

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

June 30, 1995

For the quarterly period ended.....  
Or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-3779

SAN DIEGO GAS & ELECTRIC COMPANY

(Exact name of registrant as specified in its charter)

CALIFORNIA 95-1184800  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

101 ASH STREET, SAN DIEGO, CALIFORNIA 92101  
(Address of principal executive offices) (Zip Code)

(619) 696-2000

Registrant's telephone number, including area code.....

No Change

Former name, former address and former fiscal year, if changed since last report

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

116,538,035

Common Stock outstanding July 31, 1995 .....

PART I - FINANCIAL INFORMATION  
SAN DIEGO GAS & ELECTRIC COMPANY  
STATEMENTS OF CONSOLIDATED INCOME  
(In thousands except per share amounts)

	Three Months Ended June 30,	
	1995	1994
	(Unaudited)	
Operating Revenues		
Electric	\$ 354,716	\$ 352,013
Gas	76,745	78,260
Diversified operations	13,778	13,777
Total operating revenues	445,239	444,050
Operating Expenses		
Electric fuel	20,481	33,490
Purchased power	84,937	81,442
Gas purchased for resale	28,477	31,071
Maintenance	17,425	16,209
Depreciation and decommissioning	68,027	65,008
Property and other taxes	11,191	11,119
General and administrative	44,630	61,762
Other	52,547	50,481
Income taxes	38,036	29,659
Total operating expenses	365,751	380,241
Operating Income	79,488	63,809
Other Income and (Deductions)		

Writedown of real estate . . . . .	-	(25,000)
Allowance for equity funds used during construction . . . . .	1,453	2,155
Taxes on nonoperating income . . . . .	1,398	10,038
Other - net . . . . .	(3,350)	(1,072)
	-----	-----
Total other income and (deductions)	(499)	(13,879)
	-----	-----
Income Before Interest Charges . . . . .	78,989	49,930
	-----	-----
Interest Charges		
Long-term debt . . . . .	25,355	22,782
Short-term debt and other . . . . .	4,411	3,406
Allowance for borrowed funds used during construction . . . . .	(671)	(1,064)
	-----	-----
Net interest charges . . . . .	29,095	25,124
	-----	-----
Income from Continuing Operations . . . . .	49,894	24,806
Discontinued Operations, Net of Income Taxes . . . . .	(678)	(58,025)
	-----	-----
Net Income (Loss) (before preferred dividend requirements) . . . . .	49,216	(33,219)
Preferred Dividend Requirements . . . . .	1,915	1,915
	-----	-----
Earnings (Loss) Applicable to Common Shares . . . . .	\$ 47,301	\$ (35,134)
	=====	=====
Average Common Shares Outstanding . . . . .	116,534	116,473
	=====	=====
Earnings Per Common Share - Continuing Operations . . . . .	\$ 0.41	\$ 0.20
	=====	=====
Earnings (Loss) Per Common Share . . . . .	\$ 0.41	\$ (0.30)
	=====	=====
Dividends Declared Per Common Share . . . . .	\$ 0.39	\$ 0.38
	=====	=====

See notes to consolidated financial statements.

PART I - FINANCIAL INFORMATION  
SAN DIEGO GAS & ELECTRIC COMPANY  
STATEMENTS OF CONSOLIDATED INCOME  
(In thousands except per share amounts)

	Six Months Ended June 30,	
	1995	1994
	----- (Unaudited) -----	
Operating Revenues		
Electric . . . . .	\$ 734,004	\$ 727,917
Gas . . . . .	161,323	177,110
Diversified operations . . . . .	27,867	27,002
	-----	-----
Total operating revenues . . . . .	923,194	932,029
	-----	-----
Operating Expenses		
Electric fuel . . . . .	44,329	68,366
Purchased power . . . . .	171,201	162,967
Gas purchased for resale . . . . .	63,142	80,745
Maintenance . . . . .	36,708	32,570
Depreciation and decommissioning . . . . .	135,845	129,067
Property and other taxes . . . . .	22,679	22,496
General and administrative . . . . .	85,587	107,023
Other . . . . .	104,483	102,726
Income taxes . . . . .	86,077	78,178
	-----	-----
Total operating expenses . . . . .	750,051	784,138
	-----	-----
Operating Income . . . . .	173,143	147,891
	-----	-----
Other Income and (Deductions)		
Writedown of real estate . . . . .	-	(25,000)
Allowance for equity funds used during construction . . . . .	3,013	4,840
Taxes on nonoperating income . . . . .	1,177	9,502
Other - net . . . . .	(2,945)	(341)
	-----	-----
Total other income and (deductions)	1,245	(10,999)
	-----	-----
Income Before Interest Charges . . . . .	174,388	136,892
	-----	-----
Interest Charges		
Long-term debt . . . . .	49,646	45,290
Short-term debt and other . . . . .	8,891	6,252
Allowance for borrowed funds used during construction . . . . .	(1,383)	(2,238)
	-----	-----
Net interest charges . . . . .	57,154	49,304
	-----	-----
Income from Continuing Operations	117,234	87,588
Discontinued Operations, Net of Income Taxes . . . . .	(6,168)	(61,011)
	-----	-----
Net Income (before preferred dividend requirements) . . . . .	111,066	26,577
Preferred Dividend Requirements . . . . .	3,831	3,831
	-----	-----
Earnings Applicable to Common Shares . . . . .	\$ 107,235	\$ 22,746
	=====	=====
Average Common Shares Outstanding . . . . .	116,533	116,482
	=====	=====
Earnings Per Common Share - Continuing Operations . . . . .	\$ 0.97	\$ 0.72
	=====	=====
Earnings Per Common Share . . . . .	\$ 0.92	\$ 0.20
	=====	=====
Dividends Declared Per Common Share . . . . .	\$ 0.78	\$ 0.76
	=====	=====

See notes to consolidated financial statements.

SAN DIEGO GAS & ELECTRIC COMPANY  
CONSOLIDATED BALANCE SHEETS  
(In thousands of dollars)

	June 30, 1995	December 31, 1994
	-----	-----
	(Unaudited)	
<b>ASSETS</b>		
Utility plant - at original cost . . . . .	\$5,406,667	\$5,329,179
Accumulated depreciation and decommissioning . .	(2,299,220)	(2,180,087)
	-----	-----
Utility plant-net . . . . .	3,107,447	3,149,092
	-----	-----
Investments and other property . . . . .	502,429	465,918
	-----	-----
<b>Current assets</b>		
Cash and temporary investments . . . . .	52,629	25,405
Funds held for debt retirement . . . . .	74,632	-
Accounts receivable . . . . .	160,948	187,988
Notes receivable . . . . .	33,194	31,806
Inventories . . . . .	78,382	75,607
Other . . . . .	35,957	34,022
	-----	-----
Total current assets . . . . .	435,742	354,828
	-----	-----
Deferred taxes recoverable in rates . . . . .	290,535	305,717
	-----	-----
Deferred charges and other assets . . . . .	334,418	322,881
	-----	-----
Total . . . . .	\$4,670,571	\$4,598,436
	=====	=====
<b>CAPITALIZATION AND LIABILITIES</b>		
<b>Capitalization</b>		
Common equity . . . . .	\$1,490,719	\$1,474,430
Preferred stock:		
Not subject to mandatory redemption . . . . .	93,493	93,493
Subject to mandatory redemption . . . . .	25,000	25,000
Long-term debt . . . . .	1,381,086	1,339,201
	-----	-----
Total capitalization . . . . .	2,990,298	2,932,124
	-----	-----
<b>Current liabilities</b>		
Short-term borrowings . . . . .	-	89,325
Long-term debt redeemable within one year . .	189,350	115,000
Current portion of long-term debt . . . . .	45,115	35,031
Accounts payable . . . . .	86,878	130,157
Dividends payable . . . . .	47,364	46,200
Taxes accrued . . . . .	45,442	5,519
Interest accrued . . . . .	21,115	23,372
Regulatory balancing accounts		
overcollected-net. . . . .	122,742	111,731
Other . . . . .	113,866	113,815
	-----	-----
Total current liabilities . . . . .	671,872	670,150
	-----	-----
Customer advances for construction . . . . .	34,549	36,250
	-----	-----
Accumulated deferred income taxes-net . . . . .	501,898	513,592
	-----	-----
Accumulated deferred investment tax credits . .	106,507	109,161
	-----	-----
Deferred credits and other liabilities . . . . .	365,447	337,159
	-----	-----
Total . . . . .	\$4,670,571	\$4,598,436
	=====	=====

See notes to consolidated financial statements.

SAN DIEGO GAS & ELECTRIC COMPANY  
 STATEMENTS OF CONSOLIDATED CASH FLOWS  
 (In thousands of dollars)

	Six Months Ended	
	June 30,	
	1995	1994
	-----	-----
	(Unaudited)	
Cash Flows from Operating Activities		
Income from Continuing Operations . . . . .	\$117,234	\$ 87,588
Adjustments to reconcile income from continuing operations to net cash provided by operating activities		
Writedown of real estate and other assets . . . . .	--	37,000
Depreciation and decommissioning . . . . .	135,845	129,067
Amortization of deferred charges and other assets . . . . .	6,392	6,704
Amortization of deferred credits and other liabilities . . . . .	(16,147)	(16,149)
Allowance for equity funds used during construction . . . . .	(3,013)	(4,840)
Deferred income taxes and investment tax credits . . . . .	(4,511)	(16,074)
Other-net . . . . .	19,811	27,925
Changes in working capital components		
Accounts and notes receivable . . . . .	25,652	15,950
Regulatory balancing accounts . . . . .	11,011	6,507
Inventories . . . . .	(2,775)	(9,864)
Other current assets . . . . .	(1,935)	333
Accrued interest and taxes . . . . .	36,623	31,679
Accounts payable and other current liabilities . . . . .	(43,228)	(42,113)
Cash flows provided (used) by discontinued operations . . . . .	(168)	4,873
	-----	-----
Net cash provided by operating activities . . . . .	280,791	258,586
	-----	-----
Cash Flows from Financing Activities		
Dividends paid . . . . .	(93,563)	(91,140)
Short-term borrowings-net . . . . .	(89,325)	(47,197)
Issuance of long-term debt . . . . .	124,641	--
Repayment of long-term debt . . . . .	(26,063)	(16,029)
Funds held for debt retirement . . . . .	(74,632)	--
Redemption of common stock . . . . .	(50)	(938)
	-----	-----
Net cash used by financing activities . . . . .	(158,992)	(155,304)
	-----	-----
Cash Flows from Investing Activities		
Utility construction expenditures . . . . .	(91,225)	(134,690)
Withdrawals from construction trust funds . . . . .	--	58,042
Contributions to decommissioning funds . . . . .	(11,016)	(11,016)
Other-net . . . . .	2,544	(1,925)
Discontinued operations . . . . .	5,122	(15,391)
	-----	-----
Net cash used by investing activities . . . . .	(94,575)	(104,980)
	-----	-----
Net increase (decrease) . . . . .	27,224	(1,698)
Cash and temporary investments, beginning of period . . . . .	25,405	12,711
	-----	-----
Cash and temporary investments, end of period . . . . .	\$ 52,629	\$ 11,013
	=====	=====
Supplemental Disclosure of Cash Flow Information		
Income tax payments . . . . .	\$ 47,240	\$ 39,041
	=====	=====
Interest payments, net of amounts capitalized . . . . .	\$ 59,411	\$ 49,756
	=====	=====
Supplemental Schedule of Noncash Investing and Financing Activities		
Real estate investments . . . . .	\$ 25,303	\$ 5,586
Cash paid . . . . .	(250)	(52)
	-----	-----
Liabilities assumed . . . . .	\$ 25,053	\$ 5,534
	=====	=====

See notes to consolidated financial statements.

1. GENERAL

SDG&E believes all adjustments necessary to present a fair statement of the consolidated financial position and results of operations for the periods covered by this report, consisting of recurring accruals, have been made. Certain prior year amounts have been reclassified for comparability.

SDG&E's significant accounting policies are described in the notes to consolidated financial statements in its 1994 Annual Report to Shareholders. SDG&E follows the same accounting policies for interim reporting purposes.

This report should be read in conjunction with SDG&E's 1994 Annual Report on Form 10-K and its Quarterly Report on Form 10-Q for the three months ended March 31, 1995. The consolidated financial statements and Management's Discussion & Analysis of Financial Condition and Results of Operations included in SDG&E's 1994 Annual Report to Shareholders were incorporated by reference into SDG&E's 1994 Annual Report on Form 10-K and filed as an exhibit thereto.

2. MATERIAL CONTINGENCIES

INDUSTRY RESTRUCTURING - CALIFORNIA PUBLIC UTILITIES  
COMMISSION

On May 24, 1995 the CPUC voted 3-1 approving a tentative plan for restructuring California's electric industry with a wholesale power pool to begin by January 1997. The plan would allow the state's investor-owned utilities to remain in the business of owning and operating power plants for utility-owned generation. The pool, operated by an independent party, would provide for economic dispatch of competing generation facilities based on spot-market clearing prices similar to a commodities market. After two years, if jurisdictional and market power issues are resolved and transition cost recovery mechanisms are in place, retail consumers would be able to buy electricity directly from specific generators. The dissenting commissioner presented an alternative plan calling for direct power sales to all customers, including residential customers, by 1997.

The proposed majority plan supports the continued development of performance-based ratemaking. In addition, the CPUC stated that it is committed to industry restructuring in a manner that "...does not compromise the financial integrity of the utilities and continues to provide them with a reasonable opportunity to earn a fair profit..." Additional hearings will be held prior to the issuance of the CPUC's final policy decision. The CPUC's timetable provides that its policy decision will be issued no sooner than August 23, 1995 and become effective no sooner than 100 days after the issuance of its final decision. SDG&E and the CPUC believe that no state or federal laws need to be changed in order for the CPUC's proposal to go forward, although the California legislature does not agree. The California legislature is currently reviewing the CPUC's proposal and plans to hold hearings commencing in August 1995. On July 24, 1995 SDG&E filed comments in support of the CPUC's majority plan.

