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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q  
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE  
SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended September 30, 2008  
Commission file number 1-14201

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SEMPRA ENERGY

(Exact name of registrant as specified in its charter)

California

33-0732627

(State or other jurisdiction of incorporation or  
organization)

(I.R.S. Employer Identification No.)

101 Ash Street, San Diego, California 92101

(Address of principal executive offices)  
(Zip Code)

(619) 696-2034

(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 Section 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  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

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

Common stock outstanding on November 6, 2008: 243,630,682

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## INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report contains statements that are not historical fact and constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words "believes," "expects," "anticipates," "plans," "estimates," "projects," "contemplates," "intends," "depends," "should," "could," "would," "may," "potential," "target," "goals," or similar expressions, or discussions of strategy or of plans are intended to identify forward-looking statements. Forward-looking statements are necessarily based upon assumptions with respect to the future, involve risks and uncertainties and are not guarantees of performance. Factors, among others, that could cause the company's actual results and future actions to differ materially from those described in forward-looking statements include:

- local, regional, national and international economic, competitive, political, legislative and regulatory conditions and developments;
- actions by the California Public Utilities Commission, the California State Legislature, the California Department of Water Resources, the Federal Energy Regulatory Commission, the Federal Reserve Board, the U.K. Financial Services Authority and other regulatory bodies in the United States and other countries;
- capital markets conditions, inflation rates, interest rates and exchange rates;
- energy and trading markets, including the timing and extent of changes in commodity prices;
- the availability of electric power, natural gas and liquefied natural gas;
- weather conditions and conservation efforts;
- war and terrorist attacks;
- business, regulatory, environmental and legal decisions and requirements;
- the status of deregulation of retail natural gas and electricity delivery;
- the timing and success of business development efforts;
- the resolution of litigation; and
- other uncertainties, all of which are difficult to predict and many of which are beyond the control of the company.

Readers are cautioned not to rely unduly on any forward-looking statements and are urged to review and consider carefully the risks, uncertainties and other factors which affect the company's business described in this report and other reports filed by the company from time to time with the Securities and Exchange Commission. These forward-looking statements represent the company's estimates and assumptions only as of the date of this report.

PART I. FINANCIAL INFORMATION  
ITEM I. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

SEMPRA ENERGY  
STATEMENTS OF CONSOLIDATED INCOME

(Dollars in millions, except per share amounts)	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
	(unaudited)			
<b>REVENUES</b>				
Sempra Utilities	\$ 2,013	\$ 1,515	\$ 6,190	\$ 5,194
Sempra Global and parent	679	1,148	2,275	3,134
<b>Total revenues</b>	<b>2,692</b>	<b>2,663</b>	<b>8,465</b>	<b>8,328</b>
<b>EXPENSES AND OTHER INCOME</b>				
Sempra Utilities:				
Cost of natural gas	(689)	(389)	(2,708)	(2,042)
Cost of electric fuel and purchased power	(311)	(184)	(694)	(496)
Sempra Global and parent:				
Cost of natural gas, electric fuel and purchased power	(431)	(331)	(1,353)	(945)
Other cost of sales	(15)	(256)	(168)	(796)
Operation and maintenance	(564)	(758)	(1,816)	(2,140)
Depreciation and amortization	(162)	(174)	(508)	(514)
Franchise fees and other taxes	(76)	(72)	(230)	(221)
Gains on sale of assets	--	--	114	6
Equity earnings (losses):				
RBS Sempra Commodities LLP	(4)	--	142	--
Other	14	1	29	(11)
Other income (expense), net	(13)	4	23	72
Interest income	12	12	36	62
Interest expense	(67)	(68)	(165)	(204)
Preferred dividends of subsidiaries	(2)	(2)	(7)	(7)
Income from continuing operations before income taxes and equity earnings of certain unconsolidated subsidiaries	384	446	1,160	1,092
Income tax expense	(94)	(135)	(423)	(341)
Equity earnings, net of income tax	18	19	57	86
Income from continuing operations	308	330	794	837
Discontinued operations, net of income tax	--	(25)	--	(27)
<b>Net income</b>	<b>\$ 308</b>	<b>\$ 305</b>	<b>\$ 794</b>	<b>\$ 810</b>
Basic earnings per share:				
Income from continuing operations	\$ 1.26	\$ 1.27	\$ 3.18	\$ 3.23
Discontinued operations, net of income tax	--	(0.10)	--	(0.11)
<b>Net income</b>	<b>\$ 1.26</b>	<b>\$ 1.17</b>	<b>\$ 3.18</b>	<b>\$ 3.12</b>
Weighted-average number of shares outstanding (thousands)	243,793	259,563	249,311	259,742
Diluted earnings per share:				
Income from continuing operations	\$ 1.24	\$ 1.24	\$ 3.13	\$ 3.16
Discontinued operations, net of income tax	--	(0.09)	--	(0.10)
<b>Net income</b>	<b>\$ 1.24</b>	<b>\$ 1.15</b>	<b>\$ 3.13</b>	<b>\$ 3.06</b>
Weighted-average number of shares outstanding (thousands)	247,904	264,279	253,407	264,416
<b>Dividends declared per share of common stock</b>	<b>\$ 0.35</b>	<b>\$ 0.31</b>	<b>\$ 1.02</b>	<b>\$ 0.93</b>

See Notes to Condensed Consolidated Financial Statements.

SEMPRA ENERGY  
CONSOLIDATED BALANCE SHEETS

(Dollars in millions)	September 30, 2008	December 31, 2007 *
	(unaudited)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 198	\$ 668
Short-term investments	413	--
Trade accounts receivable, net	675	960
Other accounts and notes receivable, net	121	114
Income taxes receivable	189	99
Deferred income taxes	150	247
Trading-related receivables and deposits, net	--	2,719
Derivative trading instruments	--	2,170
Commodities owned	--	2,231
Inventories	461	224
Regulatory assets	119	106
Fixed-price contracts and other derivatives	91	28
Other	153	398
Total current assets	2,570	9,964
Investments and other assets:		
Regulatory assets arising from fixed-price contracts and other derivatives	281	309
Regulatory assets arising from pension and other postretirement benefit obligations	144	162
Other regulatory assets	499	460
Nuclear decommissioning trusts	636	739
Investment in RBS Sempra Commodities LLP	1,912	--
Other investments	1,247	1,243
Sundry	746	956
Total investments and other assets	5,465	3,869
Property, plant and equipment:		
Property, plant and equipment	22,028	20,917
Less accumulated depreciation and amortization	(6,214)	(6,033)
Property, plant and equipment, net	15,814	14,884
Total assets	\$ 23,849	\$ 28,717

See Notes to Condensed Consolidated Financial Statements.

\* As adjusted for the retrospective adoption of FASB Staff Position FIN 39-1.

SEMPRA ENERGY  
CONSOLIDATED BALANCE SHEETS

(Dollars in millions)	September 30, 2008	December 31, 2007 *
	(unaudited)	
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Short-term debt	\$ 319	\$ 1,064
Accounts payable - trade	569	1,374
Accounts payable - other	174	189
Due to unconsolidated affiliates	37	60
Trading-related payables	--	2,265
Derivative trading instruments	--	1,672
Commodities sold with agreement to repurchase	--	500
Dividends and interest payable	164	145
Regulatory balancing accounts, net	264	481
Accrued compensation and benefits	248	265
Current portion of long-term debt	302	7
Fixed-price contracts and other derivatives	175	53
Customer deposits	158	143
Other	725	802
Total current liabilities	3,135	9,020
Long-term debt	5,864	4,553
Deferred credits and other liabilities:		
Due to unconsolidated affiliate	102	102
Customer advances for construction	153	153
Pension and other postretirement benefit obligations, net of plan assets	412	434
Deferred income taxes	799	531
Deferred investment tax credits	58	61
Regulatory liabilities arising from removal obligations	2,420	2,522
Asset retirement obligations	1,165	1,129
Other regulatory liabilities	234	265
Fixed-price contracts and other derivatives	315	332
Deferred credits and other	911	949
Total deferred credits and other liabilities	6,569	6,478
Preferred stock of subsidiaries	179	179
Minority interests	204	148
Commitments and contingencies (Note 8)		
Shareholders' equity:		
Preferred stock (50 million shares authorized; none issued)	--	--
Common stock (750 million shares authorized; 247 million and 261 million shares outstanding at September 30, 2008 and December 31, 2007, respectively; no par value)	2,265	3,198
Retained earnings	6,001	5,464
Deferred compensation	(19)	(22)
Accumulated other comprehensive income (loss)	(349)	(301)
Total shareholders' equity	7,898	8,339
Total liabilities and shareholders' equity	\$ 23,849	\$ 28,717

See Notes to Condensed Consolidated Financial Statements.

\* As adjusted for the retrospective adoption of FASB Staff Position FIN 39-1.

SEMPRA ENERGY  
CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS

(Dollars in millions)	Nine months ended September 30,	
	2008	2007
	(unaudited)	
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 794	\$ 810
Adjustments to reconcile net income to net cash provided by operating activities:		
Discontinued operations	--	27
Depreciation and amortization	508	514
Deferred income taxes and investment tax credits	165	42
Equity earnings	(228)	(75)
Gains on sale of assets	(114)	(6)
Fixed-price contracts and other derivatives	7	8
Tax benefits from share-based awards	(7)	(12)
Other	83	37
Net change in other working capital components	(408)	131
Distribution from RBS Sempra Commodities LLP	56	--
Changes in other assets	(3)	35
Changes in other liabilities	(55)	63
Net cash provided by continuing operations	798	1,574
Net cash used in discontinued operations	--	(3)
Net cash provided by operating activities	798	1,571
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Expenditures for property, plant and equipment	(1,541)	(1,357)
Proceeds from sale of assets, net of cash sold	2,071	77
Expenditures for investments	(2,180)	(17)
Distributions from investments	23	13
Purchases of nuclear decommissioning and other trust assets	(361)	(498)
Proceeds from sales by nuclear decommissioning and other trusts	350	458
Decrease in notes receivable from unconsolidated affiliates	60	--
Other	(18)	(19)
Net cash used in investing activities	(1,596)	(1,343)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Common dividends paid	(252)	(234)
Issuances of common stock	17	36
Repurchases of common stock	(1,002)	(161)
Increase in short-term debt, net	985	954
Issuance of long-term debt	650	359
Payments on long-term debt	(75)	(1,069)
Tax benefits from share-based awards	7	12
Other	(2)	(2)
Net cash provided by (used in) financing activities	328	(105)
Increase (decrease) in cash and cash equivalents	(470)	123
Cash and cash equivalents, January 1	668	920
Cash assumed in connection with FIN 46(R) consolidation	--	29
Cash and cash equivalents, September 30	\$ 198	\$ 1,072

See Notes to Condensed Consolidated Financial Statements.

SEMPRA ENERGY  
CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS

(Dollars in millions)	Nine months ended September 30,	
	2008	2007
	(unaudited)	
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Interest payments, net of amounts capitalized	\$ 142	\$ 273
Income tax payments, net of refunds	\$ 120	\$ 316
<b>SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING ACTIVITY</b>		
Increase (decrease) in accounts payable from investments in property, plant and equipment	\$ (41)	\$ 41
Fair value of stock received for services rendered	\$ --	\$ 32
Fair value of stock received for sale of investments	\$ --	\$ 26

See Notes to Condensed Consolidated Financial Statements.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 1. GENERAL

#### Principles of Consolidation

The Condensed Consolidated Financial Statements include the accounts of Sempra Energy (the company), a California-based Fortune 500 holding company, its consolidated subsidiaries and a variable interest entity of which it is the primary beneficiary. Sempra Energy's principal subsidiaries are San Diego Gas & Electric Company (SDG&E) and Southern California Gas Company (SoCalGas) (collectively referred to as the Sempra Utilities) and Sempra Global, which is the holding company for Sempra Commodities, Sempra Generation, Sempra Pipelines & Storage, Sempra LNG and other, smaller businesses. Investments in affiliated companies (primarily RBS Sempra Commodities LLP) over which Sempra Energy has the ability to exercise significant influence, but not control, are accounted for using the equity method. On April 1, 2008, substantially all of the company's commodity-marketing businesses were sold to RBS Sempra Commodities LLP (RBS Sempra Commodities), a partnership of the company and The Royal Bank of Scotland (RBS). Additional information regarding the transaction is provided in Note 3.

#### Basis of Presentation

The Condensed Consolidated Financial Statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) and in accordance with the interim-period-reporting requirements of Form 10-Q. Results of operations for interim periods are not necessarily indicative of results for the entire year. In the opinion of management, the accompanying statements reflect all adjustments necessary for a fair presentation. These adjustments are only of a normal, recurring nature.

Information in this Quarterly Report should be read in conjunction with the company's Annual Report on Form 10-K for the year ended December 31, 2007 (the Annual Report) and its Quarterly Reports on Form 10-Q for the quarters ended March 31, 2008 and June 30, 2008.

The company's significant accounting policies are described in Note 1 of the Notes to Consolidated Financial Statements in the Annual Report. The same accounting policies are followed for interim reporting purposes, except for the adoption of new accounting standards as discussed in Note 2.

The Sempra Utilities account for the economic effects of regulation on utility operations in accordance with Statement of Financial Accounting Standards (SFAS) 71, *Accounting for the Effects of Certain Types of Regulation*.

### NOTE 2. NEW ACCOUNTING STANDARDS

Recently issued pronouncements that have had or may have a significant effect on the company's financial statements are described below.

**SFAS 161, "Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133" (SFAS 161):** SFAS 161 expands the disclosure requirements in Financial Accounting Standards Board (FASB) Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133). SFAS 161 requires qualitative disclosures about

objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The company is in the process of evaluating the effect of this statement on its financial statement disclosures.

**FASB Staff Position (FSP) FASB Interpretation (FIN) No. 39-1, "Amendment of FASB Interpretation No. 39" (FSP FIN 39-1):** FSP FIN 39-1 amends FASB Interpretation No. 39, *Offsetting of Amounts Related to Certain Contracts*, to permit a reporting entity to offset fair value amounts recognized for the right to reclaim or the obligation to return cash collateral against fair value amounts recognized for derivative instruments executed with the same counterparty under the same master netting arrangement. The company adopted FSP FIN 39-1 effective January 1, 2008. The company applied FSP FIN 39-1 as a change in accounting principle through retrospective application. Each consolidated balance sheet herein reflects the offsetting of net derivative positions with fair value amounts for cash collateral with the same counterparty when management believes a legal right of setoff exists. Accordingly, December 31, 2007 amounts have been reclassified to conform to this presentation. Additional disclosure is provided in Note 6.

**FSP FAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset is Not Active" (FSP FAS 157-3):** FSP FAS 157-3 clarifies and illustrates the application of FASB Statement No. 157, *Fair Value Measurements*, for financial assets in an inactive market. FSP FAS 157-3 became effective upon issuance on October 10, 2008, and applies to periods for which financial statements have not been issued. Revisions to the fair value estimates resulting from the adoption of the FSP are to be accounted for as a change in estimate, so that any effects on the fair value measurements would be recognized in the period of adoption. The company's application of FSP FAS 157-3 impacted neither financial asset fair values nor their classification in the fair value hierarchy. Additional disclosure is provided in Note 6.

**FSP Emerging Issues Task Force (EITF) 03-6-1, "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities" (FSP EITF 03-6-1):** FSP EITF 03-6-1 states that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and are required to be included in the computation of earnings per share (EPS) under the two-class method described in FASB Statement No. 128, *Earnings per Share*. FSP EITF 03-6-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008. All prior-period EPS data are to be adjusted retrospectively to conform with the provisions of this FSP. Early application is not permitted. The company does not expect the adoption of FSP EITF 03-6-1 to have a material impact on its EPS.

**FSP FAS 133-1 and FIN 45-4, "Disclosures about Credit Derivatives and Certain Guarantees: An Amendment of FASB Statement No. 133 and FASB Interpretation No. 45; and Clarification of the Effective Date of FASB Statement No. 161" (FSP FAS 133-1 and FIN 45-4):** FSP FAS 133-1 and FIN 45-4 amends FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*, to require sellers of credit derivatives to disclose information so that financial statement users can assess the potential effect of the instruments on the company's financial position, financial performance and cash flows. This FSP also amends FASB Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*, to require guarantors to disclose the current status of the guarantee's performance risk. The FSP is effective prospectively for annual or interim reporting periods ending after November 15, 2008. The company is a guarantor under

certain arrangements and is in the process of evaluating the effect of this statement on its financial statement disclosures.

**EITF 08-5, "Issuer's Accounting for Liabilities Measured at Fair Value With a Third-Party Credit Enhancement" (EITF 08-5):** EITF 08-5 provides that an issuer of a liability with a third-party credit enhancement that is inseparable from the liability may not include the effect of the credit enhancement in the fair value measurement of the liability. EITF 08-5 is effective prospectively for reporting periods beginning after December 15, 2008. The company does not expect the effects of adopting EITF 08-5 to have a material impact on its financial position or results of operations.

### NOTE 3. INVESTMENT IN UNCONSOLIDATED ENTITIES

#### RBS Sempra Commodities

On April 1, 2008, Sempra Energy and RBS completed the formation of RBS Sempra Commodities, a partnership of the company and RBS to own and operate the commodity-marketing businesses previously operated through wholly owned subsidiaries of Sempra Energy. The company's initial equity contribution to the partnership was \$1.6 billion. RBS made an initial equity contribution of \$1.665 billion and is committed to provide any additional funding required for the ongoing operations of the partnership's businesses. Additional information regarding this commitment is provided in Note 5. As a result of the transaction, the company received approximately \$1.2 billion in cash, net of the contribution and including cash withdrawn from the businesses in anticipation of the transaction, and recorded an after-tax gain of \$67 million.

Because the partnership was formed on April 1, 2008, the annual allocation of its earnings is prorated for three-fourths of 2008. For the three months and nine months ended September 30, 2008, the company recorded \$(4) million and \$142 million, respectively, of equity earnings (losses) before income tax from RBS Sempra Commodities. The partnership income that is distributable to the company on an annual basis is computed on the partnership's basis of accounting, International Financial Reporting Standards (IFRS) as adopted by the European Union. This distributable income, on an IFRS basis, was \$136 million for the nine months ended September 30, 2008. For the three months ended September 30, 2008, the distributable income was reduced by \$29 million. In September 2008, the company received a distribution of \$56 million from the partnership, as provided in the partnership agreement to fund estimated income tax payments.

Summarized income statement information for RBS Sempra Commodities, on a GAAP basis, is as follows (in millions):

	Three months ended September 30, 2008	Nine months ended September 30, 2008
Gross revenues and fee income	\$ 48	\$ 586
Gross profit	\$ 23	\$ 540
Income (loss) from continuing operations	\$ (56)	\$ 198
Partnership net income (loss)	\$ (56)	\$ 198

The company has indemnified the partnership for certain litigation and tax liabilities related to the businesses purchased by the partnership. The fair value of these indemnities at formation of the partnership was \$5 million.

Information regarding the Sempra Commodities segment at September 30, 2008 and December 31, 2007 and for the three and nine month periods ended September 30, 2008 and 2007 is provided in Note 9. Additional information concerning this transaction is provided in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Annual Report.

#### **NOTE 4. OTHER FINANCIAL DATA**

##### **Otay Mesa Energy Center**

SDG&E has a 10-year agreement to purchase power to be generated at the Otay Mesa Energy Center, a 573-megawatt (MW) generating facility currently under construction and expected to be in commercial operation in the fourth quarter of 2009. As defined in FIN 46 (revised December 2003), *Consolidation of Variable Interest Entities - an interpretation of ARB No. 51* (FIN 46(R)), the facility owner, Otay Mesa Energy Center LLC, is a variable interest entity (Otay Mesa VIE), of which SDG&E is the primary beneficiary. Accordingly, the company has consolidated Otay Mesa VIE beginning in the second quarter of 2007. Its equity of \$188 million and \$135 million as of September 30, 2008 and December 31, 2007, respectively, is classified as Minority Interest on the Consolidated Balance Sheets.

##### **Available-for-Sale Securities**

During the nine months ended September 30, 2008, Sempra Energy and SDG&E purchased \$345 million and \$68 million, respectively, of industrial development bonds. The bonds are classified as available-for-sale securities and included in Short-Term Investments on the Consolidated Balance Sheets at September 30, 2008.

Interest rates on these securities are reset by remarketing agents on a weekly basis at rates intended to permit the bonds to be remarketed at par. The bonds were initially issued as insured, auction-rate securities, the proceeds of which were loaned to SDG&E, and are repaid with payments from SDG&E first mortgage bonds that have terms corresponding to those of the industrial development bonds that they secure. SDG&E intends to modify the credit support and liquidity requirements of the bonds in conjunction with their subsequent remarketing to investors.

## Pension and Other Postretirement Benefits

The following tables provide the components of benefit costs:

(Dollars in millions)	Pension Benefits		Other Postretirement Benefits	
	Three months ended		Three months ended	
	September 30,		September 30,	
	2008	2007	2008	2007
Service cost	\$ 17	\$ 19	\$ 5	\$ 6
Interest cost	41	41	13	13
Expected return on assets	(40)	(40)	(12)	(11)
Amortization of:				
Prior service cost (credit)	1	2	--	(1)
Actuarial loss	2	2	--	--
Curtailment	--	--	(1)	--
Regulatory adjustment	15	--	(5)	4
<b>Total net periodic benefit cost</b>	<b>\$ 36</b>	<b>\$ 24</b>	<b>\$ --</b>	<b>\$ 11</b>

(Dollars in millions)	Pension Benefits		Other Postretirement Benefits	
	Nine months ended		Nine months ended	
	September 30,		September 30,	
	2008	2007	2008	2007
Service cost	\$ 53	\$ 58	\$ 18	\$ 20
Interest cost	124	123	40	41
Expected return on assets	(120)	(119)	(36)	(33)
Amortization of:				
Prior service cost (credit)	3	4	(1)	(3)
Actuarial loss	6	7	--	4
Curtailment	--	5	(3)	--
Special termination	--	1	--	--
Regulatory adjustment	(7)	(23)	(4)	7
<b>Total net periodic benefit cost</b>	<b>\$ 59</b>	<b>\$ 56</b>	<b>\$ 14</b>	<b>\$ 36</b>

The company expects to contribute \$74 million to its pension plans and \$34 million to its other postretirement benefit plans in 2008. For the nine months ended September 30, 2008, the company made contributions of \$47 million and \$16 million to the pension plans and other postretirement benefit plans, respectively, including \$32 million and a negligible amount, respectively, for the three months ended September 30, 2008.

## Common Stock

In April 2008, the company entered into a Collared Accelerated Share Acquisition Program under which the company prepaid \$1 billion to repurchase shares of its common stock in a share forward transaction. The total number of shares purchased (subject to a minimum and maximum number of shares) was determined by dividing the \$1 billion purchase price by the volume-weighted average trading prices of shares of Sempra Energy common stock during the valuation period, minus a fixed discount and subject to a minimum and maximum price set during a hedging period. The valuation period began on April 7, 2008 and ended on October 13, 2008.

The company's outstanding shares used to calculate earnings per share are reduced by the number of shares repurchased as they are delivered to the company, and the \$1 billion purchase price was recorded as a reduction in shareholders' equity upon its prepayment. Through September 30, 2008, the company has received 15,407,961 shares, representing the minimum number of shares to be purchased under the program. Following the end of the valuation period, the company received 3,008,280 additional shares on October 16, 2008, representing the remaining shares deliverable under the program based on a final weighted average price of \$54.30 per share.

### **Earnings per Share (EPS)**

Diluted EPS for the three months ended September 30, 2008 and 2007 reflects the inclusion of 4,111,000 and 4,716,000, respectively, additional shares in the weighted-average shares outstanding for the dilutive effect of stock options, restricted stock awards and restricted stock units. Diluted EPS for the nine months ended September 30, 2008 and 2007 reflects the inclusion of 4,096,000 and 4,674,000 additional shares, respectively, in the weighted-average shares outstanding for the dilutive effect of stock options and restricted stock awards and units.

The dilution from common stock options is based on the treasury stock method, whereby the proceeds from the exercise price and unearned compensation as defined by SFAS 123 (revised 2004), *Share-Based Payment* (SFAS 123(R)), are assumed to be used to repurchase shares on the open market at the average market price for the period. The calculation excludes stock options for which the exercise price was greater than the average market price for common stock during the period. There were 1,513,721 and 755,700 such stock options outstanding during the three months ended September 30, 2008 and 2007, respectively, and 1,494,935 and 29,754 such stock options outstanding during the nine months ended September 30, 2008 and 2007, respectively. The company had no outstanding stock options that were antidilutive due to the inclusion of unearned compensation in the assumed proceeds under the treasury stock method during the three and nine months ended September 30, 2008. The company had no such antidilutive stock options during the three months ended September 30, 2007 and 696,712 stock options outstanding during the nine months ended September 30, 2007, that were antidilutive due to the inclusion of unearned compensation in the assumed proceeds under the treasury method.

The dilution from unvested restricted stock awards and units is based on the treasury stock method, whereby assumed proceeds equivalent to the unearned compensation as defined by SFAS 123(R) related to the awards and units are assumed to be used to repurchase shares on the open market at the average market price for the period. There were 431,401 antidilutive restricted stock units and no antidilutive restricted stock awards during the nine months ended September 30, 2008. There were no antidilutive restricted stock awards or units outstanding during the three months ended September 30, 2008. There were no antidilutive restricted stock units or awards for the three and nine months ended September 30, 2007.

### **Share-Based Compensation**

Total share-based compensation expense, net of income tax, was \$22 million and \$21 million for the nine months ended September 30, 2008 and 2007, respectively. Pursuant to the company's share-based compensation plans, 783,500 non-qualified stock options and 643,250 restricted stock units were granted during the nine months ended September 30, 2008, primarily in January 2008.

As of September 30, 2008, 6,532,608 shares were authorized and available for future grants of share-based awards.

## Capitalized Interest

The company recorded \$26 million and \$84 million of capitalized interest for the three months and nine months ended September 30, 2008, respectively, including the debt-related portion of allowance for funds used during construction for the Sempra Utilities. The company recorded \$29 million and \$75 million of capitalized interest for the three months and nine months ended September 30, 2007, respectively, including the debt-related portion of allowance for funds used during construction.

## Comprehensive Income

The following is a reconciliation of net income to comprehensive income:

(Dollars in millions)	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
Net income	\$ 308	\$ 305	\$ 794	\$ 810
Foreign currency adjustments	(30)	12	(45)	19
Financial instruments	(2)	(4)	5	3
Available-for-sale securities	--	(9)	(12)	9
Net actuarial gain	1	(1)	5	9
Prior service cost	(1)	--	(1)	2
Comprehensive income	\$ 276	\$ 303	\$ 746	\$ 852

Amounts in the table above are net of income tax expense (benefit) as follows:

(Dollars in millions)	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
Financial instruments	\$ (3)	\$ (1)	\$ 2	\$ 6
Available-for-sale securities	--	(5)	(10)	6
Net actuarial gain	1	--	3	6
Prior service cost	--	--	--	2

## Other Income (Expense), Net

Other Income (Expense), Net consists of the following:

(Dollars in millions)	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
Allowance for equity funds used during construction	\$ 9	\$ 6	\$ 25	\$ 16
Regulatory interest, net	(2)	--	(8)	(12)
Sundry, net*	(20)	(2)	6	68
Total	\$ (13)	\$ 4	\$ 23	\$ 72

\* The nine-month period in 2007 includes \$23 million net gains from interest-rate swaps, as discussed in Note 6.

## NOTE 5. DEBT AND CREDIT FACILITIES

### Committed Lines of Credit

At September 30, 2008, the company had \$4.3 billion in committed lines of credit to provide liquidity and support commercial paper (the major components of which are detailed below). Available unused credit on these lines at September 30, 2008 was \$2.9 billion.

Due to the sale of the commodity-marketing businesses as discussed in Note 3, these amounts exclude lines of credit associated with Sempra Commodities, some of which continue to be guaranteed by the company, as discussed below in "RBS Sempra Commodities." As of May 2008, RBS has replaced Sempra Energy as guarantor on all uncommitted lines of credit associated with Sempra Commodities. Additional information concerning Sempra Commodities' committed and uncommitted credit facilities is provided in Note 6 of the Notes to Consolidated Financial Statements in the Annual Report.

