UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

# FORM 10-K

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended December 31, 2001**

**Commission File Number 1-7850**

# SOUTHWEST GAS CORPORATION

**(Exact name of registrant as specified in its charter)**

| | |
|---|---|
| **California**<br>**(State or other jurisdiction of incorporation or organization)** | **88-0085720**<br>**(I.R.S. Employer Identification No.)** |
| **5241 Spring Mountain Road**<br>**Post Office Box 98510**<br>**Las Vegas, Nevada**<br>**(Address of principal executive offices)** | **89193-8510**<br>**Zip Code)** |

**Registrant's telephone number, including area code: (702) 876-7237**

**Securities registered pursuant to Section 12(b) of the Act:**

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock, $1 par value | New York Stock Exchange, Inc.<br>Pacific Stock Exchange, Inc. |
| 9.125% Trust Originated Preferred Securities | New York Stock Exchange, Inc.<br>Pacific Stock Exchange, Inc . |
| Stock Purchase Rights | New York Stock Exchange, Inc.<br>Pacific Stock Exchange, Inc. |

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 [X] No [ ]**

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

**Aggregate market value of the voting stock held by nonaffiliates of the registrant:**
$777,042,220 as of March 11, 2002

**The number of shares outstanding of common stock:**
Common Stock, $1 Par Value, 32,745,142 shares as of March 11, 2002

**DOCUMENTS INCORPORATED BY REFERENCE**

| Description | Part Into Which Incorporated |
|---|---|
| Annual Report to Shareholders for the Year Ended December 31, 2001 | Parts I, II, and IV |
| Proxy Statement dated April 2, 2002 | Part III |

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# PART I

## Item 1. BUSINESS

Southwest Gas Corporation (the Company) is incorporated, effective March 1931, under the laws of the State of California. The Company is comprised of two business segments: natural gas operations (Southwest or the natural gas operations segment) and construction services. Southwest is engaged in the business of purchasing, transporting, and distributing natural gas in portions of Arizona, Nevada and California. Southwest is the largest distributor in Arizona, selling and transporting natural gas in most of central and southern Arizona, including the Phoenix and Tucson metropolitan areas. Southwest is also the largest distributor and transporter of natural gas in Nevada, serving the Las Vegas metropolitan area and northern Nevada. In addition, Southwest distributes and transports natural gas in portions of California, including the Lake Tahoe area and the high desert and mountain areas in San Bernardino County.

Northern Pipeline Construction Co. (Northern or the construction services segment), a wholly owned subsidiary, is a full-service underground piping contractor which provides utility companies with trenching and installation, replacement, and maintenance services for energy distribution systems.

Financial information with respect to industry segments is included in Note 11 of the Notes to Consolidated Financial Statements which is included in the 2001 Annual Report to Shareholders and is incorporated herein by reference.

## NATURAL GAS OPERATIONS

### General Description

Southwest is subject to regulation by the Arizona Corporation Commission (ACC), the Public Utilities Commission of Nevada (PUCN), and the California Public Utilities Commission (CPUC). These commissions regulate public utility rates, practices, facilities, and service territories in their respective states. The CPUC also regulates the issuance of all securities by the Company, with the exception of short-term borrowings. Certain accounting practices, transmission facilities, and rates are subject to regulation by the Federal Energy Regulatory Commission (FERC).

Southwest purchases, transports, and distributes natural gas to 1,397,000 residential, commercial, and industrial customers in geographically diverse portions of Arizona, Nevada, and California. There were 60,000 customers added to the system during 2001.

The table below lists the percentage of operating margin (operating revenues less net cost of gas) by major customer class for the years indicated:

| For the Year Ended | Residential and Small Commercial | Other Sales Customers | Transportation |
|---|---|---|---|
| December 31, 2001 | 82% | 8% | 10% |
| December 31, 2000 | 84% | 3% | 13% |
| December 31, 1999 | 83% | 4% | 13% |

Southwest is not dependent on any one or a few customers to the extent that the loss of any one or several would have a significant adverse impact on earnings.

Transportation of customer-secured gas to end-users accounted for 50 percent of total system throughput in 2001. Although the volumes were significant, these customers provide a much smaller proportionate share of operating margin. In 2001, customers who utilized this service transported 127 million dekatherms, down from 148 million dekatherms in 2000. This reduction primarily reflected a shift by a number of large commercial and industrial customers from transportation service to sales service.

The demand for natural gas is seasonal. Variability in weather from normal temperatures can materially impact results of operations. It is the opinion of management that comparisons of earnings for interim periods do not reliably reflect overall trends and changes in operations. Also, earnings for interim periods can be significantly affected by the timing of general rate relief.

**Rates and Regulation**

Rates that Southwest is authorized to charge its distribution system customers are determined by the ACC, PUCN, and CPUC in general rate cases and are derived using rate base, cost of service, and cost of capital experienced in a historical test year, as adjusted in Arizona and Nevada, and projected for a future test year in California. The FERC regulates the northern Nevada transmission and liquefied natural gas (LNG) storage facilities of Paiute Pipeline Company (Paiute), a wholly owned subsidiary, and the rates it charges for transportation of gas directly to certain end-users and to various local distribution companies (LDCs). The LDCs transporting on the Paiute system are: Sierra Pacific Power Company (serving Reno and Sparks, Nevada), Avista Utilities (serving South Lake Tahoe, California), and Southwest Gas Corporation (serving Truckee and North Lake Tahoe, California and various locations throughout northern Nevada).

Rates charged to customers vary according to customer class and rate jurisdiction and are set at levels allowing for the recovery of all prudently incurred costs, including a return on rate base sufficient to pay interest on debt, preferred securities distributions, and a reasonable return on common equity. Rate base consists generally of the original cost of utility plant in service, plus certain other assets such as working capital and inventories, less accumulated depreciation on utility plant in service, net deferred income tax liabilities, and certain other deductions. Rate schedules in all service areas contain purchased gas adjustment (PGA) clauses, which allow Southwest to file for rate adjustments as the cost of purchased gas changes. In Nevada, tariffs provide for annual adjustment dates for changes in purchased gas costs. In addition, Southwest may request to adjust rates more often, if conditions warrant. In Arizona, Southwest adjusts rates monthly for changes in purchased gas costs, within pre-established limits. In California, a monthly gas cost adjustment based on forecasted monthly prices is used to adjust rates. PGA rate changes affect cash flows but have no direct impact on profit margin. Filings to change rates in accordance with PGA clauses are subject to audit by state regulatory commission staffs. Information with respect to recent general rate cases and PGA filings is included in the Rates and Regulatory Proceedings section of Management’s Discussion and Analysis (MD&A) in the 2001 Annual Report to Shareholders.

The table below lists the docketed general rate filings last initiated and/or completed within each ratemaking area:

| Ratemaking Area | Type of Filing | Month Filed | Month Final Rates Effective |
|---|---|---|---|
| Arizona | General rate case | May 2000 | November 2001 |
| California: | | | |
| Northern and Southern | General rate case | February 2002 | Pending |
| Nevada: | | | |
| Northern and Southern | General rate case | July 2001 | December 2001 |
| FERC: | | | |
| Paiute | General rate case | July 1996 | January 1997 |

**Restructuring Initiatives**

Over the past four years, both the CPUC and the PUCN have initiated the development of new rules for the further restructuring of the natural gas distribution industry to allow more competition. However, the development of new rules has slowed in recent years and, in fact, the trend is toward re-regulation after the recent unfavorable experiences in the California market related to energy pricing. There are no similar initiatives in Arizona.

In October 2000, an Energy Policy Committee was formed by the Governor of Nevada to recommend a long-term energy plan for the state. The 17-member committee, which included state government officials, utility company executives and other community and industry representatives, submitted their recommendations in January 2001. They submitted a series of policy proposals regarding conservation and alternative energy sources, but made it clear that given the instability of the electric energy market, they did not support full deregulation in the immediate future. During the 2001 session of the Nevada State Legislature, a bill was approved that repealed electric utility deregulation legislation previously passed.

**Demand for Natural Gas**

Deliveries of natural gas by Southwest are made under a priority system established by state regulatory commissions. The priority system is intended to ensure that the gas requirements of higher-priority customers, primarily residential customers and other customers who use 500 therms of gas per day or less, are fully satisfied on a daily basis before lower-priority customers, primarily electric utility and large industrial customers able to use alternative fuels, are provided any quantity of gas or capacity.

Demand for natural gas is greatly affected by temperature. On cold days, use of gas by residential and commercial customers may be as much as eight times greater than on warm days because of increased use of gas for space heating. To fully satisfy this increased high-priority demand, gas is withdrawn from storage, or peaking supplies are purchased from suppliers. If necessary, service to interruptible lower-priority customers may be curtailed to provide the needed delivery system capacity. No curtailment occurred during the latest peak heating season. Southwest maintains no backlog on its orders for gas service.

**Natural Gas Supply**

Southwest is responsible for acquiring (purchasing) and arranging delivery of (transporting) natural gas to its system for all sales customers. Southwest believes that natural gas supplies and pipeline capacity for transportation will continue to be sufficient to meet market demands in its service territories.

The primary objective of Southwest with respect to gas supply is to ensure that adequate, as well as economical, supplies of natural gas are available from reliable sources. Gas is acquired from a wide variety of sources and a mix of purchase provisions, including spot market purchases and firm supplies with a variety of terms. During 2001, Southwest acquired gas supplies from approximately 60 suppliers. This practice mitigates the risk of nonperformance by any one supplier.

Balancing reliable supply assurances with the associated costs results in a continually changing mix of purchase provisions within the supply portfolios. To address the unique requirements of its various market areas, Southwest assembles and administers separate natural gas supply portfolios for each of its jurisdictional areas. Firm and spot market natural gas purchases are made in a competitive bid environment. California purchases are subject to both fixed-price and index-based pricing arrangements. For the Nevada and Arizona portfolios, the majority of purchases involve index-based pricing arrangements. However, a portion of firm supplies is contracted on a fixed-price basis. This process allows Southwest to acquire gas at current market prices in conjunction with a level of mitigation of price volatility. In managing its gas supply portfolio, Southwest does not currently utilize stand-alone derivative financial instruments, but may do so in the future to hedge against possible price increases. Any such change would be undertaken only with regulatory commission authorization to recover costs associated with these activities.

From the second quarter of 2000 through the second quarter of 2001, Southwest experienced unprecedented increases in natural gas prices. The increase was due to many factors and was a nationwide phenomenon affecting utilities and consumers throughout the United States. These increases peaked during the winter of 2000-2001 when the system-wide average cost of gas for Southwest was nearly $7.00 per dekatherm. Prices were significantly lower by the end of 2001, averaging less than $4.00 per dekatherm in December primarily as a result of lower energy demand, increased storage levels, and general economic conditions.

Gas supplies for the southern system of Southwest (Arizona, southern Nevada, and southern California properties) are primarily obtained from producing regions in Colorado and New Mexico (San Juan basin), Texas (Permian basin), and Rocky Mountain areas. For its northern system (northern Nevada and northern California properties), Southwest primarily obtains gas from Rocky Mountain producing areas and from Canada.

Southwest arranges for transportation of gas to its Arizona, Nevada, and California service territories through the pipeline systems of El Paso Natural Gas Company (El Paso), Kern River Gas Transmission Company (Kern River), Transwestern Pipeline Company, Northwest Pipeline Corporation, Paiute Pipeline Company, and Southern California Gas Company. Supply and pipeline capacity availability on both short- and long-term bases is continually monitored by Southwest to ensure the continued reliability of service to its customers. Southwest currently receives firm transportation service, on both short- and long-term bases, for all of its service territories on the pipeline systems noted above, and also has interruptible contracts in place that allow additional capacity to be utilized should an unforeseen need arise.

The Company believes that the current level of contracted firm interstate capacity is sufficient to serve each of the service territories. As the need arises to acquire additional capacity on one of the interstate pipeline transmission systems, primarily due to customer growth, Southwest considers available options to obtain the capacity, either through the use of firm contracts with a pipeline company or by purchasing capacity on the open market.

In its Arizona service territories, Southwest receives the contractual benefit of being a full-requirements shipper on the El Paso system. The capacity needs of a full-requirements shipper are met before those of other shippers. Certain filings by El Paso with the FERC during 2001 prompted non full-requirements shippers to file a complaint with the FERC. This complaint alleges among other things that unlimited rights of full-requirements shippers cause damage to other shippers because there is insufficient pipeline capacity to serve all firm requirements for all shippers. The FERC has currently taken no action on the complaint although management believes that the status of full-requirements shippers may change as a result of these complaints. Southwest, along with the ACC and other full-requirements shippers, has and will continue to actively participate in any proceedings related to the complaint in order to serve the best interests of its Arizona customers.

**Competition**

Electric utilities are the principal competitors of Southwest for the residential and small commercial markets throughout its service areas. Competition for space heating, general household, and small commercial energy needs generally occurs at the initial installation phase when the customer/builder typically makes the decision as to which type of equipment to install and operate. The customer will generally continue to use the chosen energy source for the life of the equipment. As a result of its success in these markets, Southwest has experienced consistent growth among the residential and small commercial customer classes.

Unlike residential and small commercial customers, certain large commercial, industrial, and electric generation customers have the capability to switch to alternative energy sources. To date, Southwest has been successful in retaining most of these customers by setting rates at levels competitive with alternative energy sources such as electricity, fuel oils, and coal. However, increases in natural gas prices, if sustained for an extended period of time, may impact Southwest’s ability to retain some of these customers. Overall, management does not anticipate any material adverse impact on operating margin from fuel switching.

Southwest continues to compete with interstate transmission pipeline companies, such as El Paso, Kern River, and Tuscarora Gas Transmission Company, to provide service to certain large end-users. End-use customers located in close proximity to these interstate pipelines pose a potential bypass threat and, therefore, require Southwest to closely monitor each customer situation and provide competitive service in order to retain the customer. Southwest has remained competitive through the use of negotiated transportation contract rates, special long-term contracts with electric generation and cogeneration customers, and new tariff programs. These competitive response initiatives have helped mitigate the financial impact from the threat of bypass and the potential loss of margin currently earned from large customers.

**Environmental Matters**

Federal, state, and local laws and regulations governing the discharge of materials into the environment have had little direct impact upon Southwest. Environmental efforts, with respect to matters such as protection of endangered species and archeological finds, have increased the complexity and time required to obtain pipeline rights-of-way and construction permits. However, increased environmental legislation and regulation are also beneficial to the natural gas industry. Because natural gas is one of the most environmentally safe fossil fuels currently available, its use helps energy users comply with stricter environmental standards.

**Employees**

At December 31, 2001, the natural gas operations segment had 2,507 regular full-time equivalent employees. Southwest believes it has a good relationship with its employees. In May 1999, non-exempt employees in the Central Arizona Division voted to have the International Brotherhood of Electrical Workers (IBEW) represent them in employee-related matters with Southwest. In July 2000, Southwest, the National Labor Relations Board (NLRB) and the IBEW entered into a NLRB Settlement Agreement whereby Southwest recognized the IBEW as the bargaining agent for these employees. Subsequently, Southwest and the IBEW have been negotiating a contract. However, currently, there is no contract in place related to the 482 full-time equivalent non-exempt Central Arizona Division employees. No other natural gas operations segment employees are represented by a union.

## CONSTRUCTION SERVICES

Northern Pipeline Construction Co. (Northern or the construction services segment) is a full-service underground piping contractor, which provides utility companies with trenching and installation, replacement, and maintenance services for energy distribution systems. Northern contracts primarily with LDCs to install, repair, and maintain energy distribution systems from the town border station to the end-user. The primary focus of business operations is main and service replacement as well as new business installations. Construction work varies from relatively small projects to the piping of entire communities. Construction activity is seasonal in most areas. Peak construction periods are the summer and fall months in colder climate areas, such as the midwest. In the warmer climate areas, such as the southwestern United States, construction continues year round.

Northern business activities are often concentrated in utility service territories where existing energy lines are scheduled for replacement. An LDC will typically contract with Northern to provide pipe replacement services and new line installations. Contract terms generally specify unit-price or fixed-price arrangements. Unit-price contracts establish prices for all of the various services to be performed during the contract period. These contracts often have annual pricing reviews. During 2001, approximately 92 percent of revenue was earned under unit-price contracts. As of December 31, 2001 no significant backlog existed with respect to outstanding construction contracts.

Competition within the industry has traditionally been limited to several regional competitors in what has been a largely fragmented industry. Several national competitors also exist within the industry. Northern currently operates in approximately 17 major markets nationwide. Its customers are the primary LDCs in those markets. During 2001, Northern served 53 major customers, with Southwest accounting for approximately 33 percent of their revenues. No other customer had a relatively significant contribution to Northern revenues.

Employment fluctuates between seasonal construction periods, which are normally heaviest in the summer and fall months. At December 31, 2001, Northern had 2,000 regular full-time-equivalent employees. Employment peaked in

October 2001 when there were 2,370 employees. The majority of the employees are represented by unions and are covered by collective bargaining agreements, which is typical of the utility construction industry.

Operations are conducted from 17 field locations with corporate headquarters located in Phoenix, Arizona. All buildings are leased from third parties. The lease terms are typically five years or less. Field location facilities consist of a small building for repairs and land to store equipment.

## COMPANY RISK FACTORS

Described below are some of the identified risk factors of the Company that may have a negative impact on our future financial performance. Unless indicated otherwise, references below to “we”, “us” and “our” should be read to refer to Southwest Gas Corporation and its subsidiaries.

