Security or a nominee thereof unless (A) such depository has notified the Corporation that it is unwilling or unable to continue as depository for such Global Security and a successor depository has not been appointed by the Corporation within 90 days of receipt by the Corporation of such notification, (B) if at any time the depository ceases to be a clearing agency registered under the Exchange Act at a time when the depository is required to be so registered to act as such depository and no successor depository shall have been appointed by the Corporation within 90 days after it became aware of such cessation, (C) the Corporation, in its sole discretion, executes and delivers to the Trustee a written order signed in the name of the Corporation by its Chairman of the Board, its President or a Vice President, and by its Treasurer, an Assistant Treasurer, its Secretary or an Assistant Secretary to the effect that such Global Security, together with all other Global Securities of the same series, shall be exchangeable as described below, or (D) an Event of Default (as defined in Section 1.02 of the Indenture) has occurred and is continuing with respect to the Series HH Bonds. If any of the events described in clauses (A) through (D) of the preceding sentence occur, the beneficial owners of interests in the relevant Global Securities will be entitled to exchange those interests for definitive bonds and, without unnecessary delay but in any event not later than the earliest date on which those interests may be so exchanged, the Corporation will deliver to the Trustee definitive bonds in such form and denominations as are required by or pursuant to this Indenture, and of the same series, containing identical terms and in an aggregate principal amount equal to the principal amount of such Global Securities, such bonds to be duly executed by the Corporation. On or after the earliest date on which such beneficial interests may be so exchanged, such Global Securities shall be surrendered from time to time by the depository as shall be specified in the order from the Corporation with respect thereto (which the Corporation agrees to deliver), and in accordance with any instructions given to the Trustee and the depository (which instructions shall be in writing but need not be contained in or accompanied by an officers' certificate or be accompanied by an opinion of counsel), as shall be specified in the order from the Corporation with respect thereto to the Trustee, as the Corporation's agent for such purpose, to be exchanged, in whole or in part, for definitive bonds as described above without charge. The Trustee shall authenticate and make available for delivery, in exchange for each portion of such surrendered Global Security, a like aggregate principal amount of definitive bonds of the same series of authorized denominations and of like tenor as the portion of such Global Security to be exchanged. Promptly following any such exchange in part, such Global Security shall be returned by the Trustee to such depository or its custodian. If a definitive bond is issued in exchange for any portion of a Global Security after the close of business at the place where such exchange occurs on or after (i) any regular record date for the date the interest is due (the "Interest Payment Date") for such bond and before the opening of business at that place of payment on the next Interest Payment Date, or (ii) any special record date for the

payment of interest for such bond and before the opening of business at such place of payment on the related proposed date for the payment of the interest which was not punctually paid or duly provided for on any Interest Payment Date ("Defaulted Interest"), as the case may be, interest shall not be payable on such Interest Payment Date or proposed date for payment, as the case may be, in respect of such definitive bond, but shall be payable on the Interest Payment Date or proposed date for payment, as the case may be, only to the person to whom interest in respect of such portion of such Global Security shall be payable in accordance with the provisions of this Indenture.

(c) Subject to Clause (b) above, any exchange or transfer of a Global Security for other bonds may be made in whole or in part, and all bonds issued in exchange for or upon transfer of a Global Security or any portion thereof shall be registered in such names as the depository for such Global Security shall direct.

(d) Every bond authenticated and delivered upon registration of transfer of, or in exchange for or in lieu of, a Global Security or any portion thereof, shall be authenticated and delivered in the form of, and shall be, a Global Security, unless such bond is registered in the name of a person other than the depository for such Global Security or a nominee thereof.

Section 1.04. Unless otherwise specified as contemplated by Section 2.01 for the bonds evidenced thereby, every Global Security authenticated and delivered hereunder shall bear a legend in substantially the following form:

THIS SECURITY IS A GLOBAL SECURITY WITHIN THE MEANING OF THE INDENTURE HEREINAFTER REFERRED TO AND IS REGISTERED IN THE NAME OF A DEPOSITARY OR A NOMINEE THEREOF. THIS SECURITY MAY NOT BE EXCHANGED IN WHOLE OR IN PART FOR A SECURITY REGISTERED, AND NO TRANSFER OF THIS SECURITY IN WHOLE OR IN PART MAY BE REGISTERED, IN THE NAME OF ANY PERSON OTHER THAN SUCH DEPOSITARY OR A NOMINEE THEREOF, EXCEPT IN THE LIMITED CIRCUMSTANCES DESCRIBED IN THE INDENTURE. ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL INASMUCH AS THE REGISTERED OWNER HEREOF HAS AN INTEREST HEREIN.

Section 1.05. The fully registered bonds without coupons and the certificate of authentication to be endorsed on all Series HH Bonds shall be substantially in the form set forth on Exhibit A.

Section 1.06. The Series HH Bonds may contain or have imprinted thereon such provisions or specifications not inconsistent with the Indenture as may be required to comply with the rules of any stock exchange or any federal or state authority or commission, or to comply with usage with respect thereto; and may bear such other appropriate endorsements or notations as are authorized or permitted by the Indenture.

Section 1.07. The fully registered Series HH Bonds shall be issuable in denominations of \$1,000, \$5,000, \$10,000, \$25,000 or multiples of \$25,000 and shall be dated as provided in paragraph 1 of Section 2.01 of the Indenture. The definitive Series HH Bonds shall be numbered in such manner as the Corporation shall at any time or from time to time determine.

Section 1.08. In the manner and subject to certain conditions and limitations specified herein and in the Indenture, Series HH Bonds may be exchanged without a service charge for a like aggregate principal amount of such Series HH Bonds of other authorized denomination or denominations; provided that the Corporation may require payment of a sum or sums sufficient to reimburse it for any stamp tax or other governmental charge payable in connection therewith.

Section 1.09. The Corporation shall maintain in the City and County of San Francisco, State of California, and in such other place or places as the Corporation may designate at any time or from time to time, an office or agency where Series HH Bonds may be presented for payment, registration, transfer and exchange as provided therein or in the Indenture. Such office or agency in the City and County of San Francisco shall be the corporate trust office of the Trustee unless and until the Corporation shall designate another office or agency by notice in writing delivered to the Trustee. Notwithstanding the foregoing, if and when definitive bonds are issued, the Corporation shall maintain in the Borough of Manhattan, City and County of New York, State of New York, an office or agency where Series HH Bonds may be presented for payment, registration, transfer and exchange as provided therein or in the Indenture.

Section 1.10. No transfer or exchange of any Series HH Bonds pursuant to any of the provisions of this Article I shall be made except upon and in accordance with all of the applicable terms, provisions and conditions of said bonds and of the Indenture.

## ARTICLE II INTEREST, MATURITY DATE, REDEMPTION AND CERTAIN OTHER PROVISIONS OF SERIES HH BONDS, DUE 2018

Section 2.01. The Series HH Bonds shall bear interest at the rate, shall be expressed to mature as to principal, and shall be payable as to principal and interest at such place or places and in such money, all as provided in the form of Series HH Bond set forth on Exhibit A hereto and by the applicable provisions of the Indenture. In addition, October 17, 2003 shall be an Interest Payment Date for the Series HH Bonds for purposes of Section 2.01 of the Base Indenture (as supplemented by the Prior Supplemental Indentures), provided that no interest shall be payable on such date.

Section 2.02. The Series HH Bonds shall be subject to redemption prior to maturity as set forth in the form of Series HH Bond set forth on Exhibit A, upon notice, in the manner and otherwise upon the terms and conditions and with the effect, as provided herein and by the applicable provisions of the Indenture.

Section 2.03. The Corporation may at any time deliver to the Trustee for cancellation any Series HH Bonds previously authenticated and delivered under the Indenture which the

Corporation may have acquired in any manner whatsoever and all Series HH Bonds so delivered shall be promptly cancelled by the Trustee upon the request of the Corporation.

Section 2.04. The Series HH Bonds shall, except as in this Supplemental Indenture otherwise expressly provided, be on the terms and provisions, and shall represent such rights and be entitled to such benefits, as are applicable thereto by the terms of the Indenture.

Section 2.05. The Series HH Bonds shall be entitled to the benefits of the Renewal Fund as provided in the Indenture.

Section 2.06. The following Section 11.01A shall apply to the Series HH Bonds in lieu of Section 11.01 of the Indenture:

"Section 11.01A If the Corporation, its successors or assigns, shall

- (a) pay or cause to be paid the principal of and interest on the bonds and coupons and claims for interest thereon to become due at the time and in the manner stipulated therein and herein, and/or
  - (b) provide for the payment of the bonds and interest thereon by depositing in cash with the Trustee or other depository satisfactory to it at any time at or before maturity the entire amount due or to become due thereon for principal and interest to maturity of all the bonds outstanding, and/or
  - (c) in case of a call of all of the bonds then outstanding for redemption, deposit with the Trustee on or before the date on which all of such bonds (other than those which shall have matured by their terms) shall have been called for redemption, as provided in Article VII, the entire amount of the redemption price thereof, including interest and premium, if any, and shall deliver to the Trustee (1) proof satisfactory to the Trustee that notice of redemption as provided in Article VII has been given, or (2) proof satisfactory to the Trustee that arrangements have been made insuring that such notice will be given, or (3) a written instrument executed by the Corporation under its corporate seal, and expressed to be irrevocable, authorizing the Trustee to give such notice for and on behalf of the Corporation, and/or
  - (d) surrender to the Trustee for cancellation all the bonds and coupons thereto appertaining for which payment is not so provided,
- and shall also pay, or satisfactorily provide, all other sums due and payable hereunder by the Corporation, including the compensation and expenses of the Trustee, then and in that case,
- (i) at the request of the Corporation all the mortgaged property shall revert to the Corporation and the entire estate, right, title and interest of the Trustee and of the holders and registered owners of the bonds and coupons in respect of the mortgaged property shall thereupon cease, determine and become void; and
  - (ii) the Trustee in such case, upon the cancellation of all outstanding bonds and coupons for the payment of which cash shall not have been deposited in accordance

with the provisions of this Indenture, shall upon request of the Corporation, and at its cost and expense (A) and upon delivery to it of an opinion of counsel stating that (x) the Corporation has received from, or there has been published by, the Internal Revenue Service a ruling, or (y) since October 14, 2003 there has been a change in applicable federal income tax law, in either case to the effect that, and based thereon such opinion of counsel shall confirm that, the holders of Series HH Bonds will not recognize income, gain or loss for federal income tax purposes as a result of such defeasance and will be subject to federal income tax on the same amounts, in the same manner and at the same times as would have been the case if such defeasance had not occurred, execute to the Corporation, or its order, proper instruments acknowledging satisfaction of this Indenture and (B) shall surrender to the Corporation, or its order, all cash and deposited securities, if any, which shall then be held by it hereunder as a part of the mortgaged property (exclusive of cash held in trust as provided in Section 5.03); provided, however, that if any such property shall have been delivered to the Trustee by any person or corporation other than the Corporation, the same shall be delivered or otherwise disposed of in accordance with any reservations, limitations, conditions or provisions which may have been set forth in the instrument in writing then executed, if any, respecting the use, management or disposition thereof; and provided further that if the Corporation pursuant to clauses (1) or (2) of subdivision (c) above shall have delivered to the Trustee proof satisfactory to it that notice of redemption as provided in Article VII has been given or that arrangements have been made insuring that such notice will be given, there shall also be delivered to the Trustee an officers' certificate stating that all conditions precedent to the satisfaction and discharge of this Indenture have been complied with and an opinion of counsel stating that in his opinion such conditions precedent have been complied with."

### ARTICLE III SUNDRY PROVISIONS

Section 3.01. The recitals of fact contained herein shall be taken as the statements of the Corporation, and the Trustee assumes no responsibility for the correctness of the same. The Corporation hereby covenants and agrees that it will cause this Supplemental Indenture to be kept recorded and/or filed as may be required by law, in such manner and in such places as may be necessary fully to preserve and protect the security of the bondholders and all of the rights of the Trustee hereunder, and that it will with all reasonable dispatch deposit with the Trustee counterparts of this Supplemental Indenture bearing official notation or endorsements showing such recordation and/or filing, or in case such counterparts are not returned to the Corporation, furnish to the Trustee the best official evidence of such recordation and/or filing reasonably obtainable by the Corporation, or evidence of the taking of such other action, if any, but the Trustee, subject to the provisions of Sections 14.02 and 14.03 of the Indenture, shall in no way be liable for any failure or omission in this regard.

Section 3.02. The date of this Supplemental Indenture and the date of the Series HH Bonds are intended as and for a date for the convenient identification of this Supplemental Indenture and of the Series HH Bonds, and are not intended to indicate that this Supplemental Indenture was executed and delivered or that the Series HH Bonds were executed, delivered or

issued on said date; it being hereby provided that this Supplemental Indenture may be executed and delivered, and that the Series HH Bonds may be executed, delivered or issued, either on said date or before or after said date, and that this Supplemental Indenture is in fact executed and delivered by each party hereto on the date of its certificate of acknowledgment hereto attached.

Section 3.03. This Supplemental Indenture shall be deemed to be part of the Base Indenture, and the Corporation agrees to conform to and comply with all and singular the terms, provisions, conditions and covenants set forth therein and herein. This Supplemental Indenture shall be construed in connection with and as a part of the Indenture.

Section 3.04. It is further agreed that the Trustee accepts the trust imposed upon it by this Supplemental Indenture, upon and subject to the same terms and conditions as are expressed in Article XIV of the Base Indenture.

Section 3.05. In order to facilitate the recording of this Supplemental Indenture, the same may be, executed in several counterparts, each of which so executed shall be deemed to be an original, and such counterparts shall collectively constitute one and the same instrument.

Section 3.06. All terms used in this Supplemental Indenture which are defined in the Indenture are not defined herein shall have the meaning assigned to them in the Indenture.

Section 3.07. To the extent any provision in this Supplemental Indenture conflicts with any provision in the Indenture, the provisions of this Supplemental Indenture shall govern; provided however, that in the event such conflict would require bondholder consent, the terms and provisions of the Indenture shall govern.

Section 3.08. This Supplemental Indenture and the Series HH Bonds shall be governed by and construed in accordance with the laws of the State of California, without regard to conflicts of laws principles thereof.

Section 3.09. To the extent not otherwise addressed in this Supplemental Indenture, this Supplemental Indenture shall be subject to the provisions of Article XVII of the Indenture, the terms of which are hereby incorporated by referenced into this Indenture Supplement.

IN WITNESS WHEREOF, Southern California Gas Company has caused this Supplemental Indenture to be signed in its corporate name by one of its Vice Presidents or its Treasurer and its Secretary or an Assistant Secretary and its corporate seal to be hereunto duly

affixed, and U.S. Bank National Association, in token of its acceptance of the trust hereby established, has caused this Supplemental Indenture to be signed in its corporate name by two of its authorized officers, including one or more of its Vice Presidents, all as of October 17, 2003.

Attest:	SOUTHERN CALIFORNIA GAS COMPANY
/S/ W. DAVIS SMITH	/S/ TERRY M. FLESKES
Name: W. Davis Smith	Name: Terry M. Fleskes
Title: Assistant Secretary	Title: Vice President and Treasurer

Attest:	U.S. BANK NATIONAL ASSOCIATION
	By:

Name: Ashraf Almurdaah  
Title: Vice President

Name: Fonda Hall  
Title: Vice President

STATE OF CALIFORNIA  
COUNTY OF SAN DIEGO

On this 15..day of October, 2003, before me, ..... Notary Public, personally appeared Terry M. Fleskes, personally known to me to be one of the persons whose names are subscribed to the within instrument, and acknowledged to me that he executed the same in his authorized capacity, and that by his signature on the instrument, the entity upon behalf of which he acted executed the instrument.

WITNESS my hand and official seal.

Notary Public

My Commission expires .....

DEBORA R. COVEY . Commission # 1294854

Notary Public California San Diego County My comm. Expires Mar 20, 2005

STATE OF CALIFORNIA  
COUNTY OF SAN DIEGO

On this 15 day of October, 2003, before me, ..... Notary Public, personally appeared W. Davis Smith, personally known to me to be one of the persons whose names are subscribed to the within instrument and acknowledged to me that he executed the same in his authorized capacity and that by his signature on the instrument, the entity upon behalf of which he acted executed the instrument.

WITNESS my hand and official seal.

Notary Public

My Commission expires .....

DEBORA R. COVEY . Commission # 1294854

Notary Public California San Diego County My comm. Expires Mar 20, 2005

IN WITNESS WHEREOF, Southern California Gas Company has caused this Supplemental Indenture to be signed in its corporate name by one of its Vice Presidents or its Treasurer and its Secretary or an Assistant Secretary and its corporate seal to be hereunto duly affixed, and U.S. Bank National Association, in token of its acceptance of the trust hereby established, has caused this Supplemental Indenture to be signed in its corporate name by two of its authorized officers, including one or more of its Vice Presidents, all as of October 17, 2003.

Attest:  
  
.....

Name: W. Davis Smith  
Title: Assistant Secretary

SOUTHERN CALIFORNIA GAS COMPANY  
  
By: .....

Name: Terry M. Fleskes  
Title: Vice President and Treasurer

Attest:  
  
/S/ASHRAF ALMURDAAH  
-----

Name: Ashraf Almurdaah  
Title: Vice President

U.S. BANK NATIONAL ASSOCIATION  
  
/S/FONDA HALL  
-----

Name: Fonda Hall  
Title: Vice President

CALIFORNIA ALL-PURPOSE ACKNOWLEDGEMENT

State of California  
County of Los Angeles



On October 16, 2003, before me, Ismael Diaz, Notary Public, personally appeared Fonda Hall and Ashraf Almurdaah, personally known to me, to be the person(s) whose name(s) are subscribed to the within instrument and acknowledged to me that they executed the same in their authorized capacity(ies), and that by their signature(s) on the instrument the person(s), or the entity upon behalf of which the person(s) acted, executed the instrument.

WITNESS my hand and official seal.

Ismael Diaz

Commission # 1242949

Notary Public-California

Los Angeles County

My Comm. Expires Nov. 22, 2003

#### SCHEDULE A

Incorporated in and made a part of the Supplemental Indenture dated as of October 17, 2003, by and among Southern California Gas Company and U.S. Bank National Association, Trustee.

The descriptive names or captions do not constitute a part of the property descriptions, being used only for convenience of reference and not identification.

#### COUNTY OF SAN BERNARDINO

Those certain lots, pieces and parcels of land and other property, rights and estates situated in the County of San Bernardino, State of California, described as follows:

##### San Bernardino Base (Adjacent Parcel)

THAT PORTION OF LOT 17, LYING SOUTH OF THE ATCHISON, TOPEKA AND SANTA FE RAILROAD RIGHT OF WAY, IN BLOCK 11, OF RANCHO SAN BERNARDINO, IN THE CITY OF SAN BERNARDINO, COUNTY OF SAN BERNARDINO, STATE OF CALIFORNIA, AS PER PLAT RECORDED IN BOOK 7 OF MAPS, PAGE 2, RECORDS OF SAID COUNTY, DESCRIBED AS FOLLOWS:

BEGINNING AT A POINT ON THE WEST LINE OF SAID LOT 17, ADJOINING THE SOUTH LINE OF THE ATCHISON, TOPEKA AND SANTA FE RAILWAY RIGHT OF WAY; THENCE SOUTH ALONG THE WEST LINE OF SAID LOT, 140 FEET; THENCE EAST 200 FEET; THENCE NORTH 140 FEET; THENCE WEST 200 FEET TO THE POINT OF BEGINNING.

ASSESSOR'S PARCEL NUMBER: 0136-101-15

##### San Bernardino Base (Adjacent Parcel)

PARCEL 1:

THAT PORTION OF LOT 17, BLOCK 11 OF RANCHO SAN BERNARDINO, IN THE COUNTY OF SAN BERNARDINO, STATE OF CALIFORNIA, AS PER PLAT RECORDED IN BOOK 7, OF MAPS, PAGE 2, RECORDS OF SAID COUNTY, AND MORE PARTICULARLY DESCRIBED AS FOLLOWS:

COMMENCING AT THE INTERSECTION OF THE EAST LINE OF SAID 17 WITH THE SOUTH LINE OF ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY RIGHT OF WAY; THENCE ALONG THE EAST LINE OF SAID LOT, SOUTH 220 FEET; THENCE WEST PARALLEL TO THE SOUTH LINE OF SAID RAILWAY RIGHT OF WAY 240.54 FEET TO THE EAST LINE OF THE LAND CONVEYED TO THE SOUTHERN CALIFORNIA GAS COMPANY BY DEED RECORDED JULY 26, 1938, IN BOOK 1290, PAGE 101, OFFICIAL RECORDS; THENCE NORTH ALONG THE EAST LINE OF SAID GAS COMPANY LAND 220 FEET TO THE SOUTH LINE OF SAID RAILWAY RIGHT OF

WAY; THENCE EAST ALONG SAID RAILWAY RIGHT OF WAY 240.44 FEET TO THE POINT OF BEGINNING.

PARCEL 2:

AN EASEMENT AND RIGHT OF WAY FOR INGRESS AND EGRESS OVER PROPERTY DESCRIBED AS FOLLOWS:

PORTION OF LOTS 16 AND 17, BLOCK 11, RANCHO SAN BERNARDINO, IN THE CITY OF SAN BERNARDINO, AS PER PLAT RECORDED IN BOOK 7, OF MAPS, PAGE 2, RECORDS OF SAID COUNTY, DESCRIBED AS FOLLOWS:

BEGINNING AT A POINT IN THE EAST LINE OF "G" STREET WHICH IS 155 FEET SOUTH MEASURED ALONG SAID LINE FROM THE NORTH LINE OF SAID LOT 16, SAID POINT ALSO BEING THE SOUTHWEST CORNER OF THAT CERTAIN PARCEL OF LAND CONVEYED TO THE SIGNAL OIL COMPANY BY DEED RECORDED FEBRUARY 9, 1942, IN BOOK 1514, PAGE 419, OFFICIAL RECORDS;

THENCE EAST ALONG THE SOUTH LINE OF SAID SIGNAL OIL COMPANY LAND AND THE EASTERLY EXTENSION THEREOF 400 FEET TO THE SOUTHEAST CORNER OF THAT CERTAIN PARCEL OF LAND CONVEYED TO THE SIGNAL OIL COMPANY BY DEED RECORDED JANUARY 19, 1946, IN BOOK 1861, PAGE 231, OFFICIAL RECORDS; THENCE NORTH ALONG THE EAST LINE OF SAID OIL COMPANY'S LAND AND OF LAND CONVEYED TO THE SOUTHERN CALIFORNIA GAS COMPANY BY DEED RECORDED JULY 26, 1938, IN BOOK 1290, PAGE 101, OFFICIAL RECORDS, 254.86 FEET TO A POINT DISTANT 220 FEET SOUTH OF THE SOUTH LINE AT THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY RIGHT OF WAY; THENCE EAST 30 FEET; THENCE SOUTH 284.86 FEET TO A POINT WHICH IS 504.86 FEET SOUTH OF THE SAID SOUTH LINE OF SAID RIGHT OF WAY; THENCE WEST 430 FEET TO THE EAST LINE OF "G" STREET; THENCE NORTH ALONG SAID LAST NAMED LINE 30 FEET TO THE POINT OF BEGINNING.

ASSESSOR'S PARCEL NUMBER: 131-101-14

#### EXHIBIT A

[FORM OF REGISTERED BOND WITHOUT COUPONS, SERIES HH, DUE 2018]

[If this bond is issued as a global security, insert the following legend: THIS SECURITY IS A GLOBAL SECURITY WITHIN THE MEANING OF THE INDENTURE HEREINAFTER REFERRED TO AND IS REGISTERED IN THE NAME OF A DEPOSITARY OR A NOMINEE THEREOF. THIS SECURITY MAY NOT BE EXCHANGED IN WHOLE OR IN PART FOR A SECURITY REGISTERED, AND NO TRANSFER OF THIS SECURITY IN WHOLE OR IN PART MAY BE REGISTERED, IN THE NAME OF ANY PERSON OTHER THAN SUCH DEPOSITARY OR A NOMINEE THEREOF, EXCEPT IN THE LIMITED CIRCUMSTANCES DESCRIBED IN THE INDENTURE. ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL INASMUCH AS THE REGISTERED OWNER HEREOF HAS AN INTEREST HEREIN.]

**SOUTHERN CALIFORNIA GAS COMPANY**  
**(Incorporated under the laws of the State of California)**

**FIRST MORTGAGE BOND, SERIES HH, DUE 2018**  
**5.45%**

SOUTHERN CALIFORNIA GAS COMPANY, a corporation organized and existing under the laws of the State of California (hereinafter called the "Corporation", which term shall include any successor corporation, as defined in the Indenture hereinafter referred to), for value received, hereby promises to pay to [If this bond is issued as a global security, insert "CEDE & CO." in the foregoing - space] or registered assigns, the principal sum of in lawful money of the United States of America, on the fifteenth day of April, 2018, and to pay interest thereon from the date of this bond, at the rate of 5.45% per annum in like lawful money, payable semi-annually, on the fifteenth day of April and October in each year, to the holder of record of this bond on the immediately preceding first day of April and October, respectively, commencing April 15, 2004, until the Corporation's obligation with respect to the payment of such principal shall be discharged as provided in the Indenture hereinafter mentioned. Both the principal of and interest on this bond will be paid at the corporate trust office of U.S. Bank National Association, or its successor trustee under said Indenture, in the City and County of San Francisco, State of California [if this bond is a definitive bond, insert: ", or at the office or agency in the Borough of Manhattan, City and County of New York, State of New York, that the Corporation maintains for such purpose"]. Notwithstanding the foregoing, so long as the holder of the Series HH Bonds is a depositary, or its nominee, payment of the principal of (and premium, if any) and interest on this bond will be made by wire transfer of immediately available funds.

The provisions of this bond are continued on the reverse hereof and such continued provisions shall for all purposes have the same effect as though set forth at this place.

IN WITNESS WHEREOF, SOUTHERN CALIFORNIA GAS COMPANY has caused this bond to be signed in its corporate name by the facsimile signature of its authorized officer and a facsimile of its corporate seal to be hereto affixed and attested by its Secretary or an Assistant Secretary.

Dated:

SOUTHERN CALIFORNIA GAS COMPANY

(CORPORATE SEAL BY)

Vice President

Attest:

Secretary

[REVERSE SIDE - FORM OF REGISTERED BOND  
WITHOUT COUPONS, SERIES HH, DUE 2018]

*This bond is one of a duly authorized issue of bonds of the Corporation (herein called the "bonds"), of the series hereinafter specified, all issued and to be issued under and all equally and ratably secured by a mortgage and deed of trust dated October 1, 1940, between the Corporation and U.S. Bank National Association, as successor trustee, to which mortgage and deed of trust and all indentures supplemental thereto, including Supplemental Indentures dated, respectively, as of July 1, 1947, August 1, 1955, June 1, 1956, December 1, 1956, June 1, 1965, August 1, 1972, May 1, 1976, September 15, 1981, May 18, 1984, November 15, 1986, January 15, 1988, August 15, 1992 and October 1, 2002 (herein collectively referred to as the "Indenture"), reference is hereby made for a description of the property conveyed in trust, mortgaged and pledged, the nature and extent of the security, the rights of the registered owners of the bonds and of the Trustee or trustees in respect thereof, the terms and conditions upon which the bonds are, and are to be, secured and the circumstances under which additional bonds may be issued. The bonds may be issued for various principal sums, and may be issued in series, which may mature at different times, may bear interest at different times, may bear interest at different rates and may otherwise vary as in the Indenture provided. This bond is one of a series designated as the "First Mortgage Bonds, Series HH, due 2018" (herein called "Series HH" Bonds) of the Corporation, issued under and secured by the Indenture. Terms used but not defined herein shall have the respective meanings assigned thereto in the Indenture.*

*As provided in the Indenture, by any indenture or indentures supplemental thereto executed by the Corporation and the Trustee and consented to by the holders of not less than two-thirds (2/3) in principal amount of the bonds at the time outstanding, and, in case one or more, but less than all, of the series of bonds then outstanding are affected by such supplemental indenture, consented to by the holders of at least two-thirds (2/3) in principal amount of the bonds of each series so affected, the Indenture or any indenture supplemental thereto and the rights and obligations of the Corporation and the holders of bonds, may be modified or altered from time to time, as provided in the Indenture; provided, however, (a) that the right of any holder of any bond to receive payment of the principal of and interest on such bond, on or after the respective due dates expressed in such bond, or to institute suit for the enforcement of any such payment on or after such respective dates, shall not be impaired or affected by any such supplemental indenture without the consent of such holder, and (b) that no such modification or alteration shall reduce the proportions of bondholders' consents required as aforesaid; such proportions to be determined in each case as provided in the Indenture.*

*The Series HH Bonds are entitled to the benefits of the Renewal Fund as provided in the Indenture.*

*All or a portion of the Series HH Bonds may be redeemed at the Corporation's option at any time or from time to time.*

*The price at which the Series HH Bonds will be redeemed (the "Redemption Price") on the date fixed for such redemption (the "Redemption Date") will be equal to the greater of the following amounts: (a) 100% of the principal amount of the bonds being redeemed on the*

*Redemption Date; or (b) the sum of the present values of the remaining scheduled payments of principal and interest on the Series HH Bonds being redeemed on that Redemption Date (not including any portion of any payments of accrued and unpaid interest to the Redemption Date) discounted to the Redemption Date on a semiannual basis at the Adjusted Treasury Rate (as defined below) plus 20 basis points, as determined by the Reference Treasury Dealer (as defined below), plus, in each case, accrued and unpaid interest thereon to the Redemption Date. Notwithstanding the foregoing, installments of interest on Series HH Bonds that are due and payable on Interest Payment Dates falling on or prior to a Redemption Date will be payable on such Interest Payment Dates to the registered holders of such Series HH Bonds as of the close of business on the relevant record date. The Redemption Price will be calculated on the basis of a 360-day year consisting of twelve 30-day months.*

*Unless the Corporation defaults in payment of the Redemption Price, on and after the Redemption Date interest will cease to accrue on the Series HH Bonds or portions thereof called for redemption.*

*"Adjusted Treasury Rate" means, with respect to any Redemption Date, the rate per annum equal to the semiannual equivalent yield to maturity of the Comparable Treasury Issue, assuming a price for the Comparable Treasury Issue (expressed as a percentage of its principal amount) equal to the Comparable Treasury Price for such Redemption Date.*

*"Comparable Treasury Issue" means the United States Treasury security selected by the Reference Treasury Dealer as having a maturity comparable to the remaining term of the Series HH Bonds to be redeemed that would be utilized, at the time of selection and in accordance with customary financial practice, in pricing new issues of corporate debt securities of comparable maturity to the remaining term of such Series HH Bonds.*

*"Comparable Treasury Price" means, with respect to any Redemption Date, (A) the average of the Reference Treasury Dealer Quotations for such Redemption Date, or (B) if only one Reference Treasury Dealer Quotation is received, such Quotation.*

*"Reference Treasury Dealer" means (A) ABN AMRO Incorporated and Banc One Capital Markets, Inc. (or their respective affiliates which are Primary Treasury Dealers), and their respective successors; provided, however, that if any of the foregoing shall cease to be a*

*primary U.S. Government securities dealer in New York City (a "Primary Treasury Dealer"), the Corporation will substitute therefor another Primary Treasury Dealer(s); and (B) any other Primary Treasury Dealer selected by the Corporation.*

*"Reference Treasury Dealer Quotation" means, with respect to each Reference Treasury Dealer and any Redemption Date, the average, as determined by the Corporation, of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its*

*principal amount) quoted in writing to the Corporation by such Reference Treasury Dealer at 5:00 p.m. (New York City time) on the third business day preceding such Redemption Date.*

*In the event of redemption of this bond in part only, a new bond or Series HH Bonds and of like tenor for the unredeemed portion hereof will be issued in the name of the holder hereof upon the cancellation hereof.*

*Notice of any such redemption will be mailed to the registered owners of the Series HH Bonds to be redeemed not less than 30 nor more than 60 days before the Redemption Date. Once notice of redemption is mailed, the Series HH Bonds called for redemption will become due and payable on the Redemption Date and at the applicable redemption price, plus accrued and unpaid interest to the Redemption Date. Upon the Corporation's election to redeem all or a portion of the Series HH Bonds, that redemption will not be conditional upon receipt by the paying agent or the Trustee of monies sufficient to pay the Redemption Price.*

*In case an event of default, as defined in the Indenture, shall occur, the principal of all bonds then outstanding under the Indenture may be declared or become due and payable upon the conditions and in the manner and with the effect provided in the Indenture.*

*This bond is transferable by the registered owner hereof at the office or agency of the Corporation in said City and County of San Francisco [if this bond is a definitive bond, insert: ", or at the office or agency in the Borough of Manhattan, City and County of New York, State of New York, that the Corporation maintains for such purpose"] and in such other place or places as the Corporation may designate at any time or from time to time, and thereupon a new fully registered bond or bonds of said series, without coupons, of authorized denomination or denominations, of a like aggregate principal amount, will be issued to the transferee or transferees in exchange for this bond; and at any of said offices or agencies fully registered Series HH Bonds without coupons,*

are exchangeable for a like aggregate principal amount of other such fully registered bonds of authorized denominations; all in the manner and subject to the conditions as provided in the Indenture.

No recourse shall be had for the payment of the principal of or the interest on this bond or for any claim based hereon or on the Indenture or any indenture supplemental thereto, against any incorporator, stockholder, director or officer, past, present or future, of the Corporation, or of any predecessor or successor corporation, either directly or through the Corporation, or any such predecessor or successor corporation, whether by virtue of any constitution, statute or rule of law, or by the enforcement of any assessment or penalty, or otherwise, all such liability being waived and released by every registered owner hereof by the acceptance of this bond and as part of the consideration for the issue hereof, and being likewise waived and released by the terms of the Indenture.

This bond shall not become valid or obligatory for any purpose or be entitled to any benefit under the Indenture until U.S. Bank National Association, or its successor as Trustee under the Indenture, shall have signed the form of certificate endorsed hereon.

This bond shall be governed by and construed in accordance with the laws of the State of California, without regard to conflicts of laws principles thereof.

[FORM OF CERTIFICATE OF AUTHENTICATION]  
CERTIFICATE

This bond is one of the bonds, of the series designated therein, described in the withinmentioned Indenture.

U.S. BANK NATIONAL ASSOCIATION Trustee

By .....

Authorized Officer

**SOUTHERN CALIFORNIA GAS COMPANY**  
**TO**  
**U.S. BANK NATIONAL ASSOCIATION**

(successor by merger to U.S. Bank Trust National Association, formerly known as First Trust of California,  
National Association)

**TRUSTEE**

**SUPPLEMENTAL INDENTURE**  
**To Base Indenture dated October 1, 1940**

Dated as of December 15, 2003

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THIS SUPPLEMENTAL INDENTURE, dated as of December 15, 2003 (this "Supplemental Indenture"), is made and entered into in the City of Los Angeles, State of California by and between SOUTHERN CALIFORNIA GAS COMPANY, a corporation duly organized and existing under the laws of the State of California, and having its principal place of business in the City of Los Angeles, State of California (hereinafter sometimes called the "Corporation") and U.S. BANK NATIONAL ASSOCIATION (successor by merger to U.S. Bank Trust National Association, formerly known as First Trust of California, National Association), an association duly organized and existing under the laws of the United States of America and having a corporate trust office in the City and County of Los Angeles, State of California (hereinafter, together with its predecessors as trustees under the Indenture referred to below, sometimes called the "Trustee").

**WITNESSETH:**

WHEREAS, the Corporation has executed and delivered to the Trustee a certain Indenture (hereinafter referred to as the "Base Indenture") dated October 1, 1940, to secure bonds of the Corporation designated generally as its "First Mortgage Bonds" to be issued from time to time in one or more series, any of which series may vary from any other as to certain particulars specified in Section 2.01 of the Base Indenture, and the Corporation has executed and delivered to the Trustee supplemental indentures dated, respectively, as of July 1, 1947, May 1, 1948, June 1, 1950, April 1, 1952, August 1, 1955, June 1, 1956, December 1, 1956, July 1, 1957, October 1, 1959, July 1, 1963, September 1, 1964, June 1, 1965, December 1, 1966, October 1, 1970, August 1, 1972, September 1, 1972, October 1, 1974, May 1, 1976, October 1, 1977, November 1, 1979, February 1, 1981, September 15, 1981, April 1, 1982, August 15, 1983, May 18, 1984, December 16, 1985, March 1, 1986, November 15, 1986, December 1, 1986, January 15, 1988, June 15, 1988, November 1, 1988, December 1, 1990, October 1, 1991, August 15, 1992, December 15, 1992, March 1, 1993, June 15, 1993, November 1, 1993, November 15, 1993, October 1, 2002 and October 17, 2003 supplementing and amending the Base Indenture (each, a "Prior Supplemental Indenture," and the Base Indenture together with all Prior Supplemental Indentures and this Supplemental Indenture being herein collectively referred to as the "Indenture"), and

WHEREAS, the Base Indenture and the Prior Supplemental Indentures dated, respectively, as of July 1, 1947, May 1, 1948, June 1, 1950, April 1, 1952 and August 1, 1955, are recorded in the office of the County Recorder of each of the Counties listed below in the Official Records thereof, as stated in the Prior Supplemental Indenture dated as of June 1, 1956; the Prior Supplemental Indentures dated, respectively, as of June 1, 1956 and December 1, 1956, are so recorded as stated in the Prior Supplemental Indenture dated as of July 1, 1957; the Prior Supplemental Indenture dated as of July 1, 1957 and each subsequently dated Prior Supplemental Indenture (other than the Prior Supplemental Indenture dated October 17, 2003) is so recorded as stated in the Prior Supplemental Indenture dated as of the next succeeding date; and the Prior Supplemental Indenture dated as of October 17, 2003 is recorded in the offices of the County Recorders in the Counties of the State of California, as follows:

County	Reference	Date
Fresno	Official Records, Document 03-0287861	December 2, 2003
Imperial	Official Records, Document 03-038644	December 9, 2003
Kern	Official Records, Document 03-0203229014	October 21, 2003
Kings	Official Records, Document 03-30614	October 22, 2003
Los Angeles	Official Records, Document 03-3178339	October 23, 2003
Orange	Official Records, Document 03-001305591	October 23, 2003
Riverside	Official Records, Document 03-970240	December 11, 2003
San Bernardino	Official Records, Document 03-0800979	October 22, 2003
San Diego	Official Records, Document 03-1309741	October 28, 2003
San Luis Obispo	Official Records, Document 03-123983	October 24, 2003
Santa Barbara	Official Records, Document 03-0146116	October 22, 2003
Tulare	Official Records, Document 03-0104290	October 22, 2003
Ventura	Official Records, Document 03-0433039	November 12, 2003

WHEREAS, bonds of the Corporation of three (3) series designated, respectively, as its "First Mortgage Bonds, Series EE, due 2025," "First Mortgage Bonds, Series GG, Due 2012" and "First Mortgage Bonds, Series HH, due 2018" are outstanding as a part of the First Mortgage Bonds referred to in the Indenture, each such series of bonds, unless and until the taking of further appropriate action by the Board of Directors of the Corporation, being without limitation as to aggregate authorized principal amount; and

WHEREAS, pursuant to the provisions of Sections 2.01 and 2.02 of the Indenture, the Board of Directors has, by resolution duly adopted and delivered to the Trustee, created, as a part of the First Mortgage Bonds referred to in the Indenture, a new series of bonds designated "First Mortgage Bonds, Series II, due 2011" (the "Series II Bonds"), to be of the form, terms and provisions provided in that resolution and herein, which new series of bonds, unless and until the taking of further appropriate action by the Board of Directors, is to be without limitation as to aggregate authorized principal amount and of which series of bonds in the aggregate principal amount of \$250,000,000 are to be presently issued; and

WHEREAS, it is provided in the Indenture that all the business, franchises and properties, real, personal, and mixed, of every kind and nature whatsoever and wheresoever situated, which might thereafter be acquired by the Corporation, shall be as fully embraced within the lien thereof as if said properties were owned by the Corporation at the date of the Base Indenture and were particularly described therein and specifically conveyed thereby, excepting certain properties expressly excepted by the provisions of the Indenture; and

WHEREAS, subsequent to the execution of the most recently recorded Prior Supplemental Indenture identifying after acquired property, the Corporation has acquired properties hereinafter mentioned or referred to, all of which properties, upon the acquisition thereof by the Corporation, became and now are subject to the lien, operation and effect of the Indenture by virtue of the after-acquired property clause or other clauses thereof; the Corporation, nevertheless, desires to execute, acknowledge, deliver and cause to be recorded this Supplemental Indenture for the purposes, among others, of expressly and specifically subjecting such after-acquired properties to the lien of the Indenture and of further assuring and confirming the lien of the Indenture on all of the properties of every kind and character, whether real or

personal and regardless of the date of acquisition thereof by the Corporation, intended to be subjected to the lien thereof, and

WHEREAS, under the provisions of Sections 2.02 and 16.01 of the Indenture, the Corporation and the Trustee may execute and deliver a Supplemental Indenture (i) to set forth the particulars, permitted by Section 2.01 of the Indenture, as to which the Series II Bonds may vary from the bonds of the other series of the First Mortgage Bonds, and (ii) for any purpose not inconsistent with the terms of the Indenture; and

WHEREAS, the making, executing, delivering and recording of this Supplemental Indenture have been duly authorized by proper corporate action of the Corporation; and

WHEREAS, the issuance of the Series II Bonds and the encumbrances of the Corporation's property to secure the Series II Bonds pursuant to this Supplemental Indenture have been authorized by the Public Utilities Commission of the State of California:

NOW, THEREFORE, in consideration of the foregoing premises and of other good and valuable consideration, receipt of which is hereby acknowledged, and in order: (a) to set forth or specify (i) the form of the fully registered Series II Bonds, and the form of the certificate to be endorsed on all Series II Bonds, and (ii) the terms and provisions of the Series II Bonds, including the particulars thereof which vary from the bonds of the other series of the First Mortgage Bonds; and (b) further to secure the payment of both the principal of and interest on the bonds of the Corporation now or at any time hereafter outstanding under the Indenture, including specifically, but without limitation, all of the First Mortgage Bonds now outstanding and the \$250,000,000 aggregate principal amount of Series II Bonds and further to secure the observance and performance of all of the covenants, agreements and conditions contained in the Indenture, and without in any way limiting the generality or effect of the Indenture insofar as by any provision thereof any of the property therein or hereafter described or referred to is now subject or intended to be subject to the lien and operation thereof, but to such extent confirming such lien and operation, the Corporation has executed and delivered this Supplemental Indenture and has granted, bargained, sold, released, conveyed, mortgaged, assigned, transferred, pledged, set over and confirmed, and does hereby grant, bargain, sell, release, convey, mortgage, assign, transfer, pledge, set over and confirm unto U.S. Bank National Association, the Trustee, and to its successors or successors in the trust created by the Indenture, and to its and their assigns, forever, with power of sale, subject, to the extent applicable by the terms of the Indenture to any of the properties hereinafter referred to or described, to the exceptions (other than as expressly provided in the granting clauses of the Prior Supplemental Indentures dated respectively as of June 1, 1956, July 1, 1957, October 1, 1959, July 1, 1963, September 1, 1964 and December 1, 1966 with respect to exception (f) set forth on page 67 of the Base Indenture and reading as follows: "(f) Any gas and/or oil acreage, gas and/or oil wells, gas and/or oil reserves, or gas and/or oil leaseholds hereafter acquired by the Corporation, or any property or equipment now or hereafter owned by the Corporation and used for the development of gas and/or oil acreage or for the drilling for or production of gas and/or oil from such acreage;" which exception (f) is by said granting clauses expressly made inapplicable to certain therein specified parcels of property), reservations, conditions, terms and provisions provided in the Indenture with respect to properties subject or intended to be subject thereto, all of the properties and assets of the Corporation, real, personal and mixed, of every kind and character, whether now or hereafter

owned by the Corporation and wheresoever situated, including, without in any way limiting or modifying the generality or effect of the foregoing, all and singular, the following properties:

FIRST: All and singular the plants, properties, equipment, real and personal property, estates, interests, goodwill, generating, transmission, feeding, storing, and distribution systems, and utilities of the Corporation situated in the Counties of Fresno, Imperial, Kern, Kings, Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Luis Obispo, Santa Barbara, Tulare and Ventura, and elsewhere, in the State of California, with all and singular the franchises, ordinances, grants, easements, licenses, powers, immunities, permits, privileges, appurtenances, tenements and other rights and property thereunto appertaining or belonging, as the same now exist and as the same and any and all parts thereof may hereafter exist or be improved, added to, enlarged, extended or acquired in said counties or elsewhere in said state or any other state or states.

SECOND: All other property, real, personal and mixed, of every kind, nature and description (including, without in any way limiting the effect or the generality hereof, all facilities; all stocks, bonds and other securities from time to time conveyed, assigned, transferred, mortgaged or pledged on behalf of the Corporation, or with its consent, to the Trustee in the manner and for the purposes as provided in the Indenture; all gas manufacturing plants, boilers, engines, compressors, motors, pumps, generators, gasholders, tanks, appliances, oil storage facilities, gas storage facilities, wells, buildings, structures, plants, works and other improvements; all gas transmission and distributing lines and systems; all meters and regulators and all other apparatus, machinery, appliances, tools, furniture, fixtures, supplies, facilities and utilities and other personal property; or any right or interest in any thereof; all business and goodwill, rights, consents, franchises, ordinances, licenses, agreements, contracts, permits, easements, rights of way, leases and leasehold interests; powers, grants, privileges and immunities to construct, operate and maintain lines and other facilities or properties for conveying gas or other commodity or utility for any purpose or purposes through, under and over public streets or highways, or public or private places or property; all reversions, remainders, tolls, incomes, revenues, earnings, rents, issues and profits of any property, real, personal and mixed; and all other classes and types of property described or referred to in the Indenture), now or hereafter owned, held, possessed, acquired or enjoyed by or in any manner conferred upon or appertaining to the Corporation, including the interest of the Corporation in all leases now or hereafter owned by it, together with all and singular the tenements, hereditaments, and appurtenances belonging or in any way appertaining to each and every part of any and all property subject or intended to be subject to the lien and operation of the Indenture, and the reversion and reversions, remainder and remainders, tolls, incomes, revenues, earnings, rents, issues and profits thereof.

SAVING AND EXCEPTING, however, from the property hereby mortgaged, conveyed in trust and/or pledged, all property, whether now owned by the Corporation or hereafter acquired by it, expressly saved and excepted from the lien of the Indenture and therein referred to as the "excepted property" (except as otherwise expressly provided in any Prior Supplemental Indenture hereinabove mentioned with respect to exception (f) of said "excepted property"), unless and until, upon the occurrence of an event of default under the Indenture, the Trustee, or any receiver appointed thereunder, shall take possession of any or all of such excepted property.

TO HAVE AND TO HOLD in trust with power of sale for the equal and proportionate benefit and security of all holders of bonds of the Corporation, now or hereafter outstanding under the Indenture as from time to time in effect, and for the enforcement and payment of said bonds and interest thereon when payable, and the performance of and compliance with the covenants and conditions of the Indenture as from time to time in effect, without any preference, distinction or priority as to lien or otherwise of any of said bonds over any others thereof by reason of the difference in the time of the actual issue, sale or negotiation thereof, or for any other reason whatsoever, except as otherwise expressly provided in the Indenture as from time to time in effect, so that each and every such bond shall have the same lien and so that the principal and interest of every such bond shall, subject to the terms thereof, be equally and proportionately secured by said lien, as if such bond had been made, executed, delivered, sold and negotiated simultaneously with the execution and delivery of the Base Indenture.

IT IS HEREBY COVENANTED, DECLARED, AND AGREED by and between the parties hereto that all such bonds are issued, authenticated and delivered, or are to be issued, authenticated and delivered, and that all property subject, or to become subject, to the Indenture is to be held, subject to the covenants, conditions, uses and trusts therein set forth.

## ARTICLE I

### AMOUNT, FORM, NUMBERING, DENOMINATION, TRANSFER AND EXCHANGE OF SERIES II BONDS, DUE 2011

Section 1.01. The Series II Bonds may be issued at any time or from time to time upon and subject to the terms and provisions of the Indenture. Unless and until the taking of further appropriate action by the Board of Directors of the Corporation the Series II Bonds shall be without limitation as to aggregate authorized principal amount.

Section 1.02. The Series II Bonds shall be issued only as fully registered bonds without coupons. In addition, the Series II Bonds may be issuable in whole or in part in the form of one or more securities that evidences all or part of the bonds of such series which is issued to a depository or a nominee thereof for such series (a "Global Security") and, in such case, the Board of Directors shall appoint a clearing agency registered under the Exchange Act of 1934, as amended (the "Exchange Act"), designated to act as depository (a "depository") for such Global Securities.

Section 1.03. In the event the Series II Bonds are issued as a Global Security the following provisions, in addition to the provisions of the Indenture, shall apply:

- (a) Each Global Security authenticated under the Indenture shall be registered in the name of the depository designated for such Global Security or a nominee thereof and delivered to such depository or a nominee thereof or custodian therefor; and each such Global Security shall constitute a single bond for all purposes of this Supplemental Indenture.
- (b) Notwithstanding any other provision in this Supplemental Indenture, no Global Security may be exchanged in whole or in part for bonds registered, and no transfer of a Global Security in whole or in part may be registered, in the name of any person other than the depository for such Global Security or a nominee thereof unless (A) such depository has notified the Corporation that it is unwilling or unable to continue as depository for such Global Security and a successor depository has not been appointed by the Corporation within 90 days of receipt by the Corporation of such notification, (B) if at any time the depository ceases to be a clearing agency registered under the Exchange Act at a time when the depository is required to be so registered to act as such depository and no successor depository shall have been appointed by the Corporation within 90 days after it became aware of such cessation, (C) the Corporation, in its sole discretion, executes and delivers to the Trustee a written order signed in the name of the Corporation by its Chairman of the Board, its President or a Vice President, and by its Treasurer, an Assistant Treasurer, its Secretary or an Assistant Secretary to the effect that such Global Security, together with all other Global Securities of the same series, shall be exchangeable as described below, or (D) an Event of Default (as defined in Section 1.02 of the Indenture) has occurred and is continuing with respect to the Series II Bonds. If any of the events described in clauses (A) through (D) of the preceding sentence occur, the beneficial owners of interests in the relevant Global Securities will be entitled to exchange those interests for definitive bonds and, without unnecessary delay but in any event not later than the earliest date on which those interests may be so exchanged, the Corporation will deliver to the Trustee definitive bonds in such form and denominations as are required by or pursuant to this Indenture, and of the same series, containing identical terms and in an aggregate principal amount equal to the principal amount of such Global Securities, such bonds to be duly executed by the Corporation. On or after the earliest date on which such beneficial interests may be so exchanged, such Global Securities shall be surrendered from time to time by the depository as shall be specified in the order from the Corporation with respect thereto (which the Corporation agrees to deliver), and in accordance with any instructions given to the Trustee and the depository (which instructions shall be in writing but need not be contained in or accompanied by an officers' certificate or be accompanied by an opinion of counsel), as shall be specified in the order from the Corporation with respect thereto to the Trustee, as the Corporation's agent for such purpose, to be exchanged, in whole or in part, for definitive bonds as described above without charge. The Trustee shall authenticate and make available for delivery, in exchange for each portion of such surrendered Global Security, a like aggregate principal amount of definitive bonds of the same series of authorized denominations and of like tenor as the portion of such Global Security to be exchanged. Promptly following any such exchange in part, such Global Security shall be returned by the Trustee to such depository or its custodian. If a definitive bond is issued in exchange for any portion of a Global Security after the close of business at the place where such exchange occurs on or after (i) any regular record date for the date the interest is due (the "Interest Payment Date") for such bond and before the opening of business at that place of payment on the next Interest Payment Date, or (ii) any special record date for the payment of interest for such bond and before the opening of business at such

place of payment on the related proposed date for the payment of the interest which was not punctually paid or duly provided for on any Interest Payment Date ("Defaulted Interest"), as the case maybe, interest shall not be payable on such Interest Payment Date or proposed date for payment, as the case may be, in respect of such definitive bond, but shall be payable on the Interest Payment Date or proposed date for payment, as the case may be, only to the person to whom interest in respect of such portion of such Global Security shall be payable in accordance with the provisions of this Indenture.

(c) Subject to Clause (b) above, any exchange or transfer of a Global Security for other bonds may be made in whole or in part, and all bonds issued in exchange for or upon transfer of a Global Security or any portion thereof shall be registered in such names as the depositary for such Global Security shall direct.

(d) Every bond authenticated and delivered upon registration of transfer of, or in exchange for or in lieu of, a Global Security or any portion thereof, shall be authenticated and delivered in the form of, and shall be, a Global Security, unless such bond is registered in the name of a person other than the depositary for such Global Security or a nominee thereof.

Section 1.04. Unless otherwise specified as contemplated by Section 2.01 for the bonds evidenced thereby, every Global Security authenticated and delivered hereunder shall bear a legend in substantially the following form:

*THIS SECURITY IS A GLOBAL SECURITY WITHIN THE MEANING OF THE INDENTURE HEREINAFTER REFERRED TO AND IS REGISTERED IN THE NAME OF A DEPOSITARY OR A NOMINEE THEREOF. THIS SECURITY MAY NOT BE EXCHANGED IN WHOLE OR IN PART FOR A SECURITY REGISTERED, AND NO TRANSFER OF THIS SECURITY IN WHOLE OR IN PART MAY BE REGISTERED, IN THE NAME OF ANY PERSON OTHER THAN SUCH DEPOSITARY OR A NOMINEE THEREOF, EXCEPT IN THE LIMITED CIRCUMSTANCES DESCRIBED IN THE INDENTURE. ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL INASMUCH AS THE REGISTERED OWNER HEREOF HAS AN INTEREST HEREIN.*

Section 1.05. The fully registered bonds without coupons and the certificate of authentication to be endorsed on all Series II Bonds shall be substantially in the form set forth on Exhibit A.

Section 1.06. The Series II Bonds may contain or have imprinted thereon such provisions or specifications not inconsistent with the Indenture as may be required to comply with the rules of any stock exchange or any federal or state authority or commission, or to comply with usage with respect thereto, and may bear such other appropriate endorsements or notations as are authorized or permitted by the Indenture.

Section 1.07. The fully registered Series II Bonds shall be issuable in denominations of \$1,000, \$5,000, \$10,000, \$25,000 or multiples of \$25,000 and shall be dated as provided in paragraph 1 of Section 2.01 of the Indenture. The definitive Series II Bonds shall be numbered in such manner as the Corporation shall at any time or from time to time determine.

Section 1.08. In the manner and subject to certain conditions and limitations specified herein and in the Indenture, Series II Bonds may be exchanged without a service charge for a like aggregate principal amount of such Series II Bonds of other authorized denomination or denominations; provided that the Corporation may require payment of a sum or sums sufficient to reimburse it for any stamp tax or other governmental charge payable in connection therewith.

Section 1.09. The Corporation shall maintain in the City and County of San Francisco, State of California, and in such other place or places as the Corporation may designate at any time or from time to time, an office or agency where Series II Bonds may be presented for payment, registration, transfer and exchange as provided therein or in the Indenture. Such office or agency in the City and County of San Francisco shall be the corporate trust office of the Trustee unless and until the Corporation shall designate another office or agency by notice in writing delivered to the Trustee. Notwithstanding the foregoing, if and when definitive bonds are issued, the Corporation shall maintain in the Borough of Manhattan, City and County of New York, State of New York, an office or agency where Series II Bonds may be presented for payment, registration, transfer and exchange as provided therein or in the Indenture.

Section 1.10. No transfer or exchange of any Series II Bonds pursuant to any of the provisions of this Article I shall be made except upon and in accordance with all of the applicable terms, provisions and conditions of said bonds and of the Indenture.

## ARTICLE II

### INTEREST, MATURITY DATE, REDEMPTION AND CERTAIN OTHER PROVISIONS OF SERIES II BONDS, DUE 2011

Section 2.01. The Series II Bonds shall bear interest at the rate, shall be expressed to mature as to principal, and shall be payable as to principal and interest at such place or places and in such money, all as provided in the form of Series II Bond set forth on Exhibit A hereto and by the applicable provisions of the Indenture. In addition, December 15, 2003 shall be an Interest Payment Date for the Series II Bonds for purposes of Section 2.01 of the Base Indenture (as supplemented by the Prior Supplemental Indentures), provided that no interest shall be payable on such date.

Section 2.02. The Series II Bonds shall be subject to redemption prior to maturity as set forth in the form of Series II Bond set forth on Exhibit A, upon notice, in the manner and otherwise upon the terms and conditions and with the effect, as provided herein and by the applicable provisions of the Indenture.

Section 2.03. The Corporation may at any time deliver to the Trustee for cancellation any Series II Bonds previously authenticated and delivered under the Indenture which the Corporation may have acquired in any manner whatsoever and all Series II Bonds so delivered shall be promptly cancelled by the Trustee upon the request of the Corporation.

Section 2.04. The Series II Bonds shall, except as in this Supplemental Indenture otherwise expressly provided, be on the terms and provisions, and shall represent such rights and be entitled to such benefits, as are applicable thereto by the terms of the Indenture.

Section 2.05. The Series II Bonds shall be entitled to the benefits of the Renewal Fund as provided in the Indenture.

Section 2.06. The following Section 11.01A shall apply to the Series II Bonds in lieu of Section 11.01 of the Indenture:

"Section 11.01A If the Corporation, its successors or assigns, shall

(a) pay or cause to be paid the principal of and interest on the bonds and coupons and claims for interest thereon to become due at the time and in the manner stipulated therein and herein, and/or

(b) provide for the payment of the bonds and interest thereon by depositing in cash with the Trustee or other depositary satisfactory to it at any time at or before maturity the entire amount due or to become due thereon for principal and interest to maturity of all the bonds outstanding, and/or

(c) in case of a call of all of the bonds then outstanding for redemption, deposit with the Trustee on or before the date on which all of such bonds (other than those which shall have matured by their terms) shall have been called for redemption, as provided in Article VII, the entire amount of the redemption price thereof, including interest and premium, if any, and shall deliver to the Trustee (1) proof satisfactory to the Trustee that notice of redemption as provided in Article VII has been given, or (2) proof satisfactory to the Trustee that arrangements have been made insuring that such notice will be given, or (3) a written instrument executed by the Corporation under its corporate seal, and expressed to be irrevocable, authorizing the Trustee to give such notice for and on behalf of the Corporation, and/or

(d) surrender to the Trustee for cancellation all the bonds and coupons thereto appertaining for which payment is not so provided,

and shall also pay, or satisfactorily provide, all other sums due and payable hereunder by the Corporation, including the compensation and expenses of the Trustee, then and in that case,

(i) at the request of the Corporation all the mortgaged property shall revert to the Corporation and the entire estate, right, title and interest of the Trustee and of the holders and registered owners of the bonds and coupons in respect of the mortgaged property shall thereupon cease, determine and become void; and

(ii) the Trustee in such case, upon the cancellation of all outstanding bonds and coupons for the payment of which cash shall not have been deposited in accordance with the provisions of this Indenture, shall upon request of the Corporation, and at its cost and expense (A) and upon delivery to it of an opinion of counsel stating that (x) the Corporation has received from, or there has been published by, the Internal Revenue Service a ruling, or (y) since December 10, 2003 there has been a change in applicable federal income tax law, in either case to the effect that, and based thereon such opinion of counsel shall confirm that, the holders of Series II Bonds will not recognize income, gain or loss for federal income tax purposes as a result of such defeasance and will be subject to federal income tax on the same amounts, in the same manner and at the same times as would have been the case if such defeasance had not occurred, execute to the Corporation, or its order, proper instruments acknowledging satisfaction of this Indenture and (B) shall surrender to the Corporation, or its order, all cash and deposited securities, if any, which shall then be held by it hereunder as a part of the mortgaged property (exclusive of cash held in trust as provided in Section 5.03); provided, however, that if any such property shall have been delivered to the Trustee by any person or corporation other than the Corporation, the same shall be delivered or otherwise disposed of in accordance with any reservations, limitations, conditions or provisions which may have been set forth in the instrument in writing then executed, if any, respecting the use, management or disposition thereof; and provided further that if the Corporation pursuant to clauses (1) or (2) of subdivision (c) above shall have delivered to the Trustee proof satisfactory to it that notice of redemption as provided in Article VII has been given or that arrangements have been made insuring that such notice will be given, there shall also be delivered to the Trustee an officers' certificate stating that all conditions precedent to the satisfaction and discharge of this Indenture have been complied with and an opinion of counsel stating that in his opinion such conditions precedent have been complied with."

## ARTICLE III

### SUNDRY PROVISIONS

Section 3.01. The recitals of fact contained herein shall be taken as the statements of the Corporation, and the Trustee assumes no responsibility for the correctness of the same. The Corporation hereby covenants and agrees that it will cause this Supplemental Indenture to be kept recorded and/or filed as may be required by law, in such manner and in such places as may be necessary fully to preserve and protect the security of the bondholders and all of the rights of the Trustee hereunder, and that it will with all reasonable dispatch deposit with the Trustee counterparts of this Supplemental Indenture bearing official notation or endorsements showing such recordation and/or filing, or in case such counterparts are not returned to the Corporation, furnish to the Trustee the best official evidence of such recordation and/or filing reasonably obtainable by the Corporation, or evidence of the taking of such other action, if any, but the Trustee, subject to the provisions of Sections 14.02 and 14.03 of the Indenture, shall in no way be liable for any failure or omission in this regard.

Section 3.02. The date of this Supplemental Indenture and the date of the Series II Bonds are intended as and for a date for the convenient identification of this Supplemental Indenture and of the Series II Bonds, and are not intended to indicate that this Supplemental Indenture was executed and delivered or that the Series II Bonds were executed, delivered or issued on said date; it being hereby provided that this Supplemental Indenture may be executed and delivered, and that the Series II Bonds may be executed, delivered or issued, either on said date or before or after said date, and that this Supplemental Indenture is in fact executed and delivered by each party hereto on the date of its certificate of acknowledgment hereto attached.

Section 3.03. This Supplemental Indenture shall be deemed to be part of the Base Indenture, and the Corporation agrees to conform to and comply with all and singular the terms, provisions, conditions and covenants set forth therein and herein. This Supplemental Indenture shall be construed in connection with and as a part of the Indenture.

Section 3.04. It is further agreed that the Trustee accepts the trust imposed upon it by this Supplemental Indenture, upon and subject to the same terms and conditions as are expressed in Article XIV of the Base Indenture.

Section 3.05. In order to facilitate the recording of this Supplemental Indenture, the same may be, executed in several counterparts, each of which so executed shall be deemed to be an original, and such counterparts shall collectively constitute one and the same instrument.

Section 3.06. All terms used in this Supplemental Indenture which are defined in the Indenture are not defined herein shall have the meaning assigned to them in the Indenture.

Section 3.07. To the extent any provision in this Supplemental Indenture conflicts with any provision in the Indenture, the provisions of this Supplemental Indenture shall govern; provided however, that in the event such conflict would require bondholder consent, the terms and provisions of the Indenture shall govern.

Section 3.08. This Supplemental Indenture and the Series II Bonds shall be governed by and construed in accordance with the laws of the State of California, without regard to conflicts of laws principles thereof.

Section 3.09. To the extent not otherwise addressed in this Supplemental Indenture, this Supplemental Indenture shall be subject to the provisions of Article XVII of the Indenture, the terms of which are hereby incorporated by reference into this Indenture Supplement.

IN WITNESS WHEREOF, Southern California Gas Company has caused this Supplemental Indenture to be signed in its corporate name by one of its Vice Presidents or its Treasurer and its Secretary or an Assistant Secretary and its corporate seal to be hereunto duly affixed, and U.S. Bank National Association, in token of its acceptance of the trust hereby established, has caused this Supplemental Indenture to be signed in its corporate name by two of its authorized officers, including one or more of its Vice Presidents, all as of December 15, 2003.

Attest: SOUTHERN CALIFORNIA GAS COMPANY

/s/ CATHERINE C. LEE

/s/ TERRY M. FLESKES

Name: Catherine C. Lee

Name: Terry M. Fleskes

Title: Secretary

Title: Vice President and Treasurer

Attest:

U.S. BANK NATIONAL ASSOCIATION

-----

By: -----

Authorized Signatory

Name: Fonda Hall

Title: Vice President

STATE OF CALIFORNIA

COUNTY OF SAN DIEGO

On this 12th day of December 2003, before me, /s/ DONNA R. CORONA, Notary Public, personally appeared Terry M. Fleskes, personally known to me to be one of the persons whose names are subscribed to the within instrument, and acknowledged to me that such person executed the same in the person's authorized capacity, and that by the person signature on the instrument, the entity upon behalf of which the person acted executed the instrument

WITNESS my hand and official seal

/s/ DONNA R. CORONA

-----

Notary Public

My Commission expires ...4/21/05.....

Donna R. Corona. Commission # 1298291

Notary Public California

San Diego County

My comm. Expires



STATE OF CALIFORNIA

COUNTY OF SAN DIEGO

On this 12th day of December 2003, before me, /s/ DONNA R. CORONA., Notary Public, personally appeared Catherine C. Lee, personally known to me to be one of the persons whose names are subscribed to the within instrument, and acknowledged to me that such person executed the same in the person's authorized capacity, and that by the person signature on the instrument, the entity upon behalf of which the person acted executed the instrument.

WITNESS my hand and official seal

/s/ DONNA R. CORONA

-----

Notary Public

My Commission expires ...4/21/05.....

Donna R. Corona. Commission # 1298291

Notary Public California

San Diego County

My comm. Expires

April 21, 2005

IN WITNESS WHEREOF, Southern California Gas Company has caused this Supplemental Indenture to be signed in its corporate name by one of its Vice Presidents or its Treasurer and its Secretary or an Assistant Secretary and its corporate seal to be hereunto duly affixed, and U.S. Bank National Association, in token of its acceptance of the trust hereby established, has caused this Supplemental Indenture to be signed in its corporate name by two of its authorized officers, including one or more of its Vice Presidents, all as of December 15, 2003.

Attest:

SOUTHERN CALIFORNIA GAS COMPANY

-----

Name: Catherine C. Lee

Title: Secretary

By:

-----

Name: Terry M. Fleskes

Title: Vice President and Treasurer

Attest:

U.S. BANK NATIONAL ASSOCIATION

-----

Authorized Signatory

/S/ FONDA HALL

-----

Name: Fonda Hall

Title: Vice President

CALIFORNIA ALL-PURPOSE ACKNOWLEDGEMENT

State of California

County of Los Angeles

On December 12, 2003, before me, Serena M. Gutierrez, personally appeared Fonda Hall and Alicia Estrada, personally known to me, to be the person(s) whose name(s) are subscribed to the within instrument and acknowledged to me that they executed the same in their authorized capacity(ies), and that by their signature(s) on the instrument the person(s), or the entity upon behalf of which the person(s) acted, executed the instrument.