#### *Sempra Global*

On August 15, 2008, Sempra Global entered into a \$2.5 billion, three-year syndicated revolving credit agreement expiring in 2011. Citibank, N.A. serves as administrative agent for the syndicate of 17 lenders. The facility also provides for issuance of up to \$300 million of letters of credit on behalf of Sempra Global with the amount of borrowings otherwise available under the facility reduced by the amount of outstanding letters of credit.

Sempra Global's obligations under the credit facility are guaranteed by Sempra Energy. Borrowings bear interest at benchmark rates plus a margin that varies with market index rates and Sempra Energy's credit ratings. The facility also requires Sempra Energy to maintain at the end of each quarter a ratio of total indebtedness to total capitalization (as defined in the agreement) of no more than 65%.

At September 30, 2008, Sempra Global had letters of credit of \$115 million outstanding and no outstanding borrowings under the facility. The facility provides support for \$1.2 billion of commercial paper outstanding at September 30, 2008. At September 30, 2008, \$1 billion of the commercial paper outstanding has been reclassified to long-term debt based on management's intent and ability to maintain this level of borrowing on a long-term basis either supported by this credit facility or by issuing long-term debt. This reclassification had no impact on cash flows.

#### *Sempra Generation*

On August 15, 2008, Sempra Generation entered into a \$1 billion, three-year syndicated revolving credit agreement expiring in 2011. Citibank, N.A. serves as administrative agent for the syndicate of 17 lenders.

Sempra Generation's obligations under the credit facility are guaranteed by Sempra Energy. Borrowings bear interest at benchmark rates plus a margin that varies with market index rates and Sempra Energy's credit ratings. The facility also requires Sempra Energy to maintain at the end of each quarter a ratio of total indebtedness to total capitalization (as defined in the agreement) of no more than 65%.

At September 30, 2008, Sempra Generation had no outstanding borrowings under the facility.

## *The Sempra Utilities*

On August 15, 2008, SDG&E and SoCalGas entered into an \$800 million, three-year syndicated revolving credit agreement expiring in 2011. JPMorgan Chase Bank serves as administrative agent for the syndicate of 17 lenders. The agreement permits each utility to individually borrow up to \$600 million, subject to a combined limit of \$800 million for both utilities. It also provides for the issuance of letters of credit on behalf of each utility subject to a combined letter of credit commitment of \$200 million for both utilities with the amount of borrowings otherwise available under the facility reduced by the amount of outstanding letters of credit.

Borrowings bear interest at benchmark rates plus a margin that varies with market index rates and the borrowing utility's credit rating. The agreement also requires each utility to maintain at the end of each quarter a ratio of total indebtedness to total capitalization (as defined in the agreement) of no more than 65%.

Each utility's obligations under the agreement are individual obligations, and a default by one utility would not constitute a default or preclude borrowings by, or the issuance of letters of credit on behalf of, the other utility.

At September 30, 2008, SDG&E and SoCalGas had no outstanding borrowings and no outstanding letters of credit under this facility. The facility provides support for \$96 million of commercial paper outstanding at SoCalGas at September 30, 2008.

### **Termination of Previous Credit Facilities**

Concurrently with the effectiveness of the credit agreements described above, the following credit facilities were terminated:

- Sempra Global's \$2.5 billion and \$750 million revolving credit facilities scheduled to expire in August 2010 and November 2008, respectively.
- Sempra LNG's \$1.25 billion revolving credit facility scheduled to expire in December 2009.
- SDG&E's and SoCalGas' combined \$600 million revolving credit facility scheduled to expire in August 2010.

### **RBS Sempra Commodities**

As contemplated by the agreement to form RBS Sempra Commodities as discussed in Note 3, as a transitional measure, Sempra Energy continues to provide back-up guarantees for a portion of RBS Sempra Commodities' trading obligations and certain credit facilities with third party lenders pending novation of the remaining trading obligations to RBS. The novation of the trading obligations to RBS is expected to be fully completed and Sempra Energy's guarantee of these obligations to terminate in the first half of 2009. RBS has fully indemnified Sempra Energy in respect of any liabilities that Sempra Energy may incur under the guarantees.

RBS Sempra Commodities' net trading liabilities and credit facilities supported by Sempra Energy's guarantees at September 30, 2008 were:

- \$1.1 billion of net trading liabilities consisting of guaranteed trading obligations net of collateral. The amount of guaranteed net trading liabilities varies from day to day with the value of the trading obligations and related collateral.
- \$500 million under a three-year revolving credit facility expiring in May 2009.

Sempra Energy has also guaranteed \$344 million of \$1.72 billion of commitments to RBS Sempra Commodities under an additional credit facility. Extensions of credit under the facility are limited to and secured by a borrowing base consisting of receivables, inventories and other joint venture assets that are valued at varying percentages of current market value. At September 30, 2008, the value of the borrowing base assets exceeded \$3 billion. The facility will be reduced and expire as the borrowing base assets are transferred to RBS as contemplated by the joint venture agreement.

### **Weighted Average Interest Rate**

The company's weighted average interest rate on outstanding commercial paper was 3.07 percent at September 30, 2008.

### **Long-term Debt**

In June 2008, Sempra Energy publicly offered and sold \$500 million of 6.15-percent notes, maturing in 2018.

### **Interest-Rate Swaps**

The company's fair value interest-rate swaps and interest-rate swaps to hedge cash flows are discussed in Note 6.

## **NOTE 6. FINANCIAL INSTRUMENTS**

The company periodically uses commodity derivative instruments and interest-rate swap agreements to moderate its exposure to commodity-price and interest-rate changes and to lower its overall cost of borrowing.

### **Fair Value Hedges**

Prior to the sale of the commodity-marketing businesses as discussed in Note 3, commodity fair value hedges were associated with Sempra Commodities and recorded as trading instruments.

As of September 30, 2008 and December 31, 2007, the company had fair value interest-rate swap hedges for a notional amount of debt totaling \$450 million. The maturities of these swaps range from 2010 to 2011. These fair value hedge balances were an asset of \$9 million and \$11 million at September 30, 2008 and December 31, 2007, respectively.

Market value adjustments since inception of the interest-rate swap hedges were recorded as an increase in Fixed-Price Contracts and Other Derivatives (in noncurrent assets as Sundry or in noncurrent liabilities) and a corresponding increase or decrease in Long-Term Debt without affecting net income or other comprehensive income.

## Cash Flow Hedges

Prior to the sale of the commodity-marketing businesses as discussed in Note 3, commodity cash flow hedges were primarily associated with Sempra Commodities and were recorded primarily as trading instruments.

As of September 30, 2008 and December 31, 2007, the company, excluding Otay Mesa VIE, had established cash flow interest-rate swap hedges for notional debt balances totaling \$434 million. The maturities on the swaps at September 30, 2008 range from 2009 to 2038. Separately, Otay Mesa VIE de-designated all cash flow interest-rate swap hedges in the second quarter of 2008.

During the second quarter of 2007, the company revised its borrowing plans in anticipation of net cash proceeds to be received in connection with the transaction related to the sale of Sempra Commodities as discussed in Note 3. Accordingly, as of June 30, 2007, the company reclassified a cash flow hedge gain of \$30 million pretax from Accumulated Other Comprehensive Income (Loss) into Other Income, Net in the Statements of Consolidated Income.

The balances in Accumulated Other Comprehensive Income (Loss) at September 30, 2008 and December 31, 2007 related to all cash flow hedges were losses of \$19 million and \$24 million, respectively, net of income tax. The company expects that of these losses, \$10 million, which is net of income tax, will be reclassified into earnings during the next twelve months as the hedged items affect earnings. In connection with the consummation of the sale of Sempra Commodities as discussed in Note 3, losses of \$16 million, net of income tax, of Sempra Commodities' cash flow hedge balance were recognized and reflected in the gain on the transaction, losses of \$7 million and \$6 million, net of income tax, were recognized in the second and third quarters of 2008, respectively, and losses of \$6 million, net of income tax, will be recognized over the remainder of the year.

## Hedge Ineffectiveness

A summary of the hedge ineffectiveness gains (losses) follows:

(Dollars in millions)	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
<b>Commodity hedges:*</b>				
Cash flow hedges	\$ --	\$ --	\$ (3)	\$ 1
Fair value hedges	--	(48)	(9)	(2)
Time value exclusions from hedge assessment	--	99	--	132
<b>Total unrealized gains (losses)</b>	<b>\$ --</b>	<b>\$ 51</b>	<b>\$ (12)</b>	<b>\$ 131</b>

\* For commodity derivative instruments, the company records ineffectiveness gains (losses) in Revenues from Sempra Global and Parent on the Statements of Consolidated Income.

For the nine months ended September 30, 2008 and 2007, pretax gains (losses) arising from the ineffective portion of interest-rate cash flow hedges was a negligible amount and \$(1) million, respectively, and were recorded in Other Income (Expense), Net on the Statements of Consolidated Income. These amounts included gains (losses) of a negligible amount and \$(1) million for the three-month periods ended September 30, 2008 and 2007, respectively.

For commodity derivative instruments designated as fair value hedges, the ineffectiveness gains (losses) relate to hedges of commodity inventory and include gains (losses) that represent time

value of money, which are excluded for hedge assessment purposes. For commodity derivative instruments designated as cash flow hedges, the ineffectiveness amount for 2008 relates to hedges of natural gas purchases and sales related to transportation and storage capacity arrangements. These commodity derivative instruments were held by the company's commodity-marketing businesses which were sold into RBS Sempra Commodities on April 1, 2008, as discussed in Note 3.

### **Sempra Utilities**

At the Sempra Utilities, the use of derivative instruments is subject to certain limitations imposed by company policy and regulatory requirements. These instruments enable the company to estimate with greater certainty energy and natural gas prices to be received by the company and the corresponding prices to be charged to its customers. The Sempra Utilities record realized gains or losses on derivative instruments associated with transactions for electric energy and natural gas contracts in Cost of Electric Fuel and Purchased Power and Cost of Natural Gas, respectively, on the Statements of Consolidated Income. On the Consolidated Balance Sheets, the Sempra Utilities record corresponding regulatory assets and liabilities related to unrealized gains and losses from these derivative instruments to the extent derivative gains and losses associated with these derivative instruments will be payable or recoverable in future rates.

### **Adoption of FSP FIN 39-1**

The company adopted FSP FIN 39-1 effective January 1, 2008, which requires retroactive application. Each Consolidated Balance Sheet reflects the offsetting of net derivative positions with fair value amounts for cash collateral with the same counterparty when management believes a legal right of setoff exists. As of September 30, 2008, the company offset fair value cash collateral receivables and payables against net derivative positions of \$19 million and \$32 million, respectively. As of December 31, 2007, the company offset fair value cash collateral receivables and payables against net derivative positions of \$177 million and \$1.1 billion, respectively. The fair value of cash collateral that was not offset in the Consolidated Balance Sheets as of September 30, 2008 and December 31, 2007 was \$50 million and \$27 million, respectively. The fair value of commodity derivative assets and liabilities as of September 30, 2008 and December 31, 2007, determined in accordance with the company's netting policy, is presented below.

### **Fair Value Hierarchy**

The company's valuation techniques used to measure fair value and the definition of the three levels of the fair value hierarchy, as defined in SFAS 157, *Fair Value Measurements* (SFAS 157), are discussed in Note 11 of the Notes to Consolidated Financial Statements in the Annual Report and above in Note 2 under FSP FAS 157-3.

The following tables set forth by level within the fair value hierarchy the company's financial assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2008 and December 31, 2007. As required by SFAS 157, financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The company's assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels.

Recurring Fair Value Measures (Dollars in millions)	At fair value as of September 30, 2008*				
	Level 1	Level 2	Level 3	Netting and Collateral	Total
<b>Assets:</b>					
Other derivatives	\$ 51	\$ 66	\$ 3	\$ --	\$ 120
Nuclear decommissioning trusts**	473	158	--	--	631
Short-term investments	--	413	--	--	413
Other	1	--	--	--	1
<b>Total</b>	<b>\$ 525</b>	<b>\$ 637</b>	<b>\$ 3</b>	<b>\$ --</b>	<b>\$ 1,165</b>
<b>Liabilities:</b>					
Other derivatives	\$ --	\$ 165	\$ --	\$ --	\$ 165

Recurring Fair Value Measures (Dollars in millions)	At fair value as of December 31, 2007***				
	Level 1	Level 2	Level 3	Netting and Collateral	Total
<b>Assets:</b>					
Trading derivatives	\$ 201	\$ 2,943	\$ 446	\$ (1,197)	\$ 2,393
Commodity trading inventories	--	2,177	--	--	2,177
Other derivatives	16	45	7	--	68
Nuclear decommissioning trusts**	551	175	--	--	726
Other	86	6	7	--	99
<b>Total</b>	<b>\$ 854</b>	<b>\$ 5,346</b>	<b>\$ 460</b>	<b>\$ (1,197)</b>	<b>\$ 5,463</b>
<b>Liabilities:</b>					
Trading derivatives	\$ 200	\$ 2,116	\$ 59	\$ (302)	\$ 2,073
Other derivatives	--	32	--	--	32
<b>Total</b>	<b>\$ 200</b>	<b>\$ 2,148</b>	<b>\$ 59</b>	<b>\$ (302)</b>	<b>\$ 2,105</b>

\*On April 1, 2008, the commodity-marketing businesses were sold, as discussed in Note 3.

\*\* Excludes cash balances.

\*\*\* Amounts have been reclassified to reflect the retrospective application of FSP FIN 39-1.

The determination of the fair values above incorporates various factors required under SFAS 157. These factors include not only the credit standing of the counterparties involved and the impact of credit enhancements (such as cash deposits, letters of credit and priority interests), but also the impact of the company's nonperformance risk on its liabilities.

The following tables set forth a reconciliation primarily of changes in the fair value of net trading and other derivatives classified as level 3 in the fair value hierarchy:

(Dollars in millions)	Three months ended September 30,	
	2008	2007
Balance as of July 1	\$ 5	\$ 471
Realized and unrealized losses	--	(15)
Settlements	(2)	18
<b>Balance as of September 30</b>	<b>\$ 3</b>	<b>\$ 474</b>
<b>Change in unrealized gains (losses) relating to instruments still held as of September 30</b>	<b>\$ --</b>	<b>\$ 35</b>

(Dollars in millions)	Nine months ended September 30,	
	2008	2007
Balance as of January 1	\$ 401	\$ 519
Realized and unrealized losses	(82)	(171)
Purchases, issuances and settlements	20	126
Sale of the commodity-marketing businesses	(336)	--
Balance as of September 30	\$ 3	\$ 474
Change in unrealized gains (losses) relating to instruments still held as of September 30	\$ --	\$ 112

Gains and losses (realized and unrealized) for level 3 recurring items are primarily related to the commodity-marketing businesses and are included in Revenues from Sempra Global and Parent on the Statements of Consolidated Income for the three months ended March 31, 2008. With the sale of these businesses on April 1, 2008, level 3 recurring activity is substantially reduced.

#### NOTE 7. SEMPRAS UTILITIES' REGULATORY MATTERS

##### Sunrise Powerlink Electric Transmission Line

In December 2005, SDG&E filed an application with the California Public Utilities Commission (CPUC) for authorization to construct a 500-kilovolt (kV) electric transmission line between the Imperial Valley and the San Diego region that will be able to deliver 1,000 MW (Sunrise Powerlink). The project, as proposed by the company, was projected to cost approximately \$1.5 billion, which included an allowance for funds used during construction related to both debt and equity.

A draft decision by the Administrative Law Judge (ALJ) and a draft Commissioner's alternate decision were issued by the CPUC on October 31, 2008. The ALJ's decision, if approved by the CPUC, would deny the requested transmission project in favor of other generation-based alternatives.

The Commissioner's alternate decision, if approved by the CPUC, would conditionally approve the construction of a transmission line south of the route proposed by the company. This decision would permit SDG&E to engage in preliminary construction activities but require CPUC approval of an SDG&E compliance plan, ensuring the transmission line will primarily be used for the delivery of renewable resources, before the commencement of any construction activities that would have a material physical impact to the environment. SDG&E is uncertain whether the terms and conditions required by this decision could be timely met and will seek modifications to this draft decision. If the requested modifications are accepted and the modified alternate decision is approved by the CPUC, SDG&E expects the Sunrise Powerlink would be in commercial operation in 2012 at an estimated cost of approximately \$1.9 billion, including environmental mitigation costs and undergrounding as required in the alternate decision. A final CPUC decision is expected by the end of the year.

A final environmental impact report for the project was also issued in October 2008 jointly by the CPUC and the Bureau of Land Management (BLM). If the CPUC adopts the route identified in the Commissioner's alternate decision, the company also expects the BLM to make its decision on the project in January 2009.

## **General Rate Case (GRC)**

In July 2008, the CPUC issued a final decision in both SoCalGas' and SDG&E's 2008 general rate case (2008 GRC). The decision adopted the test-year 2008 revenue requirements, effective retroactive to January 1, 2008, and the post-test year revenue requirements that were included in the settlement agreements filed with the CPUC. The decision provides an increase in the annual revenue requirement in 2008, as compared to 2007, of \$59 million for SoCalGas and \$138 million for SDG&E, and provides average annual increases of approximately \$52 million, or three percent, for SoCalGas and \$43 million, or three percent, for SDG&E, in each of the post-test years' revenue requirements. The decision also establishes a GRC period of four years (2008-2011) and does not impose a cap on the company's earnings.

Since the final decision was not issued by June 30, 2008, the Sempra Utilities' reported net income for the first six months of 2008 was based on the 2007 authorized revenue requirement as established by the CPUC's 2004 Cost of Service decision. As the 2008 GRC decision is retroactive, the company recognized additional net income for the period January 1 through June 30, 2008 of approximately \$40 million in the third quarter of 2008.

## **Cost of Capital**

The CPUC issued a decision in May 2008 establishing a uniform, multi-year Cost of Capital Mechanism for SDG&E that will replace its existing cost of capital mechanism. The new mechanism requires a full cost of capital application every third year, with the first full application being filed in April 2010 for test-year 2011. Between test years, return on equity (ROE) would automatically be adjusted if there were significant changes in the bond market, as defined in the mechanism. In any year where the difference between the current 12-month October-September average Moody's utility bond rates and the established benchmark (currently at 6.02%) exceeds a 100-basis point trigger, an automatic adjustment to SDG&E's ROE would be made through an October 15 advice letter to become effective on January 1 of the following year. No change in ROE has been triggered for calendar year 2009. There is no provision for capital structure adjustment outside of the test year, but an adjustment may be permitted if credit ratings change in mid-cycle. The decision also allows an adjustment outside of the mechanism process upon the occurrence of an extraordinary or catastrophic event with material impact.

## **2009 Biennial Cost Allocation Proceeding (BCAP)**

In August 2006, SoCalGas, SDG&E and Southern California Edison jointly filed an application with the CPUC seeking its approval of a series of revisions to the natural gas operations and service offerings of the Sempra Utilities. The CPUC issued a final decision in December 2007 approving some, but not all, of the proposals and deferring a number of issues, including the incentive mechanism for SoCalGas' natural gas storage program, to the Sempra Utilities' BCAP where they could be addressed more fully. A settlement agreement on a majority of the storage-related issues was reached with the parties, and a draft ALJ decision was issued on November 4, 2008, recommending approval of the settlement without modification. A final decision on the uncontested settlement is expected by year-end 2008.

Effective January 1, 2008, and until such time as a resolution is achieved in the BCAP, the storage revenues and costs that were previously shared between ratepayers and shareholders are being deferred pending a regulatory decision on this matter. The settlement, if approved, would resolve the incentive mechanism for the natural gas storage program for 2008, but the shareholder amount would depend on the actual storage revenues for the calendar year.

If approved as submitted, the settlement agreement would be in effect for a six-year period (2009 through 2014) and would allow SoCalGas to invest in certain storage replacement and expansion projects that ultimately would add an estimated 145 million cubic feet per day (MMcfd) of storage injection capacity and approximately 7 billion cubic feet (Bcf) of inventory capacity. The cost of these storage investments is estimated at \$250 million, would be incremental to the capital provided in the 2008 GRC and would be treated like existing storage assets, providing additional earnings through the resulting increase in rate base. The agreement also provides that the annual net revenues (revenues less allocated embedded cost) from the unbundled storage and system operator hub services programs be split between ratepayers and shareholders on a graduated basis. The first \$15 million of net revenue would be shared 90/10 (ratepayer/shareholder), the next \$15 million shared 75/25, and all additional net revenues shared 50/50, up to a total annual shareholder cap of \$20 million (pretax). The prior mechanism provided a 50/50 split of the net revenues (2007 and prior).

### **Advanced Metering Infrastructure**

In April 2007, the CPUC approved SDG&E's request to install advanced meters with integrated two-way communications functionality, providing for remote disconnect and a home area network for all customers. SDG&E estimates expenditures for this project of \$572 million (including approximately \$500 million in capital investment), which involves the replacement of 1.4 million electric meters and 900,000 natural gas meters throughout SDG&E's service territory. Based on the evaluation of an initial installation of 4,500 meters, SDG&E plans to begin full-scale deployment in February 2009, with completion by the end of 2011.

In September 2008, SoCalGas filed an application with the CPUC for approval to upgrade approximately six million natural gas meters with an advanced metering system at an estimated cost of \$1.1 billion (including approximately \$900 million in capital investment). The company has requested a CPUC decision by mid-2009. If timely approved, installation of the meters is expected to begin in 2011 and continue through 2015.

### **Natural Gas Market OIR**

The CPUC considered natural gas market issues, including market design and infrastructure requirements, as part of its Natural Gas Market Order Instituting Rulemaking (OIR). A final decision in Phase II of this proceeding was issued in September 2006, reaffirming the adequacy of the capacity of the SoCalGas and SDG&E systems to meet then-current and forecasted demand. Among other things, this decision established revised natural gas quality standards that apply to all natural gas supplies entering the SoCalGas and SDG&E systems, including new supplies of regasified liquefied natural gas. The South Coast Air Quality Management District and the City of San Diego (jointly with Ratepayers for Affordable Clean Energy) filed petitions for review in the California Court of Appeal and the California Supreme Court challenging the CPUC's September 2006 decision and contending that the CPUC was required to prepare an environmental impact statement under the California Environmental Quality Act evaluating the environmental impacts that might result from the changes in natural gas quality standards approved by the CPUC. In November 2007, the Court of Appeal determined that the California Supreme Court had exclusive jurisdiction over the petitions for review. In July 2008, the California Supreme Court denied the petitions for review, thereby affirming the CPUC's decision in all respects.

## NOTE 8. COMMITMENTS AND CONTINGENCIES

### Legal Proceedings

At September 30, 2008, the company's reserves related to unresolved litigation matters were \$40 million. Litigation reserves related to Sempra Commodities were assumed by RBS Sempra Commodities, however, the company has indemnified RBS should the liabilities from the final resolution of these matters be greater than the reserves. The uncertainties that exist in complex legal proceedings make it difficult to estimate with reasonable certainty the costs and effects of resolving legal matters. Accordingly, actual costs incurred may differ materially from estimated costs and could materially adversely affect the company's business, cash flows, results of operations and financial condition.

#### *DWR Contract*

In February 2002, the California Energy Oversight Board (CEOB) and the CPUC filed challenges at the Federal Energy Regulatory Commission (FERC) to the Department of Water Resources' (DWR) contracts with Sempra Generation and other power suppliers. After the FERC upheld the contracts in 2003, the CEOB and CPUC appealed to the U.S. Court of Appeals for the Ninth Circuit (Ninth Circuit Court of Appeals), challenging the FERC's application of the Mobile-Sierra doctrine's "public interest" standard of review to the contracts without having first determined that the contracts met a more rigorous "just and reasonable" standard of review. In June 2008, the United States Supreme Court (Supreme Court) ruled that the FERC was correct to apply the Mobile-Sierra doctrine (which presumes that contract rates are just and reasonable) absent a demonstration that one of the contracting parties' unlawful manipulation of the market directly affected the rates. The Supreme Court ruled that the FERC should clarify its findings on this issue and consider whether the contract rates seriously harm the public interest.

At various times since the contract's inception, Sempra Generation and the DWR have also had disputes regarding the meaning of terms and performance of their agreement under which Sempra Generation sells electricity to the DWR. In 2002, in a state civil action, the DWR sought to void its contract with Sempra Generation, seeking damages, injunctive and declaratory relief and \$100 million in punitive damages. The DWR claims that Sempra Generation misrepresented its intention and ability to construct a temporary phase of one power project and, alternatively, breached its contract by failure to construct and deliver power from that phase. In June 2005, the California Court of Appeal reversed a previous summary judgment in favor of Sempra Generation, concluding that the contract language was ambiguous and presented triable issues of material fact that must be addressed by further evidence and proceedings. The case was sent back to the trial court. In January 2007, the DWR added additional claims for fraud and breach of contract. In June 2008, the California Court of Appeal upheld the trial court's denial of Sempra Generation's motion to compel the DWR to arbitrate its new claims. The case was returned to the San Diego Superior Court for further proceedings. The case is now scheduled for a jury trial in May 2009.

The DWR commenced an additional arbitration against Sempra Generation in February 2006, relating to the manner in which Sempra Generation schedules its Mexicali plant. The DWR seeks \$100 million in damages and an order terminating the contract. In July 2007, the arbitration panel issued an order finding that the DWR's claims were subject to the FERC's exclusive jurisdiction. However, in November 2007, the FERC ruled that it does not have exclusive jurisdiction to determine the claims alleged by the DWR. Sempra Generation's request that the FERC rehear or clarify this ruling was denied. Arbitration hearings are scheduled for November 2008.

In September 2008, the DWR initiated another arbitration proceeding against Sempra Generation, alleging that the company has breached the parties' agreement in various operational respects, and has violated the order issued by the first arbitration panel relating to the amount refunded to the DWR and the manner in which Sempra Generation operates. The DWR seeks \$60 million in damages and an order terminating the contract.

#### *Natural Gas Cases*

In April 2003, Sierra Pacific Resources and its utility subsidiary Nevada Power filed a lawsuit in the U.S. District Court in Nevada against major natural gas suppliers, including Sempra Energy, the Sempra Utilities and Sempra Commodities, seeking recovery of damages alleged to total more than \$150 million (before trebling). The lawsuit claims that the defendants conspired to manipulate and inflate the prices that Nevada Power had to pay for its natural gas by preventing the construction of natural gas pipelines to serve Nevada and other Western states, and reporting artificially inflated prices to trade publications. The U.S. District Court dismissed the case in November 2004, determining that the FERC had exclusive jurisdiction to resolve the claims. In September 2007, the Ninth Circuit Court of Appeals reversed the dismissal and returned the case to the District Court for further proceedings.

Five cases against Sempra Energy, Sempra Commodities, the Sempra Utilities and various other companies are pending in the U.S. District Court in Nevada. Plaintiffs claim that energy prices were unlawfully manipulated by the reporting of artificially inflated natural gas prices to trade publications and by entering into deceptive transactions such as wash trades and churning transactions. Four of the cases also include conspiracy allegations similar to those made in the Continental Forge litigation discussed below. The court dismissed four of these actions in 2005, determining that the FERC had exclusive jurisdiction to resolve the claims. The remaining case, which includes conspiracy allegations, was stayed. In September 2007, the Ninth Circuit Court of Appeals reversed the dismissal and returned the cases to the District Court for further proceedings.

#### *FERC Refund Proceedings*

The FERC is investigating prices charged to buyers in the California Power Exchange (PX) and Independent System Operator (ISO) markets by various electric suppliers. In December 2002, a FERC Administrative Law Judge (ALJ) issued preliminary findings indicating that the PX and ISO owe power suppliers \$1.2 billion for the October 2, 2000 through June 20, 2001 period (the \$3.0 billion that the California PX and ISO still owe energy companies less \$1.8 billion that the energy companies charged California customers in excess of the preliminarily determined competitive market clearing prices). In March 2003, the FERC adopted its ALJ's findings, but changed the calculation of the refund by basing it on a different benchmark of natural gas prices. This change would increase the refund obligations from \$1.8 billion to more than \$3 billion for the same time period.

