

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, 1998

COMMISSION FILE NUMBER 1-7850

SOUTHWEST GAS CORPORATION
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

CALIFORNIA
(STATE OR OTHER JURISDICTION OF
INCORPORATION OR ORGANIZATION)

88-0085720
(I.R.S. EMPLOYER
IDENTIFICATION NO.)

5241 SPRING MOUNTAIN ROAD
POST OFFICE BOX 98510
LAS VEGAS, NEVADA
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)

89193-8510
(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. Pacific Stock Exchange, Inc. |
| 9.125% Trust Originated Preferred Securities | New York Stock Exchange, Inc. Pacific Stock Exchange, Inc. |
| Stock Purchase Rights | New York Stock Exchange, Inc. 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 Y NO

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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. []

AGGREGATE MARKET VALUE OF THE VOTING STOCK HELD BY
NONAFFILIATES OF THE REGISTRANT:
\$824,362,704 at March 15, 1999

THE NUMBER OF SHARES OUTSTANDING OF COMMON STOCK:
Common Stock, \$1 Par Value, 30,531,952 shares as of March 15, 1999

DOCUMENTS INCORPORATED BY REFERENCE

| DESCRIPTION ----- | PART INTO WHICH INCORPORATED ----- |
|--|---------------------------------------|
| Annual Report to Shareholders for the Year Ended December 31, 1998 | Parts I, II, and IV |

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PART I

ITEM 1. BUSINESS

The registrant, Southwest Gas Corporation (the Company), is incorporated under the laws of the State of California effective March 1931. The executive offices of the Company are located at 5241 Spring Mountain Road, P.O. Box 98510, Las Vegas, Nevada, 89193-8510, telephone number (702) 876-7237.

The Company is principally engaged in the business of purchasing, transporting, and distributing natural gas to residential, commercial, and industrial customers in geographically diverse portions of Arizona, Nevada, and California (Southwest or the natural gas operations segment).

In April 1996, the Company acquired all of the outstanding stock of Northern Pipeline Construction Co. (Northern or the construction services segment) pursuant to a definitive agreement dated November 1995. The Company issued approximately 1,439,000 shares of common stock valued at \$24 million in connection with the acquisition. The acquisition was accounted for as a purchase. The construction services segment provides utility companies with trenching and installation, replacement, and maintenance services for energy distribution systems.

In July 1996, the Company completed the sale of the assets and liabilities of PriMerit Bank, Federal Savings Bank (PriMerit), a wholly owned subsidiary, to Norwest Corporation (Norwest) for \$191 million pursuant to a definitive agreement dated January 1996. For consolidated financial reporting purposes, the financial services activities are disclosed as discontinued operations.

Financial information with respect to industry segments is included in Note 14 of the Notes to Consolidated Financial Statements which is included in the 1998 Annual Report to Shareholders and is incorporated herein by reference.

In December 1998, the Boards of Directors of the Company and ONEOK, Inc. (ONEOK), headquartered in Tulsa, Oklahoma, announced a definitive agreement for the Company to be merged into ONEOK. The agreement calls for ONEOK to pay cash of \$28.50 for each share of Company common stock outstanding. The transaction is subject to customary conditions, including approvals from shareholders of the Company and state regulators in Arizona, California, and Nevada. ONEOK expects to account for the merger using the purchase method of accounting. If the merger is consummated, the Company would operate as a division of ONEOK.

In February 1999, the Company announced that it had received an unsolicited proposal from Southern Union Company (Southern Union), headquartered in Austin, Texas, offering to acquire the Company for \$32.00 per share in cash. The proposal is preliminary in nature and subject to a number of contingencies and uncertainties. Under the terms of the agreement with ONEOK, as a result of certain preliminary determinations made by the Board of Directors of the Company, the Board of Directors has authorized management to commence substantive discussions with Southern Union regarding its proposal. No assurances can be given that any agreement will be reached with Southern Union. The merger agreement with ONEOK remains in full force and effect.

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 1,209,000 residential, commercial, and industrial customers in geographically diverse portions of Arizona, Nevada, and California. There were 58,000 customers added to the system during 1998.

The table below lists the percentage of Southwest 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, 1998 | 84% | 5% | 11% |
| December 31, 1997 | 83 | 5 | 12 |
| December 31, 1996 | 80 | 6 | 14 |

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 on the Southwest system accounted for 48 percent of total system throughput in 1998. Although the volumes were significant, these customers provide a much smaller proportionate share of operating margin. In 1998, customers who utilized this service transported 100 million dekatherms.

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 Southwest 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, CPUC, and PUCN 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 North Lake Tahoe, California and various locations throughout northern Nevada).

Rates charged to customers vary according to customer class 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 of the Southwest service areas contain purchased gas adjustment (PGA) clauses which allow Southwest to file for rate adjustments as the cost of purchased gas changes. Generally, Southwest tariffs provide for annual adjustment dates for changes in purchased gas costs. However, Southwest may request to adjust its rates more often than once each year, if conditions warrant. These changes 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 PGA filings is included in the Rates and Regulatory Proceedings section of Management's Discussion and Analysis (MD&A), which is included in the 1998 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: | | | |
| Central and Southern..... | General rate case | November 1996 | September 1997 |
| California: | | | |
| Northern | Operational attrition | November 1997 | January 1998 |
| Nevada: | | | |
| Northern and Southern..... | General rate case | December 1995 | July 1996 |
| FERC: | | | |
| Paiute..... | General rate case | July 1996 | January 1997 |

RECENT REGULATORY AND LEGISLATIVE DEVELOPMENTS

Nevada

In 1997, the Nevada Legislature passed, and the Governor signed into law, Assembly Bill (AB) 366. AB 366 provides the statutory framework for restructuring both the natural gas and electric industries in the State of Nevada to allow competition. The legislature left most of the decision making on restructuring to the PUCN. In addition to several organizational changes, AB 366 required the PUCN to create an alternative plan of regulation by July 1, 1998. The PUCN issued two decisions during 1998. The first identified the distinct components of natural gas service. The second established a procedure by which parties may request that a service be classified as "potentially competitive." Once a service has been considered potentially competitive and the PUCN has authorized other companies to provide service under an alternative plan of regulation, Southwest could continue to provide service under its regulated rates, or set up a new subsidiary and file for an affiliate to offer service. The details of the PUCN restructuring plan are not fully developed at this time. Also remaining are numerous issues such as unbundling rates, licensing of alternative sellers, the utility's obligation to serve, and recovery of stranded costs.

California

In January 1998, the CPUC opened a rulemaking proceeding designed to reform the California natural gas industry by expanding opportunities for residential and small commercial customers to have access to competing natural gas suppliers. To accomplish this, the CPUC requested comments from interested parties, such as Southwest, to assess the current market and regulatory framework for the California natural gas industry and to develop reforms which emphasize market-oriented policies to benefit all California natural gas consumers. Southwest filed written comments with the CPUC in February 1998 addressing such issues as regulatory streamlining, unbundling, consumer protection and other competitive issues. The CPUC Division of Strategic Planning recommended that gas utilities fully unbundle services and exit the gas merchant (gas supply) business.

The CPUC established working groups to address safety concerns associated with introducing competition in providing billing, metering, and services on the customer side of the meter, and to develop consistency in policies, programs, tariffs, rules, and procedures used by gas utilities throughout the state. Reports from the working groups were submitted in August 1998.

While the CPUC initially adopted an aggressive timetable for restructuring the gas industry, legislation was enacted late in 1998 delaying the CPUC ability to restructure the gas industry for residential customers until 2000 and requiring the CPUC to report to the legislature whether such restructuring is in the public interest. The CPUC will continue to hold hearings and take evidence in preparation for the report to the legislature regarding natural gas restructuring.

Arizona

Southwest agreed, as part of the 1997 Arizona rate case settlement, to expand the eligibility for customers to qualify for transportation service. Southwest also supported a proposal to open an investigation to address competition in the natural gas industry, including the unbundling of rates and services, which was filed in May 1998 by a potential competitor of Southwest. No action has been taken on this proposal to date. In July 1998, Southwest filed a proposal that would provide all customers with the option of choosing their own gas suppliers by January 2000. The proposal was suspended into 1999 to allow gas marketers and other interested parties additional time to study the proposal.

In May 1998, the Arizona Legislature approved House Bill 2663 (Bill), providing for electric generation service competition and confirming the authority of the ACC to open the service territories of the electric companies within the state to competition. The customer choice provisions of the Bill directed that during the initial construction of a residential structure, electric and natural gas facilities, at a minimum, shall be installed in and to the structure in a manner that provides the retail energy consumer with the capability to choose between electricity and natural gas as an energy source for each appliance application. Therefore, as a result of this provision of the Bill, Southwest and other natural gas utilities in the state of Arizona are assured that a natural gas option is available to all future customers.

COMPETITION

Electric utilities are Southwest's principal competitors 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. Southwest has been successful in retaining these customers by setting rates at levels competitive with alternative energy sources such as electricity, fuel oils, and coal. As a result, management does not anticipate any material adverse impact on its operating margin from fuel switching.

Southwest continues to compete with interstate transmission pipeline companies, such as El Paso Natural Gas Company (El Paso), Kern River Gas Transmission Company (Kern River), and Tuscarora Gas Transmission Company, to provide service to 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 maintained an intensive effort to mitigate these competitive threats through the use of discounted transportation contract rates, special long-term contracts with electric generation and cogeneration customers, and new tariff programs. One such program provides an opportunity for potential bypass customers in Arizona to purchase natural gas-related services as a bundled package, including the procurement of gas supply. Southwest enters into gas

supply contracts for eligible customers, which are not included in its system supply portfolio, and provides nomination and balancing services on behalf of the customer. This program, as well as other competitive response initiatives and otherwise competitive rates, has helped mitigate the financial impact from the threat of bypass and the potential loss of margin currently earned from large customers.

DEMAND FOR NATURAL GAS

Deliveries of natural gas by Southwest are made under a priority system established by each regulatory commission having jurisdiction over Southwest. The priority system is intended to ensure that the gas requirements of higher-priority customers, primarily residential customers and nonresidential 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. Southwest maintains no backlog on its orders for gas service.

Natural gas vehicles (NGVs) represent a nontraditional source of demand for natural gas. Southwest encourages the use of NGVs throughout its service territories. As of December 31, 1998, there were 48 public- and nonpublic-access fueling stations and approximately 5,500 NGVs in use throughout Southwest service territories. As more public fueling stations come on-line and stricter vehicle emission standards are adopted, the demand for NGVs should increase.

NATURAL GAS SUPPLY

Southwest is responsible to acquire (purchase) and arrange delivery of (transport) natural gas to its system for all sales customers. Southwest believes that natural gas supplies and pipeline capacity for transportation will remain plentiful and readily available.

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, including suppliers on the spot market and those who provide firm supplies over short-term and longer-term durations. During 1998, Southwest acquired gas supplies from approximately 70 suppliers. This practice provides security against nonperformance by any one supplier.

Balancing firm supply assurances against the associated costs dictates a continually changing natural gas purchasing mix within the supply portfolios. The current purchasing strategy of Southwest primarily involves competitively-bid firm volumetric contracts with variable or index-based pricing. This strategy allows Southwest to acquire gas at current market prices but can result in 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 and help mitigate the regulatory risk of a gas cost disallowance during periods of rising prices. Any such change would be undertaken only with regulatory commission authorization.

Natural gas prices have historically demonstrated seasonal volatility with higher prices in the heating season and lower prices during the summer or off-peak consumption period. The latter part of 1996 and early 1997 witnessed particularly steep price increases, whereas the two most recent winter periods experienced more typical seasonal price volatility.

Gas supplies for the Southwest southern system (Arizona, southern Nevada, and southern California properties) are primarily obtained from producing regions in 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, Kern River, Northwest Pipeline Corporation, and Southern California Gas Company. Supply and pipeline capacity availability on both short- and long-term bases are continually monitored by Southwest to ensure the continued reliability of service to its customers. Southwest currently receives firm transportation service, both on a short- and long-term basis, for all of its service territories on the four pipeline systems noted above, and has interruptible contracts in place that allow additional capacity to be acquired as needed.

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. While firm contracts provide stability and guaranteed rights to capacity, they are generally a more expensive alternative.

Southwest continues to evaluate natural gas storage as an option to enable it to take advantage of seasonal price differentials in obtaining natural gas from a variety of sources to meet the growing demand of its 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 to comply with stricter environmental standards.

EMPLOYEES

At December 31, 1998, the natural gas operations segment had 2,429 regular full-time equivalent employees. Southwest believes it has a good relationship with its employees. No employees are represented by a union.

Reference is hereby made to Item 10 in Part III of this report on Form 10-K for information relative to the executive officers of the Company.

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 meter. 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. 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 gas 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 1998, more than 89 percent of revenue was earned under unit price contracts. As of December 31, 1998 no significant backlog exists with respect to outstanding construction contracts.

Competition within the industry is limited to several regional competitors in what can be characterized as a largely fragmented industry. Northern currently operates in approximately 15 major markets nationwide. Its customers are the primary LDCs in those markets. Construction companies typically depend on a few customers for their business. During 1998, Southwest accounted for 32 percent of Northern revenues. No other customers contributed more than 10 percent of revenues.

Employment fluctuates between seasonal construction periods, which are normally heaviest in the summer and fall months. At December 31, 1998, Northern had 1,267 regular full-time equivalent employees. Employment peaked in November 1998 when there were 1,621 employees. The majority of the employees are represented 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 two to three years. Field location facilities consist of a small building for repairs and acreage to store equipment.

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, and vehicles 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 and a portion of the corporate headquarters office complex located in Las Vegas, Nevada. Total gas plant, exclusive of leased property, at December 31, 1998, was \$2.1 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 of Southwest 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 grantors' elections.

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 map below 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.

[MAP]

[THE FOLLOWING TEXT TO BE INSERTED IN EDGAR VERSION ONLY]

[DESCRIPTION: Map of Arizona, Nevada, and California indicating the location of Southwest service areas. Service areas in Arizona include most of the central and southern areas of the state including Phoenix, Tucson, Yuma, and surrounding communities. Service areas in northern Nevada include Carson City, Yerington, Fallon, Lovelock, Winnemucca, and Elko. Service areas in southern Nevada include the Las Vegas valley (including Henderson and Boulder City) and Laughlin. Service areas in southern California include Barstow, Big Bear, Needles, and Victorville. Service areas in northern California include the north shore of Lake Tahoe and portions of Truckee. Companies providing gas transportation services for the Company are indicated by showing the location of their pipelines. Major transporters include El Paso Natural Gas Company, Kern River Gas Transmission Company, Northwest Pipeline Corporation, and Southern California Gas Company. The location of the Paiute Pipeline Company transmission pipeline (extending from the Idaho/Nevada border to the Reno/Tahoe area) and Southwest's pipeline (extending from Laughlin/Bullhead City to the Las Vegas valley) are indicated. The LNG facility is located near Lovelock, Nevada.]

The information appearing in Part I, Item 1, pages 6 and 7 with respect to the construction services segment is incorporated herein by reference.

ITEM 3. LEGAL PROCEEDINGS

The Company has been named as defendant in various legal proceedings. The ultimate dispositions of these proceedings are not presently determinable; however, it is the opinion of management that no litigation to which the Company is subject will have a material adverse impact on its financial position or results of operations.

On December 16, 1998, Arthur Klein, a purported shareholder of the Company, filed a Complaint in the Superior Court of the State of California in San Diego County (Case No. 726615) against the Company and its directors alleging one cause of action for breach of fiduciary duty. The plaintiff alleges that the consideration for the proposed merger with ONEOK is unfair and inadequate because the Company's Board of Directors approved the definitive agreement with ONEOK without conducting any auction or using another "market check" mechanism. Plaintiff is proposing to represent a class of all shareholders of the Company (excluding defendants and their affiliates and families). On March 22, 1999, the plaintiff filed an Amended Complaint in which he alleges causes of action for breach of fiduciary duty of loyalty and due care and breach of duty of candor. By his Amended Complaint, plaintiff seeks

- * to enjoin the merger with ONEOK,
- * to rescind the definitive agreement with ONEOK,
- * to implement an auction of the Company or similar process,
- * to void the \$30 million termination fee in the definitive agreement with ONEOK in the event the definitive agreement with ONEOK is terminated, the Company's Board of Directors recommends another transaction, such as the merger proposed by Southern Union Company, or in other similar circumstances, and
- * unspecified damages.

The court has ordered the parties to conduct limited discovery and set a preliminary injunction schedule, which, if followed, would result in a telephonic ruling on plaintiff's motion for a preliminary injunction in May 1999.

The Company believes that it has valid defenses to plaintiff's claims.

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 15, 1999, there were 24,186 holders of record of common stock, and the market price of the common stock was \$27. The quarterly market price of and dividends on Company common stock required by this item are included in the 1998 Annual Report to Shareholders and are incorporated herein by reference.

ITEM 6. SELECTED FINANCIAL DATA

Information required by this item is included in the 1998 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 1998 Annual Report to Shareholders and is incorporated herein by reference.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

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 1998 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. The names of the members of the Board of Directors, the principal occupation of each member and his or her employer for the last five years or longer, and the principal business of the corporation or other organization, if any, in which such occupation or employment is carried on, follow.

GEORGE C. BIEHL
Senior Vice President, Chief Financial Officer & Corporate Secretary
Southwest Gas Corporation

Director Since: 1998
Board Committees: Finance

Mr. Biehl, 51, joined the Company in 1990 as Senior Vice President and Chief Financial Officer after serving in a number of capacities with Deloitte Haskins & Sells (now Deloitte & Touche) for sixteen years and as chief financial officer for PriMerit Bank for the five years before joining the Company. He also assumed the responsibilities as Corporate Secretary for the Company in 1996. Mr. Biehl graduated from Ohio State University with a degree in accounting and earned his MBA with an emphasis in finance from Columbia University. He is a licenced CPA in several states and is a member of the American Institute of Certified Public Accountants. He is also a member of the Las Vegas Chamber of Commerce Leadership Las Vegas Program, and serves on the finance committees of several trade association groups.

MANUEL J. CORTEZ
 President and Chief Executive Officer
 Las Vegas Convention and Visitors Authority

Director Since: 1991
 Board Committees: Audit (Chairman), Compensation, Pension Plan Investment

Mr. Cortez, 60, served four terms (1977-1990) on the Clark County Commission and is a former chairman of the Commission. He has been active on various boards, including the Environmental Quality Policy Review Board, the Las Vegas Valley Water District Board of Directors, and the University Medical Center Board of Trustees, and served as chairman of the Liquor and Gaming Licensing Board and the Clark County Sanitation District. He has also held leadership roles with numerous civic and charitable organizations such as Boys and Girls Clubs of Clark County, Lied Discovery Childrens Museum, and Boys Town. Currently, Mr. Cortez holds professional memberships in the American Society of Association Executives, the Professional Convention Managers Association, the International Association of Convention and Visitors Bureaus, the American Society of Travel Agents, and is on the board of directors for the Travel Industry Association of America.

LLOYD T. DYER
 Retired President and Chief Executive Officer
 Harrah's

Director Since: 1978
 Board Committees: Executive, Compensation (Chairman), Nominating

Mr. Dyer, 71, obtained a degree in banking and finance from the University of Utah prior to his employment with Harrah's, a hotel/gaming corporation with its principal facilities in Reno and Lake Tahoe, in 1957. He was elected president and chief operating officer of Harrah's in 1975, and elected president and chief executive officer in 1978. He remained in those positions with Harrah's until his retirement in April 1980. Mr. Dyer is a trustee of the William F. Harrah Trusts.

THOMAS Y. HARTLEY
 Chairman of the Board, Southwest Gas Corporation
 President and Chief Operating Officer, Colbert Golf Design and Development

Director Since: 1991
 Board Committees: Executive (Chairman), Compensation, Nominating

Mr. Hartley, 65, obtained his degree in business from Ohio University in 1955, and was employed in various capacities by Deloitte Haskins & Sells (now Deloitte & Touche) from 1959 until his retirement as an area managing partner in 1988. He joined Southwest Gas Corporation as Director in 1991 and was elected Chairman of the Board of Directors in 1997. Mr. Hartley is actively involved in numerous business and civic activities. He is a past chairman of the UNLV Foundation and the Nevada Development Authority, and past president of the Las Vegas Founders Club. He has also held voluntary executive positions with the Las Vegas Founders Golf Foundation, the Las Vegas Chamber of Commerce, and the Boulder Dam Area Council of the Boy Scouts of America. He is a director of Sierra Health Services, Inc. and AmeriTrade Holdings Corporation.

MICHAEL B. JAGER
Private Investor

Director Since: 1989
Board Committees: Audit, Finance, Pension Plan Investment (Chairman)

Mr. Jager, 67, obtained a degree in petroleum geology from Stanford University in 1955. After a four-year employment with the Richfield Oil Corporation as a petroleum geologist, he joined Frank H. Ayres & Son Construction Company and was involved in the construction of subdivisions and homes in southern California until 1979. Since that time he has consulted in the single family residential development industry, and owns and manages a number of businesses in Nevada.

LEONARD R. JUDD
Former President, Chief Operating Officer, and Director
Phelps Dodge Corporation

Director Since: 1988
Board Committees: Executive, Compensation, Nominating (Chairman)

Mr. Judd, 60, former president, chief operating officer, and director of Phelps Dodge Corporation, joined Phelps Dodge in 1963 and worked at that company's operations in Arizona, New Mexico, and New York City. He was elected to the Phelps Dodge board of directors in 1987, president of Phelps Dodge Mining Company in 1988, and became president and chief operating officer of Phelps Dodge in 1989. He remained in those positions until the end of 1991. Mr. Judd is a member of various professional organizations and is active in numerous civic groups. He serves as a director of Morrison-Knudsen Corporation.

JAMES J. KROPID
President of James J. Kropid Investments

Director Since: 1997
Board Committees: Executive, Compensation, Finance

Mr. Kropid, 61, received his undergraduate degree from DePaul University and participated in the executive development program at the University of Illinois. He joined Centel Corporation in 1961 and became president of its Central Telephone Company-Nevada/Texas division in 1987. In 1993, the Governor of Nevada appointed him to the position of general manager of the Nevada State Industrial Insurance System, a position in which he served for almost two years. He is currently president of his own investment company. Mr. Kropid holds executive and board positions with various civic and charitable organizations including the National Conference for Community and Justice (formerly known as the National Conference of Christians and Jews), Las Vegas YMCA, and the Boy Scouts of America. He was formerly a board member for the Nevada Development Authority, United Way of Southern Nevada, and treasurer of St. Jude's Ranch for Children. He is a director of the Golf Company of Nevada.

MICHAEL O. MAFFIE
 President and Chief Executive Officer
 Southwest Gas Corporation

Director Since: 1988
 Board Committees: Executive

Mr. Maffie, 51, joined the Company in 1978 as Treasurer after seven years with Arthur Andersen & Co. He was named Vice President/Finance and Treasurer in 1982, Senior Vice President and Chief Financial Officer in 1984, Executive Vice President in 1987, President and Chief Operating Officer in 1988, and President and Chief Executive Officer in 1993. He received his undergraduate degree in accounting and his MBA degree in finance from the University of Southern California. He serves as a director of Del Webb Corporation, Boyd Gaming Corporation, and Norwest Bank/Nevada Division. A member of various civic and professional organizations, he serves as chairman of the board of United Way of Southern Nevada and trustee and treasurer of the UNLV Foundation. He also is a director of the Pacific Coast Gas Association and the Institute of Gas Technology.

CAROLYN M. SPARKS
 Co-Founder
 International Insurance Services, Ltd.

Director Since: 1988
 Board Committees: Audit, Finance (Chairperson), Pension Plan Investment

Mrs. Sparks, 57, graduated from the University of California Berkeley in 1963, and with her husband, co-founded International Insurance Services, Ltd., in 1966 in Las Vegas. She served on the University and Community College System of Nevada Board of Regents from 1984 to 1996, and in 1991 was elected to a two-year term as chair of the Board of Regents. Mrs. Sparks is actively involved with numerous charitable and civic organizations, including founding and chairing the University Medical Center Foundation and the Children's Miracle Network Telethon. She is currently chair of the Nevada Children's Center Foundation and has been elected to the Foundation Boards of the University of Nevada Las Vegas and the Community College of Southern Nevada.

ROBERT S. SUNDT
 Retired President
 Sundt Corp.

Director Since: 1987
 Board Committees: Executive, Finance, Nominating, Pension Plan Investment

Mr. Sundt, 72, has been associated with Sundt Corp. in a variety of positions since 1948. He was named President of Sundt Corp. in 1983. He is now retired and has no continuing association with Sundt Corp. He is a member of the American Institute of Constructors, Consulting Constructors Council of America, and a life director of the Associated General Contractors of America. He was a member of the American Arbitration Association and has served as an arbitrator on disputes concerning the construction industry. He is a past member of the Construction Industry Presidents Forum. Mr. Sundt is affiliated with a number of community organizations and is past chairman of the Tucson Metropolitan Chamber of Commerce.

TERRANCE "TERRY" L. WRIGHT
 President and Chief Executive Officer
 Nevada Title Insurance Company

Director Since: 1997

Board Committees: Audit, Compensation, Pension Plan Investment

Mr. Wright, 49, received his undergraduate degree in business administration and his juris doctorate from DePaul University. He joined Chicago Title Insurance Company while in law school and after graduation remained with the company and eventually moved to the Las Vegas, Nevada office. In 1978, he acquired the assets of Western Title to form what is now known as Nevada Title Insurance Company. Mr. Wright is also associate general counsel for A.G. Spanos Enterprises, Inc., one of the nation's largest apartment complex builders. He is a member of the California and Illinois bar associations and is affiliated professionally with the Las Vegas Board of Realtors, Nevada Land Title Association, Las Vegas Executives, Opportunity Village, TPC board of governors, Young President's Organization, and is past-chairman of the Nevada Development Authority. Mr. Wright is also a trustee and an executive committee member of the UNLV Foundation.

(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 | 51 | President and Chief Executive Officer | 1994-Present |
| George C. Biehl | 51 | Senior Vice President/Chief Financial Officer and Corporate Secretary | 1996-Present |
| James P. Kane | 52 | Senior Vice President and Chief Financial Officer | 1994-1996 |
| | | Senior Vice President/Operations | 1997-Present |
| | | Vice President/Southern Arizona Division | 1994-1997 |
| James F. Lowman | 52 | Senior Vice President/Central Arizona Division | 1994-Present |
| Dudley J. Sondeno | 46 | Senior Vice President/Chief Knowledge and Technology Officer | 1994-Present |
| Edward S. Zub | 50 | Senior Vice President/Regulation and Product Pricing | 1996-Present |
| | | Vice President/Rates & Regulation | 1994-1996 |

(c) Identification of Certain Significant Employees. None.

(d) Family Relationships. None of the Directors or Executive Officers are related to any other either by blood, marriage or adoption.

(e) Business Experience. Information with respect to Directors is described in (a) above. 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 1998 all but one of the required reports were filed timely. The Form 4 listing acquisitions by Carolyn Sparks, as trustee and beneficiary of the Sparks Family Trust, of 4,000 shares of Common Stock was not filed timely. An amended Form 4 for Mrs. Sparks listing the August 1998 purchase was filed in January 1999.

ITEM 11. EXECUTIVE COMPENSATION

DIRECTORS COMPENSATION

Outside directors receive an annual retainer of \$24,000, plus \$1,000 for each Board of Directors or committee meeting attended. Committee chairpersons receive an additional \$500 for each committee meeting attended. The Chairman of the Board of Directors receives an additional \$50,000 annually for serving in that capacity. Directors who are full-time employees of the Company or its subsidiaries receive no additional compensation for service on the Board.

Each outside director received in May 1998, options to purchase 2,000 shares of the Common Stock under the provisions of the Option Plan. Under the terms of the Option Plan, each outside director is entitled to receive additional options to purchase 2,000 shares of the Common Stock on the date of each Annual Meeting during the ten-year term of the Option Plan. The purchase price for the options is the market price of the Common Stock on the date of the grant and will become exercisable, in increments over three years, commencing with the first anniversary of the grant. All options granted to the outside directors will expire ten years after the date of each grant. The Option Plan contains change in control provisions.

Outside directors may defer their compensation until retirement or termination of their status as directors. Any cash they receive from the cancellation of any outstanding options as a result of a change in control of the Company may also be deferred. At retirement or termination, amounts deferred will be paid out over 5, 10, 15, or 20 years. Amounts deferred receive interest at 150 percent of the Moody's Composite Bond Rate.

The Company also provides a retirement plan for its outside directors. With a minimum of 10 years of service, an outside director can retire and receive an annual benefit for life equal to the annual retainer, at retirement, for serving on the Company's Board. Directors who retire before age 65, after satisfying the minimum service obligation, will receive retirement benefits upon reaching age 65. Upon a change in control of the Company, each of the directors of the Company with at least eight years of service will be entitled to receive retirement benefits.

EXECUTIVE COMPENSATION

The following table provides compensation earned by the Company's Chief Executive Officer and each of the four most highly compensated executive officers of the Company, at year-end 1998, for the years ended December 31, 1998, 1997, and 1996.

SUMMARY COMPENSATION TABLE (1)

| NAME AND PRINCIPAL POSITION | YEAR | ANNUAL COMPENSATION | | | | LONG-TERM COMPENSATION | | | | |
|---|------|---------------------|------------|-------------|----------------------------------|--|---------------------|-------------------------|--------------------------------------|--|
| | | SALARY(\$) | BONUS (\$) | | OTHER ANNUAL COMPENSATION(\$) | AWARDS | | | PAYOUTS | |
| | | | UTILITY(2) | NON-UTILITY | | RESTRICTED STOCK AWARD(S) (\$)(2)(3)(4) | OPTIONS/ SARS(#) | LTIP PAYOUTS (\$) | ALL OTHER COMPENSATION (\$)(5) | |
| Michael O. Maffie President & C.E.O. | 1998 | 486,301 | 234,005 | 0 | 0 | 350,997 | 25,000 | N/A | 59,410 | |
| | 1997 | 462,192 | 132,015 | 0 | 0 | 198,022 | 25,000 | N/A | 54,036 | |
| | 1996 | 435,479 | 129,602 | 500,000 | 0 | 194,403 | 90,000 | N/A | 46,210 | |
| George C. Biehl Senior Vice President/ Chief Financial Officer & Corporate Secretary | 1998 | 225,425 | 72,385 | 0 | 0 | 108,577 | 7,500 | N/A | 19,830 | |
| | 1997 | 214,877 | 40,762 | 0 | 0 | 61,143 | 7,500 | N/A | 17,329 | |
| | 1996 | 204,773 | 40,324 | 200,000 | 0 | 60,485 | 30,000 | N/A | 13,700 | |
| Edward S. Zub Senior Vice President/ Regulation & Product Pricing | 1998 | 180,137 | 59,283 | 0 | 0 | 88,928 | 7,500 | N/A | 20,352 | |
| | 1997 | 160,729 | 56,871 | 0 | 0 | 47,807 | 7,500 | N/A | 16,583 | |
| | 1996 | 138,484 | 28,802 | 0 | 0 | 43,223 | 25,000 | N/A | 12,723 | |
| James F. Lowman Senior Vice President/ Central Arizona Division | 1998 | 169,116 | 54,136 | 0 | 0 | 81,206 | 3,750 | N/A | 13,702 | |
| | 1997 | 161,401 | 35,665 | 0 | 0 | 45,998 | 3,750 | N/A | 12,279 | |
| | 1996 | 154,015 | 29,336 | 0 | 0 | 44,004 | 15,000 | N/A | 10,316 | |
| Dudley J. Sondeno Senior Vice President/ Chief Knowledge & Technology Officer | 1998 | 167,616 | 53,669 | 0 | 0 | 80,514 | 6,250 | N/A | 14,218 | |
| | 1997 | 159,901 | 30,387 | 0 | 0 | 45,581 | 6,250 | N/A | 13,983 | |
| | 1996 | 152,529 | 29,952 | 0 | 0 | 44,928 | 25,000 | N/A | 11,209 | |

- (1) All compensation reflected in the Summary Compensation Table is reported on an earned basis for each fiscal year.
- (2) Utility bonuses and restricted stock awards earned for calendar years 1996, 1997, and 1998 were paid and awarded in 1997, 1998, and 1999, respectively. Restricted stock awards are paid in Common Stock following successful completion of a three-year restriction period.
- (3) Dividends equal to the dividends paid on the Common Stock will be accrued on the restricted stock during the restriction period.
- (4) The total number of restricted stock awards granted in 1996, 1997, and 1998, for calendar years 1995, 1996, and 1997, and their value based on the closing price of the Common Stock on the New York Stock Exchange on December 31, 1998, for the named executive officers are as follows:

| | Shares | Value |
|-------------|--------|-----------|
| | ----- | ----- |
| Mr. Maffie | 33,564 | \$893,642 |
| Mr. Biehl | 10,465 | 278,631 |
| Mr. Zub | 7,504 | 199,794 |
| Mr. Lowman | 7,737 | 205,998 |
| Mr. Sondeno | 7,777 | 207,063 |

- (5) The amounts shown in this column for each year consist of above-market interest on deferred compensation (in excess of 120 percent of the Applicable Federal Long-term Rate) and matching contributions under the Company's executive deferral plan. Under the plan, executive officers may defer up to 100 percent of their annual cash compensation. Interest on such deferrals is set at 150 percent of the Moody's Seasoned Corporate Bond Rate. As part of the plan, the Company provides matching contributions that parallel the contributions

made under the Company's 401(k) plan, which is available to all Company employees, equal to one-half of the deferred amount, up to six percent of their annual salary. The breakdown of this compensation for each named executive officer is as follows:

| | Above-market Interest ----- | Matching Contributions ----- |
|-------------|-----------------------------------|------------------------------------|
| Mr. Maffie | \$44,842 | \$14,568 |
| Mr. Biehl | 13,078 | 6,752 |
| Mr. Zub | 14,963 | 5,389 |
| Mr. Lowman | 8,635 | 5,067 |
| Mr. Sondeno | 9,196 | 5,022 |

 OPTIONS/SARS GRANTED IN 1998

The following table sets forth the number of shares of the Company's Common Stock subject to stock options granted under the 1996 Stock Incentive Plan (Option Plan) to the named executive officers listed in the Summary Compensation Table during 1998, together with related information.