WITNESS my hand and official seal.

/s/ Serena M. Gutierrez

-----

Notary Public

Serena M. Gutierrez

Commission # 1264926

Notary Public-California

Los Angeles County

My Comm. Expires May 25, 2004

EXHIBIT A

[FORM OF REGISTERED BOND WITHOUT COUPONS, SERIES II, DUE 2011]

[If this bond is issued as a global security, insert the following legend: THIS SECURITY IS A GLOBAL SECURITY WITHIN THE MEANING OF THE INDENTURE HEREINAFTER REFERRED TO AND IS REGISTERED IN THE NAME OF A DEPOSITARY OR A NOMINEE THEREOF, THIS SECURITY MAY NOT BE EXCHANGED IN WHOLE OR IN PART FOR A SECURITY REGISTERED, AND NO TRANSFER OF THIS SECURITY IN WHOLE OR IN PART MAY BE REGISTERED, IN THE NAME OF ANY PERSON OTHER THAN SUCH DEPOSITARY OR A NOMINEE THEREOF, EXCEPT IN THE LIMITED CIRCUMSTANCES DESCRIBED IN THE INDENTURE. ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL INASMUCH AS THE REGISTERED OWNER HEREOF HAS AN INTEREST HEREIN.]

**SOUTHERN CALIFORNIA GAS COMPANY**  
(Incorporated under the laws of the State of California)

FIRST MORTGAGE BOND, SERIES II, DUE 2011

4.375%

No. \_\_\_\_\_

\$ \_\_\_\_\_

CUSIP No. \_\_\_\_\_

SOUTHERN CALIFORNIA GAS COMPANY, a corporation organized and existing under the laws of the State of California (hereinafter called the "Corporation", which term shall include any successor corporation, as defined in the Indenture hereinafter referred to), for value received, hereby promises to pay to [If this bond is issued as a global security, insert "CEDE & CO." in the foregoing space] or registered assigns, the principal sum of in lawful money of the United States of America, on the fifteenth day of January, 2011, and to pay interest thereon from the date of this bond, at the rate of 4.375% per annum in like lawful money, payable semi-annually, on the fifteenth day of January and July in each year, to the holder of record of this bond on the immediately preceding first day of January and July, respectively, commencing July 15, 2004, until the Corporation's obligation with respect to the payment of such principal shall be discharged as provided in the Indenture hereinafter mentioned. Both the principal of and interest on this bond will be paid at the corporate trust office of U.S. Bank National Association, or its successor trustee under said Indenture, in the City and County of San Francisco, State of California [if this bond is a definitive bond, insert: ", or at the office or agency in the Borough of Manhattan, City and County of New York, State of New York, that the Corporation maintains for such purpose"]. Notwithstanding the foregoing, so long as the holder of the Series II Bonds is a depositary, or its nominee, payment of the principal of (and premium, if any) and interest on this bond will be made by wire transfer of immediately available funds.

The provisions of this bond are continued on the reverse hereof and such continued provisions shall for all purposes have the same effect as though set forth at this place.

IN WITNESS WHEREOF, SOUTHERN CALIFORNIA GAS COMPANY has caused this bond to be signed in its corporate name by the facsimile signature of its authorized officer and a facsimile of its corporate seal to be hereto affixed and attested by its Secretary or an Assistant Secretary.

Dated:

SOUTHERN CALIFORNIA GAS COMPANY

By

-----  
Vice President

(CORPORATE SEAL)

Attest:

Secretary

[REVERSE SIDE - FORM OF REGISTERED BOND  
WITHOUT COUPONS, SERIES II, DUE 2011]

This bond is one of a duly authorized issue of bonds of the Corporation (herein called the "bonds"), of the series hereinafter specified, all issued and to be issued under and all equally and ratably secured by a mortgage and deed of trust dated October 1, 1940, between the Corporation and U.S. Bank National Association, as successor trustee, to which mortgage and deed of trust and all indentures supplemental thereto, including Supplemental Indentures dated, respectively, as of July 1, 1947, August 1, 1955, June 1, 1956, December 1, 1956, June 1, 1965, August 1, 1972, May 1, 1976, September 15, 1981, May 18, 1984, November 15, 1986, January 15, 1988, August 15, 1992, October 1, 2002, October 17, 2003 and December 15, 2003 (herein collectively referred to as the "Indenture"), reference is hereby made for a description of the property conveyed in trust, mortgaged and pledged, the nature and extent of the security, the rights of the registered owners of the bonds and of the Trustee or trustee s in respect thereof, the terms and conditions upon which the bonds are, and are to be, secured and the circumstances under which additional bonds may be issued. The bonds may be issued for various principal sums, and may be issued in series, which may mature at different times, may bear interest at different times, may bear interest at different rates and may otherwise vary as in the Indenture provided. This bond is one of a series designated as the "First Mortgage Bonds, Series II, due 2011" (herein called "Series II" Bonds) of the Corporation, issued under and secured by the Indenture. Terms used but not defined herein shall have the respective meanings assigned thereto in the Indenture.

As provided in the Indenture, by any indenture or indentures supplemental thereto executed by the Corporation and the Trustee and consented to by the holders of not less than two-thirds (2/3) in principal amount of the bonds at the time outstanding, and, in case one or more, but less than all, of the series of bonds then outstanding are affected by such supplemental indenture, consented to by the holders of at least two-thirds (2/3) in principal amount of the bonds of each series so affected, the Indenture or any indenture supplemental thereto and the rights and obligations of the Corporation and the holders of bonds, may be modified or altered from time to time, as provided in the Indenture; provided, however, (a) that the right of any holder of any bond to receive payment of the principal of and interest on such bond, on or after the respective due dates expressed in such bond, or to institute suit for the enforcement of any such payment on or after such respective dates, shall not be impaired or affected by any such supplemental indenture without the consent of such holder; and (b) that no such modification or alteration shall reduce the proportions of bondholders' consents required as aforesaid; such proportions to be determined in each case as provided in the Indenture.

The Series II Bonds are entitled to the benefits of the Renewal Fund as provided in the indenture.

All or a portion of the Series II Bonds may be redeemed at the Corporation's option at any time or from time to time.

The price at which the Series II Bonds will be redeemed (the "Redemption Price") on the date fixed for such redemption (the "Redemption Date") will be equal to the greater of the following amounts: (a) 100% of the principal amount of the bonds being redeemed on the

Redemption Date; or (b) the sum of the present values of the remaining scheduled payments of principal and interest on the Series II Bonds being redeemed on that Redemption Date (not including any portion of any payments of accrued and unpaid interest to the Redemption Date) discounted to the Redemption Date on a semiannual basis at the Adjusted Treasury Rate (as defined below) plus 20 basis points, as determined by the Reference Treasury Dealer (as defined below), plus, in each case, accrued and unpaid interest thereon to the Redemption Date. Notwithstanding the foregoing, installments of interest on Series II Bonds that are due and payable on Interest Payment Dates falling on or prior to a Redemption Date will be payable on such Interest Payment Dates to the registered holders of such Series II Bonds as of the close of business on the relevant record date. The Redemption Price will be calculated on the basis of a 360-day year consisting of twelve 30-day months.

Unless the Corporation defaults in payment of the Redemption Price, on and after the Redemption Date interest will cease to accrue on the Series II Bonds or portions thereof called for redemption.

"Adjusted Treasury Rate" means, with respect to any Redemption Date, the rate per annum equal to the semiannual equivalent yield to maturity of the Comparable Treasury Issue, assuming a price for the Comparable Treasury Issue (expressed as a percentage of its principal amount) equal to the Comparable Treasury Price for such Redemption Date.

"Comparable Treasury Issue" means the United States Treasury security selected by the Reference Treasury Dealer as having a maturity comparable to the remaining term of the Series II Bonds to be redeemed that would be utilized, at the time of selection and in accordance with customary financial practice, in pricing new issues of corporate debt securities of comparable maturity to the remaining term of such Series II Bonds.

"Comparable Treasury Price" means, with respect to any Redemption Date, (A) the average of the Reference Treasury Dealer Quotations for such Redemption Date, or (B) if only one Reference Treasury Dealer Quotation is received, such Quotation.

"Reference Treasury Dealer" means (A) Merrill Lynch, Pierce, Fenner & Smith Incorporated (or its affiliates which are Primary Treasury Dealers) and its successors; provided, however, that if any of the foregoing shall cease to be a primary U.S. Government securities dealer in New York City (a "Primary Treasury Dealer"), the Corporation will substitute therefor another Primary Treasury

Dealer; and (B) any other Primary Treasury Dealer(s) selected by the Corporation.

*"Reference Treasury Dealer Quotation"* means, with respect to each Reference Treasury Dealer and any Redemption Date, the average, as determined by the Corporation, of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its principal amount) quoted in writing to the Corporation by such Reference Treasury Dealer at 5:00 p.m. (New York City time) on the third business day preceding such Redemption Date.

*In the event of redemption of this bond in part only, a new bond or Series II Bonds of like tenor for the unredeemed portion hereof will be issued in the name of the holder hereof upon the cancellation hereof.*

*Notice of any such redemption will be mailed to the registered owners of the Series II Bonds to be redeemed not less than 30 nor more than 60 days before the Redemption Date. Once notice of redemption is mailed, the Series II Bonds called for redemption will become due and payable on the Redemption Date and at the applicable redemption price, plus accrued and unpaid interest to the Redemption Date. Upon the Corporation's election to redeem all or a portion of the Series II Bonds, that redemption will not be conditional upon receipt by the paying agent or the Trustee of monies sufficient to pay the Redemption Price.*

*In case an event of default, as defined in the Indenture, shall occur, the principal of all bonds then outstanding under the Indenture may be declared or become due and payable upon the conditions and in the manner and with the effect provided in the Indenture.*

*This bond is transferable by the registered owner hereof at the office or agency of the Corporation in said City and County of San Francisco [if this bond is a definitive bond, insert: ", or at the office or agency in the Borough of Manhattan, City and County of New York, State of New York, that the Corporation maintains for such purpose"] and in such other place or places as the Corporation may designate at any time or from time to time, and thereupon a new fully registered bond or bonds of said series, without coupons, of authorized denomination or denominations, of a like aggregate principal amount, will be issued to the transferee or transferees in exchange for this bond; and at any of said offices or agencies fully registered Series II Bonds without coupons, are exchangeable for a like aggregate principal amount of other such fully registered bonds of authorized denominations; all in the manner and subject to the conditions as provided in the Indenture.*

*No recourse shall be had for the payment of the principal of or the interest on this bond or for any claim based hereon or on the Indenture or any indenture supplemental thereto, against any incorporator, stockholder, director or officer, past, present or future, of the Corporation, or of any predecessor or successor corporation, either directly or through the Corporation, or any such predecessor or successor corporation, whether by virtue of any constitution, statute or rule of law, or by the enforcement of any assessment or penalty, or otherwise, all such liability being waived and released by every registered owner hereof by the acceptance of this bond and as part of the consideration for the issue hereof, and being likewise waived and released by the terms of the Indenture.*

*This bond shall not become valid or obligatory for any purpose or be entitled to any benefit under the Indenture until U.S. Bank National Association, or its successor as Trustee under the Indenture, shall have signed the form of certificate endorsed hereon.*

*This bond shall be governed by and construed in accordance with the laws of the State of California, without regard to conflicts of laws principles thereof.*

[FORM OF CERTIFICATE OF AUTHENTICATION]  
CERTIFICATE

*This bond is one of the bonds, of the series designated therein, described in the withinmentioned Indenture.*

U.S. BANK NATIONAL

&n bsp; ASSOCIATION Trustee

By .....

Authorized Officer

**SOUTHERN CALIFORNIA GAS  
COMPANY**

*TO*

**U.S. BANK NATIONAL ASSOCIATION**

*(successor by merger to U.S. Bank Trust National Association,  
formerly known as First Trust of California, National Association)*

*Trustee*

**SUPPLEMENTAL INDENTURE**

**To Base Indenture dated October 1, 1940**

*Dated as of December 10, 2004*

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THIS SUPPLEMENTAL INDENTURE, dated as of December 10, 2004 (this "Supplemental Indenture"), is made and entered into in the City of Los Angeles, State of California by and between SOUTHERN CALIFORNIA GAS COMPANY, a corporation duly organized and existing under the laws of the State of California, and having its principal place of business in the City of Los Angeles, State of California (hereinafter sometimes called the "Corporation") and U.S. BANK NATIONAL ASSOCIATION (successor by merger to U.S. Bank Trust National Association, formerly known as First Trust of California, National Association), an association duly organized and existing under the laws of the United States of America and having a corporate trust office in the City and County of Los Angeles, State of California (hereinafter, together with its predecessors as trustees under the Indenture referred to below, sometimes called the "Trustee").

**WITNESSETH:**

WHEREAS, the Corporation has executed and delivered to the Trustee a certain Indenture (hereinafter referred to as the "Base Indenture") dated October 1, 1940, to secure bonds of the Corporation designated generally as its "First Mortgage Bonds" to be issued from time to time in one or more series, any of which series may vary from any other as to certain particulars specified in Section 2.01 of the Base Indenture, and the Corporation has executed and delivered to the Trustee supplemental indentures dated, respectively, as of July 1, 1947, May 1, 1948, June 1, 1950, April 1, 1952, August 1, 1955, June 1, 1956, December 1, 1956, July 1, 1957, October 1, 1959, July 1, 1963, September 1, 1964, June 1, 1965, December 1, 1966, October 1, 1970, August 1, 1972, September 1, 1972, October 1, 1974, May 1, 1976, October 1, 1977, November 1, 1979, February 1, 1981, September 15, 1981, April 1, 1982, August 15, 1983, May 18, 1984, December 16, 1985, March 1, 1986, November 15, 1986, December 1, 1986, January 15, 1988, June 15, 1988, November 1, 1988, December 1, 1990, October 1, 1991, August 15, 1992, December 15, 1992, March 1, 1993, June 15, 1993, November 1, 1993, November 15, 1993, October 1, 2002, October 17, 2003 and December 15, 2003 supplementing and amending the Base Indenture (each, a "Prior Supplemental Indenture," and the Base Indenture together with all Prior Supplemental Indentures and this Supplemental Indenture being herein collectively referred to as the "Indenture"); and

WHEREAS, the Base Indenture and the Prior Supplemental Indentures dated, respectively, as of July 1, 1947, May 1, 1948, June 1, 1950, April 1, 1952 and August 1, 1955, are recorded in the office of the County Recorder of each of the Counties listed below in the Official Records thereof, as stated in the Prior Supplemental Indenture dated as of June 1, 1956; the Prior Supplemental Indentures dated, respectively, as of June 1, 1956 and December 1, 1956, are so recorded as stated in the Prior Supplemental Indenture dated as of July 1, 1957; the Prior Supplemental Indenture dated as of July 1, 1957 and each subsequently dated Prior Supplemental Indenture (other than the Prior Supplemental Indenture dated December 15, 2003) is so recorded as stated in the Prior Supplemental Indenture dated as of the next succeeding date; and the Prior Supplemental Indenture dated as of December 15, 2003 is recorded in the offices of the County Recorders in the Counties of the State of California, as follows:

<u>County</u>	<u>Reference</u>	<u>Date</u>
Fresno	Official Records, Document 03-0300288	December 18, 2003
Imperial	Official Records, Document 03-039861	December 19, 2003
Kern	Official Records, Document 03-0203273432	December 18, 2003
Kings	Official Records, Document 03-0337506	December 29, 2003
Los Angeles	Official Records, Document 03-3817178	December 18, 2003
Orange	Official Records, Document 03-001496810	December 18, 2003
Riverside	Official Records, Document 03-984000	December 17, 2003
San Bernardino	Official Records, Document 03-0930729	December 17, 2003
San Diego	Official Records, Document 03-1483662	December 17, 2003
San Luis Obispo	Official Records, Document 03-143540	December 22, 2003
Santa Barbara	Official Records, Document 03-0168576	December 17, 2003
Tulare	Official Records, Document 03-0124991	December 18, 2003
Ventura	Official Records, Document 03-0466331	December 17, 2003

WHEREAS, bonds of the Corporation of three (3) series designated, respectively, as its "First Mortgage Bonds, Series GG, Due 2012," "First Mortgage Bonds, Series HH, due 2018" and "First Mortgage Bonds, Series II, Due 2011" are outstanding as a part of the First Mortgage Bonds referred to in the Indenture, each such series of bonds, unless and until the taking of further appropriate action by the Board of Directors of the Corporation, being without limitation as to aggregate authorized principal amount; and

WHEREAS, pursuant to the provisions of Sections 2.01 and 2.02 of the Indenture, the Board of Directors has, by resolution duly adopted and delivered to the Trustee, created, as a part of the First Mortgage Bonds referred to in the Indenture, a new series of bonds designated "First Mortgage Bonds, Series JJ, due 2009" (the "Series JJ Bonds"), to be of the form, terms and provisions provided in that resolution and herein, which new series of bonds, unless and until the taking of further appropriate action by the Board of Directors, is to be without limitation as to aggregate authorized principal amount and of which series of bonds in the aggregate principal amount of \$100,000,000 are to be presently issued; and

WHEREAS, it is provided in the Indenture that all the business, franchises and properties, real, personal, and mixed, of every kind and nature whatsoever and wheresoever situated, which might thereafter be acquired by the Corporation, shall be as fully embraced within the lien thereof as if said properties were owned by the Corporation at the date of the Base Indenture and were particularly described therein and specifically conveyed thereby, excepting certain properties expressly excepted by the provisions of the Indenture; and

WHEREAS, subsequent to the execution of the most recently recorded Prior Supplemental Indenture identifying after acquired property, the Corporation has acquired properties hereinafter mentioned or referred to, all of which properties, upon the acquisition thereof by the Corporation, became and now are subject to the lien, operation and effect of the Indenture by virtue of the after-acquired property clause or other clauses thereof; the Corporation, nevertheless, desires to execute, acknowledge, deliver and cause to be recorded this Supplemental Indenture for the purposes, among others, of expressly and specifically subjecting such after-acquired properties to the lien of the Indenture and of further assuring and confirming the lien of the Indenture on all of the properties of every kind and character, whether real or personal and regardless of the date of acquisition thereof by the Corporation, intended to be subjected to the lien thereof; and

WHEREAS, under the provisions of Sections 2.02 and 16.01 of the Indenture, the Corporation and the Trustee may execute and deliver a Supplemental Indenture (i) to set forth the particulars, permitted by Section 2.01 of the Indenture, as to which the Series JJ Bonds may vary from the bonds of the other series of the First Mortgage Bonds, and (ii) for any purpose not inconsistent with the terms of the Indenture; and

WHEREAS, the making, executing, delivering and recording of this Supplemental Indenture have been duly authorized by proper corporate action of the Corporation; and

WHEREAS, the issuance of the Series JJ Bonds and the encumbrances of the Corporation's property to secure the Series JJ Bonds pursuant to this Supplemental Indenture have been authorized by the Public Utilities Commission of the State of California:

NOW, THEREFORE, in consideration of the foregoing premises and of other good and valuable consideration, receipt of which is hereby acknowledged, and in order: (a) to set forth or specify (i) the form of the fully registered Series JJ Bonds, and the form of the certificate to be endorsed on all Series JJ Bonds, and (ii) the terms and provisions of the Series JJ Bonds, including the particulars thereof which vary from the bonds of the other series of the First Mortgage Bonds; and (b) further to secure the payment of both the principal of and interest on the bonds of the Corporation now or at any time hereafter outstanding under the Indenture, including specifically, but without limitation, all of the First Mortgage Bonds now outstanding and the \$100,000,000

aggregate principal amount of Series JJ Bonds and further to secure the observance and performance of all of the covenants, agreements and conditions contained in the Indenture, and without in any way limiting the generality or effect of the Indenture insofar as by any provision thereof any of the property therein or hereafter described or referred to is now subject or intended to be subject to the lien and operation thereof, but to such extent confirming such lien and operation, the Corporation has executed and delivered this Supplemental Indenture and has granted, bargained, sold, released, conveyed, mortgaged, assigned, transferred, pledged, set over and confirmed, and does hereby grant, bargain, sell, release, convey, mortgage, assign, transfer, pledge, set over and confirm unto U.S. Bank National Association, the Trustee, and to its successors or successors in the trust created by the Indenture, and to its and their assigns, forever, with power of sale, subject, to the extent applicable by the terms of the Indenture to any of the properties hereinafter referred to or described, to the exceptions (other than as expressly provided in the granting clauses of the Prior Supplemental Indentures dated respectively as of June 1, 1956, July 1, 1957, October 1, 1959, July 1, 1963, September 1, 1964 and December 1, 1966 with respect to exception (f) set forth on page 67 of the Base Indenture and reading as follows: "(f) Any gas and/or oil acreage, gas and/or oil wells, gas and/or oil reserves, or gas and/or oil leaseholds hereafter acquired by the Corporation, or any property or equipment now or hereafter owned by the Corporation and used for the development of gas and/or oil acreage or for the drilling for or production of gas and/or oil from such acreage;" which exception (f) is by said granting clauses expressly made inapplicable to certain therein specified parcels of property), reservations, conditions, terms and provisions provided in the Indenture with respect to properties subject or intended to be subject thereto, all of the properties and assets of the Corporation, real, personal and mixed, of every kind and character, whether now or hereafter owned by the Corporation and wheresoever situated, including, without in any way limiting or modifying the generality or effect of the foregoing, all and singular, the following properties:

**FIRST:** All of the lots, pieces and parcels of land and rights or interests in real property situated in the Counties in the State of California, specifically described and mentioned or enumerated in Schedule A attached hereto, to which reference is hereby made and the same is made a part hereof with the same force and effect as if the same were here set forth at length.

**SECOND:** All and singular the plants, properties, equipment, real and personal property, estates, interests, goodwill, generating, transmission, feeding, storing, and distribution systems, and utilities of the Corporation situated in the Counties of Fresno, Imperial, Kern, Kings, Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Luis Obispo, Santa Barbara, Tulare and Ventura, and elsewhere, in the State of California, with all and singular the franchises, ordinances, grants, easements, licenses, powers, immunities, permits, privileges, appurtenances, tenements and other rights and property thereunto appertaining or belonging, as the same now exist and as the same and any and all parts thereof may hereafter exist or be improved, added to, enlarged, extended or acquired in said counties or elsewhere in said state or any other state or states.

**THIRD:** All other property, real, personal and mixed, of every kind, nature and description (including, without in any way limiting the effect or the generality hereof, all facilities; all stocks, bonds and other securities from time to time conveyed, assigned, transferred, mortgaged or pledged on behalf of the Corporation, or with its consent, to the Trustee in the manner and for the purposes as provided in the Indenture; all gas manufacturing plants, boilers, engines, compressors, motors, pumps, generators, gasholders, tanks, appliances, oil storage facilities, gas storage facilities, wells, buildings, structures, plants, works and other improvements; all gas transmission and distributing lines and systems; all meters and regulators and all other apparatus, machinery, appliances, tools, furniture, fixtures, supplies, facilities and utilities and other personal property; or any right or interest in any thereof; all business and goodwill, rights, consents, franchises, ordinances, licenses, agreements, contracts, permits, easements, rights of way, leases and leasehold interests; powers, grants, privileges and immunities to construct, operate and maintain lines and other facilities or properties for conveying gas or other commodity or utility for any purpose or purposes through, under and over public streets or highways, or public or private places or property; all reversions, remainders, tolls, incomes, revenues, earnings, rents, issues and profits of any property, real, personal and mixed; and all other classes and types of property described or referred to in the Indenture), now or hereafter owned, held, possessed, acquired or enjoyed by or in any manner conferred upon or appertaining to the Corporation, including the interest of the Corporation in all leases now or hereafter owned by it, together with all and singular the tenements, hereditaments, and appurtenances belonging or in any way appertaining to each and every part of any and all property subject or intended to be subject to the lien and operation of the Indenture, and the reversion and reversions, remainder and remainders, tolls, incomes, revenues, earnings, rents, issues and profits thereof.

**SAVING AND EXCEPTING**, however, from the property hereby mortgaged, conveyed in trust and/or pledged, all property, whether now owned by the Corporation or hereafter acquired by it, expressly saved and excepted from the lien of the Indenture and therein referred to as the "excepted property" (except as otherwise expressly provided in any Prior Supplemental Indenture hereinabove mentioned with respect to exception (f) of said "excepted property"), unless and until, upon the occurrence of an event of default under the Indenture, the Trustee, or any receiver appointed thereunder, shall take possession of any or all of such excepted property.

**TO HAVE AND TO HOLD** in trust with power of sale for the equal and proportionate benefit and security of all holders of bonds of the Corporation, now or hereafter outstanding under the Indenture as from time to time in effect, and for the enforcement and payment of said bonds and interest thereon when payable, and the performance of and compliance with the covenants and conditions of the Indenture as from time to time in effect, without any preference, distinction or priority as to lien or otherwise of any of said bonds over any others thereof by reason of the difference in the time of the actual issue, sale or negotiation thereof, or for any other reason whatsoever, except as otherwise expressly provided in the Indenture as from time to time in effect, so that each and every such bond shall have the same lien and so that the principal and interest of every such bond shall, subject to the terms thereof, be equally and proportionately secured by said lien, as if such bond had been made, executed, delivered, sold and negotiated simultaneously with the execution and delivery of the Base Indenture.

**IT IS HEREBY COVENANTED, DECLARED, AND AGREED** by and between the parties hereto that all such bonds are issued, authenticated and delivered, or are to be issued, authenticated and delivered, and that all property subject, or to become subject, to the Indenture is to be held, subject to the covenants, conditions, uses and trusts therein set forth.

#### ARTICLE I

##### AMOUNT, FORM, NUMBERING, DENOMINATION, TRANSFER AND EXCHANGE OF SERIES JJ BONDS, DUE 2009

**Section 1.01.** The Series JJ Bonds may be issued at any time or from time to time upon and subject to the terms and provisions of the Indenture. Unless and until the taking of further appropriate action by the Board of Directors of the Corporation the Series JJ Bonds shall be without limitation as to aggregate authorized principal amount.

**Section 1.02.** The Series JJ Bonds shall be issued only as fully registered bonds without coupons. In addition, the Series JJ Bonds may be issuable in whole or in part in the form of one or more securities that evidences all or part of the bonds of such series which is issued to a depository or a nominee thereof for such series (a "Global Security") and, in such case, the Board of Directors shall appoint a clearing agency registered under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), designated to act as depository (a "depository") for such Global Securities.

**Section 1.03.** In the event the Series JJ Bonds are issued as a Global Security the following provisions, in addition to the provisions of the Indenture, shall apply:

(a) Each Global Security authenticated under the Indenture shall be registered in the name of the depository designated for such Global Security or a nominee thereof and delivered to such depository or a nominee thereof or custodian therefor; and each such Global Security shall constitute a single bond for all purposes of this Supplemental Indenture.

(b) Notwithstanding any other provision in this Supplemental Indenture, no Global Security may be exchanged in whole or in part for bonds registered, and no transfer of a Global Security in whole or in part may be registered, in the name of any person other than the depository for such Global Security or a nominee thereof unless (A) such depository has notified the Corporation that it is unwilling or unable to continue as depository for such Global Security and a successor depository has not been appointed by the Corporation within 90 days of receipt by the Corporation of such notification, (B) if at any time the depository ceases to be a clearing agency registered under the Exchange Act at a time when the depository is required to be so registered to act as such depository and no successor depository shall have been appointed by the Corporation within 90 days after it became aware of such cessation, (C) the Corporation, in its sole discretion, executes and delivers to the Trustee a written order signed in the name of the Corporation by its Chairman of the Board, its President or a Vice President, and by its Treasurer, an Assistant Treasurer, its Secretary or an Assistant Secretary to the effect that such Global Security, together with all other Global Securities of the same series, shall be exchangeable as described below, or (D) an Event of Default (as defined in Section 1.02 of the Indenture) has occurred and is continuing with respect to the Series JJ Bonds. If any of the events described in clauses (A) through (D) of the preceding sentence occur, the beneficial owners of interests in the relevant Global Securities will be entitled to exchange those interests for definitive bonds and, without unnecessary delay but in any event not later than the earliest date on which those interests may be so exchanged, the Corporation will deliver to the Trustee definitive bonds in such form and denominations as are required by or pursuant to this Indenture, and of the same series, containing identical terms and in an aggregate principal amount equal to the principal amount of such Global Securities, such bonds to be duly executed by the Corporation. On or after the earliest date on which such beneficial interests may be so exchanged, such Global Securities shall be surrendered from time to time by the depository as shall be specified in the order from the Corporation with respect thereto (which the Corporation agrees to deliver), and in accordance with any instructions given to the Trustee and the depository (which instructions shall be in writing but need not be contained in or accompanied by an officers' certificate or be accompanied by an opinion of counsel), as shall be specified in the order from the Corporation with respect thereto to the Trustee, as the Corporation's agent for such purpose, to be exchanged, in whole or in part, for definitive bonds as described above without charge. The Trustee shall authenticate and make available for delivery, in exchange for each portion of such surrendered Global Security, a like aggregate principal amount of definitive bonds of the same series of authorized denominations and of like tenor as the portion of such Global Security to be exchanged. Promptly following any such exchange in part, such Global Security shall be returned by the Trustee to such depository or its custodian. If a definitive bond is issued in exchange for any portion of a Global Security after the close of business at the place where such exchange occurs on or after (i) any regular record date for the date the interest is due (the "Interest Payment Date") for such bond and before the opening of business at that place of payment on the next Interest Payment Date, or (ii) any special record date for the payment of interest for such bond and before the opening of business at such place of payment on the related proposed date for the payment of the interest which was not punctually paid or duly provided for on any Interest Payment Date ("Defaulted Interest"), as the case may be, interest shall not be payable on such Interest Payment Date or proposed date for payment, as the case may be, in respect of such definitive bond, but shall be payable on the Interest Payment Date or proposed date for payment, as the case may be, only to the person to whom interest in respect of such portion of such Global Security shall be payable in accordance with the provisions of this Indenture.

(c) Subject to Clause (b) above, any exchange or transfer of a Global Security for other bonds may be made in whole or in part, and all bonds issued in exchange for or upon transfer of a Global Security or any portion thereof shall be registered in such names as the depository for such Global Security shall direct.

(d) Every bond authenticated and delivered upon registration of transfer of, or in exchange for or in lieu of, a Global Security or any portion thereof, shall be authenticated and delivered in the form of, and shall be, a Global Security, unless such bond is registered in the name of a person other than the depository for such Global Security or a nominee thereof.

**Section 1.04.** Unless otherwise specified as contemplated by Section 2.01 for the bonds evidenced thereby, every Global Security authenticated and delivered hereunder shall bear a legend in substantially the following form:

THIS SECURITY IS A GLOBAL SECURITY WITHIN THE MEANING OF THE INDENTURE HEREINAFTER REFERRED TO AND IS REGISTERED IN THE NAME OF A DEPOSITARY OR A NOMINEE THEREOF. THIS SECURITY MAY NOT BE EXCHANGED IN WHOLE OR IN PART FOR A SECURITY REGISTERED, AND NO TRANSFER OF THIS SECURITY IN WHOLE OR IN PART MAY BE REGISTERED, IN THE NAME OF ANY PERSON OTHER THAN SUCH DEPOSITARY OR A NOMINEE THEREOF, EXCEPT IN THE LIMITED CIRCUMSTANCES DESCRIBED IN THE INDENTURE. ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL INASMUCH AS THE REGISTERED OWNER HEREOF HAS AN INTEREST HEREIN.

Section 1.05. The fully registered bonds without coupons and the certificate of authentication to be endorsed on all Series JJ Bonds shall be substantially in the form set forth on Exhibit A.

Section 1.06. The Series JJ Bonds may contain or have imprinted thereon such provisions or specifications not inconsistent with the Indenture as may be required to comply with the rules of any stock exchange or any federal or state authority or commission, or to comply with usage with respect thereto, and may bear such other appropriate endorsements or notations as are authorized or permitted by the Indenture.

Section 1.07. The fully registered Series JJ Bonds shall be issuable in denominations of \$1,000, \$5,000, \$10,000, \$25,000 or multiples of \$25,000 and shall be dated as provided in paragraph 1 of Section 2.01 of the Indenture. The definitive Series JJ Bonds shall be numbered in such manner as the Corporation shall at any time or from time to time determine.

Section 1.08. In the manner and subject to certain conditions and limitations specified herein and in the Indenture, Series JJ Bonds may be exchanged without a service charge for a like aggregate principal amount of such Series JJ Bonds of other authorized denomination or denominations; provided that the Corporation may require payment of a sum or sums sufficient to reimburse it for any stamp tax or other governmental charge payable in connection therewith.

Section 1.09. The Corporation shall maintain in the City and County of San Francisco, State of California, and in such other place or places as the Corporation may designate at any time or from time to time, an office or agency where Series JJ Bonds may be presented for payment, registration, transfer and exchange as provided therein or in the Indenture. Such office or agency in the City and County of San Francisco shall be the corporate trust office of the Trustee unless and until the Corporation shall designate another office or agency by notice in writing delivered to the Trustee. Notwithstanding the foregoing, if and when definitive bonds are issued, the Corporation shall maintain in the Borough of Manhattan, City and County of New York, State of New York, an office or agency where Series JJ Bonds may be presented for payment, registration, transfer and exchange as provided therein or in the Indenture.

Section 1.10. No transfer or exchange of any Series JJ Bonds pursuant to any of the provisions of this Article I shall be made except upon and in accordance with all of the applicable terms, provisions and conditions of said bonds and of the Indenture.

## ARTICLE II

### INTEREST, MATURITY DATE, REDEMPTION AND CERTAIN OTHER PROVISIONS OF SERIES JJ BONDS, DUE 2009

Section 2.01. The Series JJ Bonds shall bear interest at the rate, shall be expressed to mature as to principal, and shall be payable as to principal and interest at such place or places and in such money, all as provided in the form of Series JJ Bond set forth on Exhibit A hereto and by the applicable provisions of the Indenture. In addition, December 10, 2004 shall be an Interest Payment Date for the Series JJ Bonds for purposes of Section 2.01 of the Base Indenture (as supplemented by the Prior Supplemental Indentures), provided that no interest shall be payable on such date.

Section 2.02. The Series JJ Bonds shall not be subject to redemption prior to maturity.

Section 2.03. The Corporation may at any time deliver to the Trustee for cancellation any Series JJ Bonds previously authenticated and delivered under the Indenture which the Corporation may have acquired in any manner whatsoever and all Series JJ Bonds so delivered shall be promptly cancelled by the Trustee upon the request of the Corporation.

Section 2.04. The Series JJ Bonds shall, except as in this Supplemental Indenture otherwise expressly provided, be on the terms and provisions, and shall represent such rights and be entitled to such benefits, as are applicable thereto by the terms of the Indenture.

Section 2.05. The Series JJ Bonds shall be entitled to the benefits of the Renewal Fund as provided in the Indenture.

Section 2.06. The following Section 11.01A shall apply to the Series JJ Bonds in lieu of Section 11.01 of the Indenture:

"Section 11.01A If the Corporation, its successors or assigns, shall

(a) pay or cause to be paid the principal of and interest on the bonds and coupons and claims for interest thereon to become due at the time and in the manner stipulated therein and herein, and/or

(b) provide for the payment of the bonds and interest thereon by depositing in cash with the Trustee or other depositary satisfactory to it at any time at or before maturity the entire amount due or to become due thereon for principal and interest to maturity of all the bonds outstanding, and/or

(c) in case of a call of all of the bonds then outstanding for redemption, deposit with the Trustee on or before the date on which all of such bonds (other than those which shall have matured by their terms) shall have been called for redemption, as provided in Article VII, the entire amount of the redemption price thereof, including interest and premium, if any, and shall deliver to the Trustee (1) proof satisfactory to the Trustee that notice of redemption as provided in Article VII has been given, or (2) proof satisfactory to the Trustee that arrangements have been made insuring that such notice will be given, or (3) a written instrument executed by the Corporation under its corporate seal, and expressed to be irrevocable, authorizing the Trustee to give such notice for and on behalf of the Corporation, and/or

(d) surrender to the Trustee for cancellation all the bonds and coupons thereto appertaining for which payment is not so provided,

and shall also pay, or satisfactorily provide, all other sums due and payable hereunder by the Corporation, including the compensation and expenses of the Trustee, then and in that case,

(i) at the request of the Corporation all the mortgaged property shall revert to the Corporation and the entire estate, right, title and interest of the Trustee and of the holders and registered owners of the bonds and coupons in respect of the mortgaged property shall thereupon cease, determine and become void; and

(ii) the Trustee in such case, upon the cancellation of all outstanding bonds and coupons for the payment of which cash shall not have been deposited in accordance with the provisions of this Indenture, shall upon request of the Corporation, and at its cost and expense (A) and upon delivery to it of an opinion of counsel stating that (x) the Corporation has received from, or there has been published by, the Internal Revenue Service a ruling, or (y) since December 7, 2004 there has been a change in applicable federal income tax law, in either case to the effect that, and based thereon such opinion of counsel shall confirm that, the holders of Series JJ Bonds will not recognize income, gain or loss for federal income tax purposes as a result of such defeasance and will be subject to federal income tax on the same amounts, in the same manner and at the same times as would have been the case if such defeasance had not occurred, execute to the Corporation, or its order, proper instruments acknowledging satisfaction of this Indenture and (B) shall surrender to the Corporation, or its order, all cash and deposited securities, if any, which shall then be held by it hereunder as a part of the mortgaged property (exclusive of cash held in trust as provided in Section 5.03); provided, however, that if any such property shall have been delivered to the Trustee by any person or corporation other than the Corporation, the same shall be delivered or otherwise disposed of in accordance with any reservations, limitations, conditions or provisions which may have been set forth in the instrument in writing then executed, if any, respecting the use, management or disposition thereof; and provided further that if the Corporation pursuant to clauses (1) or (2) of subdivision (c) above shall have delivered to the Trustee proof satisfactory to it that notice of redemption as provided in Article VII has been given or that arrangements have been made insuring that such notice will be given, there shall also be delivered to the Trustee an officers' certificate stating that all conditions precedent to the satisfaction and discharge of this Indenture have been complied with and an opinion of counsel stating that in his opinion such conditions precedent have been complied with."

## ARTICLE III

### SUNDRY PROVISIONS

Section 3.01. The recitals of fact contained herein shall be taken as the statements of the Corporation, and the Trustee assumes no responsibility for the correctness of the same. The Corporation hereby covenants and agrees that it will cause this Supplemental Indenture to be kept recorded and/or filed as may be required by law, in such manner and in such places as may be necessary fully to preserve and protect the security of the bondholders and all of the rights of the Trustee hereunder, and that it will with all reasonable dispatch deposit with the Trustee counterparts of this Supplemental Indenture bearing official notation or endorsements showing such recordation and/or filing, or in case such counterparts are not returned to the Corporation, furnish to the Trustee the best official evidence of such recordation and/or filing reasonably obtainable by the Corporation, or evidence of the taking of such other action, if any, but the Trustee, subject to the provisions of Sections 14.02 and 14.03 of the Indenture, shall in no way be liable for any failure or omission in this regard.

Section 3.02. The date of this Supplemental Indenture and the date of the Series JJ Bonds are intended as and for a date for the convenient identification of this Supplemental Indenture and of the Series JJ Bonds, and are not intended to indicate that this Supplemental Indenture was executed and delivered or that the Series JJ Bonds were executed, delivered or issued on said date; it being hereby provided that this Supplemental Indenture may be executed and delivered, and that the Series JJ Bonds may be executed, delivered or issued, either on said date or before or after said date, and that this Supplemental Indenture is in fact executed and delivered by each party hereto on the date of its certificate of acknowledgment hereto attached.

Section 3.03. This Supplemental Indenture shall be deemed to be part of the Base Indenture, and the Corporation agrees to conform to and comply with all and singular the terms, provisions, conditions and covenants set forth therein and herein. This Supplemental Indenture shall be construed in connection with and as a part of the Indenture.

Section 3.04. It is further agreed that the Trustee accepts the trust imposed upon it by this Supplemental Indenture, upon and subject to the same terms and conditions as are expressed in Article XIV of the Base Indenture.

Section 3.05. In order to facilitate the recording of this Supplemental Indenture, the same may be, executed in several counterparts, each of which so executed shall be deemed to be an original, and such counterparts shall collectively constitute one and the same instrument.

Section 3.06. All terms used in this Supplemental Indenture which are defined in the Indenture are not defined herein shall have the meaning assigned to them in the Indenture.

Section 3.07. To the extent any provision in this Supplemental Indenture conflicts with any provision in the Indenture, the provisions of this Supplemental Indenture shall govern; provided however, that in the event such conflict would require bondholder consent, the terms and provisions of the Indenture shall govern.

Section 3.08. This Supplemental Indenture and the Series JJ Bonds shall be governed by and construed in accordance with the laws of the State of California, without regard to conflicts of laws principles thereof.

Section 3.09. To the extent not otherwise addressed in this Supplemental Indenture, this Supplemental Indenture shall be subject to the provisions of Article XVII of the Indenture, the terms of which are hereby incorporated by reference into this Indenture Supplement.

IN WITNESS WHEREOF, Southern California Gas Company has caused this Supplemental Indenture to be signed in its corporate name by one of its Vice Presidents or its Treasurer and its Secretary or an Assistant Secretary and its corporate seal to be hereunto duly affixed, and U.S. Bank National Association, in token of its acceptance of the trust hereby established, has caused this Supplemental Indenture to be signed in its corporate name by two of its authorized officers, including one or more of its Vice Presidents, all as of December 10, 2004.

Attest: SOUTHERN CALIFORNIA GAS COMPANY

Name: Thomas C. Sanger Title: Secretary Name: Terry M. Fleskes Title: Vice President and Treasurer

Attest: U.S. BANK NATIONAL ASSOCIATION

Authorized Signatory Name: Fonda Hall Title: Vice President

STATE OF CALIFORNIA COUNTY OF SAN DIEGO

On this day of December, 2004, before me, Notary Public, personally appeared Terry M. Fleskes, personally known to me to be one of the persons whose names are subscribed to the within instrument and acknowledged to me that such person executed the same in the person's authorized capacity, and that by the person's signature on the instrument, the entity upon behalf of which the person acted executed the instrument.

Witness my hand and official seal.

Notary Public

My Commission expires

STATE OF CALIFORNIA COUNTY OF SAN DIEGO

On this day of December, 2004, before me, Notary Public, personally appeared Thomas C. Sanger, personally known to me to be one of the persons whose names are subscribed to the within instrument and acknowledged to me that such person executed the same in the person's authorized capacity, and that by the person's signature on the instrument, the entity upon behalf of which the person acted executed the instrument.

Witness my hand and official seal.

Notary Public

My Commission expires

STATE OF CALIFORNIA COUNTY OF

On this day of December, 2004, before me, Notary Public, personally appeared and, personally known to me to be the persons whose names are subscribed to the within instrument and acknowledged to me that they executed the same in their authorized capacities, and that by their signatures on the instrument the persons, or the



entity upon behalf of which the persons acted, executed the instrument.

Witness my hand and official seal.

-----  
Notary Public

My Commission expires

STATE OF CALIFORNIA

COUNTY OF \_\_\_\_\_

On this \_\_\_\_\_ day of December, 2004, before me, \_\_\_\_\_, Notary Public, personally appeared \_\_\_\_\_ and \_\_\_\_\_, personally known to me to be the persons whose names are subscribed to the within instrument and acknowledged to me that they executed the same in their authorized capacities, and that by their signatures on the instrument the persons, or the entity upon behalf of which the persons acted, executed the instrument.

Witness my hand and official seal.

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Notary Public

My Commission expires

**EXHIBIT A**

[FORM OF REGISTERED BOND WITHOUT COUPONS, SERIES JJ, DUE 2009]

[If this bond is issued as a global security, insert the following legend: THIS SECURITY IS A GLOBAL SECURITY WITHIN THE MEANING OF THE INDENTURE HEREINAFTER REFERRED TO AND IS REGISTERED IN THE NAME OF A DEPOSITARY OR A NOMINEE THEREOF. THIS SECURITY MAY NOT BE EXCHANGED IN WHOLE OR IN PART FOR A SECURITY REGISTERED, AND NO TRANSFER OF THIS SECURITY IN WHOLE OR IN PART MAY BE REGISTERED, IN THE NAME OF ANY PERSON OTHER THAN SUCH DEPOSITARY OR A NOMINEE THEREOF, EXCEPT IN THE LIMITED CIRCUMSTANCES DESCRIBED IN THE INDENTURE. ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL INASMUCH AS THE REGISTERED OWNER HEREOF HAS AN INTEREST HEREIN.]

**SOUTHERN CALIFORNIA GAS COMPANY**  
(Incorporated under the laws of the State of California)

FLOATING RATE FIRST MORTGAGE BOND, SERIES JJ, DUE 2009

No. \_\_\_\_\_ \$ \_\_\_\_\_  
CUSIP No. \_\_\_\_\_

SOUTHERN CALIFORNIA GAS COMPANY, a corporation organized and existing under the laws of the State of California (hereinafter called the "Corporation," which term shall include any successor corporation, as defined in the Indenture hereinafter referred to), for value received, hereby promises to pay to \_\_\_\_\_ [If this bond is issued as a global security, insert "CEDE & CO." in the foregoing space] or registered assigns, the principal sum of \_\_\_\_\_ in lawful money of the United States of America, on the first day of December, 2009, and to pay interest thereon from the date of this bond, or from the most recent date to which interest has been paid or duly provided for, quarterly in arrears, on the first day of March, June, September and December in each year (each, an "Interest Payment Date"), commencing March 1, 2005, to the holder of record of this bond on the immediately preceding fifteenth day of February, May, August and November, as the case may be, and at Maturity at the Applicable Rate (as defined below) in like lawful money until the Corporation's obligation with respect to the payment of such principal shall be discharged as provided in the Indenture hereinafter mentioned. Both the principal of and interest on this bond will be paid at the corporate trust office of U.S. Bank National Association, or its successor trustee under said Indenture, in the City and County of San Francisco, State of California [if this bond is a definitive bond, insert: ", or at the office or agency in the Borough of Manhattan, City and County of New York, State of New York, that the Corporation maintains for such purpose"]. Notwithstanding the foregoing, so long as the holder of the Series JJ Bonds is a depositary, or its nominee, payment of the principal of (and premium, if any) and interest on this bond will be made by wire transfer of immediately available funds.

The "Applicable Rate" shall initially be equal to 2.63% and shall be reset on each Interest Payment Date other than at Maturity, beginning on March 1, 2005, to the 3 Month LIBOR Rate as of such Interest Payment Date plus .17% per year.

"3 Month LIBOR Rate" means the rate for deposits in U.S. dollars for the 3-month period commencing on the applicable Interest Payment Date which appears on Telerate Page 3750 at approximately 11:00 a.m., London time, on the second London banking day prior to the applicable Interest Payment Date. If this rate does not appear on Telerate Page 3750, the calculation agent will determine the rate on the basis of the rates at which deposits in U.S. dollars are offered by four major banks in the London interbank market (selected by the calculation agent) at approximately 11:00 a.m., London time, on the second London banking day prior to the applicable Interest Payment Date to prime banks in the London interbank market for a period of three months commencing on that Interest Payment Date and in a principal amount equal to an amount not less than \$1,000,000 that is representative for a single transaction in such market at such time. In such case, the calculation agent will request the principal London office of each of the aforesaid major banks to provide a quotation of such rate. If at least two such quotations are provided, the rate for that Interest Payment Date will be the arithmetic mean of the quotations, and, if fewer than two quotations are provided as requested, the rate for that Interest Payment Date will be the arithmetic mean of the rates quoted by major banks in New York City, selected by the calculation agent, at approximately 11:00 a.m., New York City time, on the second London banking day prior to the applicable Interest Payment Date for loans in U.S. dollars to leading European banks for a period of three months commencing on that Interest Payment Date and in a principal amount equal to an amount not less than \$1,000,000 that is representative for a single transaction in such market at such time. A London banking day is any business day in which dealings in U.S. dollars are transacted in the London interbank market.

"Telerate Page 3750" means the display page so designated on the Moneyline Telerate, Inc. (or such other page as may replace such page on that service or any successor service for the purpose of displaying London interbank offered rates of major banks).

The calculation agent will, upon the request of the holder of this bond, provide the interest rate then in effect. U.S. Bank National Association will serve as the calculation agent until such time as the Corporation appoints a successor calculation agent. All calculations made by the calculation agent in the absence of manifest error shall be conclusive for all purposes and binding on the Corporation and the holder of this bond. The Corporation may appoint a successor calculation agent with the written consent of the Trustee.

All percentages resulting from any calculation of the interest rate with respect to this bond will be rounded, if necessary, to the nearest one-hundred thousandth of a percentage point, with five one-millionths of a percentage point rounded upwards, and all dollar amounts in or resulting from any such calculation will be rounded to the nearest cent (with one-half cent being rounded upwards).

Interest on this bond shall be calculated on the basis of a 360-day year and the actual number of days in each quarterly interest period.

The provisions of this bond are continued on the reverse hereof and such continued provisions shall for all purposes have the same effect as though set forth at this place.

IN WITNESS WHEREOF, SOUTHERN CALIFORNIA GAS COMPANY has caused this bond to be signed in its corporate name by the facsimile signature of its authorized officer and a facsimile of its corporate seal to be hereto affixed and attested by its Secretary or an Assistant Secretary.

Dated:

Attest:

-----  
Secretary

[REVERSE SIDE - FORM OF REGISTERED BOND  
WITHOUT COUPONS, SERIES JJ, DUE 2009]

This bond is one of a duly authorized issue of bonds of the Corporation (herein called the "bonds"), of the series hereinafter specified, all issued and to be issued under and all equally and ratably secured by a mortgage and deed of trust dated October 1, 1940, between the Corporation and U.S. Bank National Association, as successor trustee, to which mortgage and deed of trust and all indentures supplemental thereto, including Supplemental Indentures dated, respectively, as of July 1, 1947, August 1, 1955, June 1, 1956, December 1, 1956, June 1, 1965, August 1, 1972, May 1, 1976, September 15, 1981, May 18, 1984, November 15, 1986, January 15, 1988, August 15, 1992, October 1, 2002, October 17, 2003, December 15, 2003 and December 10, 2004 (herein collectively referred to as the "Indenture"), reference is hereby made for a description of the property conveyed in trust, mortgaged and pledged, the nature and extent of the security, the rights of the registered owners of the bonds and of the Trustee or trustees in respect thereof, the terms and conditions upon which the bonds are, and are to be, secured and the circumstances under which additional bonds may be issued. The bonds may be issued for various principal sums, and may be issued in series, which may mature at different times, may bear interest at different times, may bear interest at different rates and may otherwise vary as in the Indenture provided. This bond is one of a series designated as the "First Mortgage Bonds, Series JJ, due 2009" (herein called "Series JJ Bonds") of the Corporation, issued under and secured by the Indenture. Terms used but not defined herein shall have the respective meanings assigned thereto in the Indenture.

As provided in the Indenture, by any indenture or indentures supplemental thereto executed by the Corporation and the Trustee and consented to by the holders of not less than two-thirds (2/3) in principal amount of the bonds at the time outstanding, and, in case one or more, but less than all, of the series of bonds then outstanding are affected by such supplemental indenture, consented to by the holders of at least two-thirds (2/3) in principal amount of the bonds of each series so affected, the Indenture or any indenture supplemental thereto and the rights and obligations of the Corporation and the holders of bonds, may be modified or altered from time to time, as provided in the Indenture; provided, however, (a) that the right of any holder of any bond to receive payment of the principal of and interest on such bond, on or after the respective due dates expressed in such bond, or to institute suit for the enforcement of any such payment on or after such respective dates, shall not be impaired or affected by any such supplemental indenture without the consent of such holder; and (b) that no such modification or alteration shall reduce the proportions of bondholders' consents required as aforesaid; such proportions to be determined in each case as provided in the Indenture.

The Series JJ Bonds are entitled to the benefits of the Renewal Fund as provided in the Indenture.

The Series JJ Bonds are not redeemable prior to Maturity

In case an event of default, as defined in the Indenture, shall occur, the principal of all bonds then outstanding under the Indenture may be declared or become due and payable upon the conditions and in the manner and with the effect provided in the Indenture.

This bond is transferable by the registered owner hereof at the office or agency of the Corporation in said City and County of San Francisco [if this bond is a definitive bond, insert: ", or at the office or agency in the Borough of Manhattan, City and County of New York, State of New York, that the Corporation maintains for such purpose"] and in such other place or places as the Corporation may designate at any time or from time to time, and thereupon a new fully registered bond or bonds of said series, without coupons, of authorized denomination or denominations, of a like aggregate principal amount, will be issued to the transferee or transferees in exchange for this bond; and at any of said offices or agencies fully registered Series JJ Bonds without coupons, are exchangeable for a like aggregate principal amount of other such fully registered bonds of authorized denominations; all in the manner and subject to the conditions as provided in the Indenture.

No recourse shall be had for the payment of the principal of or the interest on this bond or for any claim based hereon or on the Indenture or any indenture supplemental thereto, against any incorporator, stockholder, director or officer, past, present or future, of the Corporation, or of any predecessor or successor corporation, either directly or through the Corporation, or any such predecessor or successor corporation, whether by virtue of any constitution, statute or rule of law, or by the enforcement of any assessment or penalty, or otherwise, all such liability being waived and released by every registered owner hereof by the acceptance of this bond and as part of the consideration for the issue hereof, and being likewise waived and released by the terms of the Indenture.

This bond shall not become valid or obligatory for any purpose or be entitled to any benefit under the Indenture until U.S. Bank National Association, or its successor as Trustee under the Indenture, shall have signed the form of certificate endorsed hereon.

This bond shall be governed by and construed in accordance with the laws of the State of California, without regard to conflicts of laws principles thereof.

[FORM OF CERTIFICATE OF AUTHENTICATION]

**CERTIFICATE**

This bond is one of the bonds, of the series designated therein, described in the within-mentioned Indenture.

U.S. Bank National  
Association

Trustee

By-----

Authorized Officer

IN WITNESS WHEREOF, Southern California Gas Company has caused this Supplemental Indenture to be signed in its corporate name by one of its Vice Presidents or its Treasurer and its Secretary or an Assistant Secretary and its corporate seal to be hereunto duly affixed, and U.S. Bank National Association, in token of its acceptance of the trust hereby established, has caused this Supplemental Indenture to be signed in its corporate name by two of its authorized officers, including one or more of its Vice Presidents, all as of December 10, 2004.

Attest:

/s/ THOMAS C. SANGER

Name: Thomas C. Sanger

Title: Secretary

/s/ TERRY M. FLESKES

Name: Terry M. Fleskes

Title: Vice President and Treasurer

Attest:

U.S. BANK NATIONAL ASSOCIATION

By:

-----  
Authorized Signatory

-----  
Name: Fonda Hall

Title: Vice President

**SEMPRA ENERGY  
SEVERANCE PAY AGREEMENT**

**THIS AGREEMENT** (this "Agreement"), dated as of \_\_\_\_\_ (the "Effective Date") is made by and between SEMPRA ENERGY, a California corporation, and \_\_\_\_\_ (the "Executive").

**WHEREAS**, the Executive is currently employed by Sempra Energy or a subsidiary of Sempra Energy (Sempra Energy and its subsidiaries are hereinafter collectively referred to as the "Company") as \_\_\_\_\_; and

**WHEREAS**, the Board of Directors of Sempra Energy (the "Board") has determined that it is in the best interests of the Company to institute formalized severance arrangements for certain of the executives of the Company, including the Executive.

**NOW, THEREFORE**, in consideration of the premises and mutual covenants herein contained, the Company and the Executive hereby agree as follows:

**Section 1. Definitions.** For purposes of this Agreement, the following capitalized terms have the meanings set forth below:

"Accounting Firm" has the meaning assigned thereto in Section 9(b) hereof.

"Act" has the meaning assigned thereto in Section 2 hereof.

"Affiliate" has the meaning set forth in Rule 12b-2 promulgated under the Exchange Act.

"Beneficial Owner" has the meaning set forth in Rule 13d-3 promulgated under the Exchange Act.

"Buyer" has the meaning assigned thereto in Section 17(i) hereof.

"Cause" means (a) Prior to a Change in Control, (i) the willful failure by the Executive to substantially perform the Executive's duties with the Company (other than any such failure resulting from the Executive's incapacity due to physical or mental illness, (ii) the grossly negligent performance of such obligations referenced in clause (i) of this definition, (iii) the Executive's gross insubordination; and/or (iv) the Executive's commission of one or more acts of moral turpitude that constitute a violation of applicable law (including but not limited to a felony) which have or result in an adverse effect on the Company, monetarily or otherwise, or one or more significant acts of dishonesty. For purposes of clause (i) of this definition, no act, or failure to act, on the Executive's part shall be deemed "willful" unless done, or omitted to be done, by the Executive not in good faith and without reasonable belief that the Executive's act, or failure to act, was in the best interests of the Company. (b) From and after a Change in Control, (i) the willful and continued failure by the Executive to substantially perform the Executive's duties with the Company (other than any such failure resulting from the Executive's incapacity due to physical or mental illness or any such actual or anticipated failure after the issuance of a Notice of Termination for Good Reason by the Executive pursuant to Section 3 hereof) and/or (ii) the Executive's commission of one or more acts of moral turpitude that constitute a violation of applicable law (including but not limited to a felony) which have or result in an adverse effect on the Company, monetarily or otherwise, or one or more significant acts of dishonesty. For purposes of clause (i) of this definition, no act, or failure to act, on the Executive's part shall be deemed "willful" unless done, or omitted to be done, by the Executive not in good faith and without reasonable belief that the Executive's act, or failure to act, was in the best interests of the Company. Notwithstanding the foregoing, the Executive shall not be deemed terminated for Cause pursuant to clause (i) of this definition unless and until the Executive shall have been provided with reasonable notice of and, if possible, a reasonable opportunity to cure the facts and circumstances claimed to provide a basis for termination of the Executive's employment for Cause.

"Change in Control" shall be deemed to have occurred when:

- a. Any Person is or becomes the Beneficial Owner, directly or indirectly, of securities of the Company (not including in the securities beneficially owned by such Person any securities acquired directly from the Company or its Affiliates other than in connection with the acquisition by the Company or its Affiliates of a business) representing twenty percent (20%) or more of the combined voting power of the Company's then outstanding securities; or
- b. The following individuals cease for any reason to constitute a majority of the number of directors then serving: individuals who, on the Effective Date, constitute the Board and any new director (other than a director whose initial assumption of office is in connection with an actual or threatened election contest, including, but not limited to, a consent solicitation relating to the election of directors of the Company) whose appointment or election by the Board or nomination for election by the Company's shareholders was approved or recommended by a vote of at least two-thirds (2/3) of the directors then still in office who either were directors on the date hereof or whose appointment, election or nomination for election was previously so approved or recommended; or
- c. There is consummated a merger or consolidation of the Company or any direct or indirect subsidiary of the Company with any other corporation, other than (A) a merger or consolidation which would result in the voting securities of the Company outstanding immediately prior to such merger or consolidation continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity or any parent thereof), in combination with the ownership of any trustee or other fiduciary holding securities under an employee benefit plan of the Company, at least sixty percent (60%) of the combined voting power of the securities of the Company or such surviving entity or any parent thereof outstanding immediately after such merger or consolidation, or (B) a merger or consolidation effected to implement a recapitalization of the Company (or similar transaction) in which no Person is or becomes the Beneficial Owner, directly or indirectly, of securities of the Company (not including in the securities beneficially owned by such Person any securities acquired directly from the Company or its Affiliates other than in connection with the acquisition by the Company or its Affiliates of a business) representing twenty percent (20%) or more of the combined voting power of the Company's then outstanding securities; or
- d. The shareholders of the Company approve a plan of complete liquidation or dissolution of the Company or there is consummated an agreement for the sale or disposition by the Company of all or substantially all of the Company's assets, other than a sale or disposition by the Company of all or substantially all of the Company's assets to an entity, at least sixty percent (60%) of the combined voting power of the voting securities of which are owned by shareholders of the Company in substantially the same proportions as their ownership of the Company immediately prior to such sale.

"Change in Control Date" means the date on which a Change in Control occurs.

"Code" means the Internal Revenue Code of 1986, as amended.

"Compensation Committee" means the compensation committee of the Board.

"Consulting Period" has the meaning assigned thereto in Section 13(e) hereof.

"Date of Termination" has the meaning assigned thereto in Section 3(b) hereof.

"Disability," has the meaning set forth in the Company's long-term disability plan or its successor; *provided, however*, that the Board may not terminate the Executive's employment hereunder by reason of Disability unless (i) at the time of such termination there is no reasonable expectation that the Executive will return to work within the next ninety (90) day period and (ii) such termination is permitted by all applicable disability laws.

"Exchange Act" means the Securities Exchange Act of 1934, as amended, and the applicable rulings and regulations thereunder.

"Excise Tax" has the meaning assigned thereto in Section 9(a) hereof.

"Good Reason" means:

- a. Prior to a Change in Control, the occurrence of any of the following without the prior written consent of the Executive, unless such act or failure to act is corrected prior to the Date of Termination specified in the Notice of Termination (as discussed in Section 3 hereof):

- i. the assignment to the Executive of any duties materially inconsistent with the range of duties and responsibilities appropriate to a senior executive within the Company (such range determined by reference to past, current and reasonable practices within the Company);
  - ii. a material reduction in the Executive's overall standing and responsibilities within the Company, but not including (A) a mere change in title or (B) a transfer within the Company, which, in the case of both (A) and (B), does not adversely affect the Executive's overall status within the Company;
  - iii. a material reduction by the Company in the Executive's aggregate annualized compensation and benefits opportunities, except for across-the-board reductions (or modifications of benefit plans) similarly affecting all similarly situated executives (both of the Company and of any Person then in control of the Company) of comparable rank with the Executive;
  - iv. the failure by the Company to pay to the Executive any portion of the Executive's current compensation and benefits or any portion of an installment of deferred compensation under any deferred compensation program of the Company within thirty (30) days of the date such compensation is due;
  - v. any purported termination of the Executive's employment that is not effected pursuant to a Notice of Termination satisfying the requirements of Section 3 hereof; for purposes of this Agreement, no such purported termination shall be effective;
  - vi. the failure by the Company to obtain a satisfactory agreement from any successor of the Company requiring such successor to assume and agree to perform the Company's obligations under this Agreement, as contemplated in Section 15(c) hereof;
  - vii. the failure by the Company to provide the indemnification and D&O insurance protection Section 10 of this Agreement requires it to provide; or
  - viii. the failure by the Company to comply with any material provision of this Agreement.
- b. From and after a Change in Control, the occurrence of any of the following without the prior written consent of the Executive, unless such act or failure to act is corrected prior to the Date of Termination specified in the Notice of Termination (as discussed in Section 3 hereof):

- i. an adverse change in the Executive's title, authority, duties, responsibilities or reporting lines as in effect immediately prior to the Change in Control;
- ii. a reduction by the Company in the Executive's aggregate annualized compensation opportunities, except for across-the-board reductions in base salaries, annual bonus opportunities or long-term incentive compensation opportunities of less than ten percent (10%) similarly affecting all similarly situated executives (both of the Company and of any Person then in control of the Company) of comparable rank with the Executive; or the failure by the Company to continue in effect any material benefit plan in which the Executive participates immediately prior to the Change in Control, unless an equitable arrangement (embodied in an ongoing substitute or alternative plan) has been made with respect to such plan, or the failure by the Company to continue the Executive's participation therein (or in such substitute or alternative plan) on a basis not materially less favorable, both in terms of the amount of benefits provided and the level of the Executive's participation relative to other participants, as existed at the time of the Change in Control;
- iii. the relocation of the Executive's principal place of employment immediately prior to the Change in Control Date (the "Principal Location") to a location which is both further away from the Executive's residence and more than thirty (30) miles from such Principal Location, or the Company's requiring the Executive to be based anywhere other than such Principal Location (or permitted relocation thereof), or a substantial increase in the Executive's business travel obligations outside of the Southern California area as of the Effective Date other than any such increase that (A) arises in connection with extraordinary business activities of the Company of limited duration and (B) is understood not to be part of the Executive's regular duties with the Company;
- iv. the failure by the Company to pay to the Executive any portion of the Executive's current compensation and benefits or any portion of an installment of deferred compensation under any deferred compensation program of the Company within thirty (30) days of the date such compensation is due;
- v. any purported termination of the Executive's employment that is not effected pursuant to a Notice of Termination satisfying the requirements of Section 3 hereof; for purposes of this Agreement, no such purported termination shall be effective;
- vi. the failure by the Company to obtain a satisfactory agreement from any successor of the Company requiring such successor to assume and agree to perform the Company's obligations under this Agreement, as contemplated in Section 15(c) hereof;
- vii. the failure by the Company to provide the indemnification and D&O insurance protection Section 10 of this Agreement requires it to provide; or
- viii. the failure by the Company to comply with any material provision of this Agreement.

Following a Change in Control, the Executive's determination that an act or failure to act constitutes Good Reason shall be presumed to be valid unless such determination is deemed to be unreasonable by an arbitrator pursuant to the procedure described in Section 12 hereof. The Executive's right to terminate the Executive's employment for Good Reason shall not be affected by the Executive's incapacity due to physical or mental illness. The Executive's continued employment shall not constitute consent to, or a waiver of rights with respect to, any act or failure to act constituting Good Reason hereunder.

"Gross-Up Payment" has the meaning assigned thereto in Section 9(a) hereof.

"Incentive Compensation Awards" means awards granted under Incentive Compensation Plans providing the Executive with the opportunity to earn, on a year-by-year basis, annual and long-term incentive compensation.

"Incentive Compensation Plans" means annual incentive compensation plans and long-term incentive compensation plans of the Company, which long-term incentive compensation plans may include plans offering stock options, restricted stock and other long-term incentive compensation.

"Involuntary Termination" means (a) a termination of employment by the Company other than for Cause, death, or Disability, or (b) the Executive's resignation of employment with the Company for Good Reason; *provided, however*, that except as provided in the last paragraph of Section 6 hereof, a termination of the Executive's employment by reason of his retirement prior to a Change in Control shall not constitute an Involuntary Termination hereunder.

"JAMS Rules" has the meaning assigned thereto in Section 12 hereof.

"Notice of Termination" has the meaning assigned thereto in Section 3(a) hereof.

"Payment" has the meaning assigned thereto in Section 9(a) hereof.

"Person" has the meaning set forth in section 3(a)(9) of the Exchange Act, as modified and used in sections 13(d) and 14(d) thereof, except that such term shall not include (i) the Company or any of its Affiliates, (ii) a trustee or other fiduciary holding securities under an employee benefit plan of the Company or any of its Affiliates, (iii) an underwriter temporarily holding securities pursuant to an offering of such securities, (iv) a corporation owned, directly or indirectly, by the shareholders of the Company in substantially the same proportions as their ownership of stock of the Company, or (v) a person or group as used in Rule 13d-1(b) promulgated under the Exchange Act.