At June 30, 1995 SDG&E had approximately \$960 million of net utility plant (including approximately \$750 million of nuclear facilities) and \$60 million of deferred taxes and regulatory assets (included in "Deferred Charges and Other Assets" on the Consolidated Balance Sheets) relating to generating facilities currently being recovered in rates over various periods of time. In addition, SDG&E has long-term purchased-power commitments totaling \$3.9 billion with various utilities and other providers. Further, the CPUC's recent Biennial Resource Plan Update decision requires SDG&E to contract for an additional 500 megawatts of power over 17 to 30-year terms at an estimated cost of \$4.8 billion beginning in 1997. Prices under these contracts are estimated to exceed future market prices by \$500 million. SDG&E challenged the decision and petitioned the Federal Energy Regulatory Commission to overrule it. In February 1995 the FERC ruled favorably on SDG&E's petition. However, the CPUC and others are unwilling to accept the FERC decision as either appropriate or final. See additional discussion of the BRPU proceeding in Management's Discussion and Analysis of Financial Condition and Results of Operations.



If the CPUC proceeds with the move to a more competitive environment, if the prices of competing suppliers are as anticipated, and if the regulatory process does not provide for complete recovery of those costs that are in excess of what will otherwise be recoverable via market-based pricing structures, SDG&E would incur a charge against earnings for a significant portion of its generating facilities, the related regulatory assets and the long-term commitments. However, the CPUC has indicated that any otherwise unrecovered amounts will be provided for in the new environment. SDG&E cannot at this time predict the impact of the CPUC's tentative decision and the transition to a more competitive environment on SDG&E's financial condition and results of operations.

SDG&E believes that changes in the California utility industry and the movement toward a more competitive marketplace will require SDG&E to change its corporate structure. SDG&E is presently considering various strategies for the separation of its power generation and transmission assets from its other utility assets, much of which is dependent on the outcome of the CPUC industry restructuring proceedings and the FERC wholesale open access rule-making proceedings (see below). In connection with the proposed industry restructuring, SDG&E has applied to the CPUC for permission to form a holding company. A holding company structure would, among other things, provide a platform for the separation of SDG&E's generation and transmission assets. The CPUC's Division of Ratepayer Advocates has recommended against approval of the holding company or, in the alternative, that approval include several conditions, some of which are onerous. To date, the holding company proposal has been approved by the FERC, the Nuclear Regulatory Commission and SDG&E shareholders. SDG&E anticipates forming the holding company shortly after receiving final approval from the CPUC, whose decision is expected in the fourth quarter of 1995. See additional discussion concerning the holding company application in Management's Discussion and Analysis of Financial Condition and Results of Operations.

#### INDUSTRY RESTRUCTURING - FEDERAL ENERGY REGULATORY COMMISSION

On March 29, 1995 the FERC issued a proposed rule that if, adopted, would require all public utilities to offer wholesale "open access" transmission service on a nondiscriminatory basis. In addition, public utilities would be required to functionally unbundle their generation and transmission services, i.e. pricing them separately from each other. The FERC also stated its belief that, in this more competitive period, utilities should be allowed to recover the costs of assets and obligations made uneconomic by the changed regulatory environment. Although SDG&E's cost recovery mechanisms are not currently under the jurisdiction of the FERC, the recognition by the FERC of the propriety of such cost recovery supports the CPUC's similar position, as stated in its tentative decision (see above).

On August 3, 1995 SDG&E filed its initial comments endorsing the FERC's proposed rulemaking. SDG&E committed to filing at the FERC during early 1996 its open access tariffs. Approval of the tariffs of SDG&E and the other participating utilities, and final approval of the CPUC's industry restructuring plan would result in the creation of a bid-based wholesale electricity spot market with open-access transmission. Participating utilities would transfer complete operating control over their transmission assets to an independent system operator, which would be responsible for directing the operation of the transmission system. At least at the outset, retail customers would not participate directly as buyers in the wholesale market. SDG&E has also proposed a single entity that would ultimately own and/or lease the transmission facilities within a broad geographic area. The creation of such an entity could involve the sale, lease or other disposition of SDG&E's transmission facilities. Reply comments will be filed this fall. A final rule is expected during early 1996.



SAN ONOFRE NUCLEAR GENERATING STATION UNITS 2 & 3

In November 1994 SDG&E, Southern California Edison and the CPUC's Division of Ratepayer Advocates signed a settlement agreement on the accelerated recovery of SONGS Units 2 and 3 capital costs. It is anticipated that the rates in the agreement would be sufficient for SDG&E to recover approximately \$750 million over an eight-year period beginning in February 1996, rather than over the anticipated operational life of the units, which may extend to 2013. During the eight-year period, the authorized rate of return would be reduced from the authorized weighted average cost of capital (currently 9.76 percent) to 7.52 percent (SDG&E's 1995 authorized cost of debt). The agreement also includes a performance incentive plan that would encourage continued, efficient operation of the plant. However, continued operation of SONGS beyond the eight-year period would be at the owners' discretion. Under the plan, customers would pay about four cents per kilowatt-hour for energy delivered from SONGS during the eight-year period. This pricing plan would replace the traditional method of recovering the units' operating expenses and capital improvements. This is intended to make the plants more competitive with other sources. SDG&E is unable at this time to predict the impact of this proposal, if approved, on the results of its operations. Hearings were concluded in May 1995. A CPUC decision is expected in the fourth quarter of 1995.

NUCLEAR INSURANCE

Public liability claims that could arise from a nuclear incident are limited by law to \$9 billion for each licensed nuclear facility. For this exposure, SDG&E and the co-owners of SONGS have purchased primary insurance of \$200 million, the maximum amount available. The remaining coverage is provided by secondary financial protection required by the Nuclear Regulatory Commission and provides for loss sharing among utilities owning nuclear reactors if a costly accident occurs. SDG&E could be assessed retrospective premium adjustments of up to \$32 million in the event of a nuclear incident involving any of the licensed, commercial reactors in the United States, if the amount of the loss exceeds \$200 million.

Insurance coverage is also provided for up to \$2.8 billion of property damage and decontamination liability, and the cost of replacement power, which includes indemnity payments for up to two years, after a waiting period of 21 weeks. Coverage is provided primarily through mutual insurance companies owned by utilities with nuclear facilities. If losses at any of the nuclear facilities covered by the risk-sharing arrangements were to exceed the accumulated funds available for these insurance programs, SDG&E could be assessed retrospective premium adjustments of up to \$9 million.

3. WRITEDOWNS

In June 1994 SDG&E recorded writedowns related to the utility and its subsidiaries. SDG&E recorded a \$25 million writedown of various commercial properties, including \$19 million of subsidiary properties in Colorado Springs and in San Diego, to reflect continuing declines in commercial real estate values. As a result of the California Public Utilities Commission's proposal to restructure the electric utility industry and the uncertainty concerning the impact of competition, SDG&E also recorded a \$12 million writedown of various non-earning utility assets, including the South Bay Repower project. Additional writedowns associated with discontinued operations are described in Note 4. Additional information on the CPUC's proposed industry restructuring and its potential impacts on SDG&E is provided in Note 2.

SAN DIEGO GAS & ELECTRIC COMPANY  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

4. DISCONTINUED OPERATIONS -- WAHLCO ENVIRONMENTAL SYSTEMS, INC.

On June 6, 1995 SDG&E sold its investment in Wahlco Environmental Systems, Inc. for \$5 million. The sale of Wahlco is being accounted for as a disposal of a segment of business and SDG&E's prior periods' financial statements have been restated to reflect Wahlco as a discontinued operation. Discontinued operations consist of the following:

			Six Months Ended June 30,		Year Ended December 31,		
	1995	1994	1995	1994	1994	1993	1992
			(millions of dollars)				
Revenues	\$24	\$35	\$70	\$82	\$82		
Loss from operations before income taxes	--	(64)	(70)	(14)	(13)		
Loss on disposal before income taxes		(10)	--	--	--	--	--
Income tax benefits	4	3	7	5	3		

The loss on disposal of Wahlco was recorded in 1995 and includes the writedown of SDG&E's investment in Wahlco in March 1995 to reflect Wahlco's estimated realizable value under a proposed agreement (subsequently terminated) with a potential buyer (see Note 2 of the notes to financial statements in SDG&E's Quarterly Report on Form 10-Q for the quarter ended March 31, 1995) and Wahlco's net operating losses after 1994. The loss from discontinued operations for the six months ended June 30, 1994 was primarily due to the \$59 million writedown of Wahlco's goodwill and other intangible assets as a result of the depressed air pollution-control market and increasing competition.

Wahlco's net assets (included in "Investments and Other Property" on the Consolidated Balance Sheets) at December 31, 1994 are summarized as follows:

Current assets	\$ 40.2	
Non-current assets		18.9
Current liabilities		(27.1)
Long-term debt and other liabilities		(24.2)
	-----	
	=====	\$ 7.8

ITEM 2.  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS:

EARNINGS

Earnings per share from continuing operations for the three months ended June 30, 1995 were \$0.41, up from \$0.20 per share during the same period in 1994. Earnings per share from continuing operations for the six months ended June 30, 1995 were \$0.97, up from \$0.72 per share during the same period in 1994. The changes in earnings result primarily from a \$0.20 per share June 1994 writedown associated with utility and real estate assets. Additional information concerning the writedowns is provided in Note 3 of the notes to consolidated financial statements.

OPERATING REVENUES AND EXPENSES

Gas revenues, gas purchased for resale, and electric fuel expense decreased for the six months ended June 30, 1995 from the corresponding period in 1994 primarily due to lower natural gas prices. Purchased power expense for the six months ended June 30, 1995 was up over the corresponding 1994 period, primarily due to increased purchases of short-term energy to replace lower-cost nuclear generation as a result of the scheduled refueling of San Onofre Nuclear Generating Station Unit 2.

General and administrative expenses decreased for the six months ended June 30, 1995 compared with 1994 primarily due to the June 1994 writedowns of various non-earning utility assets described in Note 3 of the notes to consolidated financial statements.

REGULATORY MATTERS:

CALIFORNIA PUBLIC UTILITIES COMMISSION'S PROPOSED INDUSTRY  
RESTRUCTURING

On May 24, 1995 the CPUC voted 3-1 approving a tentative plan for restructuring California's electric industry with a wholesale power pool to begin by January 1997. See additional discussion of industry restructuring in Note 2 of the notes to consolidated financial statements. SDG&E cannot at this time predict the impact of the CPUC's final decision and the transition to a more competitive environment on SDG&E's financial condition and results of operations.

HOLDING COMPANY

In November 1994 SDG&E filed an application with the CPUC to form a holding company. Under the proposed structure, SDG&E would become a subsidiary of the parent company, as would SDG&E's existing subsidiaries. A CPUC decision on SDG&E's application is expected in the fourth quarter of 1995. To date, the holding company proposal has been approved by the FERC, the Nuclear Regulatory Commission and SDG&E shareholders. See additional discussion of industry restructuring and the proposed holding company plan in Note 2 of the notes to consolidated financial statements.

BIENNIAL RESOURCE PLAN UPDATE PROCEEDING

In December 1994 the CPUC issued a decision ordering SDG&E, Pacific Gas & Electric and Southern California Edison to proceed with the BRPU auction. SDG&E was ordered to begin negotiating contracts (ranging from 17 to 30 years) to purchase 500 mw of power from qualifying facilities at an estimated cost of \$4.8 billion beginning in 1997. SDG&E contended that prices for BRPU energy would be significantly higher than market prices. When the CPUC was not responsive, SDG&E petitioned the FERC, claiming the BRPU auction was illegal under the Public Utility Regulatory Policies Act of 1978. The FERC's February 1995 order declared the BRPU auction procedures unlawful.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

On June 21, 1995 the CPUC discussed the FERC's decision, but was unwilling to accept the FERC decision as either appropriate or final. The CPUC concluded that SDG&E, PG&E and Edison should attempt to reach settlements with the auction winners and reminded the utilities that contract buyouts should be reasonable and should not overlook the ratepayers' interests. The Assigned Commissioner Ruling issued on July 6, 1995 encourages settlement and reiterates what was discussed on June 21. No deadline was established for the completion of negotiations, although the utilities are required to provide the CPUC with monthly status reports summarizing negotiations.

GAS RATES

On July 19, 1995 the CPUC issued its decision on SDG&E's June 1995 application to lower core gas rates by \$16.4 million, effective August 1, 1995. This decrease is based on the decline in gas prices to levels below the Biennial Cost Allocation Proceeding's price forecast that became effective January 1, 1995. The decrease lowers the gas portion of a typical residential SDG&E natural gas bill by \$1.60 per month or 6.5 percent.

COST OF CAPITAL

On July 31, 1995 the CPUC's Division of Ratepayer Advocates issued its report on the 1996 Cost of Capital proceeding. The DRA is recommending a return on equity for SDG&E of 11.10 percent for an overall rate of return of 9.21 percent. SDG&E has requested an increase in its return on equity from 1995's 12.05 percent to 12.25 percent for 1996 and an increase in its overall rate of return from 9.76 percent authorized to 9.83 percent. A CPUC decision is expected in late 1995 with any authorized changes effective January 1, 1996.

LIQUIDITY AND CAPITAL RESOURCES:

Sources of cash for 1995 through 1999 are expected to consist of income from operations and issuances of stock and debt. Cash requirements for 1995 through 1999 include the construction program and retirements of long-term debt. SDG&E conducts a continuing review of its construction, investment and financing programs. They are revised in response to changes in competition, customer growth, inflation, customer rates, the cost of capital, and environmental and regulatory requirements.

FINANCING ACTIVITIES

SDG&E anticipates that it will continue to have short-term and intermediate-term borrowings in 1995. At December 31, 1994 SDG&E had various short-term bank lines aggregating \$170 million and two \$50 million long-term bank lines, related to which \$58 million in short-term bank loans was outstanding. During June 1995 SDG&E renegotiated the terms of these bank lines. At June 30, 1995 SDG&E had short-term bank lines of \$30 million (none outstanding) and long-term bank lines of \$280 million (\$50 million outstanding). Commitment fees are paid on the unused portion of the lines; there are no requirements for compensating balances.

SDG&E does not expect any issuances of long-term debt or preferred stock in 1995 other than refinancings. On June 6, 1995 SDG&E issued \$74 million of Industrial Development Bonds through the City of San Diego to refinance the 9-1/4 percent bonds issued in 1985. The new bonds were issued at par, due September 1, 2020. The interest rates are variable, ranging from 3.05 percent to 3.40 percent on the tax-exempt segments and 5.95 percent to 5.97 percent on the federally taxable segments. The proceeds were placed in an escrow fund to be used to call the 1985 bonds on September 1, 1995.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

SDG&E periodically enters into interest rate swap and cap agreements to moderate its exposure to interest rate changes and to lower its overall cost of borrowing. These swap and cap agreements generally remain off the balance sheet as they involve the exchange of fixed- and variable-rate interest payments without the exchange of the underlying principal amounts. The related gains or losses are reflected in the income statement as part of interest expense. SDG&E's policy is to use derivatives only as a hedge.