OPTION/SAR GRANTS IN LAST FISCAL YEAR

| NAME | INDIVIDUAL GRANTS | | | | POTENTIAL REALIZABLE VALUE AT ASSUMED ANNUAL RATES OF STOCK PRICE APPRECIATION FOR OPTION TERM (2) | |
|-------------------|--|---|---|--------------------|---|------------|
| | NUMBER OF SECURITIES UNDERLYING OPTIONS/SARS GRANTED (#) (1) | PERCENT OF TOTAL OPTIONS/SARS GRANTED TO EMPLOYEES IN FISCAL YEAR | EXERCISE OR BASE PRICE (\$/SH) | EXPIRATION DATE | 5 PERCENT | 10 PERCENT |
| Michael O. Maffie | 25,000 | 25.00 | \$23.06 | 7/20/08 | \$363,234 | \$916,734 |
| George C. Biehl | 7,500 | 7.50 | 23.06 | 7/20/08 | 108,970 | 275,020 |
| Edward S. Zub | 7,500 | 7.50 | 23.06 | 7/20/08 | 108,970 | 275,020 |
| James F. Lowman | 3,750 | 3.75 | 23.06 | 7/20/08 | 54,485 | 137,510 |
| Dudley J. Sondeno | 6,250 | 6.25 | 23.06 | 7/20/08 | 90,809 | 229,184 |

(1) Forty percent of the options become exercisable one year after the grant. Thirty percent of the options become exercisable two years after the grant, with the remaining becoming exercisable on the third anniversary of the grant.

(2) The 5 percent and 10 percent growth rates for the period ending July 20, 2008, which were determined in accordance with the rules of the SEC, illustrate that the potential future value of the granted options is linked to future increases in growth of the price of the Common Stock. Because the exercise price for the options equals the market price of the Common Stock on the date of the grant, there will be no gain to the named executive officers without an increase in the stock price. The 5 percent and 10 percent growth rates are for illustration only and are not intended to be predictive of future growth.

OPTIONS/SAR EXERCISES AND YEAR-END VALUES

Shown below is information with respect to unexercised options granted under the Option Plan to the named executive officers and held by them at December 31, 1998.

AGGREGATED OPTION/SAR EXERCISES IN 1998 AND
YEAR-END OPTION/SAR VALUES

| NAME | NO. OF SHARES ACQUIRED ON EXERCISE | VALUES REALIZED | NO. OF SECURITIES UNDERLYING UNEXERCISED OPTIONS/SARS AT DECEMBER 31, 1998 | | VALUE OF UNEXERCISED IN-THE-MONEY OPTIONS/SARS AT DECEMBER 31, 1998 (1) | |
|-------------------|--|--------------------|---|------------------|--|-------------------|
| | | | EXERCISABLE | UNEXERCISABLE(2) | EXERCISABLE | UNEXERCISABLE (2) |
| Michael O. Maffie | 0 | \$0 | 73,000 | 67,000 | \$807,375 | \$515,438 |
| George C. Biehl | 0 | 0 | 24,000 | 21,000 | 266,625 | 165,094 |
| Edward S. Zub | 0 | 0 | 20,500 | 19,500 | 225,938 | 147,656 |
| James F. Lowman | 0 | 0 | 12,000 | 10,500 | 133,313 | 82,547 |
| Dudley J. Sondeno | 0 | 0 | 20,000 | 17,500 | 222,188 | 137,578 |

(1) Represents the difference between the exercise prices for in-the-money options and the closing price of \$26.63 for the Company's Common Stock on the New York Stock Exchange on December 31, 1998, times the number of in-the-money options.

(2) Unexercisable options are those options which have been granted but cannot yet be exercised due to the Code restrictions on the value of incentive options, restrictions incorporated into the Option Plan, and the specific option agreements.

BENEFIT PLANS

Southwest Gas Basic Retirement Plan. The named executive officers participate in the Company's non-contributory, defined benefit retirement plan, which is available to all employees of the Company and its subsidiaries (other than Northern Pipeline Construction Co.). Benefits are based upon an employee's years of service, up to a maximum of 30 years, and the employee's highest 5 consecutive years salary, excluding bonuses, within the final 10 years of service.

PENSION PLAN TABLE (1)

| ANNUAL COMPENSATION | YEARS OF SERVICE | | | | |
|------------------------|------------------|----------|-----------|----------|----------|
| | 10 | 15 | 20 | 25 | 30 (2) |
| \$50,000 | \$ 8,750 | \$13,125 | \$ 17,500 | \$21,875 | \$26,250 |
| 100,000 | 17,500 | 26,250 | 35,000 | 43,750 | 52,500 |
| 150,000 | 26,250 | 39,375 | 52,500 | 65,625 | 78,750 |
| 200,000 | 35,000 | 52,500 | 70,000 | 87,500 | 105,000 |
| 250,000 | 43,750 | 65,625 | 87,500 | 109,375 | 131,250 |
| 300,000 | 52,500 | 78,750 | 105,000 | 131,250 | 157,500 |
| 350,000 | 61,250 | 91,875 | 122,500 | 153,125 | 183,750 |
| 400,000 | 70,000 | 105,000 | 140,000 | 175,000 | 210,000 |
| 450,000 | 78,750 | 118,125 | 157,500 | 196,875 | 236,250 |
| 500,000 | 87,500 | 131,250 | 175,000 | 218,750 | 262,500 |
| 550,000 | 96,250 | 144,375 | 192,500 | 240,625 | 288,750 |
| 600,000 | 105,000 | 157,500 | 210,000 | 262,500 | 315,000 |

- (1) For 1999, the maximum annual compensation that can be considered in determining benefits under the Plan is \$160,000. For future years the maximum annual compensation will be adjusted to reflect changes in the cost of living as established by the Internal Revenue Service.
- (2) Years of service beyond 30 years will not increase benefits under the basic retirement plan.

Compensation covered under the basic retirement plan is based on salary depicted in the Summary Compensation Table. As of December 31, 1998, the credited years of service for the named executive officers shown in the Summary Compensation Table are as follows: Mr. Maffie, 20 years; Mr. Biehl, 13 years; Mr. Zub, 20 years; Mr. Lowman, 29 years; and Mr. Sondeno, 19 years.

Amounts shown in the pension plan table are straight life annuity amounts notwithstanding the availability of joint survivorship benefit provisions. Benefits paid under the basic and supplemental retirement plans are not reduced by any Social Security benefits received.

Supplemental Retirement Plan. The named executive officers also participate in the Company's supplemental retirement plan (SERP). Such officers with 10 or more years of service may retire at age 55 or older and will receive benefits under the SERP. Benefits from the SERP, when added to benefits received under the basic retirement plan, will equal 60 percent of each officer's highest 12-months of salary, as depicted in the Summary Compensation Table. For Mr. Maffie, compensation used to determine such benefits includes salary, cash bonuses other than the 1996 non-utility bonus, and the payment of restrictive stock awards depicted in the Summary Compensation Table. The cost to the Company for benefits under the SERP for any one of the named executive officers cannot generally be properly allocated or determined because of the overall plan assumptions and options available.

SEVERANCE AND CHANGE IN CONTROL ARRANGEMENTS

In July 1998, the Company amended the existing employment agreements with seven of its designated officers (including the named executive officers), and entered into change in control agreements with its remaining officers. The employment agreements generally provide for the payment, upon termination of employment by the Company without cause, as defined therein, of up to one and one-half years of the amount of total annual compensation (base salary, a predetermined level of incentive compensation and fringe benefits), and up to three years of total annual compensation for Mr. Maffie. The employment agreements further provide for the payment, upon the termination of employment for

"good reason," as defined therein, within two years following a change in control of the Company, of an amount equal to two to two and one-half times total annual compensation for each of these officers, other than Mr. Maffie who would receive three times total annual compensation. The change in control agreements for the other officers parallel the change in control provisions of the employment agreements.

Restricted stock awards, stock options, or stock appreciation rights will vest and become immediately exercisable upon a change in control. Benefits under the SERP will also vest and/or accelerate. If any payment under these agreements would constitute a "parachute payment" subject to excise tax under the Code, the officer will be entitled to an additional "gross-up" payment. The terms of these agreements are for 24 months for each of the officers, other than Mr. Maffie whose agreement is for 36 months. Each of the agreements will be automatically extended annually for successive one-year periods, unless canceled by the Company.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

The directors who served on the Company's Compensation Committee during 1998 were Lloyd T. Dyer (Chairman), Manuel J. Cortez, Thomas Y. Hartley, Leonard R. Judd, James J. Kropid, and James R. Lincicome. Director Kropid joined the committee after the retirement of James R. Lincicome at last year's Annual Meeting of Shareholders. Mr. Lincicome served on the committee during 1998 until his retirement in May 1998.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

(a) Security Ownership of Certain Beneficial Owners. A group of investment companies headed by Mario J. Gabelli reported in February 1999, that it owned 3,023,883 shares of the Common Stock (approximately 9.9 percent as of March 15, 1999). The Company has been advised that the investment companies hold the shares as investment advisors for other beneficial owners.

(b) Security Ownership of Management. The following table discloses all Common Stock of the Company beneficially owned by the directors and the executive officers of the Company, as of March 15, 1999.

| DIRECTOR/EXECUTIVE OFFICER ----- | NO. OF SHARES BENEFICIALLY OWNED (1) ----- | PERCENT OF OUTSTANDING COMMON STOCK (2) ----- |
|-------------------------------------|--|---|
| George C. Biehl | 49,220 (3)(4) | * |
| Manuel J. Cortez | 6,259 (5) | * |
| Lloyd T. Dyer | 8,881 (5)(6) | * |
| Thomas Y. Hartley | 17,630 (5)(7) | * |
| Michael B. Jager | 8,620 (5)(8) | * |
| Leonard R. Judd | 6,300 (5)(9) | * |
| James J. Kropid | 3,098 (10) | * |
| Michael O. Maffie | 134,276 (3)(11) | * |
| Carolyn M. Sparks | 10,820 (5)(12) | * |
| Robert S. Sundt | 9,300 (5)(13) | * |
| Terrance L. Wright | 1,714 (14) | * |
| James F. Lowman | 30,811 (15) | * |
| Dudley J. Sondeno | 33,392 (16) | * |
| Edward S. Zub | 38,893 (17) | * |
| Other Executive Officers | 70,560 (18) | * |
| Total | 429,774 ===== | 1.4 === |

- (1) The Common Stock holdings listed in this column include performance shares granted to the Company's executive officers under the Company's Management Incentive Plan (MIP) for 1996, 1997, and 1998 and exercisable options issued under the 1996 Stock Incentive Plan (Option Plan).
- (2) As of March 15, 1999, the directors and executive officers of the Company beneficially owned, including exercisable options and MIP performance shares, 429,774 shares, which represent 1.4 percent of the Company's outstanding shares. No individual officer or director owned more than 1 percent of the Common Stock.
- (3) Number of shares does not include 6,618 shares held by the Southwest Gas Corporation Foundation, which is a charitable trust. Messrs. Maffie and Biehl are trustees of the Foundation but disclaim beneficial ownership of said shares.
- (4) The holdings include 24,000 shares which Mr. Biehl has the right to acquire through the exercise of options under the Option Plan.
- (5) The holdings include 4,300 shares which the non-employee directors have the right to acquire through the exercise of options under the Option Plan.
- (6) Number of shares include 4,581 shares over which Mr. Dyer has shared voting and investment control with his spouse through a family trust.
- (7) Number of shares include 311 shares over which Mr. Hartley has shared voting and investment control with his spouse through a family trust.
- (8) Number of shares includes 2,320 shares over which Mr. Jager has shared voting and investment control with his spouse through a family trust and 2,000 shares held in trust for Mr. Jager's spouse, over which Mr. Jager has no control.
- (9) Number of shares includes 2,000 shares over which Mr. Judd has shared voting and investment control with his spouse.
- (10) The holdings include 1,464 shares which Mr. Kropid has the right to acquire through the exercise of options under the Option Plan and 1,634 shares over which he has shared voting and investment power with his spouse through a family trust. The family trust also holds 1,500 shares of Trust Originated Preferred Securities issued by the Company's financing subsidiary, Southwest Gas Capital I.
- (11) The holdings include 73,000 shares which Mr. Maffie has the right to acquire through the exercise of options under the Option Plan and 3,044 shares over which he has shared voting and investment control with his spouse.
- (12) Number of shares includes 5,000 shares over which Mrs. Sparks has shared voting and investment control with her spouse through a family trust and 1,520 shares held as joint tenants with her spouse.
- (13) Number of shares includes 5,000 shares over which Mr. Sundt has shared voting and investment control with his spouse.
- (14) The holdings include 1,464 shares which Mr. Wright has the right to acquire through the exercise of options under the Option Plan.
- (15) The holdings include 12,000 shares which Mr. Lowman has the right to acquire through the exercise of options under the Option Plan.

- (16) The holdings include 20,000 shares which Mr. Sondeno has the right to acquire through the exercise of options under the Option Plan.
- (17) The holdings include 20,500 shares which Mr. Zub has the right to acquire through the exercise of options under the Option Plan and 105 shares held solely by his spouse.
- (18) The holdings of other executive officers include 42,000 shares that can be acquired through the exercise of options under the Option Plan.

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(c) Changes in Control. In December 1998, the Company announced a definitive agreement to be acquired by ONEOK, Inc. See ITEM 1. BUSINESS.

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 1998 Annual Report to Shareholders under the following captions:

| | |
|--|----|
| Report of Independent Public Accountants..... | 39 |
| Consolidated Balance Sheets..... | 40 |
| Consolidated Statements of Income..... | 41 |
| Consolidated Statements of Cash Flows..... | 42 |
| Consolidated Statements of Stockholders' Equity..... | 43 |
| Notes to Consolidated Financial Statements..... | 44 |

(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 February 10, 1999, reporting summary financial information for the year ended December 31, 1998.

(c) See List of exhibits.

LIST OF EXHIBITS

| EXHIBIT NUMBER ----- | DESCRIPTION OF DOCUMENT ----- |
|----------------------------|---|
| 2.01(15) | Agreement between Southwest Gas Corporation, The Southwest Companies and PriMerit Bank, Federal Savings Bank, as sellers and Norwest Corporation as buyer, dated April 10, 1996, regarding sale of assets and liabilities of PriMerit Bank. |
| 2.02(24) | Agreement and Plan of Merger by and among ONEOK, Inc., Oasis Acquisition Corporation, and Southwest Gas Corporation dated as of December 14, 1998. |
| 3(i)(20) | Restated Articles of Incorporation, as amended. |
| 3(ii) | 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, with respect to 9% Series A and Series B and 8 3/4% Series C Debentures. |
| 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(16) | Indenture between the Company and Harris Trust and Savings Bank dated July 15, 1996, with respect to Debt Securities. |
| 4.07(17) | 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(19) | 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(11) | Amended and Restated Declaration of Trust of Southwest Gas Capital I. |

- 4.11(11) 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(10) Southwest Gas Capital I Preferred Securities Guarantee by the Company and Harris Trust and Savings Bank, dated as of October 31, 1995.
- 4.14(10) Form of Subordinated Debt Security (included in the First Supplemental Indenture included as Exhibit 4.16 hereto).
- 4.15(10) Subordinated Debt Securities Indenture between the Company and Harris Trust and Savings Bank, dated as of October 31, 1995.
- 4.16(10) 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 Amended and Restated Rights Agreement between the Company and Harris Trust Company, as Rights Agent, dated as of February 9, 1999.
- 4.20 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.
- 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(18) 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(9) Southwest Gas Corporation Executive Deferral Plan, amended and restated as of May 10, 1994.
- 10.07(14) Southwest Gas Corporation Directors Deferral Plan, together with first amendment dated March 5, 1996.
- 10.08(8) Southwest Gas Corporation Board of Directors Retirement Plan, amended and restated as of October 1, 1993.
- 10.09(22) Southwest Gas Corporation Management Incentive Plan, amended and restated January 1, 1995.

- 10.10(9) Southwest Gas Corporation Supplemental Retirement Plan, amended and restated as of May 10, 1994.
- 10.11(23) Form of Employment Agreement with Company Officers.
- 10.12(23) Form of Change in Control Agreement with Company Officers.
- 10.13(12) Merger Agreement among the Company and Northern Pipeline Construction Co., dated as of November 13, 1995.
- 10.14(13) Southwest Gas Corporation 1996 Stock Incentive Plan.
- 10.15(21) \$350 million Revolving Credit Agreement among the Company, Union Bank of Switzerland, et al., dated as of June 12, 1997.
- 12.01 Computation of Ratios of Earnings to Fixed Charges and Ratios of Earnings to Combined Fixed Charges and Preferred Stock Dividends of the Company.
- 13.01 Portions of 1998 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.
- 27.01 Financial Data Schedule (filed electronically only).

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- (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 June 30, 1994.
- (10) Incorporated herein by reference to the report on Form 10-Q for the quarter ended September 30, 1995.
- (11) Incorporated herein by reference to the report on Form 8-K dated October 26, 1995.
- (12) Incorporated herein by reference to the report on Form 10-K for the year ended December 31, 1995.

- (13) Incorporated herein by reference to the Proxy Statement dated May 30, 1996.
- (14) Incorporated herein by reference to the report on Form 10-Q for the quarter ended June 30, 1996.
- (15) Incorporated herein by reference to the report on Form 8-K dated July 19, 1996.
- (16) Incorporated herein by reference to the report on Form 8-K dated July 26, 1996.
- (17) Incorporated herein by reference to the report on Form 8-K dated July 31, 1996.
- (18) Incorporated herein by reference to the report on Form 10-Q for the quarter ended September 30, 1996.
- (19) Incorporated herein by reference to the report on Form 8-K dated December 30, 1996.
- (20) Incorporated herein by reference to the report on Form 10-Q for the quarter ended March 31, 1997.
- (21) Incorporated herein by reference to the report on Form 10-Q for the quarter ended June 30, 1997.
- (22) Incorporated herein by reference to the report on Form 10-K for the year ended December 31, 1997.
- (23) Incorporated herein by reference to the report on Form 10-Q for the quarter ended September 30, 1998.
- (24) Incorporated herein by reference to the report on Form 8-K dated December 14, 1998.

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 25, 1999

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

Senior Vice President,
 Chief Financial Officer and
 Corporate Secretary

March 25, 1999

 (George C. Biehl)

/s/ EDWARD A. JANOV

Vice President, Controller and
 Chief Accounting Officer

March 25, 1999

 (Edward A. Janov)

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 ----- (George C. Biehl) | Director, Senior Vice President, Chief Financial Officer and Corporate Secretary | March 25, 1999 |
| /s/ MANUEL J. CORTEZ ----- (Manuel J. Cortez) | Director | March 25, 1999 |
| /s/ LLOYD T. DYER ----- (Lloyd T. Dyer) | Director | March 25, 1999 |
| /s/ THOMAS Y. HARTLEY ----- (Thomas Y. Hartley) | Chairman of the Board of Directors | March 25, 1999 |
| /s/ MICHAEL B. JAGER ----- (Michael B. Jager) | Director | March 25, 1999 |
| /s/ LEONARD R. JUDD ----- (Leonard R. Judd) | Director | March 25, 1999 |
| /s/ JAMES J. KROPID ----- (James J. Kropid) | Director | March 25, 1999 |
| /s/ MICHAEL O. MAFFIE ----- (Michael O. Maffie) | Director, President and Chief Executive Officer | March 25, 1999 |
| /s/ CAROLYN M. SPARKS ----- (Carolyn M. Sparks) | Director | March 25, 1999 |
| /s/ ROBERT S. SUNDT ----- (Robert S. Sundt) | Director | March 25, 1999 |
| /s/ TERRANCE L. WRIGHT ----- (Terrance L. Wright) | Director | March 25, 1999 |

EXHIBITS INDEX

| EXHIBIT NUMBER ----- | DESCRIPTION OF DOCUMENT ----- |
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| 3(ii) | Amended Bylaws of Southwest Gas Corporation. |
| 4.19 | Amended and Restated Rights Agreement between the Company and Harris Trust Company, as Rights Agent, dated as of February 9, 1999. |
| 12.01 | Computation of Ratios of Earnings to Fixed Charges and Ratios of Earnings to Combined Fixed Charges and Preferred Stock Dividends of the Company. |
| 13.01 | Portions of 1998 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. |
| 27.01 | Financial Data Schedule (filed electronically only). |

BYLAWS
OF
SOUTHWEST GAS CORPORATION

ARTICLE I

Section 1. Principal Office

The principal office for the transaction of the business of the corporation is hereby fixed and located at 5241 Spring Mountain Road, in the City of Las Vegas, County of Clark, State of Nevada.

Section 2. Other Offices

Branch or subordinate offices may at any time be established by the Board of Directors at any place or places where the corporation is qualified to do business.

Section 3. Terminology

All personal pronouns used herein are employed in a generic sense and are intended and deemed to be neutral in gender.

ARTICLE II

MEETING OF SHAREHOLDERS

Section 1. Regular Meeting

Commencing in May, 1988, the regular annual meeting of the shareholders shall be held at the principal office of the corporation, or at such other place within or without the State of California as the officers of the corporation may deem convenient and appropriate, at 10 a.m. on the second Thursday of May of each year, if not a legal holiday, and if a legal holiday, then at 10 a.m. on the next succeeding business day, for the purpose of electing a Board of Directors and transacting such other business as properly may come before the meeting; provided, however, that the Board of Directors may, by resolution, establish a different date not more than 120 days thereafter if, in its sole discretion, it deems such postponement appropriate.

Section 2. Special Meetings

Except in those instances where a particular manner of calling a meeting of the shareholders is prescribed by law or elsewhere in these Bylaws, a special meeting of the shareholders may be called at any time by the Chief Executive Officer or other officers acting for him or by the Board of Directors, or by the holders of not less than one-third of the voting shares then issued and outstanding. Each call for a special meeting of the shareholders shall state the time, place, and the purpose of such meeting; if made by the Board of Directors, it shall be by resolution duly adopted by a majority vote and entered in the minutes; if made by an authorized officer or by the shareholders, it shall be in writing and signed by the person or persons making the same, and unless the office of Secretary be vacant, delivered to the Secretary. No business shall be transacted at a special meeting other than as is stated in the call and the notice based thereon.

Section 3. Notice of Regular and Special Meetings of the Shareholders

Notice of each regular and special meeting of the shareholders of the corporation shall be given by mailing to each shareholder a notice of the time, place and purpose of such meeting addressed to him at his address as it appears upon the books of the corporation. Each such notice shall be deposited in the United States Mail with the postage thereon prepaid at least ten days prior to the time fixed for such meeting. If the address of any such shareholder does not appear on the books of the corporation and his post office address is unknown to the person mailing such notices, the notice shall be addressed to him at the principal office of the corporation.

Section 4. Quorum

At any meeting of the shareholders, the presence in person or by proxy of the holders of a majority of the shares entitled to vote at any meeting shall constitute a quorum for the transaction of business, except when it is otherwise provided by law. Any regular or special meeting of the shareholders may adjourn from day to day or from time to time if, for any reason, there are not present in person or by proxy the holders of a majority of the shares entitled to vote at said meeting. Such adjournment and the reasons therefor shall be recorded in the minutes of the proceedings.

Section 5. Waiver of Notice

When all the shareholders of the corporation are present at any meeting, or when the shareholders not represented thereat give their written consent to the holding thereof at the time and place the meeting is held, and such written consent is made a part of the

records of such meeting, the proceedings had at such meeting are valid, irrespective of the manner in which the meeting is called or the place where it is held.

Section 6. Proper Business for Shareholder Meetings

1. At a meeting of the shareholders, only such business shall be proper as shall be brought before the meeting: (i) pursuant to the corporation's notice of meeting; (ii) by or at the direction of the Board of Directors of the corporation; or (iii) by any shareholder of the corporation who is a shareholder of record at the time of giving the notice provided for herein, who shall be entitled to vote at such meeting and who complies with the notice procedures set forth herein.

2. For business to be properly brought before a meeting by a shareholder pursuant to clause (iii) above, the shareholder must have given timely notice thereof in writing to the Secretary. To be timely as to an annual meeting of shareholders, a shareholder's notice must be received at the principal executive office of the corporation not less than 120 calendar days before the date of the corporation's proxy statement released to shareholders in connection with the previous year's annual meeting; provided however, that if the date of the meeting is changed by more than 30 days from the date of the previous year's meeting, notice by shareholder to be timely must be received no later than the close of business on the 10th day following the earlier of the day on which notice of the date of the meeting was mailed to shareholders or public disclosure of such date was made. To be timely as to a special meeting of shareholders, a shareholder notice must be received not later than the call of the meeting as provided for in Section 2 of this Article II. Such shareholder notice shall set forth as to each matter the shareholder proposes to bring before the meeting: (a) a brief description of and the reasons for proposing such matter at the meeting; (b) the name and address, as they appear on the corporation's books, and the name and address of the beneficial owner, if any, on whose behalf the proposal is made; (c) the class and number of shares of the corporation which are owned beneficially and of record by such shareholder of record and by the beneficial owner, if any, on whose behalf the proposal is made; and (d) any material interest of such shareholder of record and the beneficial owner, if any, on whose behalf the proposal is made, in such proposal.

3. Notwithstanding anything in these Bylaws to the contrary, no business shall be proper at a meeting unless brought before it in accordance with the procedures set forth herein.

Further, a shareholder shall also comply with all applicable requirements of the Securities Exchange Act of 1934, as amended, and the rules and regulations thereunder with respect to the matters set forth herein.

4. The Chairman of the Board of Directors of the corporation or the individual designated as chairman of the meeting shall, if the facts warrant, determine and declare to the meeting

that business was not properly brought before the meeting and in accordance with the procedures proscribed herein, and if the chairman should so determine, that any such business not properly brought before the meeting shall not be transacted.

5. Notwithstanding anything provided herein to the contrary, the procedures for submission of shareholder proposals have not expended, altered or affected in any manner, whatever rights or limitations may exist regarding the ability of a shareholder of the corporation to submit to a proposal for consideration by shareholders of the corporation under California or federal law.

ARTICLE III

BOARD OF DIRECTORS

Section 1. Number--Quorum

The business of the corporation shall be managed by a Board of Directors, whose number shall be not fewer than eleven (11) nor greater than fourteen (14), as the Board of Directors or the shareholders by amendment of these Bylaws may establish, provided, however, that a reduction in the authorized number of directors shall not remove any director prior to the expiration of his term of office, and provided further that the shareholders may, pursuant to law, establish a different and definite number of directors or different maximum and minimum numbers of directors by amendment of the Articles of Incorporation or by a duly adopted amendment to these Bylaws. A majority of the prescribed number of directors shall be necessary to constitute a quorum for the transaction of business. At a meeting at which a quorum is present, every decision or act of a majority of the directors present made or done when duly assembled shall be valid as the act of the Board of Directors, provided that a minority of the directors, in the absence of a quorum, may adjourn from day to day but may transact no business.

Section 2. Exact Number of Directors

The number of directors of the corporation is hereby established, pursuant to the provisions of Section 1 of this Article III, as eleven (11).

Section 3. Election and Term of Office

The directors shall be elected at each annual meeting of shareholders, but if any such annual meeting is not held, or the directors are not elected thereat, the directors may be elected at any special meeting of shareholders held for that purpose. All directors shall hold office until their respective successors are elected and qualified.

Section 4. Vacancies

Vacancies in the Board of Directors may be filled by a majority of the remaining directors, though they be less than a quorum, and each director so elected shall hold office until his successor is qualified following the election at the next annual meeting of the shareholders or at any special meeting of shareholders duly called for that purpose prior to such annual meeting. A vacancy shall be deemed to exist in case the shareholders (or the Board of Directors, within the provisions of Section 1 of this Article III) shall increase the authorized number of directors, but shall fail, for a period of thirty days from the effective date of such increase, to elect the additional directors so provided for, or in case the shareholders fail at any time to elect the full number of authorized directors. When one or more of the directors shall give notice to the Board of Directors of his or their resignation from said Board, effective at a future date, the Board of Directors shall have the power to fill such vacancy or vacancies to take effect when such resignation or resignations become effective. Each director so appointed shall hold office during the remainder of the term of office of the resigning director or directors or until their successors are appointed and qualify.

Section 5. First Meeting of Directors

Immediately following each annual meeting of shareholders, the Board of Directors shall hold a regular meeting for the purpose of organization, election of officers, and the transaction of other business. Notice of such meeting is hereby dispensed with.

Section 6. Regular Meetings

Commencing in 1991, the time for other regular meetings of the Board of Directors, when held, shall be 8 a.m. on the third Tuesday of January, July, September and November, the first Tuesday of March and the second Wednesday of May, unless a different schedule is established by a resolution of the Board. If any regular meeting date shall fall on a legal holiday, then the regular meeting date shall be the business day next following.

Section 7. Special Meetings

A special meeting of the Board of Directors shall be held whenever called by the Chief Executive Officer or other officer acting for him, or by three directors. Any and all business may be transacted at a special meeting. Each call for a special meeting shall be in writing, signed by the person or persons making the same, addressed and delivered to the Secretary, and shall state the time and place of such meeting.

Section 8. Notice of Regular and Special Meetings of the Directors

No notice shall be required to be given of any regular meeting of the Board of Directors,

but each director shall take notice thereof. Notice of each special meeting of the Board of Directors shall be given to each of the directors by: (i) mailing to each of them a copy of such notice at least five days; or (ii) delivering personally or by telephone, including voice messaging system or other system or technology designed to record and communicate messages, telegraph, facsimile, electronic mail or other electronic means such notice at least 48 hours, prior to the time affixed for such meeting to the address of such director as shown on the books of the corporation. If his address does not appear on the books of the corporation, then such notice shall be addressed to him at the principal office of the corporation.