"Post-Change in Control Accrued Obligations" has the meaning assigned thereto in Section 6(a) hereof.

"Post-Change in Control Severance Payment" has the meaning assigned thereto in Section 6 hereof.

"Pre-Change in Control Accrued Obligations" has the meaning assigned thereto in Section 5(a) hereof.

"Pre-Change in Control Severance Payment" has the meaning assigned thereto in Section 5 hereof.

"Principal Location" has the meaning assigned thereto in clause (b)(iii) of the definition of Good Reason, above.

"Proprietary Information" has the meaning assigned thereto in Section 13(a) hereof.

"Release" has the meaning assigned thereto in Section 13(d) hereof.

"SERP" has the meaning assigned thereto in Section 6(b) hereof.

"Underpayment" has the meaning assigned thereto in Section 9(b) hereof.

**Section 2.** Sarbanes-Oxley Act of 2002. Notwithstanding anything herein to the contrary, if the Company determines, in its good faith judgment, that any provision of this Agreement is likely to be interpreted as a personal loan prohibited by the Sarbanes-Oxley Act of 2002 and the rules and regulations promulgated thereunder (the "Act"), then such provision shall be modified as necessary or appropriate so as to not violate the Act; and if this cannot be accomplished, then the Company shall use its reasonable efforts to provide the Executive with similar, but lawful, substitute benefit(s) at a cost to the Company not to significantly exceed the amount the Company would have otherwise paid to provide such benefit(s) to the Executive. In addition, if the

Executive is required to forfeit or to make any repayment of any compensation or benefit(s) to the Company under the Act or any other law, such forfeiture or repayment shall not constitute Good Reason.

### **Section 3. Notice and Date of Termination**

- a. Any termination of the Executive's employment by the Company or by the Executive shall be communicated by a written notice of termination to the other party (the "Notice of Termination"). Where applicable, the Notice of Termination shall indicate the specific termination provision in this Agreement relied upon and shall set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of the Executive's employment under the provision so indicated. Unless the Board determines otherwise, a Notice of Termination by the Executive alleging a termination for Good Reason must be made within 180 days of the act or failure to act that the Executive alleges to constitute Good Reason.
- b. The date of the Executive's termination of employment with the Company (the "Date of Termination") shall be determined as follows: (i) if the Executive's employment is terminated by the Company, either with or without Cause, the Date of Termination shall be the date specified in the Notice of Termination (which, in the case of a termination by the Company other than for Cause, shall not be less than two (2) weeks from the date such Notice of Termination is given unless the Company elects to pay the Executive, in addition to any other amounts payable hereunder, an amount equal to two (2) weeks of the Executive's Annual Base Salary in effect on the Date of Termination), and (ii) if the basis for the Executive's Involuntary Termination is his resignation for Good Reason, the Date of Termination shall be determined by the Company, but shall not in any event be less than fifteen (15) days nor more than sixty (60) days from the date such Notice of Termination is given.

**Section 4. Termination from the Board.** Upon the termination of the Executive's employment for any reason, the Executive's membership on the Board, the board of directors of any of the Company's Affiliates, any committees of the Board and any committees of the board of directors of any of the Company's Affiliates, if applicable, shall be automatically terminated.

### **Section 5. Severance Benefits upon Involuntary Termination Prior to Change in Control**

Except as provided in Section 6 and Section 17(i) hereof, in the event of the Involuntary Termination of the Executive prior to a Change in Control, the Company shall pay the Executive, in one lump sum cash payment as soon as practicable following such Involuntary Termination, (A) the full amount of any earned but unpaid Annual Base Salary through the Date of Termination at the rate in effect on such date, plus (B) an amount (the "Pre-Change in Control Severance Payment") equal to **[one-half (1/2) or one (1)]** times the sum of (X) the Executive's Annual Base Salary as in effect on the Date of Termination and (Y) the greater of his average annual bonus payment for the two (2) years immediately preceding the Date of Termination or the average of his target bonuses for the two (2) years immediately preceding the Date of Termination. In addition to the Pre-Change in Control Severance Payment, the Executive shall be entitled to the following additional benefits:

- a. Accrued Obligations. The Company shall pay the Executive a lump sum amount in cash equal to the sum of (A) the Executive's Annual Base Salary through the Date of Termination to the extent not theretofore paid, (B) an amount equal to any annual Incentive Compensation Awards earned with respect to fiscal years ended prior to the year that includes the Date of Termination to the extent not theretofore paid, (C) any accrued and unpaid vacation, if any, and (D) reimbursement for unreimbursed business expenses, if any, properly incurred by the Executive in the performance of his duties in accordance with policies established from time to time by the Board. (The amounts specified in clauses (A), (B), (C) and (D) shall be hereinafter referred to as the "Pre-Change in Control Accrued Obligations").
- b. Equity-Based Compensation. The Executive shall retain all rights to any equity-based compensation awards to the extent set forth in the applicable plan and/or award agreement.
- c. Welfare Benefits. Subject to Section 11 below, for a period of **[six (6) or twelve (12) months]** following the Date of Termination (and an additional **[six (6) or twelve (12) months]** if the Executive provides consulting services under Section 13(e) hereof), the Executive and his dependents shall be provided with health insurance benefits substantially similar to those provided to the Executive and his dependents immediately prior to the Date of Termination; provided, however, that such benefits shall be provided on substantially the same terms and conditions and at the same cost to the Executive as in effect immediately prior to the Date of Termination.
- d. Outplacement Services. The Executive shall receive outplacement services suitable to his position for a period of **[twelve (12), eighteen (18) or twenty-four (24) months]** following the Date of Termination, in the aggregate amount not to exceed \$50,000. Notwithstanding the foregoing, the Executive shall cease to receive outplacement services on the date the Executive accepts employment with a subsequent employer.
- e. Financial Planning Services. The Executive shall receive financial planning services for a period of **[twelve (12), eighteen (18) or twenty-four (24) months]** following the Date of Termination, at a level consistent with the benefits provided under the Company's financial planning program for the Executive as in effect immediately prior to the Date of Termination.
- f. Deferral of Payments. The Executive shall have the right to elect to defer any lump sum payments received by the Executive pursuant to this Section 5 under the terms and conditions of the Company's nonqualified deferred compensation plan.

### **Section 6. Severance Benefits upon Involuntary Termination in Connection with and after Change in Control**

Notwithstanding the provisions of Section 5 above, in the event of the Involuntary Termination of the Executive within two (2) years following a Change in Control, in lieu of the payments described in Section 5 above, the Company shall pay the Executive, in one lump sum cash payment as soon as practicable following such Involuntary Termination, (A) the full amount of any earned but unpaid Annual Base Salary through the Date of Termination at the rate in effect on such date, plus (B) an amount (the "Post-Change in Control Severance Payment") equal to **[one (1) or two (2)]** times the sum of (X) the Executive's Annual Base Salary as in effect immediately prior to the Change in Control or the Date of Termination, whichever is greater, and (Y) the greater of his average annual bonus payment for the two (2) years immediately preceding the Date of Termination or the average of his target bonuses for the two (2) years immediately preceding the Date of Termination. In addition to the Post-Change in Control Severance Payment, the Executive shall be entitled to the following additional benefits:

- a. Accrued Obligations. The Company shall pay the Executive a lump sum amount in cash equal to the sum of (A) the Executive's Annual Base Salary through the Date of Termination to the extent not theretofore paid, (B) an amount equal to any annual Incentive Compensation Awards earned with respect to fiscal years ended prior to the year that includes the Date of Termination to the extent not theretofore paid, (C) any accrued and unpaid vacation, if any, (D) reimbursement for unreimbursed business expenses, if any, properly incurred by the Executive in the performance of his duties in accordance with policies established from time to time by the Board, and (E) an amount equal to the target amount payable under any annual Incentive Compensation Awards for the fiscal year that includes the Date of Termination or, if greater, the average of the three (3) years' highest gross annual bonus awards, not necessarily consecutive, paid by the Company (or its predecessor) to the Executive under the Company's Executive Incentive Plan (or any predecessor or successor plan) in the five (5) years preceding the year of Termination multiplied by a fraction the numerator of which shall be the number of days from the beginning of such fiscal year to and including the Date of Termination and the denominator of which shall be 365, in each case to the extent not theretofore paid. (The amounts specified in clauses (A), (B), (C), (D) and (E) shall be hereinafter referred to as the "Post-Change in Control Accrued Obligations").
- b. Pension Supplement. The Executive shall receive a lump sum cash payment representing the present value as of the Date of Termination of his or her Supplemental Retirement Plan ("SERP") benefits [if eligible], to be calculated as if the Executive had reached age 62 (or his or her actual age if older), and applying either the applicable early retirement factors under the Company's tax-qualified retirement plan, if the Executive is less than age 62 but at least age 55, or actuarially determined early retirement factors if the Executive is less than age 55 and the applicable lump-sum factors under the Company's tax-qualified retirement plan; and the Executive's termination shall be a "Qualifying Termination" as defined in the Split Dollar Life Insurance Agreement, if any, entered into between the Executive and the Company.]
- c. Equity-Based Compensation. Notwithstanding the provisions of any applicable equity-compensation plan or award agreement to the contrary, all equity-based Incentive Compensation Awards (including, without limitation, stock options, stock appreciation rights, restricted stock awards, restricted stock units, performance share awards, awards covered under Section 162(m) of the Code, and dividend equivalents) held by the Executive shall immediately vest and become exercisable or payable, as the case may be, as of the Date of Termination, to be exercised or paid, as the case may be, in accordance with the terms of the applicable Incentive Compensation Plan and Incentive Compensation Award agreement, and any restrictions on any such Incentive Compensation Awards shall automatically lapse; provided, however, that any such awards granted on or after June 26, 1998 shall remain outstanding and exercisable until the earlier of (A) the later of eighteen (18) months following the Date of Termination or the period specified in the applicable Incentive Compensation Award agreements or (B) the expiration of the original term of such Incentive Compensation Award (it being understood that all Incentive Compensation Awards granted prior to or after June 26, 1998 shall remain outstanding and exercisable for a period that is no less than that provided for in the applicable agreement in effect as of the date of grant).
- d. Welfare Benefits. Subject to Section 11 below, for a period of **[six (6), twelve (12) or twenty-four (24)]** months following the Date of Termination (and an additional twelve (12) months if the Executive provides consulting services under Section 13(e) hereof), the Executive and his dependents shall be provided with life, disability, accident and health insurance benefits substantially similar to those provided to the Executive and his dependents immediately prior to the Date of Termination or the Change in Control Date, whichever is more favorable to the Executive; provided, however, that such benefits shall be provided on substantially the same terms and conditions and at the same cost to the Executive as in effect immediately prior to the Date of Termination or the Change in Control Date, whichever is more favorable to the Executive.
- e. Outplacement Services. The Executive shall receive outplacement services suitable to his position for a period of **[eighteen (18), twenty-four (24) or thirty-six (36)]** months following the Date of Termination, in the aggregate amount not to exceed \$50,000. Notwithstanding the foregoing, the Executive shall cease to receive outplacement services on the date the Executive accepts employment with a subsequent employer.
- f. Financial Planning Services. The Executive shall receive financial planning services for a period of **[eighteen (18), twenty-four (24) or thirty-six (36)]** months following the Date of Termination, at a level consistent with the benefits provided under the Company's financial planning program for the Executive as in effect immediately prior to the Date of Termination.
- g. Deferral of Payments. The Executive shall have the right to elect to defer any lump sum payments received by the Executive pursuant to this Section 6 under the terms and conditions of the Company's nonqualified deferred compensation plan.

Notwithstanding anything contained herein, if a Change in Control occurs and the Executive's employment with the Company is terminated by reason of an Involuntary Termination prior to the Change in Control Date, and if such termination of employment (i) was at the request of a third party who has taken steps reasonably calculated to effect the Change in Control or (ii) otherwise arose in connection with or in anticipation of the Change in Control, then the Executive shall, in lieu of the payments described in Section 5 hereof, be entitled

to the Post-Change in Control Severance Payment and the additional benefits described in this Section 6 as if such Involuntary Termination had occurred within two (2) years following the Change in Control.

**Section 7.** Severance Benefits upon Termination by the Company for Cause or by the Executive Other than for Good Reason. If the Executive's employment shall be terminated for Cause, or if the Executive terminates employment other than for Good Reason, the Company shall have no further obligations to the Executive under this Agreement other than the Pre-Change in Control Accrued Obligations and any amounts or benefits described in Section 10 hereof.

**Section 8.** Severance Benefits upon Termination due to Death or Disability. If the Executive's employment shall terminate by reason of death or Disability, the Company shall pay the Executive or his estate, as the case may be, the Post-Change in Control Accrued Obligations and any amounts or benefits described in Section 10 hereof. Such payments shall be in addition to those rights and benefits to which the Executive or his estate may be entitled under the relevant Company plans or programs.

**Section 9.** Certain Additional Payments by the Company.

- a. Anything in this Agreement to the contrary notwithstanding and except as set forth below, in the event it shall be determined that any payment or distribution in the nature of compensation (within the meaning of Section 280G(b)(2) of the Code) to or for the benefit of the Executive, whether paid or payable pursuant to this Agreement or otherwise (the "Payment") would be subject in its whole or in part to the excise tax imposed by Section 4999 of the Code, together with any interest or penalties imposed with respect to such excise tax (collectively, the "Excise Tax"), then the Executive shall be entitled to receive an additional payment (the "Gross-Up Payment") in an amount such that, after payment by the Executive of all taxes (and any interest or penalties imposed with respect to such taxes), including, without limitation, any income taxes (and any interest and penalties imposed with respect thereto) and Excise Tax imposed upon the Gross-Up Payment, the Executive retains an amount of the Gross-Up Payment equal to the Excise Tax imposed upon the Payment. The Company's obligation to make Gross-Up Payments under this Section 9 shall not be conditioned upon the Executive's termination of employment. For purposes of determining the amount of any Gross-Up Payment, the Executive shall be deemed to pay federal income tax at the highest marginal rate of federal income taxation in the calendar year in which the Gross-Up Payment is to be made and state and local income taxes at the highest marginal rate of taxation in the state and locality of the Executive's residence on the date on which the Gross-Up Payment is calculated for purposes of this Section 9, net of the maximum reduction in federal income taxes which could be obtained from deduction of such state and local taxes, and taking into consideration the phase-out of the Executive's itemized deductions under federal income tax law.
- b. Subject to the provisions of Section 9(c) below, all determinations required to be made under this Section 9, including whether and when a Gross-Up Payment is required, the amount of such Gross-Up Payment and the assumptions to be utilized in arriving at such determination, shall be made by a nationally recognized accounting firm as may be agreed by the Company and the Executive (the "Accounting Firm"); provided, that the Accounting Firm's determination shall be made based upon "substantial authority" within the meaning of Section 6662 of the Code. The Accounting Firm shall provide detailed supporting calculations to both the Company and the Executive within fifteen (15) business days of the receipt of notice from the Executive that there has been a Payment or such earlier time as is requested by the Company. All fees and expenses of the Accounting Firm shall be borne solely by the Company. Any Gross-Up Payment, as determined pursuant to this Section 9, shall be paid by the Company to the Executive within five (5) days of the receipt of the Accounting Firm's determination. Any determination by the Accounting Firm shall be binding upon the Company and the Executive. As a result of the uncertainty in the application of Section 4999 of the Code at the time of the initial determination by the Accounting Firm hereunder, it is possible that Gross-Up Payments that will not have been made by the Company should have been made (the "Underpayment"), consistent with the calculations required to be made hereunder. In the event the Company exhausts its remedies pursuant to Section 9(c) below and the Executive thereafter is required to make a payment of any Excise Tax, the Accounting Firm shall determine the amount of the Underpayment that has occurred, and any such Underpayment shall be promptly paid by the Company to or for the benefit of the Executive.
- c. The Executive shall notify the Company in writing of any claim by the Internal Revenue Service that, if successful, would require the payment by the Company of the Gross-Up Payment. Such notification shall be given as soon as practicable, but no later than ten (10) business days after the Executive is informed in writing of such claim. The Executive shall apprise the Company of the nature of such claim and the date on which such claim is requested to be paid. The Executive shall not pay such claim prior to the expiration of the thirty (30) day period following the date on which the Executive gives such notice to the Company (or such shorter period ending on the date that any payment of taxes with respect to such claim is due). If the Company notifies the Executive in writing prior to the expiration of such period that the Company desires to contest such claim, the Executive shall:
- give the Company any information reasonably requested by the Company relating to such claim,
  - take such action in connection with contesting such claim as the Company shall reasonably request in writing from time to time, including, without limitation, accepting legal representation with respect to such claim by an attorney reasonably selected by the Company,
  - cooperate with the Company in good faith in order effectively to contest such claim, and
  - permit the Company to participate in any proceedings relating to such claim;

provided, however, that the Company shall bear and pay directly all costs and expenses (including additional interest and penalties) incurred in connection with such contest, and shall indemnify and hold the Executive harmless, on an after-tax basis, for any Excise Tax, income tax or any other taxes (including interest and penalties) imposed as a result of such representation and payment of costs and expenses. Without limitation on the foregoing provisions of this Section 9(c), the Company shall control all proceedings taken in connection with such contest, and, at its sole discretion, may pursue or forgo any and all administrative appeals, proceedings, hearings and conferences with the applicable taxing authority in respect of such claim and may, at its sole discretion, either direct the Executive to pay the tax claimed and sue for a refund or contest the claim in any permissible manner, and the Executive agrees to prosecute such contest to a determination before any administrative tribunal, in a court of initial jurisdiction and in one or more appellate courts, as the Company shall determine; provided, however, that if the Company directs the Executive to pay such claim and sue for a refund, the Company shall advance the amount of such payment to the Executive, on an interest-free basis, and shall indemnify and hold the Executive harmless, on an after-tax basis, from any Excise Tax, income tax or any other taxes (including interest or penalties) imposed with respect to such advance or with respect to any imputed income in connection with such advance; and provided, further, that any extension of the statute of limitations relating to payment of taxes for the taxable year of the Executive with respect to which such contested amount is claimed to be due is limited solely to such contested amount. Furthermore, the Company's control of the contest shall be limited to issues with respect to which the Gross-Up Payment would be payable hereunder; and the Executive shall be entitled to settle or contest, as the case may be, any other issue raised by the Internal Revenue Service or any other taxing authority.

- d. If, after the receipt by the Executive of a Gross-Up Payment or an amount advanced by the Company pursuant to Section 9(c) above, the Executive becomes entitled to receive any refund with respect to the Excise Tax to which such Gross-Up Payment relates or with respect to such claim, the Executive shall (subject to the Company's complying with the requirements of Section 9(c) above, if applicable) promptly pay to the Company the amount of such refund (together with any interest paid or credited thereon after taxes applicable thereto). If, after the receipt by the Executive of an amount advanced by the Company pursuant to Section 9(c) above, a determination is made that the Executive shall not be entitled to any refund with respect to such claim and the Company does not notify the Executive in writing of its intent to contest such denial of refund prior to the expiration of thirty (30) days after such determination, then such advance shall be forgiven and shall not be required to be repaid, and the amount of such advance shall offset, to the extent thereof, the amount of Gross-Up Payment required to be paid.
- e. Notwithstanding any other provision of this Section 9, the Company may, in its sole discretion, withhold and pay over to the Internal Revenue Service or any other applicable taxing authority, for the benefit of the Executive, all or any portion of any Gross-Up Payment, and the Executive hereby consents to such withholding. If such payment is made by the Company to the Internal Revenue Service or other applicable taxing authority, then the Executive shall not be entitled to payment pursuant to Section 9(b) above.
- f. Any other liability for unpaid or withheld Excise Taxes shall be borne exclusively by the Company, in accordance with Section 3403 of the Code. The foregoing sentence shall not in any manner relieve the Company of any of its obligations under this Agreement.

**Section 10.** Nonexclusivity of Rights. Nothing in this Agreement shall prevent or limit the Executive's continuing or future participation in any benefit, plan, program, policy or practice provided by the Company and for which the Executive may qualify (except with respect to any benefit to which the Executive has waived his rights in writing), including, without limitation, any and all indemnification arrangements in favor of the Executive (whether under agreements or under the Company's charter documents or otherwise), and insurance policies covering the Executive, nor shall anything herein limit or otherwise affect such rights as the Executive may have under any other contract or agreement entered into after the Effective Date with the Company. Amounts which are vested benefits or which the Executive is otherwise entitled to receive under any benefit, plan, policy, practice or program of, or any contract or agreement entered into with, the Company shall be payable in accordance with such benefit, plan, policy, practice or program or contract or agreement except as explicitly modified by this Agreement. At all times during the Executive's employment with the Company and thereafter, the Company shall provide the Executive with indemnification and D&O insurance insuring the Executive against insurable events which occur or have occurred while the Executive was a director or executive officer of the Company, on terms and conditions that are at least as generous as that then provided to any other current or former director or executive officer of the Company or any Affiliate.

**Section 11.** Full Settlement; Mitigation. The Company's obligation to make the payments provided for in this Agreement and otherwise to perform its obligations hereunder shall not be affected by any set-off, counterclaim, recoupment, defense or other claim, right or action which the Company may have against the Executive or others, provided that nothing herein shall

preclude the Company from separately pursuing recovery from the Executive based on any such claim. In no event shall the Executive be obligated to seek other employment or take any other action by way of mitigation of the amounts (including amounts for damages for breach) payable to the Executive under any of the provisions of this Agreement, and such amounts shall not be reduced whether or not the Executive obtains other employment.

#### **Section 12. Dispute Resolution.**

Any disagreement, dispute, controversy or claim arising out of or relating to this Agreement or the interpretation of this Agreement or any arrangements relating to this Agreement or contemplated in this Agreement or the breach, termination or invalidity thereof shall be settled by final and binding arbitration administered by JAMS in San Diego, California in accordance with the then existing JAMS arbitration rules applicable to employment disputes (the "JAMS Rules"); provided that, notwithstanding any provision in such rules to the contrary, in all cases the parties shall be entitled to reasonable discovery. In the event of such an arbitration proceeding, the Executive and the Company shall select a mutually acceptable neutral arbitrator from among the JAMS panel of arbitrators. In the event the Executive and the Company cannot agree on an arbitrator, the arbitrator shall be selected in accordance with the then existing JAMS Rules. Neither the Executive nor the Company nor the arbitrator shall disclose the existence, content or results of any arbitration hereunder without the prior written consent of all parties, except to the extent necessary to enforce any arbitration award in a court of competent jurisdiction. Except as provided herein, the Federal Arbitration Act shall govern the interpretation of, enforcement of and all proceedings under this agreement to arbitrate. The arbitrator shall apply the substantive law (and the law of remedies, if applicable) of the state of California, or federal law, or both, as applicable, and the arbitrator is without jurisdiction to apply any different substantive law. The arbitrator shall have the authority to entertain a motion to dismiss and/or a motion for summary judgment by any party and shall apply the standards governing such motions under the Federal Rules of Civil Procedure. The arbitrator shall render an award and a written, reasoned opinion in support thereof. Judgment upon the award may be entered in any court having jurisdiction thereof. The Executive shall not be required to pay any arbitration fee or cost that is unique to arbitration or greater than any amount he would be required to pay to pursue his claims in a court of competent jurisdiction.

#### **Section 13. Executive's Covenants.**

- a. **Confidentiality.** The Executive acknowledges that in the course of his employment with the Company, he has acquired non-public privileged or confidential information and trade secrets concerning the operations, future plans and methods of doing business ("Proprietary Information") of the Company and its Affiliates; and the Executive agrees that it would be extremely damaging to the Company and its Affiliates if such Proprietary Information were disclosed to a competitor of the Company and its Affiliates or to any other person or corporation. The Executive understands and agrees that all Proprietary Information has been divulged to the Executive in confidence and further understands and agrees to keep all Proprietary Information secret and confidential (except for such information which is or becomes publicly available other than as a result of a breach by the Executive of this provision or information the Executive is required by any governmental, administrative or court order to disclose) without limitation in time. In view of the nature of the Executive's employment and the Proprietary Information the Executive has acquired during the course of such employment, the Executive likewise agrees that the Company and its Affiliates would be irreparably harmed by any disclosure of Proprietary Information in violation of the terms of this paragraph and that the Company and its Affiliates shall therefore be entitled to preliminary and/or permanent injunctive relief prohibiting the Executive from engaging in any activity or threatened activity in violation of the terms of this paragraph and to any other relief available to them. Inquiries regarding whether specific information constitutes Proprietary Information shall be directed to the Company's Senior Vice President, Public Policy (or, if such position is vacant, the Company's then Chief Executive Officer); provided, that the Company shall not unreasonably classify information as Proprietary Information.
- b. **Non-Solicitation of Employees.** The Executive recognizes that he possesses and will possess confidential information about other employees of the Company and its Affiliates relating to their education, experience, skills, abilities, compensation and benefits, and inter-personal relationships with customers of the Company and its Affiliates. The Executive recognizes that the information he possesses and will possess about these other employees is not generally known, is of substantial value to the Company and its Affiliates in developing their business and in securing and retaining customers, and has been and will be acquired by him because of his business position with the Company and its Affiliates. The Executive agrees that at all times during the Executive's employment with the Company and for a period of one (1) year thereafter, he will not, directly or indirectly, solicit or recruit any employee of the Company or its Affiliates for the purpose of being employed by him or by any competitor of the Company or its Affiliates on whose behalf he is acting as an agent, representative or employee and that he will not convey any such confidential information or trade secrets about other employees of the Company and its Affiliates to any other person; provided, however, that it shall not constitute a solicitation or recruitment of employment in violation of this paragraph to discuss employment opportunities with any employee of the Company or its Affiliates who has either first contacted the Executive or regarding whose employment the Executive has discussed with and received the written approval of the Company's Vice President, Human Resources (or, if such position is vacant, the Company's then Chief Executive Officer), prior to making such solicitation or recruitment. In view of the nature of the Executive's employment with the Company, the Executive likewise agrees that the Company and its Affiliates would be irreparably harmed by any solicitation or recruitment in violation of the terms of this paragraph and that the Company and its Affiliates shall therefore be entitled to preliminary and/or permanent injunctive relief prohibiting the Executive from engaging in any activity or threatened activity in violation of the terms of this paragraph and to any other relief available to them.
- c. **Survival of Provisions.** The obligations contained in Section 13(a) and Section 13(b) above shall survive the termination of the Executive's employment within the Company and shall be fully enforceable thereafter. If it is determined by a court of competent jurisdiction in any state that any restriction in Section 13(a) or Section 13(b) above is excessive in duration or scope or is unreasonable or unenforceable under the laws of that state, it is the intention of the parties that such restriction may be modified or amended by the court to render it enforceable to the maximum extent permitted by the law of that state.
- d. **Release; Lump Sum Payment.** In the event the Executive's employment is terminated by the Company other than for Cause, death or Disability or the Executive shall terminate his employment for Good Reason, if the Executive agrees (i) to the covenants described in Section 13(a) and Section 13(b) above, (ii) to execute a release (the "Release") of all claims substantially in the form attached hereto as Exhibit A within forty-five (45) days after the applicable Date of Termination and does not revoke such release in accordance with the terms thereof, and (iii) to provide the consulting services described in Section 13(e) below, then in consideration for such covenants, the Company shall pay the Executive a lump sum amount in cash equal to **[one-half (1/2) or one (1) times]** the sum of (A) the Executive's Annual Base Salary and (B) the greater of the Executive's target bonus for the year of termination under the Company's Executive Incentive Plan (or any successor plan) or the average of the two (2) years' highest gross annual bonus awards, not necessarily consecutive, paid by the Company (or its predecessor) to the Executive under the Company's Executive Incentive Plan (or any predecessor or successor plan) in the five (5) years preceding the year of termination. The amount specified in this Section 13(d) shall be paid as soon as practicable following the Executive's execution of the Release, and the Executive shall have the right to elect to defer such payment under the terms and conditions of the Company's nonqualified deferred compensation plan.
- e. **Consulting.** If the Executive agrees to the covenants described in Section 13(d) above, then the Executive shall have the obligation to provide consulting services to the Company as an independent contractor, commencing on the Date of Termination and ending on the **[first or second]** anniversary of the Date of Termination (the "Consulting Period"). The Executive shall hold himself available at reasonable times and on reasonable notice to render such consulting services as may be so assigned to him by the Board or the Company's then Chief Executive Officer; provided, however, that unless the parties otherwise agree, the consulting services rendered by the Executive during the Consulting Period shall not exceed twenty (20) hours each month. The Company agrees to use its best efforts during the Consulting Period to secure the benefit of the Executive's consulting services so as to minimize the interference with the Executive's other activities, including requiring the performance of consulting services at the Company's offices only when such services may not be reasonably performed off-site by the Executive.

**Section 14. Legal Fees.** In the event of the termination of the Executive's employment within two (2) years following a Change in Control, the Company shall pay to the Executive all legal fees and expenses (including but not limited to fees and expenses in connection with any arbitration) incurred by the Executive in disputing in good faith any issue arising under this Agreement relating to the termination of the Executive's employment or in seeking in good faith to obtain or enforce any benefit or right provided by this Agreement, but in each case only to the extent the arbitrator or court determines that the Executive had a reasonable basis for such claim. Notwithstanding the foregoing, in the event of the termination of the Executive's employment prior to a Change in Control, the Executive, if he is the prevailing party, shall be entitled to recover all legal fees and expenses incurred in disputing in good faith any issue arising under this Agreement.

#### **Section 15. Successors.**

- a. **Assignment by Executive.** This Agreement is personal to the Executive and without the prior written consent of the Company shall not be assignable by the Executive otherwise than by will or the laws of descent and distribution. This Agreement shall inure to the benefit of and be enforceable by the Executive's legal representatives.
- b. **Successors and Assigns of Company.** This Agreement shall inure to the benefit of and be binding upon the Company, its successors and assigns. The Company may not assign this Agreement to any person or entity (except for a successor described in Section 15(c) below) without the Executive's written consent.
- c. **Assumption.** The Company shall require any successor (whether direct or indirect, by purchase, merger, consolidation or otherwise) to all or substantially all of the business and/or assets of the Company to assume expressly and agree to perform this Agreement in the same manner and to the same extent that the Company would be required to perform it if no such succession had taken place. As used in this Agreement, "Company" shall mean the Company as hereinbefore defined and any successor to its businesses and/or assets as aforesaid that assumes and agrees to perform this Agreement by operation of law or otherwise.

**Section 16. Administration Prior to Change in Control.** Prior to a Change in Control, the Compensation Committee shall have full and complete authority to construe and interpret the provisions of this Agreement, to determine an individual's entitlement to benefits under this Agreement, to make in its sole and absolute discretion all determinations contemplated under this Agreement, to investigate and make factual determinations necessary or advisable to administer or implement this Agreement, and to adopt such rules and procedures as it deems necessary or advisable for the administration or implementation of this Agreement. All



determinations made under this Agreement by the Compensation Committee shall be final and binding on all interested persons. Prior to a Change in Control, the Compensation Committee may delegate responsibilities for the operation and administration of this Agreement to one or more officers or employees of the Company. The provisions of this Section 16 shall terminate and be of no further force and effect upon the occurrence of a Change in Control.

**Section 17. Miscellaneous.**

- a. **Governing Law.** This Agreement shall be governed by and construed in accordance with the laws of the State of California, without reference to its principles of conflict of laws. The captions of this Agreement are not part of the provisions hereof and shall have no force or effect. This Agreement may not be amended, modified, repealed, waived, extended or discharged except by an agreement in writing signed by the party against whom enforcement of such amendment, modification, repeal, waiver, extension or discharge is sought. No person, other than pursuant to a resolution of the Board or a committee thereof, shall have authority on behalf of the Company to agree to amend, modify, repeal, waive, extend or discharge any provision of this Agreement or anything in reference thereto.
- b. **Notices.** All notices and other communications hereunder shall be in writing and shall be given by hand delivery to the other party or by registered or certified mail, return receipt requested, postage prepaid, addressed, in either case, to the Company's headquarters or to such other address as either party shall have furnished to the other in writing in accordance herewith. Notices and communications shall be effective when actually received by the addressee.
- c. **Severability.** The invalidity or unenforceability of any provision of this Agreement shall not affect the validity or enforceability of any other provision of this Agreement.
- d. **Taxes.** The Company may withhold from any amounts payable under this Agreement such federal, state or local taxes as shall be required to be withheld pursuant to any applicable law or regulation.
- e. **No Waiver.** The Executive's or the Company's failure to insist upon strict compliance with any provision hereof or any other provision of this Agreement or the failure to assert any right the Executive or the Company may have hereunder, including, without limitation, the right of the Executive to terminate employment for Good Reason pursuant to Section 1 hereof, or the right of the Company to terminate the Executive's employment for Cause pursuant to Section 1 hereof shall not be deemed to be a waiver of such provision or right or any other provision or right of this Agreement.
- f. **Entire Agreement; Exclusive Benefit.** This instrument contains the entire agreement of the Executive, the Company or any predecessor or subsidiary thereof with respect to any severance or termination pay. The Pre-Change in Control Severance Payment, the Post-Change in Control Severance Payment and all other benefits provided hereunder shall be in lieu of any other severance payments to which the Executive is entitled under any other severance plan or program or arrangement sponsored by the Company, as well as pursuant to any individual employment or severance agreement that was entered into by the Executive and the Company, and, upon the Effective Date of this Agreement, all such plans, programs, arrangements and agreements are hereby automatically superseded and terminated.
- g. **No Right of Employment.** Nothing in this Agreement shall be construed as giving the Executive any right to be retained in the employ of the Company or shall interfere in any way with the right of the Company to terminate the Executive's employment at any time, with or without Cause.
- h. **Unfunded Obligation.** The obligations under this Agreement shall be unfunded. Benefits payable under this Agreement shall be paid from the general assets of the Company. The Company shall have no obligation to establish any fund or to set aside any assets to provide benefits under this Agreement.
- i. **Termination.** Notwithstanding anything contained herein, this Agreement shall automatically terminate and be of no further force and effect and no benefits shall be payable hereunder in the event that the Company sells or otherwise disposes of any part of the business or assets of the Company (other than such a sale or disposition which is part of a transaction or series of transactions which would result in a Change in Control) and as a result of such transaction, (i) the Executive becomes an employee of the buyer of such business or assets (the "Buyer") or (ii) the Executive is offered employment by the Buyer in an executive position with reasonably comparable status, compensation, benefits and severance agreement and which is consistent with the Executive's experience and education, but the Executive declines to accept such offer.
- j. **Term.** The term of this Agreement shall commence on the Effective Date and shall continue until the third (3rd) anniversary of the Effective Date; provided, however, that commencing on the second (2nd) anniversary of the Effective Date (and each anniversary of the Effective Date thereafter), the term of this Agreement shall automatically be extended for one (1) additional year, unless at least ninety (90) days prior to such date, the Company or the Executive shall give written notice to the other party that it or he, as the case may be, does not wish to so extend this Agreement. Notwithstanding the foregoing, if the Company gives such written notice to the Executive less than two (2) years after a Change in Control, the term of this Agreement shall be automatically extended until the later of (A) the date that is one (1) year after the anniversary of the Effective Date that follows such written notice or (B) the second (2nd) anniversary of the Change in Control Date.
- k. **Counterparts.** This Agreement may be executed in several counterparts, each of which shall be deemed to be an original but all of which together shall constitute one and the same instrument.

l. IN WITNESS WHEREOF, the Executive and, pursuant to due authorization from its Board of Directors, the Company have caused this Agreement to be executed as of the day and year first above written.

SEMPRA ENERGY

\_\_\_\_\_  
G. Joyce Rowland  
Senior Vice President, Human Resources

\_\_\_\_\_  
Date

EXECUTIVE

\_\_\_\_\_  
[ ]

\_\_\_\_\_  
Date

EXHIBIT A

**GENERAL RELEASE**

This GENERAL RELEASE (the "Agreement"), dated \_\_\_\_\_, is made by and between \_\_\_\_\_, a California corporation (the "Company") and \_\_\_\_\_ ("you" or "your").

WHEREAS, you and the Company have previously entered into that certain Severance Pay Agreement dated \_\_\_\_\_, 2006 (the "Severance Pay Agreement"); and

WHEREAS, Section 13(d) of the Severance Pay Agreement provides for the payment of a benefit to you by the Company in consideration for certain covenants, including your execution and non-revocation of a general release of claims by you against the Company and its subsidiaries and affiliates.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained, you and the Company hereby agree as follows:

ONE: Your signing of this Agreement confirms that your employment with the Company shall terminate at the close of business on \_\_\_\_\_, or earlier upon our mutual agreement.

TWO: As a material inducement for the payment of the benefit under Section 13 of that certain Severance Pay Agreement between you and the Company, and except as otherwise provided in this Agreement, you and the Company hereby irrevocably and unconditionally release, acquit and forever discharge the other from any and all Claims either may have against the other. For purposes of this Agreement and the preceding sentence, the words "Releasee" or "Releasees" and "Claim" or "Claims" shall have the meanings set forth below:

(a) The words "Releasee" or "Releasees" shall refer to you and to the Company and each of the Company's owners, stockholders, predecessors, successors, assigns, agents, directors, officers, employees, representatives, attorneys, advisors, parent companies, divisions, subsidiaries, affiliates (and agents, directors, officers, employees, representatives, attorneys and advisors of such parent companies, divisions, subsidiaries and affiliates) and all persons acting by, through, under or in concert with any of them.

(b) The words "Claim" or "Claims" shall refer to any charges, complaints, claims, liabilities, obligations, promises, agreements, controversies, damages, actions, causes of action, suits, rights, demands, costs, losses, debts and expenses (including attorneys' fees and costs actually incurred) of any nature whatsoever, known or unknown, suspected or unsuspected, which you or the Company now, in the past or, except as limited by law or regulation such as the Age Discrimination in Employment Act (ADEA), in the future may have, own or hold against any of the Releasees; provided, however, that the word "Claim" or "Claims" shall not refer to any charges, complaints, claims, liabilities, obligations, promises, agreements, controversies, damages, actions, causes of action, suits,

rights, demands, costs, losses, debts and expenses (including attorneys' fees and costs actually incurred) arising under [identify severance, employee benefits, stock option, indemnification and D&O and other agreements containing duties, rights obligations etc. of either party that are to remain operative]. Claims released pursuant to this Agreement by you and the Company include, but are not limited to, rights arising out of alleged violations of any contracts, express or implied, any tort, any claim that you failed to perform or negligently performed or breached your duties during employment at the Company, any legal restrictions on the Company's right to terminate employees or any federal, state or other governmental statute, regulation, or ordinance, including, without limitation: (1) Title VII of the Civil Rights Act of 1964 (race, color, religion, sex and national origin discrimination); (2) 42 U.S.C. Section 1981 (discrimination); (3) 29 U.S.C. Section 621-634 (age discrimination); (4) 29 U.S.C. Section 206(d)(1) (equal pay); (5) 42 U.S.C. Section 12101, et seq. (disability); (6) the California Constitution, Article I, Section 8 (discrimination); (7) the California Fair Employment and Housing Act (discrimination, including race, color, national origin, ancestry, physical handicap, medical condition, marital status, religion, sex or age); (8) California Labor Code Section 1102.1 (sexual orientation discrimination); (9) Executive Order 11246 (race, color, religion, sex and national origin discrimination); (10) Executive Order 11141 (age discrimination); (11) Section 503 and 504 of the Rehabilitation Act of 1973 (handicap discrimination); (12) The Worker Adjustment and Retraining Act (WARN Act); (13) the California Labor Code (wages, hours, working conditions, benefits and other matters); (14) the Fair Labor Standards Act (wages, hours, working conditions and other matters); the Federal Employee Polygraph Protection Act (prohibits employer from requiring employee to take polygraph test as condition of employment); and (15) any federal, state or other governmental statute, regulation or ordinance which is similar to any of the statutes described in clauses (1) through (14).

THREE: You and the Company expressly waive and relinquish all rights and benefits afforded by any statute (including but not limited to Section 1542 of the Civil Code of the State of California) which limits the effect of a release with respect to unknown claims. You and the Company do so understanding and acknowledging the significance of the release of unknown claims and the waiver of statutory protection against a release of unknown claims (including but not limited to Section 1542). Section 1542 of the Civil Code of the State of California states as follows:

"A GENERAL RELEASE DOES NOT EXTEND TO CLAIMS WHICH THE CREDITOR DOES NOT KNOW OR SUSPECT TO EXIST IN HIS FAVOR AT THE TIME OF EXECUTING THE RELEASE, WHICH IF KNOWN BY HIM MUST HAVE MATERIALLY AFFECTED HIS SETTLEMENT WITH THE DEBTOR."

Thus, notwithstanding the provisions of Section 1542 or of any similar statute, and for the purpose of implementing a full and complete release and discharge of the Releasees, you and the Company expressly acknowledge that this Agreement is intended to include in its effect, without limitation, all Claims which are known and all Claims which you or the Company do not know or suspect to exist in your or the Company's favor at the time of execution of this Agreement and that this Agreement contemplates the extinguishment of all such Claims.

FOUR: The parties acknowledge that they might hereafter discover facts different from, or in addition to, those they now know or believe to be true with respect to a Claim or Claims released herein, and they expressly agree to assume the risk of possible discovery of additional or different facts, and agree that this Agreement shall be and remain effective, in all respects, regardless of such additional or different discovered facts.

FIVE: You hereby represent and acknowledge that you have not filed any Claim of any kind against the Company or others released in this Agreement. You further hereby expressly agree never to initiate against the Company or others released in this Agreement any administrative proceeding, lawsuit or any other legal or equitable proceeding of any kind asserting any Claims that are released in this Agreement.

The Company hereby represents and acknowledges that it has not filed any Claim of any kind against you or others released in this Agreement. The Company further hereby expressly agrees never to initiate against you or others released in this Agreement any administrative proceeding, lawsuit or any other legal or equitable proceeding of any kind asserting any Claims that are released in this Agreement.

SIX: You hereby represent and agree that you have not assigned or transferred, or attempted to have assigned or transfer, to any person or entity, any of the Claims that you are releasing in this Agreement.

The Company hereby represents and agrees that it has not assigned or transferred, or attempted to have assigned or transfer, to any person or entity, any of the Claims that it is releasing in this Agreement.

SEVEN: As a further material inducement to the Company to enter into this Agreement, you hereby agree to indemnify and hold each of the Releasees harmless from all loss, costs, damages, or expenses, including without limitation, attorneys' fees incurred by the Releasees, arising out of any breach of this Agreement by you or the fact that any representation made in this Agreement by you was false when made.

As a further material inducement to you to enter into this Agreement, the Company hereby agrees to indemnify and hold each of the Releasees harmless from all loss, costs, damages, or expenses, including without limitation, attorneys' fees incurred by the Releasees, arising out of any breach of this Agreement by it or the fact that any representation made in this Agreement by it was knowingly false when made.

EIGHT: You and the Company represent and acknowledge that in executing this Agreement, neither is relying upon any representation or statement not set forth in this Agreement or the Severance Agreement.

NINE:

(a) This Agreement shall not in any way be construed as an admission by the Company that it has acted wrongfully with respect to you or any other person, or that you have any rights whatsoever against the Company, and the Company specifically disclaims any liability to or wrongful acts against you or any other person, on the part of itself, its employees or its agents. This Agreement shall not in any way be construed as an admission by you that you have acted wrongfully with respect to the Company, or that you failed to perform your duties or negligently performed or breached your duties, or that the Company had good cause to terminate your employment.

(b) If you are a party or are threatened to be made a party to any proceeding by reason of the fact that you were an officer or director of the Company, the Company shall indemnify you against any expenses (including reasonable attorneys' fees; provided, that counsel has been approved by the Company prior to retention, which approval shall not be unreasonably withheld), judgments, fines, settlements and other amounts actually or reasonably incurred by you in connection with that proceeding; provided, that you acted in good faith and in a manner you reasonably believed to be in the best interest of the Company. The limitations of California Corporations Code Section 317 shall apply to this assurance of indemnification.

(c) You agree to cooperate with the Company and its designated attorneys, representatives and agents in connection with any actual or threatened judicial, administrative or other legal or equitable proceeding in which the Company is or may become involved. Upon reasonable notice, you agree to meet with and provide to the Company or its designated attorneys, representatives or agents all information and knowledge you have relating to the subject matter of any such proceeding. The Company agrees to reimburse you for any reasonable costs you incur in providing such cooperation.

TEN: This Agreement is made and entered into in California. This Agreement shall in all respects be interpreted, enforced and governed by and under the laws of the State of California and applicable Federal law. Any dispute about the validity, interpretation, effect or alleged violation of this Agreement (an "arbitrable dispute") must be submitted to arbitration in San Diego, California. Arbitration shall take place before an experienced employment arbitrator licensed to practice law in such state and selected in accordance with the then existing JAMS arbitration rules applicable to employment disputes; provided, however, that in any event, the arbitrator shall allow reasonable discovery. Arbitration shall be the exclusive remedy for any arbitrable dispute. The arbitrator in any arbitrable dispute shall not have authority to modify or change the Agreement in any respect. You and the Company shall each be responsible for payment of one-half (1/2) the amount of the arbitrator's fee(s); provided, however, that in no event shall you be required to pay any fee or cost of arbitration that is unique to arbitration or exceeds the costs you would have incurred had any arbitrable dispute been pursued in a court of competent jurisdiction. The Company shall make up any shortfall. Should any party to this Agreement institute any legal action or administrative proceeding against the other with respect to any Claim waived by this Agreement or pursue any arbitrable dispute by any method other than arbitration, the prevailing party shall be entitled to recover from the non-prevailing party all damages, costs, expenses and attorneys' fees incurred as a result of that action. The arbitrator's decision and/or award shall be rendered in writing and will be fully enforceable and subject to an entry of judgment by the Superior Court of the State of California for the County of San Diego, or any other court of competent jurisdiction.

ELEVEN: Both you and the Company understand that this Agreement is final and binding eight (8) days after its execution and return. Should you nevertheless attempt to challenge the enforceability of this Agreement as provided in Paragraph TEN or, in violation of that Paragraph, through litigation, as a further limitation on any right to make such a challenge, you shall initially tender to the Company, by certified check delivered to the Company, all monies received pursuant to Section 13(d) of the Severance Pay Agreement, plus interest, and invite the Company to retain such monies and agree with you to cancel this Agreement and void the Company's obligations under Section 13(d) of the Severance Pay Agreement. In the event the Company accepts this offer, the Company shall retain such monies and this Agreement shall be canceled and the Company shall have no obligation under Section 13(d) of the Severance Pay Agreement. In the event the Company does not accept such offer, the Company shall so notify you and shall place such monies in an interest-bearing escrow account pending resolution of the dispute between you and the Company as to whether or not this Agreement and the Company's obligations under Section 13(d) of the Severance Pay Agreement shall be set aside and/or otherwise rendered voidable or unenforceable. Additionally, any consulting agreement then in effect between you and the Company shall be immediately rescinded with no requirement of notice.

TWELVE: Any notices required to be given under this Agreement shall be delivered either personally or by first class United States mail, postage prepaid, addressed to the respective parties as follows:

To Company: [TO COME]

Attn: [TO COME]

To You: \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

THIRTEEN: You understand and acknowledge that you have been given a period of forty-five (45) days to review and consider this Agreement (as well as statistical data on the persons eligible for similar benefits) before signing it and may use as much of this forty-five (45) day period as you wish prior to signing. You are encouraged, at your personal expense, to consult with an attorney

before signing this Agreement. You understand and acknowledge that whether or not you do so is your decision. You may revoke this Agreement within seven (7) days of signing it. If you wish to revoke, the Company's Vice President, Human Resources must receive written notice from you no later than the close of business on the seventh (7th) day after you have signed the Agreement. If revoked, this Agreement shall not be effective and enforceable, and you will not receive payments or benefits under Section 13(d) of the Severance Pay Agreement.

FOURTEEN: This Agreement constitutes the entire agreement of the parties hereto and supersedes any and all other agreements (except the Severance Pay Agreement) with respect to the subject matter of this Agreement, whether written or oral, between you and the Company. All modifications and amendments to this Agreement must be in writing and signed by the parties.

FIFTEEN: Each party agrees, without further consideration, to sign or cause to be signed, and to deliver to the other party, any other documents and to take any other action as may be necessary to fulfill the obligations under this Agreement.

SIXTEEN: If any provision of this Agreement or the application thereof is held invalid, the invalidity shall not affect other provisions or applications of the Agreement which can be given effect without the invalid provisions or application; and to this end the provisions of this Agreement are declared to be severable.

SEVENTEEN: This Agreement may be executed in counterparts.

I have read the foregoing General Release, and I accept and agree to the provisions it contains and hereby execute it voluntarily and with full understanding of its consequences. I am aware it includes a release of all known or unknown claims.

DATED: \_\_\_\_\_

DATED: \_\_\_\_\_

You acknowledge that you first received this Agreement on [date].

LOAN AGREEMENT

Between

CITY OF CHULA VISTA

And

SAN DIEGO GAS & ELECTRIC COMPANY

Dated as of June 1, 2004

Relating to

City of Chula Vista  
Industrial Development Revenue Refunding Bonds  
(San Diego Gas & Electric Company)  
2004 Series A, B, C, D, E and F

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WITNESSETH:

WHEREAS, the City is a municipal corporation and charter city, duly organized and existing under a freeholders' charter pursuant to which the City has the right and power to make and enforce all laws and regulations in accordance with and as more particularly provided in Sections 3, 5 and 7 of Article XI of the Constitution of the State of California and Section 200 of the Charter of the City (the "Charter"); and

WHEREAS, the City Council of the City, acting under and pursuant to the powers reserved to the City under Sections 3, 5 and 7 of Article XI of the Constitution and Section 200 of the Charter, has enacted Chapter 3.48 of the Chula Vista Municipal Code, pursuant to Ordinance No. 1970 adopted on February 9, 1982, as amended from time to time (the "Law"), establishing a program to provide financial assistance for the acquisition, construction and installation of facilities for industrial, commercial or public utility purposes; and

WHEREAS, the Borrower has duly applied to the City for financial assistance to refinance the costs of acquisition, construction and installation of certain facilities for the generation, transmission and distribution of electric energy, as more fully described in Exhibit A hereto (the "Projects"), by prepaying certain loans (collectively, the "Prior Loans") made to the Borrower with the proceeds of The City of San Diego Industrial Development Revenue Refunding Bonds (San Diego Gas, & Electric Company) 1992 Series A (the "SD 1992 Bonds"), The City of San Diego Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 1995 Series A and 1995 Series B (the "SD 1995 Bonds") and The City of Chula Vista Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 1992 Series A (the "CV 1992 Bonds" and, together with the SD 1992 Bonds and SD 1995 Bonds, the "Prior Bonds"), resulting in the refunding of the Prior Bonds; and

WHEREAS, the City after due investigation and deliberation has determined that the Projects and the refinancing thereof, and the resulting refunding of the Prior Bonds, will directly benefit the citizens of the City by substantially promoting the public interests recited in the Law and has adopted its resolutions authorizing the provision or lending of financial assistance to the Borrower to refinance the costs of acquisition, construction and installation of the Projects and to prepay the Prior Loans, and the issuance and sale of its bonds, including its Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 2004 Series A, 2004 Series B, 2004 Series C, 2004 Series D, 2004 Series E and 2004 Series F (collectively, the "Bonds"), for such purposes; and

WHEREAS, the City proposes to assist in such refinancing upon the terms and conditions set forth herein;

NOW, THEREFORE, in consideration of the premises and the respective representations and covenants herein contained, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

**SECTION 1.1 DEFINITION OF TERMS.** Unless the context otherwise requires, the terms used in this Agreement shall have the meanings specified in Section 1.01 of the Indenture of Trust, of even date herewith relating to the Bonds (the "Indenture"), by and between the City and U.S. Bank National Association, as trustee (the "Trustee"), as originally executed or as it may from time to time be supplemented or amended as provided therein, and including the Multi-Mode Annex attached thereto.

**SECTION 1.2 NUMBER AND GENDER.** The singular form of any word used herein, including the terms defined in Section 1.01 of the Indenture, shall include the plural, and vice versa. The use herein of a word of any gender shall include all genders.

**SECTION 1.3 ARTICLES, SECTIONS, ETC.** Unless otherwise specified, references to Articles, Sections and other subdivisions of this Agreement are to the designated Articles, Sections and other subdivisions of this Agreement as originally executed. The words "hereof," "herein," "hereunder" and words of similar import refer to this Agreement as a whole. The headings or titles of the several articles and sections, and the table of contents appended to copies hereof, shall be solely for convenience of reference and shall not affect the meaning, construction or effect of the provisions hereof.

ARTICLE II

REPRESENTATIONS

**SECTION 2.1 REPRESENTATIONS OF THE CITY.** The City makes the following representations as the basis for its undertakings herein contained:

- (a) The City is a municipal corporation and charter city in the State of California. Under the provisions of the Law, the City has the power to enter into the transactions contemplated by this Agreement and to carry out its obligations hereunder. The Projects constitute a "project" as that term is defined in the Law. By proper action, the City has been duly authorized to execute, deliver and duly perform this Agreement and the Indenture.
- (b) To refinance the cost of the Projects, the City will issue the Bonds which will mature, bear interest and be subject to redemption as set forth in the Indenture.
- (c) The Bonds will be issued under and secured by the Indenture, pursuant to which the City's interest in this Agreement (except certain rights of the City to give approvals and consents and to receive payment for expenses and indemnification and certain other payments) will be pledged to the Trustee as security for payment of the principal of, premium, if any, and interest on the Bonds.
- (d) The City has not pledged and will not pledge its interest in this Agreement or the First Mortgage Bonds for any purpose other than to secure the Bonds under the Indenture.
- (e) The City is not in default under any of the provisions of the laws of the State of California or the City's Charter which default would affect its existence or its powers referred to in subsection (a) of this Section 2.1.
- (f) The City has found and determined and hereby finds and determines that all requirements of the Law with respect to the issuance of the Bonds and the execution of this Agreement and the Indenture have been complied with and that refinancing the Projects by issuing the Bonds, refunding or replacing the Prior Bonds and entering into this Agreement and the Indenture will be in furtherance of the purposes of the Law.
- (g) On March 23, 2004, the City Council of the City adopted Resolution No. 2004-093 authorizing the issuance and sale of the Bonds and the execution and delivery of the Indenture, this Agreement, bond purchase agreements and official statements in connection with the sale of the Bonds.

**SECTION 2.2 REPRESENTATIONS OF THE BORROWER.** The Borrower makes the following representations as the basis for its undertakings herein contained:

- (a) The Borrower is a corporation duly formed under the laws of the State of California, is in good standing in the State of California and has the power to enter into and has duly authorized, by proper corporate action, the execution and delivery of this Agreement and all other documents contemplated hereby to be executed by the Borrower.
- (b) Neither the execution and delivery of this Agreement nor of the First Mortgage Bonds, the consummation of the transactions contemplated hereby and thereby, nor the fulfillment of or compliance with the terms and conditions hereof and thereof, conflicts with or results in a breach of any of the terms, conditions or provisions of the Borrower's Articles of Incorporation or By-laws or of any corporate actions or of any agreement or instrument to which the Borrower is now a party or by which it is bound, or constitutes a default (with due notice or the passage of time or both) under any of the foregoing, or results in the creation or imposition of any prohibited lien, charge or encumbrance whatsoever upon any of the property or assets of the Borrower under the terms of any instrument or agreement to which the Borrower is now a party or by which it is bound.
- (c) The Projects refinanced by each Series of Bonds consist and will consist of those facilities described in Exhibit A hereto, and the Borrower shall make no changes to any portion of the Projects or to the operation thereof which would affect the qualification of the Projects as a "project" under the Law or impair the exemption from gross income of the interest on the Bonds to which the Projects relate for federal income tax purposes. In particular, the Borrower shall comply with all requirements of the Tax Certificate, dated the Issue Date (the "Tax Certificate"), which is hereby incorporated by reference herein. Substantially all proceeds of the Bonds will refinance costs of components of the Projects that consist of facilities for the local furnishing of electric energy as described in the Tax Certificate. The Borrower intends to utilize such portion of the Projects as facilities for the local furnishing of electric energy throughout the foreseeable future.
- (d) The Borrower has and will have title to the Projects sufficient to carry out the purposes of this Agreement.
- (e) All certificates, approvals, permits and authorizations with respect to the construction of the Projects of agencies of applicable local governmental agencies, the State of California and the federal government have been obtained; and pursuant to such certificates, approvals, permits and authorizations the Projects has been constructed and is in operation.

ARTICLE III

ISSUANCE OF THE BONDS; APPLICATION OF PROCEEDS

**SECTION 3.1 AGREEMENT TO ISSUE BONDS; APPLICATION OF BOND PROCEEDS.** To provide funds to enable the Borrower to refinance a portion of the cost of the Projects by prepaying the Prior Loans, the City agrees that it will issue under the Indenture, sell and cause to be delivered to the purchasers thereof, the Bonds, bearing interest as provided and maturing on the date set forth in the Indenture. The City will thereupon apply the proceeds received from the sale of the Bonds as provided in Section 3.02 of the Indenture.

**SECTION 3.2 INVESTMENT OF MONEYS IN FUNDS.** Any moneys in any fund held by the Trustee shall, at the written request of an Authorized Borrower Representative, be invested or reinvested by the Trustee as provided in the Indenture. Such investments shall be held by the Trustee and shall be deemed at all times a part of the fund from which such investments were made, and the interest

accruing thereon and any profit or loss realized therefrom shall, except as otherwise provided in the Indenture, be credited or charged to such fund.

**SECTION 3.3 AMENDMENT OF DESCRIPTION OF THE PROJECTS.** In the event that the Borrower desires to amend or supplement the Projects, as described in Exhibit A hereto, and the City in its sole discretion approves of such amendment or supplement, the City will enter into, and will instruct the Trustee to consent to, such amendment or supplement upon receipt of

- (i) a certificate of an Authorized Borrower Representative describing in detail the proposed changes and stating that they will not have the effect of disqualifying any component of the Projects as a facility that may be financed pursuant to the Law;
- (ii) a copy of the proposed form of amended or supplemented Exhibit A hereto; and
- (iii) an Opinion of Bond Counsel that such proposed changes will not affect the exclusion from gross income of interest on the Bonds for federal income tax purposes.

#### ARTICLE IV

##### LOAN TO BORROWER: REPAYMENT PROVISIONS

**SECTION 4.1 LOAN TO BORROWER.** The City and the Borrower agree that the application of the proceeds of sale of the Bonds to refund and retire the Prior Bonds and the first mortgage bonds of the Borrower relating to the Prior Bonds will be deemed to be and treated for all purposes as a loan to the Borrower of an amount equal to the principal amount of the Bonds.

##### SECTION 4.2 REPAYMENT AND PAYMENT OF OTHER AMOUNTS PAYABLE

(a) The Borrower covenants and agrees to pay to the Trustee as a Repayment Installment on the loan to the Borrower pursuant to Section 4.1 hereof, on each date provided in or pursuant to the Indenture for the payment of principal (whether at maturity or upon redemption or acceleration) of, premium, if any, and/or interest on the Bonds, until the principal of, premium, if any, and interest on the Bonds shall have been fully paid or provision for the payment thereof shall have been made in accordance with the Indenture, in immediately available funds, for deposit in the Bond Fund, a sum equal to the amount then payable as principal (whether at maturity or upon redemption or acceleration), premium, if any, and interest upon the Bonds as provided in the Indenture.

Each payment required to be made pursuant to this Section 4.2(a) shall at all times be sufficient to pay the total amount of interest and principal (whether at maturity or upon redemption or acceleration) and premium, if any, then payable on the Bonds; provided that any amount held by the Trustee in the Bond Fund on any due date for a Repayment Installment hereunder shall be credited against the installment due on such date to the extent available for such purpose; and provided further that, subject to the provisions of this paragraph, if at any time the amounts held by the Trustee in the Bond Fund are sufficient to pay all of the principal of and interest and premium, if any, on the Bonds as such payments become due, the Borrower shall be relieved of any obligation to make any further payments under the provisions of this Section. Notwithstanding the foregoing, if on any date the amount held by the Trustee in the Bond Fund is insufficient to make any required payments of principal (whether at maturity or upon redemption or acceleration) and interest and premium, if any, on the Bonds as such payments become due, the Borrower shall forthwith pay such deficiency as a Repayment Installment hereunder.

The obligation of the Borrower to make any payment under this Section 4.2(a) with respect to the Bonds shall be deemed to have been satisfied to the extent of any corresponding payment by the Credit Provider under the Credit Facility, if any, for such Bonds; provided, however, that the foregoing provision shall be inapplicable to any payments made by a Bond Insurer under its Bond Insurance and, in such circumstances, the obligation of the Borrower to make any payment under this Section 4.2(a) shall remain outstanding for all purposes, not be satisfied and not be considered paid by the Borrower, and such obligations shall thereafter run to the benefit of the Bond Insurers to the extent of their payments under their Bond Insurance.

(b) The Borrower also agrees to pay to the Trustee until the principal of, premium, if any, and interest on the Bonds shall have been fully paid or provision for the payment thereof shall have been made as required by the Indenture, (i) the annual fee of the Trustee for its ordinary services rendered as trustee, and its ordinary expenses incurred under the Indenture, as and when the same become due, (ii) the reasonable fees, charges and expenses of the Trustee, the Registrar and the reasonable fees of any paying agent on the Bonds as provided in the Indenture, as and when the same become due, (iii) the reasonable fees, charges and expenses of the Trustee for the necessary extraordinary services rendered by it and extraordinary expenses incurred by it under the Indenture, as and when the same become due. The Borrower shall also pay the cost of printing any Bonds required to be furnished by the City.

(c) The Borrower also agrees to pay, within 60 days after receipt of request for payment thereof, all expenses required to be paid by the Borrower under the terms of the bond purchase agreement executed by it in connection with the sale of the Bonds, and all reasonable expenses of the City related to the financing of the Projects which are not otherwise required to be paid by the Borrower under the terms of this Agreement, including City staff costs at then applicable full cost recovery rates, without offset; provided that the City shall have obtained the prior written approval of the Authorized Borrower Representative for any expenditures other than those provided for herein or in said bond purchase agreement.

The Borrower also agrees to pay to the City on the Issue Date an issuance fee equal to 0.25% of the par amount of the Bonds, pursuant to a certificate of the Borrower.

(d) The Borrower hereby agrees to provide or cause to be provided in immediately available funds, for deposit into the Bond Purchase Fund maintained by the Tender Agent, all amounts necessary to purchase Bonds tendered for purchase in accordance with Sections 2.02(a) and 2.02(b) of the Multi-Mode Annex.

(e) In the event the Borrower should fail to make any of the payments required by subsections (a) through (d) of this Section, such payments shall continue as obligations of the Borrower until such amounts shall have been fully paid. The Borrower agrees to pay such amounts, together with interest thereon until paid, to the extent permitted by law, at the rate of one percent (1%) per annum over the rate borne by any Bonds in respect of which such payments are required to be made pursuant to said subsection (a), and one percent (1%) per annum over the average rate then borne by the Bonds as to all other payments. Interest on overdue payments required under subsection (a) or (d) above shall be paid to Bondholders as provided in the Indenture.

(f) Upon written request of the Trustee, the Borrower shall pay any Repayment Installment directly to the Paying Agent.

(g) Any unpaid obligation of the Borrower under subsections (b) through (e) of this Section 4.2 shall survive the payment and discharge of the Bonds and the termination of this Agreement.

(h) To secure the payment of the Borrower's obligations under subsection (a) of this Section 4.2, the Borrower has delivered to the Trustee the First Mortgage Bonds. The obligation of the Borrower to make payments pursuant to subsections (a) of this Section shall be deemed satisfied to the extent of payments made pursuant to the First Mortgage Bonds.

**SECTION 4.3 UNCONDITIONAL OBLIGATION.** The obligations of the Borrower to make the payments required by Section 4.2 hereof and under the First Mortgage Bonds and to perform and observe the other agreements on its part contained herein shall be absolute and unconditional, irrespective of any defense or any rights of set-off, recoupment or counterclaim it might otherwise have against the City, and during the term of this Agreement, the Borrower shall pay absolutely net the payments to be made on account of the loan as prescribed in Section 4.2 and all other payments required hereunder and under the First Mortgage Bonds, free of any deductions and without abatement, diminution or set-off. Until such time as the principal of, premium, if any, and interest on the Bonds shall have been fully paid, or provision for the payment thereof shall have been made as required by the Indenture, the Borrower (i) will not suspend or discontinue any payments provided for in Section 4.2 hereof; (ii) will perform and observe all of its other covenants contained in this Agreement; and (iii) will not terminate this Agreement except to the extent permitted by the provisions hereof and of the Indenture, or cancel or amend, supplement or otherwise modify the First Mortgage Bonds, the First Mortgage Indenture or the supplement thereto relating to the First Mortgage Bonds, except to the extent permitted by the First Mortgage Indenture, for any cause, including, without limitation, the occurrence of any act or circumstances that may constitute failure of consideration, destruction of or damage to the Projects, commercial frustration of purpose, any change in the tax or other laws of the United States of America or of the State of California or any political subdivision of either of these, or any failure of the City or the Trustee to perform and observe any covenant, whether express or implied, or any duty, liability or obligation arising out of or connected with this Agreement or the Indenture, except to the extent permitted by this Agreement.

**SECTION 4.4 ASSIGNMENT OF CITY'S RIGHTS.** As security for the payment of the Bonds, the City will assign to the Trustee the City's rights, but not its obligations, under this Agreement, including the right to receive payments hereunder (except (i) the rights of the City to receive notices under this Agreement, (ii) the right of the City to receive certain payments, if any, with respect to fees; expenses and indemnification and certain other purposes under Sections 4.2(c), 4.2(e), 6.3, 8.2 and 8.3 hereof, and (iii) the right of the City to give approvals or consents pursuant to this Agreement and any such rights under the First Mortgage Bonds and any Credit Facility relating to the Bonds) and the City hereby directs the Borrower to make the payments required hereunder (except such payments for fees, expenses and indemnification) directly to the Trustee. The Borrower hereby assents to such assignment and agrees to pay the Repayment Installments directly to the Trustee (subject to the provisions of Section 4.2(f)) without defense or set-off by reason of any dispute between the Borrower and the City or the Trustee.

**SECTION 4.5 AMOUNTS REMAINING IN FUNDS.** It is agreed by the parties hereto that after payment in full of (i) the Bonds, or after provision for such payment shall have been made as provided in the Indenture, (ii) the fees and expenses of the City in accordance with this Agreement, (iii) the fees, charges and expenses of the Trustee, the Registrar, the Paying Agents, the Auction Agent and the Broker-Dealer in accordance with the Indenture and this Agreement and (iv) all other amounts required to be paid under this Agreement and the Indenture, any amounts remaining in any fund held by the Trustee under the Indenture shall belong, subject to the requirements of Section 6.06 of the Indenture, to the Borrower and be paid to the Borrower by the Trustee.