Various parties appealed the FERC's order to the Ninth Circuit Court of Appeals. In August 2006, the Court of Appeals held that the FERC had properly established October 2, 2000 through June 20, 2001 as the refund period and had properly excluded certain short-term bilateral transactions between sellers and the DWR from the refund proceedings. However, the court also held that the FERC erred in excluding certain multi-day transactions from the refund proceedings. Finally, while the court upheld the FERC's decision not to extend the refund proceedings to the summer period (prior to October 2, 2000), it found that the FERC had erred in not considering other

remedies, such as disgorgement of profits, for tariff violations that are alleged to have occurred prior to October 2, 2000. The Ninth Circuit Court of Appeals returned the matter to the FERC for further proceedings. In November 2007, Sempra Commodities and other entities filed requests for rehearing of the Ninth Circuit Court of Appeals' August 2006 decision.

In August 2007, the Ninth Circuit Court of Appeals issued a decision reversing and remanding FERC orders declining to provide refunds in a related proceeding regarding short-term bilateral sales up to one month in the Pacific Northwest. The court found that some of the short-term sales between the DWR and various sellers (including Sempra Commodities) that had previously been excluded from the refund proceeding involving sales in the ISO and PX markets in California, were within the scope of the Pacific Northwest refund proceeding. In December 2007, Sempra Commodities and other sellers filed requests for rehearing of the Ninth Circuit Court of Appeals' August 2007 decision. It is possible that on remand, the FERC could order refunds for short-term sales to the DWR in the Pacific Northwest refund proceeding.

RBS Sempra Commodities has reserves for its estimated refund liability that reflect its estimate of the effect of the FERC's revision of the benchmark prices it will use to calculate refunds and other refund-related developments. Pursuant to the agreements related to the formation of RBS Sempra Commodities, the company has indemnified RBS related to these proceedings should the liability from the final resolution be greater than the reserves.

In a separate complaint filed with the FERC in 2002, the California Attorney General challenged the FERC's authority to establish a market-based rate system. The complaint further contended that, even if such a system were valid, electricity sellers had failed to comply with the FERC's quarterly reporting requirements. The Attorney General requested that the FERC order refunds from suppliers. The FERC dismissed the complaint and instead ordered sellers to restate their reports. After an appeal by the California Attorney General, the Ninth Circuit Court of Appeals upheld the FERC's authority to establish a market-based rate system, but ordered the case returned to the FERC for further proceedings. The Ninth Circuit Court of Appeals stated that failure to file transaction-specific quarterly reports gave the FERC authority to order refunds with respect to jurisdictional sellers. The Supreme Court has declined further review of the Ninth Circuit Court of Appeals' order. On remand, it is possible that the FERC could order refunds or disgorgement of profits for periods in addition to those covered by its prior refund orders, which would substantially increase the refunds that ultimately may be required to be paid by Sempra Commodities and other power suppliers.

#### *FERC Manipulation Investigation*

The FERC is separately investigating whether there was manipulation of short-term energy markets in the western United States that would constitute violations of applicable tariffs and warrant disgorgement of associated profits. In this proceeding, the FERC's authority is not limited to the periods relevant to the refund proceeding. In May 2002, the FERC ordered all energy companies engaged in electric energy trading activities to state whether they had engaged in various specific trading activities in violation of the PX and ISO tariffs.

In June 2003, the FERC ordered a number of entities, including Sempra Commodities, to show cause why they should not disgorge profits from certain transactions between January 1, 2000 and June 20, 2001 that are asserted to have constituted gaming and/or anomalous market behavior under the California ISO and/or PX tariffs. In October 2003, Sempra Commodities agreed to pay \$7.2 million in full resolution of these investigations. That liability was recorded as of December 31, 2003. The Sempra Commodities settlement was approved by the FERC in August 2004.

Certain California parties have sought rehearing on this order and the FERC has not yet responded.

#### *SDG&E October 2007 Wildfire Litigation*

In October 2007, San Diego County experienced catastrophic wildfires. In July 2008, the California Department of Forestry and Fire Protection (Cal Fire) issued investigation reports stating that two fires (the Witch and Rice fires) were SDG&E "power line caused" and that a third fire (the Guejito fire) occurred when a wire securing a Cox Communications' fiber optic cable came into contact with an SDG&E power line "causing an arc and starting the fire." Cal Fire states that the Rice fire burned approximately 9,500 acres and damaged 206 homes and two commercial properties. The reports indicate that the Witch and Guejito fires merged and eventually burned approximately 198,000 acres, resulted in two fatalities, injured approximately 40 firefighters and destroyed approximately 1,141 homes. Cal Fire is still investigating the perimeters of these two fires to determine the damages associated with each fire. In September 2008, the Consumer Protection and Safety Division of the CPUC issued a staff investigative report reaching substantially the same conclusions as the Cal Fire reports. However, the staff report also opines that the power lines involved in the Witch and Rice fires and the lashing wire involved in the Guejito fire were not properly designed, constructed and maintained as required by commission rules and recommends that the commission order an investigation to examine the extent to which SDG&E and Cox Communications violated commission rules.

Numerous lawsuits have been filed in San Diego County Superior Court against SDG&E seeking compensation in unspecified amounts for fire-related damages and, in several cases, punitive damages. A number of the lawsuits seek designation as a class action and many of them name Sempra Energy as an additional defendant. The lawsuits assert liability for inverse condemnation, negligence and other causes of action, and also allege that SDG&E improperly designed and maintained its power lines and failed to adequately clear adjacent vegetation. In asserting inverse condemnation claims, the plaintiffs seek to impose strict liability on SDG&E based on its status as a public utility having the power of eminent domain. A lawsuit filed by the City of San Diego seeks recovery for property damage, workers' compensation benefits for its employees, and fire suppression costs. The company has approximately \$1 billion of liability insurance coverage and has notified its insurers of the lawsuits.

#### *Other Litigation*

Sempra Energy and several subsidiaries, along with three oil and natural gas companies, the City of Beverly Hills and the Beverly Hills Unified School District, are defendants in a toxic tort lawsuit filed in Los Angeles County Superior Court by approximately 1,000 plaintiffs claiming that various emissions resulted in cancer or fear of cancer. Sempra Energy has submitted the case to its insurers, who have reserved their rights with respect to coverage. In November 2006, the court granted the defendants' summary judgment motions based on lack of medical causation for the 12 initial plaintiffs scheduled to go to trial first. The court also granted Sempra Energy's separate summary judgment motion on punitive damages. The court has stayed the case as to the remaining plaintiffs pending the appeal of the rulings.

In 1998, Sempra Energy and the Sempra Utilities converted their traditional pension plans (other than the SoCalGas union employee plan) to cash balance plans. In July 2005, a lawsuit was filed against SoCalGas in the U.S. District Court for the Central District of California alleging that the conversion unlawfully discriminated against older employees and failed to provide required disclosure of a reduction in benefits. In October 2005, the court dismissed three of the four causes

of action and, in March 2006, dismissed the remaining cause of action. Plaintiffs appealed to the Ninth Circuit Court of Appeals and, in August 2008, the court affirmed the dismissal of three of the four causes of action and reversed the District Court's dismissal of the remaining cause of action. Plaintiffs have petitioned the Ninth Circuit Court of Appeals for a rehearing of two of the three affirmed cause of action dismissals. Briefs have been filed on the petition.

#### *Resolved Matters*

The company has accrued liabilities for resolved matters of \$403 million, including \$396 million for settlements related to certain litigation arising out of the 2000 - 2001 California energy crisis.

The litigation that is the subject of these settlements and accrued liabilities is frequently referred to as the Continental Forge litigation, although the settlements also include other cases. The terms of these settlements were reported previously. In July 2008, the California Attorney General and the DWR dismissed their appeal of the final order, and the settlements became final in August 2008. The reserves recorded for the settlements in 2005 fully provide for the present value of both the cash amounts to be paid in the settlements and the price discount to be provided on electricity to be delivered under the DWR contract.

In November 2006, the U.S. District Court in San Diego dismissed a lawsuit filed by the California Attorney General in November 2005 against Sempra Commodities alleging illegal market-gaming activities during the California energy crisis and claiming unspecified civil penalties and damages. The Ninth Circuit Court of Appeals affirmed the dismissal in September 2008.

#### **Nuclear Insurance**

SDG&E and the other owners of the San Onofre Nuclear Generating Station (SONGS) have insurance to respond to nuclear liability claims related to SONGS. The insurance provides coverage of \$300 million, the maximum amount available, and includes coverage for acts of terrorism. In addition, the Price-Anderson Act provides for up to \$12.2 billion of secondary financial protection. Should any of the licensed/commercial reactors in the United States experience a nuclear liability loss that exceeds the \$300 million insurance limit, all utilities owning nuclear reactors could be assessed to provide the secondary financial protection. SDG&E's total share would be up to \$47 million, subject to an annual maximum assessment of \$7 million, unless a default were to occur by any other SONGS owner. In the event the secondary financial protection limit were insufficient to cover the liability loss, SDG&E could be subject to an additional assessment.

SDG&E and the other owners of SONGS have \$2.75 billion of nuclear property, decontamination and debris removal insurance and up to \$490 million for outage expenses and replacement power costs incurred because of accidental property damage. This coverage is limited to \$3.5 million per week for the first 52 weeks and \$2.8 million per week for up to 110 additional weeks, after a waiting period of 12 weeks. The insurance is provided through a mutual insurance company, through which insured members are subject to retrospective premium assessments (up to \$8.5 million in SDG&E's case).

The nuclear property insurance program, subscribed to by members of the nuclear power generating industry, includes an industry aggregate loss limit for non-certified acts of terrorism (as defined by the Terrorism Risk Insurance Act). The industry aggregate loss limit for property claims arising from non-certified acts of terrorism is \$3.24 billion. This limit is the maximum

amount to be paid to members who sustain losses or damages from these non-certified terrorist acts.

#### **NOTE 9. SEGMENT INFORMATION**

The company is a holding company whose subsidiaries are primarily engaged in the energy business. It has five separately managed reportable segments (SoCalGas, SDG&E, Sempra Commodities, Sempra Generation and Sempra Pipelines & Storage), which are described in the Annual Report. The Sempra Commodities segment includes the operating results of Sempra Rockies Marketing, which holds firm service capacity on the Rockies Express Pipeline. The “all other” amounts consist primarily of parent organizations and Sempra LNG. Additional information regarding Sempra Commodities is provided in Note 3.

The accounting policies of the segments are described in the Notes to Consolidated Financial Statements in the Annual Report. Segment performance is evaluated by management based on reported net income. Sempra Utility transactions are based on rates set by the CPUC and the FERC.

Discontinued operations are discussed in Note 5 of the Notes to Consolidated Financial Statements in the Annual Report. The following tables exclude amounts from discontinued operations, unless otherwise noted.

(Dollars in millions)	Three months ended September 30,				Nine months ended September 30,			
	2008		2007		2008		2007	
<b>OPERATING REVENUES</b>								
SoCalGas	\$ 1,077	40 %	\$ 819	31 %	\$ 3,776	44 %	\$ 3,168	38 %
SDG&E	949	35	716	27	2,449	29	2,084	25
Sempra Commodities	13	--	679	25	486	6	1,901	23
Sempra Generation	498	18	390	15	1,426	17	1,064	13
Sempra Pipelines & Storage	127	5	81	3	338	4	242	3
All other	49	2	--	--	44	--	(11)	--
Adjustments and eliminations	(8)	--	(1)	--	(20)	--	(63)	(1)
Intersegment revenues	(13)	--	(21)	(1)	(34)	--	(57)	(1)
<b>Total</b>	<b>\$ 2,692</b>	<b>100 %</b>	<b>\$ 2,663</b>	<b>100 %</b>	<b>\$ 8,465</b>	<b>100 %</b>	<b>\$ 8,328</b>	<b>100 %</b>
<b>INTEREST EXPENSE</b>								
SoCalGas	\$ 14		\$ 18		\$ 44		\$ 53	
SDG&E	24		24		73		71	
Sempra Commodities	3		18		19		35	
Sempra Generation	4		4		12		11	
Sempra Pipelines & Storage	4		4		10		12	
All other	43		49		91		158	
Intercompany eliminations	(25)		(49)		(84)		(136)	
<b>Total</b>	<b>\$ 67</b>		<b>\$ 68</b>		<b>\$ 165</b>		<b>\$ 204</b>	
<b>INTEREST INCOME</b>								
SoCalGas	\$ 2		\$ 8		\$ 9		\$ 22	
SDG&E	1		2		5		4	
Sempra Commodities	--		4		7		19	
Sempra Generation	2		6		6		22	
Sempra Pipelines & Storage	6		3		14		11	
All other	26		38		79		120	
Intercompany eliminations	(25)		(49)		(84)		(136)	
<b>Total</b>	<b>\$ 12</b>		<b>\$ 12</b>		<b>\$ 36</b>		<b>\$ 62</b>	
<b>DEPRECIATION AND AMORTIZATION</b>								
SoCalGas	\$ 67	41 %	\$ 71	41 %	\$ 209	41 %	\$ 210	41 %
SDG&E	68	42	75	43	223	44	225	44
Sempra Commodities	--	--	6	3	6	1	19	3
Sempra Generation	14	9	16	9	42	8	41	8
Sempra Pipelines & Storage	5	3	3	2	10	2	9	2
All other	8	5	3	2	18	4	10	2
<b>Total</b>	<b>\$ 162</b>	<b>100 %</b>	<b>\$ 174</b>	<b>100 %</b>	<b>\$ 508</b>	<b>100 %</b>	<b>\$ 514</b>	<b>100 %</b>
<b>INCOME TAX EXPENSE (BENEFIT)</b>								
SoCalGas	\$ 41		\$ 44		\$ 117		\$ 122	
SDG&E	54		28		121		101	
Sempra Commodities	(1)		66		132		156	
Sempra Generation	46		32		98		76	
Sempra Pipelines & Storage	5		1		20		(2)	
All other	(51)		(36)		(65)		(112)	
<b>Total</b>	<b>\$ 94</b>		<b>\$ 135</b>		<b>\$ 423</b>		<b>\$ 341</b>	
<b>EQUITY EARNINGS (LOSSES)</b>								
Earnings (losses) recorded before tax:								
Sempra Commodities	\$ (4)		\$ --		\$ 142		\$ --	
Sempra Generation	8		7		10		6	
Sempra Pipelines & Storage	10		(2)		30		(5)	
All other	(4)		(4)		(11)		(12)	
<b>Total</b>	<b>\$ 10</b>		<b>\$ 1</b>		<b>\$ 171</b>		<b>\$ (11)</b>	
Earnings recorded net of tax:								
Sempra Pipelines & Storage	\$ 18		\$ 19		\$ 54		\$ 46	
Sempra Commodities	--		--		3		40	
<b>Total</b>	<b>\$ 18</b>		<b>\$ 19</b>		<b>\$ 57</b>		<b>\$ 86</b>	

(Dollars in millions)	Three months ended September 30,				Nine months ended September 30,			
	2008		2007		2008		2007	
<b>NET INCOME</b>								
SoCalGas*	\$ 77	25 %	\$ 63	21 %	\$ 190	24 %	\$ 172	21 %
SDG&E*	123	40	123	40	258	32	236	29
Sempra Commodities**	(8)	(3)	87	28	181	23	313	39
Sempra Generation	94	31	58	19	162	20	122	15
Sempra Pipelines & Storage	34	11	17	6	84	11	50	6
Discontinued operations	--	--	(25)	(8)	--	--	(27)	(3)
All other	(12)	(4)	(18)	(6)	(81)	(10)	(56)	(7)
Total	\$ 308	100 %	\$ 305	100 %	\$ 794	100 %	\$ 810	100 %

\* After preferred dividends.

\*\* Includes the company's portion of RBS Sempra Commodities' joint venture earnings since the formation of the joint venture on April 1, 2008, and 100% of the commodities' marketing businesses prior to April 1, 2008. Also includes the operating results of Sempra Rockies Marketing, as well as interest, income taxes, cost allocations and other items associated with the joint venture.

(Dollars in millions)	Nine months ended September 30,			
	2008		2007	
<b>EXPENDITURES FOR PROPERTY, PLANT &amp; EQUIPMENT</b>				
SoCalGas	\$ 350	23 %	\$ 300	22 %
SDG&E	638	41	479	35
Sempra Commodities	21	1	31	2
Sempra Generation	15	1	8	1
Sempra Pipelines & Storage	195	13	180	13
All other	322	21	359	27
Total	\$ 1,541	100 %	\$ 1,357	100 %

(Dollars in millions)	September 30, 2008		December 31, 2007***	
<b>ASSETS</b>				
SoCalGas	\$ 6,366	26 %	\$ 6,406	22 %
SDG&E	8,770	37	8,499	30
Sempra Commodities	1,915	8	8,620	30
Sempra Generation	1,807	8	1,759	6
Sempra Pipelines & Storage	2,918	12	2,287	8
All other	3,058	13	2,182	8
Intersegment receivables	(985)	(4)	(1,036)	(4)
Total	\$ 23,849	100 %	\$ 28,717	100 %
<b>INVESTMENTS IN EQUITY METHOD INVESTEEES</b>				
Sempra Commodities	\$ 1,912		\$ 32	
Sempra Generation	206		205	
Sempra Pipelines & Storage	864		776	
All other	35		46	
Total	\$ 3,017		\$ 1,059	

\*\*\* Adjusted to reflect the adoption of FASB Staff position FIN 39-1.

## NOTE 10. SUBSEQUENT EVENT

On October 1, 2008, the company completed the acquisition of EnergySouth, Inc. (EnergySouth), an energy services holding company based in Mobile, Alabama, for \$511 million in cash and the assumption of debt. Through EnergySouth Midstream, EnergySouth owns and operates natural gas underground storage and related pipeline facilities in Alabama and Mississippi. Through Mobile Gas Service Corporation, EnergySouth distributes natural gas to approximately 93,000 customers in Southwest Alabama.

Summarized balance sheet information for EnergySouth as of September 30, 2008 is as follows (in millions):

	Unaudited	
Total assets	\$	710
Total liabilities	\$	493

## ITEM 2.

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

The following discussion should be read in conjunction with the financial statements contained in this Form 10-Q, "Management's Discussion and Analysis of Financial Condition and Results of Operations" contained in the company's 2007 Annual Report on Form 10-K (Annual Report), and "Risk Factors" contained in the company's 2007 Annual Report and Part II of this Form 10-Q.

## OVERVIEW

### Sempra Energy

Sempra Energy is a Fortune 500 energy services holding company. Its business units provide electric, natural gas and other energy products and services to their customers. Operations are divided into the Sempra Utilities and Sempra Global. The Sempra Utilities are Southern California Gas Company (SoCalGas) and San Diego Gas & Electric Company (SDG&E), which serve consumers from California's Central Valley to the Mexican border. Sempra Global is a holding company for most of the subsidiaries and investments of Sempra Energy that are not subject to California utility regulation. Sempra Global's principal subsidiaries and holdings provide the following energy-related products and services:

- Sempra Commodities holds the company's investment in RBS Sempra Commodities LLP (RBS Sempra Commodities), a joint-venture partnership with The Royal Bank of Scotland (RBS). The partnership was formed on April 1, 2008 from the company's commodity-marketing businesses previously reported in this segment. The partnership's commodity trading businesses serve customers in natural gas, natural gas liquids, power, petroleum and petroleum products, coal, emissions, ethanol and base metals. Further discussion is provided in Notes 3 and 5 of the Notes to Condensed Consolidated Financial Statements herein. Sempra Commodities also includes the operating results of Sempra Rockies Marketing, which holds firm service capacity on the Rockies Express Pipeline.

- Sempra Generation develops, owns and operates electric generation facilities.
- Sempra LNG develops, owns and operates receipt terminals for the importation of liquefied natural gas (LNG), and has supply and marketing agreements to provide natural gas.
- Sempra Pipelines & Storage develops, owns and operates, or holds interests in, natural gas pipelines and storage facilities in the United States and Mexico, and in companies that provide natural gas or electricity services in Argentina, Chile, Mexico and Peru. The company is currently pursuing the sale of its interests in the Argentine utilities, as discussed in Note 4 of the Notes to Consolidated Financial Statements in the Annual Report. On October 1, 2008, the company acquired EnergySouth, Inc. (EnergySouth), as discussed in Note 10 of the Notes to Condensed Consolidated Financial Statements herein. EnergySouth will be included in the Sempra Pipelines & Storage segment.

## **RESULTS OF OPERATIONS**

Net income decreased by \$16 million (2%) to \$794 million for the nine months ended September 30, 2008, but increased by \$3 million (1%) to \$308 million for the three months ended September 30, 2008, compared to the corresponding periods of 2007. The decrease in the nine-month period was primarily due to reduced earnings at Sempra Commodities and higher net losses at Parent and Other and Sempra LNG, partially offset by improved results at the Sempra Utilities, Sempra Generation and Sempra Pipelines & Storage. The increase in net income in the three-month period resulted from improved earnings at SoCalGas and the Sempra Global business units, with the exception of Sempra Commodities. Results for 2007 included losses from discontinued operations of \$27 million and \$25 million for the nine-month and three-month periods, respectively. Additional information is provided in "Business Unit Results" below.

Net Income (Loss) by Business Unit

(Dollars in millions)	Nine months ended September 30,			
	2008		2007	
<b>Sempra Utilities:</b>				
Southern California Gas Company *	\$ 190	24 %	\$ 172	21 %
San Diego Gas & Electric Company *	258	32	236	29
<b>Total Sempra Utilities</b>	<b>448</b>	<b>56</b>	<b>408</b>	<b>50</b>
<b>Sempra Global:</b>				
Sempra Commodities **	181	23	313	39
Sempra Generation	162	20	122	15
Sempra Pipelines & Storage	84	11	50	6
Sempra LNG	(33)	(4)	(27)	(3)
<b>Total Sempra Global</b>	<b>394</b>	<b>50</b>	<b>458</b>	<b>57</b>
Parent and other ***	(48)	(6)	(29)	(4)
Income from continuing operations	794	100	837	103
Discontinued operations, net of income tax	--	--	(27)	(3)
<b>Net income</b>	<b>\$ 794</b>	<b>100 %</b>	<b>\$ 810</b>	<b>100 %</b>

(Dollars in millions)	Three months ended September 30,			
	2008		2007	
<b>Sempra Utilities:</b>				
Southern California Gas Company *	\$ 77	25 %	\$ 63	21 %
San Diego Gas & Electric Company *	123	40	123	40
<b>Total Sempra Utilities</b>	<b>200</b>	<b>65</b>	<b>186</b>	<b>61</b>
<b>Sempra Global:</b>				
Sempra Commodities **	(8)	(3)	87	28
Sempra Generation	94	31	58	19
Sempra Pipelines & Storage	34	11	17	6
Sempra LNG	4	1	(4)	(1)
<b>Total Sempra Global</b>	<b>124</b>	<b>40</b>	<b>158</b>	<b>52</b>
Parent and other ***	(16)	(5)	(14)	(5)
Income from continuing operations	308	100	330	108
Discontinued operations, net of income tax	--	--	(25)	(8)
<b>Net income</b>	<b>\$ 308</b>	<b>100 %</b>	<b>\$ 305</b>	<b>100 %</b>

\* After preferred dividends.

\*\* Includes the company's portion of RBS Sempra Commodities' joint venture earnings since the formation of the joint venture on April 1, 2008, and 100% of the commodities' marketing businesses prior to April 1, 2008. Also includes the operating results of Sempra Rockies Marketing, as well as interest, income taxes, cost allocations and other items associated with the joint venture.

\*\*\* Includes after-tax interest expense (\$50 million and \$61 million for the nine months ended September 30, 2008 and 2007, respectively, and \$24 million and \$20 million for the three months ended September 30, 2008 and 2007, respectively), intercompany eliminations recorded in consolidation and certain corporate costs incurred at Sempra Global.

During the three months and nine months ended September 30, 2008, natural gas revenues and the cost of natural gas increased compared to the corresponding periods in 2007, primarily as a result of higher natural gas prices and volumes. Electric revenues increased for the three months and nine months ended September 30, 2008 compared to the corresponding periods in 2007 primarily due to higher cost of electric fuel and purchased power and higher volumes, authorized revenues and refundable costs. Electric revenues for the three months ended September 30, 2008 also included a favorable adjustment from the retroactive application of the 2008 General Rate Case (GRC) decision for the period of January 1 through June 30, 2008.

Since the final decision in the 2008 GRC was not issued by the California Public Utilities Commission (CPUC) by June 30, 2008, revenues for the first six months of 2008 associated with CPUC-regulated operations were based on the 2007 CPUC-authorized revenue established by the 2004 Cost of Service decision. An adjustment was made at both utilities in the third quarter of 2008 to reflect the authorized revenue established in the 2008 GRC for the period of January 1 through June 30, 2008. Further discussion is provided in Note 7 of the Notes to Condensed Consolidated Financial Statements herein.

Although the current regulatory framework provides that the cost of natural gas purchased for core customers be passed through to the customers on a substantially concurrent basis, SoCalGas' Gas Cost Incentive Mechanism (GCIM) and SDG&E's natural gas procurement Performance-Based Regulation (PBR) mechanism, which was in effect through March 31, 2008, allow them to share in the savings or costs from buying natural gas for their customers below or above market-based monthly benchmarks. The mechanisms permit full recovery of commodity procurement costs within a tolerance band around the benchmark price. The costs or savings outside the tolerance band are shared between customers and shareholders. Further discussion is provided in Note 7 of the Notes to Condensed Consolidated Financial Statements herein and in Notes 1 and 15 of the Notes to Consolidated Financial Statements in the Annual Report.

The tables below summarize the Sempra Utilities' natural gas and electric volumes and revenues by customer class for the nine-month periods ended September 30.

Natural Gas Sales, Transportation and Exchange  
(Volumes in billion cubic feet, dollars in millions)

	Natural Gas Sales		Transportation and Exchange		Total	
	Volumes	Revenue	Volumes	Revenue	Volumes	Revenue
2008:						
Residential	199	\$ 2,662	1	\$ 3	200	\$ 2,665
Commercial and industrial	89	1,066	213	137	302	1,203
Electric generation plants	--	--	218	80	218	80
Wholesale	--	--	13	5	13	5
	288	\$ 3,728	445	\$ 225	733	3,953
Balancing accounts and other						344
Total						\$ 4,297
2007:						
Residential	198	\$ 2,234	1	\$ 3	199	\$ 2,237
Commercial and industrial	92	856	207	155	299	1,011
Electric generation plants	--	--	199	85	199	85
Wholesale	--	--	14	6	14	6
	290	\$ 3,090	421	\$ 249	711	3,339
Balancing accounts and other						261
Total						\$ 3,600

Electric Distribution and Transmission  
(Volumes in millions of kilowatt-hours, dollars in millions)

	2008		2007	
	Volumes	Revenue	Volumes	Revenue
Residential	5,782	\$ 700	5,678	\$ 755
Commercial	5,399	610	5,391	659
Industrial	1,752	151	1,699	175
Direct access	2,296	72	2,401	88
Street and highway lighting	79	8	79	9
	15,308	1,541	15,248	1,686
Balancing accounts and other		352		(92)
Total		\$ 1,893		\$ 1,594

Although commodity costs associated with long-term contracts allocated to SDG&E from the California Department of Water Resources (DWR) (and the revenues to recover those costs) are not included in the Statements of Consolidated Income, the associated volumes and distribution revenues are included in the above table.

### *Sempra Global and Parent Revenues*

Sempra Global and Parent revenues decreased by \$859 million (27%) in the nine months ended September 30, 2008 to \$2.3 billion, and by \$469 million (41%) in the three months ended September 30, 2008 to \$679 million. The decrease in the nine months included \$1.4 billion lower revenues from Sempra Commodities. Revenues for the nine months ended September 30, 2008 and 2007 included \$486 million and \$1.9 billion, respectively, for Sempra Commodities. These revenues were primarily for periods prior to the formation of RBS Sempra Commodities. The decrease was partially offset by \$362 million higher revenues at Sempra Generation, primarily due to increased power sales and favorable mark-to-market activity on natural gas and power contracts, \$96 million higher revenues at Sempra Pipelines & Storage, primarily from Mexican pipeline operations, and \$55 million higher revenues at Sempra LNG, primarily from the commencement of commercial operations at its Energía Costa Azul LNG receipt terminal in May 2008.