CAPITAL STRUCTURE

SDG&E maintains its utility capital structure so as to obtain long-term financing at the lowest possible rates. The following table lists key financial ratios for SDG&E's utility operations.

	1995	June 30, or the twelve	December 31, 1994 or the year months then ended	then ended
Pretax interest coverage	4.8 X		4.7 X	
Internal cash generation	112 %	85 %		
Construction expenditures as a percent of capitalization	7.6 %		9.1 %	
Capital structure:				
Common equity	48 %		48 %	
Preferred stock	4 %		4 %	
Debt and leases	48 %		48 %	

SDG&E's employee savings and common stock investment plans permit SDG&E to issue common stock or to purchase it on the open market. Currently, SDG&E is purchasing the stock on the open market for these plans.

CAPITAL REQUIREMENTS

Quarterly cash dividends of \$0.39 per share have been declared the first two quarters of 1995. The dividend pay-out ratio for the 12 months ended June 30, 1995 and December 31, 1994, 1993, 1992 and 1991 were 82%, 130%, 82%, 81% and 79%, respectively. The increase for the year ended December 31, 1994 was due to the writedowns recorded during 1994. Additional information regarding the writedowns is provided in Notes 3 and 4 of the notes to consolidated financial statements. The payment of future dividends is within the discretion of the SDG&E Board of Directors and dependent upon future business conditions, earnings and other factors. Net cash flows provided by operating activities currently are sufficient to maintain the payment of dividends at the present level.

Construction expenditures were \$264 million in 1994 and are expected to be approximately \$240 million in 1995. The level of expenditures in the next few years will depend on the CPUC's proposed industry restructuring (as described in "Regulatory Matters" above), the timing of expenditures to comply with air emission reduction and other environmental requirements, and SDG&E's proposal to transport natural gas to Mexico. (Additional information concerning SDG&E's proposal to transport gas to Mexico is provided in SDG&E's 1994 Annual Report.)

OTHER

Besides the effects of items discussed in the preceding pages, the only significant change in cash flows for the six months ended June 30, 1995 compared to the corresponding 1994 period was related to the change in utility accounts receivable due to varying levels of customer receivables attributable to differences in

MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

weather. In addition, besides the items discussed in the preceding pages, the only significant changes to the balance sheet at June 30, 1995 compared to December 31, 1994 were in accounts payable and taxes accrued. Accounts payable decreased due to lower expense accruals at June 30, 1995. The increase in taxes accrued was due to the timing of payments.

## PART II - OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

There have been no significant subsequent developments in the American Trails, Public Service Company of New Mexico and North City West proceedings. Background information concerning these and the following proceedings is contained in SDG&E's 1994 Annual Report on Form 10-K and in its March 31, 1995 Quarterly Report on Form 10-Q.

#### Century Power

On July 19, 1995 the Federal Energy Regulatory Commission dismissed SDG&E's request for a rehearing of the FERC's dismissal of SDG&E's February 11, 1993 audit complaint against Tucson and Century. SDG&E may appeal this decision. SDG&E is unable to predict the ultimate outcome of these proceedings.

#### Canadian Natural Gas

On July 17, 1995 the United States Federal District Court, Southern District of California, rejected motions by Summit and Canadian Hunter to dismiss SDG&E's complaint. However, the Court granted a separate motion of Summit on other grounds, and dismissed SDG&E's lawsuit against Summit only. SDG&E has thirty days to appeal this decision. SDG&E is unable to predict the ultimate outcome of these proceedings.

#### McCartin

Plaintiffs dismissed their appeal in exchange for SDG&E's waiver of its right to recover costs.

#### Covalt

The California Supreme Court granted the plaintiffs' request for review of the California Court of Appeal decision to dismiss the case. A decision is not expected until 1996. SDG&E is unable to predict the ultimate outcome of this proceeding.

#### SONGS Personal Injury Litigation

On July 7, 1995 Jason Mettler filed a complaint in the United States District Court for the Southern District of California against Southern California Edison, SDG&E, Combustion Engineering and the Institute of Nuclear Power Operations. The allegations in the complaint are substantially identical to those contained in the complaints of R. C. Tang, Glen James, and Linda McLandrich, described in SDG&E's 1993 and 1994 Annual Report on Form 10-K and its Quarterly Report on Form 10-Q for the three months ended March 31, 1995. Plaintiff Mettler died shortly thereafter and his complaint was converted into a wrongful-death lawsuit. The lawsuit alleges that Mettler's death was the result of the emission of radiation while he was an Edison nuclear equipment operator at SONGS between 1982 and 1990. Plaintiffs have asked for general compensatory damages. The Tang, James, McLandrich and Mettler complaints were all filed by the same attorneys. There have been no significant subsequent developments in the James or McLandrich cases. SDG&E is unable to predict the ultimate outcome of these proceedings.

#### Wood Poles Preservatives

On June 20, 1995 the Pacific Justice Center filed a complaint in San Francisco County Superior Court, against Pacific Bell, Pacific Gas & Electric and two wood-pole manufacturers claiming violations of the California Safe Drinking Water and Toxic Enforcement Act (Proposition 65) for failure to warn individuals who may be exposed to wood poles treated with wood preservatives, some of which are

PART II - OTHER INFORMATION

included on the list of chemicals known to cause cancer or reproductive harm. Proposition 65 requires that prior warning be given to individuals who may be exposed to such chemicals unless the exposure will not pose a significant risk. SDG&E believes, on the basis of studies and other information, that exposures to wood poles containing such preservatives do not give rise to a significant risk and that no warning is required. Violations of the Proposition 65 warning requirement can result in penalties of up to \$2,500 per violation. Although SDG&E and Southern California Edison were not named in this lawsuit, it is anticipated that the Pacific Justice Center, to the extent it prevails in the present lawsuit, will file a separate lawsuit against Edison and SDG&E on the same grounds. SDG&E is unable to predict the ultimate outcome of these proceedings.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

Exhibit 10 - Material Contracts

10.1 Amended 1986 Long-Term Incentive Plan, amended and restated effective April 25, 1995 (incorporated by reference from SDG&E's Amendment No. 2 to Form S-4 filed February 28, 1995).

10.2 Loan Agreement with the City of San Diego in connection with the issuance of \$16.7 million of Industrial Development Revenue Refunding Bonds, dated as of June 1, 1995.

10.3 Loan Agreement with the City of San Diego in connection with the issuance of \$57.7 million of Industrial Development Revenue Refunding Bonds, dated as of June 1, 1995.

10.4 Stock Purchase Agreement dated May 15, 1995 among WES Acquisition Corp., Pacific Diversified Capital Company and Wexford Capital Corporation, as indemnitor.

Exhibit 12 - Computation of Ratios

12.1 Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividends as required under SDG&E's August 1993 registration of 5,000,000 shares of Preference Stock (Cumulative).

Exhibit 27 - Financial Data Schedule

27.1 SDG&E Financial Data Schedule for the six months ended June 30, 1995.

(b) Reports on Form 8-K

A Current Report on Form 8-K was filed on May 30, 1995 announcing the electric industry restructuring proposal made by the California Public Utilities Commission; the appointment of David Kuzma as senior vice president and chief financial officer; and the retirement of Nad Peterson as senior vice president, general counsel and corporate secretary.

A Current Report on Form 8-K was filed on April 3, 1995 announcing negotiations of an agreement with an unrelated third party for an option to acquire from Pacific Diversified Capital Company (a subsidiary of SDG&E and an 81 percent owner of Wahlco) its investment in and receivables from Wahlco.



SIGNATURE

Pursuant to the requirement of the Securities Exchange Act of 1934, the registrant has duly caused this quarterly report to be signed on its behalf by the undersigned thereunto duly authorized.

SAN DIEGO GAS & ELECTRIC COMPANY  
(Registrant)

Date: August 7, 1995  
-----

By: /s/ F.H. Ault  
-----

(Signature)  
F. H. Ault  
Vice President and Controller

LOAN AGREEMENT

Between

THE CITY OF SAN DIEGO

And

SAN DIEGO GAS & ELECTRIC COMPANY

Dated as of June 1, 1995

Relating to

\$16,700,000

The City of San Diego  
Industrial Development Revenue Refunding Bonds  
(San Diego Gas & Electric Company)  
1995 Series C

LOAN AGREEMENT

TABLE OF CONTENTS

	Page
PARTIES. . . . .	1
PREAMBLES. . . . .	1
ARTICLE I	
DEFINITIONS	
SECTION 1.1. DEFINITION OF TERMS. . . . .	2
SECTION 1.2. NUMBER AND GENDER. . . . .	2
SECTION 1.3. ARTICLES, SECTIONS, ETC. . . . .	2
ARTICLE II	
REPRESENTATIONS	
SECTION 2.1. REPRESENTATIONS OF THE CITY. . . . .	2
SECTION 2.2. REPRESENTATIONS OF THE BORROWER. . . . .	3
ARTICLE III	
ISSUANCE OF THE BONDS; APPLICATION OF PROCEEDS	
SECTION 3.1. AGREEMENT TO ISSUE BONDS; APPLICATION OF BOND PROCEEDS . . . . .	4
SECTION 3.2. INVESTMENT OF MONEYS IN FUNDS. . . . .	5
SECTION 3.3. AMENDMENT OF DESCRIPTION OF THE PROJECT. . . . .	5
ARTICLE IV	
LOAN TO BORROWER; REPAYMENT PROVISIONS	
SECTION 4.1. LOAN TO BORROWER . . . . .	5
SECTION 4.2. REPAYMENT AND PAYMENT OF OTHER AMOUNTS PAYABLE . . . . .	5
SECTION 4.3. UNCONDITIONAL OBLIGATION . . . . .	7
SECTION 4.4. ASSIGNMENT OF CITY'S RIGHTS. . . . .	8
SECTION 4.5. AMOUNTS REMAINING IN FUNDS . . . . .	8
SECTION 4.6. CREDIT FACILITY . . . . .	9
ARTICLE V	
SPECIAL COVENANTS AND AGREEMENTS	
SECTION 5.1. RIGHT OF ACCESS TO THE PROJECT . . . . .	9
SECTION 5.2. THE BORROWER'S MAINTENANCE OF ITS EXISTENCE; ASSIGNMENTS. . . . .	9
SECTION 5.3. RECORDS AND FINANCIAL STATEMENTS OF BORROWER . . . . .	10

SECTION 5.4. MAINTENANCE AND REPAIR . . . . . 11  
SECTION 5.5. QUALIFICATION IN CALIFORNIA. . . . . 11  
SECTION 5.6. TAX EXEMPT STATUS OF BONDS . . . . . 11  
SECTION 5.7. NOTICE OF RATE PERIODS . . . . . 12  
SECTION 5.8. REMARKETING OF THE BONDS . . . . . 13  
SECTION 5.9. NOTICES TO TRUSTEE AND CITY. . . . . 14

ARTICLE VI

EVENTS OF DEFAULT AND REMEDIES

SECTION 6.1. EVENTS OF DEFAULT. . . . . 14  
SECTION 6.2. REMEDIES ON DEFAULT. . . . . 16  
SECTION 6.3. AGREEMENT TO PAY ATTORNEYS' FEES AND EXPENSES. . 18  
SECTION 6.4. NO REMEDY EXCLUSIVE. . . . . 18  
SECTION 6.5. NO ADDITIONAL WAIVER IMPLIED BY ONE WAIVER . . . 18

ARTICLE VII

PREPAYMENT

SECTION 7.1. REDEMPTION OF BONDS WITH PREPAYMENT MONEYS . . . 18  
SECTION 7.2. OPTIONS TO PREPAY INSTALLMENTS . . . . . 18  
SECTION 7.3. MANDATORY PREPAYMENT . . . . . 19  
SECTION 7.4. AMOUNT OF PREPAYMENT . . . . . 19  
SECTION 7.5. NOTICE OF PREPAYMENT . . . . . 19

ARTICLE VIII

NON-LIABILITY OF CITY; EXPENSES; INDEMNIFICATION

SECTION 8.1. NON-LIABILITY OF CITY. . . . . 20  
SECTION 8.2. EXPENSES . . . . . 20  
SECTION 8.3. INDEMNIFICATION. . . . . 21

ARTICLE IX

MISCELLANEOUS

SECTION 9.1. NOTICES. . . . . 22  
SECTION 9.2. SEVERABILITY . . . . . 22  
SECTION 9.3. EXECUTION OF COUNTERPARTS. . . . . 22  
SECTION 9.4. AMENDMENTS, CHANGES AND MODIFICATIONS. . . . . 23  
SECTION 9.5. GOVERNING LAW. . . . . 23  
SECTION 9.6. AUTHORIZED BORROWER REPRESENTATIVE . . . . . 23  
SECTION 9.7. TERM OF THE AGREEMENT. . . . . 23  
SECTION 9.8. BINDING EFFECT . . . . . 23

TESTIMONIUM. . . . . 25  
SIGNATURES AND SEALS . . . . . 25  
EXHIBIT A Description of the Project . . . . .A-1

LOAN AGREEMENT

THIS LOAN AGREEMENT, dated as of June 1, 1995, by and between THE CITY OF SAN DIEGO, a municipal corporation and charter city duly organized and existing under the laws and Constitution of the State of California (the "City"), and SAN DIEGO GAS & ELECTRIC COMPANY, a corporation organized and existing under the laws of the State of California (the "Borrower"),

W I T N E S S E T H :

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 2 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 2 of the Charter, has enacted the City of San Diego Economic Development Revenue Bond Law, comprising Article 7 of Chapter IX of the San Diego Municipal Code, pursuant to Ordinance No. 0-15586 (New Series), adopted on September 14, 1981, 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 requested that the City assist in the refunding or replacement of certain outstanding bonds previously issued by the City (the "Prior Bonds") to provide the Borrower with financial assistance to acquire, construct and install certain facilities for the local furnishing of electric energy and gas (the "1985 Project"); and

WHEREAS, the City after due investigation and deliberation has adopted its ordinance authorizing the issuance of The City of San Diego Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 1995 Series C (the "Bonds") to refund and redeem a portion of the Prior Bonds; and

WHEREAS, the City proposes to assist in refinancing the portion of the 1985 Project which constitutes facilities for the local furnishing of gas (the "Project") 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 Bank of America National Trust and Savings Association, as Trustee (the "Trustee"), as originally executed or as it may from time to time be supplemented or amended as provided therein.