**SECTION 4.6 CREDIT FACILITY.** The Borrower shall deliver (or cause to be delivered) to the Trustee financial guaranty insurance policies of XL Capital Assurance Inc. insuring the scheduled payment of principal and interest on the 2004 Series A Bonds, 2004 Series B Bonds, 2004 Series C Bonds, 2004 Series D -Bonds and 2004 Series E Bonds, and Ambac Assurance Corporation insuring the scheduled payment of principal and interest on the 2004 Series F Bonds. The Borrower may provide and subsequently terminate or remove a Credit Facility with respect to the Bonds pursuant to the provisions of Section 5.01 of the Multi-Mode Annex; provided, however, that, except in connection with the redemption of Bonds, the Borrower shall not intentionally cause the termination or substitution of any Credit Facility with respect to Bonds during a Term Rate Period or a Variable Term Segment with respect to such Bonds. Not less than twenty-five days prior to the termination, removal, substitution or delivery of any Credit Facility with respect to the Bonds, the Borrower shall mail written notice of such termination, removal, substitution or delivery to the Trustee. Not less than fifteen days prior to the delivery of any substitute or new Credit Facility for the Bonds, the Borrower shall mail written notice of such substitution or delivery to each Rating Agency.

## SPECIAL COVENANTS AND AGREEMENTS

**SECTION 5.1 RIGHT OF ACCESS TO THE PROJECTS.** The Borrower agrees that during the term of this Agreement the City, the Trustee, the Bond Insurers and the duly authorized agents of any of them shall have the right at all reasonable times during normal business hours to enter upon the site of the Projects described in Exhibit A hereto to examine and inspect such Projects; provided, however, that this right is subject to federal and State of California laws and regulations applicable to such site. The rights of access hereby reserved to the City, the Trustee and the Bond Insurers may be exercised only after such Person or its agent shall have executed release of liability (which release shall not limit any of the Borrower's obligations hereunder) and secrecy agreements if requested by the Borrower in the form then currently used by the Borrower, and nothing contained in this Section or in any other provision of this Agreement shall be construed to entitle the City, the Trustee or any Bond Insurer to any information or inspection involving the confidential know-how of the Borrower.

**SECTION 5.2 THE BORROWER'S MAINTENANCE OF ITS EXISTENCE; ASSIGNMENTS;** (a) The Borrower agrees that during the term of this Agreement it will maintain its corporate existence in good standing and will not dissolve or otherwise dispose of all or substantially all of its assets and will not consolidate with or merge into another corporation or permit one or more other corporations to consolidate or merge into it; provided, that the Borrower may, without violating the covenants contained in this Section, consolidate with or merge into another corporation, or permit one or more other corporations to consolidate with or merge into it, or sell or otherwise transfer to another corporation all or substantially all of its assets and thereafter dissolve, provided that (1) either (A) the Borrower is the surviving corporation or (B) the surviving, resulting or transferee corporation, as the case may be, (i) assumes and agrees in writing to pay and perform all of the obligations of the Borrower hereunder and (ii) qualifies to do business in the State of California; and (2) the Borrower shall deliver to the Trustee an Opinion of Bond Counsel to the effect that such consolidation, merger or transfer and dissolution does not in and of itself adversely affect the exclusion from gross income for federal income tax purposes of interest on the Bonds.

(b) With the prior written consent of the City (which consent shall not be unreasonably withheld), the rights and obligations of the Borrower under this Agreement may be assigned by the Borrower, in whole or in part, subject, however, to each of the following conditions:

(i) No assignment (other than pursuant to a merger, consolidation or combination described in Section 5.2(a)) shall relieve the Borrower from primary liability for any of its obligations hereunder, and in the event of any assignment not pursuant to Section 5.2(a), the Borrower shall continue to remain primarily liable for the payments specified in Section 4.2 hereof and under the First Mortgage Bonds and for performance and observance of the other agreements on its part herein provided to be performed and observed by it, including its obligation to maintain the First Mortgage Bonds and the First Mortgage Indenture in full force and effect to secure the obligations of the Borrower hereunder.

(ii) Any assignment from the Borrower shall retain for the Borrower such rights and interests as will permit it to perform its obligations under this Agreement, and any assignee from the Borrower shall assume the obligations of the Borrower hereunder to the extent of the interest assigned.

(iii) The Borrower shall, within thirty days after delivery of such assignment, furnish or cause to be furnished to the City and the Trustee a true and complete copy of each such assignment together with an instrument of assumption.

(iv) The Borrower shall cause to be delivered to the City and the Trustee an Opinion of Bond Counsel that such assignment will not, in and of itself, affect the exclusion from gross income of interest on the Bonds for federal income tax purposes; (other than a "substantial user" of the Projects or a "related person" within the meaning of Section 147(a) of the Code or Section 103(b)(13) of the 1954 Code).

**SECTION 5.3 RECORDS AND FINANCIAL STATEMENTS OF BORROWER.** The Borrower agrees (a) to keep and maintain full and accurate accounts and records of its operations in accordance with generally accepted accounting principles, (b) to permit the Trustee for itself or on behalf of the holders of the Bonds, the Bond Insurers, and their respective designated officers, employees, agents and representatives to have access to such accounts and records and to make examinations thereof at all reasonable times and (c) upon request of the Trustee or any Bond insurer, to provide the Trustee or such Bond Insurer (as the case may be) with the Borrower's most recent audited financial statements.

**SECTION 5.4 MAINTENANCE AND REPAIR.** The Borrower agrees that as long as it owns the Projects it will (i) maintain, or cause to be maintained, the Projects in as reasonably safe condition as its operations shall permit and (ii) maintain, or cause to be maintained, the projects in good repair and in good operating condition, ordinary wear and tear excepted, making from time to time all necessary repairs thereto and renewals and replacements thereof.

**SECTION 5.5 QUALIFICATION IN CALIFORNIA.** The Borrower agrees that throughout the term of this Agreement it, or any successor or assignee as permitted by Section 5.2, will be qualified to do business in the State of California.

**SECTION 5.6 TAX EXEMPT STATUS OF BONDS.** (a) It is the intention of the parties hereto that interest on the Bonds shall be and remain excluded from gross income for federal income tax purposes. To that end, the covenants and agreements of the City and the Borrower in this Section and in the Tax Certificate are for the benefit of the Trustee and each and every person who at any time will be a holder of the Bonds. Without limiting the generality of the foregoing, the Borrower and the City agree that there shall be paid from time to time all amounts required to be rebated to the United States pursuant to the Rebate Requirement. This covenant shall survive payment in full or defeasance of the Bonds. The Borrower specifically covenants to pay or cause to be paid for and on behalf of the City to the United States at the times and in the amounts determined under Section 6.06 of the Indenture the Rebate Requirement as described in the Tax Certificate and the Indenture. The City shall not be liable to make any such payment except from funds provided by the Borrower for such purpose.

(b) The City covenants and agrees that it has not taken and will not take any action which results in interest to be paid on the Bonds being included in gross income of the holders of the Bonds for federal income tax purposes, and the Borrower covenants and agrees that it has not taken or permitted to be taken and will not take or permit to be taken any action which will cause the interest on the Bonds to become includable in gross income for federal income tax purposes; provided that neither the Borrower nor the City shall have violated these covenants if interest on any of the Bonds becomes taxable to a person solely because such person is a "substantial user" of the Projects or a "related person" within the meaning of Section 147(a) of the Code or Section 103(b)(13) of the 1954 Code; and provided further that none of the covenants and agreements herein contained shall require either the Borrower or the City to enter an appearance or intervene in any administrative, legislative or judicial proceeding in connection with any changes in applicable laws, rules or regulations or in connection with any decisions of any court or administrative agency or other governmental body affecting the taxation of interest on the Bonds. The Borrower acknowledges having read Section 6.06 of the Indenture and agrees to perform all duties imposed on it by such Section, by this Section and by the Tax Certificate. Insofar as Section 6.06 of the Indenture and the Tax Certificate impose duties and responsibilities on the City or the Borrower, they are specifically incorporated herein by reference.

(c) Notwithstanding any provision of this Section 5.6 or Section 6.06 of the Indenture, if the Borrower shall provide to the City and the Trustee an Opinion of Bond Counsel to the effect that any specified action required under this Section 5.6 and Section 6.06 of the Indenture is no longer required or that some further or different action is required to maintain the exclusion from federal income tax of interest on the Bonds, the Borrower, the Trustee and the City may conclusively rely on such opinion in complying with the requirements of this Section, and the covenants set forth in this Section 5.6 shall be deemed to be modified to that extent.

**SECTION 5.7 RATINGS; NOTICE OF RATE PERIODS.** The Borrower agrees to use its best efforts to maintain at least two ratings on the Bonds. The Borrower shall designate and give timely written notice to the Trustee as required by the Indenture prior to any change in Rate Periods for the Bonds. In addition, if the Borrower shall elect to change Rate Periods in accordance with the Indenture and the Bonds under circumstances requiring the delivery of an Opinion of Bond Counsel, the Borrower shall deliver such opinion to the Trustee concurrently with the giving of notice with respect thereto, and no such change shall be effective without an Opinion of Bond Counsel to the effect that such change is authorized or permitted by the Indenture and the Law and will not adversely affect the Tax-Exempt status of the interest on the Bonds.

**SECTION 5.8 MARKETING OF THE BONDS.** The Borrower agrees to perform all obligations and duties required of it by the Indenture with respect to the establishment of interest rates on the Bonds and the marketing thereof, and to appoint a Remarketing Agent, a Tender Agent and an Auction Agent, as necessary, as provided in the Multi-Mode Annex.

**SECTION 5.9 NOTICES TO TRUSTEE AND CITY.** The Borrower hereby agrees to provide the Trustee and the City with notice of any event of which it has knowledge which, with the passage of time or the giving of notice, would be an Event of Default, such notice to include a description of the nature of such event and what steps are being taken to remedy such Event of Default.

**SECTION 5.10 CONTINUING DISCLOSURE.** The Borrower hereby covenants and agrees, upon the adjustment of the Rate Period for the Bonds to a Term Rate Period pursuant to Section 2.01(c) (iv) of the Multi-Mode Annex and the remarketing of such Bonds in accordance with the Indenture, to comply with the continuing disclosure requirements for the Bonds as promulgated under Rule 15c2-12, as it may from time to time hereafter be amended or supplemented. Notwithstanding any other provision of this Agreement, failure of the Borrower to comply with the requirements of Rule 15c2-12 applicable to the Bonds, as it may from time to time hereafter be amended or supplemented, shall not be considered an Event of Default hereunder or under the Indenture; however, any Bondholder or beneficial owner of any Bonds may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the Borrower to comply with its obligations pursuant to this Section 5.11.

**SECTION 5.11 NON-TRANSFERABILITY OF FIRST MORTGAGE BONDS.** The First Mortgage Bonds shall not be transferable except to a successor trustee as provided in Sections 8.08 and 8.09 of the Indenture.

**SECTION 5.12 INDENTURE COVENANTS.** The Borrower acknowledges that the Indenture (including the Multi-Mode Annex) imposes certain obligations and duties on the Borrower and the Borrower hereby agrees to perform all obligations and duties required by it by the Indenture (including the Multi-Mode Annex) as if it were a party thereto,

## ARTICLE VI

### EVENTS OF DEFAULT AND REMEDIES

**SECTION 6.1 EVENTS OF DEFAULT.** Any one of the following which occurs and continues shall constitute an Event of Default pursuant to this Agreement:



- (a) failure by the Borrower to pay any amounts required to be paid under Section 4.2(a) or 4.2(d) hereof at the times required to avoid causing an Event of Default pursuant to the Indenture; or
- (b) failure of the Borrower to observe and perform any covenant, condition or agreement on its part required to be observed or performed by this Agreement, other than making the payments referred to in (a) above, which continues for a period of 60 days after written notice, which notice shall specify such failure and request that it be remedied, given to the Borrower by the City or the Trustee, unless the City and the Trustee shall agree in writing to an extension of such time; provided, however, that if the failure stated in the notice cannot be corrected within such period, the City and the Trustee will not unreasonably withhold their consent to an extension of such time if corrective action is instituted within such period and diligently pursued until the default is corrected; or
- (c) the occurrence of a "completed default" by the Borrower under the First Mortgage Indenture which results in the principal and interest on the First Mortgage Bonds becoming due and payable by reason of acceleration; or
- (d) an Act of Bankruptcy of the Borrower; or
- (e) a default under any Credit Facility if the Credit Provider notifies the Trustee in writing that such default shall be treated as an Event of Default hereunder.

The provisions of subsection (b) of this Section are subject to the limitation that the Borrower shall not be deemed in default if and so long as the Borrower is unable to carry out its agreements hereunder by reason of strikes, lockouts or other industrial disturbances; acts of public enemies; orders of any kind of the government of the United States or of the State of California or any of their departments, agencies, or officials, or any civil or military authority; insurrections, riots, epidemics, landslides; lightning; earthquake; fire; hurricanes; storms; floods; washouts; droughts; arrests; restraint of government and people; civil disturbances; explosions; breakage or accident to machinery, transmission pipes or canals; partial or entire failure of utilities; or any other cause or event not reasonably within the control of the Borrower; it being agreed that the settlement of strikes, lockouts and other industrial disturbances shall be entirely within the discretion of the Borrower, and the Borrower shall not be required to make settlement of strikes, lockouts and other industrial disturbances by acceding to the demands of the opposing party or parties when such course is, in the judgment of the Borrower, unfavorable to the Borrower. This limitation shall not apply to any default under subsections (a), (c), (d) or (e) of this Section.

**SECTION 6.2 REMEDIES ON DEFAULT.** Whenever any Event of Default shall have occurred and shall continue, the following remedies may be pursued:

- (a) The Trustee may, and at the direction of the holders of not less than 25% in aggregate principal amount of Bonds then outstanding shall, by notice in writing delivered to the Borrower with copies of such notice being sent to the City and each Bond Insurer, declare the unpaid balance of the loan payable under Section 4.2(a) of this Agreement and the interest accrued thereon to be immediately due and payable and such principal and interest shall thereupon become and be immediately due and payable. Upon any such acceleration, the Bonds shall be subject to mandatory redemption as provided in Section 4.01(b)(3) of the Multi-Mode Annex. After any such declaration of acceleration, the Trustee shall immediately take such actions as necessary to realize moneys under any Credit Facility.
- (b) The Trustee shall have access to and the right to inspect, examine and make copies of the books and records and any and all accounts, data and federal income tax and other tax returns of the Borrower.
- (c) The City or the Trustee may take whatever action at law or in equity as may be necessary or desirable to collect the payments and other amounts then due and thereafter to become due or to enforce performance and observance of any obligation, agreement or covenant of the Borrower under this Agreement or under the First Mortgage Bonds.

The provisions of clause (a) of the preceding paragraph, however, are subject to the condition that if, at any time after the loan shall have been so declared due and payable, and before any judgment or decree for the payment of the moneys due shall have been obtained or entered as hereinafter provided, there shall have been deposited with the Trustee a sum sufficient (together with any amounts held in the Bond Fund) to pay all the principal of the Bonds matured prior to such declaration and all matured installments of interest (if any) upon all the Bonds, with interest on such overdue installments of principal as provided herein, and the reasonable expenses of the Trustee, and any and all other defaults known to the Trustee (other than in the payment of principal of and interest on the Bonds due and payable solely by reason of such declaration) shall have been made good or cured to the satisfaction of the Trustee or provision deemed by the Trustee to be adequate shall have been made there for, then, and in every such case, the Bond Insurer of any Series of Bonds, or if such Bond Insurer is failing to make a payment required pursuant to such Bond Insurance, the holders of at least a majority in aggregate principal amount of the Bonds then outstanding, by written notice to the City and to the Trustee, may, on behalf of the holders of all the Bonds, rescind and annul such declaration and its consequences and waive such default; provided, (i) that no such rescission and annulment shall extend to or shall affect any subsequent default, or shall impair or exhaust any right or power consequent thereon, (ii) that there shall not be rescinded or annulled any such declaration which follows an event described in Section 6.1(e) without the written consent of each Bond Insurer, and (iii) that there shall not be rescinded or annulled any such declaration which follows an event described in Section 6.1(c) unless the corresponding acceleration of the First Mortgage Bonds shall have been rescinded or annulled. In the event that the declaration of acceleration of the First Mortgage Bonds shall have been rescinded and annulled, and payments of principal and interest due on the Bonds other than by reason of such acceleration shall have been made, the acceleration of the principal and interest on the Bonds hereunder shall be automatically rescinded and annulled without further action of the Trustee.

Anything in this Agreement to the contrary notwithstanding, upon the occurrence and continuance of an Event of Default hereunder, the Insurer then providing Bond Insurance for any Series of Bonds shall be entitled to control and direct the enforcement of all rights and remedies granted to the holders of the Bonds insured by such Bond Insurance or granted to the Trustee for the benefit of the holders of the Bonds insured by such Bond Insurance, including any acceleration of the loan payable under this Agreement and any rescission of such acceleration, provided that such rights of the Insurer shall not be applicable if such Insurer is in default of any of its payment obligations as set forth in the Bond Insurance provided by such Bond Insurer.

In case the Trustee, any Bond Insurer or the City shall have proceeded to enforce its rights under this Agreement and such proceedings shall have been discontinued or abandoned for any reason or shall have been determined adversely to the Trustee or the City, then, and in every such case, the Borrower, the Trustee, any Bond Insurer and the City shall be restored respectively to their several positions and rights hereunder, and all rights, remedies and powers of the Borrower, the Trustee, the Bond Insurer and the City shall continue as though no such action had been taken (provided, however, that any settlement of such proceedings duly entered into by the City, the Trustee or the Borrower shall not be disturbed by reason of this provision).

In case the Borrower shall fail forthwith to pay amounts due by reason of this Section 6.2 upon demand of the Trustee, the Trustee shall be entitled and empowered to institute any action or proceeding at law or in equity for the collection of the sums so due and unpaid (including sums due and unpaid on the First Mortgage Bonds), and may prosecute any such action or proceeding to judgment or final decree, and may enforce any such judgment or final decree against the Borrower and collect in the manner provided by law the moneys adjudged or decreed to be payable.

In case proceedings shall be pending for the bankruptcy or for the reorganization of the Borrower under the federal bankruptcy laws or any other applicable law, or in case a receiver or trustee shall have been appointed for the property of the Borrower or in the case of any other similar judicial proceedings relative to the Borrower, or the creditors or property of the Borrower, then the Trustee shall be entitled and empowered, by intervention in such proceedings or otherwise, to file and prove a claim or claims for the whole amount owing and unpaid pursuant to this Agreement and, in case of any judicial proceedings, to file such proofs of claim and other papers or documents as may be necessary or advisable in order to have the claims of the Trustee allowed in such judicial proceedings relative to the Borrower, its creditors or its property, and to collect and receive any moneys or other property payable or deliverable on any such claims, and to distribute such amounts as provided in the Indenture after the deduction of its charges and expenses. Any receiver, assignee or trustee in bankruptcy or reorganization is hereby authorized to make such payments to the Trustee, and to pay to the Trustee any amount due it for compensation and expenses, including expenses and fees of counsel incurred by it up to the date of such distribution.

**SECTION 6.3 AGREEMENT TO PAY ATTORNEYS' FEES AND EXPENSES.** In the event the Borrower should default under any of the provisions of this Agreement and the City or the Trustee should employ attorneys or incur other expenses for the collection of the payments due under this Agreement or the enforcement of performance or observance of any obligation or agreement on the part of the Borrower herein contained, the Borrower agrees to pay to the City or the Trustee the reasonable fees of such attorneys and such other expenses so incurred by the City or the Trustee.

**SECTION 6.4 NO REMEDY EXCLUSIVE.** No remedy herein conferred upon or reserved to the City or the Trustee is intended to be exclusive of any other available remedy or remedies, but each and every such remedy shall be cumulative and shall be in addition to every other remedy given under this Agreement or now or hereafter existing at law or in equity or by statute. No delay or omission to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed to be a waiver thereof, but any such right and power may be exercised from time to time and as often as may be deemed expedient. In order to entitle the City or the Trustee to exercise any remedy reserved to it in this Article, it shall not be necessary to give any notice, other than such notice as may be herein expressly required. Such rights and remedies as are given the City hereunder shall also extend to the Trustee, and the Trustee, the Bond Insurers and the holders of the Bonds shall be deemed third party beneficiaries of all covenants and agreements herein contained.

**SECTION 6.5 NO ADDITIONAL WAIVER IMPLIED BY ONE WAIVER.** In the event any agreement or covenant contained in this Agreement should be breached by the Borrower and thereafter waived by the City or the Trustee, such waiver shall be limited to the particular breach so waived and shall not be deemed to waive any other breach hereunder.

## ARTICLE VII

### PREPAYMENT

**SECTION 7.1 REDEMPTION OF BONDS WITH PREPAYMENT MONEYS.** By virtue of the assignment of certain of the rights of the City under this Agreement to the Trustee as is provided in Section 4.4 hereof, the Borrower agrees to and shall pay directly to the Trustee any amount permitted or required to be paid by it under this Article VII. The Trustee shall use the moneys so paid to it by the Borrower to effect redemption of the Bonds in accordance with Article IV of the Indenture on the date specified for such redemption pursuant to Section 7.5 hereof.

**SECTION 7.2 OPTIONS TO PREPAY INSTALLMENTS.** The Borrower shall have the option to prepay the amounts payable under Section 4.2 hereof, in whole or in part, by paying to the Trustee, for deposit in the Bond Fund, the amount set forth in Section 7.4 hereof, under the circumstances set forth in Section 4.01(a) of the Multi-Mode Annex; provided, however, that if any event specified in Section 4.01(a)(1)(A) through (D) of the Multi-Mode Annex gives rise to the Borrower's exercise of its option to prepay such amounts payable hereunder, the amount of such loan payment prepaid shall not exceed the original cost of the portion of the Projects affected by such event.

**SECTION 7.3 MANDATORY PREPAYMENT.** (a) The Borrower shall have and hereby accepts the obligation to prepay Repayment Installments to the extent mandatory redemption of the Bonds is required pursuant to Section 4.01(b) of the Multi-Mode Annex. The Borrower shall satisfy its obligation hereunder by prepaying such Repayment Installments within one hundred eighty (180) days after the occurrence of any event set forth in paragraphs (1) and (2) of said Section 4.01(b) giving rise to such required prepayment, and within five (5) days upon the occurrence of any event set forth in paragraph (3) thereof giving rise to such required prepayment. The amount payable by the Borrower in the event of a prepayment required by this Section shall be determined as set forth in Section 7.4 and shall be deposited in the Bond Fund.

**SECTION 7.4 AMOUNT OF PREPAYMENT.** In the case of a prepayment of the entire amount due hereunder pursuant to Section 7.2 or 7.3 hereof, the amount to be paid shall be a sum sufficient, together with other funds and the yield on any securities deposited with the Trustee and available for such purpose, to pay (1) the principal of all Bonds outstanding on the redemption date specified in the notice of redemption, plus interest accrued and to accrue to the payment or redemption date of the Bonds, plus premium, if any, pursuant to the Indenture, (2) all reasonable and necessary fees and expenses of the City, the Trustee, the Registrar, the Tender Agent and any Paying Agent accrued and to accrue through final payment of the Bonds, and (3) all other liabilities of the Borrower accrued and to accrue under this Agreement.

In the case of partial prepayment of the Repayment Installments, the amount payable shall be a sum sufficient, together with other funds deposited with the Trustee and available for such purpose, to pay the principal amount of and premium, if any, and accrued interest on the Bonds to be redeemed, as provided in the Indenture, and to pay expenses of redemption of such Bonds.

**SECTION 7.5 NOTICE OF PREPAYMENT.** The Borrower shall give forty-five days' prior written notice to the City and the Trustee specifying the date upon which any prepayment pursuant to this Article VII will be made. If, in the case of a mandatory prepayment pursuant to Section 7.3 hereof, the Borrower fails to give such notice of a prepayment required by this Section 7.5, such notice may be given by the City or by any holder or holders of ten percent (10%) or more in aggregate principal amount of the Bonds Outstanding, and shall be given by the Trustee, but solely at the times and under the circumstances provided in Section 4.01(b) of the Multi-Mode Annex. The City and the Trustee, at the request of the Borrower or any such Bondholder or Bondholders, shall forthwith take all steps necessary under the applicable provisions of the Indenture (except that the City shall not be required to make payment of any money required for such redemption) to effect redemption of all or part of the then outstanding Bonds, as the case may be, on the earliest practicable date thereafter on which such redemption may be made under applicable provisions of the Indenture.

Notwithstanding anything to the contrary in this Agreement, each notice contemplated in this Section 7.5 that is given with respect to an optional prepayment pursuant to Section 7.2 hereof may state that it is subject to and conditional upon receipt by the Trustee on or prior to the proposed prepayment date of amounts sufficient to effect such prepayment and, if a notice so states, such notice shall be of no force and effect and the prepayment need not be made and the Repayment Installments will not become due and payable on the proposed prepayment date unless such amounts are so received on or prior to the proposed prepayment date.

## ARTICLE VIII

### NON LIABILITY OF CITY; EXPENSES; INDEMNIFICATION

**SECTION 8.1 NON-LIABILITY OF CITY.** The City shall not be obligated to pay the principal of, or premium, if any, or interest on the Bonds, or to discharge any other financial liability (including but not limited to financial liability under Section 5.6 hereof) in connection herewith, except from, and to the extent of, Revenues. The Borrower hereby acknowledges that the City's sole source of moneys to repay the Bonds will be provided by the payments made by the Borrower pursuant to this Agreement (excluding payments to the City or the Trustee pursuant to Section 4.2(b), 4.2(c), 4.2(e), 5.6, 6.3, 8.2 and 8.3 of this Agreement) and the First Mortgage Bonds, together with other Revenues, including investment income on certain funds and accounts held by the Trustee under the Indenture, and hereby agrees that if the payments to be made hereunder shall ever prove insufficient to pay all principal of, and premium, if any, and interest on the Bonds as the same shall become due (whether by maturity, redemption, acceleration or otherwise), then upon notice from the Trustee, the Borrower shall pay such amounts as are required from time to time to prevent any deficiency or default in the payment of such principal, premium or interest, including, but not limited to, any deficiency caused by acts, omissions, nonfeasance or malfeasance on the part of the Trustee, the Borrower, the City or any third party.

**SECTION 8.2 EXPENSES.** The Borrower covenants and agrees to pay within thirty (30) days after billing therefor and to indemnify the City and the Trustee against all reasonable costs and charges, including fees and disbursements of attorneys, accountants, consultants, including financial consultants, engineers and other experts, and City staff costs at then-applicable full cost recovery rates, without offset, except for such costs incurred in acts of willful misconduct by the City, its elected officials, employees or agents, incurred in connection with this Agreement, the Bonds or the Indenture. The City shall notify the Borrower in writing prior to engaging any professional or expert for which the City plans to bill the Borrower.

**SECTION 8.3 INDEMNIFICATION.** The Borrower releases the City and the Trustee from, and covenants and agrees that neither the City nor the Trustee shall be liable for, and covenants and agrees, to the extent permitted by law, to indemnify, defend and hold harmless the City and the Trustee and their officers, elected officials, employees and agents from and against, any and all losses, claims, damages, liabilities or expenses, of every conceivable kind, character and nature whatsoever arising out of, resulting from or in any way connected with (1) the Projects, or the conditions, occupancy, use, possession, conduct or management of, or work done in or about, or from the planning, design, acquisition, installation or construction of the Projects or any part thereof; (2) the issuance of any Bonds or any certifications, covenants or representations made in connection therewith and the carrying out of any of the transactions contemplated by the Bonds, the Indenture and this Agreement; (3) the Trustee's acceptance or administration of the trusts under the Indenture; (4) the exercise or performance of any of the City's or Trustee's powers or duties under the Indenture or this Agreement; or (5) any untrue statement or alleged untrue statement of any material fact or omission or alleged omission to state a material fact necessary to make the statements made, in light of the circumstances under which they were made, not misleading, in any official statement or other offering circular utilized by the City or any underwriter or placement agent in connection with the sale of any Bonds; provided that such indemnity shall not be required for damages that result from sole gross negligence or willful misconduct on the part of the party seeking such indemnity. The indemnity of the Trustee required by this Section shall be only to the extent that any loss sustained by the Trustee exceeds the net proceeds the Trustee receives from any insurance carried with respect to the loss sustained. The Borrower further covenants and agrees, to the extent permitted by law, to pay or to reimburse the City and the Trustee and their officers, employees and agents for any and all reasonable costs, including but not limited to attorneys fees, liabilities or expenses incurred in connection with investigating, defending against or otherwise in connection with any such losses, claims, damages, liabilities, expenses or actions, except to the extent that the same arise out of the negligence or willful misconduct of the party claiming such payment or reimbursement. The provisions of this Section shall survive the retirement of the Bonds or resignation or removal of the Trustee.

## ARTICLE IX

### MISCELLANEOUS

**SECTION 9.1 NOTICES.** All notices, certificates or other communications shall be deemed sufficiently given on the second day following the day on which the same have been mailed by first class mail, postage prepaid, addressed to the City, the Borrower or the Trustee, as the case may be, as set forth in the Indenture. A duplicate copy of each notice, certificate or other communication given hereunder by either the City or the Borrower to the other shall also be given to the Trustee. The City, the Borrower and the Trustee may, by notice given hereunder, designate any different addresses to which subsequent notices, certificates or other communications shall be sent.

**SECTION 9.2 SEVERABILITY.** If any provision of this Agreement shall be held or deemed to be, or shall in fact be, illegal, inoperative or unenforceable, the same shall not affect any other provision or provisions herein contained or render the same invalid, inoperative, or unenforceable to any extent whatever.

**SECTION 9.3 EXECUTION OF COUNTERPARTS.** This Agreement may be simultaneously executed in several counterparts, each of which shall be an original and all of which shall constitute but one and the same instrument; provided, however, that for purposes of perfecting a security interest in this Agreement under Article 9 of the California Uniform Commercial Code, only the counterpart delivered, pledged, and assigned to the Trustee shall be deemed the original.

**SECTION 9.4 AMENDMENTS CHANGES AND MODIFICATIONS.** Except as otherwise provided in this Agreement or the Indenture, subsequent to the initial issuance of Bonds and prior to their payment in full, or provision for such payment having been made as provided in the Indenture, this Agreement may not be effectively amended, changed, modified, altered or terminated without the written consent of the Trustee.

**SECTION 9.5 GOVERNING LAW.** This Agreement shall be governed exclusively by and construed in accordance with the applicable laws of the State of California.

**SECTION 9.6 AUTHORIZED BORROWER REPRESENTATIVE.** Whenever under the provisions of this Agreement the approval of the Borrower is required or the City or the Trustee is required to take some action at the request of the Borrower, such approval or such request shall be given on behalf of the Borrower by an Authorized Borrower Representative, and the City and the Trustee shall be authorized to act on any such approval or request and neither party hereto shall have any complaint against the other or against the Trustee as a result of any such action taken.

**SECTION 9.7 TERM OF THE AGREEMENT.** This Agreement shall be in full force and effect from the date hereof and shall continue in effect as long as any of the Bonds are outstanding or the Trustee holds any moneys under the Indenture, whichever is later; provided, however, that the rights of the Trustee and the City under Section 8.2 and 8.3 hereof shall survive the termination of this Agreement, the retirement of the Bonds and the removal or resignation of the Trustee. All representations and certifications by the Borrower as to all matters affecting the Tax-Exempt status of the Bonds shall survive the termination of this Agreement.

**SECTION 9.8 BINDING EFFECT.** This Agreement shall inure to the benefit of and shall be binding upon the City, the Borrower, the Trustee and their respective successors and assigns; subject, however, to the limitations contained in Section 5.2 hereof.

IN WITNESS WHEREOF, the City of Chula Vista has caused this Agreement to be executed in its name and its seal to be hereunto affixed and attested by its duly authorized officers, and San Diego Gas & Electric Company has caused this Agreement to be executed in its name and its seal to be hereunto affixed by its duly authorized officers, all as of the date first above written.

CITY OF CHULA VISTA

By: /s/ Stephen Padilla

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Mayor

Attest:

By: /s/ Donna Norris

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City Clerk

APPROVED AS TO FORM

ANN Y MOORE

City Attorney

By: /s/ Elizabeth Wagner Hall

-----

Deputy City Attorney

SAN DIEGO GAS & ELECTRIC COMPANY

By:

-----

Authorized Officer

By:

-----

Authorized Officer

IN WITNESS WHEREOF, the City of Chula Vista has caused this Agreement to be executed in its name and its seal to be hereunto affixed and attested by its duly authorized officers, and San Diego Gas & Electric Company has caused this Agreement to be executed in its name and its seal to be hereunto affixed by its duly authorized officers, all as of the date first above written.

CITY OF CHULA VISTA

By:

-----

Mayor

Attest:

By:

-----

City Clerk

APPROVED AS TO FORM

ANN Y MOORE

City Attorney

By:

-----

Deputy City Attorney

SAN DIEGO GAS & ELECTRIC COMPANY

By: /s/ Steven D. Davis

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Authorized Officer

By: /s/ Terry M. Fleskes

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Authorized Officer

Series C Bonds

Southwest Powerlink (Eastern Supply Line) Transmission Facilities

Acquisition and construction of 500 KV electric transmission line facilities, including necessary towers, cable, foundations, and related facilities, equipment, structures and improvements (together with land and land-rights), from Imperial Valley Substation in Imperial County, California, to Miguel Substation in San Diego County, California, required by San Diego Gas & Electric Company (the "Company") to transmit needed power supplies to the Company's electric retail service area for further transmission and distribution to its customers therein and to consumers in Escondido, including necessary additions and improvements to the Miguel and Mission Substations and connecting transmission facilities, to accommodate handling of increased power supplies.

Local Transmission Facilities\*

Acquisition and construction of additions and improvements to the Company's electric transmission and subtransmission line facilities (more than 12 KV) and related substations, located within its electric retail service area including 230 KV transmission line facilities to Miguel Substation from the Mexican border, required by the Company to provide for bulk transmission of power supplies within such service area, for distribution to the Company's customers located therein and to consumers in Escondido.

Local Generation Facilities\*

Acquisition and construction of additions and improvements to electric generating stations and units that were at one time owned by the Company, located within the Company's retail electric service area and required by the Company to produce electric energy for distribution to its customers located therein and to consumers in Escondido.

Other Local Electric Facilities\*

Acquisition and construction of additions and improvements to the Company's electric distribution facilities (12 KV and under) and related substations, and customer service connections located within the Company's electric retail service area, required by the Company to provide for the transfer and distribution of electric energy to its customers located therein and to consumers in Escondido, including necessary additions and improvements to the Company's related general facilities, plant, property, vehicles, and other equipment (including land and landrights) required for the proper installation, protection, maintenance, control and operation of the foregoing local electric transmission, generation, subtransmission and distribution facilities.

\* The Facilities in each case include all necessary towers, poles, cable, foundations, controls, wiring, transformers switches, metering equipment, and other related facilities, equipment, structures, and improvements (together with necessary land and land-rights), required for the proper installation, maintenance, control or operation of such Facilities. The additions and improvements to these Facilities are required for the purpose of replacing obsolete or worn out components; providing increased quantities or reliability of energy supplies; providing service to new customers; complying with zoning and environmental (or other) ordinances, regulations or orders of public bodies or agencies; relocating facilities as required by public works; making overhead to underground conversions or otherwise providing for the continued or enhanced maintenance, control or operation of such Facilities.

EXHIBIT A-2

Description of the Projects Refinanced with the 2004 Series D Bonds and 2004 Series E Bonds

Local Electric Facilities

Acquisition and construction of additions and improvements to the electric distribution facilities (12 KV and under) and related substations of San Diego Gas & Electric Company (the "Company"), and customer service connections located within the Company's electric retail service area, required by the Company to provide for the transfer and distribution of electric energy to its customers located therein and to consumers in Escondido, including all necessary poles, foundations, cable, conduit, transformers, switches, controls, meters, substations, land and land-rights and other like facilities and equipment, as well as necessary other equipment required for the proper installation, protection, maintenance, control and operation of the foregoing local electric distribution facilities. These facilities will be required to meet the needs of new customers, maintain and improve system capabilities, and make overhead to underground conversions.

EXHIBIT A-3

Description of the Projects Refinanced with the 2004 Series F Bonds

Local Electric Facilities

Acquisition and construction of additions and improvements to the electric generation, transmission and distribution facilities required by San Diego Gas & Electric Company (the "Company") to provide for the generation, transmission and distribution of electric energy to its retail customers and to consumers in Escondido, including but not limited to all necessary turbines, generators, poles, foundations, cable, conduit, transformers, switches, controls, meters, substations, land and land-rights and other facilities, structures and equipment, as well as necessary other equipment required for the proper installation, protection, maintenance, control and operation of the foregoing local electric generation, transmission and distribution facilities. These facilities are required to meet the needs of new customers, maintain and improve system capabilities, and make overhead to underground conversions.

## EXHIBIT 12.1

## SEMPRA ENERGY

## COMPUTATION OF RATIO OF EARNINGS TO COMBINED FIXED CHARGES

## AND PREFERRED STOCK DIVIDENDS

(Dollars in millions)

	2000	2001	2002	2003	2004
Fixed Charges and Preferred Stock Dividends:					
Interest	\$ 308	\$ 358	\$ 350	\$ 351	\$ 334
Interest portion of annual rentals	8	6	4	4	4
Preferred dividends of subsidiaries (1)	18	16	14	11	12
Combined fixed charges and preferred stock dividends for purpose of ratio	\$ 334	\$ 380	\$ 368	\$ 366	\$ 350
Earnings:					
Pretax income from continuing operations	\$ 699	\$ 731	\$ 721	\$ 742	\$ 1,113
Total fixed charges (from above)	334	380	368	366	350
Less:					
Interest capitalized	3	11	29	26	8
Equity in income (loss) of unconsolidated subsidiaries and joint ventures	62	12	(55)	8	36
Total earnings for purpose of ratio	\$ 968	\$ 1,088	\$ 1,115	\$ 1,074	\$ 1,419
Ratio of earnings to combined fixed charges and preferred stock dividends	2.90	2.86	3.03	2.93	4.05

(1) In computing this ratio, "Preferred dividends of subsidiaries" represents the before-tax earnings necessary to pay such dividends, computed at the effective tax rates for the applicable periods.

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**INTRODUCTION**

*This section of the 2004 Annual Report includes management's discussion and analysis of operating results from 2002 through 2004, and provides information about the capital resources, liquidity and financial performance of Sempra Energy and its subsidiaries (collectively referred to as "the company"). This section also focuses on the major factors expected to influence future operating results and discusses investment and financing activities and plans. It should be read in conjunction with the Consolidated Financial Statements included in this Annual Report.*

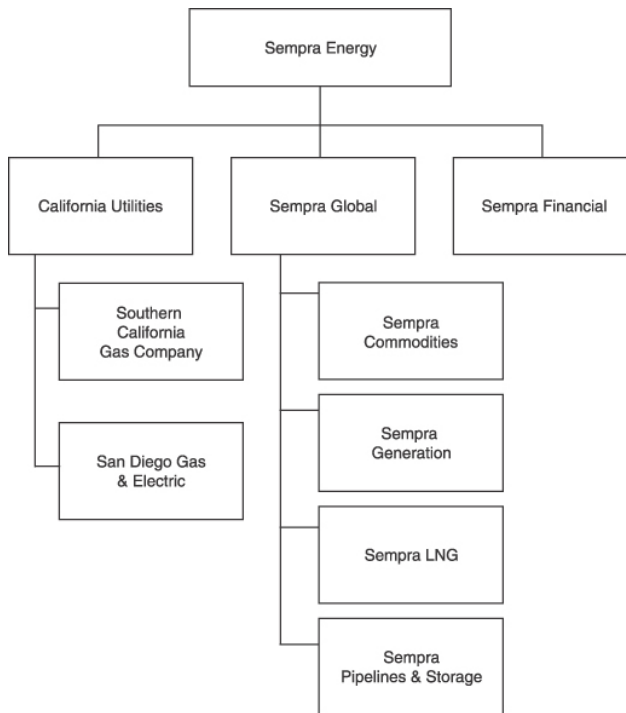
**OVERVIEW**

**Sempra Energy**

*Sempra Energy is a Fortune 500 energy services holding company. Its business units provide a wide spectrum of value-added products and services to a diverse range of customers. On January 1, 2005, the names for some of the company's subsidiaries changed. Sempra Energy Global Enterprises is now Sempra Global. Sempra Energy Financial is now Sempra Financial. Sempra Energy Trading is now Sempra Commodities. Sempra Energy Resources is now Sempra Generation. Sempra Energy International is now Sempra Pipelines & Storage. Sempra Energy LNG is now Sempra LNG.*

*In addition, on December 1, 2004, Sempra Energy Solutions' commodities business was absorbed into Sempra Commodities, while its other businesses, energy services and facilities management, are now part of Sempra Generation. As a result, certain prior-year amounts have been revised to conform to the current year's presentation.*

**SEMPRA ENERGY 1.**



SEMPRA ENERGY 2.

Summary descriptions of the operating business units are provided below and further detail is provided throughout this section of the Annual Report.

Major events during 2004 affecting the results for the year and future years (and the page number where each is discussed) include the following:

- Continuing legal proceedings concerning anti-trust claims made against the company, San Diego Gas & Electric (SDG&E) and Southern California Gas Company (SoCalGas) (101) and concerning Sempra Generation's contract with the California Department of Water Resources (DWR) (101);
- Acquisition of the Coletto Creek Power Station and nine other Texas power plants by a 50% owned joint venture (60);
- Continued development of the liquefied natural gas (LNG) business (17);
- Significantly increased net income at Sempra Commodities due to market volatility and at Sempra Generation due to increased volumes under the DWR contract (8);
- Commencement of construction by the company's generation subsidiary of the Palomar power plant to be owned by SDG&E (14);
- California Public Utilities Commission (CPUC) cost of service decision in 2004 relating to the California Utilities' rates through 2007 (11);
- Final court decision in 2004 resolving the CPUC settlement relating to SDG&E's intermediate-term power-purchase contracts (7);
- Discontinuance of Atlantic Electric & Gas (AEG) operations (10); and
- Transfer of the company's retail energy-related product and service businesses to Sempra Commodities and Sempra Generation (1).

#### **The California Utilities**

SoCalGas and SDG&E (collectively, the California Utilities) serve 23 million consumers from California's Central Valley to the Mexican border. Natural gas service is provided throughout Southern California and portions of central California through 6.3 million meters. Electric service is provided throughout San Diego County and portions of Orange County, both in Southern California, through 1.3 million meters.

#### **Sempra Global**

Sempra Global is a holding company for most of the subsidiaries of Sempra Energy that are not subject to California utility regulation.

Sempra Global's principal subsidiaries provide the following energy-related products and services:

- Sempra Commodities is a wholesale and retail trader of physical and financial products, including natural gas, power, crude oil and other commodities; a trader and wholesaler of metals, serving a broad range of customers; and an owner of synthetic fuel facilities that generate Section 29 income tax credits;
- Sempra Generation acquires, develops and operates power plants, provides energy services and facilities management, and owns mineral rights in properties that produce petroleum and natural gas;
- Sempra LNG is developing receipt terminals for the importation of LNG and has an agreement to supply natural gas to Mexico's state-owned electric utility; and
- Sempra Pipelines & Storage engages in energy-infrastructure projects in North and South America. It holds interests in companies that provide natural gas or electricity services to over 2.8 million customers in Argentina, Chile, Mexico and Peru; develops natural gas pipelines and storage facilities; and owns two small natural gas distribution utilities in the eastern United States.

SEMPRA ENERGY 3.



**Sempra Financial**

In order to reduce Sempra Energy's income taxes, Sempra Financial invests in tax-advantaged limited partnerships which own 1,300 affordable-housing properties throughout the United States.

**RESULTS OF OPERATIONS****Overall Operations**

Net income was \$895 million in 2004, a 37.9% increase over 2003, and diluted earnings per share were \$3.83, an increase of 26.4%, as described below. The percentage increase in diluted earnings per share was less than the percentage increase in earnings due to the issuance of shares in late 2003 to expand Sempra Global's businesses. The increase in net income was primarily due to increased profits at Sempra Commodities and Sempra Generation and the fact that 2003's results included a significant write-down in the Sempra Pipelines & Storage business unit.

The following table shows net income and diluted earnings per share for each of the last five years.

(Dollars in millions, except per share amounts)	Net Income	Diluted Earnings Per Share
<b>2004</b>	<b>\$ 895</b>	<b>\$ 3.83</b>
2003	\$ 649	\$ 3.03
2002	\$ 591	\$ 2.87
2001	\$ 518	\$ 2.52
2000	\$ 429	\$ 2.06

**Net Income (Loss) by Business Unit**

(Dollars in millions)	2004		Years ended December 31, 2003		2002	
<b>California Utilities</b>						
Southern California Gas Company	\$ 232	26%	\$ 209	32%	\$ 212	36%
San Diego Gas & Electric	208	23	334	52	203	34
Total Utilities	440	49	543	84	415	70
<b>Sempra Global</b>						
Sempra Commodities	320	36	157	24	149	25
Sempra Generation	137	15	71	11	42	7
Sempra Pipelines & Storage	63	7	3	—	26	5
Sempra LNG	(8)	(1)	(2)	—	—	—
Total Sempra Global	512	57	229	35	217	37
<b>Sempra Financial</b>	36	4	41	6	36	6
Parent and other*	(68)	(7)	(118)	(18)	(93)	(16)
Continuing operations	920	103	695	107	575	97
Discontinued operations	(25)	(3)	—	—	—	—
Extraordinary item	—	—	—	—	16	3
Cumulative effect of changes in accounting principles	—	—	(46)	(7)	—	—
<b>Consolidated net income</b>	<b>\$ 895</b>	<b>100%</b>	<b>\$ 649</b>	<b>100%</b>	<b>\$ 591</b>	<b>100%</b>

\* Includes after-tax interest expense of \$112 million, \$100 million and \$70 million in 2004, 2003 and 2002, respectively, intercompany eliminations recorded in consolidation and certain corporate costs incurred at Sempra Global.

### Comparison of Earnings

To assist in understanding the trend of earnings the following table summarizes the major unusual factors affecting net income and operating income in 2004, 2003 and 2002. The numbers in parentheses are the page numbers where each item is discussed herein.

(Dollars in millions)	Net Income			Operating Income	
	2004	2003	2002	2004	2003
Reported amounts	\$ 895	\$ 649	\$ 591	\$ 1,272	\$ 939
<b>Unusual items:</b>					
Discontinued operations — AEG (10)	25	—	—	—	—
AEG equity losses — disposed of in April 2004 (10)	—	5	10	—	—
Asset impairments of Frontier Energy (54) and AEG (54)	—	68	—	—	101
Gains on sale of SoCalGas' partnership property (10) and on partial sale of Luz del Sur (13)	(14)	—	—	—	—
Gain on settlement of Cameron liability (13)	(8)	—	—	—	—
Prior years' income tax issues (68)	(56)	(118)	(25)	—	—
California energy crisis litigation costs (101)	84	38	13	140	66
Regulatory issues (11)	(55)	—	—	(51)	—
SoCalGas' natural gas procurement awards (6)	—	(29)	—	—	(49)
SoCalGas sublease losses (9)	—	11	—	—	19
Resolution of vendor disputes in Argentina (13)	(12)	(11)	—	—	—
SDG&E power contract settlement (7)	—	(65)	—	—	(116)
SONGS incentive pricing (ended 12/31/03) (50)	—	(53)	(50)	—	(89)
Merger savings (91)	—	—	(25)	—	—
<b>Changes in accounting principles:</b>					
Repeal of EITF 98-10 (54)	—	29	—	—	—
Adoption of FIN 46 (30)	—	17	—	—	—
Impact of the repeal of EITF 98-10 (54)	—	(9)	—	—	(15)
Extraordinary item (48)	—	—	(16)	—	—
	\$ 859	\$ 532	\$ 498	\$ 1,361	\$ 856

### California Utility Operations

To understand the operations and financial results of the California Utilities, it is important to understand the ratemaking procedures to which they are subject.

The California Utilities are subject to various regulatory bodies and rules at national, state and local levels. The primary regulatory body is the CPUC, which regulates utility rates and operations. The Federal Energy Regulatory Commission (FERC) regulates interstate transportation of natural gas and electricity and various related matters. The Nuclear Regulatory Commission regulates nuclear generating plants. Municipalities and other local authorities regulate the location of utility assets, including natural gas pipelines and electric lines. Other business units are also subject to regulation by the FERC, various state commissions, local governmental entities, and various similar authorities in countries other than the United States.

California's electric utility industry was significantly affected by California's restructuring of the industry during 2000—2001. Beginning in mid-2000 and continuing into 2001, supply/demand imbalances and a number of other factors resulted in abnormally high electric commodity costs, leading to several legislative and regulatory responses, including a ceiling imposed on the cost of the electric commodity that SDG&E could pass on to its small-usage customers. To obtain adequate supplies of electricity, beginning in February 2001 and continuing through December 31, 2002, the DWR began purchasing power to fulfill the full net short position of the investor-owned utilities (IOUs), consisting of all electricity requirements of the IOUs' customers other than that provided by their existing generating facilities or their previously existing purchased-power contracts.

In 2003, the CPUC established the allocation of the power purchased by the DWR under long-term contracts for the IOUs' customers and the related cost responsibility among the IOUs for that power. In addition, the IOUs resumed their electric commodity procurement function for power requirements in excess of that provided by the DWR's contracts allocated to them. This is discussed further in Note 14 of the notes to Consolidated Financial Statements and under "Factors Influencing Future Performance."

The natural gas industry experienced an initial phase of restructuring during the 1980s by deregulating natural gas sales to noncore customers. Further restructuring continues to be considered, as discussed in Note 15 of the notes to Consolidated Financial Statements.

**Natural Gas Revenue and Cost of Natural Gas.** Natural gas revenues increased to \$4.5 billion in 2004 from \$4.0 billion in 2003, and the cost of natural gas increased to \$2.6 billion in 2004 from \$2.1 billion in 2003. The increases were primarily attributable to natural gas cost increases, which are passed on to customers. For natural gas revenues, this increase was offset by \$56 million of approved performance awards recognized during 2003, including \$49 million of natural gas procurement awards at SoCalGas. Performance awards are discussed in Note 15 of the notes to Consolidated Financial Statements. The company's weighted average cost per million British thermal units (mmbtu) of natural gas was \$5.94 in 2004, \$5.06 in 2003 and \$3.12 in 2002.

Under the current regulatory framework, the cost of natural gas purchased for customers and the variations in that cost are passed through to the customers on a substantially concurrent basis. However, SoCalGas' Gas Cost Incentive Mechanism (GCIM) allows SoCalGas to share in the savings or costs from buying natural gas for customers below or above market-based monthly benchmarks. The mechanism permits full recovery of all costs within a tolerance band above the benchmark price and refunds all savings within a tolerance band below the benchmark price. The costs or savings outside the tolerance band are shared between customers and shareholders. In addition, SDG&E's natural gas procurement Performance-Based Regulation (PBR) mechanism provides an incentive mechanism by measuring SDG&E's procurement of natural gas against a benchmark price comprised of monthly natural gas indices, resulting in shareholder rewards for costs achieved below the benchmark and shareholder penalties when costs exceed the benchmark. Further discussion is provided in Notes 1 and 15 of the notes to Consolidated Financial Statements.

Natural gas revenues increased to \$4.0 billion in 2003 from \$3.3 billion in 2002, and the cost of natural gas increased to \$2.1 billion in 2003 from \$1.4 billion in 2002. The change was primarily attributable to natural gas price increases, offset by reduced volumes. Revenues also increased due to the performance awards recognized during 2003.

**Electric Revenue and Cost of Electric Fuel and Purchased Power.** Electric revenues decreased to \$1,658 million in 2004 from \$1,787 million in 2003, and the cost of electric fuel and purchased power increased to \$0.6 billion in 2004 from \$0.5 billion in 2003. The decrease in revenues was due to more power being provided to SDG&E's customers by the DWR in 2004 as discussed in Note 14 of the

notes to Consolidated Financial Statements, offset by higher electric commodity costs. Additionally, 2003 revenue included the recognition of \$116 million related to the approved settlement of intermediate-term purchase power contracts in the third quarter of 2003 and higher earnings from PBR awards. Performance awards are discussed in Note 15 of the notes to Consolidated Financial Statements. The increased costs were primarily attributable to the higher electric commodity costs and higher volumes, offset by the increased power being provided by the DWR.

Electric revenues increased to \$1.8 billion in 2003 from \$1.3 billion in 2002, and the cost of electric fuel and purchased power increased to \$0.5 billion in 2003 from \$0.3 billion in 2002. The changes were attributable to several factors, including the effect of the DWR's purchasing the net short position of SDG&E during 2002, and higher electric commodity costs and volumes in 2003. In addition, the increase in revenue was due to the settlement of the intermediate-term purchase power contracts, higher PBR awards and the increase in authorized distribution revenue.

The tables below summarize the California Utilities' natural gas and electric volumes and revenues by customer class for the years ended December 31, 2004, 2003 and 2002.

**NATURAL GAS SALES, TRANSPORTATION & EXCHANGE**

(Dollars in millions, volumes in billion cubic feet)

	Natural Gas Sales		Transportation & Exchange		Total	
	Volumes	Revenue	Volumes	Revenue	Volumes	Revenue
<b>2004:</b>						
Residential	287	\$ 2,904	2	\$ 7	289	\$ 2,911
Commercial and industrial	126	1,013	276	198	402	1,211
Electric generation plants	—	2	252	90	252	92
Wholesale	—	—	20	6	20	6
	<b>413</b>	<b>\$ 3,919</b>	<b>550</b>	<b>\$ 301</b>	<b>963</b>	<b>4,220</b>
Balancing accounts and other						317
Total						<b>\$ 4,537</b>
<b>2003:</b>						
Residential	273	\$ 2,479	2	\$ 7	275	\$ 2,486
Commercial and industrial	121	863	277	189	398	1,052
Electric generation plants	—	3	241	79	241	82
Wholesale	—	—	20	4	20	4
	<b>394</b>	<b>\$ 3,345</b>	<b>540</b>	<b>\$ 279</b>	<b>934</b>	<b>3,624</b>
Balancing accounts and other						386
Total						<b>\$ 4,010</b>
<b>2002:</b>						
Residential	289	\$ 2,089	2	\$ 8	291	\$ 2,097
Commercial and industrial	117	635	294	183	411	818
Electric generation plants	—	—	264	43	264	43
Wholesale	—	—	16	12	16	12
	<b>406</b>	<b>\$ 2,724</b>	<b>576</b>	<b>\$ 246</b>	<b>982</b>	<b>2,970</b>
Balancing accounts and other						293
Total						<b>\$ 3,263</b>

**ELECTRIC TRANSMISSION AND DISTRIBUTION**  
(Dollars in millions, volumes in million kilowatt hours)

	2004		2003		2002	
	Volumes	Revenue	Volumes	Revenue	Volumes	Revenue
Residential	7,038	\$ 692	6,702	\$ 731	6,266	\$ 649
Commercial	6,592	644	6,263	674	6,053	633
Industrial	2,072	133	1,976	161	1,883	160
Direct access	3,441	105	3,322	87	3,448	117
Street and highway lighting	97	11	91	11	88	9
Off-system sales	—	—	8	—	5	—
	19,240	1,585	18,362	1,664	17,743	1,568
Balancing accounts and other		73		123		(286)
<b>Total</b>		<b>\$ 1,658</b>		<b>\$ 1,787</b>		<b>\$ 1,282</b>

Although commodity-related revenues from the DWR's purchasing of SDG&E's net short position or from the DWR's allocated contracts are not included in revenue (as explained in Note 1 of the notes to Consolidated Financial Statements), the associated volumes and distribution revenue are included in the above table.

**Other Operating Revenues and Cost of Sales.** These tables provide a breakdown of other operating revenues and cost of sales by business unit.

(Dollars in millions)	2004		2003		2002	
<b>OPERATING REVENUES</b>						
Sempra Commodities	\$ 1,680	52%	\$ 1,217	58%	\$ 910	60%
Sempra Generation*	1,647	51	773	37	437	29
Sempra Pipelines & Storage*	269	9	210	10	176	12
Sempra LNG	—	—	(2)	—	—	—
Total Sempra Global	3,596	112	2,198	105	1,523	101
Parent and Other**	(381)	(12)	(108)	(5)	(20)	(1)
<b>Total</b>	<b>\$ 3,215</b>	<b>100%</b>	<b>\$ 2,090</b>	<b>100%</b>	<b>\$ 1,503</b>	<b>100%</b>
<b>COST OF SALES</b>						
Sempra Commodities	\$ 597	34%	\$ 542	45%	\$ 293	41%
Sempra Generation	1,198	69	498	41	274	39
Sempra Pipelines & Storage	209	12	166	14	148	21
Total Sempra Global	2,004	115	1,206	100	715	101
Parent and Other**	(263)	(15)	(2)	—	(6)	(1)
<b>Total</b>	<b>\$ 1,741</b>	<b>100%</b>	<b>\$ 1,204</b>	<b>100%</b>	<b>\$ 709</b>	<b>100%</b>

\* Does not include the revenues of the unconsolidated affiliates that are part of this business unit.

\*\* Includes intercompany eliminations recorded in consolidation, including the Palomar plant in 2004 as discussed in Note 2 of the notes to Consolidated Financial Statements.

The increase in 2004 revenues compared to 2003 was primarily due to higher revenues at Sempra Generation resulting from increased volumes of power sales under the DWR contract, and higher revenues at Sempra Commodities resulting from increased commodity revenue, particularly from metals, natural gas and petroleum due to increased volatility and higher prices. The increase in cost of sales was primarily due to costs related to the higher sales volume for Sempra Generation.

The increases in 2003 compared to 2002 were primarily due to higher revenues at Sempra Commodities as the result of increased volumes and volatility in the energy commodity markets, as well as increased revenues from Sempra Generation's resumption of contract sales of electricity to the DWR in April 2002 and sales by its Twin Oaks power plant purchased in the fourth quarter of 2002.

**Other Operating Expenses.** This table provides a breakdown of other operating expenses by business unit.

(Dollars in millions)	2004		2003		2002	
<b>OTHER OPERATING EXPENSES</b>						
<b>California Utilities</b>						
Southern California Gas Company	\$ 950	40%	\$ 954	42%	\$ 872	46%
San Diego Gas & Electric	593	25	637	28	560	29
Total Utilities	1,543	65	1,591	70	1,432	75
<b>Sempra Global</b>						
Sempra Commodities	564	24	409	18	338	18
Sempra Generation	150	6	132	6	78	4
Sempra Pipelines & Storage	43	2	120	5	49	3
Sempra LNG	26	1	1	—	—	—
Total Sempra Global	783	33	662	29	465	25
Parent and Other*	45	2	34	1	4	—
<b>Total</b>	<b>\$ 2,371</b>	<b>100%</b>	<b>\$ 2,287</b>	<b>100%</b>	<b>\$ 1,901</b>	<b>100%</b>

\* Includes certain intercompany eliminations recorded in consolidation.

The increase in other operating expenses in 2004 was primarily the result of higher costs at Sempra Global, particularly at Sempra Commodities due to increased trading activity, start-up costs at Sempra LNG and higher costs at Sempra Generation due to new generating plants coming on line in 2003. Additionally, 2004 operating expenses include higher litigation costs. These increases were offset by a decrease at the California Utilities in 2004, primarily resulting from the favorable resolution of regulatory issues in 2004 and a \$75 million before-tax charge in 2003 for litigation costs and for losses associated with a sublease of portions of the SoCalGas headquarters building. Additionally, 2003 operating expenses at Sempra Pipelines & Storage include a \$77 million before-tax write-down of the carrying value of the assets of Frontier Energy, and operating costs in 2003 were affected by a \$24 million before-tax write-down of the carrying value of the assets of AEG, included in Parent and Other.

The increase in other operating expenses at the California Utilities in 2003 from 2002 was primarily the result of the charge for litigation costs and for losses associated with a sublease of portions of the SoCalGas headquarters building, and increased labor and employee benefits costs. A smaller portion of the increase was due to the California wildfires discussed in Note 15 of the notes to Consolidated Financial Statements, which primarily affected SDG&E and the costs of which are expected to be recovered in rates. General operating costs increased at Sempra Commodities due to the increased revenue activity and a full year's activities for the businesses acquired in 2002, at Sempra Generation due to the new power plants and at Sempra Pipelines & Storage due to the write-down of the carrying value of the assets of Frontier Energy. In addition, 2003 was impacted by the write-down of the carrying value of the assets of AEG and higher antitrust litigation costs at the Sempra Global companies.

**Other Income.** Other income, primarily equity earnings from unconsolidated subsidiaries and interest on regulatory balancing accounts, was \$104 million, \$26 million and \$15 million in 2004, 2003 and 2002, respectively. The increase in 2004 compared to 2003 was due to lower equity losses at Sempra Financial, increased equity earnings at Sempra Generation resulting from the acquisition of the Coletto

Creek coal plant, the \$15 million before-tax gain at SoCalGas from the sale of partnership property, the \$13 million before-tax gain on the settlement of an unpaid portion of the purchase price of the proposed Cameron LNG project for an amount less than the liability (which had been recorded as a derivative) and a \$7 million before-tax gain at Sempra Pipelines & Storage from the partial sale of Luz del Sur in 2004.

The increase for the 2003 year compared to 2002 was due to increased equity earnings at Sempra Pipelines & Storage and at other subsidiaries, and reduced balancing account interest expense, offset by higher 2002 operating results at Sempra Generation's joint ventures resulting from business interruption insurance proceeds received in 2002 related to an outage at the El Dorado plant during 2001.

**Interest Income.** Interest income was \$69 million, \$104 million and \$42 million in 2004, 2003 and 2002, respectively. The decrease in 2004 was due to \$59 million recorded as a result of the favorable resolution of income-tax issues with the Internal Revenue Service (IRS) in 2003, offset by interest recorded on income tax receivables in 2004. Additionally, the increase for 2003 compared to 2002 was due to the resolution of income tax issues in 2003.

**Interest Expense.** Interest expense was relatively unchanged at \$322 million, \$308 million and \$294 million in 2004, 2003 and 2002, respectively.

**Income Taxes.** Income tax expense was \$193 million, \$47 million and \$146 million in 2004, 2003 and 2002, respectively. The effective income tax rates were 17.3 percent, 6.3 percent and 20.2 percent, respectively. The change in income tax expense in 2004 was due primarily to higher taxable income and a \$9 million decrease in income tax credits from synthetic fuel investments, which are discussed in Note 8 of the notes to Consolidated Financial Statements. Additionally, 2003 was impacted by the favorable resolution of income-tax issues, which reduced income tax expense by \$83 million. Income before taxes in 2003 included \$59 million in interest income arising from the income tax settlement, resulting in an offsetting \$24 million income tax expense.

The changes in 2003 from 2002 were due primarily to the favorable resolution of income tax issues and a \$39 million increase in income tax credits from synthetic fuel investments, offset by a \$25 million favorable resolution of income tax issues at SDG&E in 2002.

**Discontinued Operations.** In the first quarter of 2004, Sempra Energy's board of directors approved management's plan to dispose of the company's interest in AEG, which marketed power and natural gas commodities to commercial and residential customers in the United Kingdom. Including the \$2 million loss on disposal, AEG's losses were \$25 million for the year ended December 31, 2004. Note 4 of the notes to Consolidated Financial Statements provides further details.

During 2003 and 2002, the company accounted for its investment in AEG under the equity method of accounting. As such, for the years ended December 31, 2003 and 2002, the company recorded its share of AEG's net losses, \$5 million and \$10 million, respectively, in Other Income, Net on the Statements of Consolidated Income. Effective December 31, 2003, AEG was consolidated as a result of the adoption of Financial Accounting Standards Board (FASB) Financial Interpretation No. (FIN) 46, Consolidation of Variable Interest Entities, as discussed in Note 1 of the notes to Consolidated Financial Statements.

**Net Income.** Changes in net income are summarized in the table shown previously under "Comparison of Earnings".

**Net Income by Business Unit****California Utilities**

The net income of the California Utilities was adversely affected by \$35 million in 2004 and \$32 million in 2003 of after-tax litigation costs, and favorably affected by \$55 million after tax in 2004 by the resolution of various regulatory issues as a result of the final decision on their 2004 cost of service proceedings. The litigation costs are primarily related to matters arising from the California energy crisis of 2000 — 2001. Resolution of the cost of service favorably impacted pension and other postretirement costs, income taxes and other matters in comparison to the assumptions used prior to January 1, 2004.

**Southern California Gas Company**

SoCalGas recorded net income of \$232 million, \$209 million and \$212 million in 2004, 2003 and 2002, respectively. In addition to the matters noted above, the increase in 2004 was due to higher margins and the gain on the sale of partnership property. Additionally, 2003 net income was also affected by losses associated with a long-term sublease of portions of its headquarters building, offset by the favorable resolution of income tax issues and by higher GCIM awards.

The decrease for 2003 compared to 2002 was due primarily to the litigation charges and sublease losses in 2003 and the end of sharing of merger savings (which favorably impacted earnings by \$17 million for the year ended December 31, 2002), offset by the resolution of income tax issues and higher GCIM awards in 2003.

**San Diego Gas & Electric**

SDG&E recorded net income of \$208 million, \$334 million and \$203 million, in 2004, 2003 and 2002, respectively. In addition to the matters noted above, the decrease in 2004 was primarily due to the favorable resolution of income tax issues in 2003, which positively affected 2003 earnings by \$79 million, income of \$65 million after-tax in 2003 related to the approved settlement of intermediate-term purchase power contracts (discussed in Note 14 of the notes to Consolidated Financial Statements); the 2003 Incremental Cost Incentive Pricing income for the San Onofre Nuclear Generation Station (SONGS) and higher performance awards in 2003, offset by higher electric transmission and distribution margin in 2004.

The increase in 2003 compared to 2002 was primarily due to more reductions in income tax expense in 2003 than in 2002 from favorable resolution of income tax issues, the approved settlement of the intermediate-term purchase power contracts, higher earnings from PBR awards, and higher electric transmission and distribution revenue. These factors were offset by the litigation costs and other operating expenses in 2003 and the end of sharing of the merger savings (which positively impacted earnings by \$8 million in 2002).



### Sempra Commodities

A summary of Sempra Commodities' trading margin by geographic region and product line follows:

Trading Margin (Dollars in millions)	2004		2003		2002	
<b>Geographical:</b>						
North America	\$ 689	67%	\$ 439	72%	\$ 400	71%
Europe and Asia	338	33	172	28	165	29
Total	\$ 1,027	100%	\$ 611	100%	\$ 565	100%
<b>Product Line:</b>						
Gas	\$ 314	31%	\$ 146	24%	\$ 170	30%
Power	166	16	137	22	191	34
Oil — crude and products	265	26	128	21	74	13
Metals	179	17	96	16	78	14
Other	103	10	104	17	52	9
Total	\$ 1,027	100%	\$ 611	100%	\$ 565	100%

Trading margin consists of net trading revenues less related costs (primarily brokerage, transportation and storage) plus or minus net interest income/expense.