The three months ended September 30, 2008 and 2007 included \$13 million and \$679 million, respectively, for Sempra Commodities. This decrease was partially offset by higher revenues at Sempra Generation, Sempra Pipelines & Storage and Sempra LNG, as for the nine-month period.

### *Sempra Global and Parent Cost of Natural Gas, Electric Fuel and Purchased Power*

Sempra Global and Parent cost of natural gas, electric fuel and purchased power increased by \$408 million (43%) in the nine months ended September 30, 2008 to \$1.4 billion, and by \$100 million (30%) in the three months ended September 30, 2008 to \$431 million. The increases were primarily associated with the higher revenues at Sempra Generation, Sempra Pipelines & Storage and Sempra LNG.

### *Sempra Global and Parent Other Cost of Sales*

Sempra Global and Parent other cost of sales for the nine months ended September 30, 2008 and 2007 included \$165 million and \$796 million, respectively, for Sempra Commodities. This other cost of sales was primarily for periods prior to the formation of RBS Sempra Commodities. The three months ended September 30, 2008 and 2007 included \$12 million and \$256 million, respectively, for Sempra Commodities.

### *Gains on Sale of Assets*

The gains in the nine months ended September 30, 2008 include \$109 million related to the RBS Sempra Commodities transaction as discussed in Note 3 of the Notes to Condensed Consolidated Financial Statements herein.

### *Operation and Maintenance*

Operation and maintenance expenses decreased by \$324 million (15%) in the nine months ended September 30, 2008 to \$1.8 billion, and by \$194 million (26%) in the three months ended September 30, 2008 to \$564 million. The nine months ended September 30, 2008 and 2007 included \$243 million and \$640 million, respectively, for Sempra Commodities. These operation and maintenance expenses were primarily for periods prior to the formation of RBS Sempra Commodities. The three months ended September 30, 2008 and 2007 included \$3 million and \$249 million, respectively, for Sempra Commodities. Excluding amounts for Sempra Commodities, operation and maintenance expenses increased \$52 million and \$73 million for the

three-month and nine-month periods ended September 30, 2008, respectively. The increases, primarily at SDG&E, were due to higher refundable costs and litigation expense.

#### *Equity Earnings - RBS Sempra Commodities LLP*

Earnings (losses) from the company's investment in the newly-formed RBS Sempra Commodities were \$(4) million and \$142 million in the three months and nine months ended September 30, 2008, respectively. Additional information is provided in the Sempra Commodities discussion in "Business Unit Results" below.

#### *Equity Earnings (Losses) - Other*

Equity earnings from other investments recorded before taxes increased by \$40 million (364%) in the nine months ended September 30, 2008 to \$29 million, and by \$13 million in the three months ended September 30, 2008 to \$14 million. The increases were primarily due to the start of operations of Rockies Express-West in the first quarter of 2008.

#### *Other Income (Expense), Net*

Other income, net, decreased by \$49 million (68%) in the nine months ended September 30, 2008 to \$23 million. In the three months ended September 30, 2008, other expense, net, was \$13 million compared to other income, net, of \$4 million in the three months ended September 30, 2007. The decrease in the nine months ended September 30, 2008 was primarily attributable to a \$23 million gain from interest-rate swaps in 2007, \$23 million higher losses from investments related to the company's executive retirement and deferred compensation plans in 2008, \$13 million in Mexican peso exchange losses in 2008 and \$8 million lower earnings from the sale of tax credits at Sempra Financial. The decreases were offset by a \$16 million cash payment received for the early termination of a capacity agreement for the Cameron LNG receipt terminal in 2008.

The decrease in the three-month period ended September 30, 2008 was primarily attributable to the \$13 million in Mexican peso exchange losses, \$11 million higher losses from investments related to the company's executive retirement and deferred compensation plans in 2008, offset by a \$7 million net loss from interest-rate swaps in 2007.

#### *Interest Income*

Interest income decreased by \$26 million (42%) in the nine months ended September 30, 2008 to \$36 million. The decrease was primarily attributable to lower average short-term investment balances in 2008. Short-term investment balances were higher in 2007 due to asset sales in 2006.

#### *Interest Expense*

Interest expense decreased by \$39 million (19%) in the nine months ended September 30, 2008 to \$165 million, but was comparable for the quarter-to-quarter period. The decrease in the nine months was due to the effect of the repayment of long-term debt in 2007 and lower interest rates, partially offset by higher interest expense primarily from long-term debt issued in September 2007 and June 2008. In addition, the nine months ended September 30, 2008 included \$18 million reduced interest expense related to energy crisis litigation reserves.

## *Income Taxes*

Income tax expense was \$423 million and \$341 million for the nine months ended September 30, 2008 and 2007, respectively, and the effective income tax rates were 36 percent and 31 percent, respectively. Income tax expense was \$94 million and \$135 million for the three months ended September 30, 2008 and 2007, respectively, and the effective income tax rates were 24 percent and 30 percent, respectively.

The increase in income tax expense for the nine months ended September 30, 2008 was due to higher pretax earnings and a higher effective income tax rate. The increase in the 2008 effective income tax rate was due primarily to the phase-out of synthetic fuels credits in 2007 and higher income tax expense related to Mexican currency translation and inflation adjustments, offset partially by higher favorable resolution of prior years' income tax issues.

The decrease in income tax expense for the three months ended September 30, 2008 was due primarily to lower pretax earnings and a lower effective income tax rate. The decrease in the effective income tax rate was due primarily to higher favorable resolution of prior years' income tax issues.

## *Equity Earnings, Net of Income Tax*

Equity earnings, net of income tax, decreased by \$29 million (34%) in the nine months ended September 30, 2008 to \$57 million. The decrease for the nine-month period was primarily due to an after-tax gain of \$30 million in 2007 at Sempra Commodities from the sale of investments. Equity earnings for the three months ended September 30, 2008 were comparable to the corresponding period in 2007.

## *Net Income*

Variations in net income are discussed below in "Business Unit Results."

## **Business Unit Results**

### ***Southern California Gas Company***

Net income for SoCalGas increased by \$18 million (10%) in the nine months ended September 30, 2008 to \$190 million and by \$14 million (22%) in the three months ended September 30, 2008 to \$77 million. The increase in the nine months was primarily attributable to \$11 million in higher authorized margin in 2008, net of higher operating expenses, associated with CPUC-regulated operations, \$6 million in higher regulatory awards (\$7 million in 2008 compared to \$1 million in 2007) and \$5 million as a result of a lower effective tax rate (excluding the effect of the resolution of prior years' income tax matters), offset by \$12 million lower earnings from non-core natural gas storage in accordance with the Omnibus Gas Settlements, as discussed in Note 7 of the Notes to Condensed Consolidated Financial Statements herein and Note 15 of the Notes to Consolidated Financial Statements in the Annual Report. In addition to these factors, the comparative nine-month results were favorably impacted by \$7 million from the favorable resolution of a regulatory matter in 2008 and \$5 million from the higher favorable resolution of prior years' income tax issues (\$4 million favorable in 2008 compared to \$1 million unfavorable in 2007), partially offset by \$5 million higher expense in 2008 for potential uncollectible customer receivables.

The increase in the three months ended September 30, 2008 included a benefit of \$3 million as a result of a lower effective income tax rate (excluding the effect of the resolution of prior years' income tax issues), offset by \$4 million in lower earnings from non-core natural gas storage. In addition to these factors, the three-month comparative net income was favorably impacted by \$7 million from the favorable resolution of a regulatory matter in 2008, \$7 million retroactive impact of the 2008 GRC decision for January 1 through June 30, 2008, and a \$5 million increase from the favorable resolution of prior years' income tax issues (\$4 million favorable in 2008 compared to \$1 million unfavorable in 2007), partially offset by \$4 million higher expense in 2008 associated with potential uncollectible customer receivables.

### ***San Diego Gas & Electric Company***

Net income increased by \$22 million (9%) in the nine months ended September 30, 2008 to \$258 million but remained consistent for the quarter-to-quarter periods at \$123 million. The increase in the nine months ended September 30, 2008 was primarily attributable to \$46 million due to higher authorized margin in 2008, net of higher operating costs, associated with CPUC-regulated operations and \$4 million from higher electric transmission margin. In addition to these positive factors, the comparative nine-month results were adversely impacted by \$19 million of lower favorable resolution of regulatory matters (\$7 million in 2008 compared to \$26 million in 2007) and a \$16 million higher increase in litigation reserves (\$22 million in 2008 compared to \$6 million in 2007). Net income also included \$19 million and \$17 million for the nine-month periods ended September 30, 2008 and 2007, respectively, from the favorable resolution of prior year's income tax issues.

Although net income for the three-month period in 2008 was comparable to the 2007 period, it included \$17 million higher CPUC-authorized margin, net of higher operating costs, and \$2 million from higher electric transmission margin. Offsetting these positive items for the comparative three-month results were \$26 million from the favorable resolution of a regulatory matter in 2007, \$16 million due to a higher increase in litigation reserves (\$17 million in 2008 compared to \$1 million in 2007) and \$8 million lower favorable resolution of prior years' income tax issues (\$12 million in 2008 compared to \$20 million in 2007). The three-month 2008 results also included \$33 million for the retroactive impact of the 2008 GRC decision for January 1 through June 30, 2008.

### ***Sempra Commodities***

Net income for Sempra Commodities decreased by \$132 million (42%) in the nine months ended September 30, 2008 to \$181 million and by \$95 million (109%) in the three months ended September 30, 2008 to a net loss of \$8 million. Recorded results for the second and third quarters of 2008 primarily represent the company's equity earnings from RBS Sempra Commodities, formed on April 1, 2008, and other items discussed below. Recorded results for 2007 and the first quarter of 2008 represent 100% of this business' earnings until the formation of the partnership.

The results for the three months and nine months ended September 30, 2008 included \$3 million loss and \$90 million income, respectively, in equity earnings from RBS Sempra Commodities. The nine-month period in 2008 included a \$67 million gain on the transaction with RBS, partially offset by expenses of \$36 million, primarily charges for litigation and unfavorable effects from prior years' income tax issues. RBS Sempra Commodities' loss in the third quarter of 2008 was primarily a result of losses in the U.S. power markets, which were related to declining prices and reduced liquidity associated with fewer market participants. The joint venture's other product

lines all generated positive earnings for the quarter, however, they were also adversely impacted by declining prices and reduced market liquidity.

### ***Sempra Generation***

Sempra Generation's net income increased by \$40 million (33%) in the nine months ended September 30, 2008 to \$162 million, and by \$36 million (62%) in the three months ended September 30, 2008 to \$94 million. The increase for the nine months ended September 30, 2008 was due to \$22 million higher earnings primarily due to plant scheduled major maintenance and associated down time in 2007, \$16 million higher earnings from favorable prices and merchant sales activities, and a favorable change of \$10 million in mark-to-market earnings on long-term forward contracts with RBS Sempra Commodities and other counterparties, partially offset by \$9 million of lower net interest income.

The increase for the three months ended September 30, 2008 was primarily due to a favorable change of \$25 million in mark-to-market earnings on long-term forward contracts with RBS Sempra Commodities and other counterparties and \$8 million lower income tax expense as a result of Sempra Generation's solar investments.

### ***Sempra Pipelines & Storage***

Net income for Sempra Pipelines & Storage increased by \$34 million (68%) in the nine months ended September 30, 2008 to \$84 million, and by \$17 million (100%) in the three months ended September 30, 2008 to \$34 million. The increase for the nine months ended September 30, 2008 was primarily due to \$21 million from Rockies Express-West, which began operations in the first quarter of 2008, \$7 million of higher earnings primarily from the commencement of LNG-related pipeline operations in Mexico in the second quarter of 2008, and \$7 million from improved operations and \$5 million from favorable foreign currency exchange-rate effects from its investments in Chile and Peru, partially offset by \$7 million higher taxes related to foreign income.

The increase for the three months ended September 30, 2008 was primarily due to \$8 million from the commencement of LNG-related pipeline operations in Mexico, \$7 million from Rockies Express-West, and \$2 million from improved operations and \$1 million from favorable foreign currency exchange-rate effects from its investments in Chile and Peru.

### ***Sempra LNG***

The net loss for Sempra LNG increased by \$6 million (22%) in the nine months ended September 30, 2008 to \$33 million. For the three months ended September 30, 2008, earnings improved to a net income of \$4 million compared to a net loss of \$4 million for the corresponding period in 2007. The increased loss in the nine months ended September 30, 2008 was primarily due to \$16 million of higher income tax expense related to Mexican currency translation and inflation adjustments, partially offset by a \$10 million after-tax cash payment received for the early termination of a capacity agreement with Merrill Lynch Commodities Inc. for the Cameron LNG receipt terminal. In May 2008, Sempra LNG began earning capacity revenues for Energía Costa Azul.

The increase in net income in the three months ended September 30, 2008 was primarily due to \$14 million of increased mark-to-market gain related to the natural gas marketing agreement with

RBS Sempra Commodities, partially offset by \$2 million of higher income tax expense related to Mexican currency translation and inflation adjustments.

### ***Parent and Other***

The net loss for Parent and Other increased by \$19 million (66%) in the nine months ended September 30, 2008 to \$48 million, and by \$2 million (14%) in the three months ended September 30, 2008 to \$16 million. The increase in net loss for the nine months ended September 30, 2008 was primarily attributable to \$18 million higher investment and Mexican peso exchange losses, a \$14 million gain from an interest-rate swap in 2007 and \$8 million of higher income tax expense related to Mexican currency translation and inflation adjustments, partially offset by \$14 million higher favorable resolution of prior years' income tax issues and \$10 million lower interest expense in 2008 related to litigation reserves. The change for the three months ended September 30, 2008 was primarily attributable to \$16 million in investment and Mexican peso exchange losses in 2008, partially offset by \$13 million higher favorable resolution of prior years' income tax issues.

### **CAPITAL RESOURCES AND LIQUIDITY**

The company expects its cash flows from operations to provide for dividends and a substantial portion of the funding of the company's capital expenditures. The company's expansion also requires the issuance of debt securities from time to time. On October 1, 2008, the company completed the acquisition of EnergySouth, Inc. (EnergySouth) for \$511 million in cash. The acquisition was funded by commercial paper, however, the company plans to replace these borrowings with long-term financing in the fourth quarter of 2008.

On April 1, 2008, the company completed the formation of RBS Sempra Commodities to own and operate Sempra Energy's commodity-marketing businesses, which generally comprised the Sempra Commodities segment. RBS is to provide the joint venture with all growth capital, working-capital requirements and credit support. The company's initial equity contribution to the partnership was \$1.6 billion, and RBS made an initial equity contribution of \$1.665 billion. As a result of the transaction, the company received cash of approximately \$1.2 billion, net of its contribution. The company accounts for its investment in the partnership under the equity method. The company and RBS intend that RBS Sempra Commodities will distribute all of its net income on an annual basis, although the distributions are within the discretion of the board of directors of the partnership. In limited cases, earnings allocable to the partnership may be retained by the partnership to replenish capital depleted through losses. In September 2008, the company received a distribution of \$56 million from the partnership, as provided for in the partnership agreement to fund estimated income tax payments. Additional information concerning the transaction with RBS and related credit commitments and guarantees is provided in Notes 3 and 5 of the Notes to Condensed Consolidated Financial Statements herein.

On April 1, 2008, the company entered into a share repurchase program and prepaid \$1 billion on April 7, 2008 for shares of the company's common stock to be purchased in a share forward transaction as discussed in Note 4 of the Notes to Condensed Consolidated Financial Statements herein. As a result of the recent crisis in the credit markets, the company's previously announced plans to purchase an additional \$500 million of common shares in 2009 will be reevaluated in the first quarter of 2009.

On May 22, 2008, the company's board of directors approved an increase to the company's quarterly common stock dividend to \$0.35 per share (\$1.40 annually), an increase of \$0.03 per

share (\$0.12 annually) from the \$0.32 per share (\$1.28 annually) authorized in February 2008, and targets an annual dividend payout ratio of 35 percent to 40 percent of net income.

At September 30, 2008, the company had \$198 million in unrestricted cash and cash equivalents, and \$2.9 billion in available unused, committed lines of credit to provide liquidity and support commercial paper. The lines expire in August 2011 and are syndicated with 19 different banks. The recent global credit crisis has severely affected the availability and cost of both short-term and long-term financing. If cash flows from operations were to be significantly reduced or the company were to be unable to borrow under acceptable terms, the company would reduce or postpone discretionary capital expenditures, share repurchases and/or investments in new businesses. Management continues to regularly monitor the company's ability to finance the needs of its operating, investing and financing activities in a manner consistent with its intention to maintain strong, investment-quality credit ratings.

The company's credit agreements are discussed more fully in Note 5 of the Notes to Condensed Consolidated Financial Statements herein.

At the Sempra Utilities, cash flows from operations, security issuances and/or capital contributions by Sempra Energy are expected to continue to be adequate to meet utility capital expenditure requirements. As a result of SDG&E's projected capital expenditure program, SDG&E has elected to suspend the payment of dividends on its common stock to Sempra Energy, and the level of future common dividends may be affected in order to maintain SDG&E's authorized capital structure during periods of increased capital expenditures.

Sempra Generation's long-term power sale contracts may contain collateral requirements. The DWR contracts do not contain such requirements. The collateral arrangements provide for Sempra Generation and/or the counterparty to post cash, guarantees or letters of credit to the other party for exposure in excess of established thresholds. Sempra Generation may be required to provide collateral when market price movements adversely affect the counterparty's cost of replacement energy supplies were Sempra Generation to fail to deliver the contracted amounts. As of September 30, 2008, Sempra Generation had no outstanding collateral requirements under these contracts.

Sempra Pipelines & Storage is expected to require funding from the company or external sources, or both, to continue its Liberty Gas Storage facility and other natural gas storage projects, its participation in the development of Rockies Express Pipeline (REX), a natural gas pipeline, and its planned development of pipelines to serve the Sempra LNG facility being developed in Louisiana. Sempra Pipelines & Storage will also require funding for EnergySouth's capital expenditure program, and refinancing of EnergySouth's short-term debt of \$200 million, which matures in November 2008.

Sempra LNG will require funding for its development of LNG receiving facilities. While the company's credit facilities and other Sempra Energy sources are expected to be adequate for these requirements, the company may decide to use project financing if management determines its use to be advantageous. As the projects currently under construction are put in service, Sempra LNG is expected to provide operating cash flow for further development.

#### CASH FLOWS FROM OPERATING ACTIVITIES

Net cash provided by operating activities decreased by \$773 million (49%) to \$798 million for 2008. The change was primarily due to a \$382 million decrease in net trading assets in 2007, a

\$144 million higher increase in inventory, a \$137 million decrease in income from continuing operations (adjusted for noncash items) and a \$55 million decrease in other liabilities in 2008 compared to a \$63 million increase in 2007. Net income from continuing operations (adjusted for noncash items), includes an increase of \$142 million for RBS Sempra Commodities equity earnings.

For the nine months ended September 30, 2008, the company made contributions of \$47 million and \$16 million to the pension plans and other postretirement benefit plans, respectively. If equity and bond markets remain at approximately the same levels as the end of October, the company expects qualified pension contributions to be approximately \$250 million in 2009, including \$150 million at SDG&E and \$90 million at SoCalGas. The Sempra Utilities' portion of the additional contributions will be fully recovered in future rates, and there is no earnings impact. The remaining portion is estimated to decrease earnings by approximately \$3 million after-tax in 2009.

#### CASH FLOWS FROM INVESTING ACTIVITIES

Net cash used in investing activities increased by \$253 million (19%) to \$1.6 billion for 2008. The change was primarily due to the capital contributions of \$1.6 billion to RBS Sempra Commodities and \$150 million to Rockies Express and the purchase of \$413 million in industrial revenue bonds, offset by \$2.1 billion in proceeds received from the RBS transaction and a \$60 million decrease in notes receivable from unconsolidated affiliates. The \$2.1 billion in proceeds from the RBS transaction is net of \$383 million of cash sold. Capital expenditures also increased by \$184 million.

The company expects to make capital expenditures and investments of \$2.7 billion in 2008. Significant capital expenditures and investments are expected to include \$1.1 billion for Sempra Utility plant improvements and \$1.6 billion of capital expenditures at its other subsidiaries, including the development of LNG facilities and natural gas pipelines and the acquisition of EnergySouth. These expenditures and investments are expected to be financed by cash flows from operations, cash on hand and security issuances. The \$2.7 billion does not include the investment in RBS Sempra Commodities made on April 1, 2008, nor the investment in industrial revenue bonds.

The company's 25-percent participation in the Rockies Express project required a contribution to the partnership of \$150 million in February 2008, but the company does not expect any further contribution to the project will be required in 2008. Total project cost is now estimated at approximately \$6 billion. REX-West, the segment of the pipeline which extends 713 miles from the Cheyenne Hub to Audrain County in Missouri, began interim service in January and full service in May 2008. In June 2008, the Federal Energy Regulatory Commission approved construction of REX-East, which will extend the pipeline from Audrain County to Clarington in Ohio. Construction began in July 2008. Subject to receipt of regulatory approvals, REX-East is expected to be fully operational in late 2009, with service to delivering points in Illinois, Indiana and Ohio during 2009.

Liberty, as currently permitted, is a 17 billion cubic feet (Bcf) salt-cavern natural gas storage facility located in Calcasieu Parish, Louisiana. The facility has been under construction by the company and its 25-percent partner, Proliance Transportation and Storage, LLC, and will be connected to the Cameron Pipeline under development by Sempra Pipelines & Storage to connect area LNG regasification terminals to an interstate gas transmission system. The estimated project cost is approximately \$250 million, of which \$200 million has been expended through September

30, 2008. Completion of the project has been delayed by subsurface and well-completion problems. Should ongoing corrective measures prove to be unsuccessful, the salt-cavern facility may not go into service, or may have reduced capacity when placed in service. In that event, the company may be required to take an impairment charge of up to \$65 million after tax.

Sempra LNG's Energía Costa Azul LNG receipt terminal in Baja California, Mexico, with a capacity of 1 Bcf per day, began commercial operations in May 2008. A planned nitrogen-injection facility will allow the terminal to process LNG cargoes from a wider variety of sources and will provide additional revenue from long-term firm capacity payments for the injection service. Through September 30, 2008, Sempra LNG has made expenditures of \$1.1 billion related to the terminal (including breakwater), the nitrogen-injection facility and the proposed expansion project.

Sempra LNG's Cameron LNG receipt terminal is currently under construction in Hackberry, Louisiana. Construction is expected to be completed, and capacity revenues to start, in mid-2009. The estimated costs of this project, including capitalized interest, are approximately \$800 million (excluding pre-expansion costs, which are \$42 million to date). Through September 30, 2008, Sempra LNG has made expenditures of \$741 million related to the terminal and proposed expansion project.

#### CASH FLOWS FROM FINANCING ACTIVITIES

Net cash provided by (used in) financing activities totaled \$328 million for 2008 and \$(105) million for 2007. The 2008 change was primarily due to the \$1 billion expended for the stock repurchase program, common dividends paid of \$252 million and long-term debt payments of \$75 million, offset by \$985 million short-term debt borrowings and issuances of long-term debt of \$650 million. The 2007 change was primarily due to long-term debt payments of \$1.1 billion, offset by an increase in short-term borrowings of \$954 million.

#### COMMITMENTS

At September 30, 2008, there were no significant changes to the commitments that were disclosed in the Annual Report, except for increases of \$144 million and \$16 million, respectively, related to construction commitments at Sempra LNG and Sempra Pipelines & Storage, \$236 million related to an operating lease commitment at Sempra LNG, \$500 million related to the issuance of 6.15-percent notes, and \$390 million related to natural gas contracts at SoCalGas. The future payments under these contractual commitments are expected to be \$130 million for 2008, \$286 million for 2009, \$38 million for 2010, \$29 million for 2011, \$30 million for 2012 and \$773 million thereafter.

Due to increases in natural gas forward prices, the company's commitment under the natural gas purchase agreement with Tangguh PSC contractors, which is discussed in Note 16 of the Notes to Consolidated Financial Statements in the Annual Report, has increased by \$775 million. Future payments are therefore expected to increase (decrease) by \$326 million for 2009, \$13 million for 2010, \$4 million for 2011, \$(5) million for 2012 and \$437 million thereafter.

Also, commitments related to the company's commodity-marketing businesses became the obligation of RBS Sempra Commodities as a result of the formation of that partnership. At December 31, 2007, these obligations totaled \$586 million, including \$422 million in short-term debt, \$143 million in operating leases and \$21 million in long-term debt. Additional information

regarding the short-term debt commitment is provided in Note 5 of the Notes to Condensed Consolidated Financial Statements herein.

## **FACTORS INFLUENCING FUTURE PERFORMANCE**

The Sempra Utilities' operations and Sempra Generation's long-term contracts generally provide relatively stable earnings and liquidity. However, for the next few years SDG&E is planning to reinvest its earnings in significant capital projects and is not expected to pay common dividends to Sempra Energy during that time. Also, Sempra Generation's contract with the DWR, which provides a significant portion of Sempra Generation's revenues, ends in late 2011. Due to the inability to forecast with certainty future electricity prices and the cost of natural gas, contracts entered into to replace this capacity may provide substantially lower revenue. Sempra LNG and Sempra Pipelines & Storage are expected to provide relatively stable earnings and liquidity upon the completion of their construction programs, but to require substantial funding during the construction period. Additional information regarding Sempra Pipelines & Storage's Liberty natural gas storage facility project is provided in "Capital Resources and Liquidity – Cash Flows from Investing Activities" herein. Also, until firm supply or capacity contracts are in place and effective for Sempra LNG's Cameron and Energía Costa Azul LNG regasification facilities, Sempra LNG will seek to obtain interim LNG supplies, which may result in greater variability in revenues and earnings.

As discussed in Note 3 of the Notes to Condensed Consolidated Financial Statements herein, on April 1, 2008, the company and RBS completed the formation of a partnership, RBS Sempra Commodities, to own and operate the company's commodity-marketing businesses, which generally comprise the company's Sempra Commodities segment. This transaction eliminates the company's requirements for trading guarantees and credit support for this business, except for transitional guarantees and credit support, as discussed in Note 5 of the Notes to Condensed Consolidated Financial Statements herein. The company expects somewhat lower earnings from the commodities business in the near term due to its reduced ownership after the formation of the partnership.

As discussed in Note 10 of the Notes to Condensed Consolidated Financial Statements herein, on October 1, 2008, the company completed the acquisition of EnergySouth Inc. for \$511 million in cash and the assumption of debt. This acquisition will provide the company with a majority ownership in two large underground natural gas storage facilities that, when fully developed, will have capacity of 57 billion cubic feet of natural gas.

The company may be further impacted by the current world-wide economic crisis and rapidly changing economic conditions. The impacts of the global credit market crisis on the company's credit availability and cost are discussed in "Capital Resources and Liquidity" herein. Also, the dollar has strengthened significantly against all foreign currencies, especially in Mexico and South America where the company has significant operations. These factors, coupled with very low natural gas prices which affect profitability at Sempra Generation and Sempra LNG, could, if they remain unchanged, affect profitability. Additionally, given the uncertainty of commodity markets and the lack of bank borrowings for energy infrastructure, which impact related hedging activity, growth at RBS Sempra Commodities could be dampened.

Notes 7 and 8 of the Notes to Condensed Consolidated Financial Statements herein and Notes 14 through 16 of the Notes to Consolidated Financial Statements in the Annual Report also describe matters that could affect future performance.

## **Litigation**

Note 8 of the Notes to Condensed Consolidated Financial Statements herein and Note 16 of the Notes to Consolidated Financial Statements in the Annual Report describe litigation, the ultimate resolution of which could have a material adverse effect on future performance.

## **Sempra Utilities**

Note 7 of the Notes to Condensed Consolidated Financial Statements herein and Notes 14 and 15 of the Notes to Consolidated Financial Statements in the Annual Report describe electric and natural gas regulation and rates, and other pending proceedings and investigations.

## **Sempra Global**

On October 1, 2008, the company completed the acquisition of EnergySouth based in Mobile, Alabama, for \$511 million in cash and the assumption of debt.