Section 9. Waiver of Notice

When all the directors of the corporation are present at any meeting of the Board of Directors, however called or noticed, and sign a written consent thereto on the record of such meeting, or if the majority of the directors are present, and if those not present sign in writing a waiver of notice of such meeting, whether prior to or after the holding of such meeting, which waiver shall be filed with the Secretary of the corporation, the transactions of such meeting are as valid as if had at a meeting regularly called and noticed.

Section 10. Action by Unanimous Consent of Directors

Any action required or permitted to be taken by the Board of Directors may be taken without a meeting if all members of the Board shall individually or collectively consent in writing to such action. Such written consent or consents shall be filed with the minutes of the proceedings of the Board, and such action by written consent shall have the same force and effect as if approved or taken at a regular meeting duly held. Any certificate or other document which relates to action so taken shall state that the action was taken by unanimous written consent of the Board of Directors without a meeting, and that these Bylaws authorize the directors to so act.

Section 11. Telephonic Participation in Meetings

Members of the Board may participate in a meeting through use of conference telephone or similar communications equipment, so long as all members participating in such meeting can hear one another. Participation in a meeting pursuant to this section shall constitute presence in person at such meeting.

ARTICLE IV

POWERS OF DIRECTORS

Section 1. The directors shall have power:

1. To call special meetings of the shareholders when they deem it necessary, and they shall call a meeting at any time upon the written request of shareholders holding one-third of all the voting shares:
2. To appoint and remove at pleasure all officers and agents of the corporation, prescribe their duties, fix their compensation, and require from them as necessary security for faithful service;
3. To create and appoint committees, offices, officers and agents of the corporation, and to prescribe and from time to time change their duties and compensation, but no committee shall be created and no member appointed thereto except upon approval of a majority of the whole Board of Directors; and
4. To conduct, manage, and control the affairs and business of the corporation and to make rules and regulations not inconsistent with the laws of the State of California, or the Bylaws of the corporation, for the guidance of the officers and management of the affairs of the corporation.

ARTICLE V

DUTIES OF DIRECTORS

Section 1. It shall be the duty of the directors:

1. To cause to be kept a complete record of all their minutes and acts, and of the proceedings of the shareholders, and present a full statement at the regular annual meeting of the shareholders, showing in detail the assets and liabilities of the corporation, and generally the condition of its affairs. A similar statement shall be presented at any other meeting of the shareholders when theretofore required by persons holding at least one-half of the voting shares of the corporation;
2. To declare dividends out of the profits arising from the conduct of the business, whenever such profits shall, in the opinion of the directors, warrant the same;
3. To oversee the actions of all officers and agents of the corporation, see that their duties are properly performed; and
4. To cause to be issued to the shareholders, in proportion to their several interests, certificates of stock.

ARTICLE VI

OFFICERS

Section 1. The officers shall include a Chairman of the Board of Directors, a Chief Executive Officer, who may be designated Chairman, a President, a Secretary, a Treasurer, a Controller, and may include one or more Executive Vice Presidents, Senior Vice Presidents, Vice Presidents, Assistant Vice Presidents, Assistant Secretaries, and Assistant Treasurers. All such officers shall be elected by and hold office at the pleasure of the Board of Directors, provided that the Chief Executive Officer shall have authority to dismiss any other officer. Any director shall be eligible to be the Chairman of the Board of Directors and any two or more of such offices may be held by the same person, except that the Chief Executive Officer or President may not also hold the office of Secretary. Any officer may exercise any of the powers of any other officer in the manner specified in these Bylaws, as specified from time to time by the Board of Directors, and/or as specified from time to time by the Chief Executive Officer or senior officer acting in his or her absence or incapacity, and any such acting officer shall perform such duties as may be assigned to him or her.

ARTICLE VII

FEES AND COMPENSATION

Section 1. Directors shall be reimbursed for their expenses, and shall be compensated for their services as directors in such amounts as the Board may fix by resolution. Nothing herein contained shall be construed to preclude any director from serving the corporation in any other capacity as an officer, agent, employee, or otherwise, and receiving compensation therefor.

ARTICLE VIII

INDEMNIFICATION

Section 1. Indemnification of Directors and Officers

Each person who was or is a party or is threatened to be made a party to or is involved in any threatened, pending or completed action, suit or proceeding, formal or informal, whether brought in the name of the corporation or otherwise and whether of a civil, criminal, administrative or investigative nature (hereinafter a "proceeding"), by reason of the fact that he or she, or a person of whom he or she is the legal representative, is or was a director or officer of the corporation or is or was serving at the request of the corporation as a director, officer, employee or agent of another corporation or of a partnership, joint venture, trust or other enterprise, including service with respect to employee benefit plans, whether the basis of such proceeding is an alleged action or inaction in an official capacity or in any other capacity while serving as a director or officer, shall, subject to the terms of any agreement between the corporation and such person, be indemnified and held harmless by the corporation to the fullest extent permissible under California law and the corporation's Articles of Incorporation, against all costs, charges, expenses, liabilities and

losses (including attorneys' fees, judgments, fines, ERISA excise tax or penalties and amounts paid or to be paid in settlement) reasonably incurred or suffered by such person in connection therewith, and such indemnification shall continue as to a person who has ceased to be a director or officer and shall inure to the benefit of his or her heirs, executors and administrators; provided, however, that (a) the corporation shall indemnify any such person seeking indemnification in connection with a proceeding (or part thereof) initiated by such person only if such proceeding (or part thereof) was authorized by the Board of the corporation, (b) the corporation shall indemnify such person seeking indemnification in connection with a proceeding (or part thereof) other than a proceeding by or in the name of the corporation to procure a judgment in its favor only if any settlement of such a proceeding is approved in writing by the corporation, and (c) that no such person shall be indemnified (i) except to the extent that the aggregate of losses to be indemnified exceeds the amount of such losses for which the director or officer is paid pursuant to any directors' and officers' liability insurance policy maintained by the corporation; (ii) on account of any suit in which judgment is rendered against such person for an accounting of profits made from the purchase or sale by such person of securities of the corporation pursuant to the provisions of Section 16(b) of the Securities Exchange Act of 1934 and amendments thereto or similar provisions of any federal, state or local statutory law; (iii) if a court of competent jurisdiction finally determines that any indemnification hereunder is unlawful; (iv) for acts or omissions involving intentional misconduct or knowing and culpable violation of law; (v) for acts or omissions that the director or officer believes to be contrary to the best interests of the corporation or its shareholders or that involve the absence of good faith on the part of the director or officer; (vi) for any transaction for which the director or officer derived an improper personal benefit; (vii) for acts or omissions that show a reckless disregard for the director's or officer's duty to the corporation or its shareholders in circumstances in which the director or officer was aware, or should have been aware, in the ordinary course of performing his or her duties, of a risk of serious injury to the corporation or its shareholders; (viii) for acts or omissions that constitute an unexcused pattern of inattention that amounts to an abdication of the director's or officer's duties to the corporation or its shareholders; (ix) for costs, charges, expenses, liabilities and losses arising under Section 310 or 316 of the General Corporation Law of California (the "Law"); and (x) as to circumstances in which indemnity is expressly prohibited by Section 317 of the Law. The right to indemnification conferred in this Article shall be a contract right and shall include the right to be paid by the corporation expenses incurred in defending any proceeding in advance of its final disposition; provided, however, that if the Law requires the payment of such expenses incurred by a director or officer in his or her capacity as a director or officer (and not in any other capacity in which service was or is rendered by such person while a director or officer, including, without limitation, service to an employee benefit plan) in advance of the final disposition of a proceeding, such advances shall be made only upon delivery to the corporation of an undertaking, by or on behalf of such director or officer, to repay all amounts to the corporation if it shall be ultimately determined that such person is not entitled to be indemnified.

Section 2. Indemnification of Employees and Agents

A person who was or is a party or is threatened to be made a party to or is involved in any proceedings by reason of the fact that he or she is or was an employee or agent of the corporation or is or was serving at the request of the corporation as an employee or agent of another enterprise, including service with respect to employee benefit plans, whether the basis of such action is an alleged action or inaction in an official capacity or in any other capacity while serving as an employee or agent, may, subject to the terms of any agreement between the corporation and such person, be indemnified and held harmless by the corporation to the fullest extent permitted by California law and the corporation's Articles of Incorporation, against all costs, charges, expenses, liabilities and losses (including attorneys' fees, judgments, fines, ERISA excise taxes or penalties and amounts paid or to be paid in settlement), reasonably incurred or suffered by such person in connection therewith. The immediately preceding sentence is not intended to be and shall not be considered to confer a contract right on any employee or agent (other than directors and officers) of the corporation.

Section 3. Right of Directors and Officers to Bring Suit

If a claim under Section 1 of this Article is not paid in full by the corporation within 30 days after a written claim has been received by the corporation, the claimant may at any time thereafter bring suit against the corporation to recover the unpaid amount of the claim and, if successful in whole or in part, the claimant shall also be entitled to be paid the expense of prosecuting such claim. Neither the failure of the corporation (including its Board, independent legal counsel, or its shareholders) to have made a determination prior to the commencement of such action that indemnification of the claimant is permissible in the circumstances because he or she has met the applicable standard of conduct, if any, nor an actual determination by the corporation (including its Board, independent legal counsel, or its shareholders) that the claimant has not met the applicable standard of conduct, shall be a defense to the action or create a presumption for the purpose of an action that the claimant has not met the applicable standard of conduct.

Section 4. Successful Defense

Notwithstanding any other provision of this Article, to the extent that a director or officer has been successful on the merits or otherwise (including the dismissal of an action without prejudice or the settlement of a proceeding or action without admission of liability) in defense of any proceeding referred to in Section 1 or in defense of any claim, issue or matter therein, he or she shall be indemnified against expenses (including attorneys' fees) actually and reasonably incurred in connection therewith.

Section 5. Non-Exclusivity of Rights

The right to indemnification provided by this Article shall not be exclusive of any other right which any person may have or hereafter acquire under any statute, bylaw, agreement, vote of shareholders or disinterested directors or otherwise.

Section 6. Insurance

The corporation may maintain insurance, at its expense, to protect itself and any director, officer, employee or agent of the corporation or another corporation, partnership, joint venture, trust or other enterprise against any expense, liability or loss, whether or not the corporation would have the power to indemnify such person against such expense, liability or loss under the law.

Section 7. Expenses as a Witness

To the extent that any director, officer, employee or agent of the corporation is by reason of such position, or a position with another entity at the request of the corporation, a witness in any action, suit or proceeding, he or she shall be indemnified against all costs and expenses actually and reasonably incurred by him or her on his or her behalf in connection therewith.

Section 8. Indemnity Agreements

The corporation may enter into agreements with any director, officer, employee or agent of the corporation providing for indemnification to the fullest extent permissible under the law and the corporation's Articles of Incorporation.

Section 9. Separability

Each and every paragraph, sentence, term and provision of this Article is separate and distinct so that if any paragraph, sentence, term or provision hereof shall be held to be invalid or unenforceable for any reason, such invalidity or unenforceability shall not affect the validity or unenforceability of any other paragraph, sentence, term or provision hereof. To the extent required, any paragraph, sentence, term or provision of this Article may be modified by a court of competent jurisdiction to preserve its validity and to provide the claimant with, subject to the limitations set forth in this Article and any agreement between the corporation and claimant, the broadest possible indemnification permitted under applicable law.

Section 10. Effect of Repeal or Modification

Any repeal or modification of this Article shall not adversely affect any right of indemnification of a director or officer existing at the time of such repeal or modification with respect to any action or omission occurring prior to such repeal or modification."

ARTICLE IX

CHAIRMAN OF THE BOARD

Section 1. If there shall be a Chairman of the Board of Directors, he shall, when present, preside at all meetings of the stockholders and the Board of Directors, and perform such other duties as the Bylaws or the Board of Directors shall require of him.

ARTICLE X

CHIEF EXECUTIVE OFFICER; OTHER EXECUTIVE OFFICERS

Section 1. The Board of Directors shall, at their first regular meeting, elect such officers as are required by Article VI hereof and such additional officers authorized by Article VI hereof as the Board, in its discretion, may choose to elect. If at any time the Chief Executive Officer shall be unable to act, the President (if there shall be one who is not also the Chief Executive Officer) shall act in his place and perform his duties; if the President or next most senior officer is unable to perform such duties, then the vice presidents, in such sequence as the Board of Directors may specify, shall act. If all the foregoing shall be unable to act, the senior officer among them shall appoint some other person in whom shall be vested, for the time being, all the duties and functions of Chief Executive Officer, to act until the Board of Directors can be convened and elect appropriate officers. The Chief Executive Officer (or person acting as such) shall:

1. Preside (if there shall be no Chairman of the Board of Directors or in his absence) over all meetings of the shareholders and directors;
2. Sign in behalf of the corporation contracts and other instruments in writing within the scope of his authority or if, when, and as directed so to do by the Board of Directors, but nothing herein shall limit the power of the Board of Directors to authorize such contracts and other instruments in writing to be signed by any other officer or person or limit the power of the Chief Executive Officer to delegate his authority in any such matter to another officer or other officers of the corporation. The Chief Executive Officer or any other officer specified by the Board of Directors may sign certificates of stock as provided in Article XIII hereof;
3. Delegate duties and responsibilities to any other officers and/or employees of the corporation in any manner not prohibited by these Bylaws or by the Board of Directors, and change such duties and responsibilities so delegated from time to time at will;
4. Call the directors together when he deems it necessary, and have, subject to the advice of the directors, direction of the affairs of the corporation; and

5. Generally discharge such other duties as may be required of him by the Bylaws of the corporation.

ARTICLE XI

SECRETARY

Section 1. The Board of Directors shall elect a Secretary:

1. It shall be the duty of the Secretary to keep a record of proceedings of the Board of Directors and of the shareholders, and to keep the corporate seal of the corporation. He shall be responsible for maintaining proper records showing the number of shares of stock of all classes and series issued and transferred by any shareholder, and the dates of such issuance and transfer;

2. Whenever it is provided in these Bylaws that notice shall be given either of regular or special meetings of the shareholders, regular or special meetings of the directors, or otherwise, such notice shall be given by the Secretary or by the Chief Executive Officer or by any person designated by either of them, or by any authorized person who shall have signed the call for such meeting. Any notice which the Secretary may give or serve, or act required to be done by him, may with like effect be given or served or done by or under the direction of an Assistant Secretary;

3. The Secretary shall discharge such other duties as pertain to his office or which may be prescribed by the Board of Directors.

ARTICLE XII

TREASURER

Section 1. The Treasurer shall receive and keep all the funds of the corporation and pay them out only on checks or otherwise, as directed by the Board of Directors; provided, however, that the Board of Directors may provide for a depository of the funds of the corporation, and may by resolution prescribe the manner in which said funds shall be drawn from said depository.

ARTICLE XIII

CERTIFICATES OF STOCK

Section 1. Certificates of stock shall be of such form and device as the Board of Directors may direct, and shall be signed by the genuine or facsimile signatures of the Chairman and

Chief Executive Officer or the President or any authorized Vice President and the Secretary or an Assistant Secretary. Each certificate shall express on its face its number, date of issuance, the number of shares for which and the person to whom it is issued, the kind of shares represented by said certificate, and such other matters as may be required by law. Certificates of stock may be issued prior to full payment, in harmony with all permits issued by regulatory authorities having jurisdiction in the premises, or as is otherwise allowed by law, but any certificate issued prior to full payment must show on its face what amount has been paid thereon.

ARTICLE XIV

TRANSFER OF STOCK

Section 1. Shares of stock of the corporation may be transferred at any time by the holders, or by power of attorney, or by their legal representative, by endorsement on the certificate of stock, but no transfer is valid until the surrender of the endorsed certificate. A surrendered certificate shall be delivered up for cancellation before a new one is issued in lieu thereof, and the Secretary shall preserve the certificate so canceled or a suitable record thereof. If, however, a certificate is lost or destroyed, the Board of Directors may order a new certificate issued as is by law required or permitted.

ARTICLE XV

VOTING

Section 1. At all corporate meetings, each shareholder, either in person or by proxy, shall be entitled to as many votes as he owns shares of stock; however, every shareholder entitled to vote at any election for directors shall have the right to cumulate his votes.

Section 2. Proxies

Every person entitled to vote or execute consents shall have the right to do so either in person or by one or more agents authorized by a written proxy executed by such person or his duly authorized agent and filed with the Secretary of the corporation; provided that no such proxy shall be valid after the expiration of eleven (11) months from the date of its execution, unless the person executing it specifies therein the length of time for which such proxy is to continue in force, which in no case shall exceed seven (7) years from the date of its execution.

ARTICLE XVI

INDEBTEDNESS

Section 1. The Board of Directors shall have power to incur indebtedness, and the terms and amount thereof shall be entered in the minutes. The Board of Directors shall have the power to secure said indebtedness, or any obligation or obligations of the corporation, by pledge, mortgage, deed of trust, or other security given upon any property owned by it or in which it has any interest.

ARTICLE XVII

REGISTRAR AND/OR TRANSFER AGENT

Section 1. The Board of Directors may designate and appoint one or more registrars and/or transfer agents for the registration of the stock of the corporation, and make such rules and regulations for the registrations of stock at the office of such registrars and/or transfer agents as may to the Board of Directors seem desirable. The corporation may act as its own transfer agent, at the direction of the Board of Directors. The Board of Directors may, in its discretion, fix a transfer fee for transfer of stock certificates.

ARTICLE XVIII

MISCELLANEOUS

Section 1. Meetings. Notice. When Conclusive.

An entry made in the minutes of the directors or shareholders, pursuant to resolution or recital, to the effect that the notice of such meeting required by these Bylaws to be given has been given, shall be conclusive upon the corporation, its directors, shareholders, and all other persons that such notice has been duly given in proper form and substance to the proper persons and for the requisite length of time.

ARTICLE XIX

SEAL

Section 1. The Board of Directors shall provide a suitable seal containing the name of the corporation, the years of its creation, and other appropriate words, and may alter the same at pleasure.

ARTICLE XX

AMENDMENTS TO BYLAWS

Section 1. Power of Shareholders

New Bylaws may be adopted or these Bylaws may be amended or repealed by the vote of shareholders entitled to exercise a majority of the voting power of the corporation or by the written assent of such shareholders, except as otherwise provided by law or by the Articles of Incorporation.

Section 2. Power of Directors

Subject to the right of the shareholders as provided in Section 1 of this Article XX to adopt, amend or repeal Bylaws, the Board of Directors may adopt, amend or repeal any of the Bylaws of this corporation, except that the powers of the Board of Directors to change, and/or establish the authorized number of directors of this corporation shall be as set forth in Article III of these Bylaws.

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I hereby certify that the foregoing is a full, true, and correct copy of the Bylaws of Southwest Gas Corporation, a California corporation, as in effect on the date hereof.

WITNESS my hand this 8th day of February, 1999.

George C. Biehl
Senior Vice President/Chief Financial
Officer and Corporate Secretary

BYLAWS
OF
SOUTHWEST GAS CORPORATION
(AS AMENDED 2/8/99)

SOUTHWEST GAS CORPORATION,
a California corporation

and

HARRIS TRUST COMPANY OF CALIFORNIA,
Rights Agent

AMENDED AND RESTATED RIGHTS AGREEMENT

Dated as of February 9, 1999

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AMENDED AND RESTATED RIGHTS AGREEMENT

AMENDED AND RESTATED RIGHTS AGREEMENT, dated as of February 9, 1999 between Southwest Gas Corporation, a California corporation (the "Company"), and Harris Trust Company of California, as Rights Agent.

W I T N E S S E T H

WHEREAS, the Board of Directors of the Company has authorized and declared the distribution of one right for (i) each share of Common Stock of the Company ("Common Stock") outstanding at the Close of Business (as hereinafter defined) on April 15, 1996 (the "Rights Record Date"), each right representing the right to purchase one Unit consisting, initially, of one one-hundredth of a share of Junior Participating Preference Stock, and (ii) each additional share of Common Stock which shall become outstanding between the Rights Record Date and the earliest of the Distribution Date, the Expiration Date (as such terms are hereinafter defined) and the date, if any, on which such rights may be redeemed, all upon the terms and subject to the conditions hereinafter set forth (each such right being hereinafter referred to as a "Right");

NOW, THEREFORE, the parties agree as follows:

Section 1. Certain Definitions.

(a) For purposes of this Agreement, the following terms have the meanings indicated:

"Acquiring Person" shall mean any Person who or which, alone or together with all Affiliates and Associates of such Person, shall be the Beneficial Owner (within the meaning of Section 1(b)) of a Substantial Block of Voting Stock, but shall not include (i) an Exempt Person or (ii) any Person who or which acquires a Substantial Block of Voting Stock in connection with a transaction or series of transactions approved prior to such transaction or transactions by the Board of Directors of the Company; provided that no person shall become an Acquiring Person solely as a result of a reduction in the number of shares of Voting Stock outstanding, unless and until such Person shall thereafter become the Beneficial Owner of additional shares constituting 1% or more of the general voting power of the Company.

"Affiliate" and "Associate" shall have the respective meanings ascribed to such terms in Rule 12b-2 of the General Rules and Regulations under the Exchange Act, as in effect as of the date hereof.

"Business Day" shall mean any day other than a Saturday, Sunday or day on which banking institutions in the States of California, New York or Nevada are authorized or obligated by law or executive order to close.

"Close of Business" on any given date shall mean 5:00 p.m., Las Vegas time, on such date; provided, however, that if such date is not a Business Day it shall mean 5:00 p.m., Las Vegas time, on the next succeeding Business Day.

"Common Stock" shall have the meaning assigned to it in the preamble; and "common stock" when used with reference to Persons other than the Company shall mean: (i) in the case of Persons organized in corporate form, the capital stock or equity security with the greatest voting power of such Person or, if such Person is a Subsidiary of another Person, of the Person or Persons which ultimately control such first-mentioned Person; and (ii) in the case of Persons not organized in corporate form, the units of beneficial interest which (A) represent the right to participate generally in the profits and losses of such Person (including without limitation any flow-through tax benefits resulting from an ownership interest in such Person) and (B) are entitled to exercise the greatest voting power of such Person or, in the case of a limited partnership, shall have the power to remove the general partner or partners.

"Distribution Date" shall have the meaning assigned to it in Section 3(a).

"Equivalent Stock" shall have the meaning assigned to it in Section 7(a).

"Exchange Act" shall mean the Securities Exchange Act of 1934, as amended from time to time.

"Exempt Person" shall mean the Company, any Subsidiary of the Company and any employee benefit plan or employee stock plan of the Company or of any Subsidiary of the Company, or any trust or other entity organized, established or holding shares of Common Stock by, for or pursuant to, the terms of any such plan.

"Expiration Date" shall have the meaning assigned to it in Section 7(a).

"Offer Date" shall have the meaning assigned to it in Section 3(a).

"Person" shall mean any individual, firm, corporation, partnership, limited liability company, association, group (as such term is used in Rule 13d-5 promulgated under the Exchange Act as in effect on the date hereof), trust or other entity and shall include any successor by merger (or otherwise) of any of the foregoing.

"Principal Party" shall have the meaning assigned to it in Section 13(b).

"Purchase Price" shall mean the price payable for one Unit upon exercise of a Right.

"Qualified Offer" shall mean a tender or exchange offer for all outstanding Common Stock at a price and on terms determined to be adequate and otherwise in the best interests of the Company and its shareholders (other than the Person or

an Affiliate or Associate thereof on whose behalf the offer is made) by at least a majority of the Directors who are not representatives of or affiliated with the Person making such offer or any Affiliate or Associate of such Person.

"Redemption Price" shall have the meaning assigned to it in Section 23(a).

"Right" shall have the meaning assigned to it in the preamble.

"Rights Record Date" shall have the meaning assigned to it in the preamble.

"Subject Shares" shall mean the class or series of shares then issuable on exercise of the Rights.

"Stock Acquisition Date" shall mean the date of the first public announcement by the Company or an Acquiring Person (which, for purposes of this definition, shall include, without limitation, a report filed pursuant to Section 13(d) under the Exchange Act) that an Acquiring Person has become such.

"Subsidiary" shall mean, with respect to any Person, a corporation or other entity the securities or other ownership interests of which having ordinary voting power sufficient to elect a majority of the board of directors or other persons performing similar functions are at the time directly or indirectly owned by such Person and any Affiliate of such Person.

"Substantial Block" shall mean a number of shares of Voting Stock having in the aggregate 20 percent or more of the general voting power.

"Trading Day" shall have the meaning assigned to it in Section 11(d).

"Unit" shall mean the shares or other securities issuable upon exercise of one Right, initially one one-hundredth of a share of Junior Participating Preference Stock of the Company having the rights and preferences set forth in Exhibit C, before any adjustment pursuant to Section 11(a)(ii) or Section 13.

"Voting Stock" shall mean shares of the Company's capital stock the holders of which have general voting power.

(b) For purposes of this Agreement, a Person shall be deemed the "Beneficial Owner" of any securities:

(i) which such Person or any of such Person's Affiliates or Associates beneficially owns, directly or indirectly;

(ii) which such Person or any of such Person's Affiliates or Associates has (A) the right to acquire (whether such right is exercisable immediately or only after the passage of time) pursuant to any agreement, arrangement or understanding, (whether or not in writing) or upon the exercise of any conversion, exchange or purchase rights

(other than the Rights), warrants or options, or otherwise; provided, however, that a Person shall not be deemed the "Beneficial Owner" of securities tendered pursuant to a tender or exchange offer made by or on behalf of such Person or any of such Person's Affiliates or Associates until such tendered securities are accepted for payment or exchange; or (B) the right to vote or to direct the voting of, pursuant to any agreement, arrangement or understanding (whether or not in writing); or (C) the right to dispose or to direct the disposition of, pursuant to any agreement, arrangement or understanding (whether or not in writing); or

(iii) which are beneficially owned, directly or indirectly, by any other Person with which such Person or any of such Person's Affiliates or Associates has any agreement, arrangement or understanding for the purpose of acquiring, holding, voting or disposing of any securities of the Company;

provided, however, that a Person shall not be deemed the Beneficial Owner of, or to Beneficially Own, any security if the agreement, arrangement or understanding to vote such security (1) arises solely from the grant of a revocable proxy or consent given to such Person in connection with a public proxy or consent solicitation made pursuant to, and in accordance with, the applicable rules and regulations under the Exchange Act, and (2) is not also then reportable on Schedule 13D (or any comparable or successor report) under the Exchange Act; provided, further, that a Person engaged in business as an underwriter of securities shall not be deemed the "Beneficial Owner" of securities acquired through such person's participation in good faith in a firm commitment underwriting until the expiration of the 40-day period immediately following the date of such acquisition.

Section 2. Appointment of Rights Agent. The Company hereby appoints the Rights Agent to act as agent for the Company and the holders of the Rights in accordance with the terms and conditions hereof, and the Rights Agent hereby accepts such appointment. The Company may from time to time appoint such Co-Rights Agent or Agents as it may deem necessary or desirable and determine the respective duties of the Rights Agent and the Co-Rights Agents.

Section 3. Issuance of Right Certificates.

(a) Until the Close of Business on the earlier of (i) the tenth Business Day after a Stock Acquisition Date or (ii) the tenth Business Day (or such later date as the Company's Board of Directors shall determine) after the date of the commencement by any Person (other than an Exempt Person) of, or the date of the first public announcement (such commencement date or announcement date being herein referred to as the "Offer Date") of the intent of any Person (other than an Exempt Person) to commence, a tender or exchange offer upon the successful consummation of which such Person, together with its Affiliates and Associates, would be the Beneficial Owner of 20 percent or more of the then outstanding Voting Stock (irrespective of whether any shares are actually purchased pursuant to such offer) (the tenth Business Day after the first to occur of a Stock Acquisition Date or an Offer Date being herein referred to as the "Distribution Date"),

(i) the Rights will automatically attach to, and be evidenced by, the certificates for Common Stock registered in the names of the holders of Common Stock (which certificates for Common Stock shall be deemed also to be Right Certificates) and not by separate Right Certificates, and

(ii) each Right will be transferable only in connection with the transfer of the underlying shares of Common Stock.

As soon as practicable after the Distribution Date, the Rights Agent will mail, by first-class, insured, postage prepaid mail, to each record holder of Common Stock as of the Close of Business on the Distribution Date, as shown by the records of the Company at the Close of Business on the Distribution Date, at the address of such holder shown on such records, a Right Certificate, in substantially the form of Exhibit A hereto, evidencing one Right for each share of Common Stock so held.

(b) As soon as practicable after the Rights Record Date, the Company will send a copy of a Summary of Rights, in substantially the form attached hereto as Exhibit B, by first-class mail, postage prepaid, to each record holder of Common Stock as of the Close of Business on the Rights Record Date, at the address of such holder shown on the records of the Company.

(c) The Company will cause certificates for Common Stock issued after the Rights Record Date (including replacement certificates for shares of Common Stock outstanding on or prior to the Rights Record Date), but prior to the earliest of (i) the Distribution Date, (ii) the Expiration Date and (iii) the date, if any, on which the Rights may be redeemed, to have impressed on, printed on, written on or otherwise affixed to them the following legend:

This certificate also entitles the holder hereof to certain Rights as set forth in the Rights Agreement between the Company and Harris Trust Company of California, as Rights Agent, as the same shall be amended from time to time (the "Rights Agreement"), the terms of which are hereby incorporated herein by reference and a copy of which is on file at the principal executive offices of the Company. Under certain circumstances, as set forth in the Rights Agreement, such Rights will be evidenced by separate certificates and will no longer be evidenced by this certificate. The Company will mail to the holder of this certificate a copy of the Rights Agreement without charge after receipt of a written request therefor. Under certain circumstances set forth in the Rights Agreement, Rights issued to, or held by, any Person who is, was or becomes an Acquiring Person or any Affiliate or Associate thereof (as such terms are defined in the Rights Agreement) or certain transferees of any thereof, whether currently held by or on behalf of such Person or by any subsequent holder, may be limited as provided in Section 7(f) of the Rights Agreement.

With respect to such certificates containing the foregoing legend, until the Distribution Date, the Rights associated with Common Stock represented by such certificates shall be evidenced by

such certificates alone, and the surrender for transfer of any such certificates shall also constitute the transfer of the Rights associated with the Common Stock represented by such certificate.

(d) Until the Distribution Date, the surrender for transfer of any of the certificates for Common Stock outstanding on or after the Rights Record Date, with or without a copy of the Summary of Rights attached thereto and with or without the legend set forth in subsection (c) above, shall also constitute the transfer of the Rights associated with such Common Stock. After the Distribution Date, the Rights will be evidenced solely by the Right Certificates.

Section 4. Form of Right Certificates.

(a) The Right Certificates (and the forms of assignment and certification and of election to purchase shares to be printed on the reverse thereof) shall be in substantially the form of Exhibit A hereto and may have such marks of identification or designation and such legends, summaries or endorsements printed thereon as the Company may deem appropriate and as are not inconsistent with the provisions of this Agreement, or as may be required to comply with any law or with any rule or regulation made pursuant thereto or with any rule or regulation of any stock exchange on which the Rights may from time to time be listed, or to conform to usage.