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 Project constitutes a "facility" 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 Project, 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 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 Project 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 August 3, 1992, the City Council of the City adopted Ordinance No. 0-17813 (New Series), and on March 29, 1993, the City Council adopted Ordinance No. 0-17903 (New Series) authorizing the issuance of the Bonds, and on May 1, 1995, the City Council adopted Resolution No. R-285683, authorizing 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, the Mortgage Bonds and all other documents contemplated hereby to be executed by the Borrower.

(b) Neither the execution and delivery of this Agreement or the Mortgage Bonds, the consummation of the transactions contemplated hereby, 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 Project consists and will consist of those facilities described in Exhibit A hereto, and the Borrower shall make no changes to such portion of the Project or to the operation thereof which would affect the qualification of the Project as a "facility" under the Law or, subject to Section 5.6(d) hereof, impair the exemption from gross income of the interest on the Bonds for federal income tax purposes. In particular, the Borrower shall comply with all requirements of the San Diego Gas & Electric Company Engineering and Financial Certificate, dated the Issue Date (the "Engineering Certificate"), which is hereby incorporated by reference herein. The Project consists of facilities for the local furnishing of gas as described in the Engineering Certificate. Subject to Section 5.6(d) hereof, the Borrower intends to utilize such portion of the Project as facilities for the local furnishing of gas throughout the foreseeable future.

(d) The Borrower has and will have title to the Project sufficient to carry out the purposes of this Agreement.

(e) The economic useful life of the Project is as set forth in the Engineering Certificate.

(f) All certificates, approvals, permits and authorizations with respect to the construction of the Project 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 Project 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 refinance a portion of the cost of the Project, 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 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 PROJECT. In the event that the Borrower desires to amend or supplement the Project, as described in Exhibit A hereto, and the City 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 Project 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 a portion of the Prior Bonds and the first mortgage bonds of the Borrower relating thereto 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. To evidence, secure and provide for the repayment of the loan made hereunder, the Borrower hereby and concurrently herewith delivers to the Trustee its Mortgage Bonds, of like principal amount, maturity date, interest rates and redemption provisions as the Bonds. In addition, the Borrower agrees to make the payments required by subsection (a) (to the extent such payments are not timely provided for by the payment of principal

of and interest on the Mortgage Bonds) through (d) of this Section as Repayment Installments on such loan.

(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 pursuant to the Mortgage Bonds, together with any other payments 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 of (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.

(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 private placement agreement executed by it in connection with the sale of the Bonds, and all expenses of the City related to the financing of the Project which are not otherwise required to be paid by the Borrower under the terms of this Agreement; 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 (i) on or before the Issue Date an origination fee for the Bonds in the amount of \$41,750 and (ii) annually in arrears on September 1 of each year during which any Bonds are outstanding, an annual administration fee equal to .025% of the weighted average principal amount of the Bonds outstanding during the prior twelve (12) months, as calculated by the Borrower and confirmed by the City.

(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 2.01(d) and 2.01(e) of the Indenture.

(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.

SECTION 4.3. UNCONDITIONAL OBLIGATION. The obligations of the Borrower to make the payments required by Section 4.2 hereof (including payments on the 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, 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 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 Project, 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 Mortgage 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 make payments directly to the Trustee 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 and Paying Agents 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 may provide and subsequently terminate or remove a Credit Facility with respect to the Bonds, pursuant to the provisions of Section 5.07 of the Indenture; provided, however, that, except in connection with the redemption of Bonds, the Borrower shall not intentionally cause the termination of, any Credit Facility with respect to Bonds during a Term Rate Period. Not less than twenty-five days prior to the termination, removal or substitution of any Credit Facility with respect to the Bonds, the Borrower shall mail written notice of such termination, removal or substitution to the Trustee. Not less than fifteen days prior to the delivery of any substitute Credit Facility for the Bonds, the Borrower shall mail written notice of such substitution to each Rating Agency.

## ARTICLE V

### SPECIAL COVENANTS AND AGREEMENTS

SECTION 5.1. RIGHT OF ACCESS TO THE PROJECT. The Borrower agrees that during the term of this Agreement the City, the Trustee and the duly authorized agents of either of them shall have the right at all reasonable times during normal business hours to enter upon the site of the Project described in Exhibit A hereto to examine and inspect such Project; 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 and the Trustee may be exercised only after such 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 or the Trustee 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 (subject to any applicable restrictions otherwise imposed by law or contract, including the Borrower's franchises and the City's Charter), 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 under the Mortgage Bonds, 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, except that no such opinion shall be required in the case of the reorganization described in the proxy statement of the Borrower dated March 1, 1995.

(b) The rights and obligations of the Borrower under this Agreement may be assigned by the Borrower, with the written consent of the City, 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, including payments pursuant to the Mortgage Bonds, and for performance and observance of the other agreements on its part herein provided to be performed and observed by it.

(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, result in the interest on the Bonds being determined to be includable in the gross income for federal income tax purposes of the owners thereof (other than a "substantial user" of the Project or a "related person" within the meaning of Section 103(b)(13) of the 1954 Code).

(c) The Borrower acknowledges that Section 103 of the City's Charter specifies in part as follows: "No franchises shall be transferable except with the approval of the Council expressed by ordinance."

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 and its 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, to provide the Trustee 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 Project it will (i) maintain, or cause to be maintained, the Project in as reasonably safe condition as its operations shall permit and (ii) maintain, or cause to be maintained, the Project 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 Section 148(f) of the Code and any temporary, proposed or final Treasury Regulations as may be applicable to the Bonds from time to time. 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.

(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 Project or a "related person" within the meaning of 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 hereunder shall be deemed to be modified to that extent.

(d) Notwithstanding any provision of Section 2.2(c) of this Agreement, or this Section 5.6 or Section 6.06 of the Indenture, unless and until the City shall have received an Opinion of Bond Counsel to the effect that interest on the Bonds is Tax-Exempt, the Borrower shall not be required to comply with any covenant in said sections relating to the Bonds or to the Project nor shall the Borrower be required to act consistently with any representation or warranty contained therein with respect to the Bonds or the Project. Notwithstanding any provision of Sections 3.3(iii), 5.2(a), 5.2(b)(iv) or 5.7 of this Agreement, the Borrower shall not be required to furnish an Opinion of Bond Counsel to the effect that some proposed action or omission to act will not adversely affect the Tax-Exempt status of interest on the Bonds unless and until the City shall have received an Opinion of Bond Counsel to the effect that interest on the Bonds is Tax-Exempt.

SECTION 5.7. NOTICE OF RATE PERIODS. 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. REMARKETING OF THE BONDS.

(a) The Borrower agrees to perform all obligations and duties required of it by the Indenture with respect to the remarketing of the Bonds, and, to appoint as set forth below a Remarketing Agent and a Tender Agent meeting the qualifications and otherwise meeting the requirements set forth in this Section 5.8.

(b) Tender Agent.

(i) Appointment and Duties: In order to carry out the duties and obligations of the Tender Agent contained in the Indenture, the Borrower shall appoint a Tender Agent or Tender Agents in order to carry out such duties and obligations, subject to the conditions set forth below. Each Tender Agent shall designate to the Trustee its principal office and signify its acceptance of the duties and obligations imposed upon it under the Indenture by entering into a Tender Agreement with the Borrower and such other parties as shall be appropriate, which may be combined with a Remarketing Agreement into a single document, delivered to the City, the Trustee, the Borrower and the Remarketing Agent, under which the Tender Agent shall agree, particularly (but without limitation): (A) to perform the duties and comply with the requirements imposed upon it by the Tender Agreement, the Indenture and this Agreement; and (B) to keep such books and records with respect to its activities as Tender Agent as shall be consistent with prudent industry practice and to make such books and records available for inspection by the City, the Trustee and the Borrower at all reasonable times.

(ii) Qualifications: Each Tender Agent shall be a financial institution organized and doing business under the laws of the United States or of a state thereof, authorized under such laws to exercise corporate trust powers, having a combined capital and surplus of at least Fifty Million Dollars (\$50,000,000), and subject to supervision or examination by federal or state authority. If such financial institution publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for the purposes of this Section the combined capital and surplus of such banking corporation or banking association shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published.

(c) Remarketing Agent. In order to carry out the duties and obligations contained in the Indenture, the Borrower, by an instrument in writing (which may be the Remarketing Agreement) signed by an Authorized Borrower Representative, shall select the Remarketing Agent for the Bonds subject to the conditions set forth below. The Remarketing Agent shall designate to the Trustee its principal office and signify its acceptance of the duties and obligations imposed upon it under the Indenture by a written instrument of acceptance (which may be the execution of a Remarketing Agreement) delivered to the City, the Trustee and the Borrower under which the Remarketing Agent shall agree, particularly (but without limitation): (i) to perform the duties and comply with the requirements imposed upon it by the Remarketing Agreement, the Indenture and this Agreement; and (ii) to keep such books and records with respect to its activities as Remarketing Agent as shall be consistent with prudent industry practice and to make such books and records available for inspection by the City, the Trustee and the Borrower at all reasonable times.

(d) Remarketing Agreement. In order to provide for the remarketing of the Bonds, the Borrower shall enter into a Remarketing Agreement with the Remarketing Agent and such other parties as shall be appropriate, which may be combined with a Tender Agreement into a single document. Each Remarketing Agreement shall include the following: (i) a requirement that such Remarketing Agreement shall not be terminated by the Borrower without cause for a period of at least six months after the effective date thereof; and (ii) a statement to the effect that the Remarketing Agent is not acting in an agency capacity with respect to the Borrower in establishing interest rates and Rate Periods as described in Section 2.01 of the Indenture, but is acting as agent of the City pursuant to the Law with respect to such functions.

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. The Borrower further agrees and covenants to notify the City promptly upon receiving actual notice of any non-performance by the Trustee of its duties and obligations under the Indenture or this Agreement.

SECTION 5.10. INFORMATION AND REPORTS. During any period that the Borrower is not subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, and unless and until the City has received an Opinion of Counsel to the effect that, without compliance with the restrictions set forth in the Bond form legend, the Bonds are not required to be registered under the Securities Act, the Borrower agrees to make

available to the Bondholders and the Remarketing Agent the information and reports required by Rule 144A under the Securities Act to enable resales of the Bonds to be made pursuant to Rule 144A.

## 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) occurrence of a "completed default" under and as defined in the Borrower Indenture; 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 upon the written request of any Credit Provider or 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 Credit Provider, 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)(4) of the Indenture. 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.

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 therefor, then, and in every such case, 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 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; and provided further 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 the Credit Provider.

In case the Trustee 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 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 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 such amounts 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, 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 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 MONIES. By virtue of the assignment 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 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 Indenture; provided, however, that if any event specified in Section 4.01(a)(1)(A) through (D) of the Indenture 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 Project 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 Indenture. 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) through (3) of said Section 4.01(b) giving rise to such required prepayment, and immediately upon the occurrence of any event set forth in paragraph (4) 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 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 Indenture. 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 in connection herewith, except from 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 pursuant to Section 4.2(b), 4.2(c), 5.6, 6.3, 8.2 and 8.3 of this

Agreement), 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 fifteen (15) days after billing therefor and to indemnify the City and the Trustee against all costs and charges, including fees and disbursements of attorneys, accountants, consultants, including financial consultants, engineers and other experts incurred, in the absence of willful misconduct, 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, other than under the circumstances described in Section 6.3 hereof.

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, 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 Project, 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 Project or any part thereof; (2) the issuance of any Bonds or any certifications 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, or the exercise or performance of any of its powers or duties under the Indenture; or (4) 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 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 costs, 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 follows:

To the City:           City Manager  
                          City of San Diego  
                          City Administration Building  
                          202 C Street  
                          San Diego, CA 92101  
                          Attention: Economic Development Services

To the Borrower:       San Diego Gas & Electric Company  
                          101 Ash Street  
                          P.O. Box 1831  
                          San Diego, CA 92112  
                          Attention: Treasurer

To the Trustee:        Bank of America National Trust  
                          and Savings Association  
                          333 South Beaudry Avenue  
                          Los Angeles, CA 90017  
                          Attention: Corporate Trust Division #8510

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 the 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 is outstanding or the Trustee holds any moneys under the Indenture, whichever is later. 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.

SECTION 9.9. EQUAL OPPORTUNITY AND NONDISCRIMINATION.

The Borrower agrees to use its best efforts to require any and all of its contractors, subcontractors, independent contractors and employees to comply with applicable federal, state or local equal opportunity and nondiscrimination requirements imposed by statute, ruling or regulation and to hold the City harmless from any and all liability, claims, damages or injuries to any person in connection with any failure by such contractors, subcontractors, independent contractors or employees to act in accordance with such requirements. The Borrower further agrees to monitor such contractors, subcontractors, independent contractors and employees for compliance with such equal opportunity and nondiscrimination requirements. The Borrower also agrees, upon request of the City, to provide the City with a copy of the Borrower's Equal Employment Opportunity Policy and any requested compliance information concerning any underwriters or bond counsel employed by the Borrower in connection with this Agreement.

IN WITNESS WHEREOF, The City of San Diego 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.

THE CITY OF SAN DIEGO

By \_\_\_\_\_  
Director,  
Economic Development Services

[SEAL]

Attest:

By \_\_\_\_\_  
Deputy City Clerk

APPROVED AS TO  
FORM AND LEGALITY:

JOHN W. WITT,  
City Attorney

By \_\_\_\_\_  
Deputy City Attorney

SAN DIEGO GAS & ELECTRIC COMPANY

By \_\_\_\_\_  
Assistant Treasurer

[SEAL]

Attest:

By \_\_\_\_\_  
Assistant Secretary

EXHIBIT A

Description of the Project

Local Gas Facilities

Acquisition and construction of additions and improvements to the Borrower's gas distribution (operating at pressures at or below 400 psig) facilities, located within its gas retail service area in San Diego County, required for the distribution of gas for delivery to the Borrower's customers located therein. Such facilities include the acquisition and construction of new, medium- and low-pressure distribution mains, and new customer service lines or the extension, replacement or relocation of existing such mains or portions or components thereof, regulator stations controlling the passage of gas from distribution mains of higher pressure to distribution mains of lower pressure and the volume and pressure of gas within the mains, together with all necessary valves, controls, meters, and other measuring and regulating devices, and facilities, plant, property, and other equipment and improvements (including land and land-rights) necessary for the installation, protection, maintenance, control and operation of the foregoing.