The above amounts include the before-tax impact of its synthetic fuel credits of \$79 million, \$61 million and \$28 million in 2004, 2003 and 2002, respectively, which contributed \$29 million, \$23 million and \$11 million to net income in 2004, 2003 and 2002, respectively. Synthetic fuel credits are discussed in Note 8 of the notes to Consolidated Financial Statements.

Sempra Commodities recorded net income of \$320 million in 2004 compared to \$157 million in 2003 and \$149 million in 2002, excluding the negative impact of the cumulative effect of the change in accounting principle of \$29 million in 2003 and the extraordinary gain of \$16 million in 2002. The increase in 2004 was primarily attributable to higher trading margins, resulting from increased volatility of a trending nature in the markets, particularly for metals, natural gas and petroleum.

A summary of Sempra Commodities' net unrealized revenues for trading activities follows:

(Dollars in millions)	Years ended December 31,	
	2004	2003
Balance at beginning of year	\$ 347	\$ 270
Cumulative effect adjustment	—	(50)
Additions	1,606	830
Realized	(760)	(703)
Balance at end of year	\$ 1,193	\$ 347

The estimated fair values for Sempra Commodities' net unrealized trading assets as of December 31, 2004, and the periods during which unrealized revenues are expected to be realized, are (dollars in millions):

Source of fair value	Fair Market Value at December 31, 2004	Scheduled Maturity (in months)			
		0-12	13-24	25-36	>36
Prices actively quoted	\$ 844	\$ 788	\$ 12	\$ 10	\$ 34
Prices provided by other external sources	23	(14)	—	—	37
Prices based on models and other valuation methods	(21)	(20)	—	—	(1)
Over-the-counter (OTC) revenue*	846	754	12	10	70
Exchange contracts**	347	337	21	8	(19)
Total	\$ 1,193	\$ 1,091	\$ 33	\$ 18	\$ 51

\* The present value of net unrealized revenues to be received from outstanding OTC contracts.

\*\* Cash received associated with open Exchange contracts.

**Sempra Generation**

Sempra Generation recorded net income of \$137 million in 2004; \$71 million in 2003, excluding the favorable impact of the cumulative effect of the change in accounting principle of \$9 million; and \$42 million in 2002. The 2004 net income reflects a \$7 million loss at the portions of Sempra Energy Solutions that were reorganized into Sempra Generation at the end of 2004, as described in the "Introduction" to this section. The change in accounting principle is discussed further in Note 1 of the notes to Consolidated Financial Statements. The increase in 2004 was primarily because power sales under Generation's contract with the DWR were at lower levels in 2003 and prior years than in 2004 and future years. The increase in 2003 compared to 2002 was primarily due to higher volumes of power sales to the DWR, offset by increased interest expense and start-up expenses related to Sempra Generation's new power plants.

**Sempra Pipelines & Storage**

Net income for Sempra Pipelines & Storage was \$63 million, \$3 million and \$26 million for 2004, 2003 and 2002, respectively. 2003 net income was impacted by the charge recorded to write down the carrying value of assets at Frontier Energy, as previously discussed. Additionally, the increase for 2004 was due to higher earnings from the company's Gasoducto Bajanorte natural gas pipeline and a gain on the sale of a portion of its interests in Luz del Sur, a Peruvian electric utility, offset by the impact of changes in estimates for certain income tax issues. Both 2004 and 2003 were favorably impacted by the resolution of vendor disputes in Argentina.

The change in 2003 from 2002 was primarily due to the Frontier Energy impairment, offset by increased equity earnings from its South American joint ventures, a full year of earnings from the Gasaducto Bajanorte pipeline in Mexico, which began operations in September 2002, and the favorable resolution of vendor disputes in Argentina. A discussion of the Argentine economic issue is included in Notes 1 and 3 of the notes to Consolidated Financial Statements.

**Sempra LNG**

Sempra LNG recorded net losses of \$8 million and \$2 million, respectively, for the years ended December 31, 2004 and 2003. For 2004, operating costs were offset by income from the settlement of an unpaid portion of the purchase price of the proposed Cameron liquefied natural gas project for an amount less than the liability (which had been recorded as a derivative).

**Sempra Financial**

Sempra Financial recorded net income of \$36 million in 2004, \$41 million in 2003 and \$36 million in 2002. During the third quarter of 2004, Sempra Financial sold its alternative fuel investment, Carbontronics. The transaction has been accounted for under the cost recovery method, whereby future proceeds in excess of Carbontronics' carrying value will be recorded as income as received. As a result of this sale, Sempra Financial will not be recognizing Section 29 income tax credits in the future.

The change in 2004 net income was due primarily to a decrease in tax credits, primarily due to the sale of Carbontronics, offset by lower equity losses. The increase in 2003 was due to lower amortization expense, offset by increased equity losses from certain investments.

Section 29 income tax credits are discussed further in Note 8 of the notes to Consolidated Financial Statements. Whether Sempra Financial will invest in additional affordable-housing properties will depend on Sempra Energy's income tax position.

**Parent and Other**

Net losses for Parent and Other were \$68 million, \$118 million and \$93 million in 2004, 2003 and 2002, respectively. Net losses consist primarily of interest expense and, for 2004, include the \$27 million after-tax impact of litigation costs, offset by a reduced estimate of federal and state income tax liabilities for certain prior years. Additionally, 2003 losses include the \$21 million after-tax write down of the carrying value of the assets of AEG in 2003.

The increase in 2003 losses compared to 2002 was due to the write-down of the carrying value of the assets of AEG and higher interest expense as a result of the issuance of \$1 billion of long-term notes in April 2002 and early 2003. The adoption of FIN 46 and the resulting consolidation of AEG is discussed in Note 1 of the notes to Consolidated Financial Statements.

**Book Value Per Share**

Book value per share was \$20.77, \$17.17 and \$13.79, at December 31, 2004, 2003 and 2002, respectively. The increases in 2004 and 2003 were primarily the result of comprehensive income's exceeding the dividends, and the sale of additional shares of common stock for a per-share price in excess of its book value.

**CAPITAL RESOURCES AND LIQUIDITY**

The company's California Utility operations are the major source of liquidity. Funding of other business units' capital expenditures is significantly dependent on the California Utilities paying sufficient dividends to Sempra Energy, which are expected to provide significant cash flow in 2005, and on Sempra Commodities' liquidity requirements, which can fluctuate significantly.

At December 31, 2004, the company had \$419 million in unrestricted cash and \$4.5 billion in available unused, committed lines of credit to provide liquidity and support commercial paper. At December 31, 2004, \$34 million of these lines supported variable-rate debt.

Management believes that these amounts and cash flows from operations and debt issuances will be adequate to finance capital expenditures and meet liquidity requirements and fund shareholder dividends, any new business acquisitions or start-ups, and other commitments. Forecasted capital expenditures for the next five years are discussed in "Future Construction Expenditures and Investments." If cash flows from operations were to be significantly reduced or the company were to be unable to issue new securities under acceptable terms, neither of which is considered likely, the company would be required to reduce non-utility capital expenditures, trading operations and investments in new businesses. Management continues to regularly monitor the company's ability to finance the needs of its operating, financing and investing activities in a manner consistent with its intention to maintain strong, investment-quality credit ratings. Rating agencies and others that evaluate a company's liquidity generally consider a company's capital expenditures and working capital requirements in comparison to cash from operations, available credit lines and other sources available to meet liquidity requirements.

At the California Utilities, cash flows from operations and from security issuances are expected to continue to be adequate to meet utility capital expenditure requirements and provide dividends to Sempra Energy. In June 2004, SDG&E received CPUC approval of its intended 2006 purchase from Sempra Generation of the 550-megawatt (MW) Palomar generating facility being constructed in Escondido, California. As a result, the level of SDG&E's dividends to Sempra Energy is expected to be significantly lower during the construction of the facility to enable SDG&E to increase its equity in preparation for the purchase of the completed facility. Note 2 of the notes to Consolidated Financial Statements provides additional discussion on the Palomar plant.

Sempra Commodities provides or requires cash as the level of its net trading assets fluctuates with prices, volumes, margin requirements (which are substantially affected by credit ratings and commodity price fluctuations) and the length of its various trading positions. Its status as a source or use of cash also varies with its level of borrowing from its own sources, including the credit line described below in "Cash Flows From Financing Activities." Sempra Commodities' intercompany borrowings were \$421 million at December 31, 2004, and \$359 million at December 31, 2003. Sempra Commodities' external debt was \$161 million at December 31, 2004. It had no external debt outstanding at December 31, 2003. Company management continuously monitors the level of Sempra Commodities' cash requirements in light of the company's overall liquidity. Such monitoring includes the procedures discussed in "Market Risk."

Sempra Generation's completed projects were financed through a combination of project financing, funds from the company and external borrowings. Existing and future projects are expected to be financed from Sempra Generation's cash from operations, project financing and funds from the company.

Sempra Generation's energy contracts typically contain collateral requirements related to credit lines. The collateral arrangements provide for Sempra Generation and/or the counterparty to post cash, guarantees or letters of credit to the other party for exposure in excess of established thresholds. Sempra Generation may be required to provide collateral when market price movements adversely affect the counterparty's cost of replacement energy supplies were Sempra Generation to fail to deliver the contracted amounts. As of December 31, 2004, Sempra Generation had outstanding collateral requirements under these contracts of \$139 million, of which \$81 million had been remitted.

Sempra Pipelines & Storage is expected to require funding from the company and/or external sources to continue the expansion of its existing natural gas distribution operations in Mexico and its planned development of pipelines and storage to serve LNG facilities expected to be developed in Baja California, Mexico; Louisiana and Texas, as discussed in Note 2 of the notes to Consolidated Financial Statements.

Sempra LNG will require funding for its planned development of LNG receiving facilities. While Sempra LNG's \$1.25 billion credit facility is expected to be adequate for these requirements, the company may decide to use project financing if that is believed to be advantageous.

In the longer term, Sempra Financial is expected to again be a net provider of cash through reductions of consolidated income tax payments resulting from its investments in affordable housing. However, that was not true in 2003 and 2004, and will not be true in the near term, while the company is in an alternative minimum tax position.

#### **CASH FLOWS FROM OPERATING ACTIVITIES**

Net cash provided by operating activities totaled \$949 million, \$1.1 billion and \$1.4 billion for 2004, 2003 and 2002, respectively.

The 2004 decrease in net cash provided by operating activities was due to an increase in net trading assets in 2004 compared to a decrease in 2003, increased deposits with customers and a higher increase in accounts receivable in 2004, offset by an increase in overcollected regulatory balancing accounts at SoCalGas in 2004 compared to a decrease in 2003, higher net income and higher accounts payable in 2004.

The decrease in cash flows from operations in 2003 compared to 2002 was primarily attributable to changes in regulatory balancing accounts at the California Utilities, offset by higher accounts payable in 2003 primarily due to timing.

During 2004, the company made pension plan and other postretirement benefit plan contributions of \$27 million and \$50 million, respectively.

#### **CASH FLOWS FROM INVESTING ACTIVITIES**

Net cash used in investing activities totaled \$559 million, \$1.2 billion and \$1.7 billion for 2004, 2003 and 2002, respectively.

The decrease in cash used in investing activities between 2004 and 2003 was primarily attributable to proceeds from the sale of U.S. Treasury obligations that previously securitized the Mesquite synthetic lease. The collateral was no longer necessary, since Sempra Generation bought out the lease in January 2004. The decrease in cash used in investing activities was also due to lower investments in Elk Hills (completed in 2003) and reduced capital spending for the completed Termoeléctrica de Mexicali (TDM) and Mesquite power plants, offset by investments made in Topaz Power Partners (Topaz) in 2004. In addition, the company received proceeds of \$157 million from the disposal of AEG's discontinued operations.

The decrease in cash used in investing activities in 2003 compared to 2002 was primarily due to lower capital expenditures for the TDM and Twin Oaks power plants, lower investments in U.S. Treasury obligations made in connection with the Mesquite synthetic lease, higher distributions from investments in South America, and Sempra Commodities' acquisition activities in 2002.

Expenditures for property, plant and equipment, and for those investments that effectively constitute similar expenditures, are presented in the following table.

(Dollars in millions)	
2004	\$ 1,157
2003	\$ 1,228
2002	\$ 1,524
2001	\$ 1,179
2000	\$ 963

The 2002 amount is larger than the other years due to the construction of the Sempra Generation power plants.

#### **Capital Expenditures for Property, Plant and Equipment**

Capital expenditures were \$1.1 billion in 2004 compared with \$1.0 billion in 2003 and \$1.2 billion in 2002. The decrease in 2003 from 2002 was due primarily to lower capital expenditures for the TDM and Twin Oaks power plants.

#### **The California Utilities**

Capital expenditures for property, plant, and equipment by the California Utilities were \$725 million in 2004 compared to \$762 million in 2003 and \$731 million in 2002. The higher amount in 2003 was primarily attributable to \$40 million of capital costs associated with the Southern California wildfires in October 2003.

#### **Sempra Generation**

Sempra Generation is primarily in the business of acquiring, developing and operating power plants throughout the U.S. and Mexico. The following table lists the MW capacity of each operating power

plant. All of the plants are natural gas-fired facilities, except for Coletto Creek Power and Twin Oaks Power, which are coal-fired, and a small hydroelectric plant.

Power Plant	Maximum Generating Capacity (MW)	Location
<b>Pacific Southwest:</b>		
Mesquite Power	1,250	Arlington, AZ
Termoelectrica de Mexicali (TDM)	625	Mexicali, Baja California, Mexico
Elk Hills Power (50% owned)	275*	Bakersfield, CA
El Dorado (50% owned)	240*	Boulder City, NV
	<u>2,390</u>	
<b>Texas:</b>		
Coletto Creek Power (50% owned)	316*	Goliad County, TX
Twin Oaks Power	305	Bremond, TX
Five other active Topaz Power Partners power plants (50% owned)	659*	South Central, TX
	<u>1,280</u>	
Total MW in operation	<u>3,670</u>	

\* Sempra Generation's share

Additional information concerning Sempra Generation's facilities is provided in Notes 2, 3 and 16 of the notes to Consolidated Financial Statements.

#### **Sempra LNG**

Sempra LNG develops, builds and operates LNG receipt terminals. Information concerning its projects in Baja California, Mexico; Louisiana and Texas is provided in Note 2 of the notes to Consolidated Financial Statements. The following additional matters are in process at the present time:

In January 2005, Sempra LNG signed a Heads of Agreement that will provide Tractebel LNG North America LLC with up to one-third (between 325 and 500 million cubic feet per day) of the processing capacity of the Cameron LNG facility. The non-binding agreement contemplates finalizing a definitive 20-year capacity agreement in 2005.

In January 2005, Sempra LNG was awarded a 15-year natural gas supply contract for 130 million cubic feet per day beginning in 2008. The contract supports Mexico's state-owned electric utility's future energy needs in northern Baja California and it is anticipated that it will use natural gas processed at Energia Costa Azul.

In December 2004, Sempra LNG entered into a non-binding development agreement with Alaska Gasline Port Authority to jointly consider and analyze the feasibility of building a proposed 800-mile gas pipeline from Alaska's North Slope to Valdez, where a gas liquefaction facility could be developed to export LNG to the western United States. The All-Alaska Gas Pipeline Project could be ready to deliver LNG to the West Coast receipt facilities as early as 2011. Whether the project will proceed and, if so, the ultimate extent of the company's participation are not determinable at this time.

#### **Sempra Pipelines & Storage**

Note 2 of the notes to Consolidated Financial Statements provides information concerning expenditures by Sempra Pipelines & Storage for its natural gas distribution systems in Mexico and its natural gas pipelines and storage facilities.

**Sempra Commodities**

Note 2 of the notes to Consolidated Financial Statements provides discussion of Sempra Commodities' expenditures for its Bluewater natural gas storage facility.

**Investments**

Investments and acquisition costs were \$74 million, \$202 million and \$429 million for 2004, 2003 and 2002, respectively. The decrease in 2004 was due to the sale of U.S. Treasury obligations purchased in connection with the Mesquite synthetic lease and lower investments in Elk Hills, offset by investments made in Topaz in 2004. The decrease in 2003 was due to lower investments in U.S. Treasury obligations made in connection with the Mesquite synthetic lease in 2003 compared to 2002 and Sempra Commodities' acquisition activities in 2002. A discussion of the synthetic lease is provided in Note 2 of the notes to Consolidated Financial Statements.

**Sempra Generation**

Information concerning Sempra Generation's investments in Topaz, and the El Dorado and Elk Hills power plants is provided in Note 3 of the notes to Consolidated Financial Statements. In February 2005, Sempra Generation announced its intention to add 600 MW of capacity to its Twin Oaks coal-fired generating plant in Texas.

**Sempra Pipelines & Storage**

Discussion of investing activities by Sempra Pipelines & Storage, including the \$198 million cumulative foreign currency exchange adjustment relating to Argentina, is provided in Note 3 of the notes to Consolidated Financial Statements.

**Future Construction Expenditures and Investments**

The company expects to make capital expenditures of \$1.6 billion in 2005. Significant capital expenditures are expected to include \$900 million for California utility plant improvements, \$150 million for Palomar (discussed in Note 2 of the notes to Consolidated Financial Statements) and \$300 million for the development of LNG regasification terminals. These expenditures are expected to be financed by cash flows from operations and debt issuances.

Over the next five years, the company expects to make capital expenditures of \$5 billion at the California Utilities, and has identified \$3.3 billion of capital expenditures at the other subsidiaries, including the development of the LNG facilities and pipelines, and construction of power plants by Sempra Generation. The former amount includes \$500 million for Palomar, which is being constructed by Sempra Generation and which will be purchased by SDG&E when completed in 2006.

Construction, investment and financing programs are periodically reviewed and revised by the company in response to changes in regulation, economic conditions, competition, customer growth, inflation, customer rates, the cost of capital and environmental requirements as discussed in Note 16 of the notes to Consolidated Financial Statements. In addition, the excess of existing power plants and other energy-related facilities compared to market demand in certain regions of the country and/or the plants that are owned by companies in financial distress may provide the company with opportunities to acquire existing power plants instead of or in addition to new construction.

The company's level of construction expenditures and investments in the next few years may vary substantially, and will depend on the availability of financing and business opportunities providing desirable rates of return. The company intends to finance its capital expenditures in a manner that will maintain its strong investment-grade ratings and capital structure.

## CASH FLOWS FROM FINANCING ACTIVITIES

Net cash (used in) provided by financing activities totaled \$(380) million, \$89 million and \$137 million for 2004, 2003 and 2002, respectively.

The 2004 increase in cash used in financing activities was due to higher payments on long-term debt and lower issuances of common stock, offset by an increase in short-term debt. The cash provided by financing activities decreased in 2003 due to reduced long-term borrowings and higher repayments on long-term debt and short-term borrowings, offset by an increase in stock issuances.

### Long-Term and Short-Term Debt

During 2004, the company's long-term debt decreased \$684 million to \$4.6 billion. At December 31, 2004, the company's long-term debt had a weighted average life to maturity of 8.7 years and a weighted average interest rate of 5.6 percent. In 2004, the company issued \$997 million in long-term debt.

In May 2004, the company issued \$600 million of senior unsecured notes, consisting of \$300 million of 4.75-percent fixed-rate, five-year notes and \$300 million of four-year, floating-rate notes. The proceeds of the issuance were used to repay \$500 million of debt maturing July 1, 2004, and for general corporate purposes.

In June 2004, SDG&E issued \$251 million of first mortgage bonds and applied the proceeds in July to refund an identical amount of first mortgage bonds and related tax-exempt industrial development bonds of a shorter maturity. The bonds secure the repayment of tax-exempt industrial development bonds of an identical amount, maturity and interest rate issued by the City of Chula Vista, the proceeds of which were loaned to SDG&E and which are repaid with payments on the first mortgage bonds. The bonds were initially issued as auction-rate securities, but SDG&E entered floating-for-fixed interest-rate swap agreements that effectively changed the bonds' interest rates to fixed rates in September 2004. The swaps are set to expire in 2009.

In December 2004, SoCalGas issued \$100 million of floating rate first mortgage bonds maturing in December 2009. The interest rate is based on the 3-month LIBOR rate plus 0.17%.

Repayments on long-term debt in 2004 included the \$500 million of notes payable that matured in July 2004, \$426 million of first mortgage bonds and \$66 million of rate-reduction bonds. Also in 2004, Sempra Generation purchased the assets of Mesquite Trust, thereby extinguishing \$630 million of debt outstanding, and Sempra Financial repaid \$34 million of debt incurred to acquire limited partnership interests.

In 2003, the company issued \$900 million in long-term debt, consisting of \$400 million of senior unsecured notes and \$500 million of first mortgage bonds issued by SoCalGas.

Repayments on long-term debt in 2003 included \$100 million of the borrowings under a line of credit and \$66 million of rate-reduction bonds. In 2003, Sempra Financial repaid \$36 million of debt incurred to acquire limited partnership interests. Repayments also included \$325 million of SoCalGas' first mortgage bonds. In addition, \$70 million of SoCalGas' \$75 million medium-term notes were put back to the company.

In 2002, the company issued \$1.2 billion in long-term debt, including \$600 million of equity units at Sempra Energy and \$250 million of 4.80% first mortgage bonds at SoCalGas. Each equity unit consists of \$25 principal amount of the company's 5.60% senior notes due May 17, 2007 and a contract to purchase for \$25 on May 17, 2005, between .8190 and .9992 of a share of the company's common stock, with the precise number within that range to be determined by the average market price. In addition, Sempra Generation drew down \$300 million against a line of credit to finance construction projects and acquisitions.



Repayments on long-term debt in 2002 of \$479 million included \$200 million borrowed under a line of credit, \$138 million of first mortgage bonds and \$66 million of rate-reduction bonds.

In May 2004, the California Utilities obtained a combined \$500 million three-year syndicated revolving credit facility to replace their expiring 364-day facility of a like amount. No amounts were outstanding under this facility at December 31, 2004. SoCalGas had \$30 million of commercial paper outstanding at December 31, 2004.

In May 2004, the company entered into an interest-rate swap agreement that effectively changed the interest rate on \$300 million of 7.95% notes (issued in February 2000) from fixed to floating. The swap is set to expire in 2010, the same year the related debt matures.

In June 2004, Sempra Commodities obtained a two-year syndicated revolving line of credit providing for extensions of credit (consisting of borrowings, letters of credit and other credit support accommodations) to Sempra Commodities and certain of its affiliates of up to \$1 billion. At December 31, 2004, outstanding extensions of credit under the facility totaled \$489 million, of which \$439 million was in the form of letters of credit.

In July 2004, Sempra Global obtained a \$1.5 billion three-year syndicated revolving credit facility to replace its expiring \$500 million revolving credit facility and the expiring \$400 million revolving credit facility of Sempra Generation. Sempra Global continues to have a substantially identical \$500 million three-year revolving credit facility that expires in 2006. Sempra Global had \$36 million outstanding under these lines at December 31, 2004. Sempra Global also had \$220 million of commercial paper, guaranteed by Sempra Energy, outstanding at December 31, 2004. There was no commercial paper outstanding at December 31, 2003.

In September 2004, Pacific Enterprises (PE) extended the termination date of its revolving credit agreement to September 30, 2005 and increased the revolving credit commitment from \$250 million to \$500 million. No amounts were outstanding under this facility at December 31, 2004.

In December 2004, Sempra LNG obtained a \$1.25 billion five-year syndicated revolving credit facility. The \$1.25 billion also provides for the issuance of letters of credit not exceeding \$200 million outstanding at any one time. No amounts were outstanding under this facility at December 31, 2004.

Notes 5 and 6 of the notes to Consolidated Financial Statements provide further discussion of debt activity and lines of credit.

#### **Capital Stock Transactions**

On October 14, 2003, the company completed a common stock offering of 16.5 million shares priced at \$28 per common share, resulting in net proceeds of \$448 million. The proceeds were used primarily to pay off short-term debt.

In April and May of 2002, the company publicly offered and sold \$600 million of equity units, as discussed in Note 13 of the notes to Consolidated Financial Statements. In February 2005, the company remarketed the senior notes included in the equity units for their remaining term at a rate of 4.62%.

In March 2000, the company's board of directors authorized the optional expenditure of up to \$100 million to repurchase shares of common stock from time to time in the open market or in privately negotiated transactions. Under this authorization, the company acquired 162,400 shares in 2000, 60,000 shares in 2001 and 674,400 shares in 2002.

**Dividends**

Dividends paid on common stock were \$195 million in 2004, \$182 million in 2003 and \$201 million in 2002. On February 18, 2005, the company's board of directors approved an increase in the quarterly dividend from \$0.25 per share to \$0.29 per share.

The payment and amount of future dividends are within the discretion of the company's board of directors. The CPUC's regulation of the California Utilities' capital structure limits the amounts that are available for loans and dividends to the company from the California Utilities. At December 31, 2004, SDG&E and SoCalGas could have provided a total (combined loans and dividends) of \$160 million and \$200 million, respectively, to Sempra Energy.

**Capitalization**

Total capitalization, including short-term debt and the current portion of long-term debt and excluding the rate-reduction bonds (which are non-recourse to the company), at December 31, 2004 was \$9.8 billion. The debt-to-capitalization ratio was 49 percent at December 31, 2004. Significant changes affecting capitalization during 2004 included common stock issuances, long-term borrowings and repayments, short-term borrowings, income and dividends.

**Commitments**

The following is a summary of the company's principal contractual commitments at December 31, 2004. Trading liabilities are not included herein as such derivative transactions are primarily offset by trading assets. In addition, liabilities reflecting fixed-price contracts and other derivatives are excluded as they are primarily offset against regulatory assets at the California Utilities. Additional information concerning commitments is provided above and in Notes 5, 6, 9, 12 and 16 of the notes to Consolidated Financial Statements.

(Dollars in millions)	2005	2006 and 2007	2008 and 2009	Thereafter	Total
Short-term debt	\$ 405	\$ —	\$ —	\$ —	\$ 405
Long-term debt	398	785	735	2,672	4,590
Interest on debt (1)	236	393	313	853	1,795
Due to unconsolidated affiliates	205	—	62	100	367
Preferred stock of subsidiaries subject to mandatory redemption	2	2	17	—	21
Operating leases	107	190	166	178	641
Purchased-power contracts	256	592	701	4,035	5,584
Natural gas contracts	1,099	481	41	189	1,810
Construction commitments	356	401	16	49	822
Topaz Power Partners guarantee	75	—	—	—	75
Twin Oaks coal supply	31	55	54	285	425
SONGS decommissioning	16	13	4	295	328
Other asset retirement obligations	5	9	1	5	20
Pension and postretirement benefit obligations (2)	217	477	510	1,463	2,667
Environmental commitments	18	36	—	—	54
Other	24	50	52	249	375
<b>Totals</b>	<b>\$ 3,450</b>	<b>\$ 3,484</b>	<b>\$ 2,672</b>	<b>\$ 10,373</b>	<b>\$ 19,979</b>

(1) Based on rates in effect at December 31, 2004.

(2) Amounts are before reduction for the Medicare Part D subsidy and only include expected payments for the next 10 years.

**Credit Ratings**

Credit ratings of the company and its principal subsidiaries remained unchanged at investment grade levels in 2004. As of January 31, 2005, credit ratings for Sempra Energy and its principal subsidiaries were as follows:

	Standard & Poor's	Moody's Investor Services, Inc.	Fitch
<b>SEMPRA ENERGY</b>			
Unsecured debt	BBB+	Baa1	A
Trust preferred securities	BBB-	Baa2	A-
<b>SDG&amp;E</b>			
Secured debt	A+	A1	AA
Unsecured debt	A-	A2	AA-
Preferred stock	BBB+	Baa1	A+
Commercial paper	A-1	P-1	F1+
<b>SOCALGAS</b>			
Secured debt	A+	A1	AA
Unsecured debt	A-	A2	AA-
Preferred stock	BBB+	Baa1	A+
Commercial paper	A-1	P-1	F1+
<b>PACIFIC ENTERPRISES</b>			
Preferred stock	BBB+	—	A
<b>SEMPRA GLOBAL</b>			
Unsecured debt guaranteed by Sempra Energy	—	Baa1	—
Commercial paper guaranteed by Sempra Energy	A-2	P-2	F1

As of January 31, 2005, the company has a stable outlook rating from all three credit rating agencies. During 2004, Standard & Poor's implemented new standards to assess liquidity requirements under certain predetermined stress scenarios, primarily related to Sempra Commodities. Participation in this program has not affected Standard & Poor's ratings of the company.

**FACTORS INFLUENCING FUTURE PERFORMANCE**

The California Utilities' and Sempra Generation's long-term contracts generally provide relatively stable earnings, while Sempra Generation, Sempra Pipelines & Storage and Sempra LNG provide opportunities for earnings growth and Sempra Commodities experiences significant volatility in earnings. Notes 14 through 16 of the notes to Consolidated Financial Statements also describe matters that could affect future performance.

**Litigation**

Note 16 describes significant litigation against the company, primarily cases arising from the California energy crisis and Sempra Generation's contract with the DWR.

**California Utilities**

Notes 14, 15 and 16 of the notes to Consolidated Financial Statements describe electric and natural gas restructuring and rates, the recent cost of service proceedings, and the CPUC's investigations of natural gas prices at the California-Arizona border.

**Sempra Global****Electric-Generation Assets**

As discussed in Note 2 of the notes to Consolidated Financial Statements, the company is involved in the expansion of its electric-generation capabilities, including the acquisition of the plants that now comprise Topaz, which will affect the company's future performance.

**Investments**

As discussed in "Cash Flows From Investing Activities," the company's investments will significantly impact the company's future performance.

Sempra LNG is in the process of developing Energía Costa Azul, an LNG receiving terminal in Baja California, Mexico; the Cameron LNG receiving terminal in Louisiana; and the Port Arthur LNG receiving terminal in Texas. In addition, in December 2004, Sempra LNG entered into a non-binding development agreement with Alaska Gasline Port Authority to jointly consider and analyze the feasibility of building a proposed 800-mile gas pipeline from Alaska's North Slope to Valdez, where a gas liquefaction facility could be developed to export LNG to the rest of North America. The future profitability of this business unit is dependent upon numerous factors, including the quantities of and relative prices of natural gas in North America and from LNG suppliers located elsewhere, negotiating sale and supply contracts at adequate margins, acquiring all necessary permits and completing cost-effective construction of the required facilities. Additional information regarding these activities is provided above in "Cash Flows From Investing Activities" and in Note 2 of the notes to Consolidated Financial Statements.

Beginning in 2003, the company started expanding its natural gas storage capacity by developing Bluewater Gas Storage, LLC, located in Michigan. In April 2004, the company announced the acquisition of land and associated rights for the development of a salt-cavern natural gas storage facility in Evangeline Parish, Louisiana, operating as the Pine Prairie Energy Center. In July 2004, the company announced that it had acquired the rights to develop Liberty Gas Storage, a salt-cavern gas storage facility located in Calcasieu Parish, Louisiana. Additional information regarding these activities is provided in Note 2 of the notes to Consolidated Financial Statements.

The Argentine economic decline and government responses (including Argentina's unilateral, retroactive abrogation of utility agreements early in 2002) are continuing to adversely affect the company's investment in two Argentine utilities. Information regarding this situation is provided in Notes 3 and 16 of the notes to Consolidated Financial Statements.

**Market Risk**

Market risk is the risk of erosion of the company's cash flows, net income, asset values and equity due to adverse changes in prices for various commodities, and in interest and foreign-currency rates.

The company has adopted corporate-wide policies governing its market risk management and trading activities. Assisted by the company's Energy Risk Management Group (ERMG), the company's Energy Risk Management Oversight Committee (ERMOC), consisting of senior officers, oversees company-wide energy risk management activities and monitors the results of trading and other activities to ensure compliance with the company's stated energy risk management and trading policies. Utility management receives daily information on positions and the ERMG receives information detailing positions creating market and credit risk from all company affiliates (on a delayed basis as to the California Utilities). The ERMG independently measures and reports the market and credit risk

associated with these positions. In addition, the company's subsidiaries have groups that monitor energy price risk management and trading activities independently from the groups responsible for creating or actively managing these risks.

Along with other tools, the company uses Value at Risk (VaR) to measure its exposure to market risk. VaR is an estimate of the potential loss on a position or portfolio of positions over a specified holding period, based on normal market conditions and within a given statistical confidence interval. The company has adopted the variance/covariance methodology in its calculation of VaR, and uses both the 95-percent and 99-percent confidence intervals. VaR is calculated independently by the ERMG for company subsidiaries. Historical volatilities and correlations between instruments and positions are used in the calculation.

Following is a summary of Sempra Commodities' trading VaR profile (using a one-day holding period) in millions of dollars:

	95%	99%
<b>December 31, 2004</b>	<b>\$8.0</b>	<b>\$11.3</b>
<b>2004 range</b>	<b>\$2.8 to \$ 18.7</b>	<b>\$3.9 to \$ 26.1</b>
December 31, 2003	\$2.6	\$3.7
2003 range	\$2.2 to \$ 34.0	\$3.1 to \$ 47.6

The California Utilities use energy and natural gas derivatives to manage natural gas and energy price risk associated with servicing their load requirements. The use of derivative financial instruments by the California Utilities is subject to certain limitations imposed by company policy and regulatory requirements.

Revenue recognition is discussed in Notes 1 and 11 and the additional market risk information regarding derivative instruments is discussed in Note 11 of the notes to Consolidated Financial Statements.

The following discussion of the company's primary market risk exposures as of December 31, 2004 includes a discussion of how these exposures are managed.

#### **Commodity Price Risk**

Market risk related to physical commodities is created by volatility in the prices and basis of certain commodities. The company's market risk is impacted by changes in volatility and liquidity in the markets in which these commodities or related financial instruments are traded. The company's various affiliates are exposed, in varying degrees, to price risk, primarily in the petroleum, metals, natural gas and electricity markets. The company's policy is to manage this risk within a framework that considers the unique markets, and operating and regulatory environments of each affiliate.

#### **Sempra Commodities**

Sempra Commodities derives most of its revenue from its worldwide trading activities in natural gas, electricity, petroleum products, metals and other commodities. As a result, Sempra Commodities is exposed to price volatility in the related domestic and international markets. Sempra Commodities conducts these activities within a structured and disciplined risk management and control framework that is based on clearly communicated policies and procedures, position limits, active and ongoing management monitoring and oversight, clearly defined roles and responsibilities, and daily risk measurement and reporting.

**California Utilities**

With respect to the California Utilities, market risk exposure is limited due to CPUC-authorized rate recovery of the costs of commodity purchase, sale, intrastate transportation and storage activity. However, the California Utilities may, at times, be exposed to market risk as a result of SDG&E's natural gas PBR and electric procurement activities or SoCalGas' GCIM, which are discussed in Note 15 of the notes to Consolidated Financial Statements. If commodity prices were to rise too rapidly, it is likely that volumes would decline. This would increase the per-unit fixed costs, which could lead to further volume declines. The California Utilities manage their risk within the parameters of the company's market risk management framework. As of December 31, 2004, the total VaR of the California Utilities' natural gas and electric positions was not material.

**Interest Rate Risk**

The company is exposed to fluctuations in interest rates primarily as a result of its long-term debt. The company historically has funded utility operations through long-term debt issues with fixed interest rates and these interest rates are recovered in utility rates. Some recent debt offerings have used a combination of fixed-rate and floating-rate debt. Subject to regulatory constraints, interest-rate swaps may be used to adjust interest-rate exposures.

At December 31, 2004, the California Utilities had \$1.7 billion of fixed-rate debt and \$0.3 billion of variable-rate debt. Interest on fixed-rate utility debt is fully recovered in rates on a historical cost basis and interest on variable-rate debt is provided for in rates on a forecasted basis. At December 31, 2004, utility fixed-rate debt had a one-year VaR of \$214 million and utility variable-rate debt had a one-year VaR of \$11 million. Non-utility debt (fixed-rate and variable-rate) subject to VaR modeling totaled \$2.6 billion at December 31, 2004, with a one-year VaR of \$101 million.

At December 31, 2004, the notional amount of interest-rate swap transactions totaled \$701 million. Note 6 of the notes to Consolidated Financial Statements provides further information regarding interest-rate swap transactions.

In addition, the company is ultimately subject to the effect of interest-rate fluctuation on the assets of its pension plan and other postretirement plans.

**Credit Risk**

Credit risk is the risk of loss that would be incurred as a result of nonperformance by counterparties of their contractual obligations. As with market risk, the company has adopted corporate-wide policies governing the management of credit risk. Credit risk management is performed by the ERMG and the California Utilities' credit department and overseen by the ERMOC. Using rigorous models, the ERMG and the company calculate current and potential credit risk to counterparties on a daily basis and monitor actual balances in comparison to approved limits. The company avoids concentration of counterparties whenever possible, and management believes its credit policies associated with counterparties significantly reduce overall credit risk. These policies include an evaluation of prospective counterparties' financial condition (including credit ratings), collateral requirements under certain circumstances, the use of standardized agreements that allow for the netting of positive and negative exposures associated with a single counterparty, and other security such as lock-box liens and downgrade triggers. At December 31, 2004, Sempra Commodities' 20 largest customers had balances of \$21 million to \$80 million each. The company believes that adequate reserves have been provided for counterparty nonperformance.

As described in Note 16 of the notes to Consolidated Financial Statements, Sempra Generation has a contract with the DWR to supply up to 1,900 MW of power to the state of California over 10 years,

beginning in 2001. This contract results in a significant potential nonperformance exposure with a single counterparty; however, this risk has been addressed and mitigated by the terms of the contract.

The developing LNG projects will result in significant reliance on the credit-worthiness of its major suppliers and customers of those projects.

The company monitors credit risk through a credit approval process and the assignment and monitoring of credit limits. These credit limits are established based on risk and return considerations under terms customarily available in the industry.

The company periodically enters into interest-rate swap agreements to moderate exposure to interest-rate changes and to lower the overall cost of borrowing. The company would be exposed to interest-rate fluctuations on the underlying debt should counterparties to the agreement not perform. Additional information regarding the company's use of interest-rate swap agreements is provided above under "Interest Rate Risk".

#### **Foreign Currency Rate Risk**

The company has investments in entities whose functional currency is not the U.S. dollar, which exposes the company to foreign exchange movements, primarily in Latin American currencies. As a result of the devaluation of the Argentine peso that began at the end of 2001, Semptra Pipelines & Storage has reduced the carrying value of its Argentine investments downward by a cumulative total of \$198 million as of December 31, 2004. These non-cash adjustments continue to occur based on fluctuations in the Argentine peso and have not affected net income, but have affected other comprehensive income (loss) and accumulated other comprehensive income (loss). Further discussion is provided in Note 3 of the notes to Consolidated Financial Statements.

In appropriate instances, the company may attempt to limit its exposure to changing foreign exchange rates through both operational and financial market actions. Financial actions may include entering into forward, option and swap contracts to hedge existing exposures, firm commitments and anticipated transactions. As of December 31, 2004, the company had no significant arrangements of this type.

The company's primary objective with respect to currency risk is to preserve the economic value of its overseas investments and to reduce net income volatility that would otherwise occur due to exchange-rate fluctuations.

Semptra Energy's net investment in its Latin American operating companies and the resulting cash flows are partially protected against normal exchange-rate fluctuations by rate-setting mechanisms that are intended to compensate for local inflation and currency exchange-rate fluctuations. In addition to establishing such rate-based protections, the company offsets material cross-currency transactions and net income exposure through various means, including financial instruments and short-term investments.

Because the company does not hedge its net investment in foreign countries, it is susceptible to volatility in other comprehensive income, as occurred in the last three years, primarily as a result of decoupling the Argentine peso from the U.S. dollar, as discussed in Note 3 of the notes to Consolidated Financial Statements.

#### **CRITICAL ACCOUNTING POLICIES AND KEY NON-CASH PERFORMANCE INDICATORS**

Certain accounting policies are viewed by management as critical because their application is the most relevant, judgmental and/or material to the company's financial position and results of operations, and/or because they require the use of material judgments and estimates.



The company's significant accounting policies are described in Note 1 of the notes to Consolidated Financial Statements. The most critical policies, all of which are mandatory under generally accepted accounting principles and the regulations of the Securities and Exchange Commission, are the following:

SFAS 5, "Accounting for Contingencies," establishes the amounts and timing of when the company provides for contingent losses. Details of the company's issues in this area are discussed in Note 16 of the notes to Consolidated Financial Statements.

SFAS 71, "Accounting for the Effects of Certain Types of Regulation," has a significant effect on the way the California Utilities record assets and liabilities, and the related revenues and expenses that would not be recorded absent the principles contained in SFAS 71.

SFAS 109, "Accounting for Income Taxes," governs the way the company provides for income taxes. Details of the company's issues in this area are discussed in Note 8 of the notes to Consolidated Financial Statements.

SFAS 123, "Accounting for Stock-Based Compensation" and SFAS 148, "Accounting for Stock-Based Compensation — Transition and Disclosure," give companies the choice of recognizing a cost at the time of issuance of stock options or merely disclosing what that cost would have been and not recognizing it in its financial statements. The company has elected the disclosure-only option for all options that are so eligible. The effect of this is discussed in Note 1 of the notes to Consolidated Financial Statements.

SFAS 123R, "Share-Based Payment," requires public companies to measure and record the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the awards and gives companies three methods to do so. This statement is effective for the company on July 1, 2005. Further discussion is provided in Note 1 of the notes to Consolidated Financial Statements.

SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," SFAS 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities" and SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities," have a significant effect on the balance sheets of Sempra Commodities and the California Utilities but have no significant effect on the California Utilities' income statements because of the principles contained in SFAS 71. The effect on Sempra Commodities' income statement is discussed in Note 11 of the notes to Consolidated Financial Statements.

Emerging Issues Task Force (EITF) Issue 02-3, "Issues Involved in Accounting for Derivative Contracts held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," has a significant effect on the financial statements of Sempra Commodities, which had been recording transactions in accordance with EITF Issue 98-10, which was eliminated by EITF Issue 02-3. However, most of the trading assets and liabilities of Sempra Commodities are now covered by SFAS 133, SFAS 138 and SFAS 149, which have a similar effect.

SFAS 52, "Foreign Currency Translation," is critical to the accounting for the company's international operations. The application of SFAS 52 is materially affected by the company's accounting treatment of certain U.S. dollar-denominated loans to its Argentine affiliates as though they were equity (based on expectations that repayment will not occur in the foreseeable future), which results in there not being any currency transaction gains or losses when the exchange rate between the currencies changes.

FIN 46, "Consolidation of Variable Interest Entities, an interpretation of ARB No. 51," is critical to the company's consolidation of variable interest entities (VIEs) in its financial statements. FIN 46 requires the company to consolidate VIEs for which it is the primary beneficiary, as defined, and deconsolidate any previously consolidated affiliates that do not meet the

consolidation criteria of FIN 46. Sempra Energy adopted FIN 46 on December 31, 2003, resulting in the consolidation of two VIEs for which FIN 46 deems it to be the primary beneficiary. One of the VIEs was the owner of the Mesquite Power plant. The other VIE relates to the investment in AEG. The primary effect of adopting FIN 46 was reflected in the 2003 Statement of Consolidated Income. These VIEs are discussed further in Note 1 of the notes to Consolidated Financial Statements.

In connection with the application of these and other accounting policies, the company makes estimates and judgments about various matters. The most significant of these involve:

The calculation of fair or realizable values (including the likelihood of fully realizing the value of the investments in Argentina under the Bilateral Investment Treaty and the realizable value of Frontier Energy and AEG, all of which are discussed in Note 1 of the notes to Consolidated Financial Statements).

The collectibility of receivables, regulatory assets, deferred tax assets and other assets.

The resolution of various income-tax issues between the company and the various taxing authorities.

The costs to be incurred in fulfilling certain contracts that have been marked to market.

The various assumptions used in actuarial calculations for pension and other postretirement benefit plans.

The probable costs to be incurred in the resolution of litigation.

Differences between estimates and actual amounts have had significant impacts in the past and are likely to have significant impacts in the future.

As discussed elsewhere herein, the company uses exchange quotations or other third-party pricing to estimate fair values whenever possible. When no such data is available, it uses internally developed models and other techniques. The assumed collectibility of receivables considers the aging of the receivables, the credit-worthiness of customers and the enforceability of contracts, where applicable. The assumed collectibility of regulatory assets considers legal and regulatory decisions involving the specific items or similar items. The assumed collectibility of other assets considers the nature of the item, the enforceability of contracts where applicable, the credit-worthiness of the other parties and other factors. The anticipated resolution of income-tax issues considers past resolutions of the same or similar issue, the status of any income-tax examination in progress and positions taken by taxing authorities with other taxpayers with similar issues. Costs to fulfill contracts that are carried at fair value are based on prior experience. Actuarial assumptions are based on the advice of the company's independent actuaries. The likelihood of deferred tax recovery is based on analyses of the deferred tax assets and the company's expectation of future financial and/or taxable income, based on its strategic planning.

Choices among alternative accounting policies that are material to the company's financial statements and information concerning significant estimates have been discussed with the audit committee of the board of directors.

Key non-cash performance indicators for the company's subsidiaries include numbers of customers and quantities of natural gas and electricity sold for the California Utilities, and plant availability factors at Sempra Generation's generating plants. Sempra Commodities does not use non-cash performance factors. Its key indicators are profit margins by product line and by geographic area. The California Utilities information is provided in "Overview" and "Results of Operations." For competitive reasons, Sempra Generation does not disclose its plant availability factors, but considers them to be very good. The table under "Net Income by Business Unit — Sempra Commodities" provides the information for Sempra Commodities.

Other than its two small natural gas utilities in the eastern United States, Sempra Pipelines & Storage's only consolidated operations are in Mexico. The three local natural gas distribution utilities have increased their customer count to almost 100,000 and their sales volume to almost 50 million cubic feet per day in 2004. The pipeline system had contracted capacity of 450 million cubic feet per day in 2004 and 2003.

#### **NEW ACCOUNTING STANDARDS**

Relevant pronouncements that have recently become effective and have had a significant effect on the company's financial statements are SFAS 132 (revised 2003), 143, 144 and 150, FIN 46, FASB Staff Position (FSP) 106-2 and the rescission of EITF 98-10. They are described in Note 1 of the notes to Consolidated Financial Statements. Pronouncements of particular importance to the company's financial statements are described below.

EITF Issue 98-10, "Accounting for Contracts Involved in Energy Trading and Risk Management Activities": In accordance with the EITF's rescission of Issue 98-10, the company no longer recognizes energy-related contracts under mark to market accounting unless the contracts meet the requirements stated under SFAS 133, Accounting for Derivative Instruments and Hedging Activities, which is the case for a substantial majority of the company's contracts. Upon adoption of this consensus on January 1, 2003, the company recorded the initial effect of rescinding Issue 98-10 as a cumulative effect of a change in accounting principle, which reduced after-tax earnings by \$29 million.

SFAS 143, "Accounting for Asset Retirement Obligations": SFAS 143 requires entities to record the fair value of liabilities for legal obligations related to asset retirements in the period in which they are incurred. It also requires most energy utilities, including the California Utilities, to reclassify amounts recovered in rates for future removal costs not covered by a legal obligation from accumulated depreciation to a regulatory liability.

FIN 46, "Consolidation of Variable Interest Entities, an interpretation of ARB No. 51": In January 2003, the FASB issued FIN 46 to strengthen existing accounting guidance that addresses when a company should consolidate a VIE in its financial statements.

Sempra Energy has identified two VIEs for which it is the primary beneficiary. One of the VIEs (the Mesquite Trust) was the owner of the Mesquite Power plant for which the company had a synthetic lease agreement as described in Note 2 of the notes to Consolidated Financial Statements. The company bought out the lease in January 2004 and now owns the plant. The other VIE relates to the company's investment in AEG, which was subsequently disposed of in April 2004. Sempra Energy consolidated these entities in its financial statements at December 31, 2003.

In accordance with FIN 46, the company has deconsolidated a wholly owned subsidiary trust from its financial statements. Further discussion regarding FIN 46 is provided in Note 1 of the notes to Consolidated Financial Statements.

In addition, contracts under which SDG&E acquires power from generation facilities otherwise unrelated to SDG&E could result in a requirement for SDG&E to consolidate the entity that owns the facility. As permitted by the interpretation, SDG&E is continuing the process of determining whether it has any such situations and, if so, gathering the information that would be needed to perform the consolidation. The effects of this, if any, are not expected to significantly affect the financial position of SDG&E and there would be no effect on results of operations or liquidity.

**INFORMATION REGARDING FORWARD-LOOKING STATEMENTS**

*This Annual Report contains statements that are not historical fact and constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words "estimates," "believes," "expects," "anticipates," "plans," "intends," "may," "could," "would" and "should" or similar expressions, or discussions of strategy or of plans are intended to identify forward-looking statements. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Future results may differ materially from those expressed in these forward-looking statements.*

*Forward-looking statements are necessarily based upon various assumptions involving judgments with respect to the future and other risks, including, among others, local, regional, national and international economic, competitive, political, legislative and regulatory conditions and developments; actions by the California Public Utilities Commission, the California State Legislature, the California Department of Water Resources, and the Federal Energy Regulatory Commission and other regulatory bodies in the United States and other countries; capital markets conditions, inflation rates, interest rates and exchange rates; energy and trading markets, including the timing and extent of changes in commodity prices; the availability of natural gas; weather conditions and conservation efforts; war and terrorist attacks; business, regulatory, environmental and legal decisions and requirements; the status of deregulation of retail natural gas and electricity delivery; the timing and success of business development efforts; and other uncertainties, all of which are difficult to predict and many of which are beyond the control of the company. Readers are cautioned not to rely unduly on any forward-looking statements and are urged to review and consider carefully the risks, uncertainties and other factors which affect the company's business described in this report and other reports filed by the company from time to time with the Securities and Exchange Commission.*

**FIVE YEAR SUMMARY**

 At December 31 or for the years ended December 31,  
 (Dollars in millions, except per share amounts)

	2004	2003	2002	2001	2000
Operating revenues					
California utilities:					
Natural Gas	\$ 4,537	\$ 4,010	\$ 3,263	\$ 4,371	\$ 3,305
Electric	1,658	1,787	1,282	1,676	2,184
Other	3,215	2,090	1,503	1,683	1,271
Total	\$ 9,410	\$ 7,887	\$ 6,048	\$ 7,730	\$ 6,760
Operating income	\$ 1,272	\$ 939	\$ 987	\$ 997	\$ 884
Income from continuing operations, before extraordinary item and cumulative effect of changes in accounting principles	\$ 920	\$ 695	\$ 575	\$ 518	\$ 429
Net income	\$ 895	\$ 649	\$ 591	\$ 518	\$ 429
Income per common share from continuing operations before extraordinary item and cumulative effect of changes in accounting principles:					
Basic	\$ 4.03	\$ 3.29	\$ 2.80	\$ 2.54	\$ 2.06
Diluted	\$ 3.93	\$ 3.24	\$ 2.79	\$ 2.52	\$ 2.06
Net income per common share:					
Basic	\$ 3.92	\$ 3.07	\$ 2.88	\$ 2.54	\$ 2.06
Diluted	\$ 3.83	\$ 3.03	\$ 2.87	\$ 2.52	\$ 2.06
Dividends declared per common share	\$ 1.00	\$ 1.00	\$ 1.00	\$ 1.00	\$ 1.00
Return on common equity	20.5%	19.3%	21.4%	19.5%	15.7%
Effective income tax rate	17.3%	6.3%	20.2%	29.1%	38.6%
Price range of common shares	\$ 37.93- 29.51	\$ 30.90- 22.25	\$ 26.25- 15.50	\$ 28.61- 17.31	\$ 24.88- 16.19
Weighted average rate base:					
SoCalGas	\$ 2,351	\$ 2,273	\$ 2,222	\$ 2,262	\$ 2,329
SDG&E	\$ 2,755	\$ 2,619	\$ 2,452	\$ 2,334	\$ 2,263
AT DECEMBER 31					
Current assets	\$ 8,776	\$ 7,866	\$ 7,010	\$ 4,692	\$ 6,525
Total assets	\$ 23,643	\$ 21,988	\$ 20,242	\$ 17,378	\$ 17,850
Current liabilities	\$ 9,082	\$ 8,569	\$ 7,554	\$ 5,629	\$ 7,490
Long-term debt (excludes current portion)	\$ 4,192	\$ 3,841	\$ 4,083	\$ 3,436	\$ 3,268
Trust preferred securities	\$ 200*	\$ 200*	\$ 200	\$ 200	\$ 200
Shareholders' equity	\$ 4,865	\$ 3,890	\$ 2,825	\$ 2,692	\$ 2,494
Common shares outstanding (in millions)	234.2	226.6	204.9	204.5	201.9
Book value per common share	\$ 20.77	\$ 17.17	\$ 13.79	\$ 13.16	\$ 12.35

\* Amount has been reclassified to Due to Unconsolidated Affiliates effective in 2003.

Note 1 of the notes to consolidated financial statements discusses the changes in accounting principles and the extraordinary item. Note 4 discusses the discontinued operation. Note 16 discusses litigation and other contingencies.

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**MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS**

*Management is responsible for the preparation of the company's consolidated financial statements and related information appearing in this report. Management believes that the consolidated financial statements fairly present the form and substance of transactions and that the financial statements reasonably present the company's financial position and results of operations in conformity with generally accepted accounting principles. Management also has included in the company's financial statements amounts that are based on estimates and judgments, which it believes are reasonable under the circumstances.*

*Deloitte & Touche LLP, an independent registered public accounting firm, audits the company's consolidated financial statements in accordance with the standards of the Public Company Accounting Oversight Board and provides an objective, independent review of the fairness of reported operating results and financial position.*

*The board of directors of the company has an Audit Committee composed of six non-management directors. The committee meets periodically with financial management, the internal auditors and Deloitte & Touche LLP to review accounting, control, auditing and financial reporting matters.*

**MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

*Company management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Exchange Act Rules 13a-15(f). Under the supervision and with the participation of company management, including the principal executive officer and principal financial officer, the company conducted an evaluation of the effectiveness of its internal control over financial reporting based on the framework in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on the company's evaluation under the framework in Internal Control — Integrated Framework, management concluded that the company's internal control over financial reporting was effective as of December 31, 2004. Management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2004 has been audited by Deloitte & Touche LLP, as stated in its report, which is included herein.*

SEMPRA ENERGY 33.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of Sempra Energy:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control over Financial Reporting, that Sempra Energy and subsidiaries (the "Company") maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that the Company maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on the criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on the criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

SEMPRA ENERGY 34.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2004 of the Company and our report dated February 22, 2005 expressed an unqualified opinion on those financial statements and included an explanatory paragraph regarding the Company's adoption of two new accounting standards.

*Deloitte & Touche LLP*

San Diego, California  
February 22, 2005

SEMPRA ENERGY 35.



**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of Sempra Energy:

We have audited the accompanying consolidated balance sheets of Sempra Energy and subsidiaries (the "Company") as of December 31, 2004 and 2003, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Sempra Energy and subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of December 31, 2004, based on the criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 22, 2005 expressed an unqualified opinion on management's assessment of the effectiveness of the Company's internal control over financial reporting and an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

As described in Note 1 to the financial statements, the Company adopted Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations, effective January 1, 2003, and Financial Accounting Standards Board Interpretation No. 46, Consolidation of Variable Interest Entities — an Interpretation of ARB No. 51, effective December 31, 2003.

*Schutte & Touche LLP*

San Diego, California  
February 22, 2005

**SEMPRA ENERGY**  
**STATEMENTS OF CONSOLIDATED INCOME**

(Dollars in millions, except per share amounts)	Years ended December 31,		
	2004	2003	2002
<b>OPERATING REVENUES</b>			
California utilities:			
Natural gas	\$ 4,537	\$ 4,010	\$ 3,283
Electric	1,668	1,787	1,282
Other	3,215	2,090	1,503
Total operating revenues	<u>9,410</u>	<u>7,887</u>	<u>6,048</u>
<b>OPERATING EXPENSES</b>			
California utilities:			
Cost of natural gas	2,593	2,071	1,381
Cost of electric fuel and purchased power	576	541	297
Other cost of sales	1,741	1,204	709
Other operating expenses	2,371	2,287	1,901
Depreciation and amortization	621	615	596
Franchise fees and other taxes	236	230	177
Total operating expenses	<u>8,138</u>	<u>6,948</u>	<u>5,061</u>
Operating income	1,272	939	987
Other income, net	104	26	15
Interest income	69	104	42
Interest expense	(322)	(308)	(294)
Preferred dividends of subsidiaries	(10)	(10)	(11)
Trust preferred distributions by subsidiary	—	(9)	(18)
Income from continuing operations before income taxes	1,113	742	721
Income tax expense	193	47	146
Income from continuing operations	920	695	575
Loss from discontinued operations, net of tax (Note 4)	(23)	—	—
Loss on disposal of discontinued operations, net of tax (Note 4)	(2)	—	—
Income before extraordinary item and cumulative effect of changes in accounting principles	895	695	575
Extraordinary item, net of tax (Note 1)	—	—	16
Income before cumulative effect of changes in accounting principles	895	695	591
Cumulative effect of changes in accounting principles, net of tax (Note 1)	—	(46)	—
Net income	<u>\$ 895</u>	<u>\$ 649</u>	<u>\$ 591</u>
Basic earnings per share:			
Income from continuing operations	\$ 4.03	\$ 3.29	\$ 2.80
Discontinued operations, net of tax	(0.11)	—	—
Extraordinary item, net of tax	—	—	0.08
Cumulative effect of changes in accounting principles, net of tax	—	(0.22)	—
Net income	<u>\$ 3.92</u>	<u>\$ 3.07</u>	<u>\$ 2.88</u>
Weighted-average number of shares outstanding (thousands)	228,271	211,740	205,003
Diluted earnings per share:			
Income from continuing operations	\$ 3.93	\$ 3.24	\$ 2.79
Discontinued operations, net of tax	(0.10)	—	—
Extraordinary item, net of tax	—	—	0.08
Cumulative effect of changes in accounting principles, net of tax	—	(0.21)	—
Net income	<u>\$ 3.83</u>	<u>\$ 3.03</u>	<u>\$ 2.87</u>
Weighted-average number of shares outstanding (thousands)	233,852	214,482	206,062
Dividends declared per share of common stock	\$ 1.00	\$ 1.00	\$ 1.00

See notes to Consolidated Financial Statements.

**SEMPRA ENERGY**  
**CONSOLIDATED BALANCE SHEETS**

(Dollars in millions)	December 31, 2004	December 31, 2003
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 419	\$ 409
Short-term investments	15	386
Trade accounts receivable, net	950	749
Other accounts and notes receivable, net	82	125
Due from unconsolidated affiliate	4	—
Deferred income taxes	15	—
Interest receivable	80	62
Trading-related receivables and deposits, net	2,606	2,350
Derivative trading instruments	2,339	1,607
Commodities owned	1,547	1,420
Regulatory assets arising from fixed-price contracts and other derivatives	152	144
Other regulatory assets	103	89
Inventories	172	147
Other	222	158
Current assets of continuing operations	<u>8,706</u>	<u>7,646</u>
Current assets of discontinued operations	70	220
Total current assets	<u>8,776</u>	<u>7,866</u>
Investments and other assets:		
Due from unconsolidated affiliates	42	55
Regulatory assets arising from fixed-price contracts and other derivatives	500	650
Other regulatory assets	619	552
Nuclear decommissioning trusts	612	570
Investments	1,164	1,112
Sundry	844	707
Total investments and other assets	<u>3,781</u>	<u>3,646</u>
Property, plant and equipment:		
Property, plant and equipment	16,203	15,319
Less accumulated depreciation and amortization	<u>(5,117)</u>	<u>(4,843)</u>
Property, plant and equipment, net	<u>11,086</u>	<u>10,476</u>
Total assets	<u>\$ 23,643</u>	<u>\$ 21,988</u>

See notes to Consolidated Financial Statements.

**SEMPRA ENERGY**  
**CONSOLIDATED BALANCE SHEETS**

(Dollars in millions)	December 31, 2004	December 31, 2003
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities:</b>		
Short-term debt	\$ 405	\$ 28
Accounts payable — trade	1,020	725
Accounts payable — other	106	63
Due to unconsolidated affiliates	205	1
Income taxes payable	187	336
Deferred income taxes	—	31
Trading-related payables	3,182	2,255
Derivative trading instruments sold, not yet purchased	1,484	1,340
Commodities sold with agreement to repurchase	513	922
Dividends and interest payable	123	136
Regulatory balancing accounts, net	509	424
Fixed-price contracts and other derivatives	157	148
Current portion of long-term debt	398	1,433
Other	776	675
Current liabilities of continuing operations	9,065	8,517
Current liabilities of discontinued operations	17	52
Total current liabilities	9,082	8,569
Long-term debt	4,192	3,841
<b>Deferred credits and other liabilities:</b>		
Due to unconsolidated affiliates	162	362
Customer advances for construction	97	89
Postretirement benefits other than pensions	129	131
Deferred income taxes	420	368
Deferred investment tax credits	78	84
Regulatory liabilities arising from cost of removal obligations	2,359	2,238
Regulatory liabilities arising from asset retirement obligations	333	303
Other regulatory liabilities	67	109
Fixed-price contracts and other derivatives	500	680
Asset retirement obligations	326	313
Deferred credits and other	854	832
Total deferred credits and other liabilities	5,325	5,509
Preferred stock of subsidiaries	179	179
Commitments and contingencies (Note 16)		
<b>SHAREHOLDERS' EQUITY</b>		
Preferred stock (50 million shares authorized; none issued)	—	—
Common stock (750 million shares authorized; 234 million and 227 million shares outstanding at December 31, 2004 and 2003, respectively)	2,301	2,028
Retained earnings	2,961	2,298
Deferred compensation relating to ESOP	(32)	(35)
Accumulated other comprehensive income (loss)	(365)	(401)
Total shareholders' equity	4,865	3,890
<b>Total liabilities and shareholders' equity</b>	<b>\$ 23,643</b>	<b>\$ 21,988</b>

See notes to Consolidated Financial Statements.

**SEMPRA ENERGY**  
**STATEMENTS OF CONSOLIDATED CASH FLOWS**

(Dollars in millions)	Years ended December 31,		
	2004	2003	2002
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income	\$ 895	\$ 649	\$ 591
Adjustments to reconcile net income to net cash provided by operating activities:			
Discontinued operations, net of tax	25	—	—
Depreciation and amortization	621	615	596
Deferred income taxes and investment tax credits	13	(118)	(143)
Non-cash rate reduction bond expense	75	68	82
Equity in (income) losses of unconsolidated affiliates	(36)	(8)	55
Impairment losses	12	101	—
Loss (gain) on sale and disposition of assets	(15)	8	14
Foreign currency loss (gain)	—	8	(63)
Extraordinary item, net of tax	—	—	(16)
Cumulative effect of changes in accounting principles, net of tax	—	46	—
Other, net	37	23	(2)
Net changes in other working capital components	(427)	(154)	203
Changes in other assets	(200)	(71)	84
Changes in other liabilities	(21)	(26)	40
Net cash provided by continuing operations	979	1,141	1,441
Net cash used in discontinued operations	(30)	—	—
Net cash provided by operating activities	<u>949</u>	<u>1,141</u>	<u>1,441</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Expenditures for property, plant and equipment	(1,083)	(1,049)	(1,214)
Investments in and acquisitions of subsidiaries, net of cash acquired	(74)	(202)	(429)
Proceeds from disposal of discontinued operations	157	—	—
Proceeds from sale of assets	372	29	—
Dividends received from unconsolidated affiliates	59	72	11
Affiliate loans	—	(99)	(82)
Other, net	10	1	(9)
Net cash used in investing activities	<u>(559)</u>	<u>(1,248)</u>	<u>(1,723)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Common dividends paid	(195)	(182)	(201)
Issuances of common stock	110	505	9
Repurchases of common stock	(5)	(7)	(17)
Issuances of long-term debt	997	900	1,150
Payments on long-term debt	(1,670)	(601)	(479)
Increase (decrease) in short-term debt, net	397	(518)	(307)
Other, net	(14)	(8)	(18)
Net cash (used in) provided by financing activities	<u>(380)</u>	<u>89</u>	<u>137</u>
Increase (decrease) in cash and cash equivalents	10	(18)	(145)
Cash and cash equivalents, January 1	409	427	572
Cash and cash equivalents, December 31	<u>\$ 419</u>	<u>\$ 409</u>	<u>\$ 427</u>

See notes to Consolidated Financial Statements.

	2004	Years ended December 31, 2003	2002
<b>CHANGES IN OTHER WORKING CAPITAL COMPONENTS</b>			
(Excluding cash and cash equivalents, and debt due within one year)			
Accounts and notes receivable	\$ (346)	\$ (231)	\$ (121)
Net trading assets	(442)	81	66
Income taxes, net	(66)	72	137
Inventories	(25)	(13)	(11)
Regulatory balancing accounts	79	(156)	170
Regulatory assets and liabilities	(23)	(30)	1
Other current assets	(31)	(8)	51
Accounts payable	324	98	(103)
Other current liabilities	103	33	13
Net changes in other working capital components	<u>\$ (427)</u>	<u>\$ (154)</u>	<u>\$ 203</u>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>			
Interest payments, net of amounts capitalized	\$ 318	\$ 296	\$ 279
Income tax payments, net of refunds	<u>\$ 254</u>	<u>\$ 118</u>	<u>\$ 140</u>
<b>SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES</b>			
Common dividends paid in stock	<u>\$ 35</u>	<u>\$ 25</u>	<u>\$ 4</u>
Acquisition of subsidiaries:			
Assets acquired	\$ —	\$ —	\$ 1,134
Cash paid, net of cash acquired	—	—	(119)
Liabilities assumed	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 1,015</u>
Consolidation of variable interest entities:			
Assets recorded	\$ —	\$ 820	\$ —
Liabilities recorded	—	(881)	—
Total	<u>\$ —</u>	<u>\$ (61)</u>	<u>\$ —</u>

See notes to Consolidated Financial Statements.