(b) Any Right Certificate issued pursuant to Section 3(a) or Section 22 that represents Rights Beneficially Owned by: (i) an Acquiring Person or any Associate or Affiliate of any Acquiring Person, (ii) a transferee of an Acquiring Person (or of any such Associate or Affiliate) who becomes a transferee after the Acquiring Person becomes such, or (iii) a transferee of an Acquiring Person (or of any such Associate or Affiliate) who becomes a transferee prior to or concurrently with the Acquiring Person becoming such and receives such Rights pursuant to either (A) a transfer (whether or not for consideration) from the Acquiring Person to holders of equity interests in such Acquiring Person or to any Person with whom such Acquiring Person has any continuing agreement, arrangement or understanding regarding the transferred Rights, or (B) a transfer which the Board of Directors of the Company has determined is part of a plan, arrangement or understanding which has as a primary purpose or effect avoidance of Section 7(f), and any Right Certificate issued pursuant to Section 6 or Section 11 upon transfer, exchange, replacement or adjustment of any other Right Certificate referred to in this sentence, shall contain (to the extent feasible and reasonably identifiable as such) the following legend:

The Rights represented by this Right Certificate are or were beneficially owned by a Person who was or became an Acquiring Person or an Affiliate or Associate of an Acquiring Person (as such terms are defined in the Rights Agreement) or certain transferees thereof. Accordingly, under certain circumstances as provided in the Rights Agreement, this Right Certificate and the Rights represented hereby may be limited as provided in Section 7(f) of such Agreement.

Section 5. Countersignature and Registration.

(a) The Right Certificates shall be executed on behalf of the Company by its President or any of its Vice Presidents, either manually or by facsimile signature, and have

affixed thereto the Company's seal or a facsimile thereof which shall be attested by the Secretary or an Assistant Secretary of the Company, either manually or by facsimile signature. The Right Certificates shall be manually countersigned by the Rights Agent and shall not be valid for any purpose unless so countersigned. In case any officer of the Company who shall have signed any of the Right Certificates shall cease to be such officer of the Company before countersignature by the Rights Agent and issuance and delivery by the Company, such Right Certificates, nevertheless, may be countersigned by the Rights Agent, issued and delivered with the same force and effect as though the person who signed such Right Certificates had not ceased to be such officer of the Company; and any Right Certificate may be signed on behalf of the Company by any person who, at the actual date of the execution of such Right Certificate, shall be a proper officer (as specified above) of the Company to sign such Right Certificate, although at the date of the execution of this Rights Agreement any such person was not such an officer.

(b) Following the Distribution Date, the Rights Agent will keep or cause to be kept books for registration and transfer of the Right Certificates issued hereunder. Such books shall show the names and addresses of the respective holders of the Right Certificates, the number of Rights evidenced on its face by each Right Certificate, the date of each Right Certificate and the number of each Right Certificate.

Section 6. Transfer, Split Up, Combination and Exchange of Right Certificates; Mutilated, Destroyed, Lost or Stolen Right Certificates.

(a) Subject to the provisions of Section 4(b), Section 7(f) and Section 14, at any time after the Close of Business on the Distribution Date, and prior to the Close of Business on the Expiration Date or the day prior to the day, if any, on which the Rights are to be redeemed pursuant to Section 23, any Right Certificate or Certificates may be transferred, split up, combined or exchanged for another Right Certificate or Right Certificates, entitling the registered holder to purchase such number of Units as the Right Certificate or Right Certificates surrendered then entitled such holder to purchase. Any registered holder desiring to transfer, split up, combine or exchange any Right Certificate shall make such request in writing delivered to the Rights Agent, and shall surrender the Right Certificate(s) to be transferred, split up, combined or exchanged, with the form of assignment on the reverse side(s) thereof duly completed and executed, at the stock transfer office of the Rights Agent. Thereupon the Rights Agent shall countersign and deliver to the persons entitled thereto the Right Certificate(s) requested. The Company may require payment of a sum sufficient to cover any tax or governmental charge that may be imposed in connection with any transfer, split up, combination or exchange of Right Certificates. Notwithstanding the foregoing, neither the Rights Agent nor the Company shall be obligated to take any action whatsoever with respect to the transfer of any such surrendered Right Certificate unless and until the registered holder shall have completed and signed the certificate contained in the form of assignment on the reverse side of such Right Certificate and shall have provided such additional evidence of the identity of the Beneficial Owner (or former Beneficial Owner) or Affiliates or Associates thereof as the Company shall reasonably request.

(b) Upon receipt by the Company and the Rights Agent of evidence reasonably satisfactory to them of the loss, theft, destruction or mutilation of a Right Certificate, and, in case of loss, theft or destruction, of indemnity or security reasonably satisfactory to them,

and reimbursement to the Company and the Rights Agent of all reasonable expenses incidental thereto, and upon surrender to the Rights Agent and cancellation of the Right Certificate, if mutilated, the Company will execute and deliver a new Right Certificate of like tenor to the Rights Agent for delivery to the registered owner in lieu of the Right Certificate so lost, stolen, destroyed or mutilated.

Section 7. Exercise of Rights; Purchase Price; Expiration Date of Rights.

(a) Subject to Section 7(f), and unless earlier redeemed as provided in Section 23, the registered holder of any Right Certificate may exercise the Rights evidenced thereby in whole or in part at any time after the Distribution Date upon surrender of the Right Certificate, with the form of election to purchase on the reverse side thereof duly completed and executed, to the Rights Agent at the stock transfer office of the Rights Agent, together with payment of the Purchase Price for each Unit as to which the Rights are exercised, at or prior to the Close of Business on the tenth anniversary of the Rights Record Date or such other date to which the Rights may be extended as provided in this Agreement (the latest of such dates being herein referred to as the "Expiration Date"). If at any time after the Distribution Date but prior to the Expiration Date the Company is unable, under its Articles of Incorporation, to issue the number and class of shares required to be issued upon the exercise of all of the outstanding Rights, the Company may issue upon exercise of any of the Rights shares of capital stock or other securities of the Company of equivalent value to the shares so required to be issued ("Equivalent Stock"), as determined by the Board of Directors.

(b) The Purchase Price for each Unit pursuant to the exercise of a Right shall initially be \$45.00, shall be subject to adjustment from time to time as provided in Sections 11 and 13 and shall be payable in lawful money of the United States of America.

(c) Upon receipt of a Right Certificate, with the form of election to purchase duly executed, accompanied by payment of the Purchase Price for the Units to be purchased and an amount equal to any applicable transfer tax in cash, or by certified check, bank draft or money order payable to the order of the Company, the Rights Agent shall thereupon promptly (i) requisition from the Company or any transfer agent of the Company a certificate for the number of shares to be purchased and the Company will comply, and hereby irrevocably authorizes its transfer agent to comply, with all such requests, (ii) requisition from the Company the amount of cash to be paid in lieu of issuance of a fractional share, when appropriate, in accordance with Section 14, and (iii) promptly after receipt of such certificate from any such transfer agent, cause the same to be delivered to or upon the order of the registered holder of such Right Certificate, registered in such name or names as may be designated by such holder, and, when appropriate, after receipt promptly deliver such cash in lieu of a fractional share to or upon the order of the registered holder of such Right Certificate; provided, however, that in the case of the purchase, in connection with the exercise of a Right, of securities other than shares of stock, the Rights Agent shall promptly take the appropriate actions with respect thereto as shall as nearly as practicable correspond to the actions described in the foregoing clauses (i) through (iii).

(d) The Company shall not be required to pay any transfer tax which may be payable in respect of any transfer involved in the transfer or delivery of Right Certificates, or the

issuance or delivery of certificates in a name other than that of the registered holder of the Right Certificate evidencing Rights surrendered for exercise, or to issue or deliver any certificates upon the exercise of any Rights, until any such tax shall have been paid (any such tax being payable by the holder of such Right Certificate at the time of surrender) or until it has been established to the Company's satisfaction that no such tax is due.

(e) In case the registered holder of any Right Certificate shall exercise less than all the Rights evidenced thereby, a new Right Certificate evidencing Rights equivalent to the Rights remaining unexercised shall be issued by the Rights Agent to the registered holder of such Right Certificate or to his duly authorized assigns, subject to the provisions of Section 14.

(f) Notwithstanding any provision of this Agreement to the contrary, upon the occurrence of any of the events described in any of clauses (A), (B), (C) or (D) of Section 11(a)(ii), the adjustment provided for under Section 11(a)(ii) shall not apply with respect to any Rights that are at the time of the occurrence of such event Beneficially Owned by (i) an Acquiring Person or by any Associate or Affiliate of such Acquiring Person (which Acquiring Person or Affiliate or Associate engages in, or realizes the benefit of, one or more of the transactions described in clause (A) or clause (B) of Section 11(a)(ii), realizes the benefits set forth in clause (C) of Section 11(a)(ii) or, alone or together, become the Beneficial Owner(s) of a number of shares of Voting Stock which equals or exceeds the percentage of the general voting power as provided in clause (D) of Section 11(a)(ii), as the case may be), or (ii) a transferee of an Acquiring Person or of any Associate or Affiliate of such Acquiring Person (which Acquiring Person or Associate or Affiliate engages in, or realizes the benefit of, one or more of the transactions described in clause (A) or clause (B) of Section 11(a)(ii), realizes the benefits set forth in clause (C) of Section 11(a)(ii) or, alone or together with such Acquiring Person or any such Associate or Affiliate, become the Beneficial Owner(s) of a number of shares of Voting Stock which equals or exceeds the percentage of the general voting power as provided in clause (D) of Section 11(a)(ii), as the case may be) (A) who becomes a transferee after the Acquiring Person becomes such, or (B) who becomes a transferee prior to or concurrently with the Acquiring Person becoming such and receives such Rights pursuant to either (1) a transfer (whether or not for consideration) from the Acquiring Person to holders of equity interests in such Acquiring Person or to any Person with whom such Acquiring Person has any continuing agreement, arrangement or understanding regarding the transferred Rights or (2) a transfer which the Board of Directors of the Company has determined is part of a plan, arrangement or understanding which has as a primary purpose or effect the avoidance of this Section 7(f). Upon the exercise of such Rights, the holders thereof shall be entitled to receive, upon payment of the Purchase Price, the number of Units issuable upon exercise of such Rights without giving effect to the adjustment provided for under Section 11(a)(ii). The Company shall use all reasonable efforts to insure that the provisions of this Section 7(f) and Section 4(b) are complied with, but shall have no liability to any holder of Right Certificates or other Person as a result of its making or failing to make any determinations with respect to an Acquiring Person or its Affiliates, Associates or transferees hereunder.

(g) Notwithstanding anything in this Agreement to the contrary, neither the Rights Agent nor the Company shall be obligated to undertake any action with respect to a registered holder upon the occurrence of any purported exercise as set forth in this Section 7 unless such registered holder shall have (i) completed and signed the certificate contained in the

form of election to purchase set forth on the reverse side of the Right Certificate surrendered for such exercise, and (ii) provided such additional evidence of the identity of the Beneficial Owner (or former Beneficial Owner) or Affiliates or Associates thereof as the Company shall reasonably request.

Section 8. Cancellation and Destruction of Right Certificates.

All Right Certificates surrendered for the purpose of exercise, transfer, split up, combination or exchange shall, if surrendered to the Company or to any of its agents, be delivered to the Rights Agent for cancellation or in cancelled form, or, if surrendered to the Rights Agent, shall be cancelled by it, and no Right Certificates shall be issued in lieu thereof except as expressly permitted by this Agreement. The Company shall deliver to the Rights Agent for cancellation and retirement, and the Rights Agent shall so cancel and retire, any other Right Certificate purchased or acquired by the Company otherwise than upon the exercise thereof. The Rights Agent shall deliver all cancelled Right Certificates to the Company, or shall, at the written request of the Company, destroy such cancelled Right Certificates, and in such case shall deliver a certificate of destruction thereof to the Company.

Section 9. Reservation and Availability of Shares; Registration.

(a) The Company covenants and agrees that it shall (i) on or prior to the Rights Record Date, take all such action as shall be necessary to cause to be reserved and kept available out of its authorized and unissued capital stock, the number, class and series of shares that will be sufficient to permit the exercise in full of all Rights to be outstanding as of the Rights Record Date, (ii) no later than promptly following the Distribution Date, take all such action as shall be necessary to cause to be reserved and kept available out of its authorized and unissued capital stock, the number of additional shares that will, from time to time, be sufficient to permit the exercise in full of all Rights from time to time outstanding, (iii) take all such action as may be necessary to insure that all shares delivered upon exercise of Rights shall, at the time of delivery of the certificates for such shares (subject to payment of the Purchase Price), be duly and validly authorized and issued and fully paid and nonassessable, and (iv) pay when due and payable any and all federal and state transfer taxes and charges which may be payable in respect of the issuance or delivery of the Right Certificates or of any shares upon the exercise of Rights (except as otherwise provided in Section 7(d)).

(b) The Company agrees to take all such action, from and after the Distribution Date, as may be necessary or appropriate to permit the issuance of shares in connection with the exercise of the Rights, including any required registration under (i) the Securities Act of 1933, as amended from time to time (the "Securities Act"), and (ii) the securities or "blue sky" laws of the various states and obtaining any necessary approvals of the California Public Utilities Commission and any other governmental agency as shall be required by law. The Company may temporarily suspend, for a period of time not to exceed 120 days, the exercisability of the Rights in order to prepare and file a registration statement or statements for the purpose of effecting any such registration and permit such statement(s) to become effective and to prepare and file any application or applications for the purpose of obtaining any such approvals and permit such approvals to be obtained. At the commencement and termination of any such suspension, the Company shall issue a public announcement and shall provide written

notice to the Rights Agent, stating that the exercisability of the Rights has been temporarily suspended, or that such suspension has terminated, as the case may be.

(c) If and so long as the stock issuable upon the exercise of Rights is listed on any national securities exchange, the Company shall use its reasonable efforts to cause all shares reserved for issuance upon exercise of Rights to be listed on such exchange upon official notice of issuance upon such exercise.

Section 10. Record Date. Each Person in whose name any stock certificate is issued upon the exercise of Rights shall for all purposes be deemed to have become the holder of record of the shares represented thereby on, and such certificate shall be dated, the date upon which the Right Certificate evidencing such Rights was duly surrendered and payment of the Purchase Price (and any applicable transfer taxes) was made. Prior to the exercise of the Rights evidenced thereby, the holder of a Right Certificate shall not be entitled to any rights of a shareholder of the Company with respect to shares for which the Rights shall be exercisable, including without limitation the right to vote or to receive dividends or other distributions, and such holder shall not be entitled to receive any notice of any proceedings of the Company, except as provided herein.

Section 11. Adjustment of Purchase Price, Number of Shares or Number of Rights. The Purchase Price, the number and kind of shares or other securities covered by each Right and the number of Rights outstanding are subject to adjustment from time to time as provided in this Section 11.

(a) (i) In the event the Company shall at any time after the date of this Agreement (A) declare and pay a dividend on the shares which are subject to the Rights ("Subject Shares") payable in shares of stock of the Company, (B) subdivide or split the Subject Shares, (C) combine or consolidate the Subject Shares into a smaller number of shares or effect a reverse stock split of the Subject Shares or (D) issue any shares of its capital stock in a reclassification of the Subject Shares (including any such reclassification in connection with a consolidation or merger in which the Company is the continuing or surviving corporation), then, and in each such event, except as otherwise provided in this Section 11(a), the Purchase Price in effect at the time of the record date for such dividend or of the effective date of such subdivision, split, reverse split, combination, consolidation or reclassification, and the number and kind of shares of capital stock issuable on such date, shall be proportionately adjusted so that the holder of any Right exercised after such time shall be entitled to receive the aggregate number and kind of shares of capital stock which, if such Right had been exercised immediately prior to such date and at a time when the transfer books of the Company were open, he would have received upon such exercise and been entitled to receive by virtue of such dividend, subdivision, split, reverse split, combination, consolidation or reclassification. If an event occurs which would require an adjustment under both this Section 11(a)(i) and Section 11(a)(ii), the adjustment provided for in this Section 11(a)(i) shall be in addition to, and shall be made prior to, any adjustment required pursuant to Section 11(a)(ii).

(ii) In the event that at any time after the date of this Agreement

(A) any Acquiring Person, or any Associate or Affiliate of any Acquiring Person, directly or indirectly (1) shall merge into the Company or any of its Subsidiaries or otherwise combine with the Company or any of its Subsidiaries and the Company or such Subsidiary shall be the continuing or surviving corporation of such merger or combination and the Common Stock shall remain outstanding and the outstanding shares thereof shall not be changed into or exchanged for stock or other securities of the Company or of any other Person or cash or any other property, or (2) shall sell or otherwise transfer in one or more transactions, assets to the Company or any of its Subsidiaries in exchange for 25 percent or more of the shares of any class of capital stock of the Company or any of its Subsidiaries, and the Common Stock shall remain outstanding and unchanged, or

(B) directly or indirectly, any Acquiring Person, or any Associate or Affiliate of any Acquiring Person, shall (1) in one or more transactions, transfer any assets to the Company or any of its Subsidiaries in exchange (in whole or in part) for shares of any class of capital stock of the Company or any of its Subsidiaries or for securities exercisable for or convertible into shares of any class of capital stock of the Company or any of its Subsidiaries or otherwise obtain from the Company or any of its Subsidiaries, with or without consideration, any additional shares of any class of capital stock of the Company or any of its Subsidiaries or other securities exercisable for or convertible into shares of any class of capital stock of the Company or any of its Subsidiaries (other than as part of a pro rata distribution by the Company or such Subsidiary to all holders of Common Stock), (2) sell, purchase, lease, exchange, mortgage, pledge, transfer or otherwise dispose (in one or more transactions), to, from or with, as the case may be, the Company or any of its Subsidiaries, assets on terms and conditions less favorable to the Company or such Subsidiary than the Company or such Subsidiary would be able to obtain in arm's-length negotiation with an unaffiliated third party, (3) receive any compensation from the Company or any of the Company's Subsidiaries other than compensation for full-time employment as a regular employee, or fees for serving as director, at rates in accordance with the Company's (or its Subsidiaries') past practices, or (4) receive the benefit, directly or indirectly (except proportionately as a shareholder), of any loans, advances, guarantees, pledges or other financial assistance provided by the Company or any of its Subsidiaries, on terms and conditions less favorable to the Company or such Subsidiary than the Company or such Subsidiary would be able to obtain in arm's-length negotiation with an unaffiliated third party, or

(C) during any such time as there is an Acquiring Person, there shall be any reclassification of securities (including any reverse stock split), or recapitalization of the Company, or any merger or consolidation of the Company with any of its Subsidiaries or any other similar transaction or series of transactions involving the Company or any of its Subsidiaries (whether or not with or into or otherwise involving an Acquiring Person or any Affiliate or Associate of such Acquiring Person) which has the effect, directly or indirectly, of increasing by more than one percent the proportionate share of the outstanding

shares of any class of equity securities, or of securities exercisable for or convertible into equity securities, of the Company or any of its Subsidiaries which is directly or indirectly owned by any Acquiring Person or any Associate or Affiliate of any Acquiring Person, or

(D) any Person shall become an Acquiring Person otherwise than pursuant to a Qualified Offer,

then, and in each such case, but subject to the provisions of Section 27, proper provision shall be made so that each holder of a Right, except as provided below and in Section 7(f), shall, on and after the later of (I) the date of the occurrence of an event described in clause (A), (B), (C) or (D) of this Section 11(a)(ii), or (II) the date of the expiration of the period within which the Rights may be redeemed pursuant to Section 23 (as the same may have been amended as provided in Section 26), have the right to receive, upon exercise thereof at the then current Purchase Price, such number of shares of Common Stock as shall equal the result obtained by (x) multiplying the then current Purchase Price by the then number of Units for which a Right is then exercisable and dividing that product by (y) 50 percent of the current market price per share of Common Stock (determined in accordance with Section 11(d)) on the date of the occurrence of the relevant event listed above in clause (A), (B), (C) or (D) of this subparagraph (ii); provided, however, that if the transaction that would otherwise give rise to the foregoing adjustment is also subject to the provisions of Section 13, then only the provisions of Section 13 shall apply and no adjustment shall be made pursuant to this Section 11(a)(ii). The Company shall not consummate any such merger, combination, transfer or transaction referred to in any of such clauses (A), (B) and (C) unless prior thereto there shall be sufficient authorized but unissued Common Stock to permit the exercise in full of the Rights in accordance with the foregoing sentence, unless the Board of Directors has determined to issue Equivalent Stock in accordance with Section 7(a); provided, however, that in no case may the Company consummate any such merger, combination, transfer or transaction if at the time of or immediately after such transaction there are any rights, warrants or other instruments or securities outstanding or agreements in effect which would substantially diminish or otherwise eliminate the benefits intended to be afforded by the Rights.

In the event that the Company issues Equivalent Stock upon the exercise of any Rights pursuant to the immediately preceding paragraph, then, upon any such exercise, proper provision shall be made so that the holder of a Right (except as provided in Section 7(f)) shall have the right to receive, upon such exercise at the then current Purchase Price, such number of shares or other units of Equivalent Stock of the Company as shall equal the result obtained by (x) multiplying the then current Purchase Price by the number of Units for which a Right is then exercisable and dividing that product by (y) 50 percent of the current market price per share or other unit of the Equivalent Stock of the Company (determined on substantially the same basis as is prescribed by Section 11(d) with respect to the valuation of Common Stock) on the date of occurrence of the relevant event listed above in clause (A), (B), (C) or (D) of this subparagraph (ii). In the event that at any time the Company should be prohibited by law, by any provision of its Articles of Incorporation, or by any instrument or agreement to which the Company is a party or by which it is bound, from issuing, or should be unable under its Articles of Incorporation to issue, sufficient Equivalent Stock to permit the exercise of all outstanding Rights in accordance

with the foregoing sentence, then, in lieu of issuing such Equivalent Stock upon such exercise, the Company shall pay to each holder of a Right (except as provided in Section 7(f)) upon surrender of the Right as provided herein but without payment of the Purchase Price, an amount in cash for each Right equal to the Purchase Price.

(b) In case the Company shall at any time after the Rights Record Date fix a record date for the issuance of rights or warrants to all holders of Common Stock or Subject Shares entitling them (for a period expiring within 45 calendar days after such record date) to subscribe for or purchase Common Stock or Subject Shares or securities convertible into Common Stock or Subject Shares at a price per share (or having a conversion price per share, if a security convertible into Common Stock) less than the current market price per share (determined in accordance with Section 11(d)) on such record date, the Purchase Price to be in effect after such record date shall be determined by multiplying the Purchase Price in effect immediately prior to such record date by a fraction, of which the numerator shall be the total number of shares of Common Stock and Subject Shares outstanding on such record date plus the number of shares of Common Stock which the aggregate offering price of the total number of shares so to be offered (and/or the aggregate initial conversion price of the convertible securities so to be offered) would purchase at such current market price and of which the denominator shall be the total number of shares of Common Stock and Subject Shares outstanding on such record date plus the number of additional shares to be offered for subscription or purchase (or into which the convertible securities to be offered are initially convertible). In case such subscription or purchase price may be paid, in whole or in part, in a form other than cash, the value of such consideration shall be as determined in good faith by the Board of Directors of the Company, whose determination shall be described in a statement filed with the Rights Agent. Shares owned by or held for the account of the Company shall not be deemed outstanding for the purpose of any such computation. Such adjustment shall be made successively whenever such a record date is fixed, and in the event that such rights or warrants are not so issued, the Purchase Price shall be adjusted to be the Purchase Price which would then be in effect if such record date had not been fixed.

(c) In case the Company shall at any time after the Rights Record Date fix a record date for the making of a distribution on the shares of Common Stock or the Subject Shares, whether by way of a dividend, distribution, reclassification of stock, recapitalization, reorganization or partial liquidation of the Company or otherwise (and including any such distribution made in connection with a consolidation or merger in which the Company is the continuing corporation), of subscription rights or warrants (excluding those referred to in Section 11(b)), evidences of indebtedness or other assets (other than (i) regular periodic cash dividends, (ii) a dividend payable in Common Stock or (iii) a distribution which is part of or is made in connection with a transaction to which Section 11(a)(ii) or Section 13 applies), the Purchase Price to be in effect after such record date shall be determined by multiplying the Purchase Price in effect immediately prior to such record date by a fraction, of which the numerator shall be the current market price per share of Common Stock (determined in accordance with Section 11(d)) on such record date, less the fair market value applicable to one share of Common Stock (as determined in good faith by the Board of Directors of the Company, whose determination shall be described in a statement filed with the Rights Agent) of such assets or evidences of indebtedness or of such subscription rights or warrants so to be distributed, and of which the denominator shall be such current market price per share of Common Stock. Such adjustments

shall be made successively whenever such a record date is fixed; and in the event that such distribution is not so made, the Purchase Price shall again be adjusted to be the Purchase Price which would then be in effect if such record date had not been fixed.

(d) For the purpose of any computation hereunder, the "current market price" per share of Common Stock on any date shall be deemed to be the average of the daily closing prices per share of such Common Stock for the 30 consecutive Trading Days immediately prior to such date; provided, however, that in the event that the current market price per share of Common Stock is determined during a period following the announcement by the issuer of such Common Stock of a dividend or distribution on such Common Stock payable in shares of such Common Stock or securities convertible into shares of Common Stock (other than the Rights), and prior to the expiration of 30 Trading Days after the ex-dividend date for such dividend or distribution, then, and in each such case, the current market price shall be appropriately adjusted to reflect the current market price per share of Common Stock in connection with ex-dividend trading. The closing price for each day shall be the last sale price, regular way, or, in case no such sale takes place on such day, the average of the closing bid and asked prices, regular way, in either case as reported in the principal consolidated transaction reporting system with respect to securities listed or admitted to trading on the New York Stock Exchange or, if the shares of Common Stock are not listed or admitted to trading on the New York Stock Exchange, as reported in the principal consolidated transaction reporting system with respect to securities listed on the principal national securities exchange on which the shares of Common Stock are listed or admitted to trading or, if the shares of Common Stock are not listed or admitted to trading on any national securities exchange, the average of the high bid and low asked prices in the over-the-counter market, as reported by the National Association of Securities Dealers, Inc., Automated Quotation System ("NASDAQ"). If on any such date the shares of Common Stock are not quoted by any such organization, the fair market value of such shares on such date as determined in good faith by the Board of Directors of the issuer of such Common Stock shall be used. Any such determination of current market price shall be described in a statement filed with the Rights Agent.

For the purpose of any computation hereunder, the "current market price" of a Unit shall be deemed to be equal to the current market price per share of Common Stock, and the "current market price" of a Subject Share shall be deemed to be equal to the current market price per share of Common Stock divided by the number of Subject Shares which comprise a Unit.

For purposes of this Agreement, the term "Trading Day" shall mean a day on which the principal national securities exchange on which the shares of Common Stock are listed or admitted to trading is open for the transaction of business or, if the shares of Common Stock are not listed or admitted to trading on any national securities exchange, a Business Day.

(e) No adjustment in the Purchase Price shall be required unless such adjustment would require an increase or decrease of at least one percent in such Price; provided, however, that any adjustments which by reason of this Section 11(e) are not required to be made shall be carried forward and taken into account in any subsequent adjustment. All calculations under this Section 11 shall be made to the nearest cent or to the nearest one-hundredth of a share, as the case may be. Notwithstanding the proviso to the first sentence of this Section 11(e), any adjustment required by this Section 11 shall be made no later than the earlier of (i) three years

from the date of the transaction which gives rise to such adjustment or (ii) the date of the expiration of the right to exercise any Rights.

(f) In the event that at any time, as a result of an adjustment made pursuant to Section 11(a), the holder of any Right thereafter exercised shall become entitled to receive any shares of capital stock of the Company other than shares of Common Stock, thereafter the number of such other shares so receivable upon exercise of any Right shall be subject to adjustment from time to time in a manner and on terms as nearly equivalent as practicable to the provisions, with respect to such shares, contained in Sections 11(a) through (c), inclusive, and the provisions of Sections 7, 9, 10, 13 and 14 with respect to the shares of Common Stock shall apply on like terms to any such other shares.

(g) All Rights originally issued by the Company subsequent to any adjustment made to the Purchase Price hereunder shall represent the right to purchase, at the adjusted Purchase Price, the number of shares purchasable from time to time hereunder upon exercise of the Rights, all subject to further adjustment as provided herein.

(h) Unless the Company shall have exercised its election as provided in Section 11(i), upon each adjustment of the Purchase Price as a result of the calculations made in Sections 11(b) and (c), each Right outstanding immediately prior to the making of such adjustment shall thereafter evidence the right to purchase, at the adjusted Purchase Price, that number of shares (calculated to the nearest one-hundredth) obtained by (i) multiplying (x) the number of shares covered by a Right immediately prior to such adjustment by (y) the Purchase Price in effect immediately prior to such adjustment of the Purchase Price and (ii) dividing the product so obtained by the Purchase Price in effect immediately after such adjustment of the Purchase Price.

(i) The Company may elect on or after the date of any adjustment of the Purchase Price to adjust the number of Rights, in substitution for any adjustment in the number of shares purchasable upon the exercise of each Right. Each of the Rights outstanding after such adjustment of the number of Rights shall be exercisable for the number of Units for which a Right was exercisable immediately prior to such adjustment. Each Right held of record prior to such adjustment of the number of Rights shall become that number of Rights (calculated to the nearest one-hundredth) obtained by dividing the Purchase Price in effect immediately prior to adjustment of the Purchase Price by the Purchase Price in effect immediately after adjustment of the Purchase Price. The Company shall make a public announcement of its election to adjust the number of Rights, indicating the record date for the adjustment, and, if known at the time, the amount of the adjustment to be made. This record date may be the date on which the Purchase Price is adjusted or any day thereafter, but, if the Right Certificates have been issued, shall be at least 10 days later than the date of the public announcement. If Right Certificates have been issued, upon each adjustment of the number of Rights pursuant to this Section 11(i) the Company shall, as promptly as practicable, cause to be distributed to holders of record of Right Certificates on such record date Right Certificates evidencing, subject to Section 14, the additional Rights to which such holders shall be entitled as a result of such adjustment, or, at the option of the Company, shall cause to be distributed to such holders of record in substitution and replacement for the Right Certificates held by such holders prior to the date of adjustment, and upon surrender thereof, if required by the Company, new Right Certificates evidencing all the Rights

to which such holders shall be entitled after such adjustment. Right Certificates so to be distributed shall be issued, executed and countersigned in the manner provided for herein (and may bear, at the option of the Company, the adjusted Purchase Price) and shall be registered in the names of the holders of record of Right Certificates on the record date specified in the public announcement.

(j) Irrespective of any adjustment or change in the Purchase Price or the number of shares issuable upon the exercise of the Rights, the Right Certificates theretofore and thereafter issued may continue to express the Purchase Price per share and the number of shares which were expressed in the initial Right Certificates issued hereunder.

(k) In any case in which this Section 11 requires that an adjustment in the Purchase Price be made effective as of the record date for a specified event, the Company may elect to defer until the occurrence of such event the issuance to the holder of any Right exercised after such record date the additional shares or securities of the Company, if any, issuable as a consequence of such adjustment; provided, however, that the Company shall deliver to such holder a due bill or other appropriate instrument evidencing such holder's right to receive such additional shares or securities upon the occurrence of such event.

(l) Anything in this Section 11 to the contrary notwithstanding, the Company shall be entitled to make such adjustments in the number of shares which may be acquired upon exercise of the Rights, and such adjustments in the Purchase Price, in addition to those adjustments expressly required by the other subsections of this Section 11, as and to the extent that the Company, in its sole discretion, shall determine to be advisable, in order that, in the event of (i) any reclassification, consolidation or subdivision of the Common Stock, (ii) any reorganization or partial liquidation of the Company or similar transaction, (iii) any issuance wholly for cash of any Common Stock at less than the current market price, (iv) any issuance wholly for cash of Common Stock or securities which by their terms are convertible into or exchangeable for Common Stock, (v) any stock dividends or (vi) any issuance of rights, options or warrants, hereafter made by the Company to holders of its Common Stock as provided herein above in this Section 11, (x) the holders of the Rights in any such event shall be treated equitably and in accordance with the purpose and intent of this Agreement, and (y) to the extent reasonably possible, such event shall not, in the opinion of counsel for the Company, result in the shareholders of the Company being subject to any United States federal income tax liability by reason thereof.