**OUR LIQUIDITY, AND IN CERTAIN CIRCUMSTANCES, EARNINGS, COULD BE ADVERSELY AFFECTED BY THE COST OF PURCHASING NATURAL GAS DURING PERIODS IN WHICH NATURAL GAS PRICES ARE RISING SIGNIFICANTLY.**

Rate schedules in each of our service territories contain purchased gas adjustment clauses which permit us to file for rate adjustments to recover increases in the cost of purchased gas. Increases in the cost of purchased gas have no direct impact on our profit margins, but do affect cash flows and can therefore impact the amount of our capital resources. Natural gas prices were unusually high during the first half of 2001, but have since dropped. We have used short-term borrowings in the past to temporarily finance increases in purchased gas costs, and we expect to do so during 2002, if the need again arises.

We may file requests for rate increases to cover the rise in the costs of purchased gas. Due to the nature of the regulatory process, there is a risk of a disallowance of full recovery of these costs during any period in which there has been a substantial run-up of these costs. Any material disallowance of purchased gas costs could have a material impact on cash flow and earnings. Gas procurement costs for our southern California customers are under review by the California Public Utilities Commission. Hearings in this matter were held in January 2002 with a final decision anticipated in the second quarter of 2002.

**SIGNIFICANT CUSTOMER GROWTH IN ARIZONA AND NEVADA COULD STRAIN OUR CAPITAL RESOURCES AND IMPACT EARNINGS.**

We continue to experience significant population and customer growth throughout our service territories. During 2001 we added 60,000 customers, a four percent growth rate. Over the last several years, customer growth has averaged five percent. This growth has required large amounts of capital to finance the investment in new transmission and distribution plant. In 2001, our natural gas construction expenditures totaled $248 million. Approximately 74 percent of these current-period expenditures represented new construction, and the balance represented costs associated with routine replacement of existing transmission, distribution and general plant.

Cash flows from operating activities (net of dividends) have been inadequate, and are expected to continue to be inadequate, to fund all necessary capital expenditures. We have been funding this shortfall through the issuance of additional debt and equity securities, and will continue to do so. Our ability to issue additional securities is dependent upon, among other things, conditions in the capital markets, regulatory authorizations and our level of earnings.

Our ability to earn the rates of return authorized by the Arizona Corporation Commission and the Public Utilities Commission of Nevada is also adversely affected by significant customer growth, because the rates we charge our distribution customers in Arizona and Nevada are derived using rate base, cost of service and cost of capital experienced in an historical test year, as adjusted. This results in “regulatory lag” which delays our recovery of some of the costs of capital improvements and operating costs from customers in Arizona and Nevada.

**OUR EARNINGS ARE GREATLY AFFECTED BY VARIATIONS IN TEMPERATURE DURING THE WINTER HEATING SEASON.**

The demand for natural gas is seasonal and is greatly affected by temperature. Variability in weather from normal temperatures can materially impact results of operations. On cold days, use of gas by residential and commercial customers may be as much as eight times greater than on warm days because of the increased use of gas for space heating. Weather has been and will continue to be one of the dominant factors in our financial performance.

**UNCERTAIN ECONOMIC CONDITIONS MAY AFFECT OUR ABILITY TO FINANCE CAPITAL EXPENDITURES AND TO REFINANCE MATURING DEBT.**

Our ability to finance capital expenditures, to refinance maturing debt and other matters will depend upon general economic conditions in the capital markets. The direction of interest rates is uncertain. Declining interest rates are generally believed to be favorable to utilities while rising interest rates are believed to be unfavorable because of the high capital costs of utilities. In addition, our authorized rate of return is based upon certain assumptions regarding interest rates. If interest rates are lower than assumed rates, our authorized rate of return could be reduced. If interest rates are higher than assumed rates, our ability to earn our authorized rate of return may be adversely impacted.

**OUR ABILITY TO PAY DIVIDENDS, ALTHOUGH RESTRICTED BY CALIFORNIA CORPORATION LAW, IS MORE LIKELY TO BE DEPENDENT UPON FUTURE EARNINGS, OUR ABILITY TO REFINANCE MATURING DEBT AND THE TERMS OF OUR DEBT INSTRUMENTS.**

We do not anticipate that restrictions imposed by California Corporation Law will impact our ability to pay dividends in the foreseeable future.

It is likely that the amount of dividends declared by our Board of Directors will depend to a substantial degree on the level of our future earnings, our ability to refinance debt of $308 million which matures in 2002, and the terms of our debt instruments. None of our current debt instruments directly restricts our ability to pay dividends. Certain of our debt instruments do, however, contain leverage and net worth covenants. We do not anticipate that these covenants will impact our ability to pay dividends unless the amount to be paid out in dividends greatly exceeds our earnings. The last year dividends paid exceeded earnings was 1997. In 2001, earnings exceeded the amount paid out in dividends by an aggregate of $11 million.

## Item 2. PROPERTIES

The plant investment of Southwest consists primarily of transmission and distribution mains, compressor stations, peak shaving/storage plants, service lines, meters, and regulators which comprise the pipeline systems and facilities located in and around the communities served. Southwest also includes other properties such as land, buildings, furnishings, work equipment, vehicles and software systems in plant investment. The northern Nevada and northern California properties of Southwest are referred to as the northern system; the Arizona, southern Nevada, and southern California properties are referred to as the southern system. Several properties are leased by Southwest, including an LNG storage plant on its northern Nevada system, a portion of the corporate headquarters office complex located in Las Vegas, Nevada, and the administrative offices in Phoenix, Arizona. Total gas plant, exclusive of leased property, at December 31, 2001 was $2.6 billion, including construction work in progress. It is the opinion of management that the properties of Southwest are suitable and adequate for its purposes.

Substantially all gas main and service lines are constructed across property owned by others under right-of-way grants obtained from the record owners thereof, on the streets and grounds of municipalities under authority conferred by franchises or otherwise, or on public highways or public lands under authority of various federal and state statutes. None of the numerous county and municipal franchises are exclusive, and some are of limited duration. These franchises are renewed regularly as they expire, and Southwest anticipates no serious difficulties in obtaining future renewals.

With respect to the right-of-way grants, Southwest has had continuous and uninterrupted possession and use of all such rights-of-way, and the associated gas mains and service lines, commencing with the initial stages of the construction of such facilities. Permits have been obtained from public authorities in certain instances to cross or to lay facilities along roads and highways. These permits typically are revocable at the election of the grantor and Southwest occasionally must relocate its facilities when requested to do so by the grantor. Permits have also been obtained from railroad companies to cross over or under railroad lands or rights-of-way, which in some instances require annual or other periodic payments and are revocable at the election of the grantors.

Southwest operates two primary pipeline transmission systems: (i) a system owned by Paiute, a wholly owned subsidiary, extending from the Idaho-Nevada border to the Reno, Sparks, and Carson City areas and communities in the Lake Tahoe area in both California and Nevada and other communities in northern and western Nevada; and (ii) a system extending from the Colorado River at the southern tip of Nevada to the Las Vegas distribution area.

The following map shows the locations of major Southwest facilities and transmission lines, and principal communities to which Southwest supplies gas either as a wholesaler or distributor. The map also shows major supplier transmission lines that are interconnected with the Southwest systems.

The information appearing in **Part I, Item 1. Business**, page 5 with respect to the construction services segment is incorporated herein by reference.

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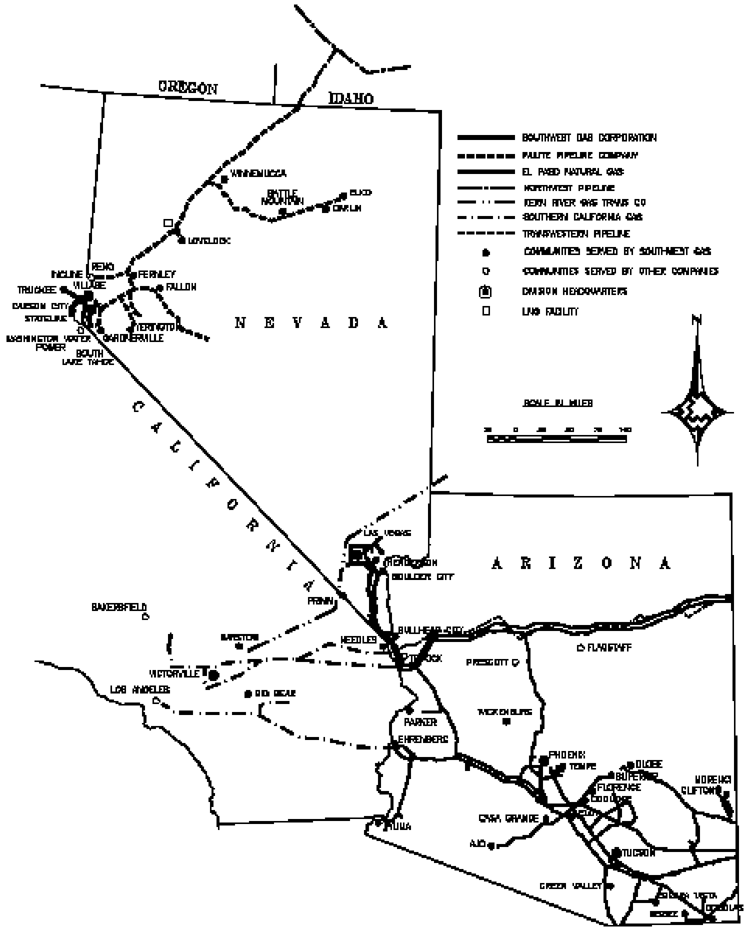

**Item 3. LEGAL PROCEEDINGS**

Litigation is pending in the U.S. District Court for the District of Arizona consisting of two cases that were originally filed in the District of Arizona (Civ '99 1294 PHX ROS and Civ '00 0119 PHX ROS), two cases that were transferred to the District of Arizona from the U.S. District Court for the Northern District of Oklahoma (Civ '00 1775 PHX ROS and Civ '00 1812 PHX ROS) and one case that was transferred to the District of Arizona from the U.S. District Court for the District of Nevada (Civ '00 0452 PHX ROS). All of the litigation relates to the now terminated acquisition of the Company by ONEOK, Inc. (ONEOK) and the rejection of competing offers from Southern Union Company (Southern Union). After multiple court rulings on motions to dismiss and motions for summary judgment, only a few of the original claims remain.

**Original Claims of Southern Union**

On July 19, 1999, Southern Union filed a complaint against the Company, several of its officers and directors, ONEOK and others. The complaint was amended on October 11, 1999 and July 24, 2000. As amended, the complaint alleged that the Company, Michael O. Maffie, President and Chief Executive Officer of the Company, Thomas Y. Hartley, Chairman of the Board of the Company, and Edward S. Zub, Senior Vice President Regulation and Pricing of the Company, ONEOK and others conspired to block Company shareholders from voting upon the Southern Union offer and have acted to ensure that the Company's Board of Directors would approve and recommend the ONEOK offer to the Company's shareholders and to influence the vote of members of regulatory commissions required to approve the proposed acquisition of the Company by ONEOK in violation of state and federal criminal laws. The complaint, as amended, further alleged that the defendants fraudulently induced Southern Union to enter into the February 21, 1999 confidentiality and standstill agreement, Southwest breached the terms of that agreement and its covenant of good faith and fair dealing, and all defendants, other than Southwest, Mr. Hartley and Mr. Zub, intentionally interfered with a business relationship between the Company and Southern Union and tortiously interfered with contractual relations between the Company and Southern Union. The complaint, as amended, further alleged that the defendants violated both the federal and Arizona racketeering statutes.

Southern Union sought damages in an amount not less than $750 million to be trebled for the alleged violations of state and federal criminal law, compensatory damages in an amount not less than $750 million, plus interest, rescission of the confidentiality and standstill agreement between the Company and Southern Union and punitive damages.

**Original Claims of ONEOK**

On January 21, 2000, ONEOK filed a complaint against the Company in the U.S. District Court for the Northern District of Oklahoma and amended its complaint on August 23, 2000. As amended, the complaint sought rescission of the merger agreement executed by the Company and ONEOK (the "Merger Agreement") due to fraudulent inducement, damages for fraudulent inducement and damages for breach of contract. The action was transferred to the U.S. District Court for the District of Arizona (Case No. Civ '00 1775 PHX ROS) on September 18, 2000.

**Original Claims of the Company**

On April 30, 1999, the Company filed a complaint against Southern Union in the U.S. District Court for the District of Nevada alleging a breach of the confidentiality and standstill agreement between the Company and Southern Union, breach of the implied covenant of good faith and fair dealing, misappropriation of trade secrets, intentional interference with contract, intentional interference with prospective economic advantage and other violations of California and Nevada law. The Company amended its complaint on May 6, 1999, adding an additional claim against Southern Union pursuant to Section 14(a) of the Securities Exchange Act of 1934. On July 22, 1999, Southern Union filed a motion for leave to amend its answer in the Nevada federal action and to assert counterclaims against the Company. The counterclaims mirror the contractual claims filed by Southern Union in the Arizona action described above. Southern Union's motion for leave to amend was granted. On March 8, 2000, this action was transferred to the U.S. District Court for the District of Arizona (Case No. Civ '00 0452 PHX ROS).

On January 24, 2000, the Company filed a complaint against ONEOK and Southern Union in the U.S. District Court for the District of Arizona (Case No. Civ '00 0119 PHX ROS). The lawsuit sought unspecified damages from ONEOK for breach of contract, breach of the implied covenant of good faith and fair dealing, fraud in the inducement, and fraud related to its actions connected to the Merger Agreement and its cancellation of the Merger Agreement. The lawsuit also sought unspecified damages from Southern Union for breach of contract, breach of the implied covenant of good faith and fair dealing, and interference with a contract, all related to attempts by Southern Union to block the proposed Southwest Gas-ONEOK combination after the unsolicited offer by Southern Union was rejected by the Company.

**Claims That Remain**

U.S. District Judge Roslyn O. Silver presides over the Arizona litigation. Through the course of the litigation, Judge Silver has dismissed with prejudice numerous claims, most recently by order dated January 4, 2002. Following conclusion of a trial on the merits, any of the parties may appeal Judge Silver's dismissal of some or all of the claims that have been dismissed.

The following claims involving the Company and its officers and directors have not been dismissed:

(1) Claims by Southern Union for fraudulent inducement against the Company and Mr. Maffie and claims by Southern Union for breach of contract and breach of covenant of good faith and fair dealing against the Company. Damages for these claims are limited to out-of-pocket expenses of Southern Union and any punitive damages Southern Union can prove.

(2) Claims by ONEOK for fraudulent inducement against the Company. Damages for this claim are limited to out-of-pocket expenses of ONEOK and any punitive damages ONEOK can prove.

(3) Claims by the Company against ONEOK for breach of contract, breach of the implied covenant of good faith and fair dealing, fraud in the inducement and fraud. Damages for these claims are limited to out-of-pocket expenses of the Company and any punitive damages the Company can prove.

All claims against Southern Union by the Company have been dismissed.

A trial date for the remaining claims is set for October 2002. It is anticipated that the trial could last two to three months.

There is also an ongoing joint federal, state and county criminal investigation in Phoenix, Arizona concerning activities surrounding the failed acquisition of the Company by ONEOK. The Company is cooperating fully with this investigation.

*Other Proceedings*

The Company has been named as defendant in various other legal proceedings. The ultimate dispositions of these proceedings are not presently determinable; however, it is the opinion of management that none of this litigation will have a material adverse impact on the Company's financial position or results of operations.

**Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

# PART II

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

The principal markets on which the common stock of the Company is traded are the New York Stock Exchange and the Pacific Stock Exchange. At March 11, 2002, there were 23,003 holders of record of common stock, and the market price of the common stock was $23.73. The quarterly market price of and dividends on Company common stock required by this item are included in the 2001 Annual Report to Shareholders and are incorporated herein by reference.

## Item 6. SELECTED FINANCIAL DATA

Information required by this item is included in the 2001 Annual Report to Shareholders and is incorporated herein by reference.

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

Information required by this item is included in the 2001 Annual Report to Shareholders and is incorporated herein by reference.

## Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Information responding to Item 7A appears in the 2001 Annual Report to Shareholders under the heading "Management's Discussion and Analysis" and under Notes 6 and 7 of the Notes to Consolidated Financial Statements. This information is incorporated herein by reference. Other risk information is included under the heading "Company Risk Factors" in **Item 1. Business** of this report.

## Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The Consolidated Financial Statements of Southwest Gas Corporation and Notes thereto, together with the report of Arthur Andersen LLP, Independent Public Accountants, are included in the 2001 Annual Report to Shareholders and are incorporated herein by reference.

## Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

## PART III

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

(a) *Identification of Directors.* Information with respect to Directors is set forth under the heading "Election of Directors" in the definitive Proxy Statement dated April 2, 2002, which by this reference is incorporated herein.

(b) *Identification of Executive Officers.* The name, age, position and period position held during the last five years for each of the Executive Officers of the Company are as follows:

| Name | Age | Position | Period Position Held |
|---|---|---|---|
| Michael O. Maffie | 54 | President and Chief Executive Officer | 1997-Present |
| George C. Biehl | 54 | Executive Vice President/Chief Financial Officer and Corporate Secretary Senior Vice President/Chief Financial Officer and Corporate Secretary | 2000-Present<br>1997-2000 |
| James P. Kane | 55 | Executive Vice President/Operations<br>Senior Vice President/Operations<br>Vice President/Southern Arizona Division | 2000-Present<br>1997-2000<br>1997 |
| Edward S. Zub | 53 | Executive Vice President/Consumer Resources and Energy Services Senior Vice President/Regulation and Product Pricing | 2000-Present<br>1997-2000 |
| James F. Lowman | 55 | Senior Vice President/Central Arizona Division | 1997-Present |
| Jeffrey W. Shaw | 43 | Senior Vice President/Finance and Treasurer<br>Vice President/Treasurer | 2000-Present<br>1997-2000 |
| Thomas R. Sheets | 51 | Senior Vice President/Legal Affairs and General Counsel Vice President/General Counsel | 2000-Present<br>1997-2000 |
| Dudley J. Sondeno | 49 | Senior Vice President/Chief Knowledge and Technology Officer | 1997-Present |
| Edward A. Janov | 47 | Vice President/Chief Accounting Officer Vice President/Controller and Chief Accounting Officer | 2001- Present<br>1997-2000 |

(c) *Identification of Certain Significant Employees.* None.