Principal holdings of EnergySouth include EnergySouth Midstream, Inc. (EnergySouth Midstream) and Mobile Gas Service Corp.

EnergySouth Midstream is the general partner in and 91-percent owner of Bay Gas Storage Company (Bay Gas), a facility located 40 miles north of Mobile that provides underground storage and delivery of natural gas. It is the easternmost storage facility on the Gulf Coast, with direct service to the Florida market. Currently, Bay Gas has 11.4 Bcf of working natural gas storage capacity that is fully contracted and operational. An additional 5 Bcf is 64-percent contracted and under construction with a scheduled in-service date of mid-2010. There are plans to increase the total Bay Gas capacity to 27 Bcf of underground salt-dome storage.

EnergySouth Midstream also owns 60 percent of Mississippi Hub, LLC (Mississippi Hub), a company developing high-turn, underground salt-dome natural gas storage in Simpson County, Mississippi. This facility has planned direct interconnections to the natural gas production areas in eastern Texas, Oklahoma and Arkansas, as well as the Northeast market. Currently, Mississippi Hub's first 7.5 Bcf of storage capacity is in construction. Long-term commitments are in place for 4 Bcf of this capacity. Operations are slated to commence in mid-2010. There are plans to increase the total Mississippi Hub capacity to 30 Bcf of high-turn, salt-dome storage.

Mobile Gas Service Corp., an Alabama natural gas distribution utility, serves approximately 93,000 customers in southwest Alabama.

Sempra Pipelines & Storage's expansion of existing pipelines in Baja California, Mexico and the spur line to provide service to Sempra LNG's Energía Costa Azul terminal with interconnections to the U.S. border were placed in service in the second quarter of 2008.

In July 2008, Sempra Generation announced the planned development of a solar-energy project, a 10-megawatt (MW) photovoltaic power-generation site next to the company's El Dorado Energy power plant near Boulder City, Nevada. The project is expected to be completed by year-end.

As discussed in "Cash Flows From Investing Activities," the company's investments will significantly impact the company's future performance. Information regarding these investments is provided in "Capital Resources and Liquidity" herein and "Capital Resources and Liquidity" and "Factors Influencing Future Performance" in the Annual Report.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Certain accounting policies are viewed by management as critical because their application is the most relevant, judgmental and/or material to the company's financial position and results of operations, and/or because they require the use of material judgments and estimates. These accounting policies are discussed in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Annual Report.

The company's significant accounting policies are described in Note 1 of the Notes to Consolidated Financial Statements in the Annual Report.

## NEW ACCOUNTING STANDARDS

Recently issued pronouncements that have had or may have a significant effect on the company's financial statements are described in Note 2 of the Notes to Condensed Consolidated Financial Statements herein.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

On April 1, 2008, Sempra Energy and The Royal Bank of Scotland (RBS) completed the formation of their previously announced partnership, RBS Sempra Commodities LLP, to own and operate the commodity-marketing businesses previously held as subsidiaries of Sempra Energy. The company accounts for its investment in the partnership under the equity method. As a result of the transaction, Sempra Energy no longer holds directly the financial instruments related to these businesses that subjected the company to the market risk, commodities price risk and credit risk factors as discussed in the Annual Report. However, the joint venture partnership is still subject to these risks, which could impact Sempra Energy's portion of partnership earnings.

As of September 30, 2008, the total Value at Risk (VaR) of the Sempra Utilities' commodity positions was not material.

The company's one-year VaR for long-term debt has increased as a result of considerable interest-rate volatility during 2008. The following table shows the nominal amount and the one-year VaR for long-term debt, excluding commercial paper, at September 30, 2008 and December 31, 2007:

(Dollars in millions)	September 30, 2008		December 31, 2007	
	Nominal Debt	One-Year VaR	Nominal Debt	One-Year VaR
Utility fixed-rate*	\$ 2,793	\$ 738	\$ 2,655	\$ 480
Utility variable-rate*	\$ 411	\$ 39	\$ 418	\$ 9
Non-utility, fixed-rate and variable-rate*	\$ 1,959	\$ 368	\$ 1,482	\$ 130

\* After the effects of interest-rate swaps.

## ITEM 4. CONTROLS AND PROCEDURES

Company management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Exchange Act Rules 13a-15(f). The company has designed and maintains disclosure controls and procedures to ensure that information required to be

disclosed in the company's reports is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission and is accumulated and communicated to the company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating these controls and procedures, management recognizes that any system of controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired objectives and necessarily applies judgment in evaluating the cost-benefit relationship of other possible controls and procedures. In addition, the company has investments in unconsolidated entities accounted for using the equity method and consolidates a variable interest entity as defined in Financial Accounting Standards Board Interpretation No. 46(R) that it does not control or manage and consequently, its disclosure controls and procedures with respect to these entities are necessarily limited to oversight or monitoring controls that the company has implemented to provide reasonable assurance that the objectives of the company's disclosure controls and procedures as described above are met. Effective April 1, 2008, as discussed in Note 3 of the Notes to Consolidated Financial Statements herein, the company's commodity-marketing businesses are no longer wholly owned subsidiaries of the company. The company's ownership interests are reported on the equity method and are therefore subject to the controls and procedures applied to equity-method investments as discussed above.

There have been no changes in the company's internal control over financial reporting during the company's most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the company's internal control over financial reporting.

Under the supervision and with the participation of management, including the Chief Executive Officer and the Chief Financial Officer, the company evaluated the effectiveness of the design and operation of the company's disclosure controls and procedures as of September 30, 2008, the end of the period covered by this report. Based on that evaluation, the company's Chief Executive Officer and Chief Financial Officer concluded that the company's disclosure controls and procedures were effective at the reasonable assurance level.

## **PART II - OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

The Los Angeles Regional Water Quality Control Board has asserted violations of the California Water Code by SoCalGas in connection with certain maintenance activities in Los Angeles County's Sullivan Canyon. In June 2008, the board dismissed without prejudice a related lawsuit to provide an opportunity for the parties to resolve this matter without litigation. SoCalGas believes that the resolution will impose upon it fines and penalties of no more than \$750,000.

On July 13, 2007, SDG&E, one of its employees, and an SDG&E contractor were convicted in a federal jury trial on criminal charges of environmental violations in connection with the 2000 – 2001 dismantlement of a natural gas storage facility. SDG&E was also convicted of a related charge of making a false statement to a governmental agency. SDG&E is subject to a maximum fine of \$2 million. On December 7, 2007, the trial court set aside all of the convictions and granted all of the defendants a new trial on all counts. The government has appealed the trial court's decision.

Except for the matters described in Notes 7 and 8 of the Notes to Condensed Consolidated Financial Statements herein, neither the company nor its subsidiaries are party to, nor is their

property the subject of, any material pending legal proceedings other than routine litigation incidental to their businesses.

#### **ITEM 1A. RISK FACTORS**

There have been no material changes in risk factors as previously disclosed in the company's 2007 Annual Report on Form 10-K except as follows. Generally, there was a reduction in risks associated with Sempra Commodities as a result of the reduction of the company's interests in this business associated with the transaction with RBS discussed in Note 3 of the Notes to Condensed Consolidated Financial Statements herein. However, the company continues to provide back-up guarantees for certain trading obligations and credit facilities during the transition of the business to the partnership. RBS has fully indemnified the company in respect of any liabilities that the company may incur under the guarantees. These transitional measures are discussed in Note 5 of the Notes to Condensed Consolidated Financial Statements herein.

The recent global credit crisis has severely affected the availability and cost of both short-term and long-term financing. If cash flows from operations were to be significantly reduced or the company were to be unable to borrow under acceptable terms, the company would reduce or postpone discretionary capital expenditures, share repurchases and/or investments in new businesses.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

### Purchases of Equity Securities:

On September 11, 2007, the board of directors authorized the repurchase of additional shares of the company's common stock provided that the amounts expended for such purposes do not exceed the greater of \$2 billion or amounts expended to purchase no more than 40 million shares.

On April 1, 2008, the company entered into a Collared Accelerated Share Acquisition Program under which the company paid \$1 billion to repurchase shares of its common stock, as discussed in the company's Current Report on Form 8-K dated April 1, 2008 and in Note 4 of the Notes to Condensed Consolidated Financial Statements herein.

The following table sets forth information concerning purchases made by the company, from the programs authorized above, of its common stock during the third quarter of 2008:

	Total Number of Shares Purchased (1)	Average Price Paid Per Share (1)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Dollar Value of Shares that may Yet be Purchased Under the Plans or Programs
July 2008				
August 2008				
September 2008				
	(1)	(1)	(1)	\$1 billion remaining (2)

(1) The company's publicly announced Collared Accelerated Share Acquisition Program which began in April 2008 was completed on October 13, 2008. A total of 18,416,241 shares were purchased at a weighted average price of \$54.30 per share under this program, none of which were received in the third quarter of 2008. Additional information regarding the program is provided in Note 4 of the Notes to Condensed Consolidated Financial Statements herein.

(2) Approximately \$1 billion remains authorized by the board of directors for the purchase of additional shares. As a result of the recent crisis in the credit markets, the company's previously announced plans to purchase \$500 million in 2009 will be reevaluated in the first quarter of 2009. The company also may, from time to time, purchase shares of its common stock from restricted stock plan participants who elect to sell a sufficient number of vesting restricted shares to meet minimum statutory tax withholding requirements.

## ITEM 6. EXHIBITS

### Exhibit 10 -- Material Contracts

10.1 Sempra Energy Employee Stock Ownership Plan and Trust Agreement effective 1/1/2001.

### Exhibit 12 -- Computation of ratios

12.1 Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividends.

### Exhibit 31 -- Section 302 Certifications

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

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

### Exhibit 32 -- Section 906 Certifications

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

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

### Exhibit 99 -- Unaudited Pro Forma Condensed Consolidated Financial Information

99.1 Unaudited Pro Forma Condensed Statement of Consolidated Income for the Nine Months Ended September 30, 2008.

SIGNATURE

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

SEMPRA ENERGY,  
(Registrant)

Date: November 10, 2008

By: /s/ Joseph A. Householder

Joseph A. Householder  
Senior Vice President, Controller and  
Chief Accounting Officer

**SEMPRA ENERGY**

**EMPLOYEE STOCK OWNERSHIP PLAN AND TRUST AGREEMENT**

**(Formerly Known As PACIFIC ENTERPRISES  
EMPLOYEE STOCK OWNERSHIP PLAN AND TRUST AGREEMENT)**

**(As Amended and Restated Effective as of January 1, 2001)**

**SEMPRA ENERGY**

**EMPLOYEE STOCK OWNERSHIP PLAN AND TRUST AGREEMENT**

WHEREAS, the Thrifty Drug Stores Co. Inc. and Borun Bros. Retirement Plan and Trust Agreement was adopted, effective September 1, 1950, and has been amended from time to time;

WHEREAS, as a condition of the sale of Thrifty Corporation (the "Sale") the Employee Stock Ownership Plan was assumed by Pacific Enterprises and renamed the Pacific Enterprises Employee Stock Ownership Plan and Trust;

WHEREAS, further amendments have been made and it is desirable to incorporate these amendments in a single document;

WHEREAS, Pacific Enterprises is now a subsidiary of Sempra Energy; and

WHEREAS, Sempra Energy has replaced Pacific Enterprises as Plan Sponsor and Administrator of this Plan;

NOW, THEREFORE, the Sempra Energy Employee Stock Ownership Plan and Trust Agreement (Complete Restatement) is set forth completely herein as amended and restated effective as of January 1, 2001.

THIS AGREEMENT, made and entered into by and between Sempra Energy, a California corporation, and U.S. Trust Company, National Association, as Trustee, hereafter referred to as "Trustee," evidences this full restatement of the Pacific Enterprises Employee Stock Ownership Plan and Trust, hereafter referred to as either "the Plan" or "the Trust," heretofore established for qualified employees of the Companies. This Plan is a stock bonus plan qualified under Section 401(a) of the Code, is designated as an employee stock ownership plan as defined in Section 4975(e) (7) of the Code, and is designed to invest primarily in Stock.

W I T N E S S E T H

ARTICLE I.  
DESIGNATION OF TRUST

1.1 Title.

This retirement plan and trust agreement shall be known as "SEMPRA ENERGY EMPLOYEE STOCK OWNERSHIP PLAN AND TRUST AGREEMENT."

1.2 Definitions.

All capitalized terms used in this Plan shall have the meaning set forth in this Section 1.2 unless the context clearly indicates otherwise or such terms are not defined in this Section 1.2.

"Administrative Committee" or "Committee" shall mean the Sempra Energy Pension and Benefits Committee which has been appointed by resolution of the Board of Directors to administer the Plan pursuant to Article XV.

"Anniversary Date" shall mean the last day of each calendar month.

"Beneficiary" or "Beneficiaries" shall mean the person or persons, including a trustee, personal representative, or other fiduciary, last designated in writing by a Participant in accordance with the provisions of Section 3.2 to receive the benefits specified hereunder in the event of the Participant's death.

"Board of Directors" shall mean the Board of Directors of Sempra Energy.

"Break in Employment" shall mean any termination of employment by reason of resignation, discharge, death, or retirement, or any change in employment status by which a Participant ceases to meet the definition of Employee, except the

following periods of absence if the Employee was in the service of the Company on the date immediately preceding the commencement of such period:

(a) Service in the Armed Forces of the United States or the Public Health Service of the United States as a result of which such Employee is entitled to reemployment rights pursuant to the provisions of Section 459 of Title 50 of the United States Code, provided that the Employee returns to work within the time period specified in Section 459, failure to return within such time period deemed to constitute a Break in Employment as of the day following the date last worked.

(b) Leaves of absence granted by the employing Company in writing, before or after the absence, for any purpose, including sickness, accident, other casualty, or for the convenience of one of the Companies, and periods of vacation, and any extensions thereof. Failure to return to work at the completion of one of the periods set forth above or upon reasonable recall from absence granted will constitute a Break in Employment effective as of the last day of such period or as of the date of failure to return upon a date specified pursuant to such recall.

Notwithstanding the foregoing, an Employee who does not return to the service of one of the Companies as a result of the Employee's death during any period set forth above shall be deemed to have incurred a Break in Employment upon the date of death.

"Code" shall mean the Internal Revenue Code of 1986, as amended from time to time.

"Company" or "Companies" shall mean Sempra Energy, a California corporation; and unless the context indicates otherwise, any subsidiary which, by resolution of its board of directors and with the written approval of Sempra Energy elects or has elected to participate herein.

"Compensation" shall mean and include (subject to the provisions of subparagraph (a) or (b) below, as appropriate) the full amount of any salary, wage, bonus, shift differential, vacation or overtime pay, compensation paid during authorized leaves of absence, and similar payments made to or on behalf of an Employee during the time an Employee is a Participant and on account of employment (other than contributions to this Plan), all before reduction on account of any withholding such as income taxes, Social Security taxes, and amounts otherwise excludable from income by reason of Sections 125, 132(f)(9), 402(e)(3), 402(h)(1)(B) or 403(b), but excluding, however, health and welfare payments, meals, expense account allowances, maintenance payments, income realized on stock options and any other such payments.

Notwithstanding the foregoing, for any Plan Year commencing, the maximum amount of an Employee's Compensation taken into account under this Plan shall not exceed the dollar limitation then in effect under Section 401(a)(17) of the Code. For purposes of this Subsection, the applicable annual Compensation limit for any Plan Year shall be the limit in effect on January 1 of the calendar year that includes the first day of such Plan Year. If Compensation for a period of less than twelve (12) months is used for any Plan Year, then the otherwise applicable annual Compensation limit under this Subsection is reduced in the same proportion as the reduction in the twelve-month period. No proration shall be required solely because Compensation is limited to Compensation for the portion of Plan Year during which an Eligible Employee is an Active Participant.

"Effective Date" shall mean the original effective date of the Plan, September 1, 1950, provided, however, the effective date of this restatement of the Plan is January 1, 2002.

"Eligible Employee" shall mean every Employee of the Company including officers thereof, who are eligible to participate in a Company sponsored Plan. Eligible Employee shall exclude leased employees described in Section 414(n) of the Code. The provisions of each Plan hereunder and the eligibility of any Employee to participate therein shall be as set forth in the plan documents governing each such Plan, a current copy of which shall be attached hereto from time to time as an exhibit to this Plan.

"Employee" shall mean every employee of the Company or a Related Company.

"ERISA" shall mean the Employee Retirement Income Security Act of 1974, as amended from time to time.

“ESOP Suspense Account” shall mean the account established under Section 5.3 hereof to hold Stock purchased with the proceeds of an Exempt Loan pending the allocation of such Stock to individual ESOP accounts. A separate ESOP Suspense Account may be established with respect to each Exempt Loan made to the Plan and the provisions of this Plan may be applied, at the direction of the Committee, separately with respect to each ESOP Suspense Account or by combining such separate ESOP Suspense Accounts.

“Exempt Loan” shall mean any loan to the Plan or Trust not prohibited by Section 4975(c) of the Code, which meets the requirement set forth in Section 4975(d)(3) of the Code and the Regulations promulgated thereunder, the proceeds of which are used to finance the acquisition of Stock or refinance such a loan.

“Fiduciary” shall mean all persons defined in Section 3(21) of ERISA associated in any manner with the control, management, operation and administration of the Plan, and the Company shall be the “Named Fiduciary” for purposes of Section 402 of ERISA, except that each Participant shall be a named fiduciary for such purposes with respect to the exercise of voting rights under Section 8.1(n) and with respect to the issuance of instructions to the Trustees to tender or not tender Stock as permitted in Article XII of this agreement.

“Fiscal Year” shall mean the fiscal period employed by the Company for financial reporting purposes. The Plan Year and the Limitation Year, for purposes of this Plan, shall mean the calendar year.

“Hour of Service” shall mean:

- (a) Each hour for which an Employee is paid, or entitled to payment, by the Company or a Related Company for the performance of duties for the Company or a Related Company during any Plan Year;
- (b) Each hour for which an Employee is paid, or entitled to payment, by the Company or a Related Company on (4) Hours of Service shall not be credited for a payment which solely reimburses an Employee for medical or medically related expenses incurred by the Employee.
- (c) For purposes of determining Hours of Service and for purposes of determining to which Plan Year Hours of Service shall be credited, the rules set forth in Department of Labor Regulations 2530.200b-2(b) & (c) and other applicable regulations issued by the Department of Labor shall be followed, and such rules are incorporated herein by reference.

“Plan” shall mean a plan sponsored by Sempra Energy or any Related Company which is qualified under Code Section 401(a) and which permits employee deferral of compensation pursuant to Code Section 401(k).

“One Year Break in Service” shall mean a Plan Year in which the Employee completes 500 or fewer Hours of Service.

“Participant” shall mean any Eligible Employee who becomes eligible for participation in accordance with the provisions of this Plan.

“KPlan” shall mean a plan sponsored by Sempra Energy or any Related Company which is qualified under code Section 401(a) and which permits employee deferral of compensation pursuant to Code Section 401(k).

“Related Company” shall mean (i) each corporation which is a member of a controlled group of corporations (within the meaning of Section 1563(a) of the Internal Revenue Code, determined without regard to Section 1563(a)(4) and (e)(3)(C) thereof) of which the Company is a component member, (ii) each entity (whether or not incorporated) which is under common control with the Company, as such common control is defined in Section 414(c) of the Internal Revenue Code and Regulations issued thereunder, (iii) any organization which is a member of an affiliated service group (within the meaning of Section 414(m) of the Code) of which the Company is a member, and (iv) any leasing organization (as defined in Section 414(n) of the Code) to the extent its employees constitute leased employees (within the meaning of Section 414(n)) with respect to the Company; provided, however, for purposes of this Plan the phrase “more than 50 percent” shall be substituted for the phrase “at least 80 percent” each place it appears in Section 1563(a)(1) of the Code. Said term shall also include each predecessor employer as required by section 414(a) of the Code.

“Sponsor” shall mean Sempra Energy.

“Stock” shall mean the common stock of the Sponsor and any qualifying employer security as defined in Section 407(d)(5) of ERISA and Section 4975(e)(8) of the Code, any asset held temporarily pending investment in such a qualifying employer security and any security which is reasonably expected to become and which in a reasonable period does become such a qualifying employer security.

“Trust” shall mean the trust which is established to hold and invest contributions made under this agreement.

“Trustee” or “Trustees” shall mean the trustees named above or any successor acting as Trustee under the Trust.

“Year of Service” shall mean (i) each Plan Year in which the Employee completes or previously has completed 1,000 or more Hours of Service, and also (ii) the Plan Year in which the Employee becomes a Participant in cases where the eligibility requirements are satisfied over a period which encompasses more than one Plan Year.

## ARTICLE II. EMPLOYEES ENTITLED TO PARTICIPATE

### 2.1 Eligibility Requirements.

#### (a) Participants as of Date of Closing of Sale.

All Eligible Employees who were Participants on the Date of Closing of the Sale and were employed by the Company on the first day of the calendar month following the closing of the Sale shall continue as Participants.

#### (b) Other Employees.

All other present and future Eligible Employees who were employed or shall become employed by the Company shall become eligible to participate in this Plan on the first day that they become eligible to participate in a Company- sponsored KPlan.

#### (c) Reemployed Participants.

If a Participant incurs a Break in Employment and subsequently is reemployed, participation in this Plan shall resume on the first day of such reemployment.

#### (d) Change of Employment Status.

For purposes of this Section 2.1, any person who becomes an Eligible Employee after employment by a Related Company shall become eligible to participate in this Plan on the first day of the first pay period after such person has both been employed by the Company and has satisfied the eligibility requirements of this Section 2.1, taking such employment with a Related Company into account. In addition, any Employee who has been excluded from Eligible Employee status who becomes an Eligible Employee after such exclusion shall become eligible to participate in this Plan on the first day of the first pay period after such person has both attained Eligible Employee status and has satisfied the eligibility requirements of this Section 2.1, taking such previous employment with the Company into account.

#### (e) Inactive Participants.

Any person for whom an account is maintained under the Plan, but who does not satisfy the current eligibility requirements of this Article II shall be an Inactive Participant. Inactive Participants shall not be entitled to allocations under Sections 6.6 and 11.10 with respect to any period for which they are Inactive Participants.

## ARTICLE III. PARTICIPATION IN THE PLAN

### 3.1 Participation.

Employees become Participants in accordance with Section 2.1. The Committee shall notify each Employee within a reasonable time of the date that the Employee becomes a Participant in this Plan.

### 3.2 Designation of Beneficiary.

Each Employee who becomes a Participant shall designate in writing the Beneficiary or Beneficiaries whom such Employee desires to receive the benefits under the Company-sponsored KPlan (for which he is then eligible) in the event of his death. The Beneficiary designation for such KPlan, and the rules and interpretations thereunder in the event of a failure, lapse or other irregularity in the Beneficiary designation shall in all cases be controlling for this Plan.

### 3.3 Termination or Suspension of Participation.

Participation of a Participant shall commence as of the first day of eligibility as determined under Section 2.1 and shall continue during subsequent employment with the Company or a Related Company and until the date on which the Participant has a Break in Employment.

A person may not withdraw from participation under this Plan except by termination of the Participant's employment with the Company and all Related Companies.

## ARTICLE IV. CONTRIBUTIONS BY PARTICIPATING EMPLOYEES

### 4.1 Participants Not Required to Contribute.

The benefits under this Plan arise solely from contributions made by the Companies, and Participants are not required to make any contributions hereunder. Provided, however that benefits hereunder are contingent upon employee deferrals to a Company-sponsored KPlan, with the exception of benefits resulting from allocations made under Section 6.6(c).

## ARTICLE V. COMPANY CONTRIBUTIONS

### 5.1 Obligation.

The Companies, subject to their rights under Article X, will make contributions to the Trust for each Fiscal Year in the amounts determined as set forth in Section 5.2. All payments of contributions shall be made directly to the Trustee and may be made on any date or dates selected by the Companies; provided, however, that the total annual contribution of each Company shall be paid on or before the date on which the federal income tax return of such Company is due, including any extensions of time obtained for the filing thereof. The Trustee agrees to hold and administer the contributions of the Companies in trust pursuant to the terms of this agreement.

### 5.2 Company Contributions:

#### (a) General Contributions.

Each Plan Year the Companies shall contribute such amounts as the Board of Directors may determine in its sole discretion.

#### (b) Limitation.

In no event shall a Company's contribution for any taxable year exceed an amount equal to fifteen percent (15%) of the Compensation paid by it during the taxable year to all its Participants under this Plan. If in any Fiscal Year the contribution of the Company is less than fifteen percent (15%) of the total Compensation otherwise paid or accrued to all Participants employed by the Company for such Fiscal Year, the difference between the amount contributed and said fifteen percent (15%) may be carried forward and contributed in succeeding Fiscal Years in order of time; provided, however, in no event shall the amount to be carried forward to a succeeding Fiscal Year exceed fifteen percent (15%) of the total Compensation paid or accrued to all Participants employed by the Company for such succeeding Fiscal Year nor shall contributions in such succeeding Fiscal Year be made which would violate the prohibitions of Section 6.6 hereof. To the

extent that contributions are made to service principal payments on an Exempt Loan, the fifteen percent (15%) limitation of this Section 5.2(c) shall be increased to twenty five percent (25%) plus an amount equal to the contributions used to service interest on such Exempt Loan.

### 5.3 Exempt Loans.

The Trustees may cause the Trust to enter into one or more Exempt Loans to finance the acquisition of Stock or refinance an existing Exempt Loan. Notwithstanding anything contained herein to the contrary, proceeds of an Exempt Loan shall be used, within a reasonable time after receipt by the Trust, only for the following purposes:

- (a) to acquire stock;
- (b) to repay principal and interest with respect to the same Exempt Loan; or
- (c) to repay principal and interest with respect to any previous Exempt Loan.

An Exempt Loan shall be repaid only from amounts and the proceeds of such loan, from Company contributions in cash and earnings attributable thereto, from any collateral given for the loan, and from dividends paid on Stock (whether or not allocated to Participants).

Stock acquired by the Plan through an Exempt Loan shall be added to and maintained in the ESOP Suspense Account and shall thereafter be released from the ESOP Suspense Account and allocated to accounts of Participants as provided in Sections 6.5 and 6.6.

## ARTICLE VI. ALLOCATION TO PARTICIPANTS' ACCOUNTS

### 6.1 Participant's ESOP Account.

The Administrative Committee shall establish an ESOP account for each Participant which account shall be credited quarterly with such Participant's share of Company contributions as allocated to such Participant pursuant to this Article VI. Such allocated account balance for each Participant shall be transferred to the KPlan in which he participates as provided in Section 6.6(b) and (c). A transfer made pursuant to this Section 6.1 and Section 6.6 (other than Section 6.6(c)) shall be deemed to satisfy the Employer matching obligation under the KPlan to the extent of the transfer. The Committee shall notify each Participant that a transfer to the Participant's KPlan account has been made.

Such notification shall be made no less frequently than annually. The fact of such allocation and notification shall not vest in any Participant any right, title or interest in the Trust assets, except at the time or times and upon the terms and conditions herein provided and shall not create any liability against the Companies or the Trustees except to the extent expressly herein provided.

### 6.2 Forfeitures.

Any amount credited to a Participant's ESOP account shall be fully vested and nonforfeitable.

### 6.3 Evaluation of Participants' Accounts.

Annually, as of each Anniversary Date, and more often as it deems appropriate the Trustee shall revalue the Trust assets, excluding the Companies' contributions made to the Trustees as of that day and excluding all Stock in the ESOP Suspense Account, so as to reflect any increase or decrease in the market or cash value of all such assets compared with the value of such assets as of the next preceding Anniversary Date. Any such increase or decrease shall be allocated among accounts of Participants and Inactive Participants in the proportion that the balance of each such account as of the immediately preceding Anniversary Date bears to the total balance of all such accounts as of such immediately preceding Anniversary Date. The Companies and the Trustees do not in any manner or to any extent whatever warrant, guarantee or represent that the value of a Participant's account shall at any time equal or exceed the amounts previously contributed thereto by the Companies and shall not be liable or responsible for the inadequacy of the Fund to meet and discharge any or all payments and liabilities under this Plan.

### 6.4 Companies' Contributions.

The Companies' contributions for each Fiscal Year shall be used by the Trustee to make payments of principal and interest on the Exempt Loan(s).