Section 12. Certification of Adjusted Purchase Price or Number of Shares. Whenever an adjustment is made as provided in Section 11 or 13, the Company shall (i) promptly prepare a certificate setting forth such adjustment, and a brief statement of the facts accounting for such adjustment, (ii) promptly file with the Rights Agent and with each transfer agent for the Common Stock a copy of such certificate, and (iii) mail a brief summary thereof to each holder of a Right Certificate in accordance with Section 25. Notwithstanding the foregoing sentence, the failure of the Company to give such notice shall not affect the validity of, or the force or effect of, the requirement for such adjustment.

Section 13. Consolidation, Merger or Sale or Transfer of Assets or Earning Power.

(a) In the event that, at any time after an Acquiring Person has become such,

(i) the Company shall consolidate with, or merge with and into, any other Person and the Company shall not be the continuing or surviving corporation of such consolidation or merger,

(ii) any other Person(s) shall consolidate or merge with and into the Company, the Company shall be the continuing or surviving corporation of such merger and, in connection with such consolidation or merger, all or part of the Common Stock shall be changed into or exchanged for stock or other securities of the Company or of any other Person or cash or any other property, or

(iii) the Company shall sell or otherwise transfer (or one or more of its Subsidiaries shall sell or otherwise transfer), in one or more transactions, assets or earning power aggregating more than 50 percent of the assets or earning power of the Company and its Subsidiaries (taken as a whole) to any other Person, (other than a pro rata distribution by the Company of assets (including securities) of the Company or any of its Subsidiaries to all holders of the Company's Common Stock),

then, on and after the later of (I) the date of the occurrence of an event described in clause (i), (ii) or (iii) of this Section 13(a), or (II) the date of the expiration of the period within which the Rights may be redeemed pursuant to Section 23 (as the same may have been amended as provided in Section 26):

(A) proper provision shall be made so that each holder of a Right shall thereafter have the right to receive, upon the exercise thereof at the then current Purchase Price, such number of shares of common stock of the Principal Party as shall be equal to the result obtained by (x) multiplying the then current Purchase Price by the number of Units for which a Right is then exercisable and dividing that product by (y) 50 percent of the current market price per share of the common stock of the Principal Party (determined in the same manner as the current market price of Common Stock is determined under Section 11(d)) on the date of consummation of such consolidation, merger, sale or transfer;

(B) the Principal Party shall thereafter be liable for, and shall assume, by virtue of such consolidation, merger, sale or transfer, all the obligations and duties of the Company pursuant to this Agreement, and proper provision shall be made for the foregoing, provided that the Principal Party shall, prior to the first occurrence of an event described in clause (i), (ii) or (iii) of this Section 13(a), have caused to be reserved out of its authorized and unissued shares of common stock (or its authorized and issued shares of common stock held in its treasury), for issuance pursuant to this Agreement, the number of shares of common stock that will be sufficient to permit the exercise in full of the Rights after the occurrence of such event;

(C) the term "Company" wherever used in this Agreement shall thereafter be deemed to refer to such Principal Party; and

(D) the Principal Party shall, in addition to the reservation of shares of its common stock as provided in the proviso to clause (B) above, take such steps (including without limitation compliance with the Company's other obligations as set forth in Section 9) in connection with such consummation as may be necessary to assure that the provisions hereof shall thereafter be applicable, as nearly as reasonably may be, in relation to the shares of its Common Stock thereafter deliverable upon the exercise of the Rights; provided, however, that, upon the subsequent occurrence of any merger, consolidation, sale of all or substantially all assets, recapitalization, reclassification of shares, reorganization or other extraordinary transaction in respect of such Principal Party, each holder of a Right shall thereupon be entitled to receive, upon exercise of a Right and payment of the Purchase Price, such cash, shares, rights, warrants and other property which such holder would have been entitled to receive had such holder, at the time of such transaction, owned the shares of common stock of the Principal Party purchasable upon the exercise of a Right, and such Principal Party shall take such steps (including, but not limited to, reservation of shares of stock) as may be necessary to permit the subsequent exercise of the Rights in accordance with the terms hereof for such cash, shares, rights, warrants and other property.

(b) For purposes of this Agreement, "Principal Party" shall mean

(i) in the case of any transaction described in clause (i) or (ii) of Section 13(a), (A) the Person that is the issuer of the securities into which shares of Common Stock are converted in such merger or consolidation, or, if there is more than one such issuer, the issuer the common stock of which has the greatest market value, or (B) if no securities are so issued, (x) the Person that is the other party to the merger or consolidation and that survives said merger or consolidation, or, if there is more than one such Person, the Person the common stock of which has the greatest market value or (y) if the Person that is the other party to the merger or consolidation does not survive the merger or consolidation, the Person that does so survive (including the Company if it survives); and

(ii) in the case of any transaction described in clause (iii) of Section 13(a), the Person that is the party receiving the greatest portion of the assets or earning power transferred pursuant to such transaction or transactions, or, if each Person that is a party to such transaction or transactions receives the same portion of the assets or earning power so transferred or if the Person receiving the greatest portion of the assets or earning power cannot be determined, whichever of such Persons is the issuer of common stock having the greatest market value of shares outstanding;

provided, however, that in any such case, (1) if the common stock of such Person is not at such time and has not been continuously over the preceding 12-month period registered under Section

12 of the Exchange Act, and such Person is a direct or indirect Subsidiary of another corporation the common stock of which is and has been so registered, "Principal Party" shall refer to such other corporation; (2) if the common stock of such Person is not and has not been so registered and such Person is not a direct or indirect Subsidiary of another corporation the common stock of which is and has been so registered, "Principal Party" shall refer to the corporation which ultimately controls such Person; (3) in case such Person is a Subsidiary, directly or indirectly, of more than one corporation, the common stocks of all of which are and have been so registered, "Principal Party" shall refer to whichever of such corporations is the issuer of common stock having the greatest market value of shares held by the public; and (4) if the common stock of such Person is not and has not been so registered and such Person is owned, directly or indirectly, by a joint venture formed by two or more Persons that are not owned, directly or indirectly, by the same Person, the rules set forth in clauses (1), (2) and (3) above shall apply to each of the chains of ownership having an interest in such joint venture as if such Person were a "Subsidiary" of both or all of such joint ventures and the Principal Party in each such chain shall bear the obligations set forth in this Section 13 in the same ratio as its direct or indirect interests in such Person bear to the total of such interests.

(c) The Company shall not consummate any such consolidation, merger, sale or transfer unless prior thereto the Company and the Principal Party shall have executed and delivered to the Rights Agent a supplemental agreement making valid provision for the results described in clause (A) of Section 13(a) and confirming that the Principal Party will perform its obligations under this Section 13(a); provided, however, that in no case may the Company consummate any such consolidation, merger, sale or transfer if (i) at the time of or immediately after such transaction there are any rights, warrants or other instruments or securities outstanding or agreements in effect which would substantially diminish or otherwise eliminate the benefits intended to be afforded by the Rights or (ii) prior to, simultaneously with or immediately after such transaction, the shareholders of the Person which constitutes, or would constitute, the Principal Party for purposes of this Section 13 shall have received a distribution of Rights previously owned by such Person or any of its Affiliates and Associates.

(d) The provisions of this Section 13 shall similarly apply to successive mergers or consolidations or sales or other transfers. This Section 13 shall not be applicable to a transaction described in Subparagraphs (i), (ii) or (iii) of Subsection (a) of this Section if (i) such transaction is consummated with a Person or Persons who acquired Common Stock pursuant to a Qualified Offer (or a wholly owned subsidiary of any such Person or Persons), (ii) the price per share of Common Stock offered in such transaction or distributable to shareholders upon conclusion of such transaction is not less than the price per share of Common Stock paid to all holders of Common Stock whose shares were purchased pursuant to such Qualified Offer and (iii) the form of consideration being offered to the remaining holders of Common Stock pursuant to such transaction or distributable to shareholders upon conclusion of such transaction is the same as the form of consideration paid pursuant to such Qualified Offer. Upon conclusion of any transaction described in the foregoing sentence, all Rights shall expire.

Section 14. Fractional Rights and Fractional Shares.

(a) The Company shall not be required to issue fractions of Rights or to distribute Right Certificates which evidence fractional Rights. If the Company shall elect not to

issue such fractional Rights, in lieu of such fractional Rights, there shall be paid to the registered holders of the Right Certificates with regard to which such Fractional Rights would otherwise be issuable an amount in cash equal to the same fraction of the current market value of a whole Right. For the purposes of this Section 14(a), the current market value of a whole Right shall be the closing price of the Rights for the Trading Day immediately prior to the date on which such fractional Rights would have been otherwise issuable. The closing price for any day shall be the last sale price, regular way, or, in case no such sale takes place on such day, the average of the closing bid and asked prices, regular way, in either case as reported in the principal consolidated transaction reporting system with respect to securities listed or admitted to trading on the New York Stock Exchange or, if the Rights are not listed or admitted to trading on the New York Stock Exchange, as reported in the principal consolidated transaction reporting system with respect to securities listed on the principal national securities exchange on which the Rights are listed or admitted to trading or, if the Rights are not listed or admitted to trading on any national securities exchange, the average of the high bid and low asked prices in the over-the-counter market, as reported by NASDAQ. If on any such date the Rights are not quoted by any such organization, the fair value of the Rights on such date as determined in good faith by the Board of Directors of the Company shall be used. Any such determination of current market value shall be described in a statement filed with the Rights Agent.

(b) The Company shall not be required to issue fractions of shares upon exercise of a Right or to distribute certificates which evidence fractional shares. In lieu of fractional shares, the Company shall pay to the registered holders of Right Certificates at the time such Right Certificates are exercised as herein provided an amount in cash equal to the same fraction of the current market value of a share of Common Stock. For purposes of this Section 14, the current market value of a share of Common Stock shall be the closing price of a share of Common Stock (as determined pursuant to the second sentence of Section 11(d)) for the Trading Day immediately prior to the date of such exercise.

(c) The holder of a Right by the acceptance thereof expressly waives his right to receive any fractional Rights or any fractional shares upon exercise of a Right.

Section 15. Rights of Action. All rights of action in respect of this Agreement are vested in the respective registered holders of the Right Certificates (and prior to the Distribution Date, the registered holders of the Common Stock), and any registered holder of any Right Certificate (or, prior to the Distribution Date, any registered holder of the Common Stock), without the consent of the Rights Agent or of the holder of any other Right Certificate (or, prior to the Distribution Date, any other registered holder of the Common Stock), may, on his own behalf and for his own benefit, enforce, and may institute and maintain, any suit, action or proceeding against the Company to enforce, or otherwise act in respect of, his right to exercise the Rights evidenced by such Right Certificate in the manner provided in such Right Certificate and in this Agreement. Without limiting the foregoing or any remedies available to the holders of Rights, it is specifically acknowledged that the holders of Rights would not have an adequate remedy at law for any breach of this Agreement and will be entitled to specific performance of the obligations under, and injunctive relief against actual or threatened violations of the obligations of any Person subject to, this Agreement.

Section 16. Agreement of Right Holders. Every holder of a Right by accepting the same, consents and agrees with the Company and the Rights Agent and with every other holder of a Right that:

(a) prior to the Distribution Date, the Rights will be transferable only in connection with the transfer of Common Stock;

(b) on and after the Distribution Date, the Right Certificates will be transferable only on the registry books of the Rights Agent and then if surrendered at the stock transfer office of the Rights Agent, duly endorsed or accompanied by a proper instrument of transfer; and

(c) the Company and the Rights Agent may deem and treat the person in whose name the Right Certificate (or, prior to the Distribution Date, the associated Common Stock certificate) is registered as the absolute owner thereof and of the Rights evidenced thereby (notwithstanding any notations of ownership or writing on the Right Certificates or the associated Common Stock certificate made by anyone other than the Company or the Rights Agent) for all purposes whatsoever, and neither the Company nor the Rights Agent shall be affected by any notice to the contrary.

Section 17. Right Certificate Holder Not Deemed a Shareholder. No holder, as such, of any Right Certificate shall be entitled to vote, receive dividends or be deemed for any purpose the holder of Common Stock or any other securities of the Company which may at any time be issuable on the exercise of the Rights represented thereby, nor shall anything contained herein or in any Right Certificate be construed to confer upon the holder of any Right Certificate, as such, any of the rights of a shareholder of the Company or any right to vote for the election of directors or upon any matter submitted to shareholders at any meeting thereof, or to give or withhold consent to any corporate action, or to receive notice of meetings or other actions affecting shareholders (except as provided in Section 24), or to receive dividends or subscription rights, or otherwise, until the Right or Rights evidenced by such Right Certificate shall have been exercised in accordance with the provisions hereof.

Section 18. Concerning the Rights Agent.

(a) The Company agrees to pay to the Rights Agent reasonable compensation for all services rendered by it hereunder and, from time to time, on demand of the Rights Agent, its reasonable expenses and counsel fees and other disbursements incurred in the administration and execution of this Agreement and the exercise and performance of its duties hereunder. The Company also agrees to indemnify the Rights Agent for, and to hold it harmless against, any loss, liability, or expense incurred, without negligence, bad faith or willful misconduct on the part of the Rights Agent, for anything done or omitted by the Rights Agent in connection with the acceptance and administration of this Agreement, including the costs and expenses of defending against any claim of liability in the premises.

(b) The Rights Agent shall be protected and shall incur no liability for or in respect of any action taken, suffered or omitted by it in connection with its administration of this Agreement in reliance upon any Right Certificate or Certificate for Common Stock or for other

securities of the Company, instrument of assignment or transfer, power of attorney, endorsement, affidavit, letter, notice, direction, consent, certificate, statement, or other paper or document believed by it, acting with reasonable care, to be genuine and to be signed, executed and, where necessary, verified or acknowledged, by the proper person or persons.

If and for so long as the Rights are listed on the New York Stock Exchange or the American Stock Exchange, the Rights Agent, if its principal offices are located outside New York City, shall maintain in the New York City area facilities for the servicing of the Rights in the area of Manhattan located south of Chambers Street. Such facilities may consist of either an office or agency where transactions in the Rights are serviced directly or a "drop" where Common Stock certificates, Right Certificates, and other instruments relating to transactions in Rights may be received for redelivery to an office or agency outside New York City, all in accordance with the applicable rules of the stock exchange on which the Rights are listed.

Section 19. Merger or Consolidation or Change of Name of Rights Agent.

(a) Any corporation into which the Rights Agent or any successor Rights Agent may be merged or with which it may be consolidated, or any corporation resulting from any merger or consolidation to which the Rights Agent or any successor Rights Agent shall be a party, or any corporation succeeding to the stock transfer business of the Rights Agent or any successor Rights Agent, shall be the successor to the Rights Agent under this Agreement without the execution or filing of any paper or any further act on the part of any of the parties hereto, provided that such corporation would be eligible for appointment as a successor Rights Agent under the provisions of Section 21. In case at the time such successor Rights Agent shall succeed to the agency created by this Agreement any of the Right Certificates shall have been countersigned but not delivered, any such successor Rights Agent may adopt the countersignature of the predecessor Rights Agent and deliver such Right Certificates so countersigned, and in case at that time any of the Right Certificates shall not have been countersigned, any successor Rights Agent may countersign such Right Certificates either in the name of the predecessor Rights Agent or in the name of the successor Rights Agent and in all such cases such Right Certificates shall have the full force provided in the Right Certificates and in this Agreement.

(b) In case at any time the name of the Rights Agent shall be changed and at such time any of the Right Certificates shall have been countersigned but not delivered, the Rights Agent may adopt the countersignature under its prior name and deliver Right Certificates so countersigned, and in case at that time any of the Right Certificates shall not have been countersigned, the Rights Agent may countersign such Right Certificates either in its prior name or in its changed name, and in all such cases such Right Certificates shall have the full force provided in the Right Certificates and in this Agreement.

Section 20. Duties of Rights Agent. The Rights Agent undertakes the duties and obligations imposed by this Agreement upon the following terms and conditions, by all of which the Company and the holders of Right Certificates, by their acceptance thereof, shall be bound:

(a) The Rights Agent may consult with legal counsel (who may be legal counsel for the Company), and the opinion of such counsel shall be full and complete

authorization and protection to the Rights Agent as to any action taken or omitted by it in good faith and in accordance with such opinion.

(b) Whenever in the performance of its duties under this Agreement the Rights Agent shall deem it necessary or desirable that any fact or matter be proved or established by the Company prior to taking or suffering any action hereunder, such fact or matter (unless other evidence in respect thereof be herein specifically prescribed) may be deemed to be conclusively proved and established by a certificate signed by the President, any Vice President, or the Secretary of the Company and delivered to the Rights Agent, and such certificate shall be full authorization to the Rights Agent for any action taken or suffered in good faith by it under the provisions of this Agreement in reliance upon such certificate.

(c) The Rights Agent shall be liable hereunder only for its own negligence, bad faith or willful misconduct.

(d) The Rights Agent shall not be liable for or by reason of any of the statements of fact or recitals contained in this Agreement or in the Right Certificates (except its countersignature thereof) or be required to verify the same, but all such statements and recitals are and shall be deemed to have been made by the Company only.

(e) The Rights Agent shall not be under any responsibility in respect of the validity of this Agreement or the execution and delivery hereof (except the due execution hereof by the Rights Agent) or in respect of the validity or execution of any Right Certificate (except its countersignature thereof), nor shall it be responsible for any breach by the Company of any covenant or condition contained in this Agreement or in any Right Certificate, nor shall it be responsible for any adjustment required under the provisions of Section 11 or 13 or responsible for the manner, method or amount of any such adjustment or the ascertaining of the existence of facts that would require any such adjustment (except with respect to the exercise of Rights evidenced by Right Certificates after actual notice of any such adjustment), nor shall it by any act hereunder be deemed to make any representation or warranty as to the authorization or reservation of any shares of stock to be issued pursuant to this Agreement or any Right Certificate or as to whether any shares of stock will, when issued, be validly authorized and issued, fully paid and nonassessable.

(f) The Company agrees that it will perform, execute, acknowledge and deliver or cause to be performed, executed, acknowledged and delivered all such further and other acts, instruments and assurances as may reasonably be required by the Rights Agent for the carrying out or performance by the Rights Agent of the provisions of this Agreement.

(g) The Rights Agent is hereby authorized and directed to accept instructions with respect to the performance of its duties hereunder from the President, any Vice President or the Secretary of the Company, and to apply to such officers for advice or instructions in connection with its duties, and it shall not be liable for any action taken or suffered to be taken by it in good faith in accordance with instructions of any such officer.

(h) The Rights Agent and any shareholder, director, officer or employee of the Rights Agent may buy, sell or deal in any of the Rights or other securities of the Company or

become pecuniarily interested in any transaction in which the Company may be interested, or contract with or lend money to the Company or otherwise act as fully and freely as though it were not Rights Agent under this Agreement. Nothing herein shall preclude the Rights Agent from acting in any other capacity for the Company or for any other legal entity.

(i) The Rights Agent may execute and exercise any of the rights or powers hereby vested in it or perform any duty hereunder either itself or by or through its attorneys or agents, and the Rights Agent shall not be answerable or accountable for any act, default, neglect or misconduct of any such attorneys or agents or for any loss to the Company resulting from any such act, default, neglect or misconduct, provided reasonable care was exercised in the selection and continued employment thereof.

(j) If, with respect to any Right Certificate surrendered to the Rights Agent for exercise or transfer, the certificate attached to the form of assignment or form of election to purchase, as the case may be, has either not been completed or indicates an affirmative response to clause 1 and/or 2 thereof, the Rights Agent shall not take any further action with respect to such requested exercise or transfer without first obtaining the Company's approval.

Section 21. Change of Rights Agent. Unless the Company and the Rights Agent agree to a shorter time period, the Rights Agent or any successor Rights Agent may resign and be discharged from its duties under this Agreement upon 15 days' notice in writing mailed to the Company and to each transfer agent of Common Stock by registered or certified mail, and to the holders of the Right Certificates by first-class mail. Unless the Company and the Rights Agent agree to a shorter time period, the Company may remove the Rights Agent or any successor Rights Agent upon 15 days' notice in writing, mailed to the Rights Agent or successor Rights Agent, as the case may be, and to each transfer agent of Common Stock by registered or certified mail, and to the holders of the Right Certificates by first-class mail. If the Rights Agent shall resign or be removed or shall otherwise become incapable of acting, the Company shall appoint a successor to the Rights Agent. If the Company shall fail to make such appointment within a period of 15 days after such removal or after it has been notified in writing of such resignation or incapacity by the resigning or incapacitated Rights Agent or by the holder of a Right Certificate (who shall, with such notice, submit his Right Certificate for inspection by the Company), then the registered holder of any Right Certificate may apply to any court of competent jurisdiction for the appointment of a new Rights Agent. Any successor Rights Agent, whether appointed by the Company or by such a court, shall be a corporation organized and doing business under the laws of the United States or of any state of the United States in good standing, which is authorized under such laws to exercise stock transfer powers and is subject to supervision or examination by federal or state authority and which has at the time of its appointment as Rights Agent a combined capital and surplus of at least \$100,000,000. After appointment, the successor Rights Agent shall be vested with the same powers, rights, duties and responsibilities as if it had been originally named as Rights Agent without further act or deed, but the predecessor Rights Agent shall deliver and transfer to the successor Rights Agent any property at the time held by it hereunder, and execute and deliver any further assurance, conveyance, act or deed necessary for the purpose. Not later than the effective date of any such appointment, the Company shall file notice thereof in writing with the predecessor Rights Agent and each transfer agent of Common Stock and mail a notice thereof in writing to the registered holders of the Right Certificates. Failure to give any notice provided for in this Section 21, however, or any defect therein, shall

not affect the legality or validity of the resignation or removal of the Rights Agent or the appointment of the successor Rights Agent, as the case may be.

Section 22. Issuance of New Right Certificates. Notwithstanding any of the provisions of this Agreement or of the Rights to the contrary, the Company may, at its option, issue new Right Certificates evidencing Rights in such form as may be approved by its Board of Directors to reflect any adjustment or change in the Expiration Date, the Purchase Price per share or the number or kind or class of shares of stock or other securities or property purchasable under the Right Certificates made in accordance with the provisions of this Agreement.

Section 23. Redemption.

(a) The Board of Directors of the Company may, at its option and as provided herein, and notwithstanding the provisions of Sections 11 and 13 of this Agreement, elect to redeem all but not less than all of the then outstanding Rights at a redemption price of \$.01 per Right, appropriately adjusted to reflect any stock split, stock dividend, reclassification or similar transaction occurring after the date hereof (such redemption price being herein referred to as the "Redemption Price") at any time up to the Close of Business on a Stock Acquisition Date.

(b) Immediately upon the action of the Board of Directors of the Company electing to redeem the Rights, the Company shall make a public announcement thereof, and from and after the date of such announcement, without any further action and without any further notice, the right to exercise the Rights will terminate and the only right thereafter of the holders of Rights shall be to receive the Redemption Price. As soon as practicable after the election of the Board of Directors to redeem the Rights, the Company shall give notice of such redemption to the holders of the then outstanding Rights by mailing such notice to all such holders at their last addresses as they appear upon the registry books of the Rights Agent. Any notice which is mailed in the manner herein provided shall be deemed given, whether or not the holder receives the notice. Each such notice of redemption will state the method by which the payment of the Redemption Price will be made.

Section 24. Notice of Proposed Actions. In case the Company, after the Rights become exercisable, shall propose (i) to pay any dividend payable in stock of any class to the holders of its Common Stock or the Subject Shares or to make any other distribution to the holders of its Common Stock or Subject Shares (other than a regular periodic cash dividend), or (ii) to offer to the holders of its Common Stock or Subject Shares rights or warrants to subscribe for or to purchase any additional shares of Common Stock or shares of stock of any class or any other securities, rights or options, or (iii) to effect any reclassification of its Common Stock or Subject Shares (other than a reclassification involving only the subdivision of outstanding shares of Common Stock) or any recapitalization or reorganization of the Company, or (iv) to effect any consolidation or merger into or with, or to effect any sale or other transfer (or to permit one or more of its Subsidiaries to effect any sale or other transfer), in one or more transactions, of more than 50 percent of the assets or earning power of the Company and its Subsidiaries (taken as a whole) to, any other Person, or (v) to effect the liquidation, dissolution or winding up of the Company, then, in each such case, the Company shall give to each holder of a Right, in accordance with Section 25, a notice of such proposed action, which shall specify the record date for the purposes of such dividend, distribution of rights or warrants, or the date on which such

reclassification, recapitalization, reorganization, consolidation, merger, sale, transfer, liquidation, dissolution or winding up is to take place and the date of participation therein by the holders of Common Stock and/or Subject Shares, if any such date is to be fixed, and such notice shall be so given in the case of any action covered by clause (i) or (ii) above at least twenty days prior to the record date for determining holders of the Common Stock and/or Subject Shares for purposes of such action, and in the case of any such other action, at least twenty days prior to the date of the taking of such proposed action or the date of participation therein by the holders of Common Stock and/or Subject Shares, whichever shall be the earlier. The failure to give notice required by this Section 24 or any defect thereon shall not affect the legality or validity of the action taken by the Company or the vote upon any such action.

Section 25. Notices. Notices or demands authorized by this Agreement to be given or made by the Rights Agent or by the holder of any Right Certificate to or on the Company shall be sufficiently given or made if sent by first-class mail, postage prepaid, addressed (until another address is filed in writing with the Rights Agent) as follows:

Harris Trust Company of California
601 South Figueroa Street, 49th Floor
Los Angeles, California 90017

Subject to the provisions of Section 21, any notice or demand authorized by this Agreement to be given or made by the Company or by the holder of any Right Certificate to or on the Rights Agent shall be sufficiently given or made if sent by first-class mail, postage prepaid, addressed (until another address is filed in writing with the Company) as follows:

Southwest Gas Corporation
5241 Spring Mountain Road
P.O. Box 98510
Las Vegas, Nevada 89193-8510
Attention: Chief Financial Officer

Notices or demands authorized by this Agreement to be given or made by the Company or the Rights Agent to or on the holder of any Right Certificate shall be sufficiently given or made if sent by first-class mail, postage prepaid, addressed to such holder at the address of such holder as shown on the registry books of the Company.

Section 26. Supplements and Amendments. Prior to the Distribution Date and subject to the penultimate sentence of this Section 26, the Company and the Rights Agent shall, if the Company so directs, supplement or amend any provision of this Agreement without the approval of any holders of certificates representing shares of Common Stock. From and after the Distribution Date and subject to the penultimate sentence of this Section 26, the Company and the Rights Agent shall, if the Company so directs, supplement or amend this Agreement without the approval of any holders of Right Certificates in order (i) to cure any ambiguity, (ii) to correct or supplement any provision contained herein which may be defective or inconsistent with any other provisions herein, (iii) to shorten or lengthen any time period hereunder or (iv) to change or supplement the provisions hereof in any manner which the Company may deem necessary or

desirable and which shall not adversely affect the interests of the holders of Right Certificates; provided, however, this Agreement may not be supplemented or amended to lengthen, pursuant to clause (iii) of this sentence, (A) a time period relating to when the Rights may be redeemed at such time as the Rights are not then redeemable, or (B) any other time period, unless such lengthening is for the purpose of protecting, enhancing or clarifying the rights of, and/or the benefits to, the holders of Rights. Upon the delivery of a certificate from an appropriate officer of the Company which states that the proposed supplement or amendment is in compliance with the terms of this Section 26, the Rights Agent shall execute such supplement or amendment. Notwithstanding anything contained in this Agreement to the contrary: (1) no supplement or amendment shall be made which changes the Redemption Price, the Purchase Price or the number of shares or Units for which a Right is exercisable; and (2) the duration of the Rights may not be shortened without the written consent of the registered holders thereof (other than by a redemption of the Rights pursuant to Section 23). Prior to the Distribution Date, the interests of the holders of Rights shall be deemed coincident with the interests of the holders of Common Stock.

Section 27. Exchange.

(a) The Board of Directors of the Company may, at its option, at any time after any Person becomes an Acquiring Person, exchange all or part of the then outstanding and exercisable Rights (which shall not include Rights that have become subject to the provisions of Section 7(f) hereof) for Common Stock at an exchange ratio of one share of Common Stock per Right, appropriately adjusted to reflect any stock split, stock dividend or similar transaction occurring after the date hereof (such exchange ratio being hereinafter referred to as the "Exchange Ratio").

(b) Immediately upon the action of the Board of Directors of the Company ordering the exchange of any Rights pursuant to subsection (a) of this Section and without any further action and without any notice, the right to exercise such Rights shall terminate and the only right thereafter of a holder of such Rights shall be to receive that number of shares of Common Stock equal to the number of such Rights held by such holder multiplied by the Exchange Ratio. The Company shall promptly give public notice of any such exchange; provided, however, that the failure to give, or any defect in, such notice shall not affect the validity of such exchange. The Company promptly shall mail a notice of any such exchange to all of the holders of such Rights at their last addresses as they appear upon the registry books of the Rights Agent. Any notice which is mailed in the manner herein provided shall be deemed given, whether or not the holder receives the notice. Each such notice of exchange will state the method by which the exchange of the Common Stock for Rights will be effected and, in the event of any partial exchange, the number of Rights which will be exchanged. Any partial exchange shall be effected pro rata based on the number of Rights (other than Rights which have become subject to the provisions of Section 7(f) hereof) held by each holder of Rights.

(c) In the event that there shall not be sufficient authorized Common Stock to permit an exchange of Rights as contemplated in accordance with this Section, the Company shall take all such action as may be necessary to authorize additional Common Stock or Equivalent Stock for issuance upon exchange of the Rights.

Section 28. Successors. All the covenants and provisions of this Agreement by or for the benefit of the Company or the Rights Agent shall bind and inure to the benefit of their respective successors and assigns hereunder.

Section 29. Determination and Actions Taken by the Board of Directors. For all purposes of this Agreement, any calculation of the number of shares of Common Stock (or other applicable securities hereunder) outstanding at any particular time, including for purposes of determining the particular percentage of such outstanding shares of Common Stock (or other securities) of which any Person is the Beneficial Owner, shall be made in accordance with the last sentence of Rule 13d-3(d)(1)(i) (as in effect on the date of this Agreement) of the General Rules and Regulations under the Exchange Act. The Board of Directors of the Company shall have the exclusive power and authority to administer this Agreement and to exercise all rights and powers specifically granted to such Board or to the Company, or as may be necessary or advisable in the administration of this Agreement, including without limitation the right and power to (i) interpret the provisions of this Agreement, and (ii) make all determinations deemed necessary or advisable for the administration of this Agreement (including a determination to redeem or not redeem the Rights or to amend the Agreement). All such actions, calculations, interpretations and determinations (including, for purposes of clause (B) below, all omissions with respect to the foregoing) which are done or made by the Board in good faith, shall (A) be final, conclusive and binding on the Company, the Rights Agent, the holders of the Rights and all other parties, and (B) not subject the Board to any liability to the holders of the Rights.

Section 30. Conditions to the Agreement. The effectiveness of this Agreement and each and every right and obligation obtained or incurred pursuant hereto, including, but not limited to, the exercisability of the Rights, is conditioned upon (a) the Company having received all necessary approvals and consents from all local, state and federal regulatory authorities having jurisdiction over the Company and the transactions contemplated by this Agreement and (b) the absence of any statute, rule, regulation, injunction or other order (whether temporary, preliminary or permanent) enacted, issued, promulgated, enforced or entered into by any United States, state or local legislative body, governmental agency or commission or court of competent jurisdiction which is in effect and has the effect of making the distribution or exercise of the Rights illegal or otherwise prohibiting the consummation of the transactions contemplated by this Agreement.

Section 31. Benefits of this Agreement. Nothing in this Agreement shall be construed to give to any Person other than the Company, the Rights Agent and the registered holders of the Right Certificates (and, prior to the Distribution Date, the holders of Common Stock) any legal or equitable right, remedy or claim under this Agreement. This Agreement shall be for the sole and exclusive benefit of the Company, the Rights Agent and the registered holders of the Right Certificates (and, prior to the Distribution Date, the holders of Common Stock).