LOAN AGREEMENT

Between

THE CITY OF SAN DIEGO

And

SAN DIEGO GAS & ELECTRIC COMPANY

Dated as of June 1, 1995

Relating to

\$57,650,000

The City of San Diego  
Industrial Development Revenue Refunding Bonds  
(San Diego Gas & Electric Company)  
1995 Series A  
1995 Series B



LOAN AGREEMENT

TABLE OF CONTENTS

	Page
PARTIES	1
PREAMBLES	1
ARTICLE I	
DEFINITIONS	
SECTION 1.1. DEFINITION OF TERMS	2
SECTION 1.2. NUMBER AND GENDER	2
SECTION 1.3. ARTICLES, SECTIONS, ETC.	2
ARTICLE II	
REPRESENTATIONS	
SECTION 2.1. REPRESENTATIONS OF THE CITY	2
SECTION 2.2. REPRESENTATIONS OF THE BORROWER	3
ARTICLE III	
ISSUANCE OF THE BONDS; APPLICATION OF PROCEEDS	
SECTION 3.1. AGREEMENT TO ISSUE BONDS; APPLICATION OF BOND PROCEEDS	4
SECTION 3.2. INVESTMENT OF MONEYS IN FUNDS	5
SECTION 3.3. AMENDMENT OF DESCRIPTION OF THE PROJECT	5
ARTICLE IV	
LOAN TO BORROWER; REPAYMENT PROVISIONS	
SECTION 4.1. LOAN TO BORROWER	5
SECTION 4.2. REPAYMENT AND PAYMENT OF OTHER AMOUNTS PAYABLE	5
SECTION 4.3. UNCONDITIONAL OBLIGATION	7
SECTION 4.4. ASSIGNMENT OF CITY'S RIGHTS	8
SECTION 4.5. AMOUNTS REMAINING IN FUNDS	8
SECTION 4.6. CREDIT FACILITY	9
ARTICLE V	
SPECIAL COVENANTS AND AGREEMENTS	
SECTION 5.1. RIGHT OF ACCESS TO THE PROJECT	9

SECTION 5.2.	THE BORROWER'S MAINTENANCE OF ITS EXISTENCE; ASSIGNMENTS	9
SECTION 5.3.	RECORDS AND FINANCIAL STATEMENTS OF BORROWER	10
SECTION 5.4.	MAINTENANCE AND REPAIR	11
SECTION 5.5.	QUALIFICATION IN CALIFORNIA	11
SECTION 5.6.	TAX EXEMPT STATUS OF BONDS	11
SECTION 5.7.	NOTICE OF RATE PERIODS	12
SECTION 5.8.	REMARKETING OF THE BONDS	12
SECTION 5.9.	NOTICES TO TRUSTEE AND CITY	14

ARTICLE VI

EVENTS OF DEFAULT AND REMEDIES

SECTION 6.1.	EVENTS OF DEFAULT	14
SECTION 6.2.	REMEDIES ON DEFAULT	15
SECTION 6.3.	AGREEMENT TO PAY ATTORNEYS' FEES AND EXPENSES	17
SECTION 6.4.	NO REMEDY EXCLUSIVE	17
SECTION 6.5.	NO ADDITIONAL WAIVER IMPLIED BY ONE WAIVER	18

ARTICLE VII

PREPAYMENT

SECTION 7.1.	REDEMPTION OF BONDS WITH PREPAYMENT MONEYS	18
SECTION 7.2.	OPTIONS TO PREPAY INSTALLMENTS	18
SECTION 7.3.	MANDATORY PREPAYMENT	18
SECTION 7.4.	AMOUNT OF PREPAYMENT	19
SECTION 7.5.	NOTICE OF PREPAYMENT	19

ARTICLE VIII

NON-LIABILITY OF CITY; EXPENSES; INDEMNIFICATION

SECTION 8.1.	NON-LIABILITY OF CITY	20
SECTION 8.2.	EXPENSES	20
SECTION 8.3.	INDEMNIFICATION	20

ARTICLE IX

MISCELLANEOUS

SECTION 9.1.	NOTICES	21
SECTION 9.2.	SEVERABILITY	22
SECTION 9.3.	EXECUTION OF COUNTERPARTS	22

SECTION 9.4.	AMENDMENTS, CHANGES AND MODIFICATIONS	22
SECTION 9.5.	GOVERNING LAW	22
SECTION 9.6.	AUTHORIZED BORROWER REPRESENTATIVE	22
SECTION 9.7.	TERM OF THE AGREEMENT	23
SECTION 9.8.	BINDING EFFECT	23
TESTIMONIUM		24
SIGNATURES AND SEALS		24
EXHIBIT A	Description of the Project	A-1

LOAN AGREEMENT

THIS LOAN AGREEMENT, dated as of June 1, 1995, by and between THE CITY OF SAN DIEGO, a municipal corporation and charter city duly organized and existing under the laws and Constitution of the State of California (the "City"), and SAN DIEGO GAS & ELECTRIC COMPANY, a corporation organized and existing under the laws of the State of California (the "Borrower"),

W I T N E S S E T H :

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 2 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 2 of the Charter, has enacted the City of San Diego Economic Development Revenue Bond Law, comprising Article 7 of Chapter IX of the San Diego Municipal Code, pursuant to Ordinance No. 0-15586 (New Series), adopted on September 14, 1981, 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 requested that the City assist in the refunding or replacement of certain outstanding bonds previously issued by the City (the "Prior Bonds") to provide the Borrower with financial assistance to acquire, construct and install certain facilities for the local furnishing of electric energy and gas (the "1985 Project"); and

WHEREAS, the City after due investigation and deliberation has adopted its ordinance authorizing the issuance of The City of San Diego Industrial Development Revenue Refunding Bonds (San Diego Gas & Electric Company) 1995 Series A and 1995 Series B (collectively, the "Bonds") to refund and redeem a portion of the Prior Bonds; and

WHEREAS, the City proposes to assist in refinancing the portion of the 1985 Project which constitutes facilities for the local furnishing of electric energy (the "Project") 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 Bank of America National Trust and Savings Association, as Trustee (the "Trustee"), as originally executed or as it may from time to time be supplemented or amended as provided therein.

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 Project constitutes a "facility" 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 Project, 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 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 Project 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 August 3, 1992, the City Council of the City adopted Ordinance No. 0-17813 (New Series), and on March 29, 1993, the City Council adopted Ordinance No. 0-17903 (New Series) authorizing the issuance of the Bonds, and on May 1, 1995, the City Council adopted Resolution No. R-285683, authorizing 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, the Mortgage Bonds and all other documents contemplated hereby to be executed by the Borrower.

(b) Neither the execution and delivery of this Agreement or the Mortgage Bonds, the consummation of the transactions contemplated hereby, 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 Project consists and will consist of those facilities described in Exhibit A hereto, and the Borrower shall make no changes to such portion of the Project or to the operation thereof which would affect the qualification of the Project as a "facility" under the Law or impair the exemption from gross income of the interest on the Bonds for federal income tax purposes. In particular, the Borrower shall comply with all requirements of the San Diego Gas & Electric Company Engineering and Financial Certificate, dated the Issue Date (the "Engineering Certificate"), which is hereby incorporated by reference herein. The Project consists of facilities for the local furnishing of electric energy as described in the Engineering Certificate. The Borrower intends to utilize such portion of the Project as facilities for the local furnishing of electric energy throughout the foreseeable future.

(d) The Borrower has and will have title to the Project sufficient to carry out the purposes of this Agreement.

(e) The economic useful life of the Project is as set forth in the Engineering Certificate.

(f) All certificates, approvals, permits and authorizations with respect to the construction of the Project 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 Project 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 refinance a portion of the cost of the Project, 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 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 PROJECT. In the event that the Borrower desires to amend or supplement the Project, as described in Exhibit A hereto, and the City 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 Project 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 a portion of the Prior Bonds and the first mortgage bonds of the Borrower relating thereto 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. To evidence, secure and provide for the repayment of the loan made hereunder, the Borrower hereby and concurrently herewith delivers to the Trustee its Mortgage Bonds, of like principal amount, maturity date, interest rates and redemption provisions as the Bonds. In addition, the Borrower agrees to make the payments required by subsection (a) (to the extent such payments are not timely provided for by the payment of principal of and interest on the Mortgage Bonds) through (d) of this Section as Repayment Installments on such loan.



(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 pursuant to the Mortgage Bonds, together with any other payments 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 of (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.

(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 expenses of the City related to the financing of the Project which are not otherwise required to be paid by the Borrower under the terms of this Agreement; 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 (i) on or before the Issue Date an origination fee for the Bonds in the amount of \$144,125 and (ii) annually in arrears on September 1 of each year during which any Bonds are outstanding, an annual administration fee equal to .025% of the weighted average principal amount of the Bonds outstanding during the prior twelve (12) months, as calculated by the Borrower and confirmed by the City.

(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 2.01(d) and 2.01(e) of the Indenture.

(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.

**SECTION 4.3. UNCONDITIONAL OBLIGATION.** The obligations of the Borrower to make the payments required by Section 4.2 hereof (including payments on the 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, 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 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 Project, 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 Mortgage 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 make payments directly to the Trustee 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 and Paying Agents 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 may provide and subsequently terminate or remove a Credit Facility with respect to a Series of Bonds, pursuant to the provisions of Section 5.07 of the Indenture; provided, however, that, except in connection with the redemption of Bonds, the Borrower shall not intentionally cause the termination of, any Credit Facility with respect to Bonds during a Term Rate Period. Not less than twenty-five days prior to the termination, removal or substitution of any Credit Facility with respect to a Series of Bonds, the Borrower shall mail written notice of such termination, removal or substitution to the Trustee. Not less than fifteen days prior to the delivery of any substitute Credit Facility for a Series of Bonds, the Borrower shall mail written notice of such substitution to each Rating Agency.

## ARTICLE V

### SPECIAL COVENANTS AND AGREEMENTS

SECTION 5.1. RIGHT OF ACCESS TO THE PROJECT. The Borrower agrees that during the term of this Agreement the City, the Trustee and the duly authorized agents of either of them shall have the right at all reasonable times during normal business hours to enter upon the site of the Project described in Exhibit A hereto to examine and inspect such Project; 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 and the Trustee may be exercised only after such 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 or the Trustee 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 (subject to any applicable restrictions otherwise imposed by law or contract, including the Borrower's franchises and the City's Charter), 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 under the Mortgage Bonds, 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, except that no such opinion shall be required in the case of the reorganization described in the proxy statement of the Borrower dated March 1, 1995.

(b) The rights and obligations of the Borrower under this Agreement may be assigned by the Borrower, with the written consent of the City, 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, including payments pursuant to the Mortgage Bonds, and for performance and observance of the other agreements on its part herein provided to be performed and observed by it.

(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, result in the interest on the Bonds being determined to be includable in the gross income for federal income tax purposes of the owners thereof (other than a "substantial user" of the Project or a "related person" within the meaning of Section 103(b)(13) of the 1954 Code).

(c) The Borrower acknowledges that Section 103 of the City's Charter specifies in part as follows: "No franchises shall be transferable except with the approval of the Council expressed by ordinance."

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 and its 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, to provide the Trustee 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 Project it will (i) maintain, or cause to be maintained, the Project in as reasonably safe condition as its operations shall permit and (ii) maintain, or cause to be maintained, the Project 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 Section 148(f) of the Code and any temporary, proposed or final Treasury Regulations as may be applicable to the Bonds from time to time. 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.

(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 Project or a "related person" within the meaning of 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 hereunder shall be deemed to be modified to that extent.

SECTION 5.7. NOTICE OF RATE PERIODS. 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. REMARKETING OF THE BONDS.

(a) The Borrower agrees to perform all obligations and duties required of it by the Indenture with respect to the remarketing of the Bonds, and, to appoint as set forth below a Remarketing Agent and a Tender Agent meeting the qualifications and otherwise meeting the requirements set forth in this Section 5.8.

(b) Tender Agent.

(i) Appointment and Duties: In order to carry out the duties and obligations of the Tender Agent contained in the Indenture, the Borrower shall appoint a Tender Agent or Tender Agents in order to carry out such duties and obligations, subject to the conditions set forth below. Each Tender Agent shall designate to the Trustee its principal office and signify its acceptance of the duties and obligations imposed upon it under the Indenture by entering into a Tender Agreement with the Borrower and such other parties as shall be appropriate, which may be combined with a Remarketing Agreement into a single document, delivered to the City, the Trustee, the Borrower and each Remarketing Agent, under which the Tender Agent shall agree, particularly (but without limitation): (A) to perform the duties and comply with the requirements imposed upon it by the Tender Agreement, the Indenture and this Agreement; and (B) to keep such books and records with respect to its activities as Tender Agent as shall be consistent with prudent industry practice and to make such books and records available for inspection by the City, the Trustee and the Borrower at all reasonable times.

(ii) Qualifications: Each Tender Agent shall be a financial institution organized and doing business under the laws of the United States or of a state thereof, authorized under such laws to exercise corporate trust powers, having a combined capital and surplus of at least Fifty Million Dollars (\$50,000,000), and subject to supervision or examination by federal or state authority. If such financial institution publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for the purposes of this Section the combined capital and surplus of such banking corporation or banking association shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published.

(c) Remarketing Agent. In order to carry out the duties and obligations contained in the Indenture, the Borrower, by an instrument in writing (which may be the Remarketing Agreement) signed by an Authorized Borrower Representative, shall select the Remarketing Agent(s) for each series of Bonds subject to the conditions set forth below. Each Remarketing Agent shall designate to the Trustee its principal office and signify its acceptance of the duties and obligations imposed upon it under the Indenture by a written instrument of acceptance (which may be the execution of a Remarketing Agreement) delivered to the City, the Trustee and the Borrower under which the Remarketing Agent shall agree, particularly (but without limitation): (i) to perform the duties and comply with the requirements imposed upon it by the Remarketing Agreement, the Indenture and this Agreement; and (ii) to keep such books and records with respect to its activities as Remarketing Agent as shall be consistent



with prudent industry practice and to make such books and records available for inspection by the City, the Trustee and the Borrower at all reasonable times.