(d) *Family Relationships.* No Directors or Executive Officers are related to any other either by blood, marriage, or adoption.

(e) *Business Experience.* Information with respect to Directors is set forth under the heading "Election of Directors" in the definitive Proxy Statement dated April 2, 2002, which by this reference is incorporated herein. All Executive Officers have held responsible positions with the Company for at least five years as described in (b) above.

(f) *Involvement in Certain Legal Proceedings.* None.

(g) *Promoters and Control Persons.* None.

*Section 16(a) Beneficial Ownership Reporting Compliance.* Section 16(a) of the Securities Exchange Act of 1934 requires officers and directors, and persons who own more than ten percent of a registered class of equity securities, to file reports of ownership and changes in ownership with the Securities and Exchange Commission (SEC) and the New York Stock Exchange. Officers, directors, and beneficial owners of more than ten percent of any class of equity securities are required by SEC regulation to furnish the Company with copies of all Section 16(a) forms they file.

The Company has adopted procedures to assist its directors and executive officers in complying with Section 16(a) of the Securities and Exchange Act of 1934, as amended, which includes assisting in the preparation of forms for filing. For 2001, all the required reports were filed timely.

**Item 11. EXECUTIVE COMPENSATION**

Information with respect to executive compensation is set forth under the heading “Executive Compensation and Benefits” in the definitive Proxy Statement dated April 2, 2002, which by this reference is incorporated herein.

**Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT**

(a) *Security Ownership of Certain Beneficial Owners.* Information with respect to security ownership of certain beneficial owners is set forth under the heading “Securities Ownership by Nominees, Executive Officers, and Beneficial Owners” in the definitive Proxy Statement dated April 2, 2002, which by this reference is incorporated herein.

(b) *Security Ownership of Management.* Information with respect to security ownership of management is set forth under the heading “Securities Ownership by Nominees, Executive Officers, and Beneficial Owners” in the definitive Proxy Statement dated April 2, 2002, which by this reference is incorporated herein.

(c) *Changes in Control.* None.

**Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

None.

## PART IV

**Item 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K**

(a) The following documents are filed as part of this report on Form 10-K:

(1) The Consolidated Financial Statements of the Company (including the Report of Independent Public Accountants) required to be reported herein are incorporated by reference to the information reported in the 2001 Annual Report to Shareholders under the following captions:



(2) All schedules have been omitted because the required information is either inapplicable or included in the Notes to Consolidated Financial Statements.

(3) See **LIST OF EXHIBITS**.

(b) Reports on Form 8-K.

The Company filed a Form 8-K, dated January 4, 2002 reporting court orders further addressing the allowable claims and damage issues in litigation pending among Southern Union, ONEOK and the Company.

The Company filed a Form 8-K, dated February 19, 2002 reporting summary financial information for the quarter and year ended December 31, 2001.

(c) See **LIST OF EXHIBITS**.

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**LIST OF EXHIBITS**

| Exhibit Number | Description of Document |
| --- | --- |
| 3(i)(16) | Restated Articles of Incorporation, as amended. |
| 3(ii)(20) | Amended Bylaws of Southwest Gas Corporation. |
| 4.01(1) | Indenture between the Company and Bank of America National Trust and Savings Association, as successor by merger to Security Pacific National Bank, as Trustee, dated August 1, 1986. |
| 4.02(6) | Sixth Supplemental Indenture of the Company to Bank of America National Trust and Savings Association, as successor by merger to Security Pacific National Bank, as Trustee, dated as of June 16, 1992, supplementing and amending the Indenture dated as of August 1, 1986, with respect to 9 3/4% Debentures, Series F, due 2002. |
| 4.03(7) | Indenture between Clark County, Nevada, and Bank of America Nevada as Trustee, dated September 1, 1992, with respect to the issuance of $130,000,000 Industrial Development Revenue Bonds (Southwest Gas Corporation), $30,000,000 1992 Series A, due 2027, and $100,000,000 1992 Series B, due 2032. |
| 4.04(8) | Indenture between Clark County, Nevada, and Harris Trust and Savings Bank as Trustee, dated December 1, 1993, with respect to the issuance of $75,000,000 Industrial Development Revenue Bonds (Southwest Gas Corporation), 1993 Series A, due 2033. |
| 4.05(8) | Indenture between City of Big Bear Lake, California, and Harris Trust and Savings Bank as Trustee, dated December 1, 1993, with respect to the issuance of $50,000,000 Industrial Development Revenue Bonds (Southwest Gas Corporation Project), 1993 Series A, due 2028. |
| 4.06(12) | Indenture between the Company and Harris Trust and Savings Bank dated July 15, 1996, with respect to Debt Securities. |
| 4.07(13) | First Supplemental Indenture of the Company to Harris Trust and Savings Bank dated August 1, 1996, supplementing and amending the Indenture dated as of July 15, 1996, with respect to 7 1/2% and 8% Debentures, due 2006 and 2026, respectively. |
| 4.08(15) | Second Supplemental Indenture of the Company to Harris Trust and Savings Bank dated December 30, 1996, supplementing and amending the Indenture dated as of July 15, 1996, with respect to Medium-Term Notes. |
| 4.09(3) | Certificate of Trust of Southwest Gas Capital I. |
| 4.10(10) | Amended and Restated Declaration of Trust of Southwest Gas Capital I. |
| 4.11(10) | Form of Preferred Security (attached as Annex I to Exhibit A to the Amended and Restated Declaration of Trust of Southwest Gas Capital I included as Exhibit 4.10 hereto). |
| 4.12(4) | Form of Guarantee with respect to Preferred Securities. |
| 4.13(9) | Southwest Gas Capital I Preferred Securities Guarantee by the Company and Harris Trust and Savings Bank, dated as of October 31, 1995. |

| | |
|---|---|
| 4.14(9) | Form of Subordinated Debt Security (included in the First Supplemental Indenture included as Exhibit 4.16 hereto). |
| 4.15(9) | Subordinated Debt Securities Indenture between the Company and Harris Trust and Savings Bank, dated as of October 31, 1995. |
| 4.16(9) | First Supplemental Indenture between the Company and Harris Trust and Savings Bank, dated as of October 31, 1995, supplementing and amending the Indenture dated as of October 31, 1995, with respect to the 9.125% Subordinated Debt Securities. |
| 4.17(2) | Form of Deposit Agreement. |
| 4.18(2) | Form of Depositary Receipt (attached as Exhibit A to Deposit Agreement included as Exhibit 4.17 hereto). |
| 4.19(20) | Amended and Restated Rights Agreement between the Company and Harris Trust Company, as Rights Agent, dated as of February 9, 1999. |
| 4.20(22) | Indenture between Clark County, Nevada, and Harris Trust and Savings Bank as Trustee, dated as of October 1, 1999, with respect to the issuance of $35,000,000 Industrial Development Revenue Bonds (Southwest Gas Corporation), Series 1999A and Taxable Series 1999B or convertibles of Series B (Series C and D), due 2038. |
| 4.21 | The Company hereby agrees to furnish to the SEC, upon request, a copy of any instruments defining the rights of holders of long-term debt issued by Southwest Gas Corporation or its subsidiaries. |
| 4.22(21) | Third Supplemental Indenture between the Company and the Bank of New York, dated as of February 13, 2001, supplementing and amending the Indenture dated as of December 30, 1996, with respect to the $200,000,000, 8.375% Notes, due 2011. |
| 10.01(5) | Participation Agreement among the Company and General Electric Credit Corporation, Prudential Insurance Company of America, Aetna Life Insurance Company, Merrill Lynch Interfunding, Bank of America through purchase of Valley Bank of Nevada, Bankers Trust Company and First Interstate Bank of Nevada, dated as of July 1, 1982. |
| 10.02(14) | Amended and Restated Lease Agreement between the Company and Spring Mountain Road Associates, dated as of July 1, 1996. |
| 10.03(8) | Financing Agreement between the Company and Clark County, Nevada, dated September 1, 1992. |
| 10.04(8) | Financing Agreement between the Company and Clark County, Nevada, dated as of December 1, 1993. |
| 10.05(8) | Project Agreement between the Company and City of Big Bear Lake, California, dated as of December 1, 1993. |
| 10.06(18)* | Southwest Gas Corporation Management Incentive Plan, amended and restated January 1, 1995. |
| 10.07(19)* | Amended Form of Employment Agreement with Company Officers. |
| 10.08(19)* | Amended Form of Change in Control Agreement with Company Officers. |
| 10.09(11)* | Southwest Gas Corporation 1996 Stock Incentive Plan. |

| | |
|---|---|
| 10.10(17) | $350 million Revolving Credit Agreement among the Company, Union Bank of Switzerland, et al., dated as of June 12, 1997. |
| 10.11(22)* | Southwest Gas Corporation Supplemental Retirement Plan, amended and restated as of March 1, 1999. |
| 10.12(22)* | Southwest Gas Corporation Executive Deferral Plan, amended and restated as of March 1, 1999. |
| 10.13(22)* | Southwest Gas Corporation Directors Deferral Plan, amended and restated as of March 1, 1999. |
| 10.14(22)* | Southwest Gas Corporation Board of Directors Retirement Plan, amended and restated as of March 1, 1999. |
| 10.15(22) | Financing Agreement between the Company and Clark County, Nevada, dated as of October 1, 1999. |
| 12.01 | Computation of Ratios of Earnings to Fixed Charges of Southwest Gas Corporation. |
| 13.01 | Portions of 2001 Annual Report incorporated by reference to the Form 10-K. |
| 21.01 | List of subsidiaries of Southwest Gas Corporation. |
| 23.01 | Consent of Arthur Andersen LLP, Independent Public Accountants. |
| 99.01 | Receipt of Assurances from Arthur Andersen LLP. |

(1) Incorporated herein by reference to the Registration Statement on Form S-3, No. 33-7931.
(2) Incorporated herein by reference to the Registration Statement on Form S-3, No. 33-55621.
(3) Incorporated herein by reference to the Registration Statement on Form S-3, No. 33-62143.
(4) Incorporated herein by reference to Amendment No. 1 to Registration Statement on Form S-3, No. 33-62143.
(5) Incorporated herein by reference to the report on Form 10-K for the year ended December 31, 1982.
(6) Incorporated herein by reference to the report on Form 10-Q for the quarter ended June 30, 1992.
(7) Incorporated herein by reference to the report on Form 10-Q for the quarter ended September 30, 1992.
(8) Incorporated herein by reference to the report on Form 10-K for the year ended December 31, 1993.
(9) Incorporated herein by reference to the report on Form 10-Q for the quarter ended September 30, 1995.
(10) Incorporated herein by reference to the report on Form 8-K dated October 26, 1995.
(11) Incorporated herein by reference to the Proxy Statement dated May 30, 1996.
(12) Incorporated herein by reference to the report on Form 8-K dated July 26, 1996.
(13) Incorporated herein by reference to the report on Form 8-K dated July 31, 1996.
(14) Incorporated herein by reference to the report on Form 10-Q for the quarter ended September 30, 1996.
(15) Incorporated herein by reference to the report on Form 8-K dated December 30, 1996.

(16) Incorporated herein by reference to the report on Form 10-Q for the quarter ended March 31, 1997.
(17) Incorporated herein by reference to the report on Form 10-Q for the quarter ended June 30, 1997.
(18) Incorporated herein by reference to the report on Form 10-K for the year ended December 31, 1997.
(19) Incorporated herein by reference to the reports on Form 10-Q for the quarters ended September 30, 1998, September 30, 2000 and September 30, 2001.
(20) Incorporated herein by reference to the report on Form 10-K for the year ended December 31, 1998.
(21) Incorporated herein by reference to the report on Form 8-K dated February 13, 2001.
(22) Incorporated herein by reference to the report on Form 10-K for the year ended December 31, 1999.
* Compensation Plans

## SIGNATURES

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

SOUTHWEST GAS CORPORATION

Date: March 22, 2002

By /s/ MICHAEL O. MAFFIE

Michael O. Maffie,
President and Chief Executive Officer

## SIGNATURES

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

| Signature | Title | Date |
|---|---|---|
| /s/ GEORGE C. BIEHL<br>(George C. Biehl) | Executive Vice President,<br>Chief Financial Officer and<br>Corporate Secretary | March 22, 2002 |
| /s/ EDWARD A. JANOV<br>(Edward A. Janov) | Vice President and<br>Chief Accounting Officer | March 22, 2002 |

**SIGNATURES**

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

| Signature | Title | Date |
|---|---|---|
| /s/ GEORGE C. BIEHL<br>(George C. Biehl) | Director, Executive Vice President,<br>Chief Financial Officer and<br>Corporate Secretary | March 22, 2002 |
| /s/ MANUEL J. CORTEZ<br>(Manuel J. Cortez) | Director | March 22, 2002 |
| /s/ MARK M. FELDMAN<br>(Mark M. Feldman) | Director | March 22, 2002 |
| /s/DAVID H. GUNNING<br>(David H. Gunning) | Director | March 22, 2002 |
| /s/ THOMAS Y. HARTLEY<br>(Thomas Y. Hartley) | Chairman of the Board<br>of Directors | March 22, 2002 |
| /s/ MICHAEL B. JAGER<br>(Michael B. Jager) | Director | March 22, 2002 |
| /s/ LEONARD R. JUDD<br>(Leonard R. Judd) | Director | March 22, 2002 |
| /s/ JAMES J. KROPID<br>(James J. Kropid) | Director | March 22, 2002 |
| /s/ MICHAEL O. MAFFIE<br>(Michael O. Maffie) | Director, President and<br>Chief Executive Officer | March 22, 2002 |
| /s/ CAROLYN M. SPARKS<br>(Carolyn M. Sparks) | Director | March 22, 2002 |
| /s/ TERRANCE L. WRIGHT<br>(Terrance L. Wright) | Director | March 22, 2002 |

## EXHIBIT INDEX

| Exhibit Number | Description of Document |
|---|---|
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| 99.01 | Receipt of Assurances from Arthur Andersen LLP. |

EXHIBIT 12.01

SOUTHWEST GAS CORPORATION

COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES
(THOUSANDS OF DOLLARS)

| | FOR THE YEAR ENDED DECEMBER 31, | | | | |
|---|---|---|---|---|---|
| | 2001 | 2000 | 1999 | 1998 | 1997 |
| 1. Fixed charges: | | | | | |
| A) Interest expense | $ 80,139 | $ 70,659 | $ 63,110 | $ 63,416 | $ 63,247 |
| B) Amortization | 1,886 | 1,564 | 1,366 | 1,243 | 1,164 |
| C) Interest portion of rentals | 9,346 | 8,572 | 8,217 | 7,531 | 6,973 |
| D) Preferred securities distributions | 5,475 | 5,475 | 5,475 | 5,475 | 5,475 |
| Total fixed charges | $ 96,846 | $ 86,270 | $ 78,168 | $ 77,665 | $ 76,859 |
| 2. Earnings (as defined): | | | | | |
| E) Pretax income from continuing operations | $ 56,741 | $ 51,939 | $ 60,955 | $ 83,951 | $ 21,328 |
| Fixed Charges (1. above) | 96,846 | 86,270 | 78,168 | 77,665 | 76,859 |
| Total earnings as defined | $153,587 | $138,209 | $139,123 | $161,616 | $ 98,187 |
| 3. Ratio of earnings to fixed charges | 1.59 | 1.60 | 1.78 | 2.08 | 1.28 |

# FINANCIAL REVIEW

CONSOLIDATED SELECTED FINANCIAL STATISTICS

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 | 1998 | 1997 |
|---|---|---|---|---|---|
| (Thousands of dollars, except per share amounts) | | | | | |
| Operating revenues | $1,396,688 | $1,034,087 | $ 936,866 | $ 917,309 | $ 732,010 |
| Operating expenses | 1,262,705 | 905,457 | 805,654 | 763,139 | 629,749 |
| Operating income | $ 133,983 | $ 128,630 | $ 131,212 | $ 154,170 | $ 102,261 |
| Net income | $ 37,156 | $ 38,311 | $ 39,310 | $ 47,537 | $ 16,469 |
| Total assets at year end | $2,369,612 | $2,232,337 | $1,923,442 | $1,830,694 | $1,769,059 |
| Capitalization at year end: | | | | | |
| Common equity | $ 561,200 | $ 533,467 | $ 505,425 | $ 476,400 | $ 385,979 |
| Trust originated preferred securities | 60,000 | 60,000 | 60,000 | 60,000 | 60,000 |
| Long-term debt | 796,351 | 896,417 | 859,291 | 812,906 | 778,693 |
| | $1,417,551 | $1,489,884 | $1,424,716 | $1,349,306 | $1,224,672 |
| Common stock data: | | | | | |
| Return on average common equity | 6.8% | 7.4% | 8.0% | 11.0% | 4.3% |
| Earnings per share | $ 1.16 | $ 1.22 | $ 1.28 | $ 1.66 | $ 0.61 |
| Diluted earnings per share | $ 1.15 | $ 1.21 | $ 1.27 | $ 1.65 | $ 0.61 |
| Dividends paid per share | $ 0.82 | $ 0.82 | $ 0.82 | $ 0.82 | $ 0.82 |
| Payout ratio | 71% | 67% | 64% | 49% | N/A |
| Book value per share at year end | $ 17.27 | $ 16.82 | $ 16.31 | $ 15.67 | $ 14.09 |
| Market value per share at year end | $ 22.35 | $ 21.88 | $ 23.00 | $ 26.63 | $ 18.69 |
| Market value per share to book value per share | 129% | 130% | 141% | 170% | 133% |
| Common shares outstanding at year end (000) | 32,493 | 31,710 | 30,985 | 30,410 | 27,387 |
| Number of common shareholders at year end | 23,243 | 24,092 | 22,989 | 24,489 | 25,833 |
| Ratio of earnings to fixed charges | 1.59 | 1.60 | 1.78 | 2.08 | 1.28 |