Section 32. Governing Law. This Agreement and each Right Certificate issued hereunder shall be deemed to be a contract made under the laws of the State of California and for all purposes shall be governed by and construed in accordance with the laws of such State applicable to contracts to be made and performed entirely within such State. The rights and obligations of the Rights Agent under this Agreement shall be governed by and construed in accordance with the laws in effect in the State of California.

Section 33. Counterparts. This Agreement may be executed in any number of counterparts and each of such counterparts shall for all purposes be deemed to be an original, and all such counterparts shall together constitute but one and the same instrument.

Section 34. Section Headings. Descriptive headings of the several Sections of this Agreement are inserted for convenience only and shall not control or affect the meaning or construction of any of the provisions hereof.

Section 35. Severability. If any term, provision, covenant or restriction of this Agreement is held by a court of competent jurisdiction or other authority to be invalid, illegal, or unenforceable, (i) such invalid, illegal or unenforceable term, provision, covenant or restriction shall nevertheless be valid, legal and enforceable to the extent, if any, provided by such court or authority, and (ii) the remainder of the terms, provisions, covenants and restrictions of this Agreement shall remain in full force and effect and shall in no way be affected, impaired or invalidated.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed as of the day and year first above written.

SOUTHWEST GAS CORPORATION:

By: /s/ Jeffrey W. Shaw

Title: Vice President/Treasurer

HARRIS TRUST COMPANY OF CALIFORNIA:

By: /s/ John A. Castellanos

Title: Assistant Vice President

Exhibit A

[Form of Right Certificate]

Certificate No. R-

_____ Rights

NOT EXERCISABLE AFTER PUBLIC ANNOUNCEMENT OF REDEMPTION IS MADE. THE RIGHTS ARE SUBJECT TO REDEMPTION, AT THE OPTION OF THE COMPANY, AT \$.01 PER RIGHT ON THE TERMS SET FORTH IN THE AGREEMENT. IN THE EVENT THAT THE RIGHTS REPRESENTED BY THIS CERTIFICATE ARE ISSUED TO A PERSON WHO IS AN ACQUIRING PERSON OR AN ASSOCIATE OR AFFILIATE THEREOF (AS SUCH TERMS ARE DEFINED IN THE RIGHTS AGREEMENT) OR CERTAIN TRANSFEREES THEREOF, THIS RIGHT CERTIFICATE AND THE RIGHTS REPRESENTED HEREBY MAY BE SUBJECT TO CERTAIN LIMITATIONS IN THE CIRCUMSTANCES SPECIFIED IN SECTION 7 OF THE RIGHTS AGREEMENT.

RIGHT CERTIFICATE

This certifies that _____, or registered assigns, is the registered owner of the number of Rights set forth above, each of which entitles the owner thereof, subject to the terms, provisions and conditions of the Amended And Restated Rights Agreement, dated as of _____, 1998 (the "Rights Agreement"), between Southwest Gas Corporation, (the "Company"), and Harris Trust Company of California (the "Rights Agent"), to purchase from the Company, unless the Rights have been previously redeemed, at any time after the Distribution Date (as such term is defined in the Rights Agreement) and prior to the Expiration Date (as such term is defined in the Rights Agreement), or the date, if any, on which the Rights evidenced by this Certificate may be redeemed, at the stock transfer office of the Rights Agent, or its successors as Rights Agent, one one-hundredth of a fully paid and nonassessable share of Junior Participating Preference Stock ("Preference Shares"), at a purchase price of \$45.00 (the "Purchase Price"), upon presentation and surrender of this Right Certificate with the Form of Election to Purchase duly completed and executed. The number of Rights evidenced by this Right Certificate as set forth above (and the number of shares which may be purchased upon exercise thereof), and the Purchase Price set forth above, are the number and Purchase Price as of the date of the Rights Agreement based on the Preference Shares as constituted on such date.

Upon the occurrence of an event described in clause (A), (B), (C) or (D) of Section 11(a)(ii) of the Rights Agreement, the holder of any Rights that are, or were, beneficially owned by an Acquiring Person or an Associate or Affiliate thereof (as such terms are defined in the Rights Agreement) or certain transferees thereof which engaged in, or realized the benefit of, an event or transaction or transactions described in clause (A), (B), (C) or (D) of such Section 11(a)(ii), shall not be entitled to the benefit of the adjustment described in such Section 11(a)(ii).

As provided in the Rights Agreement, the Purchase Price and the number and class of shares which may be purchased upon the exercise of the Rights evidenced by this Right Certificate are subject to modification and adjustment upon the happening of certain events.

This Right Certificate is subject to all of the terms, provisions and conditions of the Rights Agreement, which terms, provisions and conditions are hereby incorporated herein by reference and made a part hereof and to which Rights Agreement reference is hereby made for a full description of the rights, limitations of rights, obligations, duties and immunities hereunder of the Rights Agent, the Company and the holders of the Right Certificates, which limitations of rights include the temporary suspension of the exercisability of such Rights under specific circumstances set forth in the Rights Agreement. Copies of the Rights Agreement are on file at the above-mentioned office of the Rights Agent and at the principal office of the Company.

This Right Certificate, with or without other Right Certificates, upon surrender at the stock transfer office of the Rights Agent set forth above, may be exchanged for another Right Certificate or Right Certificates of like tenor and date evidencing Rights entitling the holder to purchase such number of shares as the Rights evidenced by the Right Certificate or Right Certificates surrendered shall have entitled such holder to purchase. If this Right Certificate shall be exercised in part, the holder shall be entitled to receive upon surrender hereof another Right Certificate or Right Certificates for the number of whole Rights not exercised.

Subject to the provisions of the Rights Agreement, the Rights evidenced by this Certificate may be redeemed by the Company at its option at a redemption price of \$.01 per Right.

No fractional shares will be issued upon the exercise of any Rights evidenced hereby, but in lieu thereof a cash payment may be made, as provided in the Rights Agreement.

No holder of this Right Certificate shall be entitled to vote or receive dividends or be deemed for any purpose the holder of shares or of any other securities of the Company which may at any time be issuable on the exercise hereof, nor shall anything contained in the Rights Agreement or herein be construed to confer upon the holder hereof, as such, any of the rights of a shareholder of the Company or any right to vote for the election of directors or upon any matter submitted to shareholders at any meeting thereof, or to give or withhold consent to any corporate action, or to receive notice of meetings or other actions affecting shareholders (except as provided in the Rights Agreement), or to receive dividends or subscription rights, or otherwise, until the Right or Rights evidenced by this Right Certificate shall have been exercised as provided in the Rights Agreement.

This Right Certificate shall not be valid or obligatory for any purpose until it shall have been countersigned by the Rights Agent.

WITNESS the facsimile signatures of the proper officers of the Company.

Dated as of _____, ____.

SOUTHWEST GAS CORPORATION

By: _____
Title:

Countersigned:

HARRIS TRUST COMPANY OF CALIFORNIA

By: _____

By: _____
Authorized Signature

[Form of Reverse Side of Right Certificate]

FORM OF ASSIGNMENT

(To be executed by the registered holder if such holder desires to transfer the Right Certificate.)

FOR VALUE RECEIVED _____ hereby sells, assigns and transfers unto _____

(Please print name and address of transferee)

this Right Certificate, together with all right, title and interest therein, and does hereby irrevocably constitute and appoint _____ Attorney to transfer the within Right Certificate on the books of the within-named Corporation, with full power of substitution.

Dated: _____, _____ Signature

Signature Guaranteed:

CERTIFICATE

The undersigned hereby certifies (after due inquiry and to the best knowledge of the undersigned) by checking the appropriate boxes that:

(1) this Right Certificate [] is [] is not being sold, assigned and transferred by or on behalf of a Person who is or was an Acquiring Person or an Affiliate or Associate of an Acquiring Person (as such terms are defined in the Rights Agreement);

(2) the undersigned [] did [] did not acquire the Rights evidenced by this Right Certificate from any Person who is, was or subsequently became an Acquiring Person or an Affiliate or Associate of an Acquiring Person.

Date: _____, _____ Signature

Signature Guaranteed:

NOTICE

The signature to the foregoing Assignment and Certificate must correspond to the name as written upon the face of this Right Certificate in every particular, without alteration or enlargement or any change whatsoever.

FORM OF ELECTION TO PURCHASE

(To be executed if holder desires to exercise the Right Certificate.)

To Southwest Gas Corporation and [Rights Agent]:

The undersigned hereby irrevocably elects to exercise _____ Rights represented by this Right Certificate and to purchase the shares issuable upon the exercise of such Rights and requests that certificates for such shares be issued in the name of:

Please insert social security or other identifying number: _____

(Please print name and address)

_____ If such number of Rights shall not be all the Rights evidenced by this Right Certificate, a new Right Certificate for the balance remaining of such Rights shall be registered in the name of and delivered to:

Please insert social security or other identifying number: _____

(Please print name and address)

Dated: _____, _____

Signature: _____
(Signature must conform in all respects to name of holder as specified on the face of this Right Certificate)

Signature Guaranteed:

CERTIFICATE

The undersigned hereby certifies (after due inquiry and to the best knowledge of the undersigned) by checking the appropriate boxes that:

(1) the Rights evidenced by this Right Certificate [] are [] are not being exercised by or on behalf of a Person who is or was an Acquiring Person or an Affiliate or Associate of an Acquiring Person (as such terms are defined in the Rights Agreement);

(2) the undersigned [] did [] did not acquire the Rights evidenced by this Right Certificate from any person who is, was or subsequently became an Acquiring Person or an Affiliate or Associate of an Acquiring Person.

Date: _____, _____
Signature

Signature Guaranteed:

NOTICE

The signature to the foregoing Election to Purchase and Certificate must correspond to the name as written upon the face of this Right Certificate in every particular, without alteration or enlargement or any change whatsoever.

EXHIBIT B

[Form of Summary of Rights]

On March 5, 1996, the Board of Directors of Southwest Gas Corporation (the "Company") declared a distribution of one Right for each outstanding share of common stock (the "Common Stock") of the Company. The distribution is to be made as of April 15, 1996 (the "Record Date") to the shareholders of record on that date. Each Right entitles the registered holder to purchase from the Company, initially, one one-hundredth of a share of Junior Participating Preference Stock ("Preference Stock") at a price of \$45.00 (the "Purchase Price"), subject to adjustment. The description and terms of the Rights are set forth in a Rights Agreement between the Company and Harris Trust Company of California, as Rights Agent.

Shares of Preference Stock purchasable upon exercise of the Rights will be entitled to dividends of 100 times the dividends, per share, declared on shares of the Common Stock and in the event of liquidation will be entitled to a minimum preferential liquidating distribution of \$100 per share and an aggregate liquidating distribution, per share, of 100 times the distribution made per share of Common Stock. In the event no dividends are declared on shares of Common Stock, holders of Preference Stock will be entitled to receive at least \$1.00 per share of Common Stock for each quarter that a dividend is not declared on shares of Common Stock. The holders of Preference Stock will vote together with holders of Common Stock and in the event of any merger, consolidation or other transaction in which shares of Common Stock are exchanged, each share of Preference Stock will be entitled to receive 100 times the amount received per each share of Common Stock.

Because of the Preference Stock' dividend and liquidation rights, the value when issued of the one one-hundredth interest in a share of Preference Stock purchasable upon exercise of each Right should approximate the value of one share of Common Stock.

Until the earlier to occur of (i) 10 business days following a public announcement that a person or group of affiliated or associated persons (an "Acquiring Person") has acquired beneficial ownership of 20% or more of the Company's general voting power other than pursuant to a Qualified Offer (as defined below), the date of such public announcement being called the "Stock Acquisition Date," or (ii) 10 business days (or such later date as may be determined by action of the Board of Directors) following the commencement of, or announcement of an intention to make, a tender offer or exchange offer the consummation of which would result in the beneficial ownership by a person or group of 20% or more of the Company's general voting power (the date of such earlier occurrence being called the "Distribution Date"), the Rights will be evidenced by the certificates representing the Common Stock and will be transferred with and only with the Common Stock. New Common Stock certificates issued after the Record Date upon transfer or new issuance of shares of Common Stock will contain a notation incorporating the Rights Agreement by reference, and the surrender for transfer of any certificate for shares of Common Stock, even without such notation or a copy of this Summary of Rights being attached thereto, will also constitute the transfer of the Rights associated with the shares of Common Stock represented by such certificate. As soon as

practicable following the Distribution Date, separate certificates evidencing the Rights ("Right Certificates") will be mailed to holders of record of the Common Stock as of the close of business on the Distribution Date and such separate Right Certificates alone will evidence the Rights.

The Rights are not exercisable until the Distribution Date. The Rights will expire on the tenth anniversary of the Record Date (the "Final Expiration Date"), unless the Final Expiration Date is extended or unless the Rights are earlier redeemed or exchanged by the Company, as described below.

The Purchase Price payable, the number of shares or other securities or property issuable upon exercise of the Rights, and the number of outstanding Rights, are subject to adjustment from time to time to prevent dilution.

A Qualified Offer is a tender offer or exchange offer for all outstanding shares of Common Stock which is determined by the non-affiliated directors to be adequate and otherwise in the best interests of the Company and its shareholders.

In the event that any person becomes an Acquiring Person other than by a purchase pursuant to a Qualified Offer, proper provision shall be made so that each holder of a Right, other than Rights beneficially owned by the Acquiring Person (which will not be entitled to the benefit of such adjustment) will thereafter have the right to receive upon exercise that number of shares of Common Stock or Common Stock equivalents having a market value of two times the exercise price of the Right.

In the event that, at any time after an Acquiring Person has become such, the Company is acquired in a merger or other business combination transaction (other than a merger which follows a Qualified Offer at the same or a higher price) or 50% or more of its consolidated assets or earning power are sold, proper provision will be made so that each holder of a Right will thereafter have the right to receive, upon the exercise thereof at the then current exercise price of the Right, that number of shares of common stock of the acquiring company which at the time of such transaction will have a market value of two times the exercise price of the Right.

At any time after an Acquiring Person has become such, the Board of Directors of the Company may exchange the Rights (other than Rights owned by such person or group), in whole or in part, at an exchange ratio of one share of Common Stock per Right (subject to adjustment).

Up to and including the tenth business day after a Stock Acquisition Date, the Board of Directors of the Company may redeem the Rights in whole, but not in part, at a price of \$.01 per Right (the "Redemption Price"). Immediately upon any redemption of the Rights, the right to exercise them will terminate and the only right of the holders will be to receive the Redemption Price.

The terms of the Rights may be amended by the Board of Directors without the consent of the holders of the Rights at any time prior to the Distribution Date. Thereafter the Rights may be amended to make changes which do not adversely affect the interests of the

holders of the Rights, or which shorten or lengthen time periods, subject to certain limitations set forth in the Rights Agreement.

Until a Right is exercised, the holder thereof, as such, will have no rights as a shareholder of the Company, including, but, not limited to, the right to vote or to receive dividends. The exercise of the Rights is subject to compliance with applicable legal and regulatory requirements, including, approval of the California Public Utilities Commission.

A copy of the Rights Agreement has been filed with the Securities and Exchange Commission as an Exhibit to a registration statement on Form 8-A. A copy of the Rights Agreement is available free of charge from the Company. This summary description of the Rights does not purport to be complete and is qualified in its entirety by reference to the Rights Agreement, which is incorporated herein by reference.

SOUTHWEST GAS CORPORATION
COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES
(THOUSANDS OF DOLLARS)

| CONTINUING OPERATIONS | FOR THE YEAR ENDED DECEMBER 31, | | | | |
|---|---------------------------------|------------------|------------------|------------------|------------------|
| | 1998 | 1997 | 1996 | 1995 | 1994 |
| 1. Fixed charges: | | | | | |
| A) Interest expense | \$ 63,416 | \$ 63,247 | \$ 54,674 | \$ 52,844 | \$ 48,688 |
| B) Amortization | 1,243 | 1,164 | 1,494 | 1,569 | 1,426 |
| C) Interest portion of rentals | 7,531 | 6,973 | 6,629 | 4,435 | 4,743 |
| D) Preferred securities distributions | 5,475 | 5,475 | 5,475 | 913 | 0 |
| Total fixed charges | <u>\$ 77,665</u> | <u>\$ 76,859</u> | <u>\$ 68,272</u> | <u>\$ 59,761</u> | <u>\$ 54,857</u> |
| 2. Earnings (as defined): | | | | | |
| E) Pretax income from continuing operations | \$ 83,951 | \$ 21,328 | \$ 10,448 | \$ 3,493 | \$ 38,119 |
| Fixed Charges (1. above) | 77,665 | 76,859 | 68,272 | 59,761 | 54,857 |
| Total earnings as defined | <u>\$ 161,616</u> | <u>\$ 98,187</u> | <u>\$ 78,720</u> | <u>\$ 63,254</u> | <u>\$ 92,976</u> |
| 3. Ratio of earnings to fixed charges | <u>2.08</u> | <u>1.28</u> | <u>1.15</u> | <u>1.06</u> | <u>1.69</u> |

| ADJUSTED FOR INTEREST ALLOCATED TO DISCONTINUED OPERATIONS | FOR THE YEAR ENDED DECEMBER 31, | | | | |
|--|---------------------------------|------------------|------------------|------------------|-------------------|
| | 1998 | 1997 | 1996 | 1995 | 1994 |
| 1. Fixed charges: | | | | | |
| A) Interest expense | \$ 63,416 | \$ 63,247 | \$ 54,674 | \$ 52,844 | \$ 48,688 |
| B) Amortization | 1,243 | 1,164 | 1,494 | 1,569 | 1,426 |
| C) Interest portion of rentals | 7,531 | 6,973 | 6,629 | 4,435 | 4,743 |
| D) Preferred securities distributions | 5,475 | 5,475 | 5,475 | 913 | -- |
| E) Allocated interest [1] | -- | -- | -- | 9,636 | 7,874 |
| Total fixed charges | <u>\$ 77,665</u> | <u>\$ 76,859</u> | <u>\$ 68,272</u> | <u>\$ 69,397</u> | <u>\$ 62,731</u> |
| 2. Earnings (as defined): | | | | | |
| F) Pretax income from continuing operations | \$ 83,951 | \$ 21,328 | \$ 10,448 | \$ 3,493 | \$ 38,119 |
| Fixed Charges (1. above) | 77,665 | 76,859 | 68,272 | 69,397 | 62,731 |
| Total earnings as defined | <u>\$ 161,616</u> | <u>\$ 98,187</u> | <u>\$ 78,720</u> | <u>\$ 72,890</u> | <u>\$ 100,850</u> |
| 3. Ratio of earnings to fixed charges | <u>2.08</u> | <u>1.28</u> | <u>1.15</u> | <u>1.05</u> | <u>1.61</u> |

[1] Represents allocated interest through the period ended December 31, 1995. Carrying costs for the period subsequent to year end through the disposition of the discontinued operations were accrued and recorded as disposal costs.

SOUTHWEST GAS CORPORATION
 COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES AND PREFERRED DIVIDENDS
 (THOUSANDS OF DOLLARS)

| CONTINUING OPERATIONS | FOR THE YEAR ENDED DECEMBER 31, | | | | |
|---|---------------------------------|-----------|-----------|-----------|-----------|
| | 1998 | 1997 | 1996 | 1995 | 1994 |
| 1. Combined fixed charges: | | | | | |
| A) Total fixed charges | \$ 77,665 | \$ 76,859 | \$ 68,272 | \$ 59,761 | \$ 54,857 |
| B) Preferred dividends [1] | - | - | - | 404 | 826 |
| Total fixed charges and preferred dividends | \$ 77,665 | \$ 76,859 | \$ 68,272 | \$ 60,165 | \$ 55,683 |
| 2. Earnings | \$ 161,616 | \$ 98,187 | \$ 78,720 | \$ 63,254 | \$ 92,976 |
| 3. Ratio of earnings to fixed charges and preferred dividends | 2.08 | 1.28 | 1.15 | 1.05 | 1.67 |

| ADJUSTED FOR INTEREST ALLOCATED TO DISCONTINUED OPERATIONS | FOR THE YEAR ENDED DECEMBER 31, | | | | |
|---|---------------------------------|-----------|-----------|-----------|------------|
| | 1998 | 1997 | 1996 | 1995 | 1994 |
| 1. Combined fixed charges: | | | | | |
| A) Total fixed charges | \$ 77,665 | \$ 76,859 | \$ 68,272 | \$ 69,397 | \$ 62,731 |
| B) Preferred dividends [1] | - | - | - | 404 | 826 |
| Total fixed charges and preferred dividends | \$ 77,665 | \$ 76,859 | \$ 68,272 | \$ 69,801 | \$ 63,557 |
| 2. Earnings | \$ 161,616 | \$ 98,187 | \$ 78,720 | \$ 72,890 | \$ 100,850 |
| 3. Ratio of earnings to fixed charges and preferred dividends | 2.08 | 1.28 | 1.15 | 1.04 | 1.59 |

[1] Preferred and preference dividends have been adjusted to represent the pretax earnings necessary to cover such dividend requirements.

| Year Ended December 31, | 1998 | 1997 | 1996 | 1995 | 1994 |
|--|-------------|-------------|-------------|-------------|-------------|
| (Thousands of dollars, except per share amounts) | | | | | |
| Operating revenues..... | \$ 917,309 | \$ 732,010 | \$ 644,061 | \$ 563,502 | \$ 599,553 |
| Operating expenses..... | 763,139 | 629,749 | 572,488 | 505,090 | 510,863 |
| Operating income..... | \$ 154,170 | \$ 102,261 | \$ 71,573 | \$ 58,412 | \$ 88,690 |
| Income from continuing operations..... | \$ 47,537 | \$ 16,469 | \$ 6,574 | \$ 2,654 | \$ 23,524 |
| Income (loss) from discontinued operations, net of tax()1..... | -- | -- | -- | (17,536) | 2,777 |
| Net income (loss)..... | \$ 47,537 | \$ 16,469 | \$ 6,574 | \$ (14,882) | \$ 26,301 |
| Net income (loss) applicable to common stock..... | \$ 47,537 | \$ 16,469 | \$ 6,574 | \$ (15,189) | \$ 25,791 |
| Total assets at year end..... | \$1,830,694 | \$1,769,059 | \$1,560,269 | \$1,532,527 | \$1,453,582 |
| Capitalization at year end | | | | | |
| Common equity..... | \$ 476,400 | \$ 385,979 | \$ 379,616 | \$ 356,050 | \$ 348,556 |
| Preferred stocks..... | -- | -- | -- | -- | 4,000 |
| Trust originated preferred securities..... | 60,000 | 60,000 | 60,000 | 60,000 | -- |
| Long-term debt..... | 812,906 | 778,693 | 665,221 | 607,945 | 678,263 |
| | \$1,349,306 | \$1,224,672 | \$1,104,837 | \$1,023,995 | \$1,030,819 |
| Common stock data | | | | | |
| Return on average common equity..... | 11.0% | 4.3% | 1.8% | (4.1)% | 7.6% |
| Basic earnings (loss) per share | | | | | |
| Continuing operations..... | \$ 1.66 | \$ 0.61 | \$ 0.25 | \$ 0.10 | \$ 1.09 |
| Discontinued operations..... | -- | -- | -- | (0.76) | 0.13 |
| Basic earnings (loss) per share..... | \$ 1.66 | \$ 0.61 | \$ 0.25 | \$ (0.66) | \$ 1.22 |
| Diluted earnings (loss) per share..... | \$ 1.65 | \$ 0.61 | \$ 0.25 | \$ (0.66) | \$ 1.22 |
| Dividends paid per share..... | \$ 0.82 | \$ 0.82 | \$ 0.82 | \$ 0.82 | \$ 0.80 |
| Payout ratio..... | 49% | N/A | N/A | N/A | 66% |
| Book value per share at year end..... | \$ 15.67 | \$ 14.09 | \$ 14.20 | \$ 14.55 | \$ 16.38 |
| Market value per share at year end..... | \$ 26.63 | \$ 18.69 | \$ 19.25 | \$ 17.63 | \$ 14.13 |
| Market value per share to book value per share..... | 170% | 133% | 136% | 121% | 86% |
| Common shares outstanding at year end (000)..... | 30,410 | 27,387 | 26,733 | 24,467 | 21,282 |
| Number of common shareholders at year end..... | 24,489 | 25,833 | 26,371 | 25,133 | 20,765 |
| Ratio of earnings to fixed charges | | | | | |
| Continuing operations..... | 2.08 | 1.28 | 1.15 | 1.06 | 1.69 |
| Adjusted for interest allocated to discontinued operations... | 2.08 | 1.28 | 1.15 | 1.05 | 1.61 |

1. Contribution from the financial services segment, including the 1995 loss on sale of the Bank.

| Year Ended December 31, | 1998 | 1997 | 1996 | 1995 | 1994 |
|--|-------------|-------------|-------------|-------------|-------------|
| (Thousands of dollars) | | | | | |
| Sales..... | \$ 753,338 | \$ 569,542 | \$ 506,200 | \$ 524,914 | \$ 560,207 |
| Transportation..... | 46,259 | 45,123 | 40,161 | 38,588 | 39,061 |
| Other..... | -- | -- | -- | -- | 285 |
| Operating revenue..... | 799,597 | 614,665 | 546,361 | 563,502 | 599,553 |
| Net cost of gas sold..... | 329,849 | 209,338 | 187,580 | 227,456 | 249,922 |
| Operating margin..... | 469,748 | 405,327 | 358,781 | 336,046 | 349,631 |
| Expenses | | | | | |
| Operations and maintenance.... | 209,172 | 201,159 | 198,364 | 187,969 | 178,310 |
| Depreciation and amortization..... | 80,231 | 74,528 | 67,443 | 62,492 | 57,284 |
| Other..... | 31,646 | 29,393 | 28,156 | 27,173 | 25,347 |
| Operating income..... | \$ 148,699 | \$ 100,247 | \$ 64,818 | \$ 58,412 | \$ 88,690 |
| Contribution to consolidated net income (loss)..... | \$ 44,830 | \$ 15,825 | \$ 3,919 | \$ 2,654 | \$ 23,524 |
| Total assets at year end..... | \$1,772,418 | \$1,717,025 | \$1,498,099 | \$1,357,034 | \$1,277,727 |
| Net gas plant at year end..... | \$1,459,362 | \$1,360,294 | \$1,278,457 | \$1,137,750 | \$1,035,916 |
| Construction expenditures and property additions..... | \$ 179,361 | \$ 164,528 | \$ 210,743 | \$ 166,183 | \$ 141,390 |
| Cash flow, net | | | | | |
| From operating activities..... | \$ 189,465 | \$ 45,923 | \$ 47,931 | \$ 97,754 | \$ 84,074 |
| From investing activities..... | (176,731) | (170,455) | (41,804) | (163,718) | (141,547) |
| From financing activities..... | (12,632) | 132,349 | (11,456) | 71,056 | 61,422 |
| Net change in cash..... | \$ 102 | \$ 7,817 | \$ (5,329) | \$ 5,092 | \$ 3,949 |
| Total throughput (thousands of therms) | | | | | |
| Sales..... | 1,103,264 | 914,732 | 818,329 | 805,884 | 881,868 |
| Transportation..... | 1,001,372 | 1,030,857 | 968,208 | 1,016,011 | 914,791 |
| Total throughput..... | 2,104,636 | 1,945,589 | 1,786,537 | 1,821,895 | 1,796,659 |
| Weighted average cost of gas purchased (\$/therm)..... | \$ 0.27 | \$ 0.35 | \$ 0.27 | \$ 0.21 | \$ 0.30 |
| Customers at year end..... | 1,209,000 | 1,151,000 | 1,092,000 | 1,029,000 | 980,000 |
| Employees at year end..... | 2,429 | 2,447 | 2,420 | 2,383 | 2,359 |
| Degree days -- actual..... | 2,321 | 1,976 | 1,896 | 1,781 | 2,091 |
| Degree days -- ten-year average..... | 2,043 | 2,022 | 2,033 | 2,021 | 2,068 |

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 its regulated natural gas transmission and distribution activities and nonregulated activities. In 1996, the Company completed the sale of PriMerit Bank, Federal Savings Bank (the Bank), which was reported as discontinued operations. The loss on disposition was included in the 1995 results of operations.

The Company is principally engaged in the business of purchasing, transporting, and distributing natural gas (Southwest or natural gas operations segment). Southwest is the largest distributor in Arizona, selling and transporting natural gas in most of southern, central, and northwestern Arizona, including the Phoenix and Tucson metropolitan areas. Southwest is also the largest distributor and transporter of natural gas in Nevada, and serves 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 in northern California and high desert and mountain areas in San Bernardino County.

As of December 31, 1998 Southwest had 1,209,000 residential, commercial, industrial, and other customers, of which 689,000 customers were located in Arizona, 403,000 in Nevada, and 117,000 in California. Residential and commercial customers represented over 99 percent of the total customer base. During 1998, Southwest added 58,000 customers, a five percent increase, of which 28,000 customers were added in Arizona, 28,000 in Nevada, and 2,000 in California. Customer growth over the past three years averaged over 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 five percent in 1999. During 1998, 57 percent of operating margin was earned in Arizona, 33 percent in Nevada, and 10 percent in California. During this same period, Southwest earned 84 percent of operating margin from residential and small commercial customers, 5 percent from other sales customers, and 11 percent from transportation customers. These patterns are similar to prior years and are expected to continue.

In April 1996, the Company acquired all of the outstanding stock of Northern Pipeline Construction Co. (Northern or construction services segment) pursuant to a definitive agreement dated November 1995. The Company issued approximately 1,439,000 shares of common stock valued at \$24 million in connection with the acquisition. The acquisition was accounted for as a purchase. Goodwill in the amount of approximately \$10 million was recorded by Northern and is being amortized over 25 years. Northern provides utility companies with trenching and installation, replacement, and maintenance services for energy distribution systems.

In December 1998, the Boards of Directors of the Company and ONEOK, Inc. (ONEOK), headquartered in Tulsa, Oklahoma, announced a definitive agreement for the Company to be merged into ONEOK. The agreement calls for ONEOK to pay cash of \$28.50 for each share of Company common stock outstanding. The transaction is subject to customary conditions, including approvals from shareholders of the Company and state regulators in Arizona, California, and Nevada. ONEOK expects to account for the merger using the purchase method of accounting. If the merger is consummated, the Company would operate as a division of ONEOK.

In connection with the proposed merger into ONEOK, the Company incurred approximately \$1.1 million (pretax) of financial advisor and legal costs, which were included in Other income (deductions), net, during the fourth quarter of 1998. Additional amounts of financial advisor, legal, and accounting-related expenses will be incurred during the merger process and, depending on the successful completion of the merger, are estimated at \$2 million to \$5 million.

In February 1999, the Company announced that it had received an unsolicited proposal from Southern Union Company (Southern Union), headquartered in Austin, Texas, offering to acquire the Company for \$32.00 per share in cash. The proposal is preliminary in nature and subject to a number of contingencies and uncertainties. Under the terms of the agreement with ONEOK, as a result of certain preliminary determinations made by the Board of Directors of the Company, the Board of Directors has authorized management to commence substantive discussions with Southern Union regarding its proposal. No assurances can be given that any agreement will be reached with Southern Union. The merger agreement with ONEOK remains in full force and effect.

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 population growth throughout its service territories. This growth has required large amounts of capital to finance the investment in infrastructure, in the form of new transmission and distribution plant, to satisfy consumer demand. For example, during the three-year period ended December 31, 1998, total gas plant increased from \$1.6 billion to \$2 billion, or at an annual rate of nine percent.

During 1998, capital expenditures were \$179 million. Approximately 75 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 \$166 million of the required capital resources pertaining to these construction expenditures. The remainder was provided from net external financing activities. The improvement in operating cash flows from expected levels was due to higher earnings and timing differences principally associated with deferred purchased gas cost recoveries and income taxes.