(d) Remarketing Agreement. In order to provide for the remarketing of the Bonds, the Borrower shall enter into a Remarketing Agreement with each Remarketing Agent and such other parties as shall be appropriate, which may be combined with a Tender Agreement into a single document. Each Remarketing Agreement shall include the following: (i) a requirement that the Remarketing Agreement shall not be terminated by the Borrower without cause for a period of at least six months after the effective date thereof; and (ii) a statement to the effect that the Remarketing Agent is not acting in an agency capacity with respect to the Borrower in establishing interest rates and Rate Periods as described in Section 2.01 of the Indenture, but is acting as agent of the City pursuant to the Law with respect to such functions.

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. The Borrower further agrees and covenants to notify the City promptly upon receiving actual notice of any non-performance by the Trustee of its duties and obligations under the Indenture or this Agreement.

## 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) occurrence of a "completed default" under and as defined in the Borrower Indenture; 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 upon the written request of any Credit Provider or 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 Credit Provider, 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)(4) of the Indenture. 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.

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 therefor, then, and in every such case, 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 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; and provided further 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 the Credit Provider.

In case the Trustee 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 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 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 such amounts 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, 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 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 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 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 Indenture; provided, however, that if any event specified in Section 4.01(a)(1)(A) through (D) of the Indenture 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 Project 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 Indenture. 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) through (3) of said Section 4.01(b) giving rise to such required prepayment, and immediately upon the occurrence of any event set forth in paragraph (4) 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 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 of any Series 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 Indenture. 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 in connection herewith, except from 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 pursuant to Section 4.2(b), 4.2(c), 5.6, 6.3, 8.2 and 8.3 of this Agreement), 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 fifteen (15) days after billing therefor and to indemnify the City and the Trustee against all costs and charges, including fees and disbursements of attorneys, accountants, consultants, including financial consultants, engineers and other experts incurred, in the absence of willful misconduct, 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, other than under the circumstances described in Section 6.3 hereof.

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, 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 Project, 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 Project or any part thereof; (2) the issuance of any Bonds or any certifications 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, or the exercise or performance of any of its powers or duties under the Indenture; or (4) 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 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 costs, 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 follows:



To the City: City Manager  
City of San Diego  
City Administration Building  
202 C Street  
San Diego, CA 92101  
Attention: Economic Development Services

To the Borrower: San Diego Gas & Electric Company  
101 Ash Street  
P.O. Box 1831  
San Diego, CA 92112  
Attention: Treasurer

To the Trustee: Bank of America National Trust and  
Savings Association  
333 South Beaudry Avenue  
Los Angeles, CA 90017  
Attention: Corporate Trust Division, #8510

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 the 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 is outstanding or the Trustee holds any moneys under the Indenture, whichever is later. 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.

SECTION 9.9. EQUAL OPPORTUNITY AND NONDISCRIMINATION. The Borrower agrees to use its best efforts to require any and all of its contractors, subcontractors, independent contractors and employees to comply with applicable federal, state or local equal opportunity and nondiscrimination requirements imposed by statute, ruling or regulation and to hold the City harmless from any and all liability, claims, damages or injuries to any person in connection with any failure by such contractors, subcontractors, independent contractors or employees to act in accordance with such requirements. The Borrower further agrees to monitor such contractors, subcontractors, independent contractors and employees for compliance with such equal opportunity and nondiscrimination requirements. The Borrower also agrees, upon request of the City, to provide the City with a copy of the Borrower's Equal Employment Opportunity Policy and any requested compliance information concerning any underwriters or bond counsel employed by the Borrower in connection with this Agreement.

IN WITNESS WHEREOF, The City of San Diego 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.

THE CITY OF SAN DIEGO

By \_\_\_\_\_  
Director,  
Economic Development Services

[SEAL]

Attest:

By \_\_\_\_\_  
Deputy City Clerk

APPROVED AS TO FORM  
AND LEGALITY:

JOHN W. WITT,  
City Attorney

By \_\_\_\_\_  
Deputy City Attorney

SAN DIEGO GAS & ELECTRIC COMPANY

By \_\_\_\_\_  
Assistant Treasurer

[SEAL]

Attest:

By \_\_\_\_\_  
Assistant Secretary

EXHIBIT A

Description of the Project

Local Electric Facilities

Acquisition and construction of additions and improvements to the Borrower's electric distribution facilities (12 KV and under) and related substations, and customer service connections located within the Borrower's electric retail service area, required by the Borrower to provide for the transfer and distribution of electric energy to its customers located therein, 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.

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STOCK PURCHASE AGREEMENT

DATED AS OF MAY 15, 1995

AMONG

WES ACQUISITION CORP.,

PACIFIC DIVERSIFIED CAPITAL COMPANY

AND WEXFORD CAPITAL CORPORATION,

AS INDEMNITOR

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TABLE OF CONTENTS

	Page
ARTICLE I	1
TRANSACTIONS AT THE CLOSING	1
1.1 Shares and Purchased Loans	1
1.2 Closing	1
1.3 Purchase Price	1
1.4 Contribution to Capital	2
ARTICLE II	2
REPRESENTATIONS AND WARRANTIES	2
2.1 Representations and Warranties of the Seller	2
2.2 Representations and Warranties of the Buyer	3
ARTICLE III	5
CERTAIN COVENANTS AND AGREEMENTS	5
3.1 Consents	5
3.2 Efforts to Consummate	5
3.3 Confidential Information	5
3.4 Negotiation With Others	6
3.5 H-S-R Act Filings	6
ARTICLE IV	6
TAXES	6
4.1 Tax Indemnification	6
4.2 Procedures Relating to Indemnification of Tax Claims	7
4.3 Section 338(h)(10) Election.	8
4.4 Survival of Tax Provisions	8
4.5 Real Property Taxes	9
4.6 Tax Return Filings	9
4.7 Termination of Tax Sharing Agreements	9
ARTICLE V	10
CONDITIONS OF	10
5.1 Conditions of Obligations of the Buyer	10
5.2 Conditions to Obligations of the Seller	11
ARTICLE VI	12
INDEMNIFICATION	12
6.1 Indemnification by the Seller	12
6.2 Indemnification by the Indemnitor	12

6.3	Defense of Claims	13
6.4	Heller Claims	14
6.5	Remedies Cumulative	14
ARTICLE VII		14
	SURVIVAL OF REPRESENTATION AND WARRANTIES; AMENDMENT, MODIFICATION AND WAIVER	14
7.1	Survival of Representations and Warranties, Etc.	14
7.2	Amendment, Modification and Waiver	15
ARTICLE VIII		15
	TERMINATION	15
8.1	Right of Termination	15
8.2	Effect of Termination	15
ARTICLE IX		16
	MISCELLANEOUS	16
9.1	Expenses	16
9.2	Entire Agreement	16
9.3	Publicity	16
9.4	Descriptive Headings	16
9.5	Notices	16
9.6	Counterparts	17
9.7	Governing Law	17
9.8	Benefits of Agreement	17

STOCK PURCHASE AGREEMENT dated as of May 15, 1995, among WES Acquisition Corp., a Delaware corporation (the "Buyer"), Pacific Diversified Capital Company, a California corporation (the "Seller"), and Wexford Capital Corporation, a Delaware corporation, as indemnitor hereunder (the "Indemnitor").

The Seller owns an aggregate of 14,260,000 shares (the "Shares") of common stock, par value \$.01 (the "Common Stock"), of Wahlco Environmental Systems, Inc., a Delaware corporation (the "Company") and has outstanding \$24,428,831.89 aggregate principal amount in loans (the "Loans") to the Company. The Seller desires to sell to the Buyer, and the Buyer desires to purchase from the Seller the Shares, and \$4,900,000 principal amount of the Loans (the "Purchased Loans"), all upon the terms and subject to the conditions set forth in this Agreement.

NOW, THEREFORE, in consideration of the mutual benefits to be derived from this Agreement and of the representations, warranties, conditions and promises hereinafter contained, the Buyer, the Seller and the Indemnitor hereby agree as follows:

## ARTICLE I

### TRANSACTIONS AT THE CLOSING

1.1 Shares and Purchased Loans. Upon the terms and subject to the conditions hereinafter set forth, at the Closing (as hereinafter defined) the Seller agrees to sell and deliver to the Buyer, and the Buyer agrees to purchase from the Seller, all right, title and interest in and to the Shares and the Purchased Loans, in each case, except as set forth on Schedule 1 hereto, free and clear of all of the following (hereinafter collectively referred to as "Claims"): security interests, liens, pledges, claims, charges, escrows, encumbrances, options, rights of set-off, rights of first refusal, mortgages, indentures, security agreements or other agreements, arrangements, contracts, commitments, understandings or obligations, of any nature whatsoever, whether written or oral and whether or not relating in any way to credit or the borrowing of money.

1.2 Closing. The closing (the "Closing") of the transactions contemplated by this Agreement shall take place at the offices of O'Melveny & Myers, 610 Newport Center Drive, Suite 1700, Newport Beach, California 92660-6429 on a business day which shall be no later than May 15, 1995 (the "Closing Date").

1.3 Purchase Price. The purchase price to be paid to the Buyer for the Shares and the Purchased Loans shall be an amount equal to \$5,000,000 (the "Purchase Price"), of which \$4,900,000 shall be allocated to the Purchased Loans and \$100,000 shall be allocated to the Shares. At the Closing, (i) against delivery to the Buyer of evidence of the Purchased Loans, the Buyer shall pay



to the Seller by wire transfer the amount of \$4,900,000 and (ii) against delivery to the Escrow Agent (as hereinafter defined) of one or more stock certificates, endorsed by the Seller in blank for transfer to the Buyer, representing the Shares, the Buyer shall deliver to the Escrow Agent by wire transfer the amount of \$100,000 ("Stock Purchase Price"). At the Closing, the Buyer and the Seller shall enter into a mutually acceptable escrow agreement (the "Escrow Agreement") with a mutually acceptable bank having capital and surplus of at least \$100,000,000 (the "Escrow Agent"). The Escrow Agreement shall provide that upon the expiration of the applicable waiting period, including any extension thereof, under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (the "H-S-R Act"), the Escrow Agent shall transfer (a) certificates representing the Shares endorsed by the Seller in blank for transfer to the Buyer, and (b) the Stock Purchase Price to the Seller by delivery of a certified check or by wire transfer ("Stock Acquisition"). The parties hereto intend to treat the Company and its Subsidiaries as part of the Selling Consolidated Group for all periods up to and including the date of the Stock Acquisition and shall file all Federal income tax returns in accordance with such intention.

1.4 Contribution to Capital. Concurrently with the Closing, Seller shall contribute to the capital of the Company all Loans, together with any accrued but unpaid interest, fees or other charges payable by the Company to Seller in connection with the Loans (collectively, the "Contributed Loans") except for the Purchased Loans. The documentation evidencing the foregoing contribution to capital shall be satisfactory to Buyer.

## ARTICLE II

### REPRESENTATIONS AND WARRANTIES

2.1 Representations and Warranties of the Seller. The Seller represents and warrants to the Buyer as follows:

(a) Seller's Title to the Shares. Except as set forth on Schedule 1 attached hereto, the Seller is the lawful owner, of record and beneficially, of the Shares and the Purchased Loans and has, and will transfer to the Buyer as provided hereunder, good and marketable title to the Shares and the Purchased Loans, free and clear of any Claims, and the Seller has the absolute right and power to sell, assign, convey and transfer the Shares and the Purchased Loans and all rights and benefits incident to the ownership thereof. Delivery of the Shares and the Purchased Loans to the Buyer as provided hereunder will (i) pass good and marketable title to the Shares and the Purchased Loans to the Buyer, free and clear of any Claims and (ii) convey, free and clear of any Claims, any and all rights and benefits incident to the ownership of the Shares or the Purchased Loans. There are no

outstanding options, warrants or rights to purchase or otherwise acquire any of the Shares or the Purchased Loans, and there are no agreements, arrangements or undertakings between the Seller and any other person or entity with respect to the voting, sale or disposition of any of the Shares or the Purchased Loans or any other matters relating to or affecting the Shares or the Purchased Loans. The Seller acquired the Shares in transactions exempt from registration under the Securities Act of 1933, as amended (the "Securities Act"), and in compliance with any applicable state securities laws. The sale of the Shares by the Seller to the Buyer is exempt from registration under the Securities Act.

(b) Seller's Authority. The execution, delivery and performance of this Agreement and the consummation of the transactions contemplated hereby have been duly and validly authorized by all necessary corporate action by the Seller. This Agreement is the legal, valid and binding obligation of the Seller, enforceable in accordance with its own terms. Neither the execution, delivery and performance of this Agreement, nor compliance by the Seller with any of the provisions hereof will except as set forth on Schedule 1 hereto, (i) conflict with or result in a breach of the certificate of incorporation or the by-laws of the Seller, (ii) conflict with or result in a default (or give rise to any right of termination, cancellation or acceleration) under any of the terms, conditions or provisions of any note, bond, lease, mortgage, indenture, license, agreement or other instrument or obligation to which is a party, or by which the Seller or any of its properties or assets may be bound or affected, (iii) violate any law, statute, rule or regulation or order, writ, injunction or decree applicable to the Seller any of its properties or assets. Except as set forth on Schedule 1 attached hereto, no consent or approval by, or any notification of or filing with, any person (governmental or private) is required in connection with the execution, delivery and performance by the Seller, or the consummation of the transactions contemplated hereby.

(c) The principal amount of Loans outstanding recited in the second paragraph of this Agreement constitutes the entire principal amount of outstanding loans made by Seller to the Company.

2.2 Representations and Warranties of the Buyer. The Buyer represents and warrants to the Seller as follows:

(a) Organization, Standing and Power. The Buyer is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and has all requisite corporate power and authority to enter into this Agreement and to perform its obligations hereunder and to consummate the transactions contemplated hereby. The Buyer qualifies to make the Section 338(h)(10) election referred to in Section 4.3 hereof. The Buyer has delivered to the Seller true, complete and correct copies

of the certificate of incorporation and By-laws of the Buyer, in each case as amended to the date hereof.