NATURAL GAS OPERATIONS

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 | 1998 | 1997 |
|---|---|---|---|---|---|
| (Thousands of dollars) | | | | | |
| Sales | $1,149,918 | $ 816,358 | $ 740,900 | $ 753,338 | $ 569,542 |
| Transportation | 43,184 | 54,353 | 50,255 | 46,259 | 45,123 |
| Operating revenue | 1,193,102 | 870,711 | 791,155 | 799,597 | 614,665 |
| Net cost of gas sold | 677,547 | 394,711 | 330,031 | 329,849 | 209,338 |
| Operating margin | 515,555 | 476,000 | 461,124 | 469,748 | 405,327 |
| Expenses: | | | | | |
| Operations and maintenance | 253,026 | 231,175 | 221,258 | 209,172 | 201,159 |
| Depreciation and amortization | 104,498 | 94,689 | 88,254 | 80,231 | 74,528 |
| Taxes other than income taxes | 32,780 | 29,819 | 27,610 | 31,646 | 29,393 |
| Operating income | $ 125,251 | $ 120,317 | $ 124,002 | $ 148,699 | $ 100,247 |
| Contribution to consolidated net income | $ 32,626 | $ 33,908 | $ 35,473 | $ 44,830 | $ 15,825 |
| Total assets at year end | $2,289,111 | $2,154,641 | $1,855,114 | $1,772,418 | $1,717,025 |
| Net gas plant at year end | $1,825,571 | $1,686,082 | $1,581,102 | $1,459,362 | $1,360,294 |
| Construction expenditures and property additions | $ 248,352 | $ 205,161 | $ 207,773 | $ 179,361 | $ 164,528 |
| Cash flow, net: | | | | | |
| From operating activities | $ 103,848 | $ 109,872 | $ 165,220 | $ 189,465 | $ 45,923 |
| From investing activities | (246,462) | (203,325) | (207,024) | (176,731) | (170,455) |
| From financing activities | 154,727 | 95,481 | 40,674 | (12,632) | 132,349 |
| Net change in cash | $ 12,113 | $ 2,028 | $ (1,130) | $ 102 | $ 7,817 |
| Total throughput (thousands of therms) | | | | | |
| Sales | 1,261,263 | 1,107,674 | 1,037,409 | 1,103,264 | 914,732 |
| Transportation | 1,268,203 | 1,482,700 | 1,186,859 | 1,001,372 | 1,030,857 |
| Total throughput | 2,529,466 | 2,590,374 | 2,224,268 | 2,104,636 | 1,945,589 |
| Weighted average cost of gas purchased ($/therm) | $ 0.55 | $ 0.42 | $ 0.28 | $ 0.27 | $ 0.35 |
| Customers at year end | 1,397,000 | 1,337,000 | 1,274,000 | 1,209,000 | 1,151,000 |
| Employees at year end | 2,507 | 2,491 | 2,482 | 2,429 | 2,447 |
| Degree days - actual | 1,963 | 1,938 | 1,928 | 2,321 | 1,976 |
| Degree days - ten-year average | 1,970 | 1,991 | 2,031 | 2,043 | 2,022 |

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

The following discussion of Southwest Gas Corporation and subsidiaries (the Company) includes information related to regulated natural gas transmission and distribution activities and non-regulated activities.

The Company is comprised of two business segments: natural gas operations (Southwest or the natural gas operations segment) and construction services. Southwest is engaged in the business of purchasing, transporting, and distributing natural gas in portions of Arizona, Nevada and California. Southwest is the largest distributor in Arizona, selling and transporting natural gas in most of central and southern Arizona, including the Phoenix and Tucson metropolitan areas. Southwest is also the largest distributor and transporter of natural gas in Nevada, serving the Las Vegas metropolitan area and northern Nevada. In addition, Southwest distributes and transports natural gas in portions of California, including the Lake Tahoe area and the high desert and mountain areas in San Bernardino County.

As of December 31, 2001 Southwest had 1,397,000 residential, commercial, industrial, and other customers, of which 785,000 customers were located in Arizona, 485,000 in Nevada, and 127,000 in California. Residential and commercial customers represented over 99 percent of the total customer base. During 2001, Southwest added 60,000 customers, a four percent increase, of which 31,000 customers were added in Arizona, 26,000 in Nevada, and 3,000 in California. Customer growth over the past three years averaged five percent annually. These additions are largely attributed to population growth in the service areas. Based on current commitments from builders, customer growth is expected to approximate four percent in 2002. During 2001, 58 percent of operating margin was earned in Arizona, 34 percent in Nevada, and 8 percent in California. During this same period, Southwest earned 82 percent of operating margin from residential and small commercial customers, 8 percent from other sales customers, and 10 percent from transportation customers. In 2000, Southwest earned 84 percent of operating margin from residential and small commercial customers, 3 percent from other sales customers and 13 percent from transportation customers. The difference between years was primarily due to a number of large commercial and industrial customers moving from transportation service to sales service.

Northern Pipeline Construction Co. (Northern or the construction services segment), a wholly owned subsidiary, is a full-service underground piping contractor which provides utility companies with trenching and installation, replacement, and maintenance services for energy distribution systems.

### CAPITAL RESOURCES AND LIQUIDITY

The capital requirements and resources of the Company generally are determined independently for the natural gas operations and construction services segments. Each business activity is generally responsible for securing its own financing sources. The capital requirements and resources of the construction services segment are not material to the overall capital requirements and resources of the Company.

Southwest continues to experience significant customer growth. Financing this growth has required large amounts of capital to pay for new transmission and distribution plant, to keep up with consumer demand. During the three-year period ended December 31, 2001, total gas plant increased from $2 billion to $2.6 billion, or at an annual rate of eight percent. Customer growth was the primary reason for the plant increase as Southwest added 189,000 net new customers during the three-year period. Southwest expects to add approximately 60,000 customers in 2002.

During 2001, capital expenditures for the natural gas operations segment were $248 million. Approximately 74 percent of these current-period expenditures represented new construction and the balance represented costs associated with routine replacement of existing transmission, distribution, and general plant. Cash flows from operating activities of Southwest (net of dividends) provided $78 million of the required capital resources pertaining to these construction expenditures. The remainder was provided from external financing activities. Normally, internally generated funds provide a larger proportionate share of capital resources required for construction purposes. However, such cash flows were unfavorably impacted by unusually high working capital requirements resulting from gas costs that exceeded the amounts recovered from customers during much of 2001. This situation is now reversing as recovery rates have been adjusted and natural gas prices have declined.

In February 2001, the Company issued $200 million in Notes, due 2011, bearing interest at 8.375%. The net proceeds from the sale of the Notes were used to finance the construction, completion, extension and improvement of the pipeline systems and facilities located in and around the communities served by Southwest. Those capital expenditures were originally funded, in part, with short-term debt, which was repaid with the net proceeds of the Notes.

In March 2002, the Job Creation and Worker Assistance Act of 2002 (Act) was signed into law. This Act provides a three-year, 30 percent "bonus" tax depreciation deduction for businesses. Southwest estimates the bonus depreciation deduction will reduce federal income taxes paid by approximately $40 million to $50 million over the next three years (2002-2004).

Southwest estimates construction expenditures during the three-year period ending December 31, 2004 will be approximately $675 million. Of this amount, $225 million are expected to be incurred in 2002. During the three-year period, cash flow from operating activities (net of dividends) is estimated to fund approximately 80 percent of the gas operations total construction expenditures, including the impacts of the Act. The remaining cash requirements are expected to be provided by external financing sources. The timing, types, and amounts of these additional external financings will be dependent on a number of factors, including conditions in the capital markets, timing and amounts of rate relief, growth levels in Southwest service areas and earnings. These external financings may include the issuance of both debt and equity securities, bank and other short-term borrowings, and other forms of financing. Southwest has a total of $400 million in securities registered with the Securities and Exchange Commission (SEC) which are available for future financing needs.

Current maturities of long-term debt were $308 million at December 31, 2001. In June 2002, the $350 million revolving credit facility, of which $200 million is designated as long-term debt, and the $100 million Series F debentures will mature. The Company intends to refinance the long-term portion of the revolving credit agreement and the Series F debentures on a long-term basis but no firm agreements are in place at this time. The timing, types, and amounts of these external financings will be dependent on conditions in the capital markets. Once the debt has been refinanced, or long-term agreements have been entered into, the Current maturities of long-term debt line item should

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

return to normal levels. The Company also intends to maintain short-term borrowing capacity at a level sufficient to cover working capital needs.

All Company debt is recorded on its balance sheets. The Company has long-term operating leases, which are described in Note 2 "Utility Plant" of the Notes to Consolidated Financial Statements. No debt instruments have credit triggers or other clauses that result in default if Company bond ratings are lowered by rating agencies. Certain Company debt instruments contain customary leverage, net worth and other covenants, and securities ratings covenants that, if set in motion, would increase financing costs. To date, the Company has not incurred any increased financing costs as a result of these covenants.

The Company does not currently utilize stand-alone derivative instruments for speculative purposes or for hedging and does not have foreign currency exposure. Southwest has fixed-price gas purchase contracts, which are considered normal purchases occurring in the ordinary course of business. None of the Company's long-term financial instruments or other contracts are derivatives, or contain embedded derivatives.

Liquidity refers to the ability of an enterprise to generate adequate amounts of cash to meet its cash requirements. Several general factors that could significantly affect capital resources and liquidity in future years include inflation, growth in the economy, changes in income tax laws, changes in the ratemaking policies of regulatory commissions, interest rates, the level of natural gas prices and the level of Company earnings. The most significant negative factor affecting liquidity in 2001 was the high natural gas prices.

The rate schedules in all of the service territories of Southwest contain purchased gas adjustment (PGA) clauses, which permit adjustments to rates as the cost of purchased gas changes. The PGA mechanism allows Southwest to change the gas cost component of the rates charged to its customers to reflect increases or decreases in the price expected to be paid to its suppliers and companies providing interstate pipeline transportation service. On an interim basis, Southwest generally defers over or under collections of gas costs to PGA balancing accounts. In addition, Southwest uses this mechanism to either refund amounts over-collected or recoup amounts under-collected as compared to the price paid for natural gas during the period since the last PGA rate change went into effect. During the second half of 2000 and the first half of 2001, Southwest experienced high gas purchase prices relative to amounts recovered in rates for gas purchases. Natural gas prices have declined significantly in recent months. At December 31, 2001, the combined balances in PGA accounts were $84 million. At their peak in February 2001, the combined balances were $161 million. The balances should continue to trend downward since recovery rates have been adjusted, assuming prices paid for gas purchases remain similar to levels embedded in sales rates. Southwest utilizes short-term borrowings to temporarily finance PGA balances. Southwest currently has short-term borrowing capacity of $150 million, which the Company believes is adequate to meet anticipated needs. Short-term borrowing capacity was $225 million earlier in 2001. A $75 million credit facility expired in November 2001 and was not renewed.

In Arizona, Southwest adjusts rates monthly for changes in purchased gas costs, within pre-established limits. In California, a monthly gas cost adjustment based on forecasted monthly prices is utilized. Monthly adjustments are designed to provide a more timely recovery of gas costs and to send appropriate pricing signals to customers. In Nevada, tariffs provide for annual adjustment dates for changes in purchased gas costs. In addition, Southwest may request to adjust rates more often, if conditions warrant. Filings to change rates in accordance with PGA clauses are subject to audit by state regulatory commission staffs. See RATES AND REGULATORY PROCEEDINGS for details of these filings.

PGA changes affect cash flows but have no direct impact on profit margin. In addition, since Southwest is permitted to accrue interest on PGA balances, the cost of incremental, PGA-related short-term borrowings will be offset, and there should be no material negative impact to earnings. However, gas cost deferrals and recoveries can impact comparisons between periods of individual income statement captions. These include Gas operating revenues, Net cost of gas sold, Net interest deductions and Other income (deductions).

Other effects of the reduction in gas costs and adjustments to recovery rates are visible in Company balance sheets. The Prepaids and other current assets line item decreased $46 million during 2001 primarily due to the deferral and collection of gas costs through the PGA accounts. Significantly lower gas costs during the latter half of 2001 contributed to the $86 million decrease in the Accounts payable line item.

The Company has a common stock dividend policy which states that common stock dividends will be paid at a prudent level that is within the normal dividend payout range for its respective businesses, and that the dividend will be established at a level considered sustainable in order to minimize business risk and maintain a strong capital structure throughout all economic cycles. The quarterly common stock dividend was 20.5 cents per share throughout 2001. The current dividend of 20.5 cents per share has been paid quarterly since September 1994.

Securities ratings issued by nationally recognized ratings agencies provide a method for determining the credit worthiness of an issuer. Company debt ratings are important because long-term debt constitutes a significant portion of total capitalization. These debt ratings are a factor considered by lenders when determining the cost of debt for the Company (i.e., the better the rating, the lower the cost to borrow funds).

Since January 1997, Moody's Investors Service, Inc. (Moody's) has rated Company unsecured long-term debt at Baa2. Moody's debt ratings range from Aaa (best quality) to C (lowest quality). Moody's applies a Baa2 rating to obligations which are considered medium grade obligations (i.e., they are neither highly protected nor poorly secured).

The Company's unsecured long-term debt rating from Fitch, Inc. (Fitch) is BBB. Fitch debt ratings range from AAA (highest credit quality) to D (defaulted debt obligation). The Fitch rating of BBB indicates a credit quality that is considered prudent for investment.

The Company's unsecured long-term debt rating from Standard and Poor's Ratings Services (S&P) is BBB-. S&P debt ratings range from AAA (highest rating possible) to D (obligation is in default). The S&P rating of BBB- indicates the debt is regarded as having an adequate capacity to pay interest and repay principal.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

A securities rating is not a recommendation to buy, sell, or hold a security and is subject to change or withdrawal at any time by the rating agency. The three securities ratings discussed above are essentially equivalent.

Results of operations are impacted by inflation. Natural gas, labor, and construction costs are the categories most significantly impacted by inflation. Changes to Southwest cost of gas are generally recovered through PGA mechanisms and do not significantly impact net earnings. Labor is a component of the cost of service, and construction costs are the primary component of rate base. In order to recover increased costs, and earn a fair return on rate base, general rate cases are filed by Southwest, when deemed necessary, for review and approval by regulatory authorities. Regulatory lag, that is, the time between the date increased costs are incurred and the time such increases are recovered through the ratemaking process, can impact earnings. See RATES AND REGULATORY PROCEEDINGS for discussion of recent rate case proceedings.

JANUARY 2002 SALE OF UNDEVELOPED PROPERTY

In January 2002, the Company sold all of its interests in undeveloped property located in northern Arizona. The property was originally acquired as a potential site for underground natural gas storage during the gas supply shortages of the 1970s, but was never developed. The sale will result in a one-time pre-tax gain of $8.9 million, which will be recognized in the first quarter of 2002.

CONSOLIDATED RESULTS OF OPERATIONS

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 |
|---|---|---|---|
| (Thousands of dollars) | | | |
| CONTRIBUTION TO NET INCOME | | | |
| Natural gas operations | $32,626 | $33,908 | $35,473 |
| Construction services | 4,530 | 4,403 | 3,837 |
| Net income | $37,156 | $38,311 | $39,310 |
| EARNINGS PER SHARE | | | |
| Gas operations | $ 1.02 | $ 1.08 | $ 1.16 |
| Construction services | 0.14 | 0.14 | 0.12 |
| Consolidated | $ 1.16 | $ 1.22 | $ 1.28 |

See separate discussions at RESULTS OF NATURAL GAS OPERATIONS and RESULTS OF CONSTRUCTION SERVICES. Average shares outstanding increased by 751,000 shares between 2001 and 2000, and 681,000 shares between 2000 and 1999, primarily resulting from continuing issuances under the Dividend Reinvestment and Stock Purchase Plan.

RESULTS OF NATURAL GAS OPERATIONS

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 |
|---|---|---|---|
| (Thousands of dollars) | | | |
| Gas operating revenues | $1,193,102 | $870,711 | $791,155 |
| Net cost of gas sold | 677,547 | 394,711 | 330,031 |
| Operating margin | 515,555 | 476,000 | 461,124 |
| Operations and maintenance expense | 253,026 | 231,175 | 221,258 |
| Depreciation and amortization | 104,498 | 94,689 | 88,254 |
| Taxes other than income taxes | 32,780 | 29,819 | 27,610 |
| Operating income | 125,251 | 120,317 | 124,002 |
| Other income (expense) | 7,694 | (1,765) | (2,925) |
| Income before interest and income taxes | 132,945 | 118,552 | 121,077 |
| Net interest deductions | 78,746 | 68,892 | 61,597 |
| Preferred securities distributions | 5,475 | 5,475 | 5,475 |
| Income tax expense | 16,098 | 10,277 | 18,532 |
| Contribution to consolidated net income | $ 32,626 | $ 33,908 | $ 35,473 |

2001 VS. 2000

The gas segment contribution to consolidated net income for 2001 decreased $1.3 million from 2000. Growth in operating margin and improvement in other income (expense) was more than offset by higher operating and financing costs.