Southwest estimates construction expenditures during the three-year period ending December 31, 2001 will be approximately \$580 million. During the three-year period, cash flow from operating activities (net of dividends) is estimated to fund approximately 60 percent of the gas operations total construction expenditures. A portion of the construction expenditure funding will be provided by \$20 million of funds held in trust, at December 31, 1998, from the issuance of industrial development revenue bonds (IDRB). 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 merger-related developments (see Note 13 of the Notes to Consolidated Financial Statements). These external financings may include the issuance of both debt and equity securities, bank and other short-term borrowings, and other forms of financing. Under the definitive agreement with ONEOK, common stock issuances are currently limited to those necessary under employee benefit and dividend reinvestment plans.

Liquidity refers to the ability of an enterprise to generate adequate amounts of cash to meet its cash requirements. 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, and the level of 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. Southwest must first obtain regulatory approval before changing the rates it charges for recovery of gas costs. 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. 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. Generally, tariffs for Southwest provide for annual adjustment dates for changes in purchased gas costs. In addition, Southwest may request to adjust rates more often than once each year, if conditions warrant. These changes impact cash flows but have no direct impact on profit margin. See RATES AND REGULATORY PROCEEDINGS for details of these filings.

The Company has established 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 1998.

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 Investor Service 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).

Since September 1997, Duff & Phelps Credit Rating Co. has rated Company unsecured long-term debt at BBB. Duff & Phelps debt ratings range from AAA (highest rating possible) to DD (defaulted debt obligation). The Duff & Phelps 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 (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.

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 impact of inflation on results of operations has diminished in recent years. Natural gas, labor, and construction costs are the categories most significantly impacted by inflation. Changes to Company cost of gas are generally recovered through PGA mechanisms and do not significantly impact net earnings when approved as filed. 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 its 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.

CONSOLIDATED RESULTS OF OPERATIONS
CONTRIBUTION TO NET INCOME

| Year Ended December 31, | 1998 | 1997 | 1996 |
|-----------------------------|----------|----------|---------|
| (Thousands of dollars) | | | |
| Natural gas operations..... | \$44,830 | \$15,825 | \$3,919 |
| Construction services..... | 2,707 | 644 | 2,655 |
| Net income..... | \$47,537 | \$16,469 | \$6,574 |

1998 VS. 1997 Earnings per share for the year ended December 31, 1998 were \$1.66, a \$1.05 increase from per share earnings of \$0.61 recorded for the year ended December 31, 1997. Current-year earnings were composed of \$1.57 per share from natural gas operations and \$0.09 per share from construction services. Prior-year results included the impact of three nonrecurring events which reduced earnings by \$4.1 million, or \$0.15 per share. Average shares outstanding increased by 1.5 million shares between years, primarily resulting from a 2.5 million share common stock issuance in August 1998.

1997 VS. 1996 Earnings per share for the year ended December 31, 1997 were \$0.61, a \$0.36 increase from per share earnings of \$0.25 recorded for the year ended December 31, 1996. The 1997 earnings were composed of \$0.59 per share from natural gas operations and \$0.02 per share from construction services. Average shares outstanding increased by 1.2 million shares between years, primarily resulting from continuing issuances under the Dividend Reinvestment and Stock Purchase Plan.

RESULTS OF NATURAL GAS OPERATIONS

| Year Ended December 31, | 1998 | 1997 | 1996 |
|--|-----------|-----------|-----------|
| (Thousands of dollars) | | | |
| Gas operating revenues..... | \$799,597 | \$614,665 | \$546,361 |
| Net cost of gas sold..... | 329,849 | 209,338 | 187,580 |
| Operating margin..... | 469,748 | 405,327 | 358,781 |
| Operations and maintenance expense..... | 209,172 | 201,159 | 198,364 |
| Depreciation and amortization..... | 80,231 | 74,528 | 67,443 |
| Taxes other than income taxes..... | 31,646 | 29,393 | 28,156 |
| Operating income..... | 148,699 | 100,247 | 64,818 |
| Other income (deductions), net..... | (2,115) | (12,979) | (760) |
| Income before interest and income taxes..... | 146,584 | 87,268 | 64,058 |
| Net interest deductions..... | 62,284 | 61,751 | 53,003 |
| Preferred securities distributions..... | 5,475 | 5,475 | 5,475 |
| Income tax expense..... | 33,995 | 4,217 | 1,661 |
| Contribution to consolidated net income..... | \$ 44,830 | \$ 15,825 | \$ 3,919 |

1998 VS. 1997 The gas segment contribution to consolidated net income increased \$29 million from 1997. The increase was the result of record first quarter earnings driven by cooler temperatures, rate relief, and customer growth. The second and third quarters were substantially better than the prior year, primarily as a result of customer growth, second quarter weather, and rate design improvements. Fourth quarter results were about the same as the prior year.

Operating margin increased \$64 million, or 16 percent, in 1998. Arizona rate relief, effective September 1997, contributed \$23 million towards the increase. Customer growth accounted for \$16 million as Southwest added 58,000 customers during the year, a five percent increase. The remaining \$25 million was due to differences in heating demand caused by weather variations between periods.

Operations and maintenance expenses increased \$8 million, or four percent, reflecting increases in labor and other costs, including the incremental expenses associated with meeting the needs of a growing customer base.

Depreciation expense and general taxes increased \$8 million, or eight percent, as a result of construction activities. Average gas plant in service increased \$136 million, or eight percent, compared to the prior year. This was attributed to the upgrade of existing operating facilities and the expansion of the system to accommodate customer growth.

Net interest deductions increased less than one percent between years. Stronger-than-expected cash flows from operating activities, coupled with a 2.5 million share common stock offering, reduced the need to issue net new debt during the year.

Other income (deductions), net improved \$10.9 million. Prior year results included two nonrecurring charges recorded in the fourth quarter (see discussion below). In connection with the proposed merger into ONEOK, the Company incurred approximately \$1.1 million (pretax) of financial advisor and legal costs, which were included in other income (deductions), net, during the fourth quarter of 1998. Additional amounts of financial advisor, legal, and accounting-related costs will be incurred during the merger process. See Note 13 of the Notes to Consolidated Financial Statements for additional disclosures related to the proposed merger.

1997 VS. 1996 The gas segment contribution to consolidated net income increased \$11.9 million from 1996. The increase was the result of fundamental improvements in operating margin coupled with more favorable weather conditions.

Operating margin increased \$47 million, or 13 percent, due to customer growth, rate relief, and the return to more normal winter season temperatures following consecutive years of record-setting warm weather. Rate relief in Arizona and Nevada accounted for approximately \$20 million of the operating margin increase. Colder-than-normal weather during the fourth quarter of 1997 partially offset the effects of first quarter warmer-than-normal temperatures and, overall, weather-related factors resulted in \$19 million of additional operating margin. During 1997, Southwest added 59,000 customers, a five percent increase, contributing \$8 million towards the change in operating margin.

Depreciation expense and general taxes increased \$8.3 million, or nine percent, as a result of construction activities in 1997. Average gas plant in service increased \$162 million, or ten percent, during this same period. This was attributed to the upgrade of existing operating facilities and the expansion of the system to accommodate customer growth.

Net interest deductions during 1997 increased \$8.7 million, or 17 percent, from 1996. Average total debt outstanding during this period increased due to the financing of construction expenditures and working capital needs and included higher short-term debt, the issuance of medium-term notes during 1997, and the drawdown of IDR funds held in trust. The increase in short-term debt reflected the need for short-term financing to cover higher gas costs experienced during the 1996/1997 winter heating season.

During the fourth quarter of 1997, Southwest recognized nonrecurring charges to income related to cost overruns on two separate construction projects. These charges are reflected in other income (deductions), net. An \$8 million nonrecurring pretax charge resulted from cost overruns experienced during expansion of the northern California service territory. A second pretax charge, for \$5 million, related to cost overruns on a nonutility construction project. A subsidiary of the Company was building a liquefied natural gas (LNG) storage and distribution system to serve several small towns. The project was completed in 1998. See Note 11 of the Notes to Consolidated Financial Statements for additional disclosures related to these projects. Partially offsetting these charges was the recognition of a \$3.4 million income tax benefit related to the successful settlement

in November 1997 of open tax issues dating back as far as 1988. The combined impact of these three nonrecurring events was a \$4.1 million, or \$0.15 per share, after-tax reduction to earnings.

RATES AND REGULATORY PROCEEDINGS

CALIFORNIA GENERAL RATE CASES. Southwest last filed general rate applications for its California jurisdictions with the California Public Utilities Commission (CPUC) in 1994. Increased rates went into effect in January 1995 and continued through 1998 as part of a settlement agreement. In addition, annual operational attrition increases have been received in northern California. However, primarily as a result of the northern California expansion proposal described below, the Company filed a petition with the CPUC in March 1999 requesting an extension of the rate case cycle. Approval of this petition would result in a general rate moratorium through December 2000 at a minimum.

NEVADA GENERAL RATE CASES. In December 1995, Southwest filed general rate cases for its northern and southern Nevada jurisdictions. Increased rates went into effect in July 1996 as part of a settlement agreement. The settlement agreement also specified a moratorium on future general rate increase requests until April 1999.

ARIZONA GENERAL RATE CASE. In November 1996, Southwest filed its most recent general rate application with the Arizona Corporation Commission (ACC) seeking approval to increase revenues for both Arizona rate jurisdictions. In August 1997, the ACC approved a settlement of the general rate case providing the Company with a \$32 million annualized general rate increase effective September 1997. There is no rate moratorium in Arizona on future general rate filings.

FERC GENERAL RATE CASE. In July 1996, Paiute Pipeline Company, a wholly owned subsidiary of the Company, filed a general rate case with the Federal Energy Regulatory Commission (FERC) seeking approval to increase rates. Effective January 1997, the FERC authorized a \$3.2 million annualized general rate increase. The settlement prohibits Paiute from filing for a rate increase until December 1999.

NORTHERN CALIFORNIA EXPANSION PROJECT. In December 1993, Southwest filed an application with the CPUC to expand its northern California service territory and extend service into Truckee, California. The application included a proposed regulatory mechanism for recovering the cost of the expansion. In May 1994, rate and cost recovery issues related to the expansion application were combined by the CPUC with a January 1994 general rate application Southwest had filed with the CPUC. In September 1994, a Joint Motion and Stipulation and Settlement Agreement (Settlement) was presented to the CPUC which resolved the general rate case and addressed the expansion related cost recovery issues. In December 1994, the Settlement was approved. In April 1995, Southwest received CPUC approval for the certificate of public convenience and necessity to serve the expansion areas.

In its filing, Southwest had indicated that expansion into Truckee would occur in three phases and result in the conversion of an estimated 9,200 customers to natural gas service from their existing fuel, primarily propane. The CPUC established a cost cap of \$29.1 million for the project.

In 1995, Southwest completed Phase I of the expansion project, which involved transmission system reinforcement and distribution system expansion to accommodate approximately 940 customers. Construction costs of \$7.1 million were on target with the cost estimate approved by the CPUC.

Phase II of the project involved extending the transmission system to Truckee and expanding the distribution system to accommodate an estimated 4,200 customers. The cost cap apportioned to Phase II was approximately \$13.8 million. The incurred cost of Phase II was \$28.8 million. An estimated \$9.2 million of the Phase II cost overrun was due to changes in project scope, such as adjustments for design changes required by governmental bodies, changes in facilities necessitated by requirements beyond Southwest's control, and costs incurred to accommodate customer service requests.

Examples of adjustments for changes in project scope included the requirement to haul excavated soil off-site to be screened whereas normal and anticipated practice is to screen on-site, asphalt repairs which were greater than expected due to increased paving requirements imposed after construction started, and the installation of more facilities under asphalt than anticipated. Other unexpected or externally imposed costs pertained to extended yard lines, underground boring, environmental studies, right-of-way acquisitions, and engineering design work.

Due to the Phase II cost overruns and difficult construction environment experienced, construction of Phase III was postponed to reevaluate the economics of completing the project.

In July 1997, Southwest filed an application requesting authorization from the CPUC to modify the terms and conditions of the certificate of public convenience and necessity granted in 1995. In this application, Southwest requested that the originally approved cost cap of \$29.1 million be increased to \$46.8 million; that the scope of Phase III construction be revised to include only an estimated 2,900 of the initially estimated 4,200 customers; and that customer applicants desiring service in the expansion area who were not identified to receive service during the expansion phases as modified within the new application be subject to the existing main and service extension rules. Southwest proposed to recover the incremental costs above the original cost cap through a surcharge mechanism. Concurrently, the Truckee town manager, on behalf of the Truckee Town Council, wrote a letter to the CPUC in support of the application.

The areas requested to be excluded from the revised scope of Phase III are the most distant points from existing mains and present some of the most challenging geographic conditions in the expansion area. Extension of mains to serve the estimated 1,300 customers in the excluded areas would be considerably more expensive than the service areas in Phases I and II. Furthermore, these areas have significantly lower customer density than the remainder of the expansion project; therefore, expected revenues would be insufficient to justify the anticipated construction costs.

In August 1997, the Office of Ratepayer Advocates (ORA) for the CPUC filed a protest to the Southwest application indicating that the terms of the original agreement should be adhered to. Southwest responded with written comments in support of its application. In September 1997, a prehearing conference was held to discuss the filing, the ORA protest, and Southwest comments.

The administrative law judge (ALJ) made a preliminary ruling in favor of the ORA protest, but allowed the parties an additional 20 days to supplement their comments. During this time, Southwest and the ORA, pursuant to direction from the CPUC, began to negotiate a settlement agreement, and the procedural schedule was adjusted to allow the negotiations to continue beyond the 20-day period.

In January 1998, a settlement involving all parties to the proceeding was executed and filed with the CPUC which redefined the terms and conditions for completing the project and recovering the additional project costs. Although CPUC approval of the settlement was still required, management anticipated approval of the all-party settlement. In February 1998, a prehearing conference was held before the ALJ and the assigned Commissioner for the purpose of taking public comment on the settlement agreement. There was no opposition to the settlement agreement from the Truckee Town Council at the conference, or in a letter written by the Truckee town manager to the CPUC subsequent to the conference.

Under the January 1998 proposed settlement, Southwest agreed, among other things, to absorb \$8 million in cost overruns experienced in Phase II of the project. Southwest also agreed to an \$11 million cost cap (with a maximum of \$3,800 per customer) for Phase III of the project. The Phase III project scope would be modified as requested in the July 1997 application. In addition, Southwest agreed not to file its next general rate case until the completion of Phase III. Based on the proposed settlement, Southwest recognized an \$8 million pretax charge in the fourth quarter of 1997.

In May 1998, the ALJ issued an unexpected Proposed Decision (PD) rejecting the January 1998 all-party settlement and directing Southwest to complete the project under the terms and conditions of the 1995 certificate. A PD that ignores an all-party settlement is rare and inconsistent with CPUC policies and procedures established in 1992. Subsequent to the PD, the Truckee Town Council took a formal position in opposition to the settlement, although they were not a party to the proceeding, and had not previously opposed the settlement.

In July 1998, the CPUC voted to adopt the PD and reject the all-party settlement, and ordered Southwest to proceed with all deliberate speed to complete the project under the terms and scope of the 1995 certificate. Southwest filed a Motion for Stay (Motion) of order and petitioned the CPUC for rehearing (Petition) in August 1998. The CPUC stated in its order that Southwest was required to show extraordinary circumstances to readjudicate the original settlement. Because no evidentiary hearings were conducted, management did not have the opportunity to demonstrate that such extraordinary circumstances exist; however, it believes that such circumstances do exist. In September 1998, the CPUC denied the Motion and in January 1999, the Petition was denied. As a result, in February 1999, Southwest petitioned the Supreme Court of the State of California for review of the July 1998 CPUC decision. Such a petition is discretionary with the Supreme Court, and if accepted, could take up to two years to be heard.

In September 1998, Southwest filed a civil lawsuit in the United States Federal District Court naming the Town of Truckee as a defendant for an indeterminate amount of damages. Southwest asserts that actions taken by the Town of Truckee resulted in unanticipated changes in project

scope, which materially contributed to the cost overruns experienced during the construction of Phase II of the project.

In November 1998, Southwest, together with representatives from the town of Truckee, met before a federal mediator to reconcile the disputes and claims against each other. As a result of the mediation, Southwest and representatives of the town of Truckee are attempting to negotiate a Settlement Agreement and Mutual Release (Agreement). If an Agreement is reached, it would need to be ratified by the Truckee Town Council and approved by the CPUC, and likely would address the civil suit against the town of Truckee, the remaining project scope, and recovery of project costs among other items. An Agreement might also require Southwest to postpone the filing of its next California general rate case. If an Agreement is reached, it is anticipated that it will be presented to the Truckee Town Council at a town meeting. If ratified by the Truckee Town Council, Southwest would include the Agreement as part of a new application it plans to file with the CPUC to reopen the prior California general rate case and certificate proceeding in order to modify the original Settlement approved in December 1994.

Management believes that subsequent events may reduce the remaining scope and estimated costs of the project; however, preliminary estimates indicate that it could cost an additional \$23 million to \$25 million to complete the project under the terms of the 1995 certificate without modification. An additional pretax write-off of up to \$24 million could be recorded under this scenario. This estimate is comprised of approximately \$7 million related to costs incurred through Phase II, and up to \$17 million for the forecasted construction costs. However, Southwest will actively pursue the described regulatory and legal proceedings with the intent of reversing or mitigating the effects of the July 1998 CPUC action. Management believes that a reasonable possibility of modifying the existing CPUC orders pertaining to the expansion project exists through pursuit of the legal and regulatory remedies that have been outlined, although there can be no assurance of a favorable outcome. As a result, Southwest has not recorded any additional write-offs beyond the \$8 million recognized in the fourth quarter of 1997. Management also believes that civil litigation offers a reasonable possibility of recovering certain amounts spent to deal with changes in scope necessitated by unanticipated third party actions.

PGA FILINGS

The following table shows the most recent PGA changes authorized by rate jurisdiction (thousands of dollars):

| Jurisdiction | Annualized Revenue Adjustment | Percentage | Effective Date |
|----------------------|-------------------------------------|------------|-------------------|
| Arizona: | | | |
| Central and Southern | \$46,900 | 14% | April 1998 |
| California: | | | |
| Northern | 2,600 | 19 | January 1998 |
| Southern | 10,000 | 19 | December 1997 |
| Nevada: | | | |
| Northern | (782) | (1) | November 1998 |
| Southern | (3,000) | (2) | November 1998 |

ARIZONA PGA FILING. In March 1998, the ACC approved a purchased gas adjustment (PGA) filing submitted by Southwest in January 1998 to recover deferred purchased gas costs in Arizona. This filing, which became effective in April 1998, resulted in an annual revenue increase of \$46.9 million, or 14 percent. The increase in rates was designed to recover the accumulated PGA balance related to Arizona customers, and to eliminate the refunds previously built into the rate structure. PGA changes impact cash flows but have no direct impact on profit margin.

In October 1998, the ACC approved a proposal by the ACC staff, to modify the methodology used by Arizona natural gas utilities in calculating and revising customer rates to reflect changes in the cost of gas. The modifications, which will become effective in June 1999, will use a twelve-month rolling average of the commodity cost of gas and related transportation costs. The updated rates will be reflected in customer bills each month. The changes are designed to reduce volatility on customer bills and in the PGA balance. The mechanism also provides for recovery from customers of the existing balance in the deferred purchased gas cost account.

NEVADA PGA FILING. In January 1997, Southwest submitted an out-of-period PGA filing in Nevada in response to a substantial run-up in the commodity cost of natural gas during November and December of 1996. In September 1997, the Public Utilities Commission of Nevada (PUCN) approved the filing providing annual increases of \$10.1 million, or nine percent, in the southern Nevada rate jurisdiction, and \$6 million, or 14 percent, in the northern Nevada rate jurisdiction.

In June 1997, Southwest submitted its annual PGA filing in compliance with the Nevada Gas Tariff. The filing covered the period from April 1996 through March 1997. Southwest requested annual increases of \$23.1 million, or 18 percent, in the southern Nevada rate jurisdiction, and \$8.4 million, or 17 percent, in the northern Nevada rate jurisdiction.

In an order issued in December 1997, the PUCN found that "Southwest failed to mitigate the risk inherent in a portfolio of all indexed-priced contracts and failed to reasonably quantify the costs of any risk mitigation." As a result, gas costs of \$3.8 million in southern Nevada and \$1.8 million in northern Nevada were disallowed. The approved annualized revenue increase, after consideration of the amounts disallowed, was \$17.3 million, or 14 percent in southern Nevada, and \$5.2 million, or 11 percent in northern Nevada.

In December 1997, Southwest filed a Petition for Reconsideration (Petition) of the decision with the PUCN on the grounds that the findings of fact and conclusions of law are contrary to binding legislative enactments and judicial decisions. Specifically, the Petition asserted, among other things, that the PUCN violated its settled obligation in the previous PGA docket, which included the same winter period, in finding Southwest to be imprudent. Effectively, the PUCN allowed a previously settled claim to be relitigated. In addition, management also believes that the PUCN failed to follow its previous rules and practices surrounding a PGA proceeding, or changed those rules effective with the disallowance order and sought to retroactively apply them, which would have required compliance with formal rulemaking procedures mandated by Nevada Statutes. In February 1998, the PUCN reaffirmed the original order.

In March 1998, Southwest filed a petition for judicial review (appeal) of the final order of the PUCN with the Nevada District Court (NDC). The appeal alleged the same procedural irregularities as were included in the Petition. In November 1998, the NDC issued an order in which the December 1997 order

was determined to be void on procedural grounds. Specifically, the decision found that the Chairman of the PUCN did not have a majority when proceedings were reopened to accept additional evidence in support of a cost disallowance. This decision, if not overturned on appeal, has the effect of allowing Southwest a full recovery of the gas costs requested in the June 1997 PGA filing.

In December 1998, the PUCN filed a motion with the NDC asking for an amendment or alteration of the November 1998 NDC decision. Oral arguments were heard in February 1999. The NDC affirmed its prior order in favor of the Company. The PUCN filed a notice of appeal to the Nevada Supreme Court in February 1999. No substantive action is expected to take place during 1999.

In June 1998, Southwest submitted its annual PGA filing in compliance with the Nevada Gas Tariff. Effective November 1998, new rates were approved by the PUCN. No gas cost disallowances were ordered and no prudency issues were raised. The new rates, reflecting a lower cost of gas, resulted in annualized revenue decreases of \$3 million, or two percent in the southern Nevada rate jurisdiction, and \$782,000, or one percent in the northern Nevada rate jurisdiction. These PGA changes impact cash flows but have no direct impact on profit margin.

RESULTS OF CONSTRUCTION SERVICES

| Year Ended December 31, | 1998 | 1997 |
|--|-----------|-----------|
| (Thousands of dollars) | | |
| Construction revenues..... | \$117,712 | \$117,345 |
| Cost of construction..... | 108,911 | 112,194 |
| Gross profit..... | 8,801 | 5,151 |
| General and administrative expenses..... | 2,931 | 2,777 |
| Income from operations..... | 5,870 | 2,374 |
| Other income (expense), net..... | 326 | 379 |
| Income before interest and income taxes..... | 6,196 | 2,753 |
| Interest expense..... | 1,070 | 1,467 |
| Income tax expense..... | 2,419 | 642 |
| Contribution to consolidated net income..... | \$ 2,707 | \$ 644 |

1998 VS. 1997 The construction services segment contribution to consolidated net income increased \$2.1 million from 1997. The increase was the result of a fundamental improvement in gross profit margin coupled with favorable weather conditions.

With comparable revenues of approximately \$117 million, gross profit increased \$3.6 million from 1997. The improvement is attributed to obtaining more profitable new contracts, eliminating less profitable contracts, implementing cost containment measures, and favorable winter weather conditions in several of the cold-climate operating areas during the first and fourth quarters of 1998.

General and administrative expenses remained relatively constant, while interest expense decreased approximately \$397,000. Timely billings to customers coupled with collections of accounts receivable and the timing of equipment purchases had a direct impact in reducing interest costs.

1997 VS. 1996 Contribution to consolidated net income from construction services was \$644,000 in 1997. In 1996, construction services contributed \$2.7 million, however, those results excluded the preacquisition months January through April which are typically loss months. The decline was primarily

a result of lower-than-anticipated revenues caused by various project cancellations and curtailments in portions of California, Washington, Missouri, and Kansas. Northern reorganized and closed offices in some of those areas to pursue new contracts in other areas to improve profitability. Comparative information by major income statement caption was not provided for 1996 since those results were for a partial year.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 133 "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. It requires an entity to recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. SFAS No. 133 also requires that changes in the fair value of derivative instruments be recognized currently in earnings in the income statement unless specific hedge accounting criteria are met. Special hedge accounting for qualified hedges allows changes in the fair value of derivative instruments to be offset in the income statement in the period in which the related changes in the fair value of the item being hedged occurs. Hedge accounting requires an entity to formally document, designate, and assess hedge effectiveness. This statement is effective for quarters of fiscal years beginning after June 15, 1999 (i.e., first quarter of 2000). The Company does not currently utilize stand-alone derivatives for speculative purposes or for hedging, and does not have foreign currency exposure. However, the Company is reviewing gas supply and other contracts for potential embedded derivatives that may need to be recognized and disclosed under the requirements of this complex statement.

YEAR 2000 READINESS DISCLOSURE

Most companies have computer systems that use two digits to identify a year in the date field (e.g. "98" for 1998). These systems must be modified to handle turn-of-the-century calculations. If not corrected, system failures or miscalculations could occur, potentially causing disruptions of operations, including, among other things the inability to process transactions, send invoices, or engage in other normal business activities. The Year 2000 issue also threatens disruptions in government services, telecommunications, and other essential industries. This creates potential risk for all companies, even if their own computer systems are Year 2000 compliant.

In 1994, the Company initiated a comprehensive review of its computer systems to identify processes that could be adversely affected by Year 2000 issues. By early 1995, the Company identified computer application systems that required modification or replacement. Since that time, the Company has focused on converting all business-critical systems to be Year 2000 compliant.

In addition to the evaluation and remediation of computer application systems and components, the Company has also developed a comprehensive Year 2000 compliance plan. As part of this plan, the Company has formed a Year 2000 project team with the mission of ensuring that all critical systems, facilities, and processes are identified and analyzed for Year 2000 compliance. The project team consists of representatives from several strategic departments of the Company.

The Year 2000 plan includes specific timetables for categories of tasks for each department as follows:

- (1) Assess Year 2000 issues -- complete;
- (2) Analyze, prioritize, and catalog Year 2000 issues -- substantially complete;
- (3) Create action plans -- in process and due by the first quarter of 1999;
- (4) Implement plans and validate compliance -- in process and due by the third quarter of 1999.

The Company's top priority is to ensure that natural gas can be received from suppliers and delivered to customers. To accomplish this, the Company has sent inquiries to its five major providers of interstate natural gas transportation service. All of these providers have responded to the inquiries indicating that they intend to be Year 2000 compliant before the end of 1999. The Company has also evaluated its gas pipeline delivery systems, which are the systems used to distribute natural gas from the interstate pipelines to the customer. These systems utilize an extensive network of hardware and software devices that schedule, regulate, measure, or otherwise facilitate the flow of natural gas. Of these devices, approximately 70 percent are Year 2000 compliant, while approximately 30 percent were determined to be noncompliant or were in the process of being replaced or remediated. Remediation or replacement of the noncompliant devices is expected to be completed by the middle of 1999.

Many of the Company's business-critical computer systems are Year 2000 compliant. For example, the customer service system which supports customer billing, accounts receivable, and other customer service functions is Year 2000 compliant. The general ledger accounting system of the Company is also Year 2000 compliant. Year 2000 compliance work on other systems, such as accounts payable, purchasing, human resources, and payroll, is in process. In total, approximately 80 percent (including work-in-progress) of the Company's computer applications are currently Year 2000 compliant. The Company has also assessed its other computer components, such as computer equipment and software, and determined that approximately 90 percent of these components are Year 2000 compliant. The Company projects that both the computer application systems and the other computer components will be Year 2000 compliant by the third quarter of 1999.

The Company has initiated communications with suppliers and vendors to determine the extent to which those companies are addressing Year 2000 compliance issues. The Company is requiring business-critical suppliers and vendors to certify compliance in order to continue doing business with the Company. In addition, the Company is identifying and contacting alternate suppliers and vendors as part of a Year 2000 contingency plan. All of the companies contacted have responded that efforts are underway to become compliant.

The Company is also assessing and remediating Year 2000 issues related to embedded system devices (such as microcontrollers used in equipment and machinery), data exchange functions, networks, telecommunications, security access and building control systems, forms, reports, and other business processes and activities. The Company expects these areas to be Year 2000 compliant by the third quarter of 1999.

The Company is in the process of developing contingency scenarios for each district and division. These scenarios will consider the systems, operations, and devices that have been identified as at risk for failure. These scenarios will attempt to forecast what failures might occur, where the failures might occur, as well as the impact of the failures on dependent systems, operations, and devices. As part of this process, the Company will identify the most reasonably likely worst case Year 2000 scenario. The Company will then prepare for this scenario by developing contingency plans for all "high risk" systems, operations, and devices. This process will culminate in the development of a "Contingency Plan Operations Guide." This guide will document specific items associated with the Company's Year 2000 contingency plans including personnel-related items, non-labor resources required by the plan, command and decision authority roles, and location and function of a contingency command center. The Contingency Plan Operations Guide is scheduled for completion during the third quarter of 1999.

The Company estimates that the cost of remediation will be approximately \$2 million. Expenditures of approximately \$1 million have already been incurred in connection with systems that have been converted. The remediation costs include internal labor costs, as well as fees and expenses paid to outside contractors specifically associated with reprogramming or replacing noncompliant components. At the present time, the Company does not expect that such expenditures will have a material impact on results of operations or financial condition.

The Company's Year 2000 plans, including costs and completion schedules, are based on management's best estimates. These estimates were derived using numerous assumptions of future events including, but not limited to, third party modification plans, availability of qualified personnel, support of software vendors, and other factors. The Company is also relying on the representations made by significant third party suppliers and vendors.

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, natural gas prices, the effects of regulation/deregulation, the timing and amount of rate relief, the outcome of Southwest's challenges to regulatory actions in California and Nevada, changes in capital requirements and funding, Year 2000 remediation efforts, acquisitions, competition, and merger-related developments (see Note 13 of the Notes to Consolidated Financial Statements).