#### 6.5 Release from ESOP Suspense Account.

Stock acquired for the Trust through an Exempt Loan shall be released from the ESOP Suspense Account when the Exempt Loan is repaid in accordance with the provisions of this Section 6.5.

- (a) For each calendar month until the Exempt Loan is fully repaid, the number of shares of Company Stock released from the ESOP Suspense Account shall equal the number of unreleased shares immediately before such release of the current calendar month multiplied by the "Release Fraction." As used herein, the Release Fraction shall be a fraction the numerator of which is the amount of principal and interest paid on the Exempt Loan for such current calendar month and the denominator of which is the sum of the numerator plus the principal and interest to be paid on such Exempt Loan in all future calendar months during the duration of the term of such Exempt Loan (determined without reference to any possible extensions of renewals thereof). Notwithstanding the foregoing, in the event such Exempt Loan shall be repaid with the proceeds of a subsequent Exempt Loan (the "Substitute Loan"), such repayment shall not operate to release all such Stock in the ESOP Suspense Account, but, rather, such release shall be effected pursuant to the foregoing provisions of this Section 6.5 on the basis of payments of principal and interest on such Substitute Loan.
- (b) If required by any financing or similar agreement, in lieu of applying the provisions of Section 6.5(a) hereof with respect to such Exempt Loan or Substitute Loan, shares shall be released from the ESOP Suspense Account as the principal amount of an Exempt Loan is repaid (and without regard to interest payments), provided the following three conditions are satisfied:
- (1) The Exempt Loan must provide for annual payments of principal and interest at a cumulative rate that is not less rapid at any time than level annual payments of such amounts for ten years.
  - (2) The interest portion of any payment is disregarded only to the extent it would be treated as interest under standard loan amortization tables.
  - (3) If the Exempt Loan is renewed, extended or refinanced, the sum of the expired duration of the Exempt Loan and the renewal, extension or new Exempt Loan period must not exceed ten years.
- (c) It is intended that the provisions of this Section 6.5 shall be applied and construed in a manner consistent with the requirements and provisions of Treasury Regulation 54.4975-7(b)(8), and any successor regulation thereto. All Stock released from the ESOP Suspense Account during any Plan Year shall be allocated among Participants as prescribed by Sections 6.6 and 11.10.

#### 6.6 Allocation of Shares Released from ESOP Suspense Account.

Shares of Stock released from the ESOP Suspense Account for a calendar month in accordance with Section 6.5 hereof shall be held in the Trust on an unallocated basis until allocated on, or before, the Anniversary Date of that Plan Year. Except with respect to shares released from the ESOP Suspense Account through use of dividends on shares allocated to Participants, the allocation of such shares among the accounts of Participants shall be made in accordance with the following.

- (a) On or about the last day of each calendar month as well as on or before each Anniversary Date shares shall be allocated to Participants' ESOP accounts. The number of shares to be allocated for a calendar month other than a calendar month ending with the Anniversary Date shall be equal to the lesser of (i) the number of shares required for the employer matching contribution for the Company KPlans for such calendar month, and (ii) the number of shares released from the ESOP

Suspense Account since any prior allocation. The number of shares allocated as of the Anniversary Date shall be all shares released but not previously allocated during the Plan Year.

- (b) Shares shall be allocated to a Participant's ESOP accounts by first determining the number of shares to which the Participant is entitled as an employer matching contribution under the Company sponsored KPlan in which he or she participates from the last allocation date up through the present allocation date. That number of shares and partial shares shall form the numerator of a fraction, the denominator of which is the total number of shares to which all Participants are entitled to as an employer matching contribution in all Company sponsored KPlans. That fraction shall be multiplied by the total number of shares to be allocated and the resulting number of shares and partial shares shall be allocated to each Participant's ESOP account.

Notwithstanding the foregoing, the aggregate number of shares allocated under this Section 6.6(b) shall not exceed the number of shares to which all Participants are entitled as an employer matching contribution under the KPlans. As of the end of each calendar month, amounts allocated under this Section 6.6(b) to each Participant's ESOP account shall be transferred to that Participant's KPlan account.

- (c) In the event that there remain shares to be allocated after allocations under Section 6.6(b) are complete, the excess shall be allocated to each Participant who is an Eligible Participant (as defined below) in the same proportion that his or her Compensation bears to the aggregate Compensation of all Eligible Participants. "Eligible Participant" shall mean a Participant who (i) is employed by the Company on the Anniversary Date, and (ii) whose terms of employment are not governed by a collective bargaining agreement, unless an applicable collective bargaining agreement removes this condition. As of the end of each Plan Year, amounts allocated under this Section 6.6(c) to a Participant's ESOP account shall be transferred to that Participant's KPlan account.

- (d) The allocation of shares released from the ESOP Suspense Account on account of payment of exempt loans from dividends allocated to Participants' accounts shall be as provided in Section 11.10. All Stock in the Trust, other than Stock held in the ESOP Suspense Account as of an Anniversary Date, must be allocated to Participant ESOP accounts as of such date.

#### 6.7 Limitation on Annual Additions.

Notwithstanding anything else contained herein, the Annual Additions, as defined in Appendix A, to the ESOP account of a Participant shall not exceed the lesser of \$30,000 (as adjusted for increases in the cost of living as described in Code Section 415(d)) or 25% of the Participant's Section 415 Compensation from the Company and all Related Companies during the Plan Year, in accordance with the provisions of Appendix A attached hereto. If, in any Plan Year, no more than one-third of contributions to the Plan are allocated to Participants who are Highly Compensated Employees, the \$30,000 limitation (as adjusted) shall be increased by the lesser of \$30,000 or the amount of Stock contributed or purchased with cash contributed to the Plan and the above limitations shall not apply to contributions to the Plan which are used to make interest payments under an Exempt Loan.

#### 6.8 Special Limitations on 401(m) Contributions.

With respect to each Plan Year, any Employer matching contributions, as defined in Section 401(m) of the Code, and Employee "after-tax contributions," as defined in regulations under Section 401(m) of the Code, under the Plan for the Plan Year (hereafter referred to collectively as "401(m) Contributions") shall not exceed the limitations on such contributions by or on behalf of Highly Compensated Employees under Section 401(m) of the Code, as provided in this Section. For purposes of this Section 6.8, any allocations made pursuant to Section 6.6(b) shall be treated as 401(m) Contributions. In the event that 401(m) Contributions under this Plan by or on behalf of Highly Compensated Employees for any Plan Year exceed the limitations of this Section for any reason, such excess 401(m) Contributions and any income allocable thereto shall be disposed of in accordance with Section 6.9.

- (a)

401(m) Contributions by and on behalf of Participants for a Plan Year shall satisfy the Average Contribution Percentage test set forth in (i)(A) below or the alternative Average Contribution Percentage test set forth in (i)(B) below, or to the extent required by regulations under Code Section 401(m), shall satisfy the test identified in (ii) below.

(i) (A) The Average Contribution Percentage for Eligible Employees who are Highly Compensated Employees shall not be more than the Average Contribution Percentage of all other Eligible Employees multiplied by 1.25, or

(B) The excess of the Average Contribution Percentage for Eligible Employees who are Highly Compensated Employees over the Average Contribution Percentage for all other Eligible Employees shall not be more than two (2) percentage points, and the Average Contribution Percentage for the Highly Compensated Employees shall not be more than the Average Contribution Percentage of all other Eligible Employees multiplied by 2.00.

(ii) The Average Contribution Percentage for Highly Compensated Employees eligible to participate in this Plan and a plan of the Company or a Related Company that satisfies the requirements of Section 401(k) of the Code, including, if applicable, this Plan, shall be reduced to the extent necessary to satisfy the requirements of Treasury Regulations Section 1.401(m)-2 or similar such rule relating to the multiple use of the alternative test described in (i) (B) above.

(b) For purposes of Sections 6.8, 6.9 and 6.10, the following definitions shall apply:

(i) "Average Contribution Percentage" means, with respect to a group of Eligible Employees for a Plan Year, the average of the Contribution Percentage, calculated separately for each Eligible Employee in such group.

(ii) The "Contribution Percentage" means for any Eligible Employee the percentage determined by dividing the sum of 401(m) Contributions under the Plan on behalf of each Eligible Employee for such Plan Year, by such Eligible Employee's Compensation for such Plan Year in accordance with regulations prescribed by the Secretary of the Treasury under Code Section 401(m). To the extent determined by the Committee and in accordance with regulations issued by the Secretary of the Treasury under Code Section 401(m)(3), elective deferrals on behalf of an Eligible Employee and any qualified nonelective contributions, within the meaning of Code Section 401(m)(4)(C), on behalf of an Eligible Employee may also be taken into account for purposes of calculating the Contribution Percentage of such Eligible Employee, but shall not otherwise be taken into account.

(iii) "Compensation" means Compensation determined by the Committee in accordance with Section 414(s) of the Code, including to the extent determined by the Committee, amounts deducted from an Employee's wages or salary that are not currently includable in the Employee's gross income by reason of the application of Code Sections 402(e)(3), 125 or 132(f)(4).

(iv) "Highly Compensated Employee" shall have the meaning ascribed to it in Section 6.10.

(c) In the event that as of the last day of a Plan Year this Plan satisfies the requirements of Section 410(b) of the Code only if aggregated with one or more other plans, or if one or more other plans satisfy the requirements of Section 410(b) of the Code only if aggregated with this Plan, then this Section shall be applied by determining the Contribution Percentages of Eligible Employees as if all such plans were a single plan, in accordance with regulations prescribed by the Secretary of the Treasury under Section 401(m) of the Code.

(d)

For the purposes of this Section, the Contribution Percentage for any Eligible Employee who is a Highly Compensated Employee under two or more Code Section 401(a) plans of a Company or a Related Company to the extent required by Code Section 401(m), shall be determined in a manner taking into account the participant after-tax contributions and matching contributions for such Eligible Employee under each of such plans.

(e) The determination and treatment of the Contribution Percentage of any Participant shall satisfy such other requirements as may be prescribed by the Secretary of the Treasury.

(f) The Committee shall keep or cause to have kept such records as are necessary to demonstrate that the Plan satisfies the requirements of Code Section 401(m) and the regulations thereunder, in accordance with regulations prescribed by the Secretary of the Treasury.

6.9 Provisions for Reduction of Excess 401(m) Contributions by or on Behalf of Highly Compensated Employees.

(a) The Committee shall determine, as soon as is reasonably possible following the close of the Plan Year, if 401(m) Contributions by or on behalf of Highly Compensated Employees satisfy the Average Contribution Percentage test for such Plan Year. If, pursuant to the determination by the Committee, 401(m) Contributions by or on behalf of a Highly Compensated Employee must be reduced to enable the Plan to satisfy the Average Contribution Percentage test, then to the extent necessary to eliminate the excess, excess 401(m) Contributions made on behalf of such Highly Compensated Employee (and income, allocable to such excess 401(m) Contributions) shall be distributed (after withholding any applicable income tax on such amounts). If administratively feasible, excess 401(m) Contributions and income allocable thereto, shall be distributed to Highly Compensated Employees within two and one-half (2½) months following the close of the Plan Year for which the excess Contributions were made, but in any event no later than the end of the first Plan Year following the Plan Year for which the excess Contributions were made, notwithstanding any other provision in this Plan. A distribution made pursuant to this Section 6.9(a) may be made from this Plan or from the KPlan to which excess 401(m) Contributions have been transferred for the Participant receiving the distribution. A distribution under this Section 6.9(a) shall be deemed to satisfy the Employer matching obligation under the KPlan to the extent of the distribution. If it becomes necessary to distribute amounts hereunder in order to satisfy the requirements of Code Section 401(m), distributions first shall be made from the portion of a Participant's account consisting of Company Stock.

(b) The Committee shall determine the amount of any excess 401(m) Contributions made by or on behalf of Highly Compensated Employees for a Plan Year on the basis of the respective portions of excess 401(m) Contribution made on behalf of such Highly Compensated Employees. Excess 401(m) Contributions shall be distributed by reducing the 401(m) Contributions of the Highly Compensated Employee with the highest dollar amount of such 401(m) Contributions and so forth until the Plan satisfies the Average Contribution Percentage test. For each Highly Compensated Employee, the amount of excess 401(m) Contributions shall be equal to the total 401(m) contributions (plus any amounts treated as matching contributions) made on behalf of such Highly Compensated Employee (determined prior to the application of the foregoing provisions of this subparagraph (b)) minus the amount determined by multiplying the Highly Compensated Employee's Contribution Percentage (determined after the application of the foregoing provisions of this subparagraph (b)) by his Compensation.

(c) For purposes of satisfying the Average Contribution Percentage test, income allocable to a Participant's excess 401(m) Contributions, as determined under (b) above, shall be determined in accordance with any reasonable method used by the Plan

for allocating income to Participant Accounts, provided such method does not discriminate in favor of Highly Compensated Employees and is consistently applied to all Participants for all corrective distributions under the Plan for a Plan Year.

Alternatively, the Committee may determine that income on excess 401(m) Contributions shall be calculated in accordance with the method set forth in the KPlan. The Committee shall not be liable to any Highly Compensated Employee (or his Beneficiary, if applicable) for any losses caused by misestimating the amount of any excess 401(m) Contributions on behalf of a Highly Compensated Employee and the income attributable to such excess.

- (d) To the extent required by regulations under Section 401(m) or 415 of the Code, any 401(m) Contributions in excess of the limitations of Section 6.8 distributed to a Highly Compensated Employee in accordance with the applicable provisions of the KPlan shall be treated as an Annual Addition under Section 6.7 for the Plan Year for which the excess 401(m) Contribution was made, notwithstanding such distribution.

#### 6.10 Highly Compensated Employee

- (a) A Highly Compensated Employee includes highly compensated active employees and highly compensated former employees.
- (b) A highly compensated active employee includes any Employee who performs service for an Employer during the determination year and who, during the look back year: (i) received compensation from the employer in excess of \$80,000 (as adjusted pursuant to section 415(d) of the Code) and was a member of the top-paid group for such preceding year; or (ii) who is a 5 percent owner at any time during the look-back year or determination year.
- (c) For this purpose, the determination year shall be the Plan Year. The look-back year shall be the twelve-month period immediately preceding the determination year.
- (d) A highly compensated former employee includes any Employee who separated from service (or was deemed to have separated) prior to the determination year, performs no service for an Employer during the determination year, and was a highly compensated active employee for either the separation year or any determination year ending on or after the Employee's 55<sup>th</sup> birthday.
- (e) The determination of who is a Highly Compensated Employee, including the determinations of the number and identity of Employees in the top-paid group, will be made in accordance with section 414(q) of the Code and the regulations issued thereunder.

### ARTICLE VII. BENEFITS

#### 7.1 Vesting of Interests.

The interests of each Participant in the Participant's ESOP account shall at all times be fully vested and non-forfeitable.

#### 7.2 Distribution of Benefits.

The benefit distributable to a Participant from the Participant's ESOP account upon termination of participation shall be the equivalent of the shares credited to the Participant's ESOP account as of the date on which the distribution is to occur. Generally, the timing of the transfer of ESOP account balances to KPlans will be such that, all distributions shall be made from the respective KPlans rather than this Plan. Payment of such benefit shall occur, notwithstanding anything to the contrary contained herein, no later than 60 days following the close of the later of the Plan Year in which the Participant attains age 65 or the Plan Year in which the Participant has a Break in Employment (unless the Participant or Beneficiary elect otherwise or unless the amount of the Participant's benefit has not been calculated by that date or the Participant cannot be located, in which case distribution shall occur no later than 60 days after the payment can be calculated or the Participant located).

When a Participant ceases to participate, the Participant or the Participant's Beneficiary shall have the right to demand whether from this Plan or from the Participant's KPlan; by delivery to the Company of an election within ten days after an election form has been delivered, that the benefit be distributed in whole shares of Stock with cash distributed in lieu of any fractional share based on the value of the Stock on the Settlement Date as defined in the KPlan. Subject to the condition in the judgment of the Committee that cash in the trust is available, if no such election is made within such period, the benefit distributable to a Participant or Beneficiary shall be made solely in cash and distributed in a single lump sum. If cash is not available, the distribution shall be made in a single distribution in whole shares of Stock with cash distributed in lieu of any fractional share based on the value of the Stock on the Settlement Date as defined in the KPlan. If the nonforfeitable balance in the Participant's ESOP account at the time participation ceases exceeds \$5,000, distribution shall be made upon a Break in Employment only if the Participant consents to a distribution of the nonforfeitable balance of the Participant's ESOP account in writing. If the Participant does not so consent (unless Treasury regulations otherwise provide and the Committee adopt different rules), the distribution of the amounts payable shall be delayed until after the end of the Plan Year in which occurs the Participant's death or the attainment of age 65. If the nonforfeitable balance in the Participant's ESOP account at the time participation ceases is \$5,000 or less, distribution shall be made whether or not the consent of the Participant is obtained.

Any Inactive Participant who attains age 65 may elect to withdraw 100%, and not less than 100%, of the portion of such individual's ESOP account which is attributable to benefits accrued under the Plan prior to the date of the closing of the Sale. Such election shall be in a form prescribed by the Committee and may be made at any time. Such individual's ESOP account shall be valued for purposes of Section 6.3 as of the date the individual's fully completed election is acknowledged as received by the Committee or its delegate. Distribution of benefits from the ESOP account shall be accomplished as soon as practicable after receipt of such election. The in-service distribution right described in this paragraph shall be applicable only with respect to benefits accrued under the Plan as of the date of closing of the Sale.

Distribution of a Participant's benefit as set forth above shall be full payment in satisfaction of any obligation of the Companies or Trustees hereunder.

Notwithstanding anything to the contrary contained herein, distribution under the Plan shall comply with Section 401(a)(9) of the Code and regulations promulgated thereunder. Accordingly, unless otherwise permitted by law, the entire interest of each Participant shall be distributed, by April 1 of the calendar year following the later of (i) calendar year in which the Participant reaches age 70½, or (ii) for any Participant who is not a five percent owner of the Company (as defined in Code Section 416) at any time during the Plan Year ending with or within the calendar year in which the Participant retires. Each Participant who is a five percent owner for the Plan Year ending in the calendar year in which such Participant attains age 70½, shall have his or her ESOP accounts distributed by April 1 following the calendar year in which such Participant attains age 70½. Distribution shall be made over a period not greater than the life of such Participant (or over the lives of the Participant and the Participant's Beneficiary) or over a period not extending beyond the life expectancy of the Participant (or over a period not extending beyond the life expectancy of the Participant and the Participant's Beneficiary). If a distribution has begun in accordance with the preceding sentence and the Participant dies before the entire interest has been distributed to the Participant, the remaining portion of the Participant's interest shall be distributed at least as rapidly as under the method of distribution being used under the preceding sentence as of the date of death. If a Participant dies before the distribution of the Participant's interest has begun, the entire interest shall be distributed within five years after the date of death unless the requirements of one of the two following exceptions are satisfied:

- (a) The Participant's interest will be distributed to a Beneficiary over the life of such Beneficiary or over a period not extending beyond the life expectancy of such Beneficiary and the distributions begin not later than one year following the date of the Participant's death (or such later date as permitted by law), or
- (b) the Participant's interest will be distributed to or for the benefit of the Participant's surviving spouse over the life expectancy of such surviving spouse or over a period not extending beyond the life expectancy of such surviving spouse and the distributions begin no later than the date on which the Participant would have attained age 70½ (if the surviving spouse dies

before such distributions begin, this second exception shall be applied as if the surviving spouse were the Participant). For purposes of this paragraph and to the extent permitted by law, any amount paid to a Participant's child shall be treated as if it had been paid to the Participant's surviving spouse if such amount will become payable to the surviving spouse upon such child reaching majority (or other designated event permitted by law).

Subject to the foregoing, benefits payable upon the death of a Participant shall be transferred to the KPlan in which the Participant participates and shall be distributed from the KPlan in accordance with the provisions of the KPlan.

### 7.3 Inability to Locate Participant.

If a distribution to a Participant or Beneficiary is not made within three years after such distribution would otherwise be payable because such Participant or Beneficiary cannot be located, the Committee shall direct the Trustee to forfeit such amount to the Participants KPlan. The forfeited amount shall be reallocated (as of the Anniversary Date coincident with or next succeeding the expiration of the aforesaid time limit) to the KPlan participants in accordance with such KPlan. If, after such forfeiture, the Participant or Beneficiary later claims such benefit, such account shall be reinstated under the terms of such KPlan.

### 7.4 Diversification.

A Participant may elect, within 90 days after the close of the first Plan Year after the Plan Year when the Participant becomes a Qualified Participant and within 90 days of the close of each of the four succeeding Plan Years, to direct the investment of 25% of the total value of such Participant's ESOP account (to the extent such value is not subject to a prior election pursuant to this Section 7.5). Such a Qualified Participant may also elect, within 90 days after the close of the Plan Year within which the last such election is offered, to direct the investment of 50% of the total value of the Participant's ESOP account, to the extent such value is not subject to a prior election pursuant to this Section 7.5. The determination of the value subject to Participant investment direction pursuant to this Section 7.5 shall be based on the value of the Participant's ESOP account on the Anniversary Date preceding any election. For purposes of this Section 7.5 a "Qualified Participant" shall mean an individual who (a) has completed at least ten years of participation under this Plan after addition of the ESOP Feature on September 1, 1984 and (b) has attained age 55.

An individual who is a "Qualified Participant" hereunder shall have with respect to any share of Stock transferred to a KPlan under Section 6.6, such rights as such participant would have had under Code Section 401(a) (28) had such share of Stock remained in this Plan.

## ARTICLE VIII. RIGHTS AND DUTIES OF TRUSTEES

### 8.1 Investments.

The assets of the Trust (except for those assets the investment of which is directed by Participants under section 7.5) shall be invested exclusively in Stock except for the purposes of making Plan distributions to Participants or paying Plan administrative expenses, or pending the investment of contributions or other cash receipts in Stock, or pending repayment of an Exempt Loan. Notwithstanding anything contained in this agreement to the contrary, funds received by the Trust for the purpose of the payment of an Exempt Loan may be invested in any and all reasonable cash equivalent money market investments, including but not limited to, certificates of deposit, Eurodollar time deposits, commercial paper, money market funds, and specifically including investment in U.S. Trust Market Rate Accounts.

The Trustee shall have the authority and power to:

- (a) sell, transfer, mortgage, pledge, lease or otherwise dispose of, or grant options with respect to any Trust assets at public or private sale;
- (b) borrow from any lender (including the Sponsor or any shareholder of the Sponsor) pursuant to an Exempt Loan, as defined in the Plan, to acquire Stock as authorized by this Agreement, to enter into lending agreements upon any terms (including

reasonable interest and security for the loan) as may be appropriate or necessary; provided, that where required by Section 4975(e)(7) of the Code and regulations thereunder, any collateral given by the Trustees shall be limited to Stock acquired with the proceeds of such loan, and any loan incurred by the Trust for the acquisition of Stock shall be repaid by the Trustees only from contributions to the Trust by the Companies and earnings thereon, dividends on Stock acquired with borrowed funds, the proceeds of other such loans, and earnings upon any collateral given for the loan;

- (c) vote any stocks, including Stock in accordance with Section 8.1(n) of the Plan (and subject to Article XII hereof), bonds or other securities held in the Trust, or otherwise consent to or request any action on the part of the issuer in person or by proxy;
- (d) purchase or offer to purchase any security including Stock from any individual or entity either on an established market or directly from such individual or entity, without regard to any prevailing market price;
- (e) give general or specific proxies or powers of attorney with or without powers of substitution;
- (f) participate in reorganizations, recapitalizations, consolidations, mergers, liquidations and similar transactions with respect to Stock or any other securities, or any entity in which assets of the Trust are invested;
- (g) deposit such Stock or other securities in any voting trust, or with any protective or like committee, or with a trustee or with depositories designated thereby;
- (h) exercise any options, subscription rights and conversion privileges;
- (i) sue, defend, compromise, arbitrate or settle any suit or legal proceeding or any claim due them or on which they are liable;
- (j) contract or otherwise enter into transactions between themselves as Trustees and the Sponsor, its subsidiaries and affiliates, or any Sponsor shareholders, for the acquisition or sale of Stock;
- (k) perform all acts which the Trustees shall deem necessary or appropriate and exercise any and all powers and authority of the Trustees under this Agreement;
- (l) exercise any of the powers of an owner, with respect to such Stock and other securities or other property compromising the Trust assets;
- (m) form or incorporate and own or maintain any entity including but not limited to a partnership, corporation or trust;
- (n) vote any Stock only in accordance with the following provision:
  - (i) As of the record date immediately preceding the meeting there shall be no allocated shares which have not been transferred to a KPlan.
  - (ii) The Trustee shall vote all unallocated shares of Stock in accordance with instructions received from the Committee which shall be the named Fiduciary for the purpose of voting such shares.
  - (iii) Any materials prepared by parties other than the Sponsor with respect to any contested matter concerning any meeting or submission of consent forms shall be mailed directly to the Participants by the Trustee upon payment in advance by such parties of all reasonable expenses of Trustee in connection therewith; and
  - (iv) The Trustee shall adopt such procedures as shall best implement and carry out the foregoing provisions of this subparagraph (n);
  - (v) Participants shall retain such voting rights as is required by Code Section 409(e) with respect to allocated shares transferred from this Plan to a KPlan.
- (o) generally do all such acts, execute all such instruments, take all such proceedings, and exercise all such rights and privileges with relation to property constituting reasonable expenses of Trustee in connection therewith; and

(vii) The Trustee shall adopt such procedures as shall best implement and carry out the foregoing provisions of this subparagraph (n);

(p) generally do all such acts, execute all such instruments, take all such proceedings, and exercise all such rights and privileges with relation to property constituting the assets of the Trust as if the Trustee was the absolute owner thereof; subject to the foregoing.

The Trust shall be held, administered, invested and reinvested in the manner provided herein as a single fund, without distinction between principal and income, and the Trustee shall not be required to segregate or invest separately any share of any Participant in the Trust. In addition to the powers provided above, the Trustee may borrow or lend money, encumber the Trust or any of its property, and obligate the Trust for repayment, upon such terms and conditions as the Trustee may determine, except the Trustee shall not either directly or indirectly borrow from, lend to, or encumber the Trust or any of its properties in a manner which would constitute a prohibited transaction under, Section 4975 of the Code.

#### 8.2 Collection of Principal and Income.

The Trustee shall collect the principal and income of the Trust as the same shall become due and payable and may give binding receipt therefor. If at any time there shall be a default in the payment of such principal or income, or any controversy shall arise with respect to obligations or liabilities due to or from the Trustee, including any claim that may be asserted for taxes, the Trustee shall take such action as it deems advisable, whether by legal proceedings, compromise or otherwise. The Trustee shall be under no obligation to take any legal action of whatever nature, unless there shall be sufficient property in the Trust to save harmless the Trustee with respect to any expenses or losses to which it may be subject through taking such action.

#### 8.3 Joinder of Parties.

Except as otherwise provided by law, in any action or other judicial proceedings affecting the Trust it shall be necessary to join as parties only the Trustee and the companies and no Participants or other persons having an interest in the Trust assets shall be entitled to any notice or service of process.

#### 8.4 Employment of Counsel.

The Trustee may consult with legal counsel (who may be counsel for the Companies) with respect to the construction of this agreement or their duties hereunder, or with respect to any legal proceedings or any question of law, and shall be fully protected with respect to any action taken or omitted by them in good faith pursuant to the advice of such counsel.

#### 8.5 Records.

The Trustee shall keep a full record of the administration of the Trust which the Companies, or their representatives, including independent accountants selected by them, shall have the right to examine at any time during the Trustee's regular business hours. The Companies shall cause an audit to be performed of such records at the close of each fiscal year by independent accountants selected by them. Failure by the Companies to disapprove within sixty (60) days after receipt of the audit report shall be considered an approval. The approval by the Companies of any report of audit shall be binding as to all matters embraced in the report on all parties to this agreement and on all Participants, to the same extent as if the account of the Trustee had been settled by judgment or decree of a court of competent jurisdiction in which the Trustee, the Companies and all persons having or claiming any interest in the Trust were parties; provided, however, that nothing herein contained shall deprive the Trustee of power to have its account judicially settled if so desired. The Companies shall not be liable to any person or Participant for approving, disapproving, or failure to approve any audit report.