Operating margin increased $39.6 million, or eight percent, in 2001 as a result of customer growth, rate relief, and a return to normal weather. Southwest added 60,000 new customers during the last 12 months. This customer growth, coupled with increased margin from electric generation and industrial customers, contributed $30 million in incremental margin. An additional $5.3 million of incremental margin was realized in 2001 from general rate relief. In Arizona, annualized rate relief of $21.6 million was granted effective November 2001. The Company expected the general rate increase in April 2001. This seven-month delay resulted in unrealized operating margin of approximately $15 million. In Nevada, annualized rate relief of $19.4 million was granted effective December 2001. The remainder of the net change in operating margin between periods was due to weather as average temperatures during 2001 were normal versus moderately warmer-than-normal average temperatures during 2000.

Operations and maintenance expense increased $21.9 million, or nine percent, reflecting general increases in labor and maintenance costs, higher uncollectible expenses, and incremental costs associated with servicing additional customers. Management believes the increase in uncollectible expenses is due to high natural gas prices coupled with the downturn of the economy, and is not a trend that should continue beyond 2002.

Depreciation expense and general taxes increased $12.8 million, or ten percent, as a result of construction activities. Average gas plant in service increased $180 million, or eight percent, compared to the prior year. This was attributed to the continued expansion and upgrading of the gas system to accommodate customer growth.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Net interest deductions increased $9.9 million, or 14 percent, as the Company financed both the new construction necessary to keep up with customer growth, and unrecovered purchased gas costs.

Other income (expense) improved $9.5 million in 2001, primarily as a result of increased interest income of $5.9 million on PGA balances and a $3 million pretax gain on the sale of certain assets.

During 2001, Southwest recognized $2.5 million of income tax benefits associated with the resolution of state income tax issues. During 2000, Southwest recognized $6 million of income tax benefits associated with the favorable resolution of certain federal income tax issues and the statutory closure of open federal tax years. The 2001 effective income tax rate for the gas operations segment was 33 percent.

2000 VS. 1999

The gas segment contribution to consolidated net income for 2000 decreased $1.6 million from 1999. Growth in operating margin was more than offset by higher operating and financing costs.

Operating margin increased $14.9 million, or three percent, in 2000. The increase was primarily due to customer growth as the Company added 63,000, or five percent, new customers during 2000. Differences in heating demand between periods partially offset the impact of customer growth, as both periods were moderately warmer than normal.

Operations and maintenance expense increased $9.9 million, or four percent, as a result of continued expansion and upgrading of the gas system to accommodate customer growth.

Depreciation expense and general taxes increased $8.6 million, or seven percent, as a result of construction activities. Average gas plant in service increased $173 million, or eight percent, compared to the prior year. This was attributed to the continued expansion and upgrading of the gas system to accommodate customer growth.

Net interest deductions increased $7.3 million, or 12 percent, over 1999 due to the financing of growth-related construction expenditures and higher interest rates on variable-rate debt instruments.

During 2000, Southwest recognized $6 million of income tax benefits associated with the favorable resolution of certain federal income tax issues and the statutory closure of open federal tax years. As a result, the effective income tax rate for the gas operations segment was 23 percent.

RATES AND REGULATORY PROCEEDINGS

Arizona General Rate Case. In May 2000, Southwest filed a general rate application with the Arizona Corporation Commission (ACC) seeking approval to increase revenues by $37.1 million, or nine percent, annually for its Arizona rate jurisdiction. Southwest sought rate relief for increased operating costs, changes in financing costs, declining average residential usage, and improvements and additions to the distribution system. In October 2001, the ACC authorized Southwest to increase rates by $21.6 million, or five percent, annually, effective November 2001. The timing of the increase was important to Southwest because it provided the benefit of having new rates in place at the beginning of the 2001-2002 heating season. The ACC order also approved changes in rate design that should improve revenue stability in Arizona. For example, the residential basic service charge was increased by $1.00 per month. In addition, the base gas cost rate was increased, allowing Southwest to recover the deferred PGA balance more rapidly.

Nevada General Rate Cases. In July 2001, Southwest filed general rate applications with the Public Utilities Commission of Nevada (PUCN) seeking approval to increase annualized revenues by $21.7 million in its southern Nevada rate jurisdiction and $7.7 million in its northern Nevada rate jurisdiction. In November 2001, Southwest received approval from the PUCN to increase rates by $13.5 million, or five percent, annually in southern Nevada and $5.9 million, or five percent, annually in northern Nevada effective December 2001. In January 2002, the PUCN settled several open issues in the case regarding rate design. Changes included increasing the residential basic service charge by $2.00 per month in both jurisdictions, which should improve revenue stability in Nevada. The changes were effective February 2002 and did not impact the amount of rate relief granted.

California General Rate Cases. In February 2002, Southwest filed general rate applications with the California Public Utilities Commission (CPUC) for its northern and southern California jurisdictions. The application seeks annual increases over a five-year period beginning January 2003, which cumulatively amount to $6.3 million in northern California and $17.2 million in southern California. For 2003, an annualized $2.7 million, or 13 percent, revenue increase was requested for the northern jurisdiction and an annualized $6.7 million, or eight percent, revenue increase was requested for the southern jurisdiction. Additional smaller annual revenue increases are proposed in the subsequent years of the application through 2007. Hearings are expected to begin in the third quarter of 2002. The last general rate increases received in California were January 1998 in northern California and January 1995 in southern California.

FERC Jurisdiction. In July 1996, Paiute Pipeline Company, a wholly owned subsidiary of the Company, filed its most recent general rate case with the Federal Energy Regulatory Commission (FERC). The FERC authorized a general rate increase effective January 1997. Additional rate relief is not yet necessary and, therefore, no general rate case filing is planned during 2002.

PGA FILINGS

Arizona PGA Filings ($64.9 million unrecovered PGA balance at December 31, 2001). In Arizona, Southwest adjusts rates monthly for changes in purchased gas costs, within pre-established limits. In January 2002, Southwest filed an advice letter with the ACC to eliminate a temporary rate adjustment surcharge, which was otherwise set to expire at the end of the second quarter of 2002. This action was taken in recognition of moderating gas costs and projections of PGA balancing account activity. The filing was approved effective February 2002, and will reduce revenues by $31.9 million annually with no reduction to margin.

Nevada PGA Filings ($10.1 million unrecovered PGA balance at December 31, 2001). In December 2001, Southwest submitted an out-of-cycle PGA filing to the PUCN for a $29.2 million decrease for southern Nevada customers. In January 2002, an additional decrease of $13.9 million was requested. The total of the two filings, $43.1 million, was

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

agreed to in a settlement among all parties and approved by the PUCN to become effective in February 2002. The filings were made in advance of the scheduled annual date to allow customers to receive the benefit of decreases experienced in natural gas costs. PGA changes impact cash flows but have no direct impact on profit margin.

In October 2001, Southwest submitted an out-of-cycle PGA filing to the PUCN to reduce rates in both the southern and northern Nevada rate jurisdictions. In November 2001, rate decreases of $48.6 million, or 17 percent, for southern Nevada and $15 million, or 14 percent, for northern Nevada were approved by the PUCN effective December 2001.

In June 2001, the PUCN approved an agreement allowing Southwest to increase rates by $74.6 million annually to recover higher gas costs. Effective July 2001, rates increased $47.2 million, or 23 percent, in southern Nevada and $27.4 million, or 36 percent in northern Nevada. The agreement followed a thorough review by the Bureau of Consumer Protection (BCP) and PUCN Staff of the gas purchasing practices of Southwest. The out-of-cycle PGA filing was submitted by Southwest in January 2001 to recover gas costs incurred through December 2000.

In October 2000, Southwest submitted an out-of-cycle PGA filing to the PUCN to recover gas costs incurred through September 2000. A settlement related to this filing resulted in a gas cost rate increase of $38.5 million, or 24 percent, in southern Nevada and $16.8 million, or 30 percent, in northern Nevada, effective January 2001. In a related order issued May 2001, the PUCN directed that Southwest meet with PUCN staff and the BCP in the third quarter of 2001 to establish guidelines for Southwest to follow in constructing its Nevada gas supply portfolio for coming years. The guidelines may include a requirement to utilize call options to mitigate future price risks. Meetings were held but no agreement was reached. During the third quarter of 2001, the three parties filed separate guideline proposals with the PUCN. The PUCN has not yet acted on this matter.

Effective December 2000, the PUCN approved an annual PGA filing submitted in June 2000 granting annual increases of $13.9 million, or nine percent, in southern Nevada and $6 million, or 11 percent, in northern Nevada.

California PGA Filings ($8.5 million unrecovered PGA balance at December 31, 2001). Effective December 2000, the CPUC authorized Southwest to change the cost of gas included in sales rates each month to reflect the projected cost of gas for the current month. The treatment of monthly over/under-recoveries of gas costs varies by magnitude. Small amounts may be included in the following month's estimated cost of gas for immediate recovery/refund. Large amounts may be deferred to the PGA account to be amortized over longer periods to avoid excessive fluctuation in prices. This mechanism allows the most timely recovery of gas costs within the three-state operating area.

California Order Instituting Investigation (OII). In July 2001, the CPUC ordered an investigation into the reasonableness of Southwest natural gas procurement practices and costs from June 1999 through May 2001, and related measures taken to minimize gas costs beyond May 2001. During the third quarter of 2001, Southwest filed a detailed report and testimony with the CPUC on these matters for both its northern and southern California service territories. The OII resulted from complaints by southern California customers about the size of monthly PGA rate increases that were necessary due to the unusually high cost of natural gas during the winter of 2000-2001. In regards to the southern California jurisdiction, the Office of Ratepayer Advocate and the County of San Bernardino recommended disallowances of $7.3 million and $11.7 million, respectively. No issues were raised related to the northern California rate jurisdiction. The proposed disallowances were based solely on decisions by Southwest not to purchase gas for storage during the winter of 2000-2001. Hearings were held in January 2002 with a final decision anticipated in the second quarter of 2002. Southwest defended its decisions related to storage, based on testimony which demonstrated that injecting additional volumes of natural gas into storage during the 2000 injection season (April through September) could not be economically justified based on market conditions and price forecasts that existed at the time decisions were made. Management believes it has adequately defended the prudency of its gas procurement practices and, as a result, believes there is no legal basis for a disallowance.

RESULTS OF CONSTRUCTION SERVICES

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 |
| --- | --- | --- | --- |
| | (Thousands of dollars) | | |
| Construction revenues | $203,586 | $163,376 | $145,711 |
| Cost of construction | 189,429 | 150,678 | 134,790 |
| Gross profit | 14,157 | 12,698 | 10,921 |
| General and administrative expenses | 5,026 | 3,986 | 3,312 |
| Income from operations | 9,131 | 8,712 | 7,609 |
| Other income (expense) | 871 | 821 | 946 |
| Income before interest and income taxes | 10,002 | 9,533 | 8,555 |
| Interest expense | 1,985 | 1,779 | 1,605 |
| Income tax expense | 3,487 | 3,351 | 3,113 |
| Contribution to consolidated net income | $ 4,530 | $ 4,403 | $ 3,837 |

2001 VS. 2000

The 2001 contribution to consolidated net income from construction services increased $127,000 from the prior year. The increase was principally due to higher revenues that resulted from obtaining additional work. Revenues increased 25 percent, while the gross profit margin percentage decreased slightly. Gross profit increased $1.5 million.

General and administrative expenses, as a percent of revenue, remained relatively constant as did interest expense.

2000 VS. 1999

The 2000 contribution to consolidated net income from construction services increased $566,000 from the prior year. The increase was principally due to additional revenues that resulted from obtaining several new contracts and favorable winter weather conditions. Revenues increased 12 percent, while the gross profit margin percentage remained relatively constant. Gross profit increased $1.8 million.

General and administrative expenses, as a percent of revenue, remained relatively constant as did interest expense.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 is effective for fiscal years beginning after December 15, 2001. In all cases, SFAS No. 142 must be adopted as of the beginning of a fiscal year. SFAS No. 142 requires that the amortization of goodwill be eliminated and that existing goodwill be evaluated for impairment. Goodwill will be tested for impairment at least annually using a two-step process that begins with an estimation of the fair value of a reporting unit. The first step is a screen for potential impairment, and the second step measures the amount of impairment, if any. However, if certain criteria are met, the requirement to test goodwill for impairment annually can be satisfied without a remeasurement of the fair value of a reporting unit. The Company has included $7.7 million of goodwill resulting from the purchase of Northern Pipeline Construction Co. on its consolidated balance sheet at December 31, 2001. The annual amortization expense associated with goodwill is $400,000. Management does not anticipate any significant impact to the financial position or results of operations of the Company as a result of SFAS No. 142.

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations." SFAS No. 143 requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred. The asset retirement obligations included within the scope of SFAS No. 143 are those that are unavoidable as a result of the acquisition, construction, development, or normal operation of long-lived assets. The standard requires that a legal obligation associated with the retirement of tangible long-lived assets be recognized as a liability when incurred. When a liability for an asset retirement obligation is initially recorded, the entity capitalizes a cost by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. Entities are also required to recognize period-to-period changes for the liability related to asset retirement obligations resulting from the passage of time and/or revisions to either the timing or the amount of the original estimate of undiscounted cash flows. Upon settlement of the liability, an entity either settles the obligation for its recorded amount or incurs a gain or loss. Upon initial application of SFAS No. 143, entities are required to recognize the following items in the statement of financial position: a liability for any existing asset retirement obligations adjusted for cumulative accretion to the date of adoption of SFAS No. 143, an asset retirement cost capitalized as an increase to the carrying amount of the associated long-lived asset, and accumulated depreciation for the capitalized cost. SFAS No. 143 is effective for financial statements issued for fiscal years beginning after June 15, 2002, with early adoption encouraged. Management has not yet quantified the effects of the new standard on the financial position or results of operations of the Company.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets and supersedes FASB Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." SFAS No. 144 also supercedes the accounting and reporting provisions of Accounting Principles Board (APB) Opinion No. 30, "Reporting the Results of Operations-Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions," for the disposal of a segment of a business (as previously defined in that Opinion). Because SFAS No. 121 did not address the accounting for a segment of a business accounted for as a discontinued operation under APB Opinion No. 30, two accounting models existed for long-lived assets to be disposed of. The FASB decided to establish a single accounting model, based on the framework established in SFAS No. 121, for long-lived assets to be disposed of by sale. The FASB also decided to resolve other implementation issues related to SFAS No. 121. SFAS No. 144 is effective for financial statements issued for fiscal years beginning after December 15, 2001, with early adoption encouraged. Management does not anticipate any significant impact to the financial position or results of operations of the Company as a result of SFAS No. 144.

MERGER LITIGATION

Litigation is pending in Arizona related to the now terminated acquisition of the Company by ONEOK Inc. (ONEOK). For additional information, see ITEM 3. LEGAL PROCEEDINGS, in the 2001 Form 10-K filed by the Company with the SEC.

In January 2002, United States District Court Judge Roslyn O. Silver in Phoenix, Arizona, issued two orders further addressing the allowable claims and damage issues in litigation presently pending among Southern Union Company (Southern Union), ONEOK and the Company.

The first order confirms that Southern Union claims against the Company and ONEOK are now limited to claims for Southern Union's out-of-pocket expenses, estimated at approximately $1 million (according to Court filings), and any punitive damages that it can prove. The second order limits Company claims against ONEOK to out-of-pocket expenses and any punitive damages that it can prove. Likewise, the single remaining ONEOK claim against the Company is limited to out-of-pocket expenses and any punitive damages that it can prove. The second order also dismisses the claims of the Company and ONEOK against Southern Union. The Company believes that it will prevail on the remaining Southern Union and ONEOK claims and that its potential exposure on these claims, including punitive damages, will not have a material impact on its financial condition.

CRITICAL ACCOUNTING POLICIES

A critical accounting policy is one which is very important to the portrayal of the financial condition and results of a company, and requires the most difficult, subjective or complex judgments of management. The need to make estimates about the effect of items that are uncertain is what makes these judgments difficult, subjective and/or complex. Management makes subjective judgments about the accounting and regulatory treatment of many items. The following are examples of accounting policies that are critical to the financial statements of the Company. For more information regarding the significant accounting policies of the Company, see Note 1 of the Notes to Consolidated Financial Statements.

- - Natural gas operations are subject to the regulation of the Arizona Corporation Commission, the Public Utilities Commission of Nevada, the California Public Utilities Commission, and the Federal Energy Regulatory Commission. The accounting policies of the Company conform to generally accepted accounting principles applicable to rate-regulated enterprises and reflect the effects of the ratemaking process. As such, the Company is allowed to defer as regulatory assets, costs that otherwise would have been expensed if it is probable future recovery from customers will occur. If rate recovery is no longer probable, due to competition or the actions of regulators, the

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Company would be required to write off the related regulatory asset. Refer to Note 4 of the Notes to Consolidated Financial Statements for a list of regulatory assets.

- - The income tax calculations of the Company require estimates due to regulatory complications, the multiple states in which the Company operates, and future tax rate changes. The Company uses the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. A change in the regulatory treatment, or significant changes in tax-related estimates or assumptions, could have a material impact on the financial position and results of operations of the Company.

- - Depreciation is computed at composite rates considered sufficient to amortize costs over the estimated remaining lives of assets, and includes adjustments for the cost of removal, and salvage value. Depreciation studies are performed periodically and prospective changes in rates are estimated to make up for past differences. These studies are reviewed and approved by the appropriate regulatory agency. Changes in estimates of depreciable lives or changes in depreciation rates mandated by regulations could effect the results of operations of the Company in periods subsequent to the change.