**SEMPRA ENERGY**  
**STATEMENTS OF CONSOLIDATED CHANGES IN SHAREHOLDERS' EQUITY**  
**Years ended December 31, 2004, 2003 and 2002**

(Dollars in millions)	Comprehensive Income	Common Stock	Retained Earnings	Deferred Compensation Relating to ESOP	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance at December 31, 2001		\$ 1,495	\$ 1,475	\$ (36)	\$ (242)	\$ 2,692
Net income	\$ 591		591			591
Comprehensive income adjustments:						
Foreign currency translation losses (Note 1)	(162)				(162)	(162)
Pension	(35)				(35)	(35)
Comprehensive income	<u>\$ 394</u>					
Common stock dividends declared			(205)			(205)
Issuance of equity units (Note 13)		(61)				(61)
Issuance of common stock		18				18
Repurchase of common stock		(16)				(16)
Common stock released from ESOP				3		3
Balance at December 31, 2002		1,436	1,861	(33)	(439)	2,825
Net income	\$ 649		649			649
Comprehensive income adjustments:						
Foreign currency translation gains (Note 1)	57				57	57
Pension	(16)				(16)	(16)
SFAS 133	(3)				(3)	(3)
Comprehensive income	<u>\$ 687</u>					
Common stock dividends declared			(212)			(212)
Equity units adjustment		6				6
Quasi-reorganization adjustment (Note 1)		19				19
Issuance of common stock		553				553
Tax benefit related to employee stock options		13				13
Repurchase of common stock		(6)				(6)
Common stock released from ESOP		7		(2)		5
Balance at December 31, 2003		2,028	2,298	(35)	(401)	3,890
Net income	\$ 895		895			895
Comprehensive income adjustments:						
Foreign currency translation gains (Note 1)	40				40	40
Pension	28				28	28
Available-for-sale securities	4				4	4
SFAS 133	(36)				(36)	(36)
Comprehensive income	<u>\$ 931</u>					
Common stock dividends declared			(232)			(232)
Quasi-reorganization adjustment (Note 1)		86				86
Issuance of common stock		172				172
Tax benefit related to employee stock options		16				16
Repurchase of common stock		(5)				(5)
Common stock released from ESOP		4		3		7
Balance at December 31, 2004		<u>\$ 2,301</u>	<u>\$ 2,961</u>	<u>\$ (32)</u>	<u>\$ (365)</u>	<u>\$ 4,865</u>

See notes to Consolidated Financial Statements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

#### Principles of Consolidation

The Consolidated Financial Statements include the accounts of Sempra Energy (the company), its majority-owned subsidiaries and the variable-interest entities of which it is the primary beneficiary (as discussed further in New Accounting Standards below). Investments in affiliated companies over which Sempra Energy has the ability to exercise significant influence, but not control, are accounted for using the equity method. Further discussion of investments in unconsolidated subsidiaries is provided in Note 3. All material intercompany accounts and transactions have been eliminated.

During the fourth quarter of 2004, Sempra Commodities assumed the management of the commodities business of Sempra Energy Solutions, and Sempra Generation assumed the management of Sempra Energy Solutions' other two business lines — energy services and facilities management. Since Sempra Commodities and Sempra Generation are each separate reportable segments of the company, in accordance with Statement of Financial Accounting Standards (SFAS) 131, Disclosures about Segments of an Enterprise and Related Information, the prior years' financial statements have been restated to reflect the change in reporting of Sempra Energy Solutions' results of operation and financial position.

#### Quasi-Reorganization

In 1993, Pacific Enterprises (PE) effected a quasi-reorganization for financial reporting purposes as of December 31, 1992. Certain of the liabilities established in connection with the quasi-reorganization were favorably resolved in 2003 and 2004, resulting in adjustments to common stock in these years. The remaining liabilities will be resolved in future years and management believes the provisions established for these matters are adequate.

#### Use of Estimates in the Preparation of the Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the reporting period, and the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. Actual amounts can differ significantly from those estimates.

#### Basis of Presentation

Certain prior-year amounts have been reclassified to conform to the current year's presentation.

#### Regulatory Matters

##### Effects of Regulation

The accounting policies of the company's principal utility subsidiaries, San Diego Gas & Electric (SDG&E) and Southern California Gas Company (SoCalGas) (collectively, the California Utilities), conform with generally accepted accounting principles for regulated enterprises and reflect the policies of the California Public Utilities Commission (CPUC) and the Federal Energy Regulatory Commission (FERC).

The California Utilities prepare their financial statements in accordance with the provisions of SFAS 71, Accounting for the Effects of Certain Types of Regulation, under which a regulated utility records a regulatory asset if it is probable that, through the ratemaking process, the utility will recover that asset from customers. To the extent that recovery is no longer probable as a result of changes in regulation or the utility's competitive position, the related regulatory assets would be written off. In addition, SFAS 144, Accounting for the Impairment or Disposal of Long-Lived Assets, requires that a loss be recognized whenever a regulator excludes all or part of utility plant or regulatory assets from ratebase.



Regulatory liabilities represent reductions in future rates for amounts due to customers. Information concerning regulatory assets and liabilities is provided below in "Revenues," "Regulatory Balancing Accounts" and "Regulatory Assets and Liabilities."

#### Regulatory Balancing Accounts

The amounts included in regulatory balancing accounts at December 31, 2004, represent net payables (payables net of receivables) of \$178 million and \$331 million for SoCalGas and SDG&E, respectively. The corresponding amounts at December 31, 2003 were net payables of \$86 million and \$338 million, respectively.

Except for certain costs subject to balancing account treatment, fluctuations in most operating and maintenance accounts affect utility earnings. Balancing accounts provide a mechanism for charging utility customers the amount actually incurred for certain costs, primarily commodity costs. The CPUC has also approved balancing account treatment for variances between forecast and actual for SoCalGas' and SDG&E's commodity costs and volumes, eliminating the impact on earnings from any throughput and revenue variances from adopted forecast levels. Additional information on regulatory matters is included in Notes 14 and 15.

#### Regulatory Assets and Liabilities

In accordance with the accounting principles of SFAS 71, the company records regulatory assets and regulatory liabilities as discussed above.

Regulatory assets (liabilities) as of December 31 relate to the following matters:

(Dollars in millions)	2004	2003
<b>SDG&amp;E</b>		
Fixed-price contracts and other derivatives	\$ 500	\$ 560
Recapture of temporary rate reduction*	183	259
Deferred taxes recoverable in rates	278	271
Unamortized loss on retirement of debt, net	46	44
Employee benefit costs	160	35
Cost of removal obligation**	(913)	(846)
Asset retirement obligation**	(333)	(303)
Other	29	24
Total	(50)	44
<b>SoCalGas</b>		
Fixed-price contracts and other derivatives	148	233
Environmental remediation	42	44
Unamortized loss on retirement of debt, net	44	45
Cost of removal obligation**	(1,446)	(1,392)
Deferred taxes refundable in rates	(199)	(194)
Employee benefit costs	65	(77)
Other	7	9
Total	(1,339)	(1,332)
PE — Employee benefit costs (transferred to SoCalGas in 2004)	—	72
Total PE consolidated	(1,339)	(1,260)
<b>Total</b>	<b>\$ (1,389)</b>	<b>\$ (1,216)</b>

\* In connection with electric industry restructuring, which is described in Note 14, SDG&E temporarily reduced rates to its small-usage customers. That reduction is being recovered in rates through 2007.

\*\* This is related to SFAS 143, *Accounting for Asset Retirement Obligations*, which is discussed below in "New Accounting Standards."

Net regulatory assets (liabilities) are recorded on the Consolidated Balance Sheets at December 31 as follows:

(Dollars in millions)	2004	2003
Current regulatory assets	\$ 255	\$ 233
Noncurrent regulatory assets	1,119	1,202
Current regulatory liabilities*	(4)	(1)
Noncurrent regulatory liabilities	(2,759)	(2,650)
Total	\$ (1,389)	\$ (1,216)

\* Included in Other Current Liabilities.

All of these assets either earn a return, generally at short-term rates, or the cash has not yet been expended and the assets are offset by liabilities that do not incur a carrying cost.

#### Cash and Cash Equivalents

Cash equivalents are highly liquid investments with maturities of three months or less at the date of purchase.

#### Restricted cash

Restricted cash was \$15 million and \$23 million at December 31, 2004 and 2003, respectively. The amounts are included in current assets under the caption Short-term Investments and are primarily used to serve as cash collateral for certain debt agreements.

#### Collection Allowances

The allowance for doubtful accounts was \$8 million, \$19 million and \$12 million at December 31, 2004, 2003 and 2002, respectively. The company recorded a provision for doubtful accounts of \$12 million, \$5 million and \$13 million in 2004, 2003 and 2002, respectively.

The allowance for realization of trading assets was \$56 million, \$67 million and \$86 million at December 31, 2004, 2003 and 2002, respectively. The company recorded a provision (reduction thereof) for trading assets of \$3 million, \$(4) million and \$20 million in 2004, 2003 and 2002, respectively.

#### Trading Instruments

Trading assets and trading liabilities (described further in Note 11) include option premiums paid and received, unrealized gains and losses from exchange-traded futures and options, over-the-counter (OTC) swaps, forwards, physical commodities and options. Trading instruments are recorded by Sempra Commodities on a trade-date basis and the majority of such derivative instruments are adjusted daily to current market value. Unrealized gains and losses on OTC transactions reflect amounts which would be received from or paid to a third party upon net settlement of the contracts. Unrealized gains and losses on OTC transactions are reported separately as assets and liabilities unless a legal right of setoff exists under an enforceable netting arrangement.

In October 2002, the Emerging Issues Task Force (EITF) rescinded fair value accounting for recording energy-trading activities and required contracts subsequently entered into to be accounted for at historical cost or the lower of cost or market, unless the contracts meet the requirements for fair value accounting under SFAS 133 and 149, as discussed below in "New Accounting Standards." Energy

transportation and storage contracts are recorded at cost. Energy commodity inventory is being recorded at the lower of cost or market. The company's base metals and concentrates inventory continues to be recorded at fair value in accordance with Accounting Research Bulletin (ARB) No. 43, Restatement and Revision of Accounting Research Bulletins. Further discussion of EITF Issue 98-10 is provided below in "New Accounting Standards."

Futures and exchange-traded option transactions are recorded as contractual commitments on a trade-date basis and carried at current market value based on current closing exchange quotations. Derivative commodity swaps and forward transactions are accounted for as contractual commitments on a trade-date basis and carried at fair value derived from current dealer quotations and underlying commodity-exchange quotations. OTC options are carried at fair value based on the use of valuation models that utilize, among other things, current interest, commodity and volatility rates. For long-dated forward transactions, current market values are derived using internally developed valuation methodologies based on available market information. When there is an absence of observable market data at inception, the value of the transaction is its cost. Where market rates are not quoted, current interest, commodity and volatility rates are estimated by reference to current market levels. Given the nature, size and timing of transactions, estimated values may differ significantly from realized values. Changes in market values are reflected in net income. Although trading instruments may have scheduled maturities in excess of one year, the actual settlement of these transactions can occur sooner, resulting in the current classification of trading assets and liabilities on the Consolidated Balance Sheets.

#### **Inventories**

At December 31, 2004, inventory shown on the Consolidated Balance Sheets, which does not include Commodities Owned, included natural gas of \$115 million, and materials and supplies of \$57 million. The corresponding balances at December 31, 2003 were \$89 million and \$58 million, respectively. Natural gas at the California Utilities (\$111 million and \$84 million at December 31, 2004 and 2003, respectively) is valued by the last-in first-out (LIFO) method. When the California Utilities' inventory is consumed, differences between the LIFO valuation and replacement cost are reflected in customer rates. Materials and supplies at the California Utilities are generally valued at the lower of average cost or market.

#### **Income Taxes**

Income tax expense includes current and deferred income taxes from operations during the year. In accordance with SFAS 109, Accounting for Income Taxes, the company records deferred income taxes for temporary differences between the book and tax bases of assets and liabilities. Investment tax credits from prior years are being amortized to income by the California Utilities over the estimated service lives of the properties. Other credits, mainly low-income housing and synthetic-fuel tax credits, are recognized in income as earned. The company follows certain provisions of SFAS 109 that permit regulated enterprises to recognize deferred taxes as regulatory assets or liabilities if it is probable that such amounts will be recovered from, or returned to, customers. The company follows Accounting Principles Board Opinion (APBO) 23, Accounting for Income Taxes — Special Areas, in recording deferred taxes for investments in foreign subsidiaries and the undistributed earnings of foreign subsidiaries.

#### **Property, Plant and Equipment**

Property, plant and equipment primarily represents the buildings, equipment and other facilities used by the California Utilities to provide natural gas and electric utility services, and by Sempra Generation.

The cost of plant includes labor, materials, contract services and certain expenditures, including refurbishments, replacement of major component parts and labor and overheads incurred to install the

parts, incurred during a major maintenance outage of a generating plant. Maintenance costs are expensed as incurred. In addition, the cost of utility plant includes an allowance for funds used during construction (AFUDC). The cost of non-utility plant includes capitalized interest. The cost of most retired depreciable utility plant minus salvage value is charged to accumulated depreciation.

Property, plant and equipment balances by major functional categories are as follows:

(Dollars in billions)	Property, Plant and Equipment at		2004	Depreciation rates for years ended	
	2004	December 31, 2003		2003	December 31, 2002
<b>California Utilities:</b>					
Natural gas operations	\$ 8.1	\$ 7.8	3.65%	4.27%	4.25%
Electric distribution	3.4	3.2	4.11%	4.70%	4.66%
Electric transmission	1.0	0.9	3.06%	3.09%	3.17%
Construction work in progress	0.5	0.4	NA	NA	NA
Other electric	0.6	0.5	11.33%	9.53%	9.37%
<b>Total</b>	<b>13.6</b>	<b>12.8</b>			
<b>Other operations:</b>					
Land and land rights	0.1	0.1			
Buildings and leasehold improvements	0.2	0.2			
Machinery and equipment	1.9	1.8			
Construction work in progress	0.3	0.3			
Other	0.1	0.1			
<b>Total</b>	<b>2.6</b>	<b>2.5</b>	<b>various</b>	<b>various</b>	<b>various</b>
<b>Total</b>	<b>\$ 16.2</b>	<b>\$ 15.3</b>			

Accumulated depreciation and decommissioning of natural gas and electric utility plant in service were \$3.3 billion and \$1.4 billion, respectively, at December 31, 2004, and were \$3.1 billion and \$1.4 billion, respectively, at December 31, 2003. The discussion of SFAS 143 under "New Accounting Standards" describes a change in presentation of accumulated depreciation. Depreciation expense is based on the straight-line method over the useful lives of the assets or, for the California Utilities, a shorter period prescribed by the CPUC. Notes 14 and 15 include a discussion of the industry restructuring, which affected recorded depreciation. Accumulated depreciation for power plants at Semptra Generation was \$47 million and \$17 million at December 31, 2004 and 2003, respectively. Depreciation expense is computed using the straight-line method over the asset's estimated original composite useful life or the remaining term of the site leases, whichever is lower.

AFUDC, which represents the cost of debt and equity funds used to finance the construction of utility plant, is added to the cost of utility plant. Although it is not a current source of cash, AFUDC increases income and is recorded partly as an offset to interest charges and partly as a component of Other Income, Net in the Statements of Consolidated Income. AFUDC amounted to \$18 million, \$29 million and \$34 million for 2004, 2003 and 2002, respectively. Total capitalized carrying costs, including AFUDC and the impact of Semptra Generation's construction projects, were \$27 million, \$55 million and \$63 million for 2004, 2003 and 2002, respectively.

#### Goodwill and Intangible Assets

Goodwill represents the excess of the purchase price over the fair value of the net assets of acquired companies. Goodwill is not amortized, but is tested annually for impairment in accordance with SFAS 142, Goodwill and Other Intangible Assets.

In accordance with the transitional guidance of SFAS 142, recorded goodwill attributable to the company was tested for impairment in 2002 by comparing its fair value to its carrying value, using a discounted cash flow methodology. As a result, in 2002, Sempra Pipelines & Storage recorded a pre-tax charge of \$6 million related to the impairment of goodwill associated with its two domestic subsidiaries. Impairment losses are reflected in Other Operating Expenses in the Statements of Consolidated Income. Also during 2002, Sempra Commodities completed several acquisitions as further discussed in Note 2. As a result of Sempra Commodities' acquisition of the metals warehousing business, the company recorded \$21 million of goodwill on the Consolidated Balance Sheets. In addition, a \$16 million after-tax extraordinary gain, which reflected a tax benefit of \$2 million, was recorded in 2002 related to the purchase of the base metals and concentrates businesses at prices below the net sums of the fair values of the assets and liabilities acquired.

During 2003, Sempra Pipelines & Storage purchased the remaining minority interests in its Mexican subsidiaries, which resulted in the recording of an addition to goodwill of \$6 million and of another intangible asset of \$4 million.

The changes in the carrying amount of goodwill (included in Noncurrent Sundry Assets on the Consolidated Balance Sheets) since January 1, 2003 are as follows:

(Dollars in millions)	Sempra Commodities	Sempra Generation	Other	Total
Balance as of January 1, 2003	\$ 164	\$ 18	\$ —	\$ 182
Goodwill acquired during 2003	—	—	6	6
Balance as of December 31, 2003 and 2004	\$ 164	\$ 18	\$ 6	\$ 188

Sempra Commodities and Sempra Generation are the only reportable segments that have goodwill. In addition, the unamortized goodwill related to unconsolidated subsidiaries (included in Investments on the Consolidated Balance Sheets), primarily those located in South America, was \$296 million and \$299 million at December 31, 2004 and 2003, respectively, before foreign-currency translation adjustments. Including foreign-currency translation adjustments, these amounts were \$238 million and \$232 million, respectively. Other intangible assets were not material at December 31, 2004 or 2003.

#### Long-Lived Assets

The company periodically evaluates whether events or circumstances have occurred that may affect the recoverability or the estimated useful lives of long-lived assets, the definition of which does not include unconsolidated subsidiaries. Impairment of long-lived assets occurs when the estimated future undiscounted cash flows are less than the carrying amount of the assets. If that comparison indicates that the assets' carrying value may be permanently impaired, the potential impairment is measured based on the difference between the carrying amount and the fair value of the assets based on quoted market prices or, if market prices are not available, on the estimated discounted cash flows. This calculation is performed at the lowest level for which separately identifiable cash flows exist. Further discussion of SFAS 144 is provided in "New Accounting Standards." During the third and fourth quarters of 2003, the company recorded before-tax impairment charges of \$77 million and \$24 million, respectively, to write down the carrying value of the assets of Frontier Energy and Atlantic Electric & Gas Limited (AEG), respectively. This is discussed further in "New Accounting Standards" below and in Note 4. The carrying value of unconsolidated subsidiaries is evaluated for impairment based on the requirements of APBO 18, The Equity Method of Accounting for Investments in Common Stock.

#### Nuclear Decommissioning Liability

At December 31, 2004 and 2003, as the result of implementing SFAS 143, SDG&E had asset retirement obligations of \$328 million and \$316 million, respectively, and related regulatory liabilities of

\$333 million and \$303 million, respectively. Additional information on San Onofre Nuclear Generating Station (SONGS) decommissioning costs is included below in "New Accounting Standards."

#### Legal Fees

Legal fees that are associated with a past event and not expected to be recovered in the future are accrued when it is probable that they will be incurred.

#### Comprehensive Income

Comprehensive income includes all changes, except those resulting from investments by owners and distributions to owners, in the equity of a business enterprise from transactions and other events, including foreign-currency translation adjustments, minimum pension liability adjustments and certain hedging activities. The components of other comprehensive income, which consists of all these changes other than net income as shown on the Statements of Consolidated Income, are shown in the Statements of Consolidated Changes in Shareholders' Equity.

The components of Accumulated Other Comprehensive Income, net of income taxes, at December 31, 2004 are as follows:

Foreign-currency translation loss	\$ (294)
Financial instruments	(39)
Minimum pension liability adjustments	(36)
Unrealized gains on available-for-sale securities	4
Balance as of December 31, 2004	<u>\$ (365)</u>

#### Stock-Based Compensation

The company has stock-based employee compensation plans, which are described in Note 10. The company accounts for these plans under the recognition and measurement principles of APBO 25, Accounting for Stock Issued to Employees, and related Interpretations. No stock-based employee compensation cost is reflected in net income for options granted after 1998 since those options had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table provides the pro forma effects of recognizing compensation expense in accordance with SFAS 123, Accounting for Stock-Based Compensation:

	2004	Years ended December 31,	
		2003	2002
Net income as reported	<b>\$ 895</b>	\$ 649	\$ 591
Stock-based employee compensation expense included in the computation of net income, net of tax (attributable to stock option grants before 1999 and restricted stock awards)	<b>24</b>	13	3
Total stock-based employee compensation under fair value method for all grants and awards, net of tax	<b>(30)</b>	(20)	(11)
Pro forma net income	<b>\$ 889</b>	\$ 642	\$ 583
Earnings per share:			
Basic — as reported	<b>\$3.92</b>	\$3.07	\$2.88
Basic — pro forma	<b>\$3.89</b>	\$3.03	\$2.84
Diluted — as reported	<b>\$3.83</b>	\$3.03	\$2.87
Diluted — pro forma	<b>\$3.80</b>	\$2.99	\$2.83

## Revenues

Revenues of the California Utilities are primarily derived from deliveries of electricity and natural gas to customers and changes in related regulatory balancing accounts. Revenues from electricity and natural gas sales and services are generally recorded under the accrual method and recognized upon delivery. The portion of SDG&E's electric commodity that was procured for its customers by the California Department of Water Resources (DWR) and delivered by SDG&E is not included in SDG&E's revenues or costs. Costs associated with long-term contracts allocated to SDG&E from the DWR also were not included in the Statements of Consolidated Income, since the DWR retains legal and financial responsibility for these contracts. Note 14 includes a discussion of the electric industry restructuring. Natural gas storage contract revenues are accrued on a monthly basis and reflect reservation, storage and injection charges in accordance with negotiated agreements, which have terms of up to three years. Operating revenue includes amounts for services rendered but unbilled (approximately one-half month's deliveries) at the end of each year.

Through 2003, operating costs of SONGS Units 2 and 3, including nuclear fuel and related financing costs, and incremental capital expenditures were recovered through the Incremental Cost Incentive Pricing (ICIP) mechanism, which allowed SDG&E to receive 4.4 cents per kilowatt-hour for SONGS generation. Any differences between these costs and the incentive price affected net income. For the year ended December 31, 2003, ICIP contributed \$53 million to SDG&E's net income. Beginning in 2004, the CPUC has provided for traditional rate-making treatment, under which the SONGS ratebase started over at January 1, 2004, essentially eliminating earnings from SONGS except from increases in ratebase in 2004 and beyond.

Additional information concerning utility revenue recognition is discussed above under "Regulatory Matters."

Sempra Commodities generates a substantial portion of its revenues from market making and trading activities, as a principal, in natural gas, electricity, petroleum, metals and other commodities, for which it quotes bid and ask prices to end users and other market makers. Principal transaction revenues are recognized on a trade-date basis, and include realized gains and losses, and the net change in the fair value of unrealized gains and losses. Sempra Commodities also earns trading profits as a dealer by structuring and executing transactions. Sempra Commodities utilizes derivative instruments to reduce its exposure to unfavorable changes in market prices, which are subject to significant and volatile fluctuation. These instruments include futures, forwards, swaps and options. Options, which are either exchange-traded or directly negotiated between counterparties, provide the holder with the right to buy from or sell to the other party an agreed amount of a commodity at a specified price within a specified period or at a specified time.

As a writer of options, Sempra Commodities generally receives an option premium and then manages the risk of an unfavorable change in the value of the underlying commodity by entering into related transactions or by other means. Forward and future transactions are contracts for delivery of commodities in which the counterparty agrees to make or take delivery at a specified price. Commodity swap transactions may involve the exchange of fixed and floating payment obligations without the exchange of the underlying commodity. Sempra Commodities' financial instruments represent contracts with counterparties whereby payments are linked to or derived from market indices or on terms predetermined by the contract.

Non-derivative contracts are being carried at cost and accounted for on an accrual basis and, therefore, the related profit or loss will be recognized as the contract is performed. Derivative instruments are discussed further in Note 11.

Sempra Generation's revenues are derived primarily from the sale of electric energy to governmental and wholesale power marketing entities and are recognized in accordance with the provisions of

EITF 91-6, Revenue Recognition of Long-term Power Supply Contracts, and EITF 96-17, Revenue Recognition Under Long-term Power Sales Contracts that Contain Both Fixed and Variable Terms. During 2004 and 2003, electric energy sales to the DWR accounted for a significant portion of total Sempra Generation's revenues. Additionally, a small portion of Sempra Generation's revenue, formerly included in the operations of Sempra Energy Solutions, is generated from energy related products and services to commercial, industrial, government and institutional markets.

The consolidated foreign subsidiaries of Sempra Pipelines & Storage, all of which operate in Mexico, recognize revenue similarly to the California Utilities, except that SFAS 71 is not applicable due to the different regulatory environment.

#### **Extraordinary Gain**

During 2002, Sempra Commodities acquired two businesses for amounts less than the fair values of the businesses' net assets. In accordance with SFAS 141, Business Combinations, those differences were recorded as extraordinary income.

#### **Foreign Currency Translation**

The assets and liabilities of the company's foreign operations are generally translated into U.S. dollars at current exchange rates, and revenues and expenses are translated at average exchange rates for the year. Resulting translation adjustments do not enter into the calculation of net income or retained earnings, but are reflected in Comprehensive Income and Accumulated Other Comprehensive Income, a component of shareholders' equity, as described in Note 3. To reflect the fluctuation in the Argentine peso, the functional currency of the company's Argentine operations, Sempra Pipelines & Storage adjusted its investment in its two Argentine natural gas utility holding companies downward by \$1 million, upward by \$26 million and downward by \$102 million in 2004, 2003 and 2002, respectively. A similar adjustment has been made to its investment in Chile to reflect the fluctuation in the Chilean peso, the functional currency of the company's Chilean operations, upward by \$22 million and \$43 million in 2004 and 2003, respectively, and downward by \$8 million in 2002. These non-cash adjustments did not affect net income, but did reduce or increase comprehensive income and accumulated other comprehensive income (loss). Smaller adjustments have been made to operations in other countries. Additional information concerning these investments is described in Note 3.

Currency transaction gains and losses in a currency other than the entity's functional currency are included in the calculation of consolidated net income. The company recorded \$8 million of currency transaction losses in 2003 and \$63 million of gains in 2002. In 2004, the currency transaction gains were not material.

#### **Transactions with Affiliates**

##### **Loans to Unconsolidated Affiliates**

In December 2001, Sempra Pipelines & Storage issued two U.S. dollar denominated loans totaling \$35 million and \$22 million to its affiliates Camuzzi Gas Pampeana S. A. and Camuzzi Gas del Sur S. A., respectively. These loans have variable interest rates (9.02% at December 31, 2004) and are due in January 2006 and June 2005, respectively. The balances outstanding under the notes were \$42 million and \$55 million at December 31, 2004 and 2003, respectively. These amounts are included in non-current assets under Due from Unconsolidated Affiliates, because they are expected to be refinanced for longer terms.

##### **Loans from Unconsolidated Affiliates**

At both December 31, 2004 and 2003, Sempra Pipelines & Storage had long-term notes payable to affiliates which include \$60 million at 6.47% due April 1, 2008 and \$100 million at 6.62% due April 1,



2011. The loans are due to Chilquinta Energia Finance Co. LLC and are secured by Sempra Pipelines & Storage's investments in Chilquinta Energia S.A. and Luz del Sur S.A.A. (Luz del Sur), which are discussed in Note 3.

In February 2000, a wholly owned subsidiary trust of the company issued 8,000,000 shares of preferred stock in the form of 8.90% Cumulative Quarterly Income Preferred Securities, Series A (QUIPS). The QUIPS have cumulative preferences as to distributions, are nonvoting and have par and liquidation values of \$25 per share. Cash dividends are paid quarterly and the QUIPS were scheduled to mature on February 23, 2030, subject to extension to a date not later than February 23, 2049, and shortening to a date not earlier than February 23, 2015. The QUIPS are subject to mandatory redemption and the company has guaranteed payments to the extent that the trust does not have funds available to make distributions. The trust has no assets except its corresponding receivable from Sempra Energy. The QUIPS are callable on or after February 23, 2005 and there are no sinking fund provisions. The company reclassified the \$200 million of mandatorily redeemable trust preferred securities to Due to Unconsolidated Affiliates as a result of the adoption of Financial Accounting Standard Board Interpretation (FIN) 46 effective December 31, 2003. In addition, dividend payments required on these instruments, previously recorded as Preferred Dividends of Subsidiaries and Trust Preferred Distributions, were recorded as Interest Expense in 2004 and for the last six months of 2003 on the company's Statements of Consolidated Income. The company intends to redeem the \$200 million of mandatorily redeemable trust preferred securities prior to the end of February 2005. Therefore, that amount is classified as a current liability under Due to Unconsolidated Affiliates at December 31, 2004.

#### Revenues and Expenses with Unconsolidated Affiliates

During 2004 and 2003, Sempra Generation recorded \$60 million and \$61 million, respectively, in sales to El Dorado, an unconsolidated affiliate, and recorded \$71 million and \$69 million, respectively, of purchases from El Dorado for those same years. Additionally, during 2004, Sempra Commodities recorded \$28 million of purchases from Topaz Power Partners (Topaz), an unconsolidated affiliate. The sales to Topaz were not material.

#### New Accounting Standards

**SFAS 123 (revised 2004), "Share-Based Payment" (SFAS 123R):** In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS 123R, a revision of SFAS 123, Accounting for Stock-Based Compensation (SFAS 123), which establishes the accounting for transactions in which an entity exchanges its equity instruments for goods or services received. This statement requires companies to measure and record the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award and gives companies three alternative transition methods. The modified prospective method requires companies to recognize compensation cost for unvested awards that are outstanding on the effective date based on the fair value that the company had originally estimated for purposes of preparing its SFAS 123 pro forma disclosures. For all new awards that are granted or modified after the effective date, a company would use SFAS 123R's measurement model. The second alternative is a variation of the modified prospective method, allowing companies to restate earlier interim periods in the year that SFAS 123R is adopted using applicable SFAS 123 pro forma amounts. Under the third alternative, the modified retrospective method, companies would apply the modified prospective method, but also restate their prior financial statements to include the amounts that were previously reported in their pro forma disclosures under the original provisions of SFAS 123. The company has not determined the transition method it will use. The effective date of this statement is July 1, 2005 for the company.

**SFAS 132 (revised 2003), "Employers' Disclosures about Pensions and Other Postretirement Benefits":** This statement revised employers' disclosures about pension plans and other

postretirement benefit plans. It requires disclosures beyond those in the original SFAS 132 about the assets, obligations, cash flows and net periodic benefit cost of defined benefit pension plans and other defined postretirement plans. It does not change the measurement or recognition of those plans. Note 9 provides additional information on employee benefit plans.

**SFAS 143, "Accounting for Asset Retirement Obligations":** Beginning in 2003, SFAS 143 requires entities to record liabilities for future costs expected to be incurred when assets are retired from service, if the retirement process is legally required. It requires recording of the estimated retirement cost over the life of the related asset by depreciating the present value of the obligation (measured at the time of the asset's acquisition) and by accreting the present value of the estimated future obligation over the asset's estimated useful life. The adoption of SFAS 143 on January 1, 2003 resulted in the recording of an addition to utility plant of \$71 million, representing the company's share of SONGS' estimated future decommissioning costs (as discounted to the present value at the dates the units began operation), and accumulated depreciation of \$41 million related to the increase to utility plant, for a net increase of \$30 million. It also requires the reclassification of utilities' estimated removal costs, which had historically been recorded in accumulated depreciation, to a regulatory liability. At December 31, 2004 and 2003, these costs were \$1.4 billion at both dates for SoCalGas, and \$913 million and \$846 million, respectively, for SDG&E. Implementation of SFAS 143 has had no effect on results of operations and is not expected to have a significant effect in the future.

On January 1, 2003, the company recorded additional asset retirement obligations of \$20 million associated with the future retirement of a former power plant and three storage facilities.

In accordance with SFAS 143, Sempra Energy identified several other assets for which retirement obligations exist, but whose lives are indeterminate. A liability for these asset retirement obligations will be recorded if and when a life is determinable.

The changes in the asset retirement obligations for the years ended December 31, 2004 and 2003 are as follows (dollars in millions):

	2004	2003
Balance as of January 1	\$ 337*	\$ —
Adoption of SFAS 143	—	329
Accretion expense	24	22
Payments	(10)	(14)
Revision of estimated cash flows	(3)	—
Balance as of December 31	\$ 348*	\$ 337*

\* The current portion of the obligation is included in Other Current Liabilities on the Consolidated Balance Sheets.

In June 2004, the FASB issued a proposed interpretation, Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143. The interpretation would clarify that a legal obligation to perform an asset retirement activity that is conditional on a future event is within the scope of SFAS 143. Accordingly, the interpretation would require an entity to recognize a liability for a conditional asset retirement obligation if the liability's fair value can be reasonably estimated. A final interpretation is expected to be issued by the FASB in the first quarter of 2005 and would be effective for the company on December 31, 2005. The company has not determined the effect the proposed interpretation would have on its financial statements if the proposed interpretation is adopted.

**SFAS 144, "Accounting for Impairment or Disposal of Long-Lived Assets":** In August 2001, the FASB issued SFAS 144, which replaces SFAS 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of. It applies to all long-lived assets. Among other things, SFAS 144 requires that an impairment loss be recorded if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows.

During the third and fourth quarters of 2003, the company recorded impairment charges of \$77 million and \$24 million to write down the carrying value of the assets of Frontier Energy and AEG, respectively. The Frontier Energy impairment resulted from reductions in actual and anticipated sales of natural gas by the utility. The AEG impairment was due to less-than-anticipated customer growth. These charges are included in Other Operating Expenses in the Statements of Consolidated Income. In applying the provisions of SFAS 144, management determined the fair value of such assets based on its estimates of discounted future cash flows.

**SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities":** Effective July 1, 2003, SFAS 149 amended and clarified accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS 133. Under SFAS 149, natural gas forward contracts that are subject to unplanned netting generally do not qualify for the normal purchases and normal sales exception. ("Unplanned netting" refers to situations whereby contracts are settled by paying or receiving money for the difference between the contract price and the market price at the date on which physical delivery would have occurred. The "normal purchases and normal sales exception" provides for not marking to market contracts that are very rarely settled by means other than physical delivery of the commodity involved in the transaction.) In addition, effective January 1, 2004, power contracts that are subject to unplanned netting and that do not meet the normal purchases and normal sales exception under SFAS 149 will continue to be marked to market. Implementation of SFAS 149 did not have a material impact on reported net income.

**SFAS 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity":** This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS 150 requires that certain mandatorily redeemable financial instruments previously classified in the mezzanine section of the balance sheet be reclassified as liabilities. The company adopted SFAS 150 beginning July 1, 2003 by reclassifying \$200 million of mandatorily redeemable trust preferred securities to Deferred Credits and Other Liabilities and \$24 million of mandatorily redeemable preferred stock of subsidiaries to Deferred Credits and Other Liabilities and to Other Current Liabilities on the Consolidated Balance Sheets. In addition, dividend payments required on these instruments, previously recorded as Preferred Dividends of Subsidiaries and Trust Preferred Distributions, are now recorded as Interest Expense on the company's Statements of Consolidated Income. For the six months ended December 31, 2003, the related amount recorded as interest expense totaled \$9 million. On December 31, 2003, the \$200 million of mandatorily redeemable trust preferred securities was further reclassified to Due to Unconsolidated Affiliates as a result of the adoption of FIN 46 as discussed below.

**SFAS 151, "Inventory Costs, an amendment of ARB No. 43, Chapter 4":** This statement amends the guidance in ARB No. 43, Chapter 4, Inventory Pricing, to clarify the accounting for abnormal amounts of idle facility expense, freight, handling cost and wasted material. This statement requires that those items be recognized as current-period charges regardless of whether they meet the criteria of "abnormal". The statement is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The company does not expect that this statement will have a material impact on the company's financial statements.

**EITF 98-10, "Accounting for Contracts Involved in Energy Trading and Risk Management Activities":** EITF 98-10 provided for marking to market commodities and arrangements that are not marked to market by SFAS 133 unless certain hedging standards specified in SFAS 133 are complied with. For the company, this consists of certain inventory, and contracts involving transportation and storage. The specified hedging standards have been complied with for a portion of the otherwise-excluded items. A substantial majority of the company's items covered by EITF 98-10 are covered by SFAS 133. On January 1, 2003, the company recorded the initial effect of Issue 98-10's rescission as a

cumulative effect of a change in accounting principle, which reduced after-tax earnings by \$29 million. Neither the cumulative nor the ongoing effect impacts the company's cash flow or liquidity. Additional information on derivative instruments is provided in Note 11.

**FIN 46, "Consolidation of Variable Interest Entities, an interpretation of ARB No. 51":** FIN 46, as revised by FIN 46R, requires an enterprise to consolidate a variable interest entity (VIE), as defined in FIN 46, if the company is the primary beneficiary of a VIE's activities. VIEs are enterprises that have certain characteristics defined in FIN 46.

Sempra Energy adopted FIN 46 on December 31, 2003, resulting in the consolidation of two VIEs for which it is the primary beneficiary. One of the VIEs (Mesquite Trust) was the owner of the Mesquite Power plant for which the company had a synthetic lease agreement. The company recorded an after-tax credit of \$9 million in the fourth quarter of 2003 for the cumulative effect of the change in accounting principle. The company bought out the lease in January 2004 and now owns the plant.

The other VIE is AEG. Consolidation of AEG resulted in Sempra Energy's recording of 100 percent of AEG's balance sheet and results of operations, whereas it previously recorded only its share of AEG's net operating results. Due to AEG's consolidation, the company recorded an after-tax charge of \$26 million in the fourth quarter of 2003 for the cumulative effect of the change in accounting principle. During the first quarter of 2004, Sempra Energy's board of directors approved management's plan to dispose of AEG. Note 4 provides further discussion concerning this matter and the April 2004 disposal of AEG. Had AEG and the Mesquite Trust been consolidated in 2003 and 2002, the company's net income would have been \$662 million and \$578 million, respectively.

The \$46 million cumulative effect recorded in 2003 on the Statements of Consolidated Income, net of the tax benefit of \$26 million, consists of the following items which are described above (dollars in millions):

FIN 46:	
Mesquite Trust	\$ 9
AEG	(26)
Net charge	(17)
EITF 98-10	(29)
Total charge	\$(46)

In addition, contracts under which SDG&E acquires power from generation facilities otherwise unrelated to SDG&E could result in a requirement for SDG&E to consolidate the entity that owns the facility. As permitted by the interpretation, SDG&E is continuing the process of determining whether it has any such situations and, if so, gathering the information that would be needed to perform the consolidation. The effects of this, if any, are not expected to significantly affect the financial position of SDG&E and there would be no effect on results of operations or liquidity.

**FASB Staff Position (FSP) 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003":** The Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the "Act") was enacted in December of 2003. The Act establishes a prescription drug benefit under Medicare, known as "Medicare Part D," and a tax-exempt federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that actuarially is at least equivalent to Medicare Part D. At December 31, 2003, the company elected a one-time deferral of the accounting for the Act, as permitted by FSP 106-1, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003.

In May 2004, the FASB issued FSP 106-2, which supersedes FSP 106-1 and provides guidance on the accounting, disclosure, effective date and transition requirements related to the Medicare Prescription Drug Act. During 2004, the company adopted FSP 106-2 retroactive to the beginning of the year.

The company and its actuarial advisors determined that benefits provided to certain participants will actuarially be at least equivalent to Medicare Part D, and, accordingly, the company will be entitled to an expected tax-exempt subsidy that reduces the company's accumulated postretirement benefit obligation under the plan at January 1, 2004 by \$102 million and the net postretirement benefit cost for 2004 by \$13 million. Employee benefit plans are discussed further in Note 9.

## **NOTE 2. RECENT ACQUISITIONS AND INVESTMENTS**

### **Sempra Commodities**

Sempra Commodities spent \$74 million and \$27 million in 2004 and 2003, respectively, related to the development of Bluewater Gas Storage, LLC, a natural gas storage facility in Michigan. Sempra Commodities owns the rights to develop the facility and to utilize its capacity to store natural gas for customers who buy, sell or transport natural gas in Michigan. The Bluewater Gas Storage facility commenced commercial operations in May 2004.

During 2002, Sempra Commodities completed \$119 million of acquisitions that added base metals trading and warehousing to its trading business. In February 2002, Sempra Commodities completed the acquisition of London-based Sempra Metals Limited, a leading metals trader on the London Metals Exchange, for \$65 million, net of cash acquired. In April 2002, Sempra Commodities completed the acquisition of the assets of New York-based Sempra Metals & Concentrates Corp., a leading global trader of copper, lead and zinc concentrates, for \$24 million. Also in April 2002, Sempra Commodities completed the acquisition of Henry Bath & Sons Limited, which provides warehousing services for non-ferrous metals in Europe and Asia, and the assets of the U.S. warehousing business of Henry Bath, Inc., for a total of \$30 million, net of cash acquired.

As discussed further in Note 1, the company recognized an extraordinary after-tax gain of \$16 million for negative goodwill for the acquisitions of the base metals and concentrates businesses. Goodwill of \$21 million was recorded in connection with the acquisition of the metals warehousing business.

### **Sempra Generation**

In August 2003, Sempra Generation obtained approvals by the California Energy Commission for the company's 550-megawatt (MW) Palomar power plant in Escondido, California. In June 2004, SDG&E received CPUC approval of its plans to purchase the Palomar plant from Sempra Generation after construction is completed in 2006. Construction of the project began in July 2004.

The 1,250-MW Mesquite Power plant, located near Phoenix, Arizona, cost \$686 million and provides electricity to wholesale energy markets in the Southwest. The first phase of commercial operations (50 percent of the plant's total capacity) began in June 2003. The second phase of commercial operations (the remaining 50 percent) began in December 2003. As of December 31, 2003, this project was owned by the Mesquite Trust and financed through a synthetic lease agreement. Through December 31, 2003, Sempra Generation had borrowed \$630 million under this facility. All amounts above \$280 million required collateralization through purchases of U.S. Treasury obligations. The collateralized U.S. Treasury obligations amounted to \$363 million at December 31, 2003. This is included in Short-Term Investments on the Consolidated Balance Sheets at December 31, 2003. As a result of implementing FIN 46, Sempra Energy consolidated the Mesquite Trust, which had total assets and total liabilities of \$643 million and \$630 million, respectively, at December 31, 2003. Further discussion of this is provided under "New Accounting Standards" in Note 1. In January 2004, Sempra Generation

purchased all of the power plant assets of Mesquite Trust for \$631 million and extinguished the related debt. The purchase required cash of \$268 million and the liquidation of the \$363 million in treasury securities held by the Mesquite Trust as collateral.

Termoeléctrica de Mexicali (TDM), a 625-MW power plant near Mexicali, Baja California, Mexico, commenced operations in July 2003. In May 2003, a federal judge issued an order finding that the U.S. Department of Energy's (DOE) abbreviated assessment of TDM and another, unaffiliated Mexicali power plant, failed to evaluate the plants' environmental impact adequately and called into question the U.S. permits they received to build their cross-border transmission lines. On July 8, 2003, the judge ordered the DOE to conduct additional environmental studies, but denied the plaintiffs' request for an injunction blocking operation of the transmission lines, thus allowing the continued operation of the TDM plant. The DOE finalized its environmental analysis per the court order on December 17, 2004, and is expected to issue a Record of Decision during the second quarter of 2005. The DOE will then determine whether to grant new permits for the cross-border transmission lines. Plaintiffs may elect to dismiss their complaint or to further challenge the agency action. If a stipulation of dismissal is not filed to terminate the litigation by August 15, 2005, the DOE will file a motion by August 22, 2005, showing cause why the court should not set aside the permits. In that event, court hearings may take place in the fourth quarter of 2005. Through December 31, 2004, TDM has made capital expenditures of \$343 million.

In October 2002, Sempra Generation purchased the 305-MW, coal-fired Twin Oaks power plant for \$120 million. Sempra Generation sells substantially all of the output of the plant under a five-year contract expiring on October 1, 2007. In connection with the acquisition, Sempra Generation also assumed a contract that includes annual commitments to purchase lignite coal for the plant until an aggregate minimum volume has been achieved or through 2025. Note 16 provides additional information on the commitments.

#### **Sempra LNG**

In April 2004, Sempra LNG announced plans to develop and construct a \$600 million liquefied natural gas (LNG) receiving terminal near Port Arthur, Texas. The terminal would be capable of processing 1.5 billion cubic feet (bcf) of natural gas per day and could be expanded to 3 bcf per day. The company is currently in the process of obtaining FERC approval for the construction of the terminal. The project is expected to begin construction in 2006, with start-up slated for 2009.

In October 2004, Sempra LNG signed a sale and purchase agreement with British Petroleum for the supply of 500 million cubic feet of natural gas per day from Indonesia's Tangguh liquefaction facility to Sempra LNG's Energía Costa Azul regasification terminal. The terminal is expected to cost between \$900 million and \$1 billion, including related pipeline costs. The 20-year agreement provides for pricing tied to the Southern California border index for natural gas and will supply half the capacity of Energía Costa Azul.

Also in October 2004, Sempra LNG entered into an agreement with Shell International Gas Limited (Shell) by which Shell has contracted to purchase half of the initial capacity of Energía Costa Azul for an initial period of 20 years. This replaces a prior arrangement that contemplated that Shell would have a 50% equity interest in Energía Costa Azul. In December 2004, Sempra LNG entered into two additional contracts: one for the construction of the terminal and one for the construction of the project's breakwater. Note 16 provides additional discussion on commitments related to these contracts.

Also in connection with this project, Mexico's national environmental agency issued an environmental permit in April 2003. Three other significant permits, an operating permit from Mexico's energy

regulatory commission, a local land-use permit from the City of Ensenada and a coastal zone use permit, were granted in 2003. The permit to construct marine facilities was received in 2004. Construction of Energía Costa Azul began in January 2005.

In January 2005, Sempra LNG was awarded a 15-year natural gas supply contract by Mexico's state-owned electric utility, Comisión Federal de Electricidad (CFE). The contract is estimated at \$1.4 billion over its life and supports the CFE's future energy needs in northern Baja California, including the Presidente Juárez power plant in Rosarito, and it is anticipated that it will use natural gas processed at Energía Costa Azul. Starting in 2008 and running through 2022, the agreement provides the CFE with an average of about 130 million cubic feet per day of natural gas.

In April 2003, Sempra LNG completed its acquisition of the proposed Cameron LNG project in Hackberry, Louisiana from a subsidiary of Dynegy, Inc. Sempra LNG paid Dynegy \$36 million for the acquisition, which included rights to the location and to the project as it stood in the licensing stage. In 2004, an additional payment of \$17 million was made as certain benchmarks and milestones of the project were met. The total cost of the project is expected to be \$700 million. The terminal is currently designed to supply 1.5 bcf of natural gas per day. Construction is expected to begin in 2005 and commercial operations are expected to begin in 2008. The FERC approved the construction and operation of the project in September 2003. Cameron LNG is currently seeking from the FERC a modest design change to its marine facilities. In December 2004, Sempra LNG contracted with Norway's Aker Kvaerner and Japan's Ishikawajima-Harima Heavy Industries to build the terminal. The contract is valued at approximately \$500 million, but is not yet binding.

Sempra LNG currently leases land in Louisiana for the development of the Cameron terminal. In connection with the purchase of Cameron, Sempra LNG and the lessor agreed to certain lease amendments, including an increase in the annual rent, addition of wharfage fees and extension of the lease term for another 30 years. The lease amendments are contingent upon obtaining project financing or commencement of construction. In December 2004, Sempra LNG renewed the terms under the original land lease for another five-year period. Rent payments included in the table of future minimum rental payment obligations in Note 16 are based on the original land lease. Should the terms of the amended lease be triggered, total rent payments and wharfage fees would be \$47 million over 30 years.

#### **Sempra Pipelines & Storage**

In April 2004, the company acquired land and associated rights for the development of a salt-cavern natural gas storage facility in Evangeline Parish, Louisiana. This facility, operating as the Pine Prairie Energy Center, will consist of three salt caverns with a total capacity of 24 bcf of natural gas. The facility is expected to cost \$175 million and to begin operations in 2006. The company is negotiating contracts to sell the capacity of this facility. FERC has issued a certificate of public convenience and necessity for the project and authorized Pine Prairie to charge market-based rates.

In July 2004, the company acquired the rights to develop a salt-cavern natural gas storage facility located in Calcasieu Parish, Louisiana. This facility, operating as Liberty Gas Storage (Liberty), is expected to have capacity of 17 bcf. Liberty is estimated to cost \$150 million and to begin operation in 2006.

In 2002, Sempra Pipelines & Storage completed construction of the 140-mile Gasoducto Bajanorte Pipeline that connects the Rosarito Pipeline south of Tijuana, Mexico with a TransCanada pipeline that connects to Arizona. Sempra Pipelines & Storage continues to incur costs for the development of a spur line connecting the Energía Costa Azul terminal to Gasoducto Bajanorte and for the expansion of the pipeline. The company has made capital expenditures of \$5 million, \$7 million and \$37 million in the pipeline in 2004, 2003 and 2002, respectively, and a total through December 31, 2004 of \$123 million.

Sempra Pipelines & Storage's Mexican subsidiaries build and operate natural gas distribution systems in Mexicali, Chihuahua and the La Laguna-Durango zone in north-central Mexico. In February 2003, Sempra Pipelines & Storage purchased the remaining minority interests in its Mexican subsidiaries. Through December 31, 2004, the distribution companies have made capital expenditures aggregating \$142 million. Total capital expenditures for these subsidiaries were \$15 million in each of 2004, 2003 and 2002.

These projects are further discussed in Note 16.

**NOTE 3. INVESTMENTS IN UNCONSOLIDATED SUBSIDIARIES**

Investments are generally accounted for under the equity method when the company has an ownership interest of twenty to fifty percent. In these cases, the company's pro rata shares of the subsidiaries' net assets are included in Investments on the Consolidated Balance Sheets, and are adjusted for the company's share of each investee's earnings or losses, dividends and foreign currency translation effects. Earnings are recorded as equity earnings on the Statements of Consolidated Income in Other Income, Net. The company accounts for certain investments in housing partnerships made before May 19, 1995 under the cost method, whereby they are amortized over ten years based on the expected residual value. The company has no unconsolidated subsidiaries where its ability to influence or control an investee differs from its ownership percentage.

The company's long-term investments are summarized as follows:

(Dollars in millions)	December 31,	
	2004	2003
<b>Equity method investments:</b>		
Chilquinta Energía	\$ 376	\$ 337
Luz del Sur	157	177
Sodigas Pampeana and Sodigas Sur	82	66
Elk Hills Power	217	218
El Dorado Energy	55	68
Topaz Power Partners	66	—
Housing partnerships	146	175
Sempra Financial synthetic-fuel partnerships	12	14
Total	1,111	1,055
Cost method investments — housing partnerships	36	47
Investments in unconsolidated subsidiaries	1,147	1,102
Other	17	10
<b>Total long-term investments</b>	<b>\$ 1,164</b>	<b>\$ 1,112</b>

For equity method investments, costs in excess of equity in net assets (goodwill) were \$238 million and \$232 million at December 31, 2004 and 2003, respectively. Through December 31, 2001, the excess of the investment over the related equity in net assets had been amortized over various periods, primarily forty years. In accordance with SFAS 142, amortization ceased in 2002. Costs in excess of the underlying equity in net assets will continue to be reviewed for impairment in accordance with APBO 18. Descriptive information concerning each of these investments follows.

**Sempra Pipelines & Storage**

Sempra Pipelines & Storage and PSEG Global (PSEG), an unaffiliated company, each own a 50-percent interest in Chilquinta Energía S.A., a Chilean electric utility.



On April 1, 2004, Sempra Pipelines & Storage and PSEG sold a portion of their interests in Luz del Sur, a Peruvian electric utility, for a total of \$62 million. Each party had a 44-percent interest in Luz del Sur prior to the sale and a 38-percent interest after the sale was completed. As a result of the sale, Sempra Pipelines & Storage recognized a \$5 million after-tax gain, which is included in Other Income, Net on the Statements of Consolidated Income.

Sempra Pipelines & Storage also owns 43 percent of two Argentine natural gas utility holding companies, Sodigas Pampeana and Sodigas Sur. As a result of the devaluation of the Argentine peso at the end of 2001 and subsequent declines in the value of the peso, Sempra Pipelines & Storage had reduced the carrying value of its investment downward by a cumulative total of \$198 million as of December 31, 2004. These non-cash adjustments continue to occur based on fluctuations in the Argentine peso. They do not affect net income, but increase or decrease other comprehensive income (loss) and accumulated other comprehensive income (loss).

The related Argentine economic decline and government responses (including Argentina's unilateral, retroactive abrogation of utility agreements early in 2002) continue to adversely affect the operations of these Argentine utilities. In 2002, Sempra Pipelines & Storage initiated arbitration proceedings under the 1994 Bilateral Investment Treaty between the United States and Argentina for recovery of the diminution of the value of its investments that has resulted from Argentine governmental actions. In 2003, Sempra Pipelines & Storage filed its legal brief with the International Center for Settlement of Investment Disputes, outlining its claims for \$258 million. The company has also presented additional information that may provide a basis for a larger award. A decision is expected in 2006. Sempra Energy also has a \$48.5 million political-risk insurance policy under which it has filed a claim to recover a portion of the investments' diminution in value and has commenced the arbitration procedure with the insurance company to determine coverage and the amount of the loss under the policy.

#### **Sempra Generation**

The 550-MW Elk Hills Power (Elk Hills) project, which is located near Bakersfield, California, began commercial operations in July 2003. Elk Hills is 50 percent owned by Sempra Generation in a joint venture with Occidental Energy Ventures Corporation.

The 480-MW El Dorado power plant, located near Las Vegas, Nevada, began commercial operations in May 2000. The El Dorado Energy project is 50 percent owned by Sempra Generation in a joint venture partnership with Reliant Energy Power Generation.

On July 1, 2004, Topaz, a 50/50 joint venture between Sempra Energy Partners and Carlyle/Riverstone, acquired ten Texas power plants from American Electric Power (AEP), including the 632-MW coal-fired Coletto Creek Power Station. Topaz acquired these assets for \$430 million in cash and the assumption of various environmental and asset retirement liabilities currently estimated at \$50 million. \$355 million of the purchase price was provided by non-recourse project financing related solely to the acquisition of the Coletto Creek Power Station. Because of possible revisions to the valuation of the environmental and asset retirement obligations, the allocation of the purchase price remains subject to adjustment until June 30, 2005.

The transaction included the acquisition of six operating power plants with generating capacity of 1,950 MW and four inactive power plants capable of generating 1,863 MW. Concurrently with the acquisition, Topaz sold one of the inactive power plants and no gain or loss was recorded on the transaction. Topaz has entered into several power sales agreements for 572 MW of Coletto Creek Power Station's capacity. As of December 31, 2004, these power sales agreements had a remaining weighted-average life of 4.4 years. Sempra Generation manages the plants.

In conjunction with the acquisition of the plants, Sempra Energy provided AEP a guarantee for certain specified liabilities described in the acquisition agreement. This guarantee is limited to \$75 million for

the first five years after the acquisition date and \$25 million for the next five years, but not more than \$75 million over the entire 10-year period. Management does not expect any material losses to result from the guarantee because performance is not expected to be required and, therefore, management believes that the fair value of the guarantee is immaterial.

**Sempra Financial**

Sempra Financial invests as a limited partner in affordable-housing properties. Sempra Financial's portfolio includes 1,300 properties throughout the United States that are expected to provide income tax benefits (primarily from income tax credits) over 10-year periods. Whether Sempra Financial will invest in additional properties will depend on Sempra Energy's income tax position.

On July 1, 2004, Sempra Financial sold its investment in an enterprise that earns Section 29 income tax credits. That investment comprised one-third of Sempra Energy's Section 29 participation, the rest being held by Sempra Commodities, and was sold because the company's alternative minimum tax position defers utilization of the credits in the determination of income taxes currently payable. The transaction has been accounted for under the cost-recovery method, whereby future proceeds in excess of the carrying value of the investment will be recorded as income when they are received. As a result of this sale, Sempra Financial will not be receiving Section 29 income tax credits in the future. Additional discussion of related income tax issues is provided in Note 8.

**Sempra Commodities**

At December 31, 2004 and 2003, Sempra Commodities had \$14 million and \$2 million, respectively, of available-for-sale securities included in Other Investments. Purchases of available-for-sale securities were \$5 million in 2004. Unrealized gains, net of tax, reported in other comprehensive income were \$4 million in 2004. No sales have been recorded since inception.

**NOTE 4. DISCONTINUED OPERATIONS**

In the first quarter of 2004, Sempra Energy's board of directors approved management's plan to dispose of its interest in AEG, which markets power and natural gas commodities to commercial and residential customers in the United Kingdom. This disposal met the criteria established for recognition as discontinued operations under SFAS 144, Accounting for the Impairment or Disposal of Long-Lived Assets. In April 2004, AEG went into administrative receivership and substantially all of the assets were sold. This transaction resulted in an after-tax loss of \$2 million in 2004, which has been reported separately on the Statements of Consolidated Income.

The net losses from discontinued operations were \$25 million for the year ended December 31, 2004 (including the \$2 million loss on disposal). During 2003 and 2002, the company accounted for its investment in AEG under the equity method of accounting. As such, for the years ended December 31, 2003 and 2002, the company recorded its share of AEG's net losses, \$5 million and \$10 million, respectively, in Other Income, Net on the Statements of Consolidated Income. Additionally, during the fourth quarter of 2003, the company recorded an after-tax charge of \$21 million to write down the carrying value of assets at AEG. Effective December 31, 2003, AEG was consolidated as a result of the adoption of FIN 46, as discussed in Note 1.

Included within the net loss from discontinued operations are AEG's operating results, summarized below:

(Dollars in millions)	Year ended December 31, 2004
Operating revenues	\$ 201
Loss from discontinued operations, before income tax benefit of \$7	\$ (30)
Loss on disposal of discontinued operations, before income tax benefit of \$4	\$ (6)

AEG's balance sheet data, excluding intercompany balances (which are significant) eliminated in consolidation, are summarized below:

(Dollars in millions)	December 31, 2004	December 31, 2003
<b>Assets:</b>		
Accounts receivable	\$ 37	\$ 137
Other current assets	33	83
<b>Total assets</b>	<b>\$ 70</b>	<b>\$ 220</b>
<b>Liabilities:</b>		
Accounts payable	\$ —	\$ 36
Other current liabilities	17	16
<b>Total liabilities</b>	<b>\$ 17</b>	<b>\$ 52</b>

**NOTE 5. SHORT-TERM BORROWINGS**

**Committed Lines of Credit**

At December 31, 2004, the company had available \$4.5 billion in unused, committed lines of credit to provide liquidity and support commercial paper. As of December 31, 2004, \$34 million of the lines supported variable-rate debt.

The California Utilities have a combined \$500 million three-year syndicated revolving credit facility under which each utility individually may borrow up to \$300 million, subject to a combined borrowing limit for both utilities of \$500 million. Borrowings under the agreement bear interest at rates varying with market rates and the utility's credit rating. The agreement requires each utility to maintain, at the end of each quarter, a ratio of total indebtedness to total capitalization (as defined in the agreement) of no more than 60 percent. Borrowings under the agreement are individual obligations of the borrowing utility and a default by one utility would not constitute a default, or preclude borrowings by, the other. At December 31, 2004, the California Utilities had no amounts outstanding under this facility. SoCalGas had \$30 million of commercial paper outstanding as of December 31, 2004.

Sempra Commodities has a two-year syndicated revolving line of credit providing up to \$1 billion of extensions of credit (consisting of borrowings, letters of credit and other credit support accommodations) to Sempra Commodities and certain of its affiliates. The agreement expires in 2006. The amount of credit extended on a non-guaranteed basis is limited by the amount of a borrowing base consisting of receivables, inventories and other assets of Sempra Commodities that secure the credit facility and that are valued for purposes of the borrowing base at varying percentages of current market value. Credit utilization above the borrowing base (up to a maximum of \$500 million) is guaranteed by Sempra Energy subject to the overall \$1 billion credit limit. Non-guaranteed extensions of credit bear interest and fees that vary with Sempra Commodities' tangible net worth, and guaranteed extensions bear interest and fees varying with Sempra Energy's credit ratings. Extensions of credit are subject to the absence of any development or event that has had or would reasonably be expected to have a material adverse effect on Sempra Commodities. The facility also requires Sempra Commodities to meet certain financial tests at the end of each quarter (including current ratio, leverage ratio and minimum consolidated net worth tests) and (while guaranteed borrowings are outstanding) also requires Sempra Energy to meet, at the end of each quarter and as defined in the credit facility, a leverage ratio of consolidated indebtedness to consolidated total capitalization of not more than 65 percent. It also imposes certain other limitations on Sempra Commodities, including limitations on other indebtedness, capital expenditures, liens, transfers of assets, investments, loans, advances, dividends, other distributions, modifications of risk-management policies and transactions with affiliates. At December 31, 2004, outstanding extensions of credit under the facility totaled \$489 million, including \$439 million in letters of credit and \$50 million in borrowings outstanding.

Sempra Global has a \$1.5 billion three-year syndicated revolving credit facility that expires in 2007, and a substantially identical \$500 million three-year revolving credit facility that expires in 2006. Borrowings under each facility are guaranteed by Sempra Energy and bear interest at rates varying with market rates and Sempra Energy's credit rating. Each facility requires Sempra Energy to maintain, at the end of each quarter, a ratio of total indebtedness to total capitalization (as identically defined in each facility) of no more than 65 percent. Sempra Global had letters of credit of \$36 million and \$220 million of commercial paper, guaranteed by Sempra Energy, outstanding at December 31, 2004. As of December 31, 2003, Sempra Global had no commercial paper and a letter of credit of \$18 million outstanding.

PE has a revolving credit commitment of \$500 million that expires in September 2005. Borrowings under the credit agreement are available to provide loans to Sempra Global and would bear interest at rates varying with market rates, PE's credit ratings and amounts borrowed. Borrowings are guaranteed by Sempra Energy and would be subject to mandatory repayment if Sempra Energy's or SoCalGas' ratio of debt to total capitalization (as defined in the agreement) were to exceed 65 percent, or should there be a change in law materially and adversely affecting the ability of SoCalGas to pay dividends or make other distributions to PE. No amounts were outstanding under this facility at December 31, 2004.

Sempra LNG has a \$1.25 billion five-year syndicated revolving credit facility that expires in 2009. The \$1.25 billion also provides for the issuance of letters of credit not exceeding \$200 million outstanding at any one time. Borrowings, letter of credit obligations and other obligations under the facility are guaranteed by Sempra Energy and bear interest at rates varying with market rates and Sempra Energy's credit ratings. The facility requires Sempra Energy to maintain, at the end of each quarter, a ratio of total indebtedness to total capitalization (as defined in the agreement) of no more than 65 percent. Sempra LNG did not have any outstanding borrowings against this line at December 31, 2004.

#### **Uncommitted Lines of Credit**

At December 31, 2004, Sempra Commodities had \$226 million in various uncommitted lines of credit that are guaranteed by Sempra Energy and bear interest at rates varying with market rates and Sempra Energy's credit rating. At December 31, 2004, Sempra Commodities had \$103 million of letters of credit and \$25 million of short-term borrowings outstanding against these lines. At December 31, 2003, Sempra Commodities had letters of credit of \$420 million, and no short-term borrowings outstanding.

#### **Other**

In addition to the lines of credit, Sempra Energy had \$80 million and \$28 million of other short-term debt outstanding at December 31, 2004 and 2003, respectively, that was due to parties other than financial institutions. The company's weighted average interest rate on the total short-term debt outstanding was 2.82% and 7.56% at December 31, 2004 and 2003, respectively.

**NOTE 6. LONG-TERM DEBT**

(Dollars in millions)	December 31,	
	2004	2003
<b>First mortgage bonds</b>		
Variable rate (2.63% at December 31, 2004) December 1, 2009	\$ 100	\$ —
4.375% January 15, 2011	100	100
Variable rates after fixed-to-floating rate swaps (2.69% at December 31, 2004) January 15, 2011	150	150
4.8% October 1, 2012	250	250
6.8% June 1, 2015	14	14
5.45% April 15, 2018	250	250
5.9% June 1, 2018	68	68
5.9% September 1, 2018	93	176
5.85% June 1, 2021	60	60
5.25% to 7% December 1, 2027	150	225
After floating-to fixed rate swap expiring 2009:		
2.516% to 2.832% January and February 2034	176	—
2.8275% May 1, 2039	75	—
6.1% September 1, 2019	—	35
Variable rates September 1, 2020	—	58
6.875% November 1, 2025	—	175
	<b>1,486</b>	<b>1,561</b>
<b>Other long-term debt</b>		
5.60% Equity Units May 17, 2007*	600	600
7.95% Notes March 1, 2010	200	500
Notes at variable rates after fixed-to-floating swap (5.97% at December 31, 2004) March 1, 2010	300	—
6.0% Notes February 1, 2013	400	400
6.95% Notes December 1, 2005	300	300
Notes at variable rates (2.82% at December 31, 2004) May 21, 2008	300	—
4.75% Notes May 15, 2009	300	—
Rate-reduction bonds, 6.31% to 6.37% at December 31, 2004 payable annually through 2007	198	263
5.9% June 1, 2014	130	130
Debt incurred to acquire limited partnerships, secured by real estate, at 7.13% to 9.35% annually through 2009	76	110
Employee Stock Ownership Plan		
Bonds at 4.213% November 1, 2014	82	82
Bonds at variable rates (3.00% at December 31, 2004) November 1, 2014	33	19
5.5% December 1, 2021	60	60
5.3% July 1, 2021	39	39
4.9% March 1, 2023	25	25
6.375% May 14, 2006	8	8
5.67% January 15, 2028	5	5
Variable rates September 2005	—	630
Notes at variable rates after a fixed-to-floating rate swap July 1, 2004	—	500
Other debt	33	15
Capitalized leases	6	8
Market value adjustments for interest rate swaps, net (expiring 2009 — 2011)	13	23
	<b>4,594</b>	<b>5,278</b>
Current portion of long-term debt	(398)	(1,433)
Unamortized discount on long-term debt	(4)	(4)
<b>Total</b>	<b>\$ 4,192</b>	<b>\$ 3,841</b>

\* 4.62% after remarketing in February 2005, as discussed in Note 13.

Excluding capital leases, which are described in Note 16, and market value adjustments for interest-rate swaps, maturities of long-term debt are:

(Dollars in millions)	
2005	\$ 398
2006	100
2007	683
2008	308
2009	425
Thereafter	2,661
Total	\$ 4,575

Holders of variable-rate bonds may require the issuer to repurchase them prior to scheduled maturity. However, since repurchased bonds would be remarketed and funds for repurchase are provided by long-term revolving credit agreements (which are generally renewed upon expiration and which are described in Note 5), it is expected that the bonds will be held to the maturities stated above.

#### Callable Bonds

At the company's option, certain bonds are callable at various dates: \$611 million in 2005, \$308 million in 2006, \$82 million in 2007, and \$169 million thereafter.

#### First Mortgage Bonds

First mortgage bonds are issued by the California Utilities and secured by a lien on their respective utility plant. The California Utilities may issue additional first mortgage bonds upon compliance with the provisions of their bond indentures, which require, among other things, the satisfaction of pro forma earnings-coverage tests on first mortgage bond interest and the availability of sufficient mortgaged property to support the additional bonds, after giving effect to prior bond redemptions. The most restrictive of these tests (the property test) would permit the issuance, subject to CPUC authorization, of an additional \$3 billion of first mortgage bonds at December 31, 2004.