(b) Authority. The execution, delivery and performance of this Agreement and the consummation of the transactions contemplated hereby, have been duly and validly authorized by all necessary corporate action by the Buyer. This agreement is the legal, valid and binding obligation of the Buyer, enforceable in accordance with its terms. Neither the execution, delivery and performance of this Agreement, nor compliance by the Buyer with any of the provisions hereof or thereof, will (i) conflict with or result in a breach of its certificate of incorporation or by-laws, in each case amended to the date hereof, or cause a default (or give rise to any right of termination, cancellation or acceleration) under any of the terms, conditions or provisions of any note, bond, lease, mortgage, indenture, license, or other agreement to which the Buyer is a party, or by which it or any of its properties or assets may be bound, or (ii) violate any law, statute, rule or regulation or order, writ, injunction or decree applicable to the Buyer any of its properties or assets. Except for a notification filing under the H-S-R Act and the expiration of the applicable waiting period, including any extension thereof, thereunder, no consent or approval by, or any notification of or filing with, any person (governmental or private) is required in connection with the execution, delivery and performance by the Buyer of this Agreement or the consummation by the Buyer of the transactions contemplated hereby, or if required, the same as been obtained or effected on or prior to the Closing.

(c) Brokers. No agent, broker, investment banker, person or firm acting on behalf of the Buyer or under the authority of the Buyer is or will be entitled to any broker's or finder's fee or any other commission or similar fee directly or indirectly from any of the parties hereto in connection with any of the transactions contemplated hereby.

(d) Acquisition for Investment Purposes. The Buyer is acquiring the Shares and the Purchased Loans (without conceding that the Purchased Loans are securities) for its own account, for investment and not with a view to distribution thereof within the meaning of applicable Federal and state securities laws. The Buyer understands that the Shares and the Purchased Loans have not been registered under the Securities Act, by reason of their issuance and sale in transactions exempt from the registration requirements of the Securities Act or the securities or blue sky laws of any state and that they must be held indefinitely unless a subsequent disposition thereof is registered under the Securities Act or applicable state securities or blue sky laws or are exempt from the registration requirements thereof.

ARTICLE III

CERTAIN COVENANTS AND AGREEMENTS

3.1 Consents. Prior to the Stock Acquisition, the Seller will cause the Company to effect the notification filing required under the H-S-R Act in order to permit the consummation of the transactions contemplated hereby.

3.2 Efforts to Consummate. Subject to the terms and conditions of this Agreement, the parties hereto shall take or cause to be taken all action and do or cause to be done all things necessary or advisable, under applicable laws, regulations and ordinances, in order to consummate and make effective, as soon as practicable, the transactions contemplated hereby, including the obtaining of all permits, authorizations, consents and approvals of any third party (private or governmental) which are required in connection with the consummation of the transactions contemplated hereby; provided, however, that this Section 3.2 shall not require any party to waive any condition to its benefit under this Agreement, or to make any payment to a third party or incur any undue burden in connection with the obtaining of any third party consent.

3.3 Confidential Information. The Buyer will keep confidential or proprietary information (as defined below) previously furnished to it by the Company and in the Exhibits and Schedules to this Agreement. If the Stock Acquisition does not occur, the Buyer will return to the Company all documents, instruments, work papers and other materials submitted to it or any of its agents or representatives. The Buyer agrees that prior to the Stock Acquisition it shall not directly or indirectly use or disclose (except as provided for in this Agreement) any confidential or proprietary information relating to the Company to any person, firm, corporation, association or other entity, nor shall the Buyer prior to the Stock Acquisition, and thereafter if the Stock Acquisition shall not occur, make use of any such confidential or proprietary information (except as provided for in this Agreement) for its own purpose or for the benefit of any person, firm, corporation or other entity. For the purposes of this Section 3.3, the term "confidential or proprietary information" shall mean all information disclosed to the Buyer by the Company or the Seller or their respective affiliates or to employees, consultants or others in a confidential relationship with the Buyer, relating to specific matters such as trade secrets, research and development activities, books and records, customer lists, suppliers, distribution channels, pricing information, private processes, formulae, functional specifications, blueprints, know-how, data, improvements, discoveries, designs, inventions, techniques, marketing plans, strategies, forecasts, new products and financial statements as they may exist from time to time except for confidential or proprietary information which (i) becomes

generally available to the public, (ii) was known to the Buyer prior to its disclosure by the Company or the Seller, (iii) was heretofore available to the Buyer on a nonconfidential basis from a source (other than the Company or the Seller) which was entitled to disclose the same or (iv) is required by law, governmental order or decree to be disclosed by the Buyer.

3.4 Negotiation With Others. From and after the date hereof until the Stock Acquisition shall have occurred or this Agreement shall have been terminated in accordance with Section 8.1 hereof, the Seller will not, directly or indirectly, (a) solicit or initiate discussions or engage in negotiations with any person relating to the possible acquisition of the Company (whether by way of merger, purchase of capital stock, purchase of assets or otherwise) or any portion of the Company (whether such negotiations are initiated by the Seller or the Company or otherwise), other than the Buyer or its designees, (b) provide information with respect to the Company to any person, other than the Buyer and its designees, relating to the possible acquisition of the Company (whether by way of merger, purchase of capital stock, purchase of assets or otherwise) or any portion of the Company or (c) enter into a transaction with any person, other than the Buyer or its designees concerning the possible acquisition of the Company (whether by way of merger, purchase of capital stock, purchase of assets or otherwise) or any portion of the Company.

3.5 H-S-R Act Filings. The Seller and the Buyer will cooperate with one another in the preparation and filing of all notices and reports required pursuant to the H-S-R Act and will comply with the requirements for providing information made pursuant thereto.

#### ARTICLE IV

##### TAXES

###### 4.1 Tax Indemnification.

For purposes of this Agreement, each reference to:

(A) "Affiliate" shall mean, with respect to any person, any entity or person that directly, or indirectly, through one or more intermediaries, controls or is controlled by, or is under common control with such person.

(B) "Code" shall mean the Internal Revenue Code of 1986, as amended;

(C) "Tax Return" shall mean any return, report, information return, or other document (including elections,

declarations, disclosures, schedules, estimates, and other returns or supporting documents) with respect to taxes;

(D) "Selling Consolidated Group" shall mean the "affiliated group" (within the meaning of section 1504 of Code) of which San Diego Gas & Electric Company ("SDG&E") is the common parent filing U.S. consolidated federal income tax returns, which include the Seller as an includible member.

(E) "Subsidiaries" shall mean, solely for purposes of this Article IV, any direct or indirect subsidiary corporation of Company.

Notwithstanding anything in this Agreement to the contrary, Seller shall indemnify Buyer and any Affiliate of Buyer, including the Company and its Subsidiaries and hold them harmless for, from and against (a) all liability for all U.S. Federal income taxes of Company and its Subsidiaries for all taxable periods ending on or before the earlier of (i) the date of the Stock Acquisition and (ii) the date the Shares are treated as acquired by Buyer for U.S. Federal income tax purposes ("Pre-Stock Acquisition Period"), including, without limitation, any liability for U.S. Federal income taxes imposed upon Company and its Subsidiaries pursuant to United States Treasury Regulation 1.1502-6 as a result of being a member of the Selling Consolidated Group and (b) all liability for U.S. Federal income taxes accruing on or before the end of the Pre-Stock Acquisition Period which result from the Election (as defined in Section 4.3 of this Agreement).

4.2 Procedures Relating to Indemnification of Tax Claims. If a claim for Taxes shall be made by any Tax authority in writing, which, if successful, might result in an indemnity payment to Buyer pursuant to Section 4.1 hereof, Buyer shall promptly notify the Seller in writing of such claim (a "Tax Claim").

With respect to any Tax Claim which might result in an indemnity payment to Buyer pursuant to Section 4.1 hereof, Seller shall be entitled to control all proceedings taken in connection with such Tax Claim (including, without limitation, selection of counsel) and, without limiting the foregoing, may at its sole expense and, subject to the prior written consent of Buyers pursue or forego any and all administrative appeals, proceedings, hearings and conferences with any Tax authority with respect thereto, and, subject to the prior written consent of Buyer, either settle the Tax Claim, pay the Tax claimed and sue for a refund where applicable law permits such refund suits, or contest such Tax Claim in any permissible manner.

#### 4.3 Section 338(h)(10) Election.

(a) With respect to the acquisition of the Shares hereunder (A) Seller and Buyer shall, and Seller shall use its best efforts to cause the Selling Consolidated Group to, jointly make a valid, timely and effective election under Section 338(h)(10) of the Code for the Company and all of its domestic Subsidiaries (the "Election"), (ii) the Selling Consolidated Group and the Buyer shall, as promptly as practicable following the Stock Acquisition, cooperate with each other to take all actions necessary and appropriate (including filing such forms, returns, elections, schedules and other documents as may be required) to effect and preserve a timely Election in accordance with the provisions of Treasury Regulation 1.338(h)(10)-1 or any successor provisions and (iii) Selling Consolidated Group and the Buyer shall report the sale of the Shares pursuant to this Agreement consistent with the Election and shall take no position to the contrary thereto in any Tax Return or any proceeding before any taxing authority; provided, however, the Election (or the equivalent thereof) shall not be made by the parties under the laws of any state or local jurisdiction, unless such election (or its equivalent) is under such state or local jurisdiction mandatory as a consequence of the Election having been made for U.S. Federal income tax purposes.

(b) In connection with the Election, Buyer and Seller and the Selling Consolidated Group will cooperate in good faith to establish the Adjusted grossed-up basis and the modified Aggregate Deemed Sales Price (each as defined under applicable U.S. Treasury Regulations), and, the allocation of the modified Aggregate Deemed Sales Price among the assets of Company. The allocations of the Adjusted grossed-up basis and the modified Aggregate Deemed Sales Price shall be made in accordance with Section 338 of the Code and any applicable U.S. Treasury Regulations. The Selling Consolidated Group and the Buyer (A) shall be bound by such allocations for purposes of determining any U.S. Federal Taxes; (B) shall prepare and file all U.S. Federal Tax Returns to be filed with any taxing authority in a manner consistent with such allocations; and (C) shall take no position inconsistent with such allocations in any U.S. Federal Tax Return, or any proceeding before any taxing authorities except as described in 4.3(a) above. In the event that such allocations are disputed by any taxing authorities, the party receiving notice of such dispute shall promptly notify and consult with the other party hereto concerning resolution of such dispute.

4.4 Survival of Tax Provisions. Any claim to be made pursuant to Sections 4.1 through 4.3 hereof must be made no later than sixty (60) days after the expiration (with valid extensions) of the applicable statute of limitations, if any, relating to the U.S. Federal income taxes at issue.

4.5 Real Property Taxes. Real property Taxes, if any, of Company and its Subsidiaries shall be treated as imposed on the Company or the Subsidiary as the case may be.

4.6 Tax Return Filings.

(a) Seller and SDG&E, as the case may be (the "Seller Filing Parties"), shall prepare or cause to be prepared and file or cause to be filed on a timely basis (in each case, at its own cost and expense and in a manner consistent with past practice) all U.S. Federal income Tax Returns with respect to Company and its Subsidiaries for taxable periods ending on or prior to the close of the Pre-Stock Acquisition Period. Seller and SDG&E shall pay all U.S. Federal income taxes shown on all such U.S. Federal income Tax Returns.

(b) Buyer shall prepare or cause to be prepared and shall file or cause to be filed on a timely basis all other Tax Returns with respect to Company and its Subsidiaries.

(c) The parties hereto shall reasonably cooperate, and shall cause their respective Affiliates, officers, employees, agents, auditors and representatives reasonably to cooperate, in preparing and filing all Tax Returns (including amended returns and claims for refund), including maintaining and making available to each other all records necessary in connection with taxes and in resolving all disputes and audits with respect to all taxable periods relating to taxes. The parties hereto recognize that Seller and its Affiliates may need access, from time to time, after the close of the Pre-Stock Acquisition Period, to certain accounting and tax records and information held by Company to the extent such records and information pertain to events occurring prior to the close of the Pre-Stock Acquisition Period; therefore, Buyer agrees that from and after the close of the Pre-Stock Acquisition Period until the expiration of the applicable statute of limitations, Buyer shall, and shall cause Company to (A) properly retain and maintain such records and (B) allow Seller to inspect, review and make copies of such records as Seller may reasonably deem necessary or appropriate from time to time, such activities to be conducted during normal business hours and at the expense of the requesting party.

4.7 Termination of Tax Sharing Agreements. The parties hereby agree and covenant that, upon the Stock Acquisition, all rights and obligations of each of Company and its Subsidiaries and Seller pursuant to any tax sharing agreement or similar arrangements shall be terminated as of the close of business on December 31, 1994, and no payments pursuant to any such tax sharing agreement or arrangements shall be made after such termination.



ARTICLE V

CONDITIONS OF CLOSING

5.1 Conditions of Obligations of the Buyer. The obligations of the Buyer to close this Agreement are subject to the satisfaction of each of the following conditions, unless any such condition is (to the extent that the same can be) waived by the Buyer:

(a) Representations and Warranties. The representations and warranties of the Seller set forth in Section 2.1 shall be true and correct in all material respects as of the date of this Agreement and as of the Closing Date as though made on and as of the Closing Date, except as otherwise contemplated by this Agreement; and the Buyer shall have received a certificate to that effect signed by the Seller.

(b) Performance of Obligations. The Seller shall have performed in all material respects the obligations required to be performed by it under this Agreement prior to and at the Closing, including without limitation, the Seller's delivery to the Escrow Agent in accordance with the Escrow Agreement of one or more stock certificates representing the Shares, duly endorsed in blank by the Seller; and the Buyer shall have received certificates to that effect signed by the Seller.

(c) Authorization. All corporate action necessary to authorize the execution, delivery and performance of this Agreement and the consummation of the transactions contemplated hereby shall have been duly and validly taken by the Seller, and the Seller shall have all necessary corporate power and authority to consummate the transactions contemplated hereby.

(d) Absence of Changes. There shall not have occurred any material adverse change in the business, operations, financial condition, results of operations, assets or liabilities of the Company after the date hereof.

(e) Covenants and Approvals. The Buyer shall have received duly executed copies of all consents and approvals contemplated by Section 2.1(b) hereof (and Schedule 1 attached hereto), in form and substance reasonably satisfactory to the Buyer and Messrs. Berlack, Israels & Liberman, counsel to the Buyer.