#### 8.6 Notices, Directions and Mailing Addresses.

All notices, orders, requests, instructions and directions of the Committee to the Trustee shall be in writing signed by any one of its members and all such communications of the Company to the Trustee shall be in writing signed by an officer of the Company; provided, however, that the Trustee may, in its discretion, accept oral orders, requests and instructions subject to confirmation in writing. The Trustee shall act and shall be fully indemnified and saved harmless by the Company pursuant to Section

8.7 of this Agreement in acting in reliance upon and in accordance with such notices, orders, requests, instructions and directions, and shall have no duty to see to the application of any funds paid in accordance therewith. The Company by any one of its officers will certify to the Trustee the appointment and termination of office of members of the Committee and specimen signatures of members of the Committee and the Trustee shall not be charged with knowledge thereof until it receives such notice. The committee will certify to the Trustee the names and specimen signatures of the Committee's chairman and secretary and any persons authorized to act for it in relation to the Trustee.

The Trustee shall not be required to determine, or make any investigation to determine the identity or mailing address of any person entitled to benefits under the Plan, and shall have discharged its obligation in that respect when they shall have sent checks and other papers by ordinary first class mail to such persons and addresses as may be furnished them by the Committee. The Trustee shall recognize only instructions given them by the Committee and shall have the right to act thereon without notice to any Participant, and without considering the rights of any Participant under the terms of this agreement which may result directly or indirectly from said Participant's interest in the Trust.

#### 8.7 Compensation and Indemnity.

The Trustee shall receive such fees and compensation as agreed upon from time to time by the Sponsor and the Trustee. Any and all expenses and liabilities of whatever nature of the Trustee in its administration of the Trust may be charged to the Trust assets. In the event of a Tender Offer (as defined in Section 12.1) or contested solicitation of proxies or consents as described in Article XII or Section 8.3(n) hereof, the Sponsor shall pay all reasonable expenses of the Trustee applicable to transmitting Sponsor materials with respect to such Tender Offer or any such contested matter. Except to the extent prohibited by law, the Sponsor shall indemnify the Trustee against, and agrees to hold the Trustee harmless from, all liabilities and claims (including reasonable attorney's fees and expenses in defending against such liabilities and claims) against the Trustee which may result from the Trustee acting under the Trust, unless such liability or expense results from negligent, reckless or willful acts of commission or omission by the Trustee, or from any breach of fiduciary responsibility by a fiduciary other than the Trustee unless the Trustee participates knowingly in such breach, has actual knowledge of such breach and fails to take reasonable remedial action to remedy such breach or, through his or her negligence in performing his or her own specific fiduciary responsibilities, has enabled such other fiduciary to commit a breach of the latter's fiduciary responsibilities. The Trustee shall be entitled to collect on the Sponsor's indemnity under this Section only from the Sponsor and shall not be entitled to payment directly or indirectly from Trust assets.

#### 8.8 Duty of Care.

The Trustee shall discharge its fiduciary responsibilities solely in the interest of the Participants and Beneficiaries of the Plan for the exclusive purpose of providing benefits to Participants and their Beneficiaries and defraying reasonable expenses of administering the Plan with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent Trustee acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims and in accordance with the documents and instruments governing this Plan and Trust, but without any duty to diversify the investments of the Plan so long as the Plan acquires and holds Stock as provided by this Plan. The Trustee shall not maintain the indicia of ownership of any Trust assets outside the jurisdiction of the district courts of the United States.

It is the intent of the Trustee under this Plan and Trust that the Trustee shall be solely responsible for its own acts or omissions. Except to the extent imposed by Section 405(a) of ERISA or otherwise by ERISA or the Code, no Fiduciary shall have the duty to question whether any other Fiduciary is fulfilling any or all of the responsibilities imposed upon such other Fiduciary by ERISA or by any Regulations or Rulings issued thereunder. No Fiduciary shall have any liability for a breach of fiduciary responsibility of another Fiduciary with respect to this Plan and Trust unless the Trustee knowingly participates in such breach and fails to take reasonable remedial action to remedy said breach or, through concealment or the Trustee's negligence in performing his or her own specific fiduciary responsibilities, has enabled such other Fiduciary to commit a breach of the latter's fiduciary responsibilities.

#### 8.9 Third Persons.

A third party dealing with the Trustee shall not be required to make any inquiry whether the Companies have instructed the Trustee, or the Trustee is otherwise authorized, to take or omit any action, or to follow the application by the Trustee of any money or property which may be paid or delivered to the Trustee.

#### 8.10 Taxes.

If the whole or any part of the Trust assets, or the proceeds thereof, shall become liable for the payment of any estate, inheritance, income or other tax, charge or assessment which the Trustee shall be required to pay, the Trustee shall have full power and authority to pay such tax, charge or assessment out of any money or other property in its hands for the account of the Participant whose interest hereunder is so liable; provided, however, in no event shall any excise taxes imposed on any party in interest or disqualified person for engaging in a prohibited transaction be paid from the Trust. In connection with such payment, the Trustee may require such releases or other documents from any lawful taxing authority as it shall deem necessary.

#### 8.11 Procedure for Establishing Funding Policy – Transmittal of Information.

The Plan is to be funded through Company contributions and earnings on such contributions; and benefits shall be paid to Participants and Beneficiaries as provided in the Plan. The Trustee shall have no duty to determine that the contributions comply with the provisions of this Plan or that the assets of the Trust are adequate to provide any benefit payable pursuant to the Plan. The Trustee need not inquire into the source of any cash or property transferred to it nor into the authority or right of the transfer or of such cash or property to transfer such assets of the Trustee. The Board of Directors of the Company shall determine investment policies from time to time that are consistent with the objectives of the Plan. To enable the Committee to perform its functions, the Companies shall supply full and timely information to the Committee on all matters relating to Employees and Participants as the Committee may require, and shall maintain such other records as the Committee may determine are necessary in order to determine the benefits due or which may become due to Participants or their Beneficiaries under the Plan.

#### 8.12 Reports.

The Trustee shall submit to the Companies such interim valuations, reports or other information as they may reasonably require. Within one hundred and eighty (180) days following (a) the close of each Fiscal Year or (b) the effective date of the removal or resignation of the Trustee, the Trustee shall file with the Company (1) a written account setting forth transactions effected by it subsequent to the end of the period covered by its last previous annual account, and listing the assets of the Trust, showing carry and market values of such assets, at the close of the period covered by such account; and (2) such information which is within the control of the Trustee as shall be necessary to fully inform the Companies of the discharge by the Trustee or its delegates of responsibilities with respect to this Plan and Trust and under Title I of ERISA.

### ARTICLE IX. RESIGNATION AND REMOVAL OF TRUSTEE

#### 9.1 Procedure.

Any Trustee may resign at any time upon delivering to the Companies a written notice of resignation, to take effect not less than thirty (30) days after the delivery thereof, unless such notice shall be waived.

Any Trustee appointed hereafter may be removed by resolution of the Board of Directors of the Company and by delivery of a certified copy of such resolution to the Trustee, together with written notice of removal, to take effect at a date specified therein, which shall not be less than thirty (30) days after delivery of such notice to the Trustee, unless such notice shall be waived.

In case of the resignation or removal of a Trustee, the Trustee shall have the right to a settlement of the Trustee's account, which may be made, at the option of the Trustee, either (a) by a judicial settlement in an action instituted by the Trustee in a court of competent jurisdiction, or (b) by agreement of settlement between the Trustee, the successor Trustee and the Companies.

Upon such settlement, all right, title and interest of such Trustee in the assets of the Trust and all rights and privileges under this agreement theretofore vested in such Trustee shall automatically and without the execution of any instrument in writing, vest in the successor Trustee and thereupon all future liability of such Trustee shall terminate; provided, however, that the Companies

in their discretion may require the execution of such documents and written instruments as are deemed necessary to cause such vesting in the successor Trustee.

Upon receipt of or giving notice of the resignation or removal of a Trustee, the Board of Directors shall by resolution forthwith appoint a successor Trustee. Any successor Trustee so appointed may qualify as such by executing, acknowledging and delivering to the Board of Directors of the Company an instrument accepting such appointment and upon delivery such successor, without further act, shall become vested with all the right, title, interest, power, discretion and duties of the predecessor Trustee with like effect as if originally named as Trustee herein. In the event that no Trustee remains and no successor Trustee is appointed pursuant to this Section 9.1, the Company shall either terminate this Plan and Trust in accordance with the provisions hereof, or shall cause the Trust assets to be distributed to another trust qualifying under the application provisions of Sections 401 and 501 of the Code.

ARTICLE X.  
AMENDMENT AND TERMINATION

10.1 Amendments.

The Sponsor shall have the right to amend this Trust from time to time by resolution of its Board of Directors and to amend or cancel any amendments. Any amendment shall be stated in an instrument in writing, executed in the same manner as this Plan, and this agreement shall be deemed to have been amended in the manner and at the time therein set forth, and all Companies and Participants shall be bound thereby; provided, however:

- (a) No amendment shall be effective which shall attempt to cause any of the assets of the Trust to be used for or diverted to purposes other than for the exclusive benefit of Participants or their Beneficiaries, except that such changes, if any, as may be required to permit the Plan to meet the requirements of the Code, or of the corresponding provisions of any subsequent revenue law, or of ERISA may be made to assure the deductibility for tax purposes of any contributions;
- (b) No amendment shall have any retroactive effects so as to deprive any Participant or Beneficiary of any benefit already accrued, except that such changes, if any, as may be required to permit the Plan to meet the requirements of the Code, or of the corresponding provisions of any subsequent revenue law, or of ERISA may be made to assure the deductibility for tax purposes of any contributions;
- (c) No amendment shall create or effect any discrimination in favor of Participants who are officers, shareholders, persons whose principal duties consist of supervising the work of other employees, or highly compensated employees; and
- (d) No amendment shall increase the duties or liabilities of the Trustee without their written consent.

10.2 Discontinuance of Plan.

- (a) It is the expectation of the Companies that they will continue this Plan and the payment of contributions hereunder indefinitely, and this Trust is irrevocable, but continuance of the Plan is not assumed as a contractual obligation of the Companies, and the right is reserved by the Companies at any time to reduce, completely suspend, or completely discontinue contributions hereunder. In the event of such complete or partial suspension or complete or partial discontinuance of contributions, any Participant whose participation is terminated during the period of such complete or partial suspension or complete or partial discontinuance shall have a vested interest in the Participant's ESOP account to the extent of one hundred percent (100%)
- (b) The Sponsor may, by resolution of its Board of Directors, terminate this Plan completely or with respect to any Company at any time upon fifteen (15) days written notice to the Trustee. Upon such complete or partial termination of the Plan the entire interest of each affected Participant in the Participant's ESOP account shall vest to the extent of one hundred percent (100%) immediately.

- (c) The Committee, in its discretion, shall direct the Trustee to distribute account balances of all affected Participants in Stock, with cash for fractional shares, or alternatively, to liquidate part or all of the assets remaining in the Trust and, after deducting estimated expenses for liquidation and distribution, to make the allocations required under Article VI, where applicable, with the same effect as though the date of completion of liquidation of the Plan was an Anniversary Date of the Plan. Following appropriate allocations, the Committee shall direct the Trustee to distribute benefits. Such direction shall be in accordance with Section 7.2 and, where appropriate, section 403 (d) (1) of ERISA and regulations of the Secretary of Labor thereunder as may affect allocation of assets upon termination of the Plan. Notwithstanding the foregoing, the provisions of this Section 10.2(c) shall be applicable only with respect to benefits accrued under the Plan as of the date of closing of the Sale.
- (d) The Committee shall direct the Trustee to allocate to the ESOP accounts of Participants all Stock released from the ESOP Suspense Account for the period preceding the date of Plan termination to the extent Company contributions have been applied to repay an Exempt Loan or Loans in accordance with Section 6.5, subject to the limitations of Article VI, as though the date of Plan termination were an Anniversary Date. Such allocated account balance for each Participant shall be transferred to the KPlan in which he participates as provided in Sections 6.6(b) and (c). Next, the Committee shall direct the Trustee to sell that number of shares of Stock held in the ESOP Suspense Account that will generate proceeds sufficient to repay entirely all principal and interest on any outstanding Exempt Loans. The proceeds of such sale shall be used to repay such loans.

#### 10.3 No Discontinuance of Trust for Failure to Contribute.

A failure of the Companies to contribute to the Trust in any year when no contribution is required under Article V shall not operate to discontinue completely this Trust.

#### 10.4 Merger or Consolidation.

Notwithstanding any other provision of this Plan, this Plan shall not be merged or consolidated with, nor shall its assets or liabilities be transferred to, any other plan unless the following condition is satisfied. This condition requires that each Participant receive benefits on a termination basis from the Plan immediately after the merger, consolidation, or transfer which are equal to or greater than the benefits the Participant would receive on a termination basis immediately before the merger, consolidation, or transfer. For this purpose, "benefits on a termination basis" shall not include any portion of the ESOP Suspense Account. Where the foregoing condition is satisfied, this Plan and Trust may be merged or consolidate with another qualified plan and trust. In the event this Plan is merged or consolidated with, or its assets are transferred to, any other plan and the foregoing condition finally is determined not to be satisfied, then the Committee shall take whatever measures are necessary to ensure the continued qualification of the Plan. If the Company merges or consolidates with or into, or transfers all or substantially all of its assets to, a successor, this Plan shall terminate unless the successor adopts this Plan within one hundred eighty (180) days following such merger, consolidation or transfer.

### ARTICLE XI. MISCELLANEOUS

#### 11.1 Contributions Not Recoverable.

Except where contributions are required to be returned to the Company by the provisions of this Plan as permitted or required by ERISA or the Code, it shall be impossible for any part of the principal or income to be used for, or diverted to, purposes other than the exclusive benefit of the Participants or their Beneficiaries. Notwithstanding the foregoing or any other provision of this Plan or Trust, contributions may be returned to the Company within one year after such contribution is made where such contributions are made by a mistake of fact, or, to the extent a deduction is disallowed under Section 404 of the Code, contributions may be returned to the Company within one year following such disallowance where the contribution is conditioned upon the deductibility of such

contribution, or as permitted or required by ERISA or the Code, where such return is necessary to avoid the limitation of benefits imposed by Section 415 of the Code.

#### 11.2 Limitation on Participants' Rights.

Participation in this Trust shall not give any Employee the right to be retained in a Company's employ, or any right or interest in this Trust other than as herein provided. The Companies reserve the right to dismiss any Employee without any liability for any claim either against the Trust, except to the extent provided for herein, or against the Companies. All benefits payable hereunder shall be provided solely from the Trust except as required by ERISA, and the Companies assume no responsibility for the acts of the Trustee. A Participant shall have no recourse towards satisfaction of benefits under this Plan or Trust other than from the Trust assets.

#### 11.3 Receipt and Release.

Any payment to any Participant or the Participant's legal representative or Beneficiary, in accordance with the provisions of this agreement, shall, to the extent thereof, be in full satisfaction of all claims against the Trustee and the Companies, any of whom may require such Participant, legal representative or Beneficiary, as a condition precedent to such payment, to execute a receipt and release therefor in such form as shall be determined by the Trustee or the Companies, as the case may be.

#### 11.4 Non-Assignability.

None of the benefits, payments, proceeds or claims of any Participant or Beneficiary shall be subject to any claim of any creditors and, in particular, the same shall not be subject to attachment or garnishment or other legal process by any legal creditor of any Participant, nor shall any such Participant have any right to alienate, anticipate, commute, pledge, encumber or assign any of the benefits or payments or proceeds which such Participant may expect to receive, contingently or otherwise, under this agreement. Notwithstanding the foregoing, the right to a benefit payable with respect to a Participant pursuant to a "qualified domestic relations order" (within the meaning of Code Section 414(p)) may be created, assigned or recognized. The Committee shall establish reasonable procedures to determine the qualified status of domestic relations orders and to administer distributions under such qualified orders. In the event a qualified domestic relations order exists with respect to a benefit payable under the Plan, the benefits otherwise payable to a Participant or Beneficiary shall be payable to the alternate payee specified in the qualified domestic relations order. Notwithstanding the foregoing or any other provision of the Plan to the contrary, upon receipt by the Committee of a judgment, order, decree or settlement agreement which expressly provides for an offset against all or part of an amount ordered or required to be paid to the Plan against a Participant's ESOP account under the Plan, such Participant's ESOP account shall be reduced or offset by the amount specified in such judgment, order, decree or settlement agreement and such amount shall promptly be paid to the Plan; provided, however, such judgment, order, decree or settlement agreement must arise from:

- (a) a judgment of conviction for a crime involving the Plan,
- (b) a civil judgment (including a consent order or decree) entered by a court in an action brought in connection with a violation (or alleged violation) of Part 4 of ERISA, or
- (c) a settlement agreement between the Secretary of Labor or the Pension Benefit Guaranty Corporation and the Participant in connection with a violation (or alleged violation) of Part 4 of ERISA by a fiduciary or any other person.

A Participant's ESOP account may also be subject to and used to satisfy (1) a lien as the result of a loan under a KPlan; (2) the enforcement of a federal tax levy made pursuant to Code Section 6331; or (3) the collection by the United States on a judgment resulting from an unpaid tax assessment.

#### 11.5 Governing Law.

This Plan and Trust shall be construed, administered, and governed in all respects under applicable federal law, and to the extent that federal law is inapplicable, under the laws of the State of California; provided, however, that if any provision is susceptible to more than one interpretation, such interpretation shall be given thereto as is consistent with this Plan being an employees' plan within the meaning of Section 401 of the Code. If any provisions of this instrument shall be held by a court of competent jurisdiction to be invalid or unenforceable, the remaining provisions hereof shall continue to be fully effective.

#### 11.6 Headings No Part of Agreement.

Headings and subheadings in this agreement are inserted for convenience of reference only and are not to be considered in construction of the provisions hereof.

#### 11.7 Instrument in Counterparts.

This agreement has been executed in several counterparts, each of which shall be deemed an original, and said counterparts shall constitute but one and the same instrument, which may be sufficiently evidenced by any one counterpart.

#### 11.8 Successors and Assigns.

This agreement shall inure to the benefit of, and be binding upon, the parties hereto and their successors and assigns.

#### 11.9 Masculine Gender includes Feminine and Neuter.

As used herein, the masculine gender shall include the feminine and neuter genders.

#### 11.10 Dividends.

Cash dividends on shares of Stock allocated to Participants' accounts may be paid currently to Participants, as determined by the Sponsor, in its sole discretion. Such dividends shall be paid in cash directly by the Sponsor, or, if so directed by the Committee, may be distributed by the Trustee after receipt from the Sponsor within 90 days after the end of the Plan Year of receipt by the Trustee. Cash dividends on shares of Stock allocated to Participants' accounts may, as determined by the Sponsor in its sole discretion, be used in whole or in part, consistent with Section 404(k) of the Code to make payments on an Exempt Loan. The Sponsor may determine that such dividends may be applied for any Plan Year up to the time when such dividends are finally allocated to accounts of Participants as of any Anniversary Date. Such dividends may not be used for payment of an Exempt Loan unless shares of Stock released for the benefit of Participants who would have otherwise been credited with the value of such dividends have a fair market value not less than the amount of such dividends which would have been allocated for the benefit of the Participant for the Plan Year as to which such dividends would have otherwise been allocated for such Participant's benefit. Under Section 6.6, the value of Stock released pursuant to this Section 11.10 shall be allocated to Participants in the same proportion that the value of dividends used for payment of the Exempt Loan would have been allocated for the benefit of such Participants.

If, applying the general rules of Section 6.6, use of cash dividends on shares of Stock allocated to Participant's accounts for payment of an Exempt Loan would not release Stock having a fair market value at least equal to the value of dividends so used, the following shall apply:

- (a) From the total of Stock released from the ESOP suspense account by virtue of payment from all dividends of an Exempt Loan, there shall first be allocated to the accounts of Participants from which dividends were used to pay the Exempt Loan, an amount of Stock equal in fair market value to such dividends utilized; and
- (b) The remainder of Stock released through use of such dividends shall be allocated as provided under Section 6.6 in the same manner as Stock released through employer contributions used to pay the Exempt Loan.

#### 11.11 Correction of Administrative Error; Special Contribution

Notwithstanding any other provision of the Plan to the contrary, the Committee shall take any and all appropriate actions to correct errors in the administration of the Plan, including, without limitation, errors in the allocation of contributions, forfeitures, and income, expenses, gains and losses to the ESOP accounts of the Participants or Beneficiaries under the Plan. Such corrective actions may include debiting or crediting a Participant's or Beneficiary's Accounts or allocating special contributions made by the Company to the Plan for purposes of correcting any failure to make contributions on a timely basis or properly allocate contributions, forfeitures, or income, expenses, gains and losses. The Committee shall determine the amount of any such special contributions required to be made by the Company, which may be made in such approximate amounts as the Committee, acting in its sole discretion, shall determine. In no event shall any corrective action taken by the Committee under this Section reduce any Participant's or Beneficiary's accrued benefit in violation of Section 411(d)(6) of the Code and the Treasury regulations thereunder.

## 11.12 Uniformed Services Employment and Reemployment Rights Act of 1994

Notwithstanding any provisions of this Plan to the contrary, contributions, benefits and service credit with respect to qualified military service will be provided in accordance with Section 414(u) of the Code.

### ARTICLE XII. TENDER OFFERS

#### 12.1 Application.

In the event of any transaction which is evidenced by the filing of a Statement on Schedule 14D-1 with the Securities and Exchange Commission or in the event of any other similar transaction (a "Tender Offer"), then, notwithstanding any provision of the Plan and Trust agreement to the contrary, the following provisions of this Article XII shall apply.

#### 12.2 Special Provisions.

In the event of a Tender Offer, the trustee for each KPlan shall seek confidential written instructions from each Participant as to whether the Stock allocated to the Participant's KPlan account should be tendered. At or prior to the time the KPlan trustee seeks such instructions, such trustee shall distribute to each such Participant copies of the material received by the trustee or filed with the Securities and Exchange Commission in connection with such offer. Sponsor materials shall be distributed at Sponsor expense. Any materials prepared by the parties other than the Sponsor shall be distributed by the Trustee only if such parties agree to pay reasonable expenses in connection therewith. The Trustee shall have the power to demand that payment for such distributions of materials be made in advance.

If a Participant does not submit instructions to the KPlan trustee, the Participant shall be deemed to have given the trustee instruction not to tender shares credited to such Participant's account. Any unallocated Stock in this Plan shall be tendered or not tendered by the Trustee in the same proportion as stock allocated to Participants' KPlan accounts from this Plan is tendered or not tendered, unless the Tender Offer is an issuer tender offer by the Company, in which case any unallocated Stock in this Plan shall not be tendered by the Trustee.

In the event that the above method for determining whether or not to tender Company Stock is challenged by judicial action, and in the event such method is deemed invalid, then the Committee shall assume full fiduciary responsibility for determining whether or not to tender Company Stock.

In exercising such fiduciary discretion, the Committee may consult with, or retain, outside experts to evaluate the tender offer, and to evaluate the prospects for the company in the event the tender offer is successful or unsuccessful. The Committee may also consider the preference of Participants as evidenced by their decision to tender or not tender the shares allocated to them in the KPlans.

The Trustee shall take all steps necessary, including appointment of a corporate trustee and/or an outside independent administrator to the extent such action, after consultation with the Sponsor, is found necessary to maintain confidentiality of Participant responses and/or to adequately discharge its obligations as Fiduciary under this Plan and Trust agreement.

### ARTICLE XIII. TOP-HEAVY PROVISIONS

#### 13.1 General.

This Article shall be interpreted in accordance with Section 416 of the Code and the regulations thereunder. Regardless of how the terms defined in this Article are otherwise defined in the Plan, the definitions in this Article shall govern for the purposes of this Article.

#### 13.2 Definitions.

- (a) The "Benefit Amount" for any Employee means (1) in the case of any defined benefit plan, the present value (the present value shall be computed using a 5% interest assumption and the mortality assumptions contained in the Plan for benefit

equivalence purposes) of the Participant's normal retirement benefit, determined on the Valuation Date as if the Employee terminated on such Valuation Date, plus the aggregate amount of distributions made to such Employee within the five-year period ending on the Determination Date (except to the extent already included on the Valuation Date) and (2) in the case of any defined contribution plan, the sum of the amount credited, on the Determination Date, to each of the accounts maintained on behalf of such employee under such plan plus the aggregate amount of distributions made to such Employee within the five-year period ending on the Determination Date.

- (b) "Company" means any company (including unincorporated organizations) participating in the Plan or plans included in the "aggregation group" as defined in this Article.
- (c) "Determination Date" means the last day of the preceding Plan Year or, in the case of the first Plan Year of the Plan, the last day of the Plan Year.
- (d) "Employees" means employees, former employees, beneficiaries, and former beneficiaries who have a Benefit Amount greater than zero on the Determination Date.
- (e) "Key Employee" means any Employee who, during the Plan Year containing the Determination Date or during the four preceding Plan Years, is:

- (1) one of the ten Employees of a company having annual compensation from such Company of more than the limitation in effect under Section 415(c)(1)(A) of the Code and owning (or considered as owing within the meaning of Section 318 of the Code) both a more than 1/2% interest and the largest interest in such Company (if two Employees have the same interest the Employee having the greater annual compensation from the Company shall be treated as having a larger interest);

- (2) a 5% owner of a Company;

- (3) a 1% owner of a Company who has an annual compensation above \$150,000; or

- (4) an officer of a company having an annual compensation greater than 50% of the amount in effect under Section 415(b) (1) (A) of the Code for any such Plan Year (however, no more than the lesser of (i) 50 employees or (ii) the greater of 3 employees or 10% of the Company's employees shall be treated as officers). For purposes of determining the number of employees taken into account under this Section 1.2(e)(4), employees described in Section 414(g)(8) of the Code shall be excluded.

This definition shall be interpreted in accordance with Section 416(i) of the Code and the regulations thereunder and such rules are hereby incorporated by reference. The term "Key Employee" shall not include any officer or employee of an entity referred to in Section 414(d) of the Code. For the purpose of this subsection, "compensation" shall mean compensation as defined in Section 414(q)(4) of the Code and shall be determined without regard to Sections 125, 402(e)(3), 402(h)(1)(B) or, in the case of employer contributions made pursuant to a salary reduction agreement, Section 403(b)(f) A "Non-Key Employee" means an Employee who is not a Key Employee.

- (f) "Valuation Date" means the first day (or such other date which is used for computing plan costs for minimum funding purposes) of the 12-month period ending on the Determination Date.
- (g) A "Year of Service" shall be calculated using the Plan rules that normally apply for determining vesting service.

### 13.3 Top-Heavy Definition.

This Plan shall be top-heavy for any Plan Year if, as of the Determination Date, the sum of the Benefit Amounts of all employees who are Key Employees exceeds 60% of the sum of the Benefit Amounts for all Employees. For purposes of this

calculation only, the following rules shall apply:

- (a) The Benefit Amounts of all employees who are not Key Employees and who were Key Employees during any prior Plan Year shall be disregarded.
- (b) The Benefit Amounts of all employees who have not received any compensation from any Company (other than benefits under this Plan) at any time during the five-year period ending on the Determination Date shall be disregarded.
- (c) This calculation shall be made by aggregating any plans qualified under Section 401(a) of the Code in which a Key Employee participates or which enables this Plan to meet the requirements of Section 401(a)(4) or 410 of the Code; all plans so aggregated constitute the “aggregation group. The Company may also aggregate any such plan to the extent that such plan, when aggregated with this aggregation group, continues to meet the requirements of Section 401(a) (4) and Section 410 of the Code.
- (d) This calculation shall be made in accordance with Section 416 of the Code and the regulations thereunder and such rules are hereby incorporated by reference.

#### 13.4 Vesting.

Participants’ ESOP accounts are at all times fully vested.

#### 13.5 Minimum Benefits or Contributions, Compensation Limitations, Section 415 Limitations. and Special Distribution Rules.