In June 2004, SDG&E issued \$251 million of first mortgage bonds and applied the proceeds in July to refund an identical amount of first mortgage bonds and related tax-exempt industrial development bonds of a shorter maturity. The bonds secure the repayment of tax-exempt industrial development bonds of an identical amount, maturity and interest rate issued by the City of Chula Vista, the proceeds of which were loaned to SDG&E and which are being repaid with payments on the first mortgage bonds. When SDG&E called the \$251 million of refunded first mortgage bonds in July 2004, it incurred \$6 million in call premium costs. These costs were recorded as regulatory assets and are being amortized over the life of the retired debt. The bonds were initially issued as auction-rate securities, but SDG&E entered into floating-for-fixed interest-rate swap agreements that effectively changed the refunding bonds' interest rates to fixed interest rates in September 2004. The swaps are set to expire in 2009.

SoCalGas called \$175 million of long-term debt in January 2004 and incurred \$2 million in call premium costs. This amount has been recorded as a regulatory asset and is being amortized over the life of the original issue.

In December 2004, SoCalGas issued \$100 million of first mortgage bonds maturing in 2009. The bonds bear interest at 0.17% above LIBOR.

**Mesquite Power**

The company consolidated Mesquite Trust, the owner of Mesquite Power, on its financial statements as of December 31, 2003 as a result of implementing FIN 46, as described in Notes 1 and 2. The debt outstanding of \$630 million consisted of notes payable due in 2005. In January 2004, Sempra Generation purchased all of the power plant assets of Mesquite Trust for \$631 million and extinguished the related debt. Therefore the liability is classified as short-term at December 31, 2003.

**Equity Units**

In April and May of 2002, the company publicly offered and issued \$600 million of equity units. Additional information on the equity units is provided in Note 13.

**Unsecured Long-term Debt**

Various long-term obligations totaling \$2.8 billion are unsecured at December 31, 2004.

On January 15, 2003, \$70 million of SoCalGas' 5.67% \$75 million medium-term notes were put back to the company.

In May 2004, the company issued \$600 million of senior unsecured notes, consisting of \$300 million of 4.75% fixed-rate notes and \$300 million of floating-rate notes maturing May 15, 2009 and May 21, 2008, respectively. The proceeds of the issuance were used to repay \$500 million of debt maturing July 1, 2004, and for general corporate purposes.

**Rate-Reduction Bonds**

In December 1997, \$658 million of rate-reduction bonds were issued on behalf of SDG&E at an average interest rate of 6.26%. These bonds were issued to facilitate the 10-percent rate reduction mandated by California's electric-restructuring law, which is described in Note 14. They are being repaid over ten years by SDG&E's residential and small-commercial customers through a specified charge on their electricity bills. These bonds are secured by the revenue streams collected from customers and are not secured by, or payable from, utility assets.

**Debt of Employee Stock Ownership Plan (ESOP) and Trust (Trust)**

The Trust covers substantially all of the employees of the parent organization, SoCalGas and most of Sempra Global's subsidiaries. The Trust is used to fund part of the retirement savings plan described in Note 9. The notes, which mature in 2014, are repriced weekly and subject to repurchase by the company at the holder's option, depending on market demand. ESOP debt was paid down by \$13 million during the last three years when approximately 538,000 shares of company common stock were released from the Trust in order to fund the employer contribution to the company savings plan. Interest on the ESOP debt amounted to \$5 million in 2004, \$6 million in 2003 and \$7 million in 2002. Dividends used for debt service amounted to \$2 million in 2004 and 2003, and \$3 million in 2002.

**Interest-Rate Swaps**

The company periodically enters into interest-rate swap agreements to moderate its exposure to interest-rate changes and to lower its overall cost of borrowing. In May 2004, Sempra Energy entered into interest-rate swaps which effectively exchanged the fixed rate on \$300 million of its \$500 million 7.95% notes for a floating rate. The swaps expire in 2010. In September 2004, SDG&E entered into interest-rate swaps to exchange the floating rates on its \$251 million Chula Vista Series 2004 bonds for fixed rates. The swaps expire in 2009. In December 2003, SoCalGas entered into an interest-rate

swap that effectively exchanged the fixed rate on \$150 million of its \$250 million 4.375% first mortgage bonds for a floating rate. The swap expires in 2011. The schedule of long-term debt reflects previous interest-rate swaps related to other debt. Accordingly, market value adjustments to long-term debt of \$10 million and \$19 million were recorded in 2004 and 2003, respectively, to reflect, without affecting net income or other comprehensive income, the unfavorable economic consequences (as measured at December 31, 2004 and 2003) of having entered into the swap transactions.

**NOTE 7. FACILITIES UNDER JOINT OWNERSHIP**

SONGS and the Southwest Powerlink transmission line are owned jointly with other utilities. The company's interests at December 31, 2004, are as follows:

(Dollars in millions)	SONGS	Southwest Powerlink
Percentage ownership	20%	91%
Utility plant in service	\$ 19	\$ 290
Accumulated depreciation and amortization	\$ —	\$ 149
Construction work in progress	\$ 16	\$ 1

The company and the other owners each holds its interest as an undivided interest as tenants in common. Each owner is responsible for financing its share of each project and participates in decisions concerning operations and capital expenditures.

The company's share of operating expenses is included in the Statements of Consolidated Income.

**SONGS Decommissioning**

Objectives, work scope and procedures for the dismantling and decontamination of the SONGS units must meet the requirements of the Nuclear Regulatory Commission (NRC), the Environmental Protection Agency, the CPUC and other regulatory bodies.

The company's share of decommissioning costs for the SONGS units is estimated to be \$328 million in 2004 dollars. Cost studies are updated every three years, with the next update expected to be submitted to the CPUC for its approval in 2006. Rate recovery of decommissioning costs is allowed until the time that the costs are fully recovered, and is subject to adjustment every three years based on the costs allowed by regulators. Collections are authorized to continue until 2013, at which time sufficient funds are expected to have been collected to fully decommission SONGS, but may be extended by CPUC approval until 2022, when the SONGS' operating license ends and the decommissioning of SONGS Units 2 and 3 would be expected to begin.

The amounts collected in rates are invested in externally managed trust funds. Amounts held by the trusts are invested in accordance with CPUC regulations that establish maximum amounts for investments in equity securities (50 percent of the qualified trust and 60 percent of the nonqualified trust), international equity securities (20 percent) and securities of electric utilities having ownership interests in nuclear power plants (10 percent). Not less than 50 percent of the equity portion of the trusts must be invested passively. The securities held by the trust are considered available for sale. These trusts are shown on the Consolidated Balance Sheets at market value. At December 31, 2004, these trusts reflected unrealized gains of \$182 million with the offsetting credits recorded on the Consolidated Balance Sheets in Asset Retirement Obligations and the related regulatory liabilities.

Unit 1 was permanently shut down in 1992, and physical decommissioning began in January 2000. Several structures, foundations and large components have been dismantled, removed and disposed of. Spent nuclear fuel has been removed from the Unit 1 Spent Fuel Pool and stored on-site in an



Independent Spent Fuel Storage Facility (ISFSI) licensed by the NRC. The remaining major work will include dismantling, removal and disposal of all remaining Unit 1 equipment and facilities (both nuclear and non-nuclear components), and decontamination of the site. These activities are expected to be completed in 2008. The ISFSI and the reactor vessel will remain on site until a permanent storage facility becomes available.

Trust investments include:

(Dollars in millions)	Maturity dates	December 31,	
		2004	2003
Municipal bonds	2005 — 2034	\$ 45	\$ 47
U.S. government issues	2005 — 2034	209	181
Short-term cash and other	2005	55	49
Stocks		303	293
<b>Total</b>		<b>\$ 612</b>	<b>\$ 570</b>

Net earnings (loss) were \$45 million in 2004, \$82 million in 2003, and \$(25) million in 2002. Proceeds from sales of securities (which are reinvested) were \$237 million in 2004, \$266 million in 2003 and \$409 million in 2002.

Customer contribution amounts are determined by estimates of after-tax investment returns, decommissioning costs and decommissioning cost escalation rates. Lower actual investment returns or higher actual decommissioning costs would result in an increase in future customer contributions.

Discussion regarding the impact of SFAS 143 is provided in Note 1. Additional information regarding SONGS is included in Notes 14 and 16.

#### NOTE 8. INCOME TAXES

The reconciliation of the statutory federal income tax rate to the effective income tax rate is as follows:

	Years ended December 31,		
	2004	2003	2002
Statutory federal income tax rate	35.0%	35.0%	35.0%
Utility depreciation	3.7	6.7	5.2
State income taxes, net of federal income tax benefit	3.8	7.0	7.0
Tax credits	(13.5)	(22.6)	(18.5)
Income from unconsolidated foreign subsidiaries	(4.2)	(4.3)	(2.0)
Settlement of Internal Revenue Service audit	—	(11.2)	(3.6)
Reduction of prior period state income tax accruals, net of federal income tax benefit	(3.1)	—	—
Reduction of interest rate on prior period federal income tax liabilities, net of tax	(1.7)	—	—
Other, net	(2.7)	(4.3)	(2.9)
<b>Effective income tax rate</b>	<b>17.3%</b>	<b>6.3%</b>	<b>20.2%</b>

The geographic components of total income from operations before income taxes are as follows:

(Dollars in millions)	Years ended December 31,		
	2004	2003	2002
Domestic	\$ 796	\$ 551	\$ 584
Foreign	317	191	137
<b>Total income before income taxes</b>	<b>\$ 1,113</b>	<b>\$ 742</b>	<b>\$ 721</b>

The components of income tax expense are as follows:

(Dollars in millions)	Years ended December 31,		
	2004	2003	2002
<b>Current:</b>			
Federal	\$ 120	\$ 80	\$ 220
State	21	74	56
Foreign	39	11	13
Total	180	165	289
<b>Deferred:</b>			
Federal	17	(126)	(138)
State	(24)	(4)	5
Foreign	26	18	(5)
Total	19	(112)	(138)
Deferred investment tax credits	(6)	(6)	(5)
Total income tax expense	\$ 193	\$ 47	\$ 146

Accumulated deferred income taxes at December 31 relate to the following:

(Dollars in millions)	2004	2003
<b>Deferred tax liabilities:</b>		
Differences in financial and tax bases of depreciable and amortizable assets	\$ 861	\$ 891
Balancing accounts and regulatory assets	124	239
Unrealized revenue	79	63
Partnership income	56	34
Loss on reacquired debt	38	38
Property taxes	25	22
Equity units	21	12
Other	11	—
Total deferred tax liabilities	1,215	1,299
<b>Deferred tax assets:</b>		
General business tax credit carryforward	193	152
Credits from alternative minimum tax	111	77
Investment tax credits	55	61
Net operating losses of foreign entities	104	112
Compensation-related items	173	134
Postretirement benefits	51	31
Other deferred liabilities	29	190
State income taxes	48	57
Bad debt allowance	18	28
Other accruals not yet deductible	35	27
Other	32	51
Total deferred tax assets	849	920
Net deferred income tax liability before valuation allowance	366	379
Valuation allowance	39	20
Net deferred income tax liability	\$ 405	\$ 399

The net deferred income tax liability is recorded on the Consolidated Balance Sheets at December 31 as follows:

(Dollars in millions)	2004	2003
Current (asset) liability	\$ (15)	\$ 31
Noncurrent liability	420	368
Total	\$ 405	\$ 399

In connection with its affordable-housing investments, the company has \$193 million of unused general business tax credits in varying amounts dating back to 1999. The ability to offset these credits against future taxable income will expire between the years 2019 and 2024. The company expects to utilize the credits prior to expiration. In addition, the company has \$111 million of alternative minimum tax credits with no expiration date. All of these credits have been included in the calculation of income tax expense.

Foreign subsidiaries have \$314 million in unused net operating losses available to reduce future income taxes, primarily in Mexico, Canada and the United Kingdom. Significant amounts of these losses become unavailable to reduce future incomes taxes beginning in 2009. Financial statement benefits have been recorded on all but \$88 million of these losses, primarily by offsetting them against deferred tax liabilities with the same expiration pattern and country of jurisdiction. No benefits have been recorded on \$88 million of the losses because they have been incurred in jurisdictions where utilization is sufficiently in doubt.

The company has not provided for U.S. income taxes on foreign subsidiaries' undistributed earnings (\$606 million at December 31, 2004), since they are expected to be reinvested indefinitely outside the U.S. It is not possible to predict the amount of U.S. income taxes that might be payable if these earnings were eventually repatriated.

The company believes it has adequately provided for income tax issues not yet resolved with federal, state and foreign tax authorities. At December 31, 2004, \$186 million was accrued for such matters. Although not probable, the most adverse resolution of these issues could result in additional charges to earnings in future periods. Based upon a consideration of all relevant facts and circumstances, the company does not believe the ultimate resolution of tax issues for all open tax periods will have a materially adverse effect upon its results of operations or financial condition.

The new American Jobs Creation Act enables companies to repatriate monies earned outside the U.S. at an income tax cost of only 15 percent of the normal rate. To achieve this reduction, the repatriation must occur by the end of 2005. The company has not completed its analysis and does not expect to be able to make a decision on the amount of such repatriations, if any, until the fourth quarter of 2005. Among other things, the decision will depend on the level of earnings outside the U.S., the debt level between the company's U.S. and non-U.S. affiliates, and administrative guidance from the Internal Revenue Service.

#### Section 29 Income Tax Credits

On July 1, 2004, Sempra Financial sold its investment in an enterprise that earns Section 29 income tax credits. That investment comprised one-third of Sempra Energy's Section 29 participation and was sold because the company's alternative minimum tax position defers utilization of the credits in the determination of income taxes currently payable. The transaction has been accounted for under the cost-recovery method, whereby future proceeds in excess of the carrying value of the investment will be recorded as income as received. As a result of this sale, Sempra Financial will not be receiving Section 29 income tax credits in the future.

The IRS has conducted various examinations of the partnerships associated with the Section 29 income tax credits, covering various years as recent as 2000, depending on the partnership. It has reported no change in the credits. From acquisition of the facilities in 1998, the company has generated Section 29 income tax credits of \$349 million through December 31, 2004, of which \$98 million were recorded for the year ended December 31, 2004.

In the next three years, if the annual average wellhead price per barrel of oil reaches a certain price, a phase-out of Section 29 credits will begin. For 2005, 2006 and 2007, those prices are \$52.17, \$53.21, and \$54.27, respectively.

**Pacific Enterprises' Quasi-Reorganization**

Effective December 31, 1992, PE effected a quasi-reorganization for financial reporting purposes. The reorganization resulted in a restatement of the company's assets and liabilities to their estimated fair value at December 31, 1992 and the elimination of PE's retained earnings deficit. Since the reorganization was for financial purposes and not a taxable transaction, the company established deferred taxes relative to the book and tax bases differences.

During 2004, the company completed an extensive analysis of PE's deferred tax accounts. The analysis resulted in a \$72 million reduction of the deferred tax liabilities and an offsetting credit to equity. The credit was recorded to equity because the balances related to tax effects of transactions prior to the quasi-reorganization. In 2004, the company also concluded its outstanding IRS examinations and appeals related to PE and its subsidiaries. As of December 31, 2004, the company's balance sheet includes a net deferred tax asset of \$15 million related to remaining reserves arising from the quasi-reorganization.

**NOTE 9. EMPLOYEE BENEFIT PLANS**

The information presented below covers the plans of the company and its principal subsidiaries.

**Pension and Other Postretirement Benefits**

The company has funded and unfunded noncontributory defined benefit plans that together cover substantially all of its employees. The plans provide defined benefits based on years of service and either final average or career salary.

The company also has other postretirement benefit plans covering substantially all of its employees. The life insurance plans are both contributory and noncontributory, and the health care plans are contributory, with participants' contributions adjusted annually. Other postretirement benefits include retiree life insurance, medical benefits for retirees and their spouses, and Medicare Part B reimbursement for certain retirees.

The company maintains dedicated assets in support of its Supplemental Executive Retirement Plan.

There were no amendments to the company's pension and other postretirement benefit plans in 2003 or 2004. During 2002, the company had amendments reflecting retiree cost of living adjustments, which resulted in an increase in the pension plan benefit obligation of \$51 million. Amendments to other postretirement benefit plans related to the transfer of employees to SDG&E and changes to their specific benefits resulted in a decrease in the benefits obligation of \$7 million. The amortization of these changes will affect pension expense in future years.

December 31 is the measurement date for the pension and other postretirement benefit plans. The following table provides a reconciliation of the changes in the plans' projected benefit obligations during the latest two years, the fair value of assets and a statement of the funded status as of the latest two year ends:

(Dollars in millions)	2004	Pension Benefits 2003	2004	Other Postretirement Benefits 2003
<b>CHANGE IN PROJECTED BENEFIT OBLIGATION:</b>				
Net obligation at January 1	\$ 2,578	\$ 2,290	\$ 954	\$ 797
Service cost	49	52	21	19
Interest cost	154	152	51	55
Actuarial loss (gain)	132	285	(64)	116
Benefit payments	(219)	(201)	(40)	(33)
Net obligation at December 31	<b>2,694</b>	<b>2,578</b>	<b>922</b>	<b>954</b>
<b>CHANGE IN PLAN ASSETS:</b>				
Fair value of plan assets at January 1	2,263	1,984	519	409
Actual return on plan assets	269	453	56	90
Employer contributions	27	27	50	53
Benefit payments	(219)	(201)	(40)	(33)
Fair value of plan assets at December 31	<b>2,340</b>	<b>2,263</b>	<b>585</b>	<b>519</b>
Benefit obligation, net of plan assets at December 31	(354)	(315)	(337)	(435)
Unrecognized net actuarial loss	278	273	221	317
Unrecognized prior service cost	74	83	(13)	(13)
Unrecognized net transition obligation	—	1	—	—
Net recorded asset (liability) at December 31	<b>\$ (2)</b>	<b>\$ 42</b>	<b>\$ (129)</b>	<b>\$ (131)</b>

The net asset (liability) is recorded on the Consolidated Balance Sheets at December 31 as follows:

(Dollars in millions)	2004	Pension Benefits 2003	2004	Other Postretirement Benefits 2003
Prepaid benefit cost	\$ 147	\$ 178	\$ —	\$ —
Accrued benefit cost	(149)	(136)	(129)	(131)
Additional minimum liability	(131)	(118)	—	—
Intangible asset	7	9	—	—
Regulatory asset	62	—	—	—
Accumulated other comprehensive income (pretax)	62	109	—	—
Net recorded asset (liability)	<b>\$ (2)</b>	<b>\$ 42</b>	<b>\$ (129)</b>	<b>\$ (131)</b>

The accumulated benefit obligation for defined benefit pension plans was \$2.5 billion and \$2.4 billion at December 31, 2004 and 2003, respectively. The following table provides information concerning pension plans with benefit obligations in excess of plan assets as of December 31.

(Dollars in millions)	2004	Projected Benefit Obligation Exceeds the Fair Value of Plan Assets 2003	2004	Accumulated Benefit Obligation Exceeds the Fair Value of Plan Assets 2003
Projected benefit obligation	\$ 2,290	\$ 2,189	\$ 694	\$ 662
Accumulated benefit obligation	\$ 2,076	\$ 1,994	\$ 692	\$ 661
Fair value of plan assets	<b>\$ 2,085</b>	<b>\$ 2,012</b>	<b>\$ 569</b>	<b>\$ 538</b>

The following table provides the components of net periodic benefit costs (income) for the years ended December 31:

(Dollars in millions)	2004	2003	Pension Benefits 2002	2004	2003	Other Postretirement Benefits 2002
Service cost	\$ 49	\$ 52	\$ 57	\$ 21	\$ 19	\$ 13
Interest cost	154	152	149	51	55	42
Expected return on assets	(154)	(161)	(204)	(36)	(35)	(39)
Amortization of:						
Transition obligation	—	1	1	—	9	9
Prior service cost	9	9	7	(1)	(1)	(1)
Actuarial (gain) loss	12	9	(18)	10	10	—
Regulatory adjustment	(116)	(14)	32	2	(4)	25
<b>Total net periodic benefit cost (income)</b>	<b>\$ (46)</b>	<b>\$ 48</b>	<b>\$ 24</b>	<b>\$ 47</b>	<b>\$ 53</b>	<b>\$ 49</b>

As described in Note 1, the company adopted FSP 106-2 in 2004 retroactive to the beginning of the year. The company and its actuarial advisors determined that benefits provided to certain participants will actuarially be at least equivalent to Medicare Part D, and, accordingly, the company will be entitled to an expected tax-exempt subsidy that reduces the company's accumulated postretirement benefit obligation under the plan at January 1, 2004 by \$102 million and the net postretirement benefit cost for 2004 by \$13 million.

The significant assumptions related to the company's pension and other postretirement benefit plans are as follows:

	2004	Pension Benefits 2003	2004	Other Postretirement Benefits 2003
<b>WEIGHTED-AVERAGE ASSUMPTIONS USED TO DETERMINE BENEFIT OBLIGATION AS OF DECEMBER 31:</b>				
Discount rate	5.66%	6.00%	5.66%	6.00%
Rate of compensation increase	4.50%	4.50%	4.50%	4.50%
<b>WEIGHTED-AVERAGE ASSUMPTIONS USED TO DETERMINE NET PERIODIC BENEFIT COSTS FOR YEARS ENDED DECEMBER 31:</b>				
Discount rate	6.00%	6.50%	6.00%	6.50%
Expected return on plan assets	7.50%	7.50%	7.32%	7.30%
Rate of compensation increase	4.50%	4.50%	4.50%	4.50%

The expected long-term rate of return on plan assets is derived from historical returns for broad asset classes consistent with expectations from a variety of sources, including pension consultants and investment advisors.

	2004	2003
<b>ASSUMED HEALTH CARE COST TREND RATES AT DECEMBER 31:</b>		
Health-care cost trend rate	19.00%*	30.00%*
Rate to which the cost trend rate is assumed to decline (the ultimate trend)	5.50%	5.50%
Year that the rate reaches the ultimate trend	2008	2008

\* This is the weighted average of the increases for all health plans. The rate for these plans ranged from 10% to 20% in 2004 and from 15% to 40% in 2003, respectively.

Assumed health-care cost trend rates have a significant effect on the amounts reported for the health-care plan costs. A one-percent change in assumed health-care cost trend rates would have the following effects:

(Dollars in millions)	1% Increase	1% Decrease
Effect on total of service and interest cost components of net periodic postretirement health-care benefit cost	\$ 13	\$ 10
Effect on the health-care component of the accumulated other postretirement benefit obligation	\$ 134	\$ 106

#### Pension Plan Investment Strategy

The asset allocation for the company's pension trust (which includes other postretirement benefit plans, except for those of the California Utilities separately described below) at December 31, 2004 and 2003 and the target allocation for 2005 by asset categories are as follows:

Asset Category	Target Allocation 2005	Percentage of Plan Assets at December 31,	
		2004	2003
U.S. Equity	45%	45%	45%
Foreign Equity	25	32	30
Fixed Income	30	23	25
Total	100%	100%	100%

The company's investment strategy is to stay fully invested at all times and maintain its strategic asset allocation, keeping the investment structure relatively simple. The equity portfolio is balanced to maintain risk characteristics similar to the S&P 1500 with respect to market capitalization, and industry and sector exposures. The foreign equity portfolios are managed to track the MSCI Europe, Pacific Rim and Emerging Markets indexes. Bond portfolios are managed with respect to the Lehman Aggregate Index. The plan does not invest in securities of the company.

#### Investment Strategy for SoCalGas' Other Postretirement Benefit Plans

The asset allocation for SoCalGas' other postretirement benefit plans at December 31, 2004 and 2003 and the target allocation for 2005 by asset categories are as follows:

Asset Category	Target Allocation 2005	Percentage of Plan Assets at December 31,	
		2004	2003
U.S. Equity	70%	73%	71%
Fixed Income	30	27	27
Cash	0	0	2
Total	100%	100%	100%

SoCalGas' other postretirement benefit plans, which are distinct from other postretirement benefit plans included in the company's pension trust (shown above), are funded by cash contributions from SoCalGas and the retirees. The asset allocation is designed to match the long-term growth of the plan's liability. These plans are managed using index funds.

**Investment Strategy for SDG&E's Postretirement Health Plans**

The asset allocation for SDG&E's postretirement health plans at December 31, 2004 and 2003 and the target allocation for 2005 by asset categories are as follows:

Asset Category	Target	Percentage of	
	Allocation	Plan Assets at	
	2005	2004	2003
U.S. Equity	25%	25%	26%
Foreign Equity	5	6	5
Fixed Income	70	69	69
Total	100%	100%	100%

SDG&E's postretirement health plans, which also are distinct from other postretirement benefit plans included in the company's pension trust (shown above), pay premiums to the health maintenance organization and point-of-service plans from company and participant contributions. SDG&E's investment strategy is to match the long-term growth rate of the liability primarily through the use of tax-exempt California municipal bonds.

**Future Payments**

The company expects to contribute \$34 million to the pension plans and \$58 million to the other postretirement benefit plans in 2005.

The following table reflects the total benefits expected to be paid for the next 10 years to current employees and retirees from the plans or from the company's assets, including both the company's share of the benefit cost and, where applicable, the participants' share of the costs, which is funded by participant contributions to the plans.

(Dollars in millions)	Pension Benefits	Other Postretirement Benefits
2005	\$ 175	\$ 42
2006	\$ 194	\$ 45
2007	\$ 190	\$ 48
2008	\$ 200	\$ 50
2009	\$ 208	\$ 52
2010 — 2014	\$ 1,168	\$ 295

The expected future Medicare Part D subsidy payments are as follows:

(Dollars in millions)	
2005	\$ —
2006	\$ 3
2007	\$ 3
2008	\$ 4
2009	\$ 4
2010 — 2014	\$24

**Savings Plans**

The company offers trustee savings plans to all eligible employees. Eligibility to participate in the plans is immediate for salary deferrals. Employees may contribute, subject to plan provisions, from one



percent to 25 percent of their regular earnings. After one year of completed service, the company begins to make matching contributions. Employer contribution amounts and methodology vary by plan, but generally the contributions are equal to 50 percent of the first 6 percent of eligible base salary contributed by employees and, if certain company goals are met, an additional amount related to incentive compensation payments.

Employer contributions are invested in company stock and had been required to remain so invested until termination of employment or until the employee's attainment of age 55, when they could be transitioned into other investments. Effective January 1, 2005, all employees have the ability to transfer employer contributions into other investments. The employees' contributions are invested in company stock, mutual funds, institutional trusts or guaranteed investment contracts (the same investments in which employees may now direct the employer contributions). The plans of certain non-wholly owned subsidiaries prohibit investments in stock of the company. In this case, the employer matching contributions are invested to mirror the employee-directed contributions. Employer contributions for the Sempra Energy and SoCalGas plans are partially funded by the Employee Stock Ownership Plan referred to below. Company contributions to the savings plans were \$25 million in 2004, \$22 million in 2003 and \$20 million in 2002. The market value of company stock held by the savings plans was \$801 million and \$675 million at December 31, 2004 and 2003, respectively.

Sempra Commodities also operates defined contribution plans outside of the United States. The contributions made by the company to such plans were \$3 million, \$3 million and \$2 million in 2004, 2003 and 2002, respectively.

#### **Employee Stock Ownership Plan**

All contributions to the ESOP Trust (described in Note 6) are made by the company; there are no contributions made by the participants. As the company makes contributions, the ESOP debt service is paid and shares are released in proportion to the total expected debt service. Compensation expense is charged and equity is credited for the market value of the shares released. Dividends on unallocated shares are used to pay debt service and are applied against the liability. The Trust held 2.1 million shares and 2.4 million shares, respectively, of Sempra Energy common stock, with fair values of \$78.7 million and \$71.6 million, at December 31, 2004 and 2003, respectively.

#### **NOTE 10. STOCK-BASED COMPENSATION**

Sempra Energy has stock-based compensation plans intended to align employee and shareholder objectives related to the long-term growth of the company. The plans permit a wide variety of stock-based awards, including nonqualified stock options, incentive stock options, restricted stock, stock appreciation rights, performance awards, stock payments and dividend equivalents.

In 2004, 2003 and 2002, 1,223,000, 1,359,500, and 544,100 shares of restricted company stock, respectively, were awarded to key employees. Compensation expense for the issuance of the restricted stock was \$37 million in 2004, \$16 million in 2003 and \$7 million in 2002. The corresponding weighted average market values per share at the time of grant were \$30.57, \$24.42 and \$24.77, respectively. Subject to earlier forfeitures upon termination of employment, the 2004 and 2003 awards are scheduled to vest at the end of four years if performance-based goals are satisfied, except in the event of a change in control or in certain cases where employment agreements provide alternate methods of vesting. The 2002 award is scheduled to vest at the end of seven years, but is also subject to earlier vesting over a four-year period upon satisfaction of objective performance-based goals. Holders of restricted stock have full voting rights. They also have full dividend rights, except for senior officers, whose dividends are reinvested to purchase additional shares that become subject to the same performance-based vesting conditions as the restricted stock to which they relate.

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In 2004, 2003 and 2002, the company granted to directors, officers and key employees options to acquire 1,389,000, 1,848,000 and 3,444,300 shares of stock, respectively. The option prices were equal to the market price of common stock at the dates of grant. The officers' and key employees' options vest over four-year periods (sooner in the event of a change in control or in certain cases of employment agreements) and expire 10 years from the dates of grant, subject to earlier expiration upon termination of employment. Compensation expense (or reduction thereof) for stock option grants (all associated with outstanding options with dividend equivalents that were issued before 2001 as discussed below) and similar awards was \$4 million, \$6 million and (\$2 million) in 2004, 2003 and 2002, respectively.

The plans permit the granting of dividend equivalents with the stock option grants. For such grants, all of which are now fully vested, recipients receive dividends during the period they hold the options.

As of December 31, 2004, 14,358,630 shares were authorized and available for future grants of restricted stock and/or stock options. In addition, on January 1 of each year, additional shares equal to 1.5 percent of the outstanding shares of Sempra Energy common stock become available for grant.

In 1995, SFAS 123 was issued. It encourages a fair-value-based method of accounting for stock-based compensation. As permitted by SFAS 123, the company adopted only its disclosure requirements and continues to account for stock-based compensation in accordance with the provisions of APBO 25. Discussion of SFAS 123R (a revision of SFAS 123) is provided in Note 1.

#### STOCK OPTION ACTIVITY

	Shares Under Option	Weighted Average Exercise Price	Options Exercisable at December 31
<b>OPTIONS WITH DIVIDEND EQUIVALENTS</b>			
December 31, 2001			
Exercised	3,320,347	\$ 22.38	2,508,328
Cancelled	(172,358)	\$ 19.87	
December 31, 2002			
Exercised	3,079,865	\$ 22.48	2,777,590
Cancelled	(876,391)	\$ 20.81	
Transfer (see table below)	(17,649)	\$ 24.72	
December 31, 2003			
Exercised	649,050	\$ 22.89	649,050
December 31, 2004			
Exercised	286,539	\$ 21.04	
December 31, 2004	362,511	\$ 22.44	362,511

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	Shares Under Option	Weighted Average Exercise Price	Options Exercisable at December 31
<b>OPTIONS WITHOUT DIVIDEND EQUIVALENTS</b>			
December 31, 2001	9,874,454	\$ 21.19	3,143,319
Granted	3,444,300	\$ 24.71	
Exercised	(223,430)	\$ 17.70	
Cancelled	(84,137)	\$ 21.70	
December 31, 2002	13,011,187	\$ 22.18	5,287,437
Granted	1,848,000	\$ 24.44	
Exercised	(1,050,199)	\$ 20.16	
Cancelled	(111,906)	\$ 23.83	
Transfer (see table above)	1,536,775	\$ 23.24	
December 31, 2003	15,233,857	\$ 22.69	8,610,732
Granted	1,389,000	\$ 30.33	
Exercised	(3,837,541)	\$ 20.96	
Cancelled	(73,110)	\$ 25.79	
<b>December 31, 2004</b>	<b>12,712,206</b>	<b>\$ 24.06</b>	<b>7,771,556</b>

Additional information on options outstanding at December 31, 2004, is as follows:

Range of Exercise Prices	Number of Shares	Weighted Average Remaining Life	Weighted Average Exercise Price
<b>Outstanding Options</b>			
\$ 16.87 - \$ 21.00	2,797,522	4.55	\$ 20.08
\$ 22.50 - \$ 25.20	7,663,183	6.80	\$ 23.90
\$ 26.31 - \$ 35.73	2,614,012	6.51	\$ 28.54
	13,074,717	6.26	\$ 24.01
<b>Exercisable Options</b>			
\$ 16.87 - \$ 21.00	2,769,397		\$ 20.09
\$ 22.50 - \$ 25.20	4,120,658		\$ 23.66
\$ 26.31 - \$ 35.73	1,244,012		\$ 26.50
	8,134,067		\$ 22.88

The grant-date fair value of each option grant (including dividend equivalents where applicable) was estimated using a modified Black-Scholes option-pricing model. Weighted average grant-date fair values for options granted in 2004, 2003 and 2002 were \$6.32, \$4.31 and \$4.45, respectively.

The assumptions that were used to determine these grant-date fair values are as follows:

	2004	2003	2002
Stock price volatility	25%	25%	22%
Risk-free rate of return	3.7%	3.4%	4.8%
Annual dividend yield	3.3%	4.1%	4.1%
Expected life	6 Years	6 Years	6 Years

**NOTE 11. FINANCIAL INSTRUMENTS****Fair Value**

The fair values of certain of the company's financial instruments (cash, temporary investments, notes receivable, dividends payable, short-term debt, debt related to Mesquite Power and customer deposits) approximate their carrying amounts. The following table provides the carrying amounts and fair values of the remaining financial instruments at December 31:

(Dollars in millions)	2004		2003	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Investments in limited partnerships	\$ 194	\$ 262	\$ 236	\$ 352
First mortgage bonds	\$ 1,486	\$ 1,521	\$ 1,561	\$ 1,578
Notes payable	1,800	1,876	1,700	1,842
Equity units	600	747	600	680
SDG&E rate-reduction bonds	198	241	263	284
Debt incurred to acquire limited partnerships	76	87	110	128
Long-term debt	434	451	414	436
Total long-term debt	\$ 4,594	\$ 4,923	\$ 4,648	\$ 4,948
Due to unconsolidated affiliates	\$ 362*	\$ 383	\$ 362*	\$ 392
Preferred stock of subsidiaries	\$ 200**	\$ 186	\$ 203**	\$ 184

\* Includes \$200 million of mandatorily redeemable trust preferred securities.

\*\* \$21 million and \$24 million in 2004 and 2003, respectively, of mandatorily redeemable preferred stock of subsidiaries is included in Deferred Credits and Other Liabilities and in Other Current Liabilities on the Consolidated Balance Sheets.

The fair values of investments in limited partnerships were based on the present value of estimated future cash flows, discounted at rates available for similar investments. The fair values of debt incurred to acquire limited partnerships were estimated based on the present value of the future cash flows, discounted at rates available for similar notes with comparable maturities. The fair values of the other long-term debt, preferred stock and mandatorily redeemable trust preferred securities are based on their quoted market prices or quoted market prices for similar securities.

**Accounting for Derivative Instruments and Hedging Activities**

The company follows the guidance of SFAS 133 and related amendments SFAS 138 and 149 (collectively SFAS 133) to account for its derivative instruments and hedging activities. Derivative instruments and related hedges are recognized as either assets or liabilities on the balance sheet, measured at fair value. Changes in the fair value of derivatives are recognized in earnings in the period of change unless the derivative qualifies as an effective hedge that offsets certain exposure.

SFAS 133 provides for hedge accounting treatment when certain criteria are met. For derivative instruments designated as fair value hedges, the gain or loss is recognized in earnings in the period of change (favorable impacts of \$68 million in 2004 and \$16 million in 2003 related to fair value hedges, and unfavorable impacts of \$3 million in 2004 and \$1 million in 2003 related to cash flow hedges) together with the offsetting gain or loss on the hedged item attributable to the risk being hedged; therefore, there is no effect on net income. For derivative instruments designated as cash flow hedges, the effective portion of the derivative gain or loss is included in other comprehensive income, but not reflected in the Statements of Consolidated Income until the corresponding hedged transaction is similarly reflected. The ineffective portion is reported in earnings immediately. The effect on other comprehensive income for the years ended December 31, 2004 and 2003 was \$36 million and

\$3 million, respectively, all related to cash flow hedges. The balance in Accumulated Other Comprehensive Income at December 31, 2004 related to cash flow hedges was \$39 million. In instances where derivatives do not qualify for hedge accounting, gains and losses are recorded in earnings immediately.

The company utilizes derivative instruments to reduce its exposure to unfavorable changes in commodity prices, which are subject to significant and often volatile fluctuation. Derivative instruments include futures, forwards, swaps, options and long-term delivery contracts. These contracts allow the company to predict with greater certainty the effective prices to be received by the company and, in the case of the California Utilities, the prices to be charged to their customers. At the California Utilities, the use of derivative financial instruments is subject to certain limitations imposed by company policy and regulatory requirements. The company classifies its forward contracts as follows:

Contracts that meet the definition of normal purchases and sales, i.e., those that rarely settle by means other than physical delivery of the commodities involved in the transaction, are eligible for the normal purchases and sales exception of SFAS 133, whereby they are accounted for under accrual accounting and recorded in Revenues or Cost of Sales on the Statements of Consolidated Income at the time of delivery. Due to the adoption of SFAS 149, the company has determined that its natural gas contracts entered into after June 30, 2003 generally do not qualify for the normal purchases and sales exception.

Electric and Natural Gas Purchases and Sales: As they relate to the California Utilities, the unrealized gains and losses related to these forward contracts are offset by regulatory assets and liabilities on the Consolidated Balance Sheets to the extent derivative gains and losses will be recoverable or payable in future rates. If gains and losses at the California Utilities are not recoverable or payable through future rates, the California Utilities apply hedge accounting if certain criteria are met. When a contract no longer meets the requirements of SFAS 133, the unrealized gains and losses and the related regulatory asset or liability will be amortized over the remaining contract life.

The following were recorded on the Consolidated Balance Sheets at December 31 related to derivatives:

(Dollars in millions)	2004	2003
Fixed-price Contracts and Other Derivatives:		
Current liabilities	\$ 157	\$ 148
Noncurrent liabilities	500	680
Total liabilities	657	828
Other current assets	8	26
Sundry assets	14	—
Total assets	22	26
Net liabilities	\$ 635	\$ 802

Regulatory assets and liabilities related to derivatives held by the California Utilities at December 31 were:

(Dollars in millions)	2004	2003
Regulatory Assets and Liabilities:		
Current regulatory assets	\$ 152	\$ 144
Other regulatory assets	500	650
Total	652	794
Current regulatory liabilities	4	1
Net regulatory assets	\$ 648	\$ 793

As of December 31, 2004, the difference between net liabilities and net regulatory assets (\$13 million) was due to market value adjustments related to fixed-to-floating interest-rate swaps. As of December 31, 2003, the difference between net liabilities and net regulatory assets (\$9 million) was primarily due to \$30 million related to a derivative contract associated with the purchase of the Cameron LNG facility offset by \$23 million related to a fixed-to-floating interest-rate swap.

Pre-tax income from transactions associated with fixed-price contracts and other derivatives included \$13 million of income in 2004 recorded in Other Income, Net and \$2 million of losses in 2003 recorded in Operating Revenues in the Statements of Consolidated Income.

#### **Market Risk**

The company's policy is to use derivative physical and financial instruments to reduce its exposure to fluctuations in interest rates, foreign currency exchange rates and commodity prices. The company also uses and trades derivative instruments in its trading and marketing of energy and other commodities. Transactions involving these instruments are with major exchanges and other firms believed to be credit-worthy. The use of these instruments exposes the company to market and credit risk, which may at times be concentrated with certain counterparties, although counterparty nonperformance is not anticipated.

#### **Interest-Rate Risk Management**

The company periodically enters into interest-rate swap agreements to moderate its exposure to interest-rate changes and to lower the overall cost of borrowing. This is described in Note 6.

#### **Energy Derivatives**

The company utilizes derivative instruments to reduce its exposure to unfavorable changes in energy prices, which are subject to significant and often volatile fluctuation. Derivative instruments are comprised of futures, forwards, swaps, options and long-term delivery contracts. These contracts allow the company to predict with greater certainty the effective prices to be received.

#### **Energy Contracts**

The California Utilities record transactions for natural gas and electric energy contracts in Cost of Natural Gas and Cost of Electric Fuel and Purchased Power, respectively, in the Statements of Consolidated Income. For open contracts not expected to result in physical delivery, changes in market value of the contracts are recorded in these accounts during the period the contracts are open, with an offsetting entry to a regulatory asset or liability. The majority of the California Utilities' contracts result in physical delivery, which is infrequent at the trading operations.

#### **Sempra Commodities**

Sempra Commodities derives revenue from market making and trading activities, as a principal, in natural gas, electricity, petroleum products, metals and other commodities, for which it quotes bid and asked prices to other market makers and end users. It also earns trading profits as a dealer by structuring and executing transactions that permit its counterparties to manage their risk profiles. Sempra Commodities utilizes derivative instruments to reduce its exposure to unfavorable changes in market prices, which are subject to significant and often volatile fluctuation. These instruments include futures, forwards, swaps and options, and represent contracts with counterparties under which payments are linked to or derived from energy market indices or on terms predetermined by the contract, which may or may not be financially settled by Sempra Commodities. Sempra Energy guarantees many of Sempra Commodities' transactions.

Sempra Commodities also derives a portion of its revenue from delivering electric and natural gas supplies to its commercial and industrial customers. Such contracts are hedged to preserve margin and reduce market risk. The derivative instruments used to hedge the transactions include swaps, forwards, futures, options or combinations thereof.

Trading instruments for all activities are recorded by Sempra Commodities on a trade-date basis and the majority of such derivative instruments are adjusted daily to current market value with gains and losses recognized in Other Operating Revenues on the Statements of Consolidated Income. These instruments are included on the Consolidated Balance Sheets as trading assets or trading liabilities and include amounts due from commodity clearing organizations, amounts due to or from trading counterparties, unrealized gains and losses from exchange-traded futures and options, derivative OTC swaps, forwards and options. Unrealized gains and losses on OTC transactions reflect amounts that would be received from or paid to a third party upon settlement of the contracts. Unrealized gains and losses on OTC transactions are reported separately as assets and liabilities unless a legal right of setoff exists under an enforceable netting arrangement. Other derivatives which qualify as hedges are accordingly recorded under hedge accounting.

As a result of the rescission of EITF 98-10 (discussed in Note 1) energy commodity inventory is being recorded at the lower of cost or market; however metals inventories continue to be recorded at fair value in accordance with ARB 43. Note 2 discusses Sempra Commodities' acquisitions made in 2002, some of which were affected by EITF 98-10.

Futures and exchange-traded option transactions are recorded as contractual commitments on a trade-date basis and are carried at fair value based on closing exchange quotations. Commodity swaps and forward transactions are accounted for as contractual commitments on a trade-date basis and are carried at fair value derived from dealer quotations and underlying commodity exchange quotations. OTC options purchased and written are recorded on a trade-date basis. OTC options are carried at fair value based on the use of valuation models that utilize, among other things, current interest, commodity and volatility rates, as applicable.

The carrying values of trading assets and trading liabilities, primarily at Sempra Commodities, approximate the following:

(Dollars in millions)	December 31,	
	2004	2003
<b>TRADING ASSETS</b>		
Trading-related receivables and deposits, net:		
Due from trading counterparties	\$ 2,371	\$ 2,215
Due from commodity clearing organizations and clearing brokers	235	135
	<u>2,606</u>	<u>2,350</u>
Derivative trading instruments:		
Unrealized gains on swaps and forwards	1,607	1,148
OTC commodity options purchased	732	459
	<u>2,339</u>	<u>1,607</u>
Commodities owned	1,547	1,420
<b>Total trading assets</b>	<b>\$ 6,492</b>	<b>\$ 5,377</b>
<b>TRADING LIABILITIES</b>		
Trading-related payables		
	<u>\$ 3,182</u>	<u>\$ 2,255</u>
Derivative trading instruments sold, not yet purchased:		
Unrealized losses on swaps and forwards	1,232	1,114
OTC commodity options written	252	226
	<u>1,484</u>	<u>1,340</u>
Commodities sold with agreement to repurchase	513	922
<b>Total trading liabilities</b>	<b>\$ 5,179</b>	<b>\$ 4,517</b>

Based on quarterly measurements, the average fair values during 2004 for trading assets and liabilities approximate \$5.7 billion and \$4.6 billion, respectively. For 2003, the amounts were \$5.1 billion and \$4.4 billion, respectively.

At Sempra Commodities, market risk from market making and trading activities arises from the potential for changes in the value of physical and financial instruments resulting from fluctuations in prices and basis for natural gas, electricity, petroleum, petroleum products, metals and other commodities. Market risk is also affected by changes in volatility and liquidity in markets in which these instruments are traded. Market risk for electric and natural gas delivery contract activity from fluctuations in natural gas or electricity prices is reduced by Sempra Commodities' hedging strategy as described above.

Sempra Commodities' credit risk from physical and financial instruments as of December 31, 2004 is represented by their positive fair value after consideration of collateral. Options written do not expose Sempra Commodities to credit risk. Exchange traded futures and options are not deemed to have significant credit exposure since the exchanges guarantee that every contract will be properly settled on a daily basis. Credit risk is also associated with its retail customers.

The following table summarizes the counterparty credit quality and exposure for Sempra Commodities at December 31, 2004 and 2003, expressed in terms of net replacement value. These exposures are net of collateral in the form of customer margin and/or letters of credit of \$1.1 billion and \$569 million at December 31, 2004 and 2003, respectively.

(Dollars in millions)	December 31,	
	2004	2003
<b>Counterparty credit quality*</b>		
Commodity exchanges	\$ 235	\$ 135
AAA	7	5
AA	259	316
A	562	484
BBB	680	371
Below investment grade and not rated	532	417
Total	\$ 2,275	\$ 1,728

\* As determined by rating agencies or internal models intended to approximate rating-agency determinations.



**NOTE 12. PREFERRED STOCK OF SUBSIDIARIES**

(in millions)	Call/ Redemption Price	December 31,	
		2004	2003
<b>Not subject to mandatory redemption:</b>			
Pacific Enterprises:			
Without par value, authorized 15,000,000 shares:			
\$4.75 Dividend, 200,000 shares outstanding	\$ 100.00	\$ 20	\$ 20
\$4.50 Dividend, 300,000 shares outstanding	\$ 100.00	30	30
\$4.40 Dividend, 100,000 shares outstanding	\$ 101.50	10	10
\$4.36 Dividend, 200,000 shares outstanding	\$ 101.00	20	20
\$4.75 Dividend, 253 shares outstanding	\$ 101.00	—	—
Total		80	80
SoCalGas:			
\$25 par value, authorized 1,000,000 shares:			
6% Series, 28,041 shares outstanding		1	1
6% Series A, 783,032 shares outstanding		19	19
Without par value, authorized 10,000,000 shares		—	—
Total		20	20
SDG&E:			
\$20 par value, authorized 1,375,000 shares:			
5% Series, 375,000 shares outstanding	\$ 24.00	8	8
4.5% Series, 300,000 shares outstanding	\$ 21.20	6	6
4.4% Series, 325,000 shares outstanding	\$ 21.00	7	7
4.6% Series, 373,770 shares outstanding	\$ 20.25	7	7
Without par value:			
\$1.70 Series, 1,400,000 shares outstanding	\$ 25.85	35	35
\$1.82 Series, 640,000 shares outstanding	\$ 26.00	16	16
Total		79	79
Total not subject to mandatory redemption		179	179
<b>Subject to mandatory redemption:</b>			
SDG&E:			
Without par value: \$1.7625 Series, 850,000 and 950,000 shares outstanding at December 31, 2004 and December 31, 2003, respectively	\$ 25.00	21*	24*
Total preferred stock		\$200	\$203

\* At December 31, 2004 and 2003, \$19 million and \$21 million, respectively, were included in Deferred Credits and Other Liabilities and \$2 million and \$3 million, respectively, were included in Other Current Liabilities on the Consolidated Balance Sheets.

PE preferred stock is callable at the applicable redemption price of each series, plus any unpaid dividends. The preferred stock is subject to redemption at PE's option at any time upon not less than 30 days' notice, at the applicable redemption price for each series, plus any unpaid dividends. All series have one vote per share and cumulative preferences as to dividends, and have a liquidation value of \$100 per share plus any unpaid dividends.

None of SoCalGas' preferred stock is callable. All series have one vote per share and cumulative preferences as to dividends, and have a liquidation value of \$25 per share plus any unpaid dividends.

All series of SDG&E's preferred stock have cumulative preferences as to dividends. The \$20 par value preferred stock has two votes per share on matters being voted upon by shareholders of SDG&E and a liquidation value at par, whereas the no-par-value preferred stock is nonvoting and has a liquidation value of \$25 per share plus any unpaid dividends. SDG&E is authorized to issue 10,000,000 shares of no-par-value preferred stock (both subject to and not subject to mandatory redemption). All series are callable at December 31, 2004. The \$1.7625 Series has a sinking fund requirement to redeem 50,000 shares at \$25 per share per year from 2005 to 2007; all remaining shares must be redeemed in 2008. On January 15, 2005, SDG&E redeemed 100,000 shares.

**NOTE 13. SHAREHOLDERS' EQUITY AND EARNINGS PER SHARE (EPS)**

The following table provides the per share computations for income from continuing operations for the year ended December 31, 2004:

	Income (millions) (numerator)	Shares (thousands) (denominator)	Per Share Amounts
Basic EPS—income from continuing operations	\$ 920	228,271	\$ 4.03
Effect of dilutive securities:			
Stock options and restricted stock awards		3,595	(0.06)
Equity Units		1,986	(0.04)
Diluted EPS—income from continuing operations	\$ 920	233,852	\$ 3.93

The only difference between basic and diluted earnings per share in 2003 and 2002 was the effect of common stock options. For 2003 and 2002, the effect of dilutive options was equivalent to an additional 2,742,000 and 1,059,000 shares, respectively. The dilution from common stock options is based on the treasury stock method, whereby the proceeds from the exercise price are assumed to be used to repurchase shares on the open market at the average market price for the year. The calculation excludes options covering an average of 0.1 million and 6.0 million shares for 2003 and 2002, respectively, for which the exercise price was greater than the average market price for common stock during the respective year. In 2004, there were no such options. The company's equity units, described below, had no dilutive effect in 2003 or 2002.

The dilution from invested restricted stock awards is based on the treasury stock method, whereby assumed proceeds equivalent to the unearned compensation related to the awards are assumed to be used to repurchase shares on the open market at the average market price for the year. In 2003 and 2002, there were restricted awards representing an average of 1.3 million and 0.7 million shares, respectively, that did not affect the calculation since their grant price was greater than the average market price for common stock during the respective year. In 2004 there were no such awards.

The company is authorized to issue 750,000,000 shares of no-par-value common stock and 50,000,000 shares of preferred stock.

Excluding shares held by the ESOP, common stock activity consisted of the following:

	2004	2003	2002
Common shares outstanding, January 1	226,598,619	204,911,572	204,475,362
Public issuance	—	16,500,000	—
Savings plan issuance*	1,638,581	1,436,526	—
Shares released from ESOP	236,620	170,613	130,486
Stock options exercised	4,124,080	1,926,590	395,788
Restricted stock	1,223,000	1,359,500	544,100
Common stock investment plan**	611,259	728,241	212,411
Shares repurchased	(181,819)	(262,286)	(818,639)
Shares forfeited and other	(74,360)	(172,137)	(27,936)
Common shares outstanding, December 31	234,175,980	226,598,619	204,911,572

\* Prior to 2003, the plan purchased shares in the open market to cover the company's contributions to the savings plan.

\*\* Participants in the Direct Stock Purchase Plan may reinvest dividends to purchase newly issued shares.

The payment of future dividends and the amount thereof are within the discretion of the company's board of directors. The CPUC's regulation of the California Utilities' capital structure limits the amounts that are available for dividends and loans to the company from the California Utilities. At December 31, 2004, SDG&E and SoCalGas could have provided a total of \$160 million and \$200 million, respectively, to Sempra Energy, through dividends and loans.

#### Equity Units

In 2002, the company issued \$600 million of equity units. Each unit consists of \$25 principal amount of the company's 5.60% senior notes due May 17, 2007 and a contract to purchase for \$25 on May 17, 2005, between .8190 and .9992 of a share of the company's common stock (with the precise number to be determined by the then-average market price). The number of shares to be issued ranges from 20 million to 24 million. The equity units are included in Long-Term Debt on the Consolidated Balance Sheets. Through December 31, 2004, \$55 million had been charged to the common stock account in connection with the transaction. In February 2005, the company remarketed the senior notes for their remaining term at a rate of 4.62%.

#### Common Stock Offering

On October 14, 2003, Sempra Energy completed a common stock offering of 16.5 million shares priced at \$28 per common share, resulting in net proceeds of \$448 million. The proceeds were used primarily to pay off short-term debt.

#### NOTE 14. ELECTRIC INDUSTRY REGULATION

##### Background

The restructuring of California's electric utility industry has significantly affected the company's electric utility operations, and the power crisis of 2000-2001 caused the CPUC to significantly modify its plan for restructuring the electricity industry. Supply/demand imbalances and a number of other factors resulted in abnormally high electric-commodity prices beginning in mid-2000 and continuing into 2001. These higher prices were initially passed through to customers and resulted in bills that in most cases were double or triple those from 1999 and early 2000. This resulted in several legislative and regulatory responses, including California Assembly Bill (AB) 265. AB 265 imposed a ceiling on the cost of the electric commodity that SDG&E could pass on to its small-usage customers from June 1, 2000 to December 31, 2002.

SDG&E accumulated the amount that it paid for electricity in excess of the ceiling rate in an interest-bearing balancing account (the AB 265 undercollection, which is included in Regulatory Balancing Accounts, Net on the Consolidated Balance Sheets) and began recovering these amounts in rates charged to customers following the end of the rate-ceiling period. The remaining AB 265 undercollection was fully collected in 2004.

Another legislative response to the power crisis resulted in the purchase by the DWR of a substantial portion of the power requirements of California's electricity users. In 2001, the DWR entered into long-term contracts with suppliers, including Sempra Generation, to provide power for the utility procurement customers of each of the California investor-owned utilities (IOUs). The CPUC has established the allocation of the power and its administrative responsibility, including collection of power contract costs from utility customers, among the IOUs. Beginning on January 1, 2003, the IOUs resumed responsibility for electric commodity procurement above their allocated share of the DWR's long-term contracts.

#### **Department of Water Resources**

The DWR's operating agreement with SDG&E, approved by the CPUC, provides that SDG&E is acting as a limited agent on behalf of the DWR in undertaking energy sales and natural gas procurement functions under the DWR contracts allocated to SDG&E's customers. Legal and financial responsibility associated with these activities continues to reside with the DWR. Therefore, the revenues and costs associated with the contracts are not included in the Statements of Consolidated Income.

In October 2003, the CPUC initiated a proceeding to consider a permanent methodology for allocating the DWR's revenue requirement beginning in 2004 through the remaining life of the DWR contracts. On December 2, 2004, the CPUC issued a decision that would shift \$790 million of the costs to SDG&E's customers over the period between implementation of the decision and 2013. On December 20, 2004, SDG&E filed an application for rehearing of the decision, arguing that the CPUC reached its decision without the proper evidentiary review of the method of calculating above-market costs. On January 13, 2005, the CPUC acted to grant rehearing on that limited issue.

Such a shift would not affect SDG&E's net income, but would adversely affect its customers' commodity costs. In the near term, the effect on SDG&E's cash flows would be minor, but could become significant in the later years unless rate ceilings imposed by Assembly Bill 1X, which freeze total rates for most residential customers at the February 2001 level, are increased to provide more-contemporaneous recovery. Until January 1, 2016, CPUC Decision 04-12-048 provides SDG&E with a true-up triggering mechanism when an overcollection or undercollection in SDG&E's power procurement balancing account exceeds approximately five percent of the prior year's recorded electric commodity revenue.

#### **Power Procurement and Resource Planning**

In 2001, the CPUC directed the IOUs to resume electric commodity procurement to cover their net short energy requirements by January 1, 2003 and also implemented legislation regarding procurement and renewables portfolio standards. In addition, the CPUC established a process for review and approval of the utilities' long-term resource and procurement plans, which is intended to identify forecasted needs for generation and transmission resources within a utility's service territory to support transmission grid reliability and to serve customers. An updated 10-year resource plan was approved by the CPUC in December 2004, in a proceeding to consider utility resource planning, including energy efficiency, contracted power, demand response, qualifying facilities, renewable generation and distributed generation. SDG&E's updated long-term resource plan incorporates the resources approved by the CPUC that are discussed below, and recognizes updated CPUC goals to

reach a 20-percent renewable resources target by 2010. The updated plan recommends a 500-kV transmission line addition in 2010, which would be processed for approval in a subsequent CPUC proceeding. The CPUC also endorsed SDG&E's continued analysis and planning for a 500-kV transmission line, adopted SDG&E's proposal for cost recovery related to utility-owned generation, recognized the debt-equivalent impact associated with long-term power purchase contracts, adopted a greenhouse gas adder for assessing new resource acquisitions, and established a cap on initial costs for new utility-owned generation resources to level the playing field with respect to power purchase options. The estimated capital cost related to this updated plan is \$700 million, to be spent by 2007, for capital projects approved by the CPUC in June 2004, as described below.

On June 9, 2004, the CPUC approved SDG&E's entering into five new electric resource contracts (including two under which SDG&E would take ownership, on a turnkey basis, of new generating assets, including the 550-MW combined-cycle Palomar plant being developed by Sempra Generation for completion in 2006). An additional, demand-response contract was also approved. The decision authorized SDG&E to recover the costs of both contracted resources and turnkey resources, but did not adopt SDG&E's specific cost recovery, ratemaking and revenue requirement proposals for the proposed turnkey resources. On July 15, 2004, three parties filed requests for rehearing of the decision. SDG&E filed its response on July 30, 2004, opposing the requests. The CPUC is expected to rule on the requests by mid-2005. In September 2004, SDG&E filed its revenue requirement and ratemaking proposals for the 45-MW combustion turbine which SDG&E will acquire as a turnkey project and filed its revenue requirement and ratemaking proposals for the Palomar plant on November 1, 2004. On January 27, 2005, the CPUC approved the revenue requirement and ratemaking proposals for the 45-MW combustion turbine. The June 9, 2004, decision did not approve SDG&E's proposals for a return on equity (ROE) for SDG&E's new generation investments higher than SDG&E's ROE on distribution assets, an equity offset for the debt-equivalent of purchase power contracts or an equity buildup for construction. These matters may be re-introduced for consideration in future CPUC proceedings.

#### **SONGS**

Southern California Edison's (Edison) CPUC decision on its 2003 General Rate Case application sets rates for SONGS, 20 percent of which is owned by SDG&E. Through December 31, 2003, the operating and capital costs of SONGS Units 2 and 3 were recovered through the ICIP mechanism which allowed SDG&E to receive 4.4 cents per kilowatt-hour for SONGS generation. For the year ended December 31, 2003, ICIP contributed \$53 million to SDG&E's net income. SDG&E's SONGS ratebase restarted at \$0 on January 1, 2004 and, therefore, SDG&E's earnings from SONGS are now generally limited to a return on new capital additions.

Edison has applied for CPUC approval to replace SONGS' steam generators, which would require an estimated capital expenditure of \$782 million. Hearings before the CPUC on Edison's application were completed on February 11, 2005 and a final decision addressing the cost effectiveness of the steam generator project is expected during the second half of 2005. SDG&E had elected not to participate in the project. SDG&E nonparticipation would result in a reduction in its share ownership in the project and a proportionate reduction in its share of SONGS' output. On February 18, 2005, an arbitrator issued a decision that, based upon Edison's cost calculations, would result in SDG&E's interest in SONGS being reduced to zero if SDG&E continues to decline to participate in the project. The arbitration decision is subject to CPUC review and approval, with a CPUC decision expected in the second half of 2006. The CPUC could require SDG&E to participate in the project or, if the reductions of SDG&E's ownership percentage resulting from the CPUC final decision were to be unacceptable, SDG&E may elect to participate.

During the most recent SONGS Unit 3 refueling outage which ended on December 28, 2004, Edison reported that it had performed inspections of two pressurizer sleeves and found evidence of

degradation. Degradation of the pressurizer sleeves has been a concern in the nuclear industry for some time. Edison had been planning to replace all of the sleeves in Units 2 and 3 during the next refueling for each unit in 2005 and 2006, but decided to move the planned replacement of Unit 3's pressurizer sleeves forward from 2006 to 2004. This extra work lengthened the 2004 outage, but allowed Edison to move the 2006 refueling outage out of the peak summer period to the fall or winter of 2006. Edison reported that it will incur about \$9 million of capital expenditures during 2005 that otherwise would have occurred in 2006. SDG&E's share would be approximately \$2 million. Edison plans to replace the pressurizer sleeves in Unit 2 during its next scheduled outage in 2005.

Also during the 2004 outage, Edison reported that it had conducted a planned inspection of the Unit 3 reactor vessel head and found indications of degradation. Although the degradation is far below the level at which leakage would occur, Edison made the repairs during the 2004 outage. While Edison reports that this is the first experience at SONGS of this kind of degradation to the reactor vessel heads, the detection and repair of similar degradation at other plants are now common in the industry. Edison reports that it plans to replace the Unit 2 and Unit 3 reactor vessel heads during refueling outages in 2009-2010.

#### **Spent Nuclear Fuel**

SONGS owners have responsibility for the interim storage of spent nuclear fuel generated at SONGS until it is accepted by the DOE for final disposal. Spent nuclear fuel has been stored in the SONGS Units 1, 2 and 3 spent fuel pools and the ISFSI. Movement of all spent fuel to the ISFSI was completed as of December 31, 2004, except for the movement of Unit 1 spent fuel stored at the Unit 2 spent fuel pool, which is expected to be completed by the end of 2005. With these moves, there will be sufficient space for the Units 2 and 3 spent fuel pools to meet requirements through mid-2007 and mid-2008, respectively.

#### **NOTE 15. OTHER REGULATORY MATTERS**

##### **Natural Gas Industry Restructuring (GIR)**

In December 2001, the CPUC issued a decision related to GIR, with implementation anticipated during 2002. On April 1, 2004, after many delays and changes, the CPUC issued a decision that adopts tariffs to implement the 2001 decision. However, by that same decision, the CPUC stayed implementation of the GIR tariffs until it issues a decision in Phase I of the Natural Gas Market Order Instituting Ratemaking (OIR) discussed below. At that time, the CPUC will reconcile the GIR market structure with whatever structure results from the Phase I decision of the Natural Gas Market OIR. If implemented, the stayed decision would unbundle the costs of SoCalGas' backbone transmission system from rates and result in revising noncore balancing account treatment to exclude the balancing of SoCalGas' backbone transmission costs and place SoCalGas at risk for recovery of \$80 million for transmission and \$81 million for storage (current dollars). The decision would create firm tradable rights for the transmission system. Other noncore costs/revenues would continue to be fully balanced until the decision in the next Biennial Cost Allocation Proceeding (BCAP) discussed below.

##### **Natural Gas Market OIR**

The CPUC's Natural Gas Market OIR was instituted in January 2004, and will be addressed in two phases. A decision on Phase I was issued in September 2004 and Phase II is awaiting CPUC direction on further proceedings. In Phase I, the CPUC's objective was to develop a process enabling the CPUC to review and pre-approve new interstate capacity contracts before they are executed. In addition, the California Utilities must submit proposals on any LNG project to which interconnection is planned, providing costs and terms, including access to the pipelines in Mexico. Phase II will primarily address emergency reserves and ratemaking policies. The CPUC's objective in the ratemaking policy

component of Phase II is to identify and propose changes to policies that create incentives that are consistent with the goal of providing adequate and reliable long-term supplies and that do not conflict with energy efficiency programs. The focus of the Gas OIR is the period from 2006 to 2016. Since GIR, discussed above, would end in August 2006 and there is overlap between GIR and the OIR issues, a number of parties (including SoCalGas) have requested the CPUC not to implement GIR.

The California Utilities have made comprehensive filings in the OIR outlining a proposed market structure that is intended to create access to new natural gas supply sources (such as LNG) for California. In their Phase I and Phase II filings, SoCalGas and SDG&E proposed a framework to provide firm tradable access rights for intrastate natural gas transportation; provide SoCalGas with continued balancing account protection for intrastate transmission and distribution revenues, thereby eliminating throughput risk; and integrate the transmission systems of SoCalGas and SDG&E so as to have common rates and rules. The California Utilities also proposed that the capital expenditures necessary to access new sources of supply be included in ratebase and that the total amount of the expenditures would be \$200 million to \$300 million.

The California Utilities also proposed a methodology and framework to be used by the CPUC for granting pre-approval of new interstate transportation agreements. The Phase I decision approved the California Utilities' transportation capacity pre-approval procedures with some modifications. SoCalGas' existing pipeline capacity contracts with Transwestern Pipeline Company expire in November 2005 and its primary contracts with El Paso Natural Gas Company (El Paso) expire in August 2006. SoCalGas recently was granted pre-approval by the CPUC of a contract for released capacity on the Kern River Gas Transmission Company system, and four capacity contracts with El Paso. The contracts would expire between 2007 and 2011. In January 2005, SDG&E was granted pre-approval of a capacity contract with El Paso that would expire in 2007. In February 2005, SoCalGas filed for pre-approval of two new capacity contracts with Transwestern that would expire in 2009 and 2011. The CPUC's decision on pre-approval of the Transwestern contracts is expected to be received by March 2005. All interstate transportation capacity under the pre-approved contracts will be used to transport natural gas supplies on behalf of the California Utilities' core residential and small commercial customers, and all costs of the capacity will be recovered in the customers' rates through each utility's Purchased Gas Account, a balancing account. In December 2004, pursuant to the Phase I decision, SoCalGas filed an application to implement proposals for transmission system integration, firm access rights, and off-system delivery services. The CPUC has determined that the ratemaking treatment and cost responsibility for any access-related infrastructure will be addressed in future applications to be filed when more is known about the particular projects. Phase II of the Gas Market OIR will review the CPUC's ratemaking policies on throughput risk to better align these with its objectives of promoting energy conservation and adequate infrastructure. Phase II will also investigate the need for emergency natural gas storage reserves and the role of the utility in backstopping the noncore market.