Management believes that regulation and the effects of regulatory accounting have the most significant impact on the financial statements. When Southwest files rate cases, capital assets, costs and gas purchasing practices are subject to review, and disallowances could occur. Regulatory disallowances in the past have not been frequent but have on occasion been significant to the operating results of the Company.

FORWARD-LOOKING STATEMENTS
This annual report contains statements which constitute "forward-looking statements" within the meaning of the Securities Litigation Reform Act of 1995 (Reform Act). All such forward-looking statements are intended to be subject to the safe harbor protection provided by the Reform Act. A number of important factors affecting the business and financial results of the Company could cause actual results to differ materially from those stated in the forward-looking statements. These factors include, but are not limited to, the impact of weather variations on customer usage, customer growth rates, natural gas prices, the effects of regulation/deregulation, the timing and amount of rate relief, changes in gas procurement practices, changes in capital requirements and funding, resolution of pending litigation, acquisitions, and competition.

## COMMON STOCK PRICE AND DIVIDEND INFORMATION

| | 2001 | | 2000 | | DIVIDENDS PAID | |
|---|---|---|---|---|---|---|
| | HIGH | LOW | HIGH | LOW | 2001 | 2000 |
| First Quarter | $22.60 | $19.81 | $23.00 | $17.06 | $0.205 | $0.205 |
| Second Quarter | 24.29 | 20.18 | 20.19 | 17.50 | 0.205 | 0.205 |
| Third Quarter | 24.38 | 18.85 | 21.25 | 16.88 | 0.205 | 0.205 |
| Fourth Quarter | 23.00 | 20.50 | 22.50 | 19.31 | 0.205 | 0.205 |
| | | | | | $0.820 | $0.820 |

The principal markets on which the common stock of the Company is traded are the New York Stock Exchange and the Pacific Stock Exchange. At March 11, 2002, there were 23,003 holders of record of common stock and the market price of the common stock was $23.73.

## CONSOLIDATED BALANCE SHEETS

| DECEMBER 31 | 2001 | 2000 |
|---|---|---|
| (Thousands of dollars, except par value) | | |
| **ASSETS** | | |
| Utility plant: | | |
| Gas plant | $2,561,937 | $2,369,697 |
| Less: accumulated depreciation | (789,751) | (728,466) |
| Acquisition adjustments, net | 2,894 | 3,124 |
| Construction work in progress | 50,491 | 41,727 |
| Net utility plant (Note 2) | 1,825,571 | 1,686,082 |
| Other property and investments | 92,511 | 91,685 |
| Current assets: | | |
| Cash and cash equivalents | 32,486 | 19,955 |
| Accounts receivable, net of allowances (Note 3) | 155,382 | 135,609 |
| Accrued utility revenue | 63,773 | 57,873 |
| Taxes receivable, net | 26,697 | 13,394 |
| Deferred purchased gas costs (Note 4) | 83,501 | 92,064 |
| Prepaids and other current assets (Note 4) | 38,310 | 84,334 |
| Total current assets | 400,149 | 403,229 |
| Deferred charges and other assets (Note 4) | 51,381 | 51,341 |
| Total assets | $2,369,612 | $2,232,337 |

The accompanying notes are an integral part of these statements.

DECEMBER 31 2001 2000 - -------------------------------------------------------------------- ------------------------- (Thousands of dollars, except par value) CAPITALIZATION AND LIABILITIES Capitalization: Common stock, $1 par (authorized - 45,000,000 shares; issued and outstanding - 32,492,832 and 31,710,004 shares) $ 34,123 $ 33,340 Additional paid-in capital 470,410 454,132 Retained earnings 56,667 45,995 - ---------------------------------- ------------------------------------------------------------ Total common equity 561,200 533,467 Company-obligated mandatorily redeemable preferred securities of the Company's subsidiary, Southwest Gas Capital I, holding solely $61.8 million principal amount of 9.125% subordinated notes of the Company due 2025 (Note 5) 60,000 60,000 Long-term debt, less current maturities (Note 6) 796,351 896,417 - -------------------------------------- -------------------------------------------------- Total capitalization 1,417,551 1,489,884 - ------------------------------------------------------------------------------------ ------------- Commitments and contingencies (Note 8) Current liabilities: Current maturities of long-term debt (Note 6) 307,641 8,139 Short-term debt (Note 7) 93,000 131,000 Accounts payable 109,167 194,679 Customer deposits 30,288 29,039 Accrued taxes 32,069 - Accrued interest 20,423 15,702 Deferred income taxes (Note 10) 24,154 48,965 Other current liabilities 36,299 54,006 - --------------------------------------------------------------------- ----------------------------- Total current liabilities 653,041 481,530 - ----------------- --------------------------------------------------------------------------- Deferred income taxes and other credits: Deferred income taxes and investment tax credits (Note 10) 217,804 204,168 Other deferred credits (Note 4) 81,216 56,755 - ------------------------------------ -------------------------------------------------------- Total deferred income taxes and other credits 299,020 260,923 - -------------------------------------------------------------- --------------------------------- Total capitalization and liabilities $2,369,612 $2,232,337

============================================================================================

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENTS OF INCOME

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 |
|---|---|---|---|
| (In thousands, except per share amounts) | | | |
| Operating revenues: | | | |
| Gas operating revenues | $1,193,102 | $ 870,711 | $791,155 |
| Construction revenues | 203,586 | 163,376 | 145,711 |
| Total operating revenues | 1,396,688 | 1,034,087 | 936,866 |
| Operating expenses: | | | |
| Net cost of gas sold | 677,547 | 394,711 | 330,031 |
| Operations and maintenance | 253,026 | 231,175 | 221,258 |
| Depreciation and amortization | 118,448 | 106,640 | 98,525 |
| Taxes other than income taxes | 32,780 | 29,819 | 27,610 |
| Construction expenses | 180,904 | 143,112 | 128,230 |
| Total operating expenses | 1,262,705 | 905,457 | 805,654 |
| Operating income | 133,983 | 128,630 | 131,212 |
| Other income and (expenses): | | | |
| Net interest deductions | (80,731) | (70,671) | (63,202) |
| Preferred securities distributions (Note 5) | (5,475) | (5,475) | (5,475) |
| Other income (deductions) | 8,964 | (545) | (1,580) |
| Total other income and (expenses) | (77,242) | (76,691) | (70,257) |
| Income before income taxes | 56,741 | 51,939 | 60,955 |
| Income tax expense (Note 10) | 19,585 | 13,628 | 21,645 |
| Net income | $ 37,156 | $ 38,311 | $ 39,310 |
| Basic earnings per share (Note 12) | $ 1.16 | $ 1.22 | $ 1.28 |
| Diluted earnings per share (Note 12) | $ 1.15 | $ 1.21 | $ 1.27 |
| Average number of common shares outstanding | 32,122 | 31,371 | 30,690 |
| Average shares outstanding (assuming dilution) | 32,398 | 31,575 | 30,965 |

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 |
|---|---|---|---|
| (Thousands of dollars) | | | |
| CASH FLOW FROM OPERATING ACTIVITIES: | | | |
| Net income | $ 37,156 | $ 38,311 | $ 39,310 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization | 118,448 | 106,640 | 98,525 |
| Deferred income taxes | (11,175) | 80,836 | (19,996) |
| Changes in current assets and liabilities: | | | |
| Accounts receivable, net of allowances | (19,773) | (47,133) | (439) |
| Accrued utility revenue | (5,900) | (1,500) | 500 |
| Deferred purchased gas costs | 8,563 | (83,013) | 48,544 |
| Accounts payable | (85,512) | 130,432 | (48) |
| Accrued taxes | 18,766 | (54,005) | 7,131 |
| Other current assets and liabilities | 34,051 | (44,917) | 2,737 |
| Other | 28,128 | (344) | 2,296 |
| Net cash provided by operating activities | 122,752 | 125,307 | 178,560 |
| CASH FLOW FROM INVESTING ACTIVITIES: | | | |
| Construction expenditures and property additions | (265,580) | (223,240) | (229,503) |
| Other | 4,318 | 3,923 | 3,521 |
| Net cash used in investing activities | (261,262) | (219,317) | (225,982) |
| CASH FLOW FROM FINANCING ACTIVITIES: | | | |
| Issuance of common stock, net | 17,061 | 15,595 | 14,997 |
| Dividends paid | (26,323) | (25,715) | (25,164) |
| Issuance of long-term debt, net | 213,026 | 45,101 | 53,348 |
| Retirement of long-term debt, net | (14,723) | (8,142) | (6,168) |
| Change in short-term debt | (38,000) | 70,000 | 9,000 |
| Net cash provided by financing activities | 151,041 | 96,839 | 46,013 |
| Change in cash and cash equivalents | 12,531 | 2,829 | (1,409) |
| Cash at beginning of period | 19,955 | 17,126 | 18,535 |
| Cash at end of period | $ 32,486 | $ 19,955 | $ 17,126 |
| Supplemental information: | | | |
| Interest paid, net of amounts capitalized | $ 74,032 | $ 67,638 | $ 61,321 |
| Income taxes paid (received), net | $ 13,186 | $ (13,417) | $ 30,090 |

The accompanying notes are an integral part of these statements.

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(In thousands, except per share amounts)

| | COMMON STOCK SHARES | COMMON STOCK AMOUNT | ADDITIONAL PAID-IN CAPITAL | RETAINED EARNINGS | TOTAL |
|---|---|---|---|---|---|
| DECEMBER 31, 1998 | 30,410 | $32,040 | $424,840 | $ 19,520 | $476,400 |
| Common stock issuances | 575 | 575 | 14,422 | | 14,997 |
| Net income | | | | 39,310 | 39,310 |
| Dividends declared Common: $0.82 per share | | | | (25,282) | (25,282) |
| DECEMBER 31, 1999 | 30,985 | 32,615 | 439,262 | 33,548 | 505,425 |
| Common stock issuances | 725 | 725 | 14,870 | | 15,595 |
| Net income | | | | 38,311 | 38,311 |
| Dividends declared Common: $0.82 per share | | | | (25,864) | (25,864) |
| DECEMBER 31, 2000 | 31,710 | 33,340 | 454,132 | 45,995 | 533,467 |
| Common stock issuances | 783 | 783 | 16,278 | | 17,061 |
| Net income | | | | 37,156 | 37,156 |
| Dividends declared Common: $0.82 per share | | | | (26,484) | (26,484) |
| DECEMBER 31, 2001 | 32,493* | $34,123 | $470,410 | $ 56,667 | $561,200 |

* At December 31, 2001, 1.9 million common shares were registered and available for issuance under provisions of the Employee Investment Plan, the Stock Incentive Plan, the Management Incentive Plan, and the Dividend Reinvestment and Stock Purchase Plan.

The accompanying notes are an integral part of these statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations. Southwest Gas Corporation (the Company) is comprised of two segments: natural gas operations (Southwest or the natural gas operations segment) and construction services. Southwest purchases, transports, and distributes natural gas to customers in portions of Arizona, Nevada, and California. The public utility rates, practices, facilities, and service territories of Southwest are subject to regulatory oversight. The timing and amount of rate relief can materially impact results of operations. Natural gas sales are seasonal, peaking during the winter months. Variability in weather from normal temperatures can materially impact results of operations. Natural gas purchases and the timing of related recoveries can materially impact liquidity. Northern Pipeline Construction Co. (Northern or the construction services segment), a wholly owned subsidiary, is a full-service underground piping contractor which provides utility companies with trenching and installation, replacement, and maintenance services for energy distribution systems.

Basis of Presentation. The Company follows generally accepted accounting principles (GAAP) in accounting for all of its businesses. Accounting for the natural gas utility operations conforms with GAAP as applied to regulated companies and as prescribed by federal agencies and the commissions of the various states in which the utility operates. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Consolidation. The accompanying financial statements are presented on a consolidated basis and include the accounts of Southwest Gas Corporation and all wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated with the exception of transactions between Southwest and Northern in accordance with Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation."

Net Utility Plant. Net utility plant includes gas plant at original cost, less the accumulated provision for depreciation and amortization, plus the unamortized balance of acquisition adjustments. Original cost includes contracted services, material, payroll and related costs such as taxes and benefits, general and administrative expenses, and an allowance for funds used during construction less contributions in aid of construction.

Deferred Purchased Gas Costs. The various regulatory commissions have established procedures to enable Southwest to adjust its billing rates for changes in the cost of gas purchased. The difference between the current cost of gas purchased and the cost of gas recovered in billed rates is deferred. Generally, these deferred amounts are recovered or refunded within one year.

Income Taxes. The Company uses the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date.

For regulatory and financial reporting purposes, investment tax credits (ITC) related to gas utility operations are deferred and amortized over the life of related fixed assets.

Gas Operating Revenues. Revenues are recorded when customers are billed. Customer billings are based on monthly meter reads and are calculated in accordance with applicable tariffs. Southwest also recognizes accrued utility revenues for the estimated amount of services rendered between the meter-reading dates in a particular month and the end of such month.

Construction Revenues. The majority of the Northern contracts are performed under unit price contracts. These contracts state prices per unit of installation. Revenues are recorded as installations are completed. Fixed-price contracts use the percentage-of-completion method of accounting and, therefore, take into account the cost, estimated earnings, and revenue to date on contracts not yet completed. The amount of revenue recognized is based on costs expended to date relative to anticipated final contract costs. Revisions in estimates of costs and earnings during the course of the work are reflected in the accounting period in which the facts requiring revision become known. If a loss on a contract becomes known or is anticipated, the entire amount of the estimated ultimate loss is recognized at that time in the financial statements.

Depreciation and Amortization. Utility plant depreciation is computed on the straight-line remaining life method at composite rates considered sufficient to amortize costs over estimated service lives, including components which adjust for salvage value and removal costs, as approved by the appropriate regulatory agency. When plant is retired from service, the original cost of plant, including cost of removal, less salvage, is charged to the accumulated provision for depreciation. Acquisition adjustments are amortized, as ordered by regulators, over periods which approximate the remaining estimated life of the acquired properties. Costs related to refunding utility debt and debt issuance expenses are deferred and amortized over the weighted-average lives of the new issues. Other regulatory assets, when appropriate, are amortized over time periods authorized by regulators. Nonutility property and equipment are depreciated on a straight-line method based on the estimated useful lives of the related assets. Goodwill amortization for each of the last three years has been $400,000. Pursuant to Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets," goodwill amortization will be eliminated as of January 2002.

Allowance for Funds Used During Construction (AFUDC). AFUDC represents the cost of both debt and equity funds used to finance utility construction. AFUDC is capitalized as part of the cost of utility plant. The Company capitalized $2.5 million in 2001, $1.6 million in 2000, and $2.3 million in 1999 of AFUDC related to natural gas utility operations. The debt portion of AFUDC is reported in the consolidated statements of income as an offset to net interest deductions and the equity portion is reported as other income. Utility plant construction costs, including

AFUDC, are recovered in authorized rates through depreciation when completed projects are placed into operation, and general rate relief is requested and granted.

Earnings Per Share. Basic earnings per share (EPS) are calculated by dividing net income by the weighted-average number of shares outstanding during the period. Diluted EPS includes additional weighted-average common stock equivalents (stock options and performance shares). Unless otherwise noted, the term "Earnings Per Share" refers to Basic EPS. A reconciliation of the shares used in the Basic and Diluted EPS calculations is shown in the following table. Net income was the same for Basic and Diluted EPS calculations.

| (In thousands) | 2001 | 2000 | 1999 |
|---|---|---|---|
| Average basic shares | 32,122 | 31,371 | 30,690 |
| Effect of dilutive securities | | | |
| Stock options | 122 | 85 | 176 |
| Performance shares | 154 | 119 | 99 |
| Average diluted shares | 32,398 | 31,575 | 30,965 |

Cash Flows. For purposes of reporting consolidated cash flows, cash and cash equivalents include cash on hand and financial instruments with a maturity of three months or less, but exclude funds held in trust from the issuance of industrial development revenue bonds (IDRB).

NOTE 2. UTILITY PLANT

Net utility plant as of December 31, 2001 and 2000 was as follows (thousands of dollars):

| DECEMBER 31 | 2001 | 2000 |
|---|---|---|
| Gas plant: | | |
| Storage | $ 3,992 | $ 3,927 |
| Transmission | 187,393 | 183,842 |
| Distribution | 2,104,006 | 1,920,357 |
| General | 188,998 | 188,686 |
| Other | 77,548 | 72,885 |
| | 2,561,937 | 2,369,697 |
| Less: accumulated depreciation | (789,751) | (728,466) |
| Acquisition adjustments, net | 2,894 | 3,124 |
| Construction work in progress | 50,491 | 41,727 |
| Net utility plant | $1,825,571 | $1,686,082 |

Depreciation and amortization expense on gas plant was $102 million in 2001, $92.4 million in 2000, and $85.6 million in 1999.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Leases and Rentals. Southwest leases the liquefied natural gas (LNG) facilities on its northern Nevada system, a portion of its corporate headquarters office complex in Las Vegas, and its administrative offices in Phoenix. The leases provide for current terms which expire in 2003, 2017, and 2009, respectively, with optional renewal terms available at the expiration dates. The final rental payments for the LNG facilities are $6.7 million due in 2002 with the lease expiring in January 2003. The rental payments for the corporate headquarters office complex are $1.8 million in 2002, $1.9 million in 2003, $2 million in each of the years 2004 through 2006, and $22.3 million cumulatively thereafter. The rental payments for the Phoenix administrative offices are $1.3 million for each of the years 2002 and 2003, $1.4 million in 2004, $1.5 million for each of the years 2005 and 2006, and $4 million cumulatively thereafter. In addition to the above, the Company leases certain office and construction equipment. The majority of these leases are short-term. These leases are accounted for as operating leases, and for the gas segment are treated as such for regulatory purposes. Rentals included in operating expenses for all operating leases were $28 million in 2001, $25.7 million in 2000, and $24.7 million in 1999. These amounts include Northern lease expenses of approximately $12.6 million in 2001, $9.2 million in 2000, and $8.4 million in 1999 for various short-term leases of equipment and temporary office sites.