If the Plan is top-heavy for any Plan Year, the following provisions shall apply to such Plan Year:

- (a) (1) Except to the extent not required by Section 416 of the Code or any other provision of law, notwithstanding any other provision of this Plan, if this Plan and all other plans which are part of the aggregation group are defined contribution plans, each Participant (and Any other employee required by Section 416 of the Code) other than Key Employees shall receive an allocation of employer contributions and forfeitures from a plan which is part of the aggregation group at least equal to 3% (or, if lesser, the largest percentage allocated to any Key Employee for the Plan Year) of such Participant’s compensation (within the meaning of Section 415(c) of the Code) for such Plan Year (the “defined contribution minimum”)
- (2) Except to the extent not required by Section 416 of the Code or any other provision of law, notwithstanding any other provisions of this Plan, if this Plan or any other plan which is part of the aggregation group is a defined benefit plan each Participant who is a participant in any such defined benefit plan (who is not a Key Employee) who accrues a full Year of Service during such Plan Year (and any other employee so required by Section 416 of the Code) shall be entitled to an annual normal retirement benefit from a defined benefit plan which is part of the aggregation group which shall not be less than the product of (1) the employee’s average compensation for the five consecutive years when the employee had the highest aggregate compensation and (2) the lesser of 2% per Year of Service or 20% (the “defined benefit minimum”) For purposes of calculating the defined benefit minimum, (1) compensation shall be defined as it is under Section 415(c) of the Code and shall not include compensation in Plan Years after the last Plan Year in which the Plan is top-heavy and (2) a Participant shall not receive a Year of Service in any Plan Year before January 1, 1984 or in any Plan Year in which the Plan is not top-heavy. This defined benefit minimum shall be expressed as a life annuity (with no ancillary benefits) commencing at normal retirement age. Benefits paid in any other form or time shall be the actuarial equivalent (as provided in the Plan for retirement benefit equivalence purposes) of such life annuity. Except to the extent not required by Section 416 of the Code or any other provisions of law, each Participant (other than Key Employees) who is not a participant in any such defined benefit plan shall receive the defined contribution minimum (as defined in paragraph (a)(1) above).

(b)

The maximum amount of a Participant's compensation which shall be taken into account under the Plan for such Plan Year shall be \$200,000. Such amount shall be adjusted in accordance with Section 416(d) (2) of the Code.

- (c) The distribution of the benefit of a Participant who is a 5% owner of a Company must begin no later than the year in which the Participant attains age 70½, subject to any exceptions contained in Section 401(a) (9) of the Code.

ARTICLE XIV.  
RIGHTS AND OPTIONS ON STOCK

14.1 Participant Protections and Rights.

This Article XIV is intended to meet the requirements of Regulation § 54.4975-11(a) (3) or any successor regulation. The protections and rights provided by this Article XIV are nonterminable.

14.2 General Restriction on Options.

Except as provided elsewhere in this Article XIV, no Stock acquired with the proceeds of an Exempt Loan may be subject to a put, call, or other option, or buy-sell or similar arrangement while held by and when distributed from this Plan, whether or not this Plan is then an employee stock ownership plan as described in Section 4975(e)(7).

14.3 Put Options on Stock Not Publicly Traded.

If, at the time of distribution, Stock distributed from the Plan is not readily tradable on an established market within the meaning of Section 409(h) of the Code and Regulations thereunder, such Stock shall be subject to a put option in the hands of a Qualified Holder by which such Qualified Holder may sell all or any part of the Stock distributed to the Trustee. Should the Trustee decline to purchase all or any part of the Stock put to it by the Qualified Holder, the Sponsor shall purchase the Stock that the Trustee declines to purchase. The put option shall be subject to the following conditions:

- (a) The term "Qualified Holder" shall mean the Participant or Beneficiary receiving the distribution of Stock, any other party to which the Stock is transferred by gift or by reason of death, and also any trustee of an individual retirement account (as defined under Code Section 408) to which all or any portion of the distributed Stock is transferred pursuant to a tax-free "rollover" transaction satisfying the requirements of Sections 402 and 408 of the Code.
- (b) During the 60-day period following any distribution of such Stock, a Qualified Holder shall have the right to require the Sponsor to purchase all or a portion of the distributed Stock held by the Qualified Holder. The purchase price to be paid for any such Stock shall be their fair market value determined (1) as of the Valuation Date coinciding with or next preceding the exercise of the put option under this Section 14.3 or, (2) in the case of a transaction between the Plan and a "disqualified person" within the meaning of Section 4975(e) (2) of the Code or a "party in interest" within the meaning of Section 3(14) of ERISA, as of the date of the transaction.
- (c) If a Qualified Holder shall fail to exercise the put option right under Section 14.3(b), the option right shall temporarily lapse upon the expiration of the 60-day period. As soon as practicable following the last day of the Plan Year in which the 60-day option period expires, the Sponsor shall notify the non-electing Qualified Holder (if the Qualified Holder is then a shareholder of record) of the valuation of the Stock as of that date. During the 60-day period following receipt of such valuation notice, the Qualified Holder shall again have the right to require the Sponsor to purchase all or any portion of the distributed Stock. The purchase price to be paid therefor shall be fair market value determined (1) as of the Valuation Date coinciding with or next preceding the exercise of the put option under this Section 14.3(c) or, (2) in the case of a transaction between the Plan and a "disqualified person" within the meaning of Section 4975(e) (2) of the Code or a "party in interest" within the meaning of section 3(14) of ERISA, as of the date of the transaction.

- (d) The foregoing put options under Section 14.3(b) and (c) hereof shall be effective solely against the Sponsor and shall not obligate the Plan or Trust in any manner.
- (e) In making the determination of fair market value, the Sponsor shall consider, to the extent permitted by law, the same methodology used to value the Stock at the time of its initial purchase by the Trustee and shall, to the extent permitted by law, include as a valuation factor at least the same proportionate share of enterprise value as was taken into account at the time of such purchase of stock.
- (f) The period during which the put option exercisable does not include any time when a Qualified Holder is unable to exercise it because the Sponsor is prohibited from honoring it by applicable Federal or State laws.
- (g) Except as otherwise required or permitted by the Code, the put options under this Section 14.3 shall satisfy the requirements of Section 54.4975-7(b) of the Treasury Regulations to the extent, if any, that such requirements apply to such put options.
- (h) A Qualified Holder must exercise the put option in writing by filing with the Trustee. If a Qualified Holder exercises the put option under this Section 14.3, payment for the Stock repurchased shall be made, in the case of a distribution of a Participant's Account within one taxable year, insubstantially equal annual payments over a period beginning not later than 30 days after the exercise of the put option and not exceeding five years (provided that adequate security and reasonable interest are provided with respect to unpaid amounts) or, in the case of other distributions, not later than 30 days after such exercise.

ARTICLE XV.  
ADMINISTRATIVE COMMITTEE

15.1 Appointment of Committee Members.

The Board of Directors shall appoint an Administrative Committee consisting of at least three members which shall have responsibility for the administration of the Plan to hold office at the pleasure of the Board. No member of the Committee shall be paid any compensation for his services from the Plan. The members of the committee shall be deemed to be fiduciaries of the Plan for purposes of compliance with the fiduciary responsibility provisions of ERISA.

15.2 Action of the Committee.

The Committee shall hold meetings upon such notice, and at such place or places, and at such intervals as it may from time to time determine.

A majority of the members of the Committee at any time in office shall constitute a quorum for the transaction of business, except where the Committee consists of an even number of members, 50% of the members shall constitute a quorum. All resolutions or other actions taken by the Committee shall be by vote of a majority of those present at a meeting of the Committee, or without a meeting by instrument in writing signed by a majority of the members of the Committee.

15.3 Powers and Duties of the Committee.

In addition to any implied powers and duties which may be needed to carry out the provisions of this resolution, the Committee shall have the following specific powers and duties and full discretion in its exercise thereof:

- (a) To make and enforce such rules and regulations as it shall deem necessary or proper for the efficient administration of the Plan;
- (b) To interpret the Plan and to decide any and all matters arising thereunder; including the right to remedy possible ambiguities, inconsistencies or omissions, provided, however, that all such interpretations and decisions shall be applied in a uniform manner to all employees similarly situated;
- (c)

To compute the amount of Plan benefits which shall be payable to any Participant or Beneficiary in accordance with the provisions of the Plan;

- (d) To authorize disbursements from the Trust (any instructions of the Committee to the Trustee shall be evidenced in writing and signed by a member of the Committee delegated with such authority by a majority of the Committee);
- (e) To employ, appoint, or engage such advisors (including but not limited to attorneys and enrolled actuaries) and such other technical and clerical personnel as may be required in the Committee's discretion for the proper administration of the Plan, except that the Committee shall not appoint or discharge trustees or investment managers; and
- (f) To adopt such amendments to the Plan and the Trust Agreement which in the judgment of the Committee, clarifies the Plan or the Trust Agreement, or are necessary or appropriate to comply with federal or state laws or regulations or to obtain the Internal Revenue Services' determination of qualified status, as long as such changes do not materially change the benefits under the Plan.

The Committee will be entitled to rely conclusively upon all tables, valuations, certificates, opinions and reports which will be furnished by any actuary, accountant, controller, counsel or other person who is employed or engaged for such purposes.

#### 15.4 Allocation of Fiduciary Responsibility.

The Committee may, in writing, allocate fiduciary responsibilities to persons who have been designated to carry out such fiduciary responsibilities.

#### 15.5 Plan Expenses.

The reasonable expenses incident to the operation of the Plan, including the compensation of personnel employed in the administration of the Plan, shall be paid by the Sponsor directly, but the Sponsor in its discretion may elect at any time to direct the Trustee to pay part or all out of the Trust, and any such election shall not bind the Sponsor as to its right to elect, with respect to the same or other expenses at any other time, to have such compensation paid directly by the Sponsor or to direct the Trustee to pay such compensation from the Trust.

#### 15.6 Claims Procedure.

##### (a) Filing a Claim for Benefits.

If an individual (hereinafter referred to as the "Applicant," which reference shall include where appropriate the authorized representative, if any, of the individual) does not receive the timely payment of the benefits which he believes he is entitled to receive under the Plan, he may make a claim for benefits in the manner hereinafter provided.

All claims for benefits under the Plan shall be made in writing and shall be signed by the Applicant. Claims shall be submitted to a representative designated by the Committee and hereinafter referred to as the "Claims Coordinator." The Claims Coordinator may, but need not, be an Employee or a member of the Committee. If the Applicant does not furnish sufficient information with the claim for the Claims Coordinator to determine the validity of the claim, the Claims Coordinator shall indicate to the Applicant any additional information which is necessary for the Claims Coordinator to determine the validity of the claim.

Each claim hereunder shall be acted on and approved or disapproved by the Claims Coordinator within 90 days following the receipt by the Claims Coordinator of the information necessary to process the claim. Should special circumstances prevent processing the claim within 90 days, the Claims Coordinator will have up to an additional period of 90 days to decide the claim, provided the Applicant is notified in writing during the initial 90-day period of the special circumstances requiring an extension and the projected date by which a decision will be made.

In the event that the Claims Coordinator denies a claim for benefits in whole or in part, the Claims Coordinator shall notify the Applicant in writing of the denial of the claim and notify the Applicant of his right to a review of the Claims Coordinator's

decision by the Committee. Such notice by the Claims Coordinator shall also set forth, in a manner calculated to be understood by the Applicant, the specific reason for such denial, the specific Plan provisions on which the denial is based, a description of any additional material or information necessary to perfect the claim with an explanation of why such material or information is necessary, and inform the Applicant of the steps that must be taken to submit the claim for further review including the time limits applicable to such procedures, and a statement of the Applicant's right to bring a civil action under Section 502(a) of ERISA following an adverse decision upon review.

(b) Appeals Procedure.

Any Applicant whose claim for benefits is denied in whole or in part (such Applicant being hereinafter referred to as the "Claimant") may appeal from such denial to the Committee for a review of the decision by the entire Committee. Such appeal must be made within three months after the denial provided above. An appeal must be submitted in writing within such period and must:

- (1) Request a review by the entire Committee of the claim for benefits under the Plan;
- (2) Set forth all of the grounds upon which the Claimant's request for review is based and any facts in support thereof; and
- (3) Set forth any issues or comments which the Claimant deems pertinent to the appeal.

The Committee shall regularly review appeals by Claimants. The Committee shall act upon each appeal within 60 days after receipt thereof unless special circumstances require an extension of the time for processing. If special circumstances require, the Committee shall be allowed an extension of up to 60 days once the Claimant has been notified of such extension in writing, prior to expiration of the initial 60 day review period. Such notice of extension shall indicate the special circumstances requiring the extension of time and the date by which the Administrator expects to render the determination on review. The decision on review will be in writing and will be delivered to the Claimant as soon as possible, but not later than 5 days after the claim determination is made.

The Committee shall make a full and fair review of each appeal and any written materials submitted by the Claimant and/or the Participating Company in connection therewith regardless of whether such information was submitted or considered in the initial benefit claim determination. The Committee may require the Claimant and/or the Participating Company to submit such additional facts, documents or other evidence as the Committee in its discretion deems necessary or advisable in making its review. The Claimant, or his duly authorized representative may request upon written application to the Committee; to review and/or copy free of charge, pertinent Plan documents, records, and other information relevant to the Claimant's claim, submit issues and submit documents, records and other information relating to the claim. The decision on review shall be made by the Committee, who may, in its discretion, hold a hearing on the denied claim. The review shall take into account all comments, documents, records and other information submitted by the Claimant relating to the claim, without regard to whether such information was submitted or considered in the initial benefit claim determination.

On the basis of its review, the Committee shall make an independent determination of the Claimant's eligibility for benefits under the Plan. The decision of the Committee on any claim for benefits shall be final and conclusive upon all parties thereto.

In the event that the Committee denies an appeal in whole or in part, the Committee shall give written notice of the decision to the Claimant, which notice shall set forth in a manner calculated to be understood by the Claimant the specific reasons for such denial and which shall make specific reference to the pertinent Plan provisions on which the Committee's decision was based and a statement that the Claimant is entitled to receive upon request and free of charge reasonable access to and copies of all documents, records and other information relevant to the Claimant's claim for benefits, as well as a statement of the Claimant's right to bring an action under Section 502(a) of ERISA. If the decision on review is not furnished within such period, the claim shall be deemed denied on review.

(c) Review of Annual Statement.

If a Participant or Beneficiary believes a statement he receives regarding his interest in the Plan is incorrect, such Participant or Beneficiary may submit a written request for correction or verification of such Annual Statement to the Claims Coordinator, and the Claims Coordinator shall respond in writing to such request in the same manner as a claim for benefits by an Applicant. If the Participant or Beneficiary believes the Claims Coordinator's response is incorrect, the Participant or Beneficiary may request in writing within 30 days of the response that the entire Committee review such statement, and the Committee shall follow the same procedure with respect to such request as provided above for a Claimant.

15.7 Disqualification of Committee Member.

No member of the Committee may act, vote or otherwise influence a decision of the Committee specifically relating to his own participation under the Plan other than a decision affecting employees generally.

15.8 Indemnification of Committee.

The Company hereby agrees to indemnify and hold harmless any member of the Committee and any other Employee with duties under the Plan from and against any and all liabilities, expenses, penalties, costs, damages or losses (including, without limitation, reasonable attorneys' fees and court costs) incurred by such Committee member or Employee arising out of or in connection with any actual or alleged act or omission of such person in connection with the operation or administration of the Plan or the Trust; provided, however, (a) the Company shall not indemnify or hold harmless any such Committee member or Employee from or against any such liability, expense, penalty, cost, damage or loss (i) that is covered by fiduciary liability insurance or (ii) that arises out of or in connection with the willful misconduct of such Committee member or Employee, and (b) in no event shall the Company's duty to indemnify any such Committee member or Employee be satisfied out of Plan assets. The preceding right of indemnification shall pass to the estate of such person and shall be in addition to any other right to which the Committee member or Employee may be entitled as a matter of law or otherwise.

IN WITNESS WHEREOF, Sempra Energy has caused this instrument to be executed in its name by an authorized officer on this \_\_\_\_ day of February, 2002.

SEMPRA ENERGY

By:

U.S. TRUST COMPANY,  
National Association

By:

APPENDIX A  
ANNUAL ADDITION LIMITS

Section 6.7 of the Plan shall be construed in accordance with this Appendix A. Unless the context clearly requires otherwise, words and phrases used in this Appendix A shall have the same meanings that are assigned to them under the Plan.

1.1 Definitions.

As used in this Appendix A, the following terms shall have the meanings specified below. “Annual Additions” shall mean the sum credited to a Participant’s Accounts for any Plan Year of (1) Company contributions, (2) forfeitures, (3) amounts credited after March 31, 1984 to an individual medical account, as defined in Code Section 415(1)(2) which is part of a Defined Benefit Plan maintained by the Company, and (4) amounts derived from contributions paid or accrued after December 31, 1985, in taxable years ending after such date, which are attributable to post-retirement medical benefits allocated to the separate account required with respect to a key employee (as defined in Section 13.2 of the Plan) under a welfare benefit plan (as defined in Code Section 419(e)) maintained by the Company.

“Defined Benefit Plan” means a plan described in Section 414(j) of the code. “Defined Contribution Plan” means a plan described in Section 414(i) of the Code.

“Section 415 Compensation” shall mean a Participant’s earned income, wages, salaries, and fees for professional services, and other amounts received for personal services actually rendered in the course of employment with a Company maintaining a plan (including, but not limited to, commissions paid salesmen, compensation for services on the basis of a percentage of profits, commissions on insurance premiums, tips and bonuses), and excluding the following:

- (a) Company contributions to a plan of deferred compensation which are not included in the Employee’s gross income for the taxable year in which contributed or employer contributions under a simplified employee pension plan to the extent such contributions are deductible by the Employee, or any distributions from a plan of deferred compensation;
  - (b) Amounts realized from the exercise of a non-qualified stock option, or when restricted stock (or property) held by the Employee either becomes freely transferable or is no longer subject to a substantial risk of forfeiture;
  - (c) Amounts realized from the sale, exchange or other disposition of stock acquired under a qualified stock option;
- and
- (d) Other amounts which received special tax benefits, or contributions made by the employer (whether or not under a salary reduction agreement) towards the purchase of an annuity described in Section 403(b) of the Code (whether or not the amounts are actually excludable from the gross income of the Employee). Compensation for any limitation year is the compensation actually paid or includable in gross income during such year.

1.2 Annual Addition Limitations.

(a) The compensation limitation of Section 4.1 of the Plan shall not apply to any contribution for medical benefits (within the meaning of Section 419A(f) (2)) after separation from service which is treated as an Annual Addition. In the event Annual Additions to all the accounts of a Participant would exceed the limitations of Section 4.1 of the Plan, they shall be reduced by reduction of Company contributions.

(b) If the Company or any Related Company contributes amounts, on behalf of Participants covered by the Plan, to other Defined Contribution Plans, the limitation on Annual Additions provided in Article IV of the Plan shall be applied to Annual Additions in the aggregate to the Plan and such other plans. Reduction of Annual Additions, where required, shall be accomplished by first refunding any voluntary contributions to Participants, then by reducing contributions under such other plans pursuant to the

directions of the Committee for administration of such other plans or under priorities, if any, established by the terms of such other plans, and then, if necessary, by reducing contributions under the Plan.

(c) In the event the limitations of Section 4.1 of the Plan or subsections (a) or (b) of this Appendix A are exceeded and the conditions specified in Treasury Regulations Section 1.415-6(b)(6) are met, the Committee may elect to apply the procedures set forth in Treasury Regulations Section 1.415-6(b)(6).

**EXHIBIT 12.1**  
**SEMPRA ENERGY**  
**COMPUTATION OF RATIO OF EARNINGS TO COMBINED FIXED CHARGES**  
**AND PREFERRED STOCK DIVIDENDS**  
**(Dollars in millions)**

	2003	2004	2005	2006	2007	September 30, 2008
Fixed charges and preferred stock dividends:						
Interest	\$ 345	\$ 332	\$ 342	\$ 413	\$ 379	\$ 241
Interest portion of annual rentals	4	4	5	6	6	2
Preferred dividends of subsidiaries (1)	11	12	10	15	14	11
Total fixed charges	360	348	357	434	399	254
Preferred dividends for purpose of ratio	-	-	-	-	-	-
Total fixed charges and preferred dividends for purpose of ratio	<u>\$ 360</u>	<u>\$ 348</u>	<u>\$ 357</u>	<u>\$ 434</u>	<u>\$ 399</u>	<u>\$ 254</u>
Earnings:						
Pretax income from continuing operations	\$ 814	\$ 1,105	\$ 947	\$ 1,732	\$ 1,649	\$ 1,217
Add:						
Total fixed charges (from above)	360	348	357	434	399	254
Distributed income of equity investees	72	59	73	431	19	85
Less:						
Interest capitalized	26	8	28	58	100	75
Equity in income (loss) of unconsolidated subsidiaries and joint ventures	5	36	66	156	90	228
Minority interest in income of consolidated subsidiaries	-	-	-	7	31	4
Total earnings for purpose of ratio	<u>\$ 1,215</u>	<u>\$ 1,468</u>	<u>\$ 1,283</u>	<u>\$ 2,376</u>	<u>\$ 1,846</u>	<u>\$ 1,249</u>
Ratio of earnings to combined fixed charges and preferred stock dividends	<u>3.38</u>	<u>4.22</u>	<u>3.59</u>	<u>5.47</u>	<u>4.63</u>	<u>4.92</u>
Ratio of earnings to fixed charges	<u>3.38</u>	<u>4.22</u>	<u>3.59</u>	<u>5.47</u>	<u>4.63</u>	<u>4.92</u>

(1) In computing this ratio, "Preferred dividends of subsidiaries" represents the before-tax earnings necessary to pay such dividends, computed at the effective tax rates for the applicable periods.

## CERTIFICATION

I, Donald E. Felsing, certify that:

1. I have reviewed this report on Form 10-Q of Sempra Energy;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements and other financial information included in this report fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report, based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 10, 2008

/s/ Donald E. Felsing

Donald E. Felsing

Chief Executive Officer

## CERTIFICATION

I, Mark A. Snell, certify that:

1. I have reviewed this report on Form 10-Q of Sempra Energy;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements and other financial information included in this report fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report, based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 10, 2008

\_\_\_\_\_  
/s/ Mark A. Snell  
Mark A. Snell  
Chief Financial Officer

Statement of Chief Executive Officer

Pursuant to 18 U.S.C. Sec 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned Chief Executive Officer of Sempra Energy (the "Company") certifies that:

- (i) the Quarterly Report on Form 10-Q of the Company filed with the Securities and Exchange Commission for the quarter ended September 30, 2008 (the "Quarterly Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 10, 2008

\_\_\_\_\_  
/s/ Donald E. Felsing  
Donald E. Felsing  
Chief Executive Officer

## Statement of Chief Financial Officer

Pursuant to 18 U.S.C. Sec 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned Chief Financial Officer of Sempra Energy (the "Company") certifies that:

- (i) the Quarterly Report on Form 10-Q of the Company filed with the Securities and Exchange Commission for the quarter ended September 30, 2008 (the "Quarterly Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 10, 2008

/s/ Mark A. Snell

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Mark A. Snell  
Chief Financial Officer

SEMPRA ENERGY  
UNAUDITED PRO FORMA CONDENSED CONSOLIDATED FINANCIAL INFORMATION

Overview

On April 1, 2008, Sempra Energy (the company) and The Royal Bank of Scotland (RBS) completed the formation of their previously announced partnership, RBS Sempra Commodities LLP (the partnership), to purchase, own and operate the commodity-marketing businesses previously held as subsidiaries of Sempra Energy. Additional information regarding the formation of the partnership is provided in the company's 2007 Annual Report on Form 10-K, Report on Form 8-K dated April 1, 2008, and Quarterly Reports on Form 10-Q for the periods ended March 31, 2008, June 30, 2008 and September 30, 2008.

The following Unaudited Pro Forma Condensed Consolidated Income Statement is presented to illustrate the pro forma effects of the transaction on the historical results of operations of the company. The unaudited pro forma condensed consolidated income statement for the nine months ended September 30, 2008 gives effect to the transaction as if it had occurred on January 1, 2008. The pro forma adjustments are based upon available information, preliminary estimates of closing information and certain assumptions that the company's management believes are reasonable, and are discussed in the accompanying notes. The Unaudited Pro Forma Condensed Consolidated Income Statements and accompanying notes should be read in conjunction with the company's 2007 Annual Report on Form 10-K and Quarterly Reports on Form 10-Q for the periods ended March 31, 2008, June 30, 2008 and September 30, 2008. An unaudited pro forma condensed consolidated balance sheet as of December 31, 2007 and unaudited pro forma condensed consolidated income statement for the year ended December 31, 2007 were previously provided as Exhibit 99.1 in the company's Report on Form 8-K dated April 1, 2008.

The unaudited pro forma financial data is provided for informational purposes only and should not be considered indicative of actual operating results that would have been achieved had the transaction been consummated on the date indicated and do not purport to indicate the results of operations as of any future date or for any future period.

SEMPRA ENERGY  
 UNAUDITED PRO FORMA CONDENSED STATEMENT OF CONSOLIDATED INCOME  
 Nine months ended September 30, 2008

(Dollars in millions, except per share amounts)	Pro Forma Adjustments			Pro Forma Sempra Energy
	Historical Sempra Energy	Reversal of Historical Commodity-marketing Businesses (1) (3)	Pro Forma Earnings from RBS Sempra Commodities LLP (2)(4)	
<b>REVENUES</b>				
Sempra Utilities	\$ 6,190	\$ --	\$ --	\$ 6,190
Sempra Global and parent	2,275	(457)	--	1,818
Total revenues	<u>8,465</u>	<u>(457)</u>	<u>--</u>	<u>8,008</u>
<b>EXPENSES AND OTHER INCOME</b>				
Sempra Utilities:				
Cost of natural gas	(2,708)	--	--	(2,708)
Cost of electric fuel and purchased power	(694)	--	--	(694)
Sempra Global and parent:				
Cost of natural gas, electric fuel and purchased power	(1,353)	--	--	(1,353)
Other cost of sales	(168)	133	--	(35)
Operation and maintenance	(1,816)	214	--	(1,602)
Depreciation and amortization	(508)	6	--	(502)
Franchise fees and other taxes	(230)	--	--	(230)
Gains on sale of assets	114	--	--	114
Equity earnings:				
RBS Sempra Commodities LLP	142	--	45	187
Other	29	--	--	29
Other income, net	23	--	--	23
Interest income	36	(5)	--	31
Interest expense	(165)	12	--	(153)
Preferred dividends of subsidiaries	(7)	--	--	(7)
Income from continuing operations before income taxes and equity earnings of certain unconsolidated subsidiaries	1,160	(97)	45	1,108
Income tax expense	(423)	40	(16)	(399)
Equity earnings, net of income tax	57	(3)	--	54
Income from continuing operations	<u>\$ 794</u>	<u>\$ (60)</u>	<u>\$ 29</u>	<u>\$ 763</u>
Basic earnings per share:				
Income from continuing operations	<u>\$ 3.18</u>			<u>\$ 3.06</u>
Weighted-average number of shares outstanding (thousands)	<u>249,311</u>			<u>249,311</u>
Diluted earnings per share:				
Income from continuing operations	<u>\$ 3.13</u>			<u>\$ 3.01</u>
Weighted-average number of shares outstanding (thousands) (5)	<u>253,407</u>			<u>253,407</u>

See Notes to Unaudited Pro Forma Condensed Statement of Consolidated Income.



## **Notes to Unaudited Pro Forma Condensed Statement of Consolidated Income**

1. Reflects the reversal of the historical results of operations for the three months ended March 31, 2008, for the company's commodity-marketing businesses sold to the partnership.
2. Reflects pro forma earnings from the company's equity investment in the partnership as allocated pursuant to the terms of the partnership agreement for the three months ended March 31, 2008. The total pro forma earnings of the partnership were based on the historical earnings of the company's commodity-marketing businesses sold to the partnership.
3. Pro forma income tax adjustments are based on the company's statutory tax rate.
4. The pro forma income tax adjustment is based on the estimated statutory rate related to the commodity-marketing businesses.
5. Diluted earnings per share for the nine months ended September 30, 2008 reflects the inclusion of 4,096,000 additional shares outstanding for the dilutive effect of stock options and restricted stock awards and units.