(f) Government Consents, Authorizations, Etc. All consents, authorizations, orders or approvals of, and filings or registrations with, any Federal, state, local or foreign governmental commission, board or other regulatory body which are required for or in connection with the execution, delivery and performance by the Seller, as applicable, of this Agreement, of the transactions contemplated hereby shall have been obtained or made,

except for a notification filing under the H-S-R Act and the expiration of the applicable waiting period, including any extension thereof, thereunder.

(g) Escrow Agreement. The Seller and the Escrow Agent shall have executed and delivered the Escrow Agreement.

(h) Opinions of Counsel. The Buyer shall have received an opinion dated the Closing Date of Messrs. Gibson, Dunn & Crutcher, counsel to the Seller, and an opinion of O'Melveny & Myers, counsel to the Company, in each case satisfactory in scope and substance to the Buyer and Messrs. Berlack, Israels & Liberman, counsel to the Buyer, to the same effect as Exhibits A and B, attached hereto, respectively.

(i) Representation Letter. The Company shall have delivered to the Buyer a letter setting forth certain representations and warranties of the Company, such letter to be satisfactory in scope and substance to the Buyer.

(j) Commitment Letter. The Buyer and the Company shall have entered into a commitment letter ("Commitment Letter") setting forth the terms upon which the parties agree that the Buyer shall commit to provide the Company with a secured term loan in a principal amount not to exceed \$2,000,000.

(k) Lender Consents. The Bank of America and Sanwa Bank shall each have delivered its written consent, in form satisfactory to the Buyer, to the transactions contemplated hereby and by the Commitment Letter including the Stock Acquisition and the creation of any liens on collateral required by the transactions contemplated by the Commitment Letter, in form satisfactory to the Buyer.

(l) Non-Foreign Status. At or prior to Closing, Seller will furnish Buyer with an affidavit prepared in accordance with section 1445(b) of the Code and applicable U.S. Treasury Regulations stating, under penalties of perjury, that Seller is not a foreign person and setting forth Seller's U.S. taxpayer identification number.

5.2 Conditions to Obligations of the Seller. The obligations of the Seller to close this Agreement are subject to the satisfaction of each of the following conditions unless waived by the Seller:

(a) Representations and Warranties. The representations and warranties of the Buyer set forth in Section 2.2 shall be true and correct in all material respects as of the date of this Agreement and as of the Closing Date as though made on and as of the Closing Date, except as otherwise contemplated by

this Agreement; and the Seller shall have received certificates to that effect signed by the Buyer.

(b) Performance of Obligations. The Buyer shall have performed in all material respects the obligations required to be performed by it under this Agreement prior to and at the Closing, including without limitation, payment of the Purchase Price, and the Seller shall have received a certificate to that effect signed by the corporate secretary of the Buyer.

(c) Authorization. All corporate action necessary to authorize the execution, delivery and performance of this Agreement and the consummation of the transactions contemplated hereby shall have been duly and validly taken by the Board of Directors of the Buyer, and the Buyer shall have full power to consummate the transactions contemplated hereby and thereby.

(d) Opinion of Counsel to the Buyer. The Seller shall have received an opinion dated the Closing Date of Messrs. Berlack, Israels & Liberman, counsel to the Buyer, satisfactory in scope and substance to the Seller and Messrs. Gibson, Dunn & Crutcher, counsel to the Seller, to the same effect as Exhibit C attached hereto.

## ARTICLE VI

### INDEMNIFICATION

6.1 Indemnification by the Seller. Except for Heller Claims (as hereinafter defined) and Tax Claims, the Seller shall indemnify and hold the Buyer harmless, from, against, for and in respect of any and all damages, losses, obligations, liabilities, claims, actions or causes of action (including, without limitation, reasonable attorneys' fees and expenses) sustained or suffered by the Buyer arising from the untruth, inaccuracy or breach of any representation, warranty, covenant or agreement of the Seller contained in or made pursuant to this Agreement or in any certificate, instrument or agreement delivered by the Seller pursuant hereto or in connection with the transactions contemplated hereby, or any facts or circumstances constituting such breach. No claim, demand, suit or cause of action shall be brought against the Seller under or pursuant to this Section 6.1 unless the Buyer at any time prior to the Survival Date, as defined below, gives the Seller written notice, with reasonable specificity, of the existence of any such claim, demand, suit or cause of action. Upon the giving of such written notice as aforesaid, the Buyer shall have the right to commence legal proceedings within 60 days thereafter for the enforcement of its rights under this Agreement.

6.2 Indemnification by the Indemnitor. Except for Heller Claims, from and after the date of the Stock Acquisition,

the Indemnitor shall indemnify and hold the Seller harmless, from, against, for and in respect of any and all damages, losses, obligations, liabilities, claims, actions or causes of action (including, without limitation, reasonable attorneys' fees and expenses) sustained or suffered by the Seller arising from the untruth, inaccuracy or breach of any representation, warranty, covenant or agreement of the Buyer contained in or made pursuant to this Agreement or in any certificate, instrument or agreement delivered by the Buyer pursuant hereto or in connection with the transactions contemplated hereby, or any facts or circumstances constituting such breach. No claim, demand, suit or cause of action shall be brought against the Indemnitor under or pursuant to this Section 6.2 unless the Seller, at any time prior to the Survival Date, as defined below, gives the Buyer written notice, with reasonable specificity, of the existence of any such claim, demand, suit or cause of action. Upon the giving of such written notice as aforesaid, the Seller shall have the right to commence legal proceedings within 60 days thereafter for the enforcement of its rights under this Agreement.

6.3 Defense of Claims. The obligations and liabilities of the Seller to indemnify the Buyer and the Indemnitor to indemnify the Seller under this Article VI with respect to claims relating to third parties shall be subject to the following terms and conditions:

(a) The party or parties to be indemnified (whether one or more, the "Indemnified Party") will give the Indemnitor or the Seller, as the case may be (the "Indemnifying Party") prompt written notice of any such claim, and the Indemnifying Party will undertake the defense thereof by representatives chosen by it. Failure to give such notice shall not affect the Indemnifying Party's duty or obligations under this Article VI, except to the extent the Indemnifying Party is prejudiced thereby. So long as the Indemnifying Party is defending any such claim actively and in good faith, the Indemnified Party shall not settle such claim. The Indemnified Party shall make available to the Indemnifying Party or its representatives all records and other materials required by them and in the possession or under the control of the Indemnified Party, for the use of the Indemnifying Party and its representatives in defending any such claim, and shall in other respects give reasonable cooperation in such defense.

(b) If the Indemnifying Party, within a reasonable time after notice of any such claim, fails to defend such claim actively and in good faith, the Indemnified Party will (upon further notice) have the right to undertake the defense, compromise or settlement of such claim or consent to the entry of a judgment with respect to such claim, on behalf of and for the account and risk of the Indemnifying Party, and the Indemnifying Party shall thereafter have no right to challenge the Indemnified Party's defense, compromise, settlement or consent to judgment therein,

provided, however, that no such failure to defend shall be deemed an admission that such claim is subject to indemnification hereunder.

(c) Anything in this Section 6.3 to the contrary notwithstanding, (i) if there is a reasonable probability that a claim may materially and adversely affect the Indemnified Party other than as a result of money damages or other money payments, the Indemnified Party shall have the right to defend, compromise or settle such claim, and (ii) the Indemnifying Party shall not, without the written consent of the Indemnified Party, settle or compromise any claim or consent to the entry of any judgment which does not include as an unconditional term thereof the giving by the claimant or the plaintiff to the Indemnified Party of a release from all liability in respect of such claim;

6.4 Heller Claims. Any claims made by Heller Financial, Inc. or its affiliates ("Heller") arising from or relating to prior negotiations among Heller, the Seller and the Company shall be split between the Seller and the Company as follows: (i) the first \$135,000 of such claims shall be paid solely by the Seller; (ii) the next \$500,000 of such claims shall be split 50% each between the Seller and the Company; and (iii) all claims in excess of (i) and (ii) above (the "Excess Claims") (i.e., in excess of the first \$635,000 in claims) shall be paid solely by the Seller, and the Seller hereby agrees to indemnify Indemnitor, the Buyer, WES and their affiliates against all such excess claims. Upon the Stock Acquisition, Indemnitor shall indemnify the Seller and its affiliates from claims of Heller that the Company has agreed to pay as set forth in clause (ii) of the preceding sentence. The Seller and the Company hereby agree to reasonably cooperate in deciding upon, and agreeing with respect to, (i) what claims of Heller, if any, should be paid by the Seller and the Company, (ii) the amount to be paid in settlement of such claims, and (iii) the conduct and defense of such claims.

6.5 Remedies Cumulative. The remedies provided for in this Article VI shall be cumulative and shall not preclude assertion by the Buyer or the Seller of any other rights or the seeking of any other remedies against the Seller or the Buyer respectively.

## ARTICLE VII

### SURVIVAL OF REPRESENTATION AND WARRANTIES; AMENDMENT, MODIFICATION AND WAIVER

7.1 Survival of Representations and Warranties, Etc. The representations and warranties of the Seller and the Buyer contained in this Agreement shall under all circumstances survive the Closing for a period of 24 months. The agreements of the

Seller, Buyer and Indemnitor contained in this Agreement shall in each case survive the Closing until they are otherwise terminated, whether by their terms or as a matter of applicable law. The respective dates upon which the representations and warranties and agreements contained in this Agreement shall expire, shall be referred to herein as the "Survival Date".

7.2 Amendment, Modification and Waiver. This Agreement shall not be altered or otherwise amended except pursuant to an instrument in writing signed by the parties hereto, except that any party to this Agreement may waive any obligation owed to it by another party under this Agreement. The waiver by any party hereto of a breach of any provision of this Agreement shall not operate or be construed as a waiver of any subsequent breach.

## ARTICLE VIII

### TERMINATION

8.1 Right of Termination. This Agreement may be terminated at any time prior to the Closing by:

(a) The mutual written consent of the Buyer and the Seller; or

(b) The Buyer, by delivery of a written notice specifying the reasons for such termination, if the conditions set forth in Section 5.1 hereof shall not have been met (or shall not, in the reasonable judgment of the Buyer, be capable of being met); or

(c) The Seller, by delivery of a written notice specifying the reasons for such termination, if the conditions set forth in Section 5.2 hereof shall not have been met (or shall not, in the reasonable judgment of the Seller, be capable of being met).

8.2 Effect of Termination. If this Agreement shall be terminated by the mutual consent of the Buyer and the Seller pursuant to Section 8.1(a), then neither party shall have any claim or right of action against the other party for breach of this Agreement. If this Agreement shall be terminated by the Buyer pursuant to Section 8.1(b), then the Buyer may bring a suit or proceeding against the Seller only for a breach of the obligations of the Seller contained in this Agreement or a breach by the Seller of the representations, warranties or covenants of the Seller contained in this Agreement which occurred prior to the date of such termination. If this Agreement shall be terminated by the Seller pursuant to Section 8.1(c), then the Seller may bring a suit or proceeding against the Buyer for the Buyer's breach of the obligations of the Buyer contained in this Agreement or a breach by

the Buyer of the representations, warranties or covenants of the Buyer contained in this Agreement which occurred prior to the date of such termination.

## ARTICLE IX

### MISCELLANEOUS

9.1 Expenses. Each party shall bear its own expenses in connection with this transaction, except that the Buyer may have its expenses reimbursed by the Company after the Stock Acquisition.

9.2 Entire Agreement. This Agreement and the Exhibits and Schedules attached hereto contain the entire agreement among the parties hereto with respect to the transactions contemplated hereby and supersede all prior agreements or understandings among the parties with respect thereto.

9.3 Publicity. The parties hereto agree that, except as otherwise required by law, they will advise and confer with each other prior to the issuance of any public reports, statements or releases pertaining to this Agreement or the transactions contemplated hereby.

9.4 Descriptive Headings. Descriptive headings are for convenience only and shall not control or affect the meaning or construction of any provision of this Agreement.

9.5 Notices. all notices or other communications which are required or permitted hereunder shall be in writing and sufficient if delivered personally or sent by registered or certified mail, postage prepaid, return receipt requested, addressed as follows:

If to the Buyer or the Indemnitor, to:

Wexford Capital Corporation  
411 West Putnam Avenue  
Greenwich, Connecticut 06830  
Attention: Robert M. Davies

with copies to:

Berlack, Israels & Liberman  
120 West 45th Street  
New York, New York 10036  
Attention: Stephen B. Selbst, Esq.

If to the Seller, to:

Pacific Diversified Capital Company  
101 Ash Street  
San Diego, California 92101  
Attention: Stephen L. Baum, President

with a copy to:

Gibson, Dunn & Crutcher  
333 South Grand Street  
Los Angeles, California 90071  
Attention: Richard Strong, Esq.

If to the Company:

Wahlco Environmental Systems, Inc.  
3600 West Segerstrom Avenue  
Santa Ana, California 92704-6495  
Attention: Henry N. Huta

with a copy to:

O'Melveny & Myers  
610 Newport Center Drive  
Suite 1700  
Newport Beach, California 92660  
Attention: David Krinsky, Esq.

or to such other address as the party to whom notice is to be given may have furnished to the other party in writing in accordance herewith. any such communication shall be deemed to have been given, in the case of personal delivery, on the date of delivery and in the case of mailing, on the third business day following that on which the piece of mail containing such communication is posted.

9.6 Counterparts. This Agreement may be executed in any number of counterparts, and each such counterpart hereof shall be deemed to be an original instrument, but all such counterparts together shall constitute but one agreement.

9.7 Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of New York.

9.8 Benefits of Agreement. All the terms and provisions of this Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns. Anything contained herein to the contrary notwithstanding, this Agreement shall not be assignable by the Seller without the consent of the Buyer. The Buyer may assign this Agreement without the



consent of the Seller, provided that such assignment shall not release the Buyer from its obligations under this Agreement.

IN WITNESS WHEREOF, each of the parties has caused this Agreement to be executed on the day and year first above written.

WES ACQUISITION CORP.

By: \_\_\_\_\_  
Name:  
Title:

PACIFIC DIVERSIFIED CAPITAL COMPANY

By: \_\_\_\_\_  
Name:  
Title:

WEXFORD CAPITAL CORPORATION,  
as Indemnitor

By: \_\_\_\_\_  
Name:  
Title:



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