The following is a schedule of future minimum lease payments for noncancellable operating leases (with initial or remaining terms in excess of one year) as of December 31, 2001 (thousands of dollars):

| YEAR ENDING DECEMBER 31 | |
|---|---|
| 2002 | $12,101 |
| 2003 | 4,891 |
| 2004 | 4,540 |
| 2005 | 4,265 |
| 2006 | 3,837 |
| Thereafter | 26,689 |
| Total minimum lease payments | $56,323 |

NOTE 3. RECEIVABLES AND RELATED ALLOWANCES

Business activity with respect to gas utility operations is conducted with customers located within the three-state region of Arizona, Nevada, and California. At December 31, 2001, the gas utility customer accounts receivable balance was $124 million. Approximately 56 percent of the gas utility customers were in Arizona, 35 percent in Nevada, and 9 percent in California. Although the Company seeks to minimize its credit risk related to utility operations by requiring security deposits from new customers, imposing late fees, and actively pursuing collection on overdue accounts, some accounts are ultimately not collected. Provisions for uncollectible accounts are recorded monthly, as needed, and are included in the ratemaking process as a cost of service. Activity in the allowance for uncollectibles is summarized as follows (thousands of dollars):

| ALLOWANCE FOR UNCOLLECTIBLES | |
|---|---|
| Balance, December 31, 1998 | $ 1,345 |
| Additions charged to expense | 1,897 |
| Accounts written off, less recoveries | (1,512) |
| Balance, December 31, 1999 | 1,730 |
| Additions charged to expense | 1,036 |
| Accounts written off, less recoveries | (1,202) |
| Balance, December 31, 2000 | 1,564 |
| Additions charged to expense | 3,874 |
| Accounts written off, less recoveries | (3,567) |
| Balance, December 31, 2001 | $ 1,871 |

NOTE 4. REGULATORY ASSETS AND LIABILITIES

Natural gas operations are subject to the regulation of the Arizona Corporation Commission (ACC), the Public Utilities Commission of Nevada (PUCN), the California Public Utilities Commission (CPUC), and the Federal Energy Regulatory Commission (FERC). Company accounting policies conform to generally accepted accounting principles applicable to rate-regulated enterprises, principally SFAS No. 71, and reflect the effects of the ratemaking process. SFAS No. 71 allows for the deferral as regulatory assets, costs that otherwise would have been expensed if it is probable future recovery from customers will occur. If rate recovery is no longer probable, due to competition or the actions of regulators, Southwest would be required to write off the related regulatory asset.

The following table represents existing regulatory assets and liabilities (thousands of dollars):

| DECEMBER 31 | 2001 | 2000 |
|---|---|---|
| Regulatory assets: | | |
| Deferred purchased gas costs | $ 83,501 | $ 92,064 |
| Accrued purchased gas costs* | - | 56,400 |
| SFAS No. 109 - Income taxes, net | 4,434 | 5,365 |
| Unamortized premium on reacquired debt | 13,607 | 14,516 |
| Other | 29,063 | 25,169 |
| | 130,605 | 193,514 |
| Regulatory liabilities | (342) | (1,587) |
| Net regulatory assets | $130,263 | $191,927 |

* Included in Prepaids and other current assets on the Consolidated Balance Sheet.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

## NOTE 5. PREFERRED SECURITIES

Preferred Securities of Southwest Gas Capital I. In October 1995, Southwest Gas Capital I (the Trust), a consolidated wholly owned subsidiary of the Company, issued $60 million of 9.125% Trust Originated Preferred Securities (the Preferred Securities). In connection with the Trust issuance of the Preferred Securities and the related purchase by the Company of all of the Trust common securities (the Common Securities), the Company issued to the Trust $61.8 million principal amount of its 9.125% Subordinated Deferrable Interest Notes, due 2025 (the Subordinated Notes). The sole assets of the Trust are and will be the Subordinated Notes. The interest and other payment dates on the Subordinated Notes correspond to the distribution and other payment dates on the Preferred Securities and Common Securities. Under certain circumstances, the Subordinated Notes may be distributed to the holders of the Preferred Securities and holders of the Common Securities in liquidation of the Trust. The Subordinated Notes became redeemable at the option of the Company on December 31, 2000, and may be redeemed at any time at a redemption price of $25 per Subordinated Note plus accrued and unpaid interest. In the event that the Subordinated Notes are repaid, the Preferred Securities and the Common Securities will be redeemed on a pro rata basis at $25 per Preferred Security and Common Security plus accumulated and unpaid distributions. Company obligations under the Subordinated Notes, the Declaration of Trust (the agreement under which the Trust was formed), the guarantee of payment of certain distributions, redemption payments and liquidation payments with respect to the Preferred Securities to the extent the Trust has funds available therefore and the indenture governing the Subordinated Notes, including the Company agreement pursuant to such indenture to pay all fees and expenses of the Trust, other than with respect to the Preferred Securities and Common Securities, taken together, constitute a full and unconditional guarantee on a subordinated basis by the Company of payments due on the Preferred Securities. As of December 31, 2001, 2.4 million Preferred Securities were outstanding.

The Company has the right to defer payments of interest on the Subordinated Notes by extending the interest payment period at any time for up to 20 consecutive quarters (each, an Extension Period). If interest payments are so deferred, distributions will also be deferred. During such Extension Period, distributions will continue to accrue with interest thereon (to the extent permitted by applicable law) at an annual rate of 9.125% per annum compounded quarterly. There could be multiple Extension Periods of varying lengths throughout the term of the Subordinated Notes. If the Company exercises the right to extend an interest payment period, the Company shall not during such Extension Period (i) declare or pay dividends on, or make a distribution with respect to, or redeem, purchase or acquire or make a liquidation payment with respect to, any of its capital stock, or (ii) make any payment of interest, principal or premium, if any, on or repay, repurchase, or redeem any debt securities issued by the Company that rank equal with or junior to the Subordinated Notes; provided, however, that restriction (i) above does not apply to any stock dividends paid by the Company where the dividend stock is the same as that on which the dividend is being paid. The Company has no present intention of exercising its right to extend the interest payment period.

NOTE 6. LONG-TERM DEBT

| DECEMBER 31 | 2001 CARRYING AMOUNT | 2001 MARKET VALUE | 2000 CARRYING AMOUNT | 2000 MARKET VALUE |
|---|---|---|---|---|
| (Thousands of dollars) | | | | |
| Debentures: | | | | |
| 9 3/4% Series F, due 2002 | $ 100,000 | $102,868 | $100,000 | $103,855 |
| 7 1/2% Series, due 2006 | 75,000 | 79,277 | 75,000 | 76,939 |
| 8% Series, due 2026 | 75,000 | 78,343 | 75,000 | 74,139 |
| Notes, 8.375%, due 2011 | 200,000 | 218,794 | - | - |
| Medium-term notes, 7.59% series, due 2017 | 25,000 | 25,555 | 25,000 | 24,263 |
| Medium-term notes, 7.75% series, due 2005 | 25,000 | 26,812 | 25,000 | 25,607 |
| Medium-term notes, 7.78% series, due 2022 | 25,000 | 25,124 | 25,000 | 23,793 |
| Medium-term notes, 7.92% series, due 2027 | 25,000 | 25,327 | 25,000 | 23,945 |
| Medium-term notes, 6.89% series, due 2007 | 17,500 | 17,973 | 17,500 | 17,006 |
| Medium-term notes, 6.76% series, due 2027 | 7,500 | 6,813 | 7,500 | 6,254 |
| Medium-term notes, 6.27% series, due 2008 | 25,000 | 24,865 | 25,000 | 23,318 |
| Unamortized discount | (5,103) | - | (2,872) | - |
| | 594,897 | | 397,128 | - |
| Revolving credit facility | 200,000 | 200,000 | 200,000 | 200,000 |
| Industrial development revenue bonds: | | | | |
| Variable-rate bonds: | | | | |
| Tax-exempt Series A, due 2028 | 50,000 | 50,000 | 50,000 | 50,000 |
| Taxable Series B, due 2038 | - | - | 8,270 | 8,270 |
| Less: funds held in trust | - | - | (3,645) | - |
| | 50,000 | | 54,625 | - |
| Fixed-rate bonds: | | | | |
| 7.30% 1992 Series A, due 2027 | 30,000 | 30,900 | 30,000 | 31,116 |
| 7.50% 1992 Series B, due 2032 | 100,000 | 103,000 | 100,000 | 103,861 |
| 6.50% 1993 Series A, due 2033 | 75,000 | 75,000 | 75,000 | 73,988 |
| 6.10% 1999 Series A, due 2038 | 12,410 | 13,310 | 12,410 | 13,270 |
| 5.95% 1999 Series C, due 2038 | 14,320 | 15,287 | 14,320 | 14,985 |
| 5.55% 1999 Series D, due 2038 | 8,270 | 8,311 | - | - |
| Unamortized discount | (3,276) | - | (3,384) | - |
| | 236,724 | | 228,346 | - |
| Other | 22,371 | - | 24,457 | - |
| | 1,103,992 | | 904,556 | |
| Less: current maturities | (307,641) | | (8,139) | - |
| Long-term debt, less current maturities | $ 796,351 | | $896,417 | |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

The Company has a $350 million revolving credit agreement, which bears interest at either the London Interbank Offering Rate (LIBOR) plus or minus a competitive margin, or the greater of the prime rate or one half of one percent plus the Federal Funds rate. Any amounts borrowed under the revolving credit agreement become payable in June 2002. The Company has designated $200 million of the total facility as long-term debt and uses the remaining $150 million for working capital purposes and has designated the related outstanding amounts as short-term debt.

The interest rate on the taxable variable-rate IDRBs averaged 5.32 percent in 2001 and 7.01 percent in 2000. The interest rate on the tax-exempt variable-rate IDRBs averaged 3.81 percent in 2001 and 4.66 percent in 2000. The rates for the variable-rate IDRBs are established on a weekly basis. The Company has the option to convert from the current weekly rates to daily rates, term rates, or variable-term rates.

The fair value of the revolving credit facility approximates carrying value. Market values for the debentures and fixed-rate IDRBs were determined based on dealer quotes using trading records for December 31, 2001 and 2000, as applicable, and other secondary sources which are customarily consulted for data of this kind. The carrying values of variable-rate IDRBs were used as estimates of fair value based upon the variable interest rates of the bonds.

In June 2002, the $350 million revolving credit facility, of which $200 million is designated as long-term debt, and the $100 million Series F debentures will mature. The Company intends to refinance the long-term portion of the revolving credit agreement and the Series F debentures on a long-term basis but no firm agreements are in place at this time. The timing, types, and amounts of these external financings will be dependent on conditions in the capital markets. Estimated maturities of long-term debt for the next five years are $308 million, $6.2 million, $6.2 million, $27.3 million, and $75 million, respectively.

NOTE 7. SHORT-TERM DEBT

As discussed in Note 6, a portion of the $350 million revolving credit facility is designated as short-term debt. This facility expires in June 2002. Short-term borrowings were $93 million and $131 million at December 31, 2001 and 2000, respectively. The weighted-average interest rates on these borrowings were 2.47 percent for 2001 and 7.12 percent for 2000.

In November 2000, the Company obtained another $75 million revolving credit facility, bearing interest at either the LIBOR plus or minus a competitive margin, or the greater of the prime rate or one half of one percent plus the Federal Funds rate. This revolving credit agreement expired in November 2001 and was not renewed.

NOTE 8. COMMITMENTS AND CONTINGENCIES

Legal and Regulatory Proceedings. In connection with an attempted merger and subsequent termination, the Company is a party to various legal proceedings. The Company has also been named as defendant in other miscellaneous legal proceedings. The Company is a party to various regulatory proceedings. The ultimate dispositions of these proceedings are not presently determinable; however, it is the opinion of management that no litigation or regulatory proceeding to which the Company is subject will have a material adverse impact on its financial position or results of operations.

## NOTE 9. EMPLOYEE BENEFITS

Southwest has a noncontributory qualified retirement plan with defined benefits covering substantially all employees. Southwest also provides postretirement benefits other than pensions (PBOP) to its qualified retirees for health care, dental, and life insurance benefits.

The following tables set forth the qualified retirement plan and PBOP funded status and amounts recognized on the Consolidated Balance Sheets and Statements of Income.

| | QUALIFIED RETIREMENT PLAN | | PBOP | |
|---|---|---|---|---|
| | 2001 | 2000 | 2001 | 2000 |
| (Thousands of dollars) | | | | |
| CHANGE IN BENEFIT OBLIGATIONS | | | | |
| Benefit obligation for service rendered to date at beginning of year (PBO/APBO) | $262,981 | $236,618 | $ 26,245 | $ 24,882 |
| Service cost | 11,057 | 10,455 | 591 | 558 |
| Interest cost | 18,805 | 16,919 | 1,856 | 1,762 |
| Actuarial loss (gain) | 2,403 | 5,489 | 812 | 193 |
| Benefits paid | (7,200) | (6,500) | (1,300) | (1,150) |
| Benefit obligation at end of year (PBO/APBO) | $288,046 | $262,981 | $ 28,204 | $ 26,245 |
| CHANGE IN PLAN ASSETS | | | | |
| Market value of plan assets at beginning of year | $281,280 | $271,880 | $ 10,958 | $ 8,946 |
| Actual return on plan assets | 23 | 15,900 | 218 | 559 |
| Employer contributions | - | - | 1,226 | 1,453 |
| Benefits paid | (7,200) | (6,500) | - | - |
| Market value of plan assets at end of year | $274,103 | $281,280 | $ 12,402 | $ 10,958 |
| Funded status | $(13,943) | $ 18,299 | $(15,802) | $(15,287) |
| Unrecognized net actuarial loss (gain) | (10,698) | (39,029) | 2,367 | 513 |
| Unrecognized transition obligation (2004/2012) | 1,632 | 2,469 | 9,537 | 10,404 |
| Unrecognized prior service cost | 123 | 180 | - | - |
| Prepaid (accrued) benefit cost | $(22,886) | $(18,081) | $ (3,898) | $ (4,370) |
| WEIGHTED-AVERAGE ASSUMPTIONS AS OF DECEMBER 31, | | | | |
| Discount rate | 7.25% | 7.25% | 7.25% | 7.25% |
| Expected return on plan assets | 9.25% | 9.00% | 9.25% | 9.00% |
| Rate of compensation increase | 4.75% | 4.75% | 4.75% | 4.75% |

For PBOP measurement purposes, a 5.5 percent annual rate of increase in the per capita cost of covered health care benefits is assumed for 2002. The rate is assumed to decrease one-half of one percent in 2003, at which time the average annual increase is projected to be five percent. The Company makes fixed contributions for health care benefits of employees who retire after 1988, but pays up to 100 percent of covered health care costs for employees

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

who retired prior to 1989. The assumed annual rate of increase noted above applies to the benefit obligations of pre-1989 retirees only.

COMPONENTS OF NET PERIODIC BENEFIT COST

| | QUALIFIED RETIREMENT PLAN | | | PBOP | | |
|---|---|---|---|---|---|---|
| | 2001 | 2000 | 1999 | 2001 | 2000 | 1999 |
| (Thousands of dollars) | | | | | | |
| Service cost | $ 11,057 | $ 10,455 | $ 9,976 | $ 591 | $ 558 | $ 572 |
| Interest cost | 18,805 | 16,919 | 15,406 | 1,856 | 1,762 | 1,643 |
| Expected return on plan assets | (25,383) | (22,681) | (20,266) | (1,073) | (858) | (664) |
| Amortization of prior service costs | 57 | 57 | 58 | - | - | - |
| Amortization of unrecognized transition obligation | 837 | 837 | 837 | 867 | 867 | 867 |
| Amortization of net (gain) loss | (568) | (694) | - | - | - | - |
| Net periodic benefit cost | $ 4,805 | $ 4,893 | $ 6,011 | $ 2,241 | $2,329 | $2,418 |

In addition to the qualified retirement plan, Southwest has a separate unfunded supplemental retirement plan which is limited to officers. The plan is noncontributory with defined benefits. Plan costs were $2.9 million in 2001, $2.2 million in 2000, and $2 million in 1999. The accumulated benefit obligation of the plan was $20.6 million at December 31, 2001.

The Employees' Investment Plan provides for purchases of Company common stock or certain other investments by eligible Southwest employees through deductions of a percentage of base compensation, subject to IRS limitations. Southwest matches one-half of amounts deferred. The maximum Company contribution is three percent of an employee's annual compensation. The cost of the plan was $3 million in 2001, $3 million in 2000, and $2.8 million in 1999. Northern has a separate plan, the cost and liability for which are not significant.

Southwest has a deferred compensation plan for all officers and members of the Board of Directors. The plan provides the opportunity to defer up to 100 percent of annual cash compensation. Southwest matches one-half of amounts deferred by officers. The maximum Company contribution is three percent of an officer's annual salary. Payments of compensation deferred, plus interest, are made in equal monthly installments over 5, 10, 15, or 20 years, as elected by the participant. Deferred compensation earns interest at a rate determined each January. The interest rate equals 150 percent of Moody's Seasoned Corporate Bond Index.