#### **Cost of Service**

On December 2, 2004, the CPUC issued a decision in the California Utilities' cost of service proceedings that essentially approved settlements recommended by most major parties to the proceedings. The decision reduces the California Utilities' annual rate revenues, effective retroactively to January 1, 2004, by an aggregate net amount of approximately \$56 million from the rates in effect during 2003. The reduced rates will remain in effect through 2007, subject to annual attrition allowances. Of the reduction, \$10 million relates to what SDG&E believes to be a computational error concerning its nuclear electric rate revenues. With respect to the \$10 million reduction, a Petition for Modification and an Application for Rehearing were filed in December 2004 and January 2005, respectively.

Attrition allowances, performance-based incentive mechanisms (PBR), which are described in the following section, and related matters are being addressed by the CPUC in Phase II of the cost of

service proceedings, expected to be decided in the first quarter of 2005. In addition to recommending changes in the PBR formulas, the CPUC's Office of Ratepayer Advocates (ORA) also proposed the possibility of performance penalties for service quality, safety and electric service reliability, without the possibility of performance awards. Hearings took place in June 2004. In July 2004, all of the active parties in Phase II who dealt with post-test-year ratemaking and performance incentives filed for adoption by the CPUC of an all-party settlement agreement for most of the Phase II issues, including annual inflation adjustments and earnings sharing. The proposed settlement does not cover performance incentives. For the interim years of 2005-2007, the Consumer Price Index would be used to adjust the escalatable authorized base rate revenues within identified floors and ceilings, each of which limits the adjustment to approximately two to five percent of the prior year's authorized base rate revenues.

The California Utilities had filed for continuation of existing PBR mechanisms for service quality and safety that would otherwise expire at the end of 2003. In January 2004, the CPUC issued a decision that extended 2003 service and safety targets through 2004, but did not determine the extent of rewards or penalties. As part of the proposed Phase II Settlement Agreement, earnings sharing, under which IOUs return to customers a percentage of earnings above specified levels, would be suspended for 2004 and resume for 2005 through 2007. The proposed earnings sharing mechanism also provides either utility the option to file for suspension of the earnings sharing mechanism if earnings fall 175 basis points or more below its authorized rate of return; however, if earnings are more than 300 basis points above the utility's authorized rate of return, the earnings sharing mechanism would be automatically suspended and trigger a formal regulatory review by the CPUC to determine whether modification of the ratemaking mechanism is required.

On February 15, 2005, the Administrative Law Judge (ALJ) and the CPUC Commissioner assigned to Phase II of the cost of service proceedings issued differing proposed decisions for consideration by the CPUC. If adopted by the CPUC, the ALJ's decision would not approve the parties' settlement of the Phase II issues, but would authorize the California Utilities to adjust their authorized revenues in each of years 2005 through 2007 on a formula basis similar to that proposed by the California Utilities and also establish performance measures with reward and penalty potentials of approximately \$20 million. In addition, the ALJ's decision would have the utilities' cost of capital reviewed on an annual basis. If adopted by the CPUC, the Commissioner's proposed decision would approve the parties' settlement and also approve performance measures for customer service, safety and reliability with the same reward and penalty provisions as the ALJ's proposed decision. The Commissioner's proposed decision also would continue the use of the cost of capital adjustment mechanism currently in place, which adjusts each utility's rate of return automatically based on market indices. The CPUC may adopt either proposed decision, as proposed or with modifications, or reject both and adopt a different result.

The California Utilities had been equally sharing between ratepayers and shareholders the estimated savings for the 1998 business combination that created Sempra Energy. Pursuant to an October 2001 CPUC decision, that sharing has ceased and all merger savings go to ratepayers beginning with 2003.

#### **Performance-Based Regulation**

PBR consists of three primary components. The first is a mechanism to adjust rates in years between general rate cases or cost of service cases. It annually adjusts base rates from those of the prior year to provide for inflation, changes in the number of customers and efficiencies.

The second component is a mechanism whereby any earnings in excess of those authorized plus a narrow band above that are shared with customers in varying degrees depending upon the amount of the additional earnings.

The third component consists of a series of measures of utility performance. Generally, if performance is outside of a band around the specified benchmark, the utility is rewarded or penalized certain dollar amounts.



The three areas that have been eligible for PBR rewards or penalties are operational incentives based on measurements of safety, reliability and customer satisfaction; demand-side management (DSM) rewards based on the effectiveness of the programs; and natural gas procurement rewards or penalties. The CPUC is also considering a new reward/penalty related to electricity procurement, now that the utilities have resumed this activity. However, as noted under "Cost of Service," Phase II of the California Utilities' current cost of service proceeding is not complete. As a result, these safety, reliability and customer satisfaction incentive mechanisms (i.e., those that are reviewed in the Cost of Service proceeding) were not in effect during 2004. However, it is not expected that the effect would be other than a one-year moratorium of the mechanisms.

PBR, DSM and Gas Cost Incentive Mechanism (GCIM) rewards are not included in the company's earnings before CPUC approval is received. The only incentive rewards approved during 2004 consisted of \$6.3 million related to SoCalGas' Year 9 GCIM, which was approved in February 2004, and \$1.5 million related to SDG&E's Year 10 natural gas PBR, which was approved in August 2004. These rewards were awarded by the CPUC subject to refund based on the outcome of the Border Price Investigation discussed below. The cumulative amount of rewards subject to refund based on the outcome of the Border Price Investigation is \$65.3 million, substantially all of which has been included in net income in 2004 or previously.

On December 30, 2004, a joint settlement agreement between the California Utilities and the ORA (collectively, the joint parties) was filed with the CPUC for approval. The settlement agreement resolves all outstanding shareholder earnings claims filed with the CPUC commencing in 2000 and those claims that would have been filed through 2007 and 2009, respectively, for SDG&E and SoCalGas, associated with DSM, energy efficiency and low-income energy efficiency programs. The proposed settlement is for \$73 million and \$14 million, respectively, for SDG&E and SoCalGas (including interest, franchise fees, uncollectible amounts and awards earned in prior years that had not yet then been requested). The joint parties requested expeditious approval of the settlement agreement, without modification. A CPUC decision is expected by the end of the second quarter of 2005.

At December 31, 2004, other performance incentives were pending CPUC approval and, therefore, were not included in the company's earnings (dollars in millions):

Program	SoCalGas	SDG&E	Total
2003 Distribution PBR	\$ —	\$ 8.2	\$ 8.2
GCIM/natural gas PBR	2.4	.2	2.6
2003 safety	.5	—	.5
Total	\$ 2.9	\$ 8.4	\$ 11.3

#### Cost of Capital

Effective January 1, 2005, SDG&E's authorized return on ratebase (ROR) and ROE became 8.18 percent and 10.37 percent, respectively, for its electric distribution and natural gas businesses, down from 8.77 percent and 10.9 percent, respectively. The decrease is a result of the CPUC's automatic triggering mechanism, which resets these rates whenever Moody's Aa utility bond yield as published by Mergent Bond Record changes by more than a specified amount. The current benchmark is 6.19 percent and an automatic adjustment would be triggered if the Mergent Aa utility bond yield were to average less than 5.19 percent or greater than 7.19 percent during the April — September timeframe of any year. The effect of the 2004 changes in ROR and ROE will be to decrease net income in 2005 by \$10 million from what it would have been if the 2005 rates had not changed from the 2004 rates. In December 2004, the CPUC ordered SDG&E to file a cost of capital application in 2005 to take effect

January 1, 2006. SDG&E had recommended that the CPUC approve a policy allowing utilities to increase the equity in their authorized capital structure to adjust for the debt equivalent effect of purchased power agreements. The CPUC has directed that such adjustment only be considered in the context of a full review of the cost of capital. The electric-transmission cost of capital is determined under a FERC proceeding and is currently at an 11.25% ROE.

Effective January 1, 2003, SoCalGas' authorized ROE is 10.82 percent and its ROR is 8.68 percent. These rates are subject to automatic adjustment if the 12-month trailing average of 30-year Treasury bond rates and the Global Insight forecast of the 30-year Treasury bond rate 12 months ahead vary by greater than 150 basis points from a benchmark, which is currently 5.38 percent. The 12-month trailing average was 5.03 percent and the Global Insight forecast was 5.44 percent at December 31, 2004.

Potential changes to this process are described above in "Cost of Service."

#### **Biennial Cost Allocation Proceeding**

The BCAP determines the allocation of authorized costs between customer classes for natural gas transportation service provided by the California Utilities and adjusts rates to reflect variances in sales volumes as compared to the forecasts previously used in establishing transportation rates. The California Utilities filed with the CPUC their 2005 BCAP applications in September 2003, requesting updated transportation rates effective January 1, 2005. In November 2003, an Assigned Commissioner Ruling stayed the BCAP applications until a decision is issued in the GIR implementation proceeding. As a result of the April 1, 2004 decision on GIR implementation as described in Natural Gas Industry Restructuring above, in May 2004 the ALJ in the 2005 BCAP issued a decision dismissing the BCAP applications. The California Utilities are required to file new BCAP applications after the stay in the GIR implementation proceeding is lifted. As a result of the deferrals and the significant decline forecasted in noncore gas throughput on SoCalGas' system, in December 2002 the CPUC issued a decision approving balancing account protection for SoCalGas' risk on local transmission and distribution revenues from January 1, 2003 until the CPUC issues its next BCAP decision. SoCalGas is seeking to continue this balancing account protection in the Natural Gas OIR proceeding.

#### **CPUC Investigation of Energy-Utility Holding Companies**

The CPUC has initiated an investigation into the relationship between California's IOUs and their parent holding companies. The CPUC broadly determined that it could, in appropriate circumstances, require the holding company to provide cash to a utility subsidiary to cover its operating expenses and working capital to the extent they are not adequately funded through retail rates. This would be in addition to the requirement of holding companies to provide for their utility subsidiaries' capital requirements, as the IOUs previously acknowledged in connection with their holding companies' formations. In January 2002, the CPUC ruled that it had jurisdiction to create the holding company system and, therefore, retains jurisdiction to enforce conditions to which the holding companies had agreed.

In a May 2004 opinion, the California Court of Appeal upheld the CPUC's assertion of limited enforcement jurisdiction, but concluded that the CPUC's interpretation of the "first priority" condition (that the holding companies could be required to infuse cash into the utilities as necessary to meet the utilities' obligation to serve) was not ripe for review. In September 2004, the California Supreme Court declined to review the California Court of Appeal's decision.

#### **CPUC Investigation of Compliance With Affiliate Rules**

In February 2003, the CPUC opened an investigation of the business activities of SDG&E, SoCalGas and Sempra Energy to determine if they have complied with statutes and CPUC decisions in the management, oversight and operations of their companies. In September 2003, the CPUC suspended

the procedural schedule until it completes an independent audit to evaluate energy-related holding company systems and affiliate activities undertaken by Sempra Energy within the service territories of SDG&E and SoCalGas. The audit, covering years 1997 through 2003, is expected to be completed by the third quarter of 2005. The scope of the audit will be broader than the annual affiliate audit. In accordance with existing CPUC requirements, the California Utilities' transactions with other Sempra Energy affiliates have been audited by an independent auditing firm each year, with results reported to the CPUC, and there have been no material adverse findings in those audits.

#### **Recovery of Certain Disallowed Transmission Costs**

In August 2002, the FERC issued Opinion No. 458, which effectively disallowed SDG&E's recovery in its transmission rates of the differentials between certain payments to SDG&E by its co-owners of the Southwest Powerlink (SWPL) under the SWPL Participation Agreements, and charges assessed to SDG&E under the California Independent System Operator (ISO) FERC tariff related to energy schedules of its SWPL co-owners. As a result, SDG&E is incurring unreimbursed costs of \$4 million to \$8 million per year. SDG&E has appealed the FERC decision to the Federal Court of Appeals, which has set oral argument for May 9, 2005.

SDG&E has challenged the propriety of the disallowed ISO charges in several proceedings. In July 2001, SDG&E filed an arbitration claim against the ISO, claiming the ISO should not charge SDG&E for the transmission losses attributable to its SWPL co-owners' energy schedules. In October 2003, the arbitrator awarded SDG&E all amounts claimed, which totaled \$22 million, including interest, as of the time of the award. The ISO appealed this result to the FERC and decision on this appeal is pending.

SDG&E has also challenged at the FERC the ISO's grid management charges assessed on the subject SWPL schedules. In January 2004, the FERC denied rehearing of its Opinion No. 463, which upheld such charges on the subject SWPL schedules for 2001 through 2003, but ordered certain refunds to SDG&E. The refunds are pending before the FERC, as is a separate proceeding involving application of the charges to the subject schedules from 2004 forward. In addition, in March 2004, SDG&E petitioned the U.S. Court of Appeals for review of these FERC orders. The court has held SDG&E's appeal in abeyance pending the FERC's disposition of other parties' rehearing requests.

SDG&E has also commenced a private arbitration to reform the SWPL Participation Agreements to remove prospectively SDG&E's obligation to provide to its SWPL co-owners the services that result in unreimbursed ISO tariff charges. The parties have agreed to hold the arbitration in abeyance pending resolution of the related FERC proceedings.

#### **Southern California Wildfires**

On June 28, 2004, SDG&E filed its catastrophic event memorandum accounts (CEMA) application with the CPUC to recover incremental operating and maintenance and capital costs of its natural gas and electric distribution systems associated with the 2003 California wildfires. In that application, SDG&E is requesting a 2005 revenue requirement of \$20 million, representing the operating and maintenance costs of \$12 million plus the 2004 and 2005 ongoing annual amounts of \$4 million to recover the \$26 million of capital costs and the authorized return thereon. The company expects no significant effect on earnings from the fires. The assigned ALJ indicated that he expects to issue a proposed decision during the first quarter of 2005.

#### **Gain on Sale Rulemaking**

A gain on sale rulemaking was issued in September 2004 in order to standardize the treatment of gains on sales of property by utilities. This rulemaking may result in the adoption of a general

ratemaking policy for allocation between utility shareholders and ratepayers of any gain or loss on sale of utility property. The CPUC will consider adopting a standard percentage allocation, probably between 5 percent and 50 percent to shareholders, rather than resolving such allocations on a case-by-case basis, as is now its practice. In unusual circumstances the CPUC would be able to depart from the standard allocation to be adopted. The CPUC intends to apply this standard percentage to sales of both depreciable property and non-depreciable property. The Rulemaking states that the new policy would replace the CPUC'S current policy of allocating to shareholders all gain or loss on sale to a municipality of a utility operating system. The final outcome of the Rulemaking may be different than that proposed for comment in the order instituting the rulemaking. No schedule has been announced yet for this proceeding.

**NOTE 16. COMMITMENTS AND CONTINGENCIES**

**Natural Gas Contracts**

The California Utilities buy natural gas under short-term and long-term contracts. Purchases are from various Southwest U.S. and Canadian suppliers and are primarily based on monthly spot-market prices. The California Utilities transport natural gas under long-term firm pipeline capacity agreements that provide for annual reservation charges, which are recovered in rates. SoCalGas has commitments with pipeline companies for firm pipeline capacity under contracts that expire at various dates through 2007. Note 15 discusses the CPUC Gas Market OIR.

SDG&E has long-term natural gas transportation contracts with various interstate pipelines that expire on various dates between 2005 and 2023. SDG&E currently purchases natural gas on a spot basis to fill its long-term pipeline capacity, and purchases additional spot market supplies delivered directly to California for its remaining requirements. SDG&E continues its ongoing assessment of its long-term pipeline capacity portfolio, including the release of a portion of this capacity to third parties. In accordance with regulatory directives, SDG&E will reconfigure its pipeline capacity portfolio by November 2005 to secure firm transportation rights from a diverse mix of U.S. and Canadian supply sources for its projected core customer natural gas requirements.

At December 31, 2004, the future minimum payments under existing natural gas contracts were:

(Dollars in millions)	Storage and Transportation	Natural Gas	Total
2005	\$ 202	\$ 897	\$ 1,099
2006	123	179	302
2007	21	158	179
2008	20	3	23
2009	16	2	18
Thereafter	189	—	189
<b>Total minimum payments</b>	<b>\$ 571</b>	<b>\$ 1,239</b>	<b>\$ 1,810</b>

Total payments under natural gas contracts were \$2.8 billion in 2004, \$2.2 billion in 2003 and \$1.4 billion in 2002.

In October 2004, Sempra LNG signed a sale and purchase agreement with British Petroleum for the supply of 500 million cubic feet of natural gas per day from Indonesia's Tangguh liquefaction facility to Sempra LNG's Energia Costa Azul regasification terminal. The 20-year agreement provides for pricing tied to the Southern California border index for natural gas and will supply half of the capacity of Energia Costa Azul.

**Purchased-Power Contracts**

For 2005, SDG&E expects to receive 49 percent of its customer power requirement from DWR allocations. Of the remaining requirements, SONGS is expected to account for 21 percent, long-term contracts for 19 percent and spot market purchases for 11 percent. The contracts expire on various dates through 2032. In addition, during 2002 SDG&E entered into contracts which will provide five percent of its 2005 total energy sales from renewable sources. These contracts expire on various dates through 2025.

Sempra Commodities is committed to purchasing \$199 million of power from an unconsolidated affiliate in varying amounts through 2014.

At December 31, 2004, the estimated future minimum payments under the long-term contracts (not including the DWR allocations) were:

(Dollars in millions)	
2005	\$ 256
2006	279
2007	313
2008	358
2009	343
Thereafter	4,035
<b>Total minimum payments</b>	<b>\$ 5,584</b>

The payments represent capacity charges and minimum energy purchases. SDG&E is required to pay additional amounts for actual purchases of energy that exceed the minimum energy commitments. Excluding DWR-allocated contracts, total payments under the contracts were \$329 million in 2004, \$396 million in 2003 and \$235 million in 2002.

**Coal Commitments**

In October 2002, Sempra Generation acquired the 305-MW Twin Oaks Power plant. In connection with the acquisition, Sempra Generation assumed a contract that includes annual commitments to purchase lignite coal either until an aggregate minimum volume has been achieved or through 2025. As of December 31, 2004, Sempra Generation's future minimum payments under the lignite coal agreement totaled \$425 million, for which payments of \$31 million are due for 2005, \$28 million for 2006, \$27 million for 2007, \$27 million for 2008, \$27 million for 2009 and \$285 million thereafter. The minimum payments have been adjusted for allowed shortfalls and 90-percent minimum take-or-pay requirements under the contract.

**Leases**

The company has leases (primarily operating) on real and personal property expiring at various dates from 2005 to 2045. Certain leases on office facilities contain escalation clauses requiring annual increases in rent ranging from 2 percent to 5 percent. The rentals payable under these leases are determined on both fixed and percentage bases, and most leases contain extension options which are exercisable by the company. The company also has long-term capital leases on real property. Property, plant and equipment included \$28 million at December 31, 2004 and \$36 million at December 31, 2003, related to these leases. The associated accumulated amortization was \$24 million and \$23 million, respectively.

At December 31, 2004, the minimum rental commitments payable in future years under all noncancellable leases were as follows:

(Dollars in millions)	Operating Leases	Capitalized Leases
2005	\$ 107	\$ 2
2006	97	1
2007	93	1
2008	84	1
2009	82	—
Thereafter	178	1
<b>Total future rental commitments</b>	<b>\$ 641</b>	<b>6</b>
Imputed interest (6% to 10%)		(1)
<b>Net commitments</b>		<b>\$ 5</b>

In connection with the quasi-reorganization described in Note 1, PE recorded liabilities of \$102 million to adjust to fair value the operating leases related to its headquarters and other facilities at December 31, 1992. The remaining amount of these liabilities was \$30 million at December 31, 2004. These leases are included in the above table at the amounts provided in the lease.

Rent expense for operating leases totaled \$88 million in 2004, \$90 million in 2003 and \$81 million in 2002. Depreciation expense for capitalized leases is included in Depreciation and Amortization on the Statements of Consolidated Income.

#### Construction Projects

Sempra Global has several subsidiaries which have developed or are in the process of constructing various capital projects in the United States and in Mexico. The following is a summary of commitments related to the projects developed or under development, the background of which is provided in Note 2.

#### Sempra Generation

Sempra Generation is primarily in the business of acquiring, developing and operating power plants throughout the U.S. and Mexico. As of the end of 2004, Sempra Generation had eleven power plants in operation, including eight that are 50% owned.

Sempra Generation has a long-term service agreement expiring in 2023 for maintenance of the turbines at the Mesquite power plant. As of December 31, 2004, commitments under this agreement totaled \$264 million, including amounts due of \$14 million in 2005, \$14 million in 2006, \$15 million in 2007, \$15 million in 2008, \$15 million in 2009 and \$191 million thereafter.

Transportation of TDM's natural gas from Ehrenberg, Arizona to the interconnection with Gasoducto Bajanorte is being provided under an agreement with an unrelated party. Under the agreement, Sempra Generation is obligated to pay a monthly reservation charge for the transport of certain quantities until 2022. The future commitments related to this contract are \$79 million. Sempra Generation also has a 20-year agreement expiring in 2023 for maintenance of the turbines at TDM. As of December 31, 2004, commitments under this agreement totaled \$83 million, including amounts due of \$6 million in 2005, \$6 million in 2006, \$7 million in 2007, \$7 million in 2008, \$7 million in 2009 and \$50 million thereafter.

Sempra Generation also has commitments for general contracting work at Palomar totaling \$99 million as of December 31, 2004. It expects to pay \$94 million in 2005 and \$5 million in 2006.

Sempra Generation continues to investigate opportunities for new projects, either independently or with unrelated parties. The success of these investigations cannot be predicted. As of December 31, 2004, Sempra Generation has no other significant construction commitments.

#### **Sempra LNG**

Sempra LNG develops, builds and operates LNG receipt terminals and will be supplying gas to CFE.

In December 2004, Sempra LNG entered into an agreement with a group of companies for the construction of the Energía Costa Azul LNG receipt facility. The companies included Techint SA de CV, Black & Veatch, Mitsubishi Heavy Industries and Vinci Construction Grands Projects. As of December 31, 2004, expected payments under this contract include \$196 million in 2005, \$191 million in 2006 and \$95 million in 2007, for a total of \$482 million over the term of the contract. Also in December 2004, a joint venture involving the Costain Group PLC and China Harbour was awarded a construction contract for the project's breakwater. As of December 31, 2004, Sempra LNG expects to make payments under this contract of \$161 million, including \$58 million in 2005, \$81 million in 2006, \$14 million in 2007 and \$8 million in 2008.

#### **Sempra Pipelines & Storage**

In 2002, Sempra Pipelines & Storage completed construction of the 140-mile Gasoducto Bajanorte Pipeline that connects the Rosarito Pipeline south of Tijuana, Mexico with the TransCanada pipeline that connects to Arizona. The 30-inch pipeline can deliver up to 500 million cubic feet per day of natural gas to new generation facilities in Baja California, including Sempra Generation's TDM power plant discussed above. Capacity on the pipeline is over 90 percent subscribed. The company had no other commitments for this pipeline at December 31, 2004.

If Sempra Pipelines & Storage proceeds with development of its Liberty project, it will pay the prior owner of its development rights \$2 million upon receipt of the related FERC permit and seven percent of the project's revenues over the first five years of operations. A liability instrument will be recorded for these earn-out provisions if and when the company completes its feasibility studies and decides to proceed with this investment.

#### **Guarantees**

As of December 31, 2004, substantially all of the company's guarantees were intercompany, whereby the parent issues the guarantees on behalf of its consolidated subsidiaries. Significant other guarantees are the \$25 million related to debt issued by Chilquinta Energía Finance Co., LLC, an unconsolidated affiliate, and the mandatorily redeemable trust preferred securities, which were redeemed in February 2005.

In conjunction with the acquisition of the former AEP power plants, Sempra Energy provided AEP a guarantee for certain specified liabilities described in the acquisition agreement. Note 3 provides additional discussion related to the guarantee.

#### **Sempra Generation's Contract with the DWR**

In May 2001, Sempra Generation entered into a ten-year agreement with the DWR to supply up to 1,900 MW of power to California. Sempra Generation may, but is not obligated to, deliver this electricity from its portfolio of natural gas-fired plants in the western United States and Baja California, Mexico. If

and when Sempra Generation uses these plants to supply the entire 1,900 MW, those sales would comprise more than two-thirds of the plants' capacity. Subsequent to the state's signing of this contract and electricity-supply contracts with other vendors, various state officials have contended that the rates called for by the contracts are too high. Based on current natural gas prices, the price of power under the long-term contracts exceeds the current spot market price for electricity. Information concerning the validity of this contract, the FERC's orders upholding this contract and the pending appeal is provided under "Legal Proceedings — DWR Contract" below.

#### **Environmental Issues**

The company's operations are subject to federal, state and local environmental laws and regulations governing hazardous wastes, air and water quality, land use, solid waste disposal and the protection of wildlife. Most of the environmental issues faced by the company have occurred at the California Utilities. However, now that Sempra Generation owns and operates several power plants and Sempra LNG is developing LNG regasification terminals, additional environmental issues will arise. As applicable, appropriate and relevant, these laws and regulations require that the company investigate and remediate the effects of the release or disposal of materials at sites associated with past and present operations, including sites at which the company has been identified as a Potentially Responsible Party (PRP) under the federal Superfund laws and comparable state laws. The company is required to obtain numerous governmental permits, licenses and other approvals to construct facilities and operate its businesses. Additionally, to comply with these legal requirements, it must spend significant sums on environmental monitoring, pollution control equipment and emissions fees. Increasing national and international concerns regarding global warming and mercury, nitrogen oxide and sulfur dioxide emissions could result in requirements for additional pollution control equipment or significant emissions fees or taxes, particularly with respect to coal-fired generation facilities, that could adversely affect Sempra Generation. In addition, existing environmental regulations could be revised or reinterpreted and other new laws and regulations could be adopted or become applicable to the company and its facilities. Costs incurred at the California Utilities to operate the facilities in compliance with these laws and regulations generally have been recovered in customer rates.

Significant costs incurred to mitigate or prevent future environmental contamination or extend the life, increase the capacity or improve the safety or efficiency of property utilized in current operations are capitalized. The company's capital expenditures to comply with environmental laws and regulations were \$22 million in 2004, \$14 million in 2003 and \$8 million in 2002 (includes only the company's share in cases of non-wholly owned affiliates). The cost of compliance with these regulations over the next five years is not expected to be significant.

The company has identified no significant environmental issues outside the United States, except for the additional environmental impact studies the DOE is conducting of the TDM power plant near Mexicali, Baja California, Mexico. Additional information regarding the environmental studies is provided below under "Legal Proceedings."

At the California Utilities, costs that relate to current operations or an existing condition caused by past operations are generally recorded as a regulatory asset due to the assurance that these costs will be recovered in rates.

The environmental issues currently facing the company or resolved during the last three years include investigation and remediation of the California Utilities' manufactured-gas sites (29 completed as of December 31, 2004 and 15 to be completed), cleanup at SDG&E's former fossil fuel power plants (all sold in 1999 and actual or estimated cleanup costs included in the transactions), cleanup of third-party waste-disposal sites used by the company, which has been identified as a PRP (investigations and remediations are continuing) and mitigation of damage to the marine environment caused by the cooling-water discharge from SONGS (the requirements for enhanced fish protection, a 150-acre artificial reef and restoration of 150 acres of coastal wetlands are in process).



Environmental liabilities are recorded when the company's liability is probable and the costs are reasonably estimable. In many cases, however, investigations are not yet at a stage where the company has been able to determine whether it is liable or, if the liability is probable, to reasonably estimate the amount or range of amounts of the cost or certain components thereof. Estimates of the company's liability are further subject to other uncertainties, such as the nature and extent of site contamination, evolving remediation standards and imprecise engineering evaluations. The accruals are reviewed periodically and, as investigations and remediation proceed, adjustments are made as necessary. Costs of future expenditures for environmental remediation obligations are not discounted to their present value. Not including the liability for SONGS marine mitigation, which SDG&E is participating in jointly with Edison, at December 31, 2004, the company's accrued liability for environmental matters was \$53.6 million, of which \$42.3 million is related to manufactured-gas sites, \$8.7 million to cleanup at SDG&E's former fossil-fueled power plants, \$2.1 million to waste-disposal sites used by the company (which has been identified as a PRP) and \$0.5 million to other hazardous waste sites. These accruals are expected to be paid ratably over the next three years.

#### **Nuclear Insurance**

SDG&E and the other owners of SONGS have insurance to respond to nuclear liability claims related to SONGS. The insurance policy provides \$300 million in coverage, which is the maximum amount available. In addition to this primary financial protection, the Price-Anderson Act provides for up to \$10.5 billion of secondary financial protection if the liability loss exceeds the insurance limit. Should any of the licensed/commercial reactors in the United States experience a nuclear liability loss which exceeds the \$300 million insurance limit, all utilities owning nuclear reactors could be assessed under the Price-Anderson Act to provide the secondary financial protection. SDG&E and the other co-owners of SONGS could be assessed up to \$201 million under the Price-Anderson Act. SDG&E's share would be \$40 million unless a default were to occur by any other SONGS owner. In the event the secondary financial protection limit were insufficient to cover the liability loss, the Price-Anderson Act provides for Congress to enact further revenue-raising measures to pay claims. These measures could include an additional assessment on all licensed reactor operators.

SDG&E and the other owners of SONGS have \$2.75 billion of nuclear property, decontamination and debris removal insurance. The coverage also provides the SONGS owners up to \$490 million for outage expenses/replacement power incurred because of accidental property damage. This coverage is limited to \$3.5 million per week for the first 52 weeks, and \$2.8 million per week for up to 110 additional weeks. There is a deductible waiting period of 12 weeks prior to receiving indemnity payments. The insurance is provided through a mutual insurance company owned by utilities with nuclear facilities. Under the policy's risk sharing arrangements, insured members are subject to retrospective premium assessments if losses at any covered facility exceed the insurance company's surplus and reinsurance funds. Should there be a retrospective premium call, SDG&E could be assessed up to \$8.8 million.

Both the nuclear liability and property insurance programs subscribed to by members of the nuclear power generating industry include industry aggregate limits for non-certified acts (as defined by the Terrorism Risk Insurance Act) of terrorism-related SONGS losses, including replacement power costs. An industry aggregate limit of \$300 million exists for liability claims, regardless of the number of non-certified acts affecting SONGS or any other nuclear energy liability policy or the number of policies in place. An industry aggregate limit of \$3.24 billion exists for property claims, including replacement power costs, for non-certified acts of terrorism affecting SONGS or any other nuclear energy facility property policy within twelve months from the date of the first act. These limits are the maximum amount to be paid to members who sustain losses or damages from these non-certified terrorist acts.

For certified acts of terrorism, the individual policy limits stated above apply.

SEMPRA ENERGY 100.

**Legal Proceedings**

Except for the matters referred to below, neither the company nor its subsidiaries are party to, nor is their property the subject of, any material pending legal proceedings other than routine litigation incidental to their businesses. At December 31, 2004, the company had accrued approximately \$250 million to provide for the costs of its legal proceedings, of which approximately \$240 million related to cases arising from the 2000-2001 California energy crisis. Management believes that none of these matters will have further material adverse effect on the company's financial condition or results of operations.

**DWR Contract**

In 2003, Sempra Generation was awarded judgment in its favor in a state civil action between Sempra Generation and the DWR, in which the DWR sought to void its 10-year contract expiring in 2011 under which the company sells electricity to the DWR. The DWR filed an appeal of this ruling in January 2004. A decision by the appellate court is expected during 2005.

The DWR continues to accept scheduled power from Sempra Generation and, although it has disputed a portion of the billings and the manner of certain deliveries, it has paid all amounts billed, as required by the contract in the event of disputes. However, the DWR has commenced an arbitration proceeding disputing Sempra Generation's performance on various operational matters. Among other proposed remedies, the DWR has requested a declaration by the arbitration panel that Sempra Generation's performance violates the terms of the contract and constitutes a material breach of the agreement, permitting it to terminate the contract. Sempra Generation believes these claims are without merit. In November 2004, the arbitration panel denied Sempra Generation's motion to dismiss claims. Arbitration is expected to occur in mid-2005.

On June 25, 2003, the FERC issued orders upholding Sempra Generation's long-term energy supply contract with the DWR, as well as contracts between the DWR and other power suppliers. The order affirmed a previous FERC conclusion that those advocating termination or alteration of the contract would have to satisfy a "heavy" burden of proof, and cited its long-standing policy to recognize the sanctity of contracts. In the order, the FERC noted that CPUC and court precedent clearly establish that allegations that contracts have become uneconomic by the passage of time do not render them contrary to the public interest under the Federal Power Act. The FERC pointed out that the contracts were entered into voluntarily in a market-based environment. The FERC found no evidence of unfairness, bad faith or duress in the original contract negotiations. It said there was no credible evidence that the contracts placed the complainants in financial distress or that ratepayers will bear an excessive burden. In December 2003, appeals of this matter filed by a number of parties, including the California Energy Oversight Board and the CPUC, were consolidated and assigned to the Ninth Circuit Court of Appeals. Oral argument on the appeal was held in December 2004, with a decision by the appellate court expected in 2005.

**California Energy Crisis**

In 2000 and 2001, California experienced a severe energy crisis characterized by dramatic increases in the prices of electricity and natural gas. The energy crisis has generated many, often duplicative, governmental investigations, regulatory proceedings and lawsuits involving numerous energy companies seeking recovery of tens of billions of dollars for allegedly unlawful activities asserted to have caused or contributed to the energy crisis. The material proceedings arising out of the energy crisis that involve the company are summarized below.

#### Natural Gas Cases

*Class-action and individual antitrust and unfair competition lawsuits filed in 2000 and thereafter, and currently consolidated in San Diego Superior Court, seek damages, alleging that Sempra Energy, SoCalGas and SDG&E, along with El Paso and several of its affiliates, unlawfully sought to control natural gas and electricity markets. In December 2003, the Court approved a settlement whereby the applicable El Paso entities will pay approximately \$1.6 billion to resolve these claims (including cases involving unrelated claims not applicable to Sempra Energy, SoCalGas or SDG&E). The proceeding against Sempra Energy and the California Utilities has not been settled and continues to be litigated. In October 2004, certain of the plaintiffs issued a news release asserting that they could recover as much as \$24 billion from Sempra Energy and the California Utilities if their allegations were upheld at trial. During the third quarter of 2004, the court denied motions for summary judgment in favor of Sempra Energy and the California Utilities. The Court of Appeal has declined to review the summary judgment denial and the companies have petitioned for review by the California Supreme Court. Interim review pending a final decision on the merits of the case is entirely at the discretion of the California Supreme Court. On January 18, 2005, the judge stated that pre-trial motions will be heard on June 3, 2005, and set a trial date of September 2, 2005.*

*Similar lawsuits have been filed by the Attorneys General of Arizona and Nevada, alleging that El Paso and certain Sempra Energy subsidiaries unlawfully sought to control the natural gas market in their respective states. The claims against the Sempra Energy defendants in the Arizona lawsuit were settled in September 2004 for \$150,000 and have been dismissed with prejudice. The Nevada Attorney General's lawsuit remains pending.*

*The company is cooperating with an investigation being conducted by the California Attorney General into possible anti-competitive behavior in the natural gas and electricity markets during the 2000-2001 energy crisis. In December 2004, several of the company's senior officers testified at investigational hearings conducted by the California Attorney General's Office. The company expects additional hearings to take place in early 2005.*

*In April 2003, Sierra Pacific Resources and its utility subsidiary Nevada Power filed a lawsuit in U.S. District Court in Las Vegas against major natural gas suppliers, and included Sempra Energy, the California Utilities and other company subsidiaries, seeking recovery of damages alleged to aggregate in excess of \$150 million (before trebling) from an alleged conspiracy to drive up or control natural gas prices, eliminate competition and increase market volatility, breach of contract and wire fraud. On January 27, 2004, the U.S. District Court dismissed the Sierra Pacific Resources case against all of the defendants, determining that this is a matter for the FERC to resolve. However, the court granted plaintiffs' request to amend their complaint. Sempra Energy filed another motion to dismiss on plaintiffs' amended complaint. After argument on November 29, 2004, the federal court dismissed the Sierra Pacific case with prejudice. Plaintiffs have filed a notice of appeal with the Ninth Circuit Court of Appeals.*

*In May 2003 and February 2004, two antitrust actions against various energy companies, including Sempra Energy and Sempra Commodities, were filed in San Diego Superior Court alleging that energy prices were unlawfully manipulated by defendants' reporting artificially inflated natural gas prices to trade publications and by entering into wash trades. Both actions were removed to U.S. District Court. In November 2003, an additional suit was filed in U.S. District Court. In September 2004, two additional lawsuits alleging substantially identical claims were filed against Sempra Energy and Sempra Commodities, among various other entities, in San Diego Superior and U.S. District Courts. Two additional, substantially identical lawsuits were filed against Sempra Commodities in November and December 2004 in the U.S. District Court in Fresno, California. In November 2004, the federal district court judge assigned to hear these cases determined that the cases originally filed in state court should*

return to that court system. On February 14, 2005, the California state court cases, including those described below, were assigned to the same judge overseeing the El Paso-related cases.

In July 2004, the City and County of San Francisco, the County of Santa Clara and the County of San Diego brought similar actions in San Diego Superior Court against various entities, including Sempra Energy, Sempra Commodities, SoCalGas and SDG&E. Six identical lawsuits were filed in the fourth quarter of 2004 in the Alameda and San Mateo Superior Courts and one in Sacramento Superior Court. In December 2004, the City of San Diego also filed an identical suit in San Diego Superior Court. These suits are also now pending before the same San Diego Superior Court judge described above.

In August 2003, a lawsuit was filed in the Southern District of New York against Sempra Energy and its subsidiary, Sempra Energy Solutions, alleging that the prices of natural gas options traded on the New York Mercantile Exchange (NYMEX) were unlawfully increased under the Federal Commodity Exchange Act by defendants' manipulation of transaction data provided to natural gas trade publications. In November 2003, another suit containing identical allegations was filed and consolidated with the New York action. Subsequently, plaintiffs dismissed Sempra Energy and Sempra Energy Solutions from these cases. On January 20, 2004, plaintiffs filed an amended consolidated complaint that named Sempra Commodities as a defendant in this lawsuit. In March 2004, defendants filed a motion to dismiss the action, which was denied by the court in September 2004. In October 2004, plaintiffs amended their complaint to allege that Sempra Commodities had engaged in natural gas wash trade transactions.

#### **Electricity Cases**

Various antitrust lawsuits, which seek class-action certification, allege that numerous entities, including Sempra Energy and certain subsidiaries (SDG&E, Sempra Commodities and Sempra Generation, depending on the lawsuit), that participated in the wholesale electricity markets unlawfully manipulated those markets. Collectively, these lawsuits allege damages against all defendants in an aggregate amount in excess of \$16 billion (before trebling). In January 2003, the federal court granted a motion to dismiss one of these lawsuits, filed by the Snohomish County, Washington Public Utility District, on the grounds that the claims contained in the complaint were subject to the filed rate doctrine and were preempted by the Federal Power Act. That ruling was appealed to the Ninth Circuit U.S. Court of Appeals. In addition, in May 2003, the Port of Seattle filed a similar complaint against a number of energy companies, including Sempra Energy, Sempra Generation and Sempra Commodities. That action was dismissed by the San Diego U.S. District Court in May 2004. Plaintiff has appealed the decision. In May and June 2004, two lawsuits substantially identical to the Port of Seattle case were filed in Washington and Oregon U.S. District Courts. These cases were transferred to the San Diego U.S. District Court and motions to dismiss were granted in both cases on February 11, 2005. In October 2004, another case was filed in Santa Clara Superior Court against Sempra Generation, alleging substantively identical claims to those in the Port of Seattle case.

In September 2004, the Ninth Circuit U.S. Court of Appeals dismissed the suit against Sempra Energy, Sempra Commodities and Sempra Generation by the Snohomish County, Washington Public Utility District. The court ruled that the FERC, not civil courts, has exclusive jurisdiction over the matter. The company believes that this decision provides a precedent for the dismissal on the basis of federal preemption and the filed rate doctrine of the other lawsuits against the Sempra Energy companies claiming manipulation of the electricity markets. Snohomish County has appealed the Ninth Circuit decision to the U.S. Supreme Court.

#### **CPUC Border Price Investigation**

In November 2002, the CPUC instituted an investigation into the Southern California natural gas market and the price of natural gas delivered to the California — Arizona border between March 2000

and May 2001. The California Utilities are the parties to the first phase of the investigation. If the investigation were to determine that the conduct of either of the California Utilities contributed to the natural gas price spikes that occurred during the investigation period, the CPUC may modify the party's natural gas procurement incentive mechanism, reduce the amount of any shareholder award for the period involved, and/or order the party to issue a refund to ratepayers. At December 31, 2004, the cumulative amount of shareholder awards, substantially all of which has been included in net income, was \$65.3 million.

On November 16, 2004, the CPUC Administrative Law Judge assigned to the investigation issued a proposed decision for consideration by the full CPUC in the first phase of the investigation that was highly critical of SoCalGas' natural gas purchase, sales, hedging and storage activities and would find that SoCalGas exercised market power and manipulated the natural gas market, significantly contributing to natural gas price spikes that also increased electricity prices. The proposed decision did not include any adverse findings or make any adverse recommendations regarding SDG&E.

On December 16, 2004, the CPUC rejected the amended proposed decision by a 3-2 vote. The two commissioners who voted in favor of the proposed decision were Commissioners Lynch and Wood, whose terms on the CPUC expired at year end. It is now up to the remaining commissioners plus any new appointees to determine whether to issue an alternate proposed decision, hold additional hearings, or issue an order terminating the investigation.

The CPUC may hold additional rounds of hearings to consider whether other companies, including other California utilities as well as the company and its non-utility subsidiaries, contributed to the natural gas price spikes. No hearings have yet been scheduled.

#### **FERC Refund Proceedings**

The FERC is investigating prices charged to buyers in the California Power Exchange (PX) and ISO markets by various electric suppliers. The FERC is seeking to determine the extent to which individual sellers have yet to be paid for power supplied during the period of October 2, 2000 through June 20, 2001 and to estimate the amounts by which individual buyers and sellers paid and were paid in excess of competitive market prices. Based on these estimates, the FERC could find that individual net buyers, such as SDG&E, are entitled to refunds and individual net sellers, such as Sempra Commodities, are required to provide refunds. To the extent any such refunds are actually realized by SDG&E, they would be refunded to ratepayers. To the extent that Sempra Commodities is required to provide refunds, they could result in payments by Sempra Commodities after adjusting for any amounts still owed to Sempra Commodities for power supplied during the relevant period (or reduced receipts if refunds are less than amounts owed to Sempra Commodities).

In December 2002, a FERC ALJ issued preliminary findings indicating that the California PX and ISO owe power suppliers \$1.2 billion for the October 2, 2000 through June 20, 2001 period (the \$3.0 billion that the California PX and ISO still owe energy companies less \$1.8 billion that the energy companies charged California customers in excess of the preliminarily determined competitive market clearing prices). On March 26, 2003, the FERC adopted its ALJ's findings, but changed the calculation of the refund by basing it on a different estimate of natural gas prices. The March 26 order estimates that the replacement formula for estimating natural gas prices will increase the refund obligations from \$1.8 billion to more than \$3 billion for the same time period. Pending in the Ninth Circuit are various parties' appeals on aspects of the FERC's order.

In a series of orders in 2004, the FERC has provided further direction and clarifications regarding the methodology to be used by the ISO and PX to recalculate the precise refund obligations and entitlements through their settlement models.

Sempra Commodities previously established reserves for its likely share of the original \$1.8 billion discussed above. During 2004, Sempra Commodities recorded additional reserves to reflect the estimated effect of the FERC's revision of the benchmark prices to be used by the FERC to calculate refunds, and Sempra Generation recorded its share of the 2004 amounts related to its transactions with Sempra Commodities.

In a separate complaint filed with the FERC in 2002, the California Attorney General challenged the FERC's authority to establish a market-based rate regime, and further contended that, even if such a regime were valid, electricity sellers had failed to comply with the FERC's quarterly reporting requirements. The Attorney General requested that the FERC order refunds from suppliers to the California PX and ISO for the period prior to October 2, 2000, and for short-term bilateral transactions entered into with the California Energy Resources Scheduler. In May 2003, and upon rehearing in September 2003, the FERC dismissed the complaint, determining that its market-based rate system was lawful, and that refunds for non-compliance with its reporting requirements were unnecessary, and instead ordered sellers to restate their reports. After an appeal by the California Attorney General, in September 2004, the Ninth Circuit Court of Appeals upheld the FERC's authority to establish a market-based rate regime, but ordered remand of the case to the FERC for further proceedings, stating that failure to file transaction-specific quarterly reports gave the FERC authority to order refunds with respect to jurisdictional sellers. In October 2004, the FERC announced that it will not appeal the court's decision. Although a group of sellers has requested the Ninth Circuit to rehear this matter, the timing and substance of the FERC's response to the remand is not yet known. However, it is possible that the FERC could order refunds or disgorgement of profits for periods in addition to those covered by its prior refund orders and substantially increase the refunds that ultimately may be required to be paid by Sempra Commodities and other power suppliers.

#### **FERC Manipulation Investigation**

The FERC is separately investigating whether there was manipulation of short-term energy markets in the western United States that would constitute violations of applicable tariffs and warrant disgorgement of associated profits. In this proceeding, the FERC's authority is not confined to the periods relevant to the refund proceeding. In May 2002, the FERC ordered all energy companies engaged in electric energy trading activities to state whether they had engaged in various specific trading activities (generally described as manipulating or "gaming" the California energy markets) in violation of the PX and ISO tariffs.

On June 25, 2003, the FERC issued several orders requiring various entities to show cause why they should not be found to have violated California ISO and PX tariffs. First, the FERC directed 43 entities, including Sempra Commodities and SDG&E, to show cause why they should not disgorge profits from certain transactions between January 1, 2000 and June 20, 2001 that are asserted to have constituted gaming and/or anomalous market behavior under the California ISO and/or PX tariffs. Second, the FERC directed more than 20 entities, including Sempra Commodities, to show cause why their activities, in partnership or in alliance with others, during the period between January 1, 2000 and June 20, 2001 did not constitute gaming and/or anomalous market behavior in violation of the tariffs. Remedies for confirmed violations could include disgorgement of profits and revocation of market-based rate authority. The FERC has encouraged the various entities to settle these issues. On October 31, 2003, Sempra Commodities agreed to pay \$7.2 million in full resolution of these investigations. That liability was recorded as of December 31, 2003. The Sempra Commodities settlement was approved by the FERC on August 2, 2004. Certain California parties have sought rehearing of this order. SDG&E and the FERC resolved the matter through a settlement, which documents the ISO's finding that SDG&E did not engage in market activities in violation of the ISO or PX tariffs, and in which SDG&E agreed to pay \$27,792 into a FERC-established fund.

On February 16, 2005, in connection with the California Senate Select Committee's investigation into Price Manipulation in the Wholesale Energy Market, Senator Dunn held a press conference and asserted that Sempra Commodities committed perjury in denying that it had engaged in three types of Enron-like strategies. Senator Dunn stated that he intends to refer the matter to the Sacramento District Attorney's Office and to seek contempt charges from the state Senate. The company denies these charges and will defend the matters vigorously.

On June 25, 2003, the FERC determined that it was appropriate to initiate an investigation into possible physical and economic withholding in the California ISO and PX markets. On August 1, 2003, the FERC staff issued an initial report that determined there was no need to further investigate particular entities, including Sempra Commodities, for physical withholding of generation. For the purpose of investigating economic withholding, both SDG&E and Sempra Commodities received data requests from the FERC staff and provided responses. In May 2004, based on the results of its investigation, the FERC's Office of Market Oversight and Investigation informed SDG&E and Sempra Commodities that their bidding procedures are no longer being investigated by the FERC.

#### **Settlement of Claims Associated with the FERC's Investigations**

During 2004, three settlements of claims associated with the FERC's investigations were announced. One settlement, in which SDG&E received a net payment of \$11.6 million in August 2004, resolves all but a few claims against The Williams Companies and Williams Power Company for the period May 1, 2000 through June 20, 2001. Another settlement, in which SDG&E received a net payment of \$13.5 million (of the \$13.8 million total SDG&E settlement allocation) in November 2004, resolves all claims against Dynegy, NRG Energy and West Coast Power LLC for the period January 1, 2000 through June 20, 2001. A third settlement, in which SDG&E received a net payment of \$14.4 million (of the \$14.7 million total SDG&E settlement allocation) in January 2005, resolves specified claims against Duke Energy for the period January 1, 2000 through June 20, 2001. On January 13, 2005, SDG&E announced a \$23.8 million settlement (including an unsecured claim in the Mirant bankruptcy proceeding valued at approximately \$2.4 million), which resolves specified claims against merchant generator Mirant Corp. for the 2000-2001 energy crisis period. The settlement is pending final CPUC, FERC and U.S. Bankruptcy Court (for Mirant) approval. In all cases, the majority of the funds was received within 20 days of receiving FERC approval with the remainder contingent on certain actions by the FERC, the ISO and the PX. Receipt of the remaining amounts by SDG&E would take place at the conclusion of the FERC refund proceeding, now expected to be in early 2006. These funds would be received for the benefit of SDG&E's bundled customers and will reimburse SDG&E for the costs of litigating this matter. In November 2004, the CPUC approved SDG&E's proposal to apply 70 percent (about \$17 million) of the refunds due to ratepayers to the AB 265 undercollection, thus facilitating the full recovery of the undercollections, as further discussed in Note 14. Claims alleged against Sempra Commodities are still pending.

#### **Other Litigation**

The Utility Consumers' Action Network (UCAN), a consumer-advocacy group which had requested a CPUC rehearing of a CPUC decision concerning the allocation of certain power contract gains between SDG&E customers and the company, appealed the CPUC's rehearing denial to the California Court of Appeal. On July 12, 2004, the Court of Appeal affirmed the CPUC's decision. On August 20, 2004, UCAN filed a Petition for Review in the California Supreme Court. On November 10, 2004, the Supreme Court denied review.

In May 2003, a federal judge issued an order finding that the DOE's environmental assessment of the TDM plant and another, unrelated Mexicali power plant failed to evaluate the plants' environmental impact adequately and called into question the U.S. permits they received to build their cross-border transmission lines. In July 2003, the judge ordered the DOE to conduct additional environmental

studies and denied the plaintiffs' request for an injunction blocking operation of the transmission lines, thus allowing the continued operation of the TDM plant. The DOE undertook to perform an Environmental Impact Study, which was completed in December 2004. Plaintiff may elect to dismiss its complaint or to further challenge the agency action. If a stipulation of dismissal is not filed to terminate the litigation by August 15, 2005, the DOE will file a motion by August 22, 2005, showing cause why the court should not set aside the permits. In that event, court hearings may take place in the fourth quarter of 2005.

The Peruvian appellate court has affirmed the dismissal of the charges against officers of Luz del Sur and others concerning the price of some utility networks transferred from the Peruvian government to Luz del Sur.

The Peruvian tax authorities (Sunat) continue to claim that Luz del Sur owes additional income taxes, interest and penalties related to a 1996 revaluation of assets. The tax court held a final hearing on November 10, 2004, with both parties presenting their cases. On November 17, 2004, Luz del Sur submitted a summary of its arguments to the tax court. The tax court ruled in December 2004 that a third revaluation study be done, which will be used as a basis for its decision. The Conata, the national assessors association, was selected to do the study. After the Conata completes its study (expected in mid 2005), the tax court has 90 business days to issue a verdict.

At December 31, 2004, Sempra Commodities remains due approximately \$100 million from energy sales made in 2000 and 2001 through the ISO and the PX markets. The collection of these receivables depends on several factors, including the FERC refund case. The company believes adequate reserves have been recorded.

#### **Argentine Investments**

As a result of the devaluation of the Argentine peso at the end of 2001 and subsequent further declines, Sempra Pipelines & Storage reduced the carrying value of its investment downward by a cumulative total of \$198 million as of December 31, 2004 (\$197 million as of December 31, 2003). These non-cash adjustments continue to occur based on fluctuations in the Argentine peso. They do not affect net income, but increase or decrease other comprehensive income (loss) and Accumulated Other Comprehensive Income (Loss).

A decision is expected in 2006 on Sempra Pipelines & Storage's arbitration proceedings under the 1994 Bilateral Investment Treaty between the United States and Argentina for recovery of the diminution of the value of Sempra Pipelines & Storage's investments that has resulted from Argentine governmental actions. Sempra Energy also has a \$48.5 million political-risk insurance policy under which it filed a claim to recover a portion of the investments' diminution in value.

#### **Department Of Energy Nuclear Fuel Disposal**

The Nuclear Waste Policy Act of 1982 made the DOE responsible for the disposal of spent nuclear fuel. However, it is uncertain when the DOE will begin accepting spent nuclear fuel from SONGS. This delay by the DOE will lead to increased cost for spent fuel storage. This cost will be recovered through SONGS revenue unless the company is able to recover the increased cost from the federal government.

#### **Electric Distribution System Conversion**

Under a CPUC-mandated program, the cost of which is included in utility rates, and through franchise agreements with various cities, SDG&E is committed, in varying amounts, to converting overhead distribution facilities to underground. As of December 31, 2004, the aggregate unexpended amount of



this commitment was \$80 million. Capital expenditures for underground conversions were \$23 million in 2004, \$28 million in 2003 and \$33 million in 2002.

**Concentration Of Credit Risk**

The company maintains credit policies and systems to manage overall credit risk. These policies include an evaluation of potential counterparties' financial condition and an assignment of credit limits. These credit limits are established based on risk and return considerations under terms customarily available in the industry. The California Utilities grant credit to utility customers and counterparties, substantially all of whom are located in their service territories, which together cover most of Southern California and a portion of central California.

As described above, Sempra Generation has a contract with the DWR to supply up to 1,900 MW of power to the state over 10 years, beginning in 2001. Sempra Generation would be at risk for the amounts of outstanding billings and the continued viability of the contract if the DWR were to default on its payments under this contract. At any given time, the average outstanding billings related to this contract are \$50 million to \$60 million.

Sempra Commodities monitors and controls its credit-risk exposures through various systems which evaluate its credit risk, and through credit approvals and limits. To manage the level of credit risk, Sempra Commodities deals with a majority of counterparties with good credit standing, enters into netting arrangements whenever possible and, where appropriate, obtains collateral or other security such as lock-box liens and downgrade triggers. Netting agreements incorporate rights of setoff that provide for the net settlement of subject contracts with the same counterparty in the event of default.

The developing LNG projects will result in significant reliance on the credit-worthiness of its major suppliers and customers of those projects.

**NOTE 17. SEGMENT INFORMATION**

The company has four separately managed reportable segments: SoCalGas, SDG&E, Sempra Commodities and Sempra Generation. The California Utilities operate in essentially separate service territories under separate regulatory frameworks and rate structures set by the CPUC. SoCalGas is a natural gas distribution utility, serving customers throughout most of southern California and part of central California. SDG&E provides electric service to San Diego and southern Orange counties and natural gas service to San Diego County. Sempra Commodities, based in Stamford, Connecticut, is primarily a wholesale trader of physical and financial energy products and other commodities, and a trader and wholesaler of metals, serving a broad range of customers in the United States, Canada, Europe and Asia. As a result of the movement of the former Sempra Energy Solutions' commodities business into Sempra Commodities, Sempra Commodities' business also includes commodity sales on a retail basis to electricity and natural gas consumers. Sempra Generation primarily acquires, develops and operates power plants throughout the U.S. and Mexico and, as a result of the movement of the former Sempra Energy Solutions' energy businesses into Sempra Generation, provides energy services and facilities management. Sempra Generation also owns mineral rights in properties that produce petroleum and natural gas.

The accounting policies of the segments are described in Note 1, and segment performance is evaluated by management based on reported net income. California Utility transactions are based on rates set by the CPUC and the FERC.

(Dollars in millions)	Years ended December 31,					
	2004		2003		2002	
<b>OPERATING REVENUES</b>						
Southern California Gas Company	\$ 3,997	42%	\$ 3,544	45%	\$ 2,858	47%
San Diego Gas & Electric	2,274	24	2,311	29	1,725	29
Sempra Commodities	1,680	18	1,217	16	910	15
Sempra Generation	1,647	18	773	10	437	7
All other	146	2	99	1	155	3
Intersegment revenues	(334)	(4)	(57)	(1)	(37)	(1)
Total	\$ 9,410	100%	\$ 7,887	100%	\$ 6,048	100%
<b>INTEREST EXPENSE</b>						
Southern California Gas Company	\$ 39		\$ 45		\$ 44	
San Diego Gas & Electric	68		73		77	
Sempra Commodities	23		31		45	
Sempra Generation	34		33		10	
All other	331		256		190	
Intercompany elimination	(173)		(130)		(72)	
Total	\$ 322		\$ 308		\$ 294	
<b>INTEREST INCOME</b>						
Southern California Gas Company	\$ 4		\$ 34		\$ 5	
San Diego Gas & Electric	25		42		10	
Sempra Commodities	8		12		11	
Sempra Generation	7		17		4	
All other	198		129		84	
Intercompany elimination	(173)		(130)		(72)	
Total	\$ 69		\$ 104		\$ 42	
<b>DEPRECIATION AND AMORTIZATION</b>						
Southern California Gas Company	\$ 255	41%	\$ 289	47%	\$ 276	46%
San Diego Gas & Electric	259	42	242	39	230	39
Sempra Commodities	23	4	23	4	21	3
Sempra Generation	44	7	21	3	10	2
All other	40	6	40	7	59	10
Total	\$ 621	100%	\$ 615	100%	\$ 596	100%
<b>INCOME TAX EXPENSE (BENEFIT)</b>						
Southern California Gas Company	\$ 154	80%	\$ 150	319%	\$ 178	122%
San Diego Gas & Electric	148	77	148	315	91	62
Sempra Commodities	161	83	67	143	75	51
Sempra Generation	91	47	27	57	40	28
All other	(361)	(187)	(345)	(734)	(238)	(163)
Total	\$ 193	100%	\$ 47	100%	\$ 146	100%
<b>NET INCOME (LOSS)</b>						
Southern California Gas Company	\$ 232	26%	\$ 209	32%	\$ 212	36%
San Diego Gas & Electric	208	23	334	52	203	34
Sempra Commodities	320	36	128	20	165	28
Sempra Generation	137	15	80	12	42	7
All other	(2)	—	(102)	(16)	(31)	(5)
Total	\$ 895	100%	\$ 649	100%	\$ 591	100%

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(Dollars in millions)	2004		At December 31 or years ended December 31,		2003		2002		
<b>ASSETS</b>									
Southern California Gas Company	\$	5,502	23%	\$	5,349	24%	\$	5,403	27%
San Diego Gas & Electric		6,834	29		6,461	29		6,285	31
Sempra Commodities		7,574	32		6,144	28		5,780	28
Sempra Generation		2,738	12		2,550	12		1,633	8
All other		1,997	8		1,988	9		1,783	9
Intersegment receivables		(1,002)	(4)		(504)	(2)		(642)	(3)
Total	\$	23,643	100%	\$	21,988	100%	\$	20,242	100%
<b>CAPITAL EXPENDITURES</b>									
Southern California Gas Company	\$	311	29%	\$	318	30%	\$	331	27%
San Diego Gas & Electric		414	38		444	42		400	33
Sempra Commodities		126	12		51	5		21	2
Sempra Generation		141	13		144	14		359	30
All other		91	8		92	9		103	8
Total	\$	1,083	100%	\$	1,049	100%	\$	1,214	100%
<b>GEOGRAPHIC INFORMATION</b>									
Long-lived assets									
United States	\$	10,975	89%	\$	10,380	89%	\$	9,548	90%
Latin America		1,177	10		1,121	10		1,062	10
Europe		98	1		87	1		18	—
Canada		—	—		—	—		3	—
Total	\$	12,250	100%	\$	11,588	100%	\$	10,631	100%
Operating revenues									
United States	\$	8,518	91%	\$	7,211	92%	\$	5,503	91%
Latin America		311	3		315	4		168	3
Europe		519	6		323	4		328	6
Canada		37	—		10	—		28	—
Asia		25	—		28	—		21	—
Total	\$	9,410	100%	\$	7,887	100%	\$	6,048	100%

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**NOTE 18. QUARTERLY FINANCIAL DATA (UNAUDITED)**

(Dollars and shares in millions, except per share amounts)	Quarters ended			
	March 31	June 30	September 30	December 31
<b>2004</b>				
Operating revenues	\$ 2,360	\$ 1,996	\$ 2,165	\$ 2,889
Operating expenses	2,028	1,776	1,820	2,514
Operating income	\$ 332	\$ 220	\$ 345	\$ 375
Income from continuing operations	\$ 221	\$ 129	\$ 231	\$ 339
Net income	\$ 197	\$ 121	\$ 231	\$ 346
<b>Basic earnings per share:</b>				
Income from continuing operations	\$ 0.97	\$ 0.56	\$ 1.01	\$ 1.47
Net income	\$ 0.86	\$ 0.52	\$ 1.01	\$ 1.50
Average common shares outstanding	228.1	230.4	229.4	230.8
<b>Diluted earnings per share:</b>				
Income from continuing operations	\$ 0.96	\$ 0.55	\$ 0.98	\$ 1.43
Net income	\$ 0.85	\$ 0.52	\$ 0.98	\$ 1.46
Average common shares outstanding	231.1	234.3	235.9	237.5
<b>2003</b>				
Operating revenues	\$ 1,923	\$ 1,840	\$ 2,058	\$ 2,066
Operating expenses	1,708	1,637	1,751	1,852
Operating income	\$ 215	\$ 203	\$ 307	\$ 214
Income before cumulative effect of changes in accounting principles	\$ 117	\$ 116	\$ 211	\$ 251
Net income	\$ 88	\$ 116	\$ 211	\$ 234
<b>Basic earnings per share:</b>				
Income before cumulative effect of changes in accounting principles	\$ 0.57	\$ 0.56	\$ 1.01	\$ 1.12
Net income	\$ 0.43	\$ 0.56	\$ 1.01	\$ 1.05
Average common shares outstanding	206.4	207.6	208.8	224.0
<b>Diluted earnings per shares:</b>				
Income before cumulative effect of changes in accounting principles	\$ 0.56	\$ 0.55	\$ 1.00	\$ 1.11
Net income	\$ 0.42	\$ 0.55	\$ 1.00	\$ 1.03
Average common shares outstanding	207.8	210.2	212.3	227.2

Operating revenues and expenses in the fourth quarter of 2004 included the favorable impact of the final cost of service decision and operating expenses included litigation costs recorded in the fourth quarter. Net income in the first and second quarters of 2004 included \$24 million and \$8 million, respectively, of losses related to the discontinuance and disposal of AEG. Net income in the fourth quarter of 2004 included the \$38 million favorable impact of income tax issues related to the reduced estimate of federal and state income tax liabilities for certain prior years and the \$7 million favorable tax adjustment related to AEG. Note 4 provides a discussion of discontinued operations.

Operating revenues in the third quarter of 2003 included the recognition of \$116 million before-tax related to the approved settlement of intermediate-term purchase power contracts at SDG&E and \$48 million of natural gas procurement awards at SoCalGas. The after-tax impacts to net income were \$65 million and \$29 million, respectively. Additionally, operating expenses in the third quarter of 2003 were impacted by a \$77 million impairment charge to write down the carrying value of the assets of Frontier

Energy and a \$74 million before-tax charge for litigation and for losses associated with a sublease of portions of the SoCalGas headquarters building. The after-tax impacts to net income were \$47 million and \$43 million, respectively.

In the first quarter of 2003, net income reflected a \$29 million charge related to the cumulative effect of a change in accounting principle at Sempra Commodities. Net income in the fourth quarter of 2003 included \$118 million related to the favorable resolution of income tax issues at the California Utilities and the unfavorable net impact of \$17 million related to the cumulative effect of changes in accounting principles.

**QUARTERLY COMMON STOCK DATA (UNAUDITED)**

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
<b>2004</b>				
Market price				
High	\$ 32.99	\$ 34.90	\$ 37.19	\$ 37.93
Low	\$ 29.51	\$ 30.80	\$ 33.97	\$ 31.00
<b>2003</b>				
Market price				
High	\$ 26.00	\$ 29.40	\$ 30.33	\$ 30.90
Low	\$ 22.25	\$ 24.05	\$ 27.31	\$ 26.36

Dividends declared were \$0.25 per share in each quarter.

SEMPRA ENERGY  
Schedule of Significant Subsidiaries at December 31, 2004

<i>Subsidiary</i>	<i>State of Incorporation or Other Jurisdiction</i>
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<i>Chilquinta Energia, S.A.</i>	<i>Chile</i>
<i>Luz del Sur, S.A.A.</i>	<i>Peru</i>
<i>San Diego Gas &amp; Electric Company</i>	<i>California</i>
<i>Sempra Energy Financial</i>	<i>California</i>
<i>Sempra Energy Global Enterprises</i>	<i>California</i>
<i>Sempra Energy International</i>	<i>California</i>
<i>Sempra Energy Resources</i>	<i>California</i>
<i>Sempra Energy Trading Corp.</i>	<i>Delaware</i>
<i>Sempra Metals Group Limited</i>	<i>United Kingdom</i>
<i>Sodigas Pampeana S.A.</i>	<i>Argentina</i>
<i>Sodigas Sur S.A.</i>	<i>Argentina</i>
<i>Southern California Gas Company</i>	<i>California</i>

Statement of Chief Executive Officer

Pursuant to 18 U.S.C. Sec 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned Chief Executive Officer of Sempra Energy (the "Company") certifies that:

(i) the Annual Report on Form 10-K of the Company filed with the Securities and Exchange Commission for the year ended December 31, 2004 (the "Annual Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and

(ii) the information contained in the Annual Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

February 23, 2005

/s/ STEPHEN L. BAUM

\_\_\_\_\_  
Stephen L. Baum  
Chief Executive Officer

Statement of Chief Financial Officer

Pursuant to 18 U.S.C. Sec 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned Chief Financial Officer of Sempra Energy (the "Company") certifies that:

(i) the Annual Report on Form 10-K of the Company filed with the Securities and Exchange Commission for the year ended December 31, 2004 (the "Annual Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and

(ii) the information contained in the Annual Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

February 23, 2005

/s/ NEAL E. SCHMALE

\_\_\_\_\_  
Neal E. Schmale  
Chief Financial Officer



I, Stephen L. Baum, certify that:

1. I have reviewed this Annual Report on Form 10-K of Sempra Energy;
2. Based on my knowledge, this Annual Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Annual Report;
3. Based on my knowledge, the financial statements and other financial information included in this Annual Report fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this Annual Report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 15(f) and 15d-15(f)) for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Annual Report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this Annual Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this Annual Report, based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

February 23, 2005

/S/ STEPHEN L. BAUM  
Stephen L. Baum  
Chief Executive Officer

I, Neal E. Schmale, certify that:

1. I have reviewed this Annual Report on Form 10-K of Sempra Energy;
2. Based on my knowledge, this Annual Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Annual Report;
3. Based on my knowledge, the financial statements and other financial information included in this Annual Report fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this Annual Report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 15(f) and 15d-15(f)) for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Annual Report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this Annual Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this Annual Report, based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

February 23, 2005

/S/ NEAL E. SCHMALE  
Neal E. Schmale  
Chief Financial Officer