At December 31, 2001, the Company had two stock-based compensation plans. These plans are accounted for in accordance with Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." In connection with the stock-based compensation plans, the Company recognized compensation expense of $3.1 million in 2001, $970,000 in 2000, and $2.2 million in 1999. Had compensation cost been determined based on the fair value of the awards at the grant dates, net income and earnings per share would have reflected the pro forma amounts indicated below (thousands of dollars, except per share amounts):

| | 2001 | 2000 | 1999 |
|---|---|---|---|
| Net income: | | | |
| As reported | $37,156 | $38,311 | $39,310 |
| Pro forma | 36,813 | 37,959 | 38,995 |
| Basic earnings per share: | | | |
| As reported | 1.16 | 1.22 | 1.28 |
| Pro forma | 1.15 | 1.21 | 1.27 |

With respect to the first plan, the Company may grant options to purchase shares of common stock to key employees and outside directors. Each option has an exercise price equal to the market price of Company common stock on the date of grant and a maximum term of ten years. The options vest 40 percent at the end of year one and 30 percent at the end of years two and three. The grant date fair value of the options was estimated using the extended binomial option pricing model. The following assumptions were used in the valuation calculation:

| | 2001 | 2000 | 1999 |
|---|---|---|---|
| Dividend yield | 3.60% | 3.90% | 4.62% |

| | | | |
|---|---|---|---|
| Risk-free interest rate range | 2.17 to 3.82% | 4.74 to 4.86% | 4.91 to 5.76% |
| Expected volatility range | 22 to 27% | 25 to 30% | 22 to 28% |
| Expected life | 1 to 3 years | 1 to 3 years | 1 to 3 years |

The following tables summarize Company stock option plan activity and related information (thousands of options):

| | 2001 | | 2000 | | 1999 | |
|---|---|---|---|---|---|---|
| | NUMBER OF OPTIONS | WEIGHTED-AVERAGE EXERCISE PRICE | NUMBER OF OPTIONS | WEIGHTED-AVERAGE EXERCISE PRICE | NUMBER OF OPTIONS | WEIGHTED-AVERAGE EXERCISE PRICE |
| Outstanding at the beginning of the year | 990 | $ 18.94 | 704 | $ 19.32 | 587 | $ 17.38 |
| Granted during the year | 317 | 23.23 | 297 | 17.96 | 118 | 28.91 |
| Exercised during the year | (184) | 15.07 | (7) | 15.80 | (1) | 15.00 |
| Forfeited during the year | - | - | (4) | 17.94 | - | - |
| Expired during the year | - | - | - | - | - | - |
| Outstanding at year end | 1,123 | $ 20.79 | 990 | $ 18.94 | 704 | $ 19.32 |
| Exercisable at year end | 597 | $ 21.00 | 591 | $ 24.18 | 481 | $ 17.77 |

The weighted-average grant-date fair value of options granted was $2.81 for 2001, $2.51 for 2000, and $4.34 for 1999. The exercise prices for the options outstanding range from $15.00 to $28.94. On December 31, 2001, the options outstanding had a weighted-average remaining contractual life of approximately 7.6 years.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

In addition to the option plan, the Company may issue restricted stock in the form of performance shares to encourage key employees to remain in its employment to achieve short-term and long-term performance goals. Plan participants are eligible to receive a cash bonus (i.e., short-term incentive) and performances shares (i.e., long-term incentive). The performance shares vest after three years from issuance and are subject to a final adjustment as determined by the Board of Directors. The following table summarizes the activity of this plan (thousands of shares):

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 |
|---|---|---|---|
| Nonvested performance shares at beginning of year | 237 | 193 | 172 |
| Performance shares granted | 142 | 111 | 83 |
| Performance shares forfeited | - | (6) | (1) |
| Shares vested and issued | (65) | (61) | (61) |
| Nonvested performance shares at end of year | 314 | 237 | 193 |
| Average grant date fair value of award | $ 19.91 | $ 21.63 | $ 26.63 |

NOTE 10. INCOME TAXES

Income tax expense (benefit) consists of the following (thousands of dollars):

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 |
|---|---|---|---|
| Current: | | | |
| Federal | $ 27,750 | $(60,628) | $ 33,152 |
| State | 2,078 | (7,465) | 6,736 |
| | 29,828 | (68,093) | 39,888 |
| Deferred: | | | |
| Federal | (9,902) | 76,334 | (15,126) |
| State | (341) | 5,387 | (3,117) |
| | (10,243) | 81,721 | (18,243) |
| Total income tax expense | $ 19,585 | $ 13,628 | $ 21,645 |

Deferred income tax expense consists of the following significant components (thousands of dollars):

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 |
|---|---|---|---|
| Deferred federal and state: | | | |
| Property-related items | $ 19,560 | $ 28,184 | $ 11,405 |
| Purchased gas cost adjustments | (26,975) | 56,321 | (19,201) |
| Employee benefits | (2,121) | (3,687) | (5,816) |
| Merger costs | - | 1,822 | (1,822) |
| All other deferred | 161 | (51) | (1,941) |
| Total deferred federal and state | (9,375) | 82,589 | (17,375) |
| Deferred ITC, net | (868) | (868) | (868) |
| Total deferred income tax expense | $(10,243) | $ 81,721 | $(18,243) |

The consolidated effective income tax rate for the period ended December 31, 2001 and the two prior periods differs from the federal statutory income tax rate. The sources of these differences and the effect of each are summarized as follows:

| YEAR ENDED DECEMBER 31 | 2001 | 2000 | 1999 |
|---|---|---|---|
| Federal statutory income tax rate | 35.0% | 35.0% | 35.0% |
| Net state tax liability | 3.2 | 2.9 | 3.0 |
| Property-related items | 1.5 | 1.7 | 1.4 |
| Effect of closed tax years and resolved issues | (4.4) | (11.6) | (1.8) |
| Tax credits | (1.5) | (1.7) | (1.4) |
| Tax exempt interest | - | (0.3) | (0.3) |
| Corporate owned life insurance | (0.5) | (0.8) | (1.0) |
| All other differences | 1.2 | 1.0 | 0.6 |
| Consolidated effective income tax rate | 34.5% | 26.2% | 35.5% |

Deferred tax assets and liabilities consist of the following (thousands of dollars):

| DECEMBER 31 | 2001 | 2000 |
|---|---|---|
| Deferred tax assets: | | |
| Deferred income taxes for future amortization of ITC | $ 9,280 | $ 9,826 |
| Employee benefits | 23,214 | 21,093 |
| Other | 6,601 | 5,115 |
| Valuation allowance | - | - |
| | 39,095 | 36,034 |
| Deferred tax liabilities: | | |
| Property-related items, including accelerated depreciation | 208,285 | 188,725 |
| Regulatory balancing accounts | 33,436 | 60,411 |
| Property-related items previously flowed through | 13,713 | 15,192 |
| Unamortized ITC | 14,668 | 15,536 |
| Debt-related costs | 4,792 | 5,104 |
| Other | 6,159 | 4,199 |
| | 281,053 | 289,167 |
| Net deferred tax liabilities | $241,958 | $253,133 |
| Current | $ 24,154 | $ 48,965 |
| Noncurrent | 217,804 | 204,168 |
| Net deferred tax liabilities | $241,958 | $253,133 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

## NOTE 11. SEGMENT INFORMATION

Company operating segments are determined based on the nature of their activities. The natural gas operations segment is engaged in the business of purchasing, transporting, and distributing natural gas. Revenues are generated from the sale and transportation of natural gas. The construction services segment is engaged in the business of providing utility companies with trenching and installation, replacement, and maintenance services for energy distribution systems.

The accounting policies of the reported segments are the same as those described within Note 1 - Summary of Significant Accounting Policies. Northern accounts for the services provided to Southwest at contractual (market) prices. At December 31, 2001 and 2000, consolidated accounts receivable included $4.3 million and $5.2 million, respectively, which were not eliminated during consolidation.

The financial information pertaining to the natural gas operations and construction services segments for each of the three years in the period ended December 31, 2001, is as follows (thousands of dollars):

| 2001 | GAS OPERATIONS | CONSTRUCTION SERVICES | ADJUSTMENTS | TOTAL |
|---|---|---|---|---|
| Revenues from unaffiliated customers | $1,193,102 | $ 135,655 | | $1,328,757 |
| Intersegment sales | - | 67,931 | 67,931 | - |
| Total | $1,193,102 | $ 203,586 | | $1,396,688 |
| Interest expense | $ 78,746 | $ 1,985 | | $ 80,731 |
| Depreciation and amortization | $ 104,498 | $ 13,950 | | $ 118,448 |
| Income tax expense | $ 16,098 | $ 3,487 | | $ 19,585 |
| Segment income | $ 32,626 | $ 4,530 | | $ 37,156 |
| Segment assets | $2,289,111 | $ 83,228 | $ (2,727) | $2,369,612 |
| Capital expenditures | $ 248,352 | $ 17,228 | | $ 265,580 |

| 2000 | GAS OPERATIONS | CONSTRUCTION SERVICES | ADJUSTMENTS | TOTAL |
|---|---|---|---|---|
| Revenues from unaffiliated customers | $ 870,711 | $ 107,686 | | $ 978,397 |
| Intersegment sales | - | 55,690 | 55,690 | - |
| Total | $ 870,711 | $ 163,376 | | $1,034,087 |
| Interest expense | $ 68,892 | $ 1,779 | | $ 70,671 |
| Depreciation and amortization | $ 94,689 | $ 11,951 | | $ 106,640 |
| Income tax expense | $ 10,277 | $ 3,351 | | $ 13,628 |
| Segment income | $ 33,908 | $ 4,403 | | $ 38,311 |
| Segment assets | $2,154,641 | $ 79,790 | $ (2,094) | $2,232,337 |
| Capital expenditures | $ 205,161 | $ 18,079 | | $ 223,240 |

| 1999 | GAS OPERATIONS | CONSTRUCTION SERVICES | ADJUSTMENTS | TOTAL |
|---|---|---|---|---|
| Revenues from unaffiliated customers | $ 791,155 | $ 95,744 | | $ 886,899 |
| Intersegment sales | - | 49,967 | | 49,967 |
| Total | $ 791,155 | $ 145,711 | | $ 936,866 |
| Interest expense | $ 61,597 | $ 1,605 | | $ 63,202 |
| Depreciation and amortization | $ 88,254 | $ 10,271 | | $ 98,525 |
| Income tax expense | $ 18,532 | $ 3,113 | | $ 21,645 |
| Segment income | $ 35,473 | $ 3,837 | | $ 39,310 |
| Segment assets | $1,855,114 | $ 68,630 | $ (302) | $1,923,442 |
| Capital expenditures | $ 207,773 | $ 21,730 | | $ 229,503 |

Construction services segment assets include deferred tax assets of $2.5 million in 2001, which were netted against gas operations segment deferred tax liabilities during consolidation. Construction services segment liabilities include taxes payable of $204,000 in 2001, which were netted against gas operations segment tax receivable during consolidation. Construction services segment assets include deferred tax assets of $2.1 million in 2000, which were netted against gas operations segment deferred tax liabilities during consolidation. Construction services segment assets include an income tax receivable of $302,000 in 1999, which was netted against gas operations segment accrued taxes during consolidation.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

## NOTE 12. QUARTERLY FINANCIAL DATA (UNAUDITED)

| QUARTER ENDED | MARCH 31 | JUNE 30 | SEPTEMBER 30 | DECEMBER 31 |
|---|---|---|---|---|
| | (Thousands of dollars, except per share amounts) | | | |
| **2001** | | | | |
| Operating revenues | $487,498 | $278,960 | $ 246,094 | $ 384,136 |
| Operating income (loss) | 74,106 | 1,111 | (4,597) | 63,363 |
| Net income (loss) | 33,809 | (11,140) | (16,488) | 30,975 |
| Basic earnings (loss) per common share* | 1.06 | (0.35) | (0.51) | 0.96 |
| Diluted earnings (loss) per common share* | 1.05 | (0.35) | (0.51) | 0.95 |
| **2000** | | | | |
| Operating revenues | $296,815 | $197,634 | $ 198,962 | $ 340,676 |
| Operating income (loss) | 56,619 | 2,583 | (4,197) | 73,625 |
| Net income (loss) | 25,198 | (9,729) | (9,680) | 32,522 |
| Basic earnings (loss) per common share* | 0.81 | (0.31) | (0.31) | 1.03 |
| Diluted earnings (loss) per common share* | 0.80 | (0.31) | (0.31) | 1.02 |
| **1999** | | | | |
| Operating revenues | $308,025 | $200,292 | $ 166,289 | $ 262,260 |
| Operating income (loss) | 62,725 | 11,530 | (2,904) | 59,861 |
| Net income (loss) | 28,266 | (3,596) | (14,188) | 28,828 |
| Basic earnings (loss) per common share* | 0.93 | (0.12) | (0.46) | 0.93 |
| Diluted earnings (loss) per common share* | 0.92 | (0.12) | (0.46) | 0.93 |

* The sum of quarterly earnings (loss) per average common share may not equal the annual earnings (loss) per share due to the ongoing change in the weighted average number of common shares outstanding.

The demand for natural gas is seasonal, and it is the opinion of management that comparisons of earnings for the interim periods do not reliably reflect overall trends and changes in the operations of the Company. Also, the timing of general rate relief can have a significant impact on earnings for interim periods. See Management's Discussion and Analysis for additional discussion of operating results.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders of
Southwest Gas Corporation:

We have audited the accompanying consolidated balance sheets of Southwest Gas Corporation (a California corporation) and its subsidiaries (the Company) as of December 31, 2001 and 2000, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Southwest Gas Corporation and its subsidiaries as of December 31, 2001 and 2000, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States.

ARTHUR ANDERSEN LLP

Las Vegas, Nevada
February 8, 2002

# SHAREHOLDER INFORMATION

## STOCK LISTING INFORMATION

Southwest Gas Corporation's common stock is listed on the New York Stock Exchange under the ticker symbol "SWX." Quotes may be obtained in daily financial newspapers or some local newspapers where it is listed under "SoWestGas."

## ANNUAL MEETING

The Annual Meeting of Shareholders will be held on May 9, 2002 at 10:00 a.m. at the Rio Suites Hotel and Casino, I-15 and Flamingo Road, Las Vegas, Nevada.

## DIVIDEND REINVESTMENT AND STOCK PURCHASE PLAN

The Southwest Gas Corporation Dividend Reinvestment and Stock Purchase Plan (DRSPP) provides common shareholders, customers, employees and residents of Arizona, California and Nevada with a simple and convenient method of investing cash dividends in additional shares of Company stock without payment of any brokerage commission.

The DRSPP features include:

Initial investments of $100, up to $100,000 annually
Automatic investing
No commissions on purchases
Safekeeping for common stock certificates

For more information contact: Shareholder Services, Southwest Gas Corporation, P. O. Box 98511, Las Vegas, NV 89193-8511 or call (702) 876-7280.

## DIVIDENDS

Dividends on common stock are declared quarterly by the Board of Directors. As a general rule, they are payable on the first day of March, June, September and December.

## INVESTOR RELATIONS

Southwest Gas Corporation is committed to providing relevant and complete investment information to shareholders, individual investors and members of the investment community. Additional copies of the Company's 2001 Annual Report on Form 10-K, without exhibits, as filed with the Securities and Exchange Commission may be obtained upon request free of charge. Additional financial information may be obtained by contacting Ken Kenny, Investor Relations, Southwest Gas Corporation, P. O. Box 98510, Las Vegas, NV 89193-8510 or by calling (702) 876-7237.

Southwest Gas Corporation information is also available on the Internet at www.swgas.com. For non-financial information, please call (702) 876-7011.

## TRANSFER AGENT

Shareholder Services
Southwest Gas Corporation
P. O. Box 98511
Las Vegas, NV 89193-8511

## REGISTRAR

Southwest Gas Corporation
P. O. Box 98510
Las Vegas, NV 89193-8510

## AUDITORS

Arthur Andersen LLP
3773 Howard Hughes Pkwy
Suite 500 South
Las Vegas, Nevada 89109

EXHIBIT 21.01

SOUTHWEST GAS CORPORATION
LIST OF SUBSIDIARIES OF THE REGISTRANT

AT DECEMBER 31, 2001

| SUBSIDIARY NAME | STATE OF INCORPORATION OR ORGANIZATION TYPE |
|---|---|
| LNG Energy, Inc. | Nevada |
| Paiute Pipeline Company | Nevada |
| Northern Pipeline Construction Co. | Nevada |
| Southwest Gas Transmission Company | Partnership between Southwest Gas Corporation and Utility Financial Corp. |
| Southwest Gas Capital I | Delaware |
| Utility Financial Corp. | Nevada |

EXHIBIT 23.01

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation of our report dated February 8, 2002, incorporated by reference in this Form 10-K, into Southwest Gas Corporation's previously filed registration statements on Form S-3 (File Nos. 333-52224 and 333-74520), Form S-8 (File No. 333-35556), and Form S-3 (File No. 333-35558).

ARTHUR ANDERSEN LLP

Las Vegas, Nevada
March 22, 2002

EXHIBIT 99.01

March 22, 2002

Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
Judiciary Plaza
450 5th Street, N.W.
Washington, D.C. 20549

Re: Confirmation of Receipt of Assurances from Arthur Andersen LLP

Dear Mr. Katz:

Arthur Andersen LLP has audited the consolidated balance sheets of Southwest Gas Corporation and subsidiaries ("the Company") as of December 31, 2001 and 2000, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2001 and has issued its report thereon dated February 8, 2002.

Please be advised that Arthur Andersen has represented that the audit was subject to its quality control system for the U.S. accounting and auditing practice to provide reasonable assurance that the engagement was conducted in compliance with professional standards and that there was appropriate continuity of Arthur Andersen personnel working on the audit, and availability of national office consultation. Availability of personnel at foreign affiliates of Arthur Andersen is not relevant to this audit.

Please contact me if you have any questions regarding this matter.

Respectfully submitted,

/s/ Edward A. Janov

Edward A. Janov
Vice President/Chief Accounting Officer