 COMMON STOCK PRICE AND DIVIDEND INFORMATION

| | 1998 | | 1997 | | Dividends Paid | |
|---------------------|----------|-----------|----------|----------|----------------|---------|
| | High | Low | High | Low | 1998 | 1997 |
| First Quarter..... | \$21 1/2 | \$17 5/16 | \$20 1/4 | \$17 1/4 | \$0.205 | \$0.205 |
| Second Quarter..... | 25 | 20 3/8 | 19 7/8 | 16 1/8 | 0.205 | 0.205 |
| Third Quarter..... | 24 1/2 | 17 3/8 | 20 1/8 | 17 3/4 | 0.205 | 0.205 |
| Fourth Quarter..... | 26 7/8 | 20 3/16 | 19 15/1 | 17 1/8 | 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 15, 1999 there were 24,186 holders of record of common stock and the market price of the common stock was \$27.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

TO THE SHAREHOLDERS,
SOUTHWEST GAS CORPORATION:

We have audited the accompanying consolidated balance sheets of Southwest Gas Corporation (a California corporation, hereinafter referred to as the Company) and subsidiaries as of December 31, 1998 and 1997, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 1998. 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 generally accepted auditing standards. 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 the Company and its subsidiaries as of December 31, 1998 and 1997, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1998 in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Las Vegas, Nevada
March 26, 1999

| December 31, | 1998 | 1997 |
|---|-------------|-------------|
| (Thousands of dollars, except par value) | | |
| ASSETS | | |
| Utility plant: | | |
| Gas plant..... | \$2,020,139 | \$1,867,824 |
| Less: accumulated depreciation..... | (612,138) | (551,083) |
| Acquisition adjustments..... | 3,881 | 4,259 |
| Construction work in progress..... | 47,480 | 39,294 |
| Net utility plant (Note 2)..... | 1,459,362 | 1,360,294 |
| Other property and investments..... | 73,926 | 64,928 |
| Current assets: | | |
| Cash and cash equivalents..... | 18,535 | 17,567 |
| Accounts receivable, net of allowances (Note 3)..... | 88,037 | 78,016 |
| Accrued utility revenue..... | 56,873 | 54,373 |
| Income tax benefit..... | -- | 19,425 |
| Deferred purchased gas costs (Note 4)..... | 57,595 | 86,952 |
| Prepays and other current assets..... | 26,346 | 32,211 |
| Total current assets..... | 247,386 | 288,544 |
| Deferred charges and other assets (Note 4)..... | 50,020 | 55,293 |
| Total assets..... | \$1,830,694 | \$1,769,059 |
| CAPITALIZATION AND LIABILITIES | | |
| Capitalization: | | |
| Common stock, \$1 par (authorized -- 45,000,000 shares; issued and outstanding -- 30,409,616 and 27,387,016 shares)..... | \$ 32,040 | \$ 29,017 |
| Additional paid-in capital..... | 424,840 | 360,683 |
| Retained earnings (accumulated deficit)..... | 19,520 | (3,721) |
| Total common equity..... | 476,400 | 385,979 |
| 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)..... | 812,906 | 778,693 |
| Total capitalization..... | 1,349,306 | 1,224,672 |
| Commitments and contingencies (Note 8) | | |
| Current liabilities: | | |
| Current maturities of long-term debt (Note 6)..... | 5,270 | 5,621 |
| Short-term debt (Note 7)..... | 52,000 | 142,000 |
| Accounts payable..... | 64,295 | 62,324 |
| Customer deposits..... | 24,333 | 21,945 |
| Accrued taxes..... | 33,480 | 21,125 |
| Accrued interest..... | 13,872 | 13,007 |
| Deferred taxes (Note 10)..... | 12,627 | 24,163 |
| Other current liabilities..... | 44,917 | 34,222 |
| Total current liabilities..... | 250,794 | 324,407 |
| Deferred income taxes and other credits: | | |
| Deferred income taxes and investment tax credits (Note 10)..... | 179,666 | 168,282 |
| Other deferred credits (Note 4)..... | 50,928 | 51,698 |
| Total deferred income taxes and other credits..... | 230,594 | 219,980 |
| Total capitalization and liabilities..... | \$1,830,694 | \$1,769,059 |

The accompanying notes are an integral part of these statements.

| Year Ended December 31, | 1998 | 1997 | 1996 |
|--|-----------|-------------|-----------|
| (Thousands of dollars) | | | |
| CASH FLOW FROM OPERATING ACTIVITIES: | | | |
| Net income..... | \$ 47,537 | \$ 16,469 | \$ 6,574 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization..... | 88,804 | 84,661 | 73,699 |
| Deferred income taxes..... | (152) | 47,476 | 17,453 |
| Changes in current assets and liabilities: | | | |
| Accounts receivable, net of allowances..... | (10,021) | (7,913) | (17,886) |
| Accrued utility revenue..... | (2,500) | (7,873) | (2,600) |
| Deferred purchased gas costs..... | 29,357 | (96,384) | (23,344) |
| Accounts payable..... | 1,971 | 12,373 | 4,964 |
| Accrued taxes..... | 31,780 | (8,277) | (19,139) |
| Other current assets and liabilities..... | 15,763 | 2,004 | 2,498 |
| Other..... | 978 | 13,889 | 9,976 |
| Net cash provided by operating activities..... | 203,517 | 56,425 | 52,195 |
| CASH FLOW FROM INVESTING ACTIVITIES: | | | |
| Construction expenditures and property additions..... | (194,621) | (169,614) | (218,835) |
| Proceeds from bank sale..... | -- | -- | 191,662 |
| Other..... | 4,327 | (1,308) | (22,112) |
| Net cash used in investing activities..... | (190,294) | (170,922) | (49,285) |
| CASH FLOW FROM FINANCING ACTIVITIES: | | | |
| Issuance of common stock, net..... | 67,180 | 12,205 | 18,110 |
| Dividends paid..... | (23,676) | (22,177) | (21,311) |
| Issuance of long-term debt, net..... | 40,864 | 120,321 | 164,876 |
| Retirement of long-term debt, net..... | (6,623) | (7,565) | (248,531) |
| Issuance (repayment) of short-term debt..... | (90,000) | 21,000 | 81,058 |
| Net cash provided by (used in) financing activities..... | (12,255) | 123,784 | (5,798) |
| Change in cash and temporary cash investments..... | 968 | 9,287 | (2,888) |
| Cash at beginning of period..... | 17,567 | 8,280 | 11,168 |
| Cash at end of period..... | \$ 18,535 | \$ 17,567 | \$ 8,280 |
| Supplemental information: | | | |
| Interest paid, net of amounts capitalized..... | \$ 61,164 | \$ 58,771 | \$ 60,008 |
| Income taxes paid (received), net..... | \$ 4,968 | \$ (33,954) | \$ 18,682 |

The accompanying notes are an integral part of these statements.

| | Common Stock | | Additional Paid-in Capital | Retained Earnings | Total |
|--|--------------|-----------|----------------------------------|----------------------|------------|
| | Shares | Amount | | | |
| (In thousands, except per share amounts) | | | | | |
| DECEMBER 31, 1995..... | 24,467 | \$ 26,097 | \$ 312,631 | \$ 17,322 | \$ 356,050 |
| Common stock issuances..... | 2,266 | 2,266 | 36,501 | | 38,767 |
| Net income..... | | | | 6,574 | 6,574 |
| Dividends declared | | | | | |
| Common: \$0.82 per share..... | | | | (21,775) | (21,775) |
| DECEMBER 31, 1996..... | 26,733 | 28,363 | 349,132 | 2,121 | 379,616 |
| Common stock issuances..... | 654 | 654 | 11,551 | | 12,205 |
| Net income..... | | | | 16,469 | 16,469 |
| Dividends declared | | | | | |
| Common: \$0.82 per share..... | | | | (22,311) | (22,311) |
| DECEMBER 31, 1997..... | 27,387 | 29,017 | 360,683 | (3,721) | 385,979 |
| Common stock issuances..... | 3,023 | 3,023 | 64,157 | | 67,180 |
| Net income..... | | | | 47,537 | 47,537 |
| Dividends declared | | | | | |
| Common: \$0.82 per share..... | | | | (24,296) | (24,296) |
| DECEMBER 31, 1998..... | 30,410* | \$ 32,040 | \$ 424,840 | \$ 19,520 | \$ 476,400 |

* At December 31, 1998 2.1 million common shares were registered and available for issuance under provisions of the Employee Investment Plan, the Stock Incentive Plan, and the Dividend Reinvestment and Stock Purchase Plan.

The accompanying notes are an integral part of these 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. Southwest's public utility rates, practices, facilities, and service territories 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. 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 revenue 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. Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation," provides that intercompany profits on sales to regulated affiliates should not be eliminated in consolidation if the sales price is reasonable and if future revenues approximately equal to the sales price will result from the rate-making process. Management believes these two criteria are being met.

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 to two years. Southwest must first obtain regulatory approval before changing the rates it charges for recovery of gas costs.

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

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.

| | 1998 | 1997 | 1996 |
|-------------------------------|--------|--------|--------|
| (In thousands) | | | |
| Average basic shares..... | 28,611 | 27,069 | 25,888 |
| Effect of dilutive securities | | | |
| Stock options..... | 108 | 61 | 27 |
| Performance shares..... | 96 | 63 | 40 |
| Average diluted shares..... | 28,815 | 27,193 | 25,955 |

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.

RECLASSIFICATIONS. Certain reclassifications have been made to amounts shown for prior years to conform to the current-year presentation.

NOTE 2.
UTILITY PLANT

Net utility plant as of December 31, 1998 and 1997 was as follows (thousands of dollars):

| December 31, | 1998 | 1997 |
|-------------------------------------|-------------|-------------|
| Gas plant: | | |
| Storage..... | \$ 3,316 | \$ 3,233 |
| Transmission..... | 170,512 | 169,033 |
| Distribution..... | 1,598,703 | 1,458,707 |
| General..... | 186,468 | 178,838 |
| Other..... | 61,140 | 58,013 |
| | 2,020,139 | 1,867,824 |
| Less: accumulated depreciation..... | (612,138) | (551,083) |
| Acquisition adjustments, net..... | 3,881 | 4,259 |
| Construction work in progress..... | 47,480 | 39,294 |
| Net utility plant..... | \$1,459,362 | \$1,360,294 |

Depreciation expense on gas plant was \$78.4 million in 1998, \$73.5 million in 1997, and \$66.9 million in 1996.

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 2004, respectively, with optional renewal terms available at the expiration dates. The rental payments for the LNG facilities are \$6.7 million annually and \$30 million in the aggregate. The rental payments for the corporate headquarters office complex are \$1.8 million for each year 1999 through 2002, \$1.9 in 2003 and \$28.2 million cumulatively thereafter. The rental payments for the Phoenix administrative offices are \$1.2 million for 1999 and 2000, \$1.3 million for each of the years 2001 through 2003, and \$1 million in the final year of the lease. 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 \$22.6 million in 1998, \$20.7 million in 1997, and \$19.9 million in 1996. These amounts include Northern lease expenses of approximately \$7.6 million in 1998, \$6.7 million in 1997, and \$6 million in 1996 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, 1998 (thousands of dollars):

Year Ending December 31,

| | |
|-----------------------------------|----------|
| 1999..... | \$10,213 |
| 2000..... | 10,004 |
| 2001..... | 10,062 |
| 2002..... | 9,999 |
| 2003..... | 6,470 |
| Thereafter..... | 29,197 |
| Total minimum lease payments..... | \$75,945 |

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, 1998, gas utility customer accounts receivable were \$67.3 million. Approximately 57 percent of the gas utility customers were in Arizona, 33 percent in Nevada, and 10 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 certain 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, 1995..... | \$ 1,227 |
| Additions charged to expense..... | 1,285 |
| Accounts written off, less recoveries..... | (1,002) |
| Balance, December 31, 1996..... | 1,510 |
| Additions charged to expense..... | 1,495 |
| Accounts written off, less recoveries..... | (1,427) |
| Balance, December 31, 1997..... | 1,578 |
| Additions charged to expense..... | 2,057 |
| Accounts written off, less recoveries..... | (2,290) |
| Balance, December 31, 1998..... | \$ 1,345 |

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). The Company's accounting policies conform to generally accepted accounting principles applicable to rate-regulated enterprises and reflect the effects of the ratemaking process. Such effects concern mainly the time at which various items enter into the determination of net income in accordance with the principle of matching costs with related revenues.

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

| December 31, | 1998 | 1997 |
|--|-----------|-----------|
| Regulatory assets: | | |
| Deferred purchased gas costs..... | \$ 57,595 | \$ 86,952 |
| SFAS No. 109 -- Income taxes, net..... | 7,870 | 9,651 |
| Unamortized premium on reacquired debt..... | 16,107 | 16,803 |
| Other..... | 21,478 | 23,048 |
| | 103,050 | 136,454 |
| Regulatory liabilities: | | |
| Supplier and other rate refunds due customers..... | (2,809) | (1,059) |
| Other..... | (241) | (1,124) |
| Net regulatory assets..... | \$100,000 | \$134,271 |

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's issuance of the Preferred Securities and the related purchase by the Company of all of the Trust's 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 are redeemable at the option of the Company on or after December 31, 2000, 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. The Company's 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 therefor and the indenture governing the Subordinated Notes, including the Company's 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, 1998, 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, | 1998 | | 1997 | | |
|--|------|--------------------|-----------------|--------------------|-----------------|
| | | Carrying Amount | Market Value | Carrying Amount | Market Value |
| (Thousands of dollars) | | | | | |
| Debentures: | | | | | |
| 9 3/4% Series F, due 2002..... | | \$100,000 | \$111,672 | \$100,000 | \$112,120 |
| 7 1/2% Series, due 2006..... | | 75,000 | 83,063 | 75,000 | 78,116 |
| 8% Series, due 2026..... | | 75,000 | 84,301 | 75,000 | 82,028 |
| Medium-term notes, 7.59% series, due 2017..... | | 25,000 | 26,817 | 25,000 | 26,214 |
| Medium-term notes, 7.78% series, due 2022..... | | 25,000 | 27,458 | 25,000 | 26,735 |
| Medium-term notes, 7.92% series, due 2027..... | | 25,000 | 27,852 | 25,000 | 27,121 |
| Medium-term notes, 6.89% series, due 2007..... | | 17,500 | 18,242 | 17,500 | 17,327 |
| Medium-term notes, 6.76% series, due 2027..... | | 7,500 | 7,277 | 7,500 | 7,079 |
| Medium-term notes, 6.27% series, due 2008..... | | 25,000 | 24,997 | -- | -- |
| Unamortized discount..... | | (3,452) | -- | (3,592) | -- |
| | | 371,548 | | 346,408 | |
| Revolving credit facility..... | | 200,000 | 200,000 | 200,000 | 200,000 |
| Industrial development revenue bonds: | | | | | |
| Variable-rate bonds | | | | | |
| Series A, due 2028..... | | 50,000 | 50,000 | 50,000 | 50,000 |
| Less funds held in trust..... | | (19,684) | -- | (25,926) | -- |
| | | 30,316 | | 24,074 | |
| Fixed-rate bonds | | | | | |
| 7.30% 1992 Series A, due 2027..... | | 30,000 | 28,484 | 30,000 | 30,288 |
| 7.50% 1992 Series B, due 2032..... | | 100,000 | 96,777 | 100,000 | 102,883 |
| 6.50% 1993 Series A, due 2033..... | | 75,000 | 63,591 | 75,000 | 67,661 |
| Unamortized discount..... | | (3,448) | -- | (3,551) | -- |
| | | 201,552 | | 201,449 | |
| Other..... | | 14,760 | -- | 12,383 | -- |
| | | 818,176 | | 784,314 | |
| Less current maturities..... | | (5,270) | | (5,621) | |
| Long-term debt, less current maturities..... | | \$812,906 | | \$778,693 | |

In October 1996, the Company filed a \$250 million shelf registration statement. In connection with this registration statement, the Company may offer, up to the registered amount, any combination of debt securities, preferred stock, depositary shares, and common stock. The Company filed a prospectus supplement in December 1996 identifying \$150 million of the shelf as medium-term notes. During 1997 and 1998, the Company issued a total of \$125 million in medium-term notes.

In June 1997, the Company entered into a \$350 million revolving credit agreement which replaced a previous \$200 million term-loan facility and a \$150 million short-term credit line. Revolving credit loans bear interest at either the London Interbank Offering Rate (LIBOR) plus or minus a competitive margin or prime rate plus one half of one percent of 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 variable-rate industrial development revenue bonds (IDRB) is established on a weekly basis and averaged 3.74 percent in 1998, 4.18 percent in 1997, and 4.16 percent in 1996. At the option of the Company, the interest period can be converted from a weekly rate to a daily-term or variable-term rate.

The fair value of the revolving credit facility approximates carrying value. Market values for the debentures and fixed-rate IDRB were determined based on dealer quotes using trading records for December 31, 1998 and 1997, as applicable, and other secondary sources which are customarily consulted for data of this kind. The carrying value of the IDRB Series due 2028 was used as the estimate of fair value based upon the variable interest rate of the bonds.

Estimated maturities of long-term debt for the next five years are expected to be \$5.3 million, \$4.9 million, \$2.5 million, \$302 million, and \$95,000, respectively.

NOTE 7.
SHORT-TERM DEBT

In June 1997, a portion of the \$350 million revolving credit facility, discussed in Note 6, replaced various credit lines which aggregated \$150 million. Short-term borrowings were \$52 million and \$142 million at December 31, 1998 and 1997, respectively. The weighted-average interest rates on these borrowings were 7.62 percent at December 31, 1998 and 6.54 percent at December 31, 1997.

In October 1997, the Company entered into a \$50 million unsecured line of credit agreement with various banks, for general working capital purposes, which expired in October 1998. During 1998 and 1997, no amounts were outstanding on this line of credit.

NOTE 8.
COMMITMENTS AND CONTINGENCIES

LEGAL PROCEEDINGS. The Company has been named as defendant in various legal proceedings. The ultimate dispositions of these proceedings are not presently determinable; however, it is the opinion of management that no litigation 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.

In 1998, the Company adopted SFAS No. 132, "Employers' Disclosures About Pensions and Other Postretirement Benefits," which standardized the disclosure requirements for pensions and other postretirement benefits. SFAS No. 132 did not change the measurement or recognition of amounts related to those plans. Prior-year amounts were reclassified to conform to the new standard. 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 | |
|--|---------------------------|------------|------------|------------|
| | 1998 | 1997 | 1998 | 1997 |
| (Thousands of dollars) | | | | |
| CHANGE IN BENEFIT OBLIGATIONS | | | | |
| Benefit obligation for service rendered to date at beginning of year (PBO/APBO)..... | \$190,389 | \$187,183 | \$ 21,698 | \$ 23,888 |
| Service cost..... | 9,130 | 9,630 | 504 | 567 |
| Interest cost..... | 14,092 | 12,945 | 1,591 | 1,638 |
| Actuarial loss (gain)..... | 14,221 | (14,870) | 1,334 | (3,415) |
| Benefits paid..... | (5,000) | (4,499) | (1,150) | (980) |
| Benefit obligation at end of year (PBO/APBO)..... | 222,832 | 190,389 | 23,977 | 21,698 |
| CHANGE IN PLAN ASSETS | | | | |
| Market value of plan assets at beginning of year..... | 232,413 | 195,994 | 3,581 | 2,408 |
| Actual return on plan assets..... | 28,272 | 35,305 | 487 | 479 |
| Employer contributions..... | -- | 5,613 | 2,611 | 693 |
| Benefits paid..... | (5,000) | (4,499) | -- | -- |
| Market value of plan assets at end of year..... | 255,685 | 232,413 | 6,679 | 3,580 |
| Funded status -- over (under)..... | 32,853 | 42,024 | (17,298) | (18,117) |
| Unrecognized net actuarial loss (gain)..... | (44,467) | (48,647) | (231) | (1,151) |
| Unrecognized transition obligation (2004/2012)..... | 4,142 | 4,979 | 12,137 | 13,004 |
| Unrecognized prior service cost..... | 295 | 352 | -- | -- |
| Prepaid (accrued) benefit cost..... | \$ (7,177) | \$ (1,292) | \$ (5,392) | \$ (6,264) |
| WEIGHTED-AVERAGE ASSUMPTIONS | | | | |
| AS OF DECEMBER 31, | | | | |
| Discount rate..... | 7.00% | 7.50% | 7.00% | 7.50% |
| Expected return on plan assets..... | 9.00% | 9.00% | 9.00% | 9.00% |
| Rate of compensation increase..... | 4.50% | 4.75% | 4.50% | 4.75% |

For PBOP measurement purposes, a seven percent annual rate of increase in the per capita cost of covered health care benefits is assumed for 1999. The rate is assumed to decrease one-half of one percent per

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

Components of net periodic benefit cost:

| | Qualified Retirement Plan | | | PBOP | | |
|---|---------------------------|----------|----------|---------|---------|---------|
| | 1998 | 1997 | 1996 | 1998 | 1997 | 1996 |
| (Thousands of dollars) | | | | | | |
| Service cost..... | \$ 9,130 | \$ 9,630 | \$ 8,762 | \$ 504 | \$ 567 | \$ 521 |
| Interest cost..... | 14,092 | 12,945 | 11,992 | 1,591 | 1,638 | 1,638 |
| Expected return on plan assets..... | (18,199) | (16,270) | (14,428) | (349) | (244) | (175) |
| Amortization of prior service costs..... | 57 | 57 | 57 | -- | -- | -- |
| Amortization of unrecognized transition obligation..... | 837 | 837 | 837 | 867 | 867 | 867 |
| Amortization of net (gain) loss..... | (32) | -- | -- | -- | 12 | 53 |
| Net periodic benefit cost..... | \$ 5,885 | \$ 7,199 | \$ 7,220 | \$2,613 | \$2,840 | \$2,904 |

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 million in 1998, \$2 million in 1997, and \$1.8 million in 1996. The accumulated benefit obligation of the plan was \$17.1 million at December 31, 1998.

The Employees' Investment Plan provides for purchases of the Company's common stock or certain other investments by eligible Southwest employees through deductions of up to 16 percent of base compensation, subject to IRS limitations. Southwest matches one-half of amounts deferred up to six percent of an employee's annual compensation. The cost of the plan was \$2.6 million in 1998, \$2.5 million in 1997, and \$2.6 million in 1996. 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. The plan provides the opportunity to defer up to 100 percent of annual cash compensation. Southwest matches one-half of amounts deferred up to six 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 represents 150 percent of Moody's Seasoned Corporate Bond Index.

At December 31, 1998, the Company had two stock-based compensation plans. These plans are accounted for in accordance with APB Opinion No. 25 "Accounting for Stock Issued to Employees." In connection with the stock-based compensation plans, the Company recognized compensation expense of \$2.1 million in 1998, \$1 million in 1997, and \$571,000 in 1996. 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):

| | | 1998 | 1997 | 1996 |
|-------------------------------|-------------|----------|----------|---------|
| Net income..... | As reported | \$47,537 | \$16,469 | \$6,574 |
| | Pro forma | 47,869 | 16,318 | 6,535 |
| Basic earnings per share..... | As reported | 1.66 | 0.61 | 0.25 |
| | Pro forma | 1.67 | 0.60 | 0.25 |

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 10 years. In 1998, 118,000 options were granted. 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:

| | 1998 | 1997 | 1996 |
|------------------------------------|---------------|---------------|---------------|
| Dividend yield..... | 3.15% | 4.09% | 4.65% |
| Risk-free interest rate range..... | 5.36 to 5.63% | 5.28 to 5.38% | 5.83 to 6.42% |
| Expected volatility range..... | 22 to 25% | 22 to 24% | 22 to 25% |
| Expected life..... | 1 to 3 years | 1 to 3 years | 1 to 3 years |

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

| | 1998 | | 1997 | | 1996 | |
|---|-------------------|---------------------------------|-------------------|---------------------------------|-------------------|---------------------------------|
| | 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..... | 472 | \$15.96 | 380 | \$15.00 | -- | -- |
| Granted during the year..... | 118 | 23.04 | 121 | 18.78 | 380 | \$15.00 |
| Exercised during the year..... | -- | -- | -- | -- | -- | -- |
| Forfeited during the year..... | (3) | 15.80 | (29) | 15.14 | -- | -- |
| Expired during the year..... | -- | -- | -- | -- | -- | -- |
| Outstanding at year end..... | 587 | \$17.38 | 472 | \$15.96 | 380 | \$15.00 |
| Exercisable at year end..... | 295 | \$16.19 | 141 | \$15.00 | -- | -- |

The weighted-average grant-date fair value of options granted was \$2.68 for 1998, \$2.26 for 1997, and \$1.79 for 1996. The exercise prices for the options granted range from \$15.00 to \$23.06. On December 31, 1998, the options outstanding had a weighted-average remaining contractual life of approximately 8.1 years.

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 performance 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, | 1998 | 1997 | 1996 |
|--|---------|---------|---------|
| Nonvested performance shares at beginning of year..... | 126 | 93 | 41 |
| Performance shares granted..... | 67 | 59 | 64 |
| Performance shares forfeited..... | -- | -- | -- |
| Shares vested and issued..... | (21) | (26) | (12) |
| Nonvested performance shares at end of year..... | 172 | 126 | 93 |
| Grant date fair value of award..... | \$18.69 | \$19.25 | \$17.63 |

NOTE 10.
INCOME TAXES

Income tax expense (benefit) consists of the following:

| Year Ended December 31, | 1998 | 1997 | 1996 |
|-------------------------------|----------|------------|------------|
| (Thousands of dollars) | | | |
| Current: | | | |
| Federal..... | \$32,267 | \$(42,921) | \$(15,087) |
| State..... | 2,519 | (2,227) | (1,566) |
| | 34,786 | (45,148) | (16,653) |
| Deferred: | | | |
| Federal..... | (268) | 47,614 | 18,832 |
| State..... | 1,896 | 2,393 | 1,695 |
| | 1,628 | 50,007 | 20,527 |
| Total income tax expense..... | \$36,414 | \$ 4,859 | \$ 3,874 |

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

| Year Ended December 31, | 1998 | 1997 | 1996 |
|--|-----------|----------|----------|
| (Thousands of dollars) | | | |
| Deferred federal and state: | | | |
| Property-related items..... | \$ 15,586 | \$19,006 | \$11,586 |
| Purchased gas cost adjustments..... | (10,344) | 37,156 | 8,437 |
| All other deferred..... | (2,746) | (5,287) | 1,372 |
| Total deferred federal and state..... | 2,496 | 50,875 | 21,395 |
| Deferred investment tax credit, net..... | (868) | (868) | (868) |
| Total deferred income tax expense..... | \$ 1,628 | \$50,007 | \$20,527 |

The consolidated effective income tax rate for the period ended December 31, 1998 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, | 1998 | 1997 | 1996 |
|---|-------|--------|-------|
| Federal statutory income tax rate..... | 35.0% | 35.0% | 35.0% |
| Net state tax liability..... | 5.5 | 4.2 | 5.0 |
| Property-related items..... | 1.3 | 3.8 | 8.8 |
| Effect of Internal Revenue Service Examination..... | -- | (16.0) | -- |
| Tax credits..... | (1.0) | (4.0) | (8.3) |
| Tax exempt interest..... | (0.3) | (1.7) | (3.7) |
| Corporate owned life insurance..... | 1.0 | (1.0) | (4.0) |
| All other differences..... | 1.9 | 2.5 | 4.3 |
| Consolidated effective income tax rate..... | 43.4% | 22.8% | 37.1% |

Deferred tax assets and liabilities consist of the following:

| December 31, | 1998 | 1997 |
|---|-----------|-----------|
| (Thousands of dollars) | | |
| Deferred tax assets: | | |
| Deferred income taxes for future amortization of ITC.... | \$ 11,673 | \$ 12,201 |
| Employee benefits..... | 9,779 | 7,459 |
| Other..... | 8,996 | 9,278 |
| Valuation allowance..... | -- | -- |
| | 30,448 | 28,938 |
| Deferred tax liabilities: | | |
| Property-related items, including accelerated depreciation..... | 149,095 | 133,539 |
| Regulatory balancing accounts..... | 23,280 | 33,626 |
| Property-related items previously flowed-through..... | 19,543 | 21,851 |
| Unamortized ITC..... | 17,271 | 18,138 |
| Debt-related costs..... | 6,258 | 6,458 |
| Other..... | 7,294 | 7,771 |
| | 222,741 | 221,383 |
| Net deferred tax liabilities..... | \$192,293 | \$192,445 |
| Current..... | \$ 12,627 | \$ 24,163 |
| Noncurrent..... | 179,666 | 168,282 |
| Net deferred tax liabilities..... | \$192,293 | \$192,445 |

At December 31, 1998, the Company has an Arizona net operating loss carryforward of \$35 million which expires in 2002. The Company anticipates utilizing the net operating loss carryforward prior to expiration. Additionally, the Company has an alternative minimum tax credit carryforward of approximately \$7.6 million, which can be carried forward indefinitely.

NOTE 11.

CALIFORNIA EXPANSION AND LNG CONSTRUCTION PROJECTS

NORTHERN CALIFORNIA EXPANSION PROJECT. In December 1993, Southwest filed an application with the California Public Utilities Commission (CPUC) to expand its northern California service territory and extend service into Truckee, California. The application included a proposed regulatory mechanism for recovering the cost of the expansion. In May 1994, rate and cost recovery issues related to the expansion application were combined by the CPUC with a January 1994 general rate application Southwest had filed with the CPUC. In September 1994, a Joint Motion and Stipulation and Settlement Agreement (Settlement) was presented to the CPUC which resolved the general rate case and addressed the expansion related cost recovery issues. In December 1994, the Settlement was approved. In April 1995, Southwest received CPUC approval for the certificate of public convenience and necessity to serve the expansion areas.

In its filing, Southwest had indicated that expansion into Truckee would occur in three phases and result in the conversion of an estimated 9,200 customers to natural gas service from their existing fuel, primarily propane. The CPUC established a cost cap of \$29.1 million for the project.

In 1995, Southwest completed Phase I of the expansion project, which involved transmission system reinforcement and distribution system expansion to accommodate approximately 940 customers. Construction costs of \$7.1 million were on target with the cost estimate approved by the CPUC.

Phase II of the project involved extending the transmission system to Truckee and expanding the distribution system to accommodate an estimated 4,200 customers. The cost cap apportioned to Phase II was approximately \$13.8 million. The incurred cost of Phase II was \$28.8 million. An estimated \$9.2 million of the Phase II cost overrun was due to changes in project scope, such as adjustments for design changes required by governmental bodies, changes in facilities necessitated by requirements beyond Southwest's control, and costs incurred to accommodate customer service requests.

Examples of adjustments for changes in project scope included the requirement to haul excavated soil off-site to be screened whereas normal and anticipated practice is to screen on-site, asphalt repairs which were greater than expected due to increased paving requirements imposed after construction started, and the installation of more facilities under asphalt than anticipated. Other unexpected or externally imposed costs pertained to extended yard lines, underground boring, environmental studies, right-of-way acquisitions, and engineering design work.

Due to the Phase II cost overruns and difficult construction environment experienced, construction of Phase III was postponed to reevaluate the economics of completing the project.

In July 1997, Southwest filed an application requesting authorization from the CPUC to modify the terms and conditions of the certificate of public convenience and necessity granted in 1995. In this application, Southwest requested that the originally approved cost cap of \$29.1 million be increased to \$46.8 million; that the scope of Phase III construction be revised to include only an estimated 2,900 of the initially estimated 4,200 customers; and that customer applicants desiring service in the expansion area who were not identified to receive service during the expansion phases as modified within the new application be subject to the existing main and service extension rules. Southwest proposed to recover the incremental costs above the original cost cap through a surcharge mechanism. Concurrently, the Truckee town manager, on behalf of the Truckee Town Council, wrote a letter to the CPUC in support of the application.

The areas requested to be excluded from the revised scope of Phase III are the most distant points from existing mains and present some of the most challenging geographic conditions in the expansion area. Extension of mains to serve the estimated 1,300 customers in the excluded areas would be considerably more expensive than the service areas in Phases I and II. Furthermore, these areas have significantly lower customer density than the remainder of the expansion project; therefore, expected revenues would be insufficient to justify the anticipated construction costs.

In August 1997, the Office of Ratepayer Advocates (ORA) for the CPUC filed a protest to the Southwest application indicating that the terms of the original agreement should be adhered to. Southwest responded with written comments in support of its application. In September 1997, a prehearing conference was held to discuss the filing, the ORA protest, and Southwest comments. The administrative law judge (ALJ) made a preliminary ruling in favor of the ORA protest, but allowed the parties an additional 20 days to supplement their comments. During this time, Southwest and the ORA, pursuant to direction from the CPUC, began to negotiate a settlement agreement, and the procedural schedule was adjusted to allow the negotiations to continue beyond the 20-day period.

In January 1998, a settlement involving all parties to the proceeding was executed and filed with the CPUC which redefined the terms and conditions for completing the project and recovering the additional project costs. Although CPUC approval of the settlement was still required, management anticipated approval of the all-party settlement. In February 1998, a prehearing conference was held before the ALJ and the assigned Commissioner for the purpose of taking public comment on the settlement agreement. There was no opposition to the settlement agreement from the Truckee Town Council at the conference, or in a letter written by the Truckee town manager to the CPUC subsequent to the conference.

Under the January 1998 proposed settlement, Southwest agreed, among other things, to absorb \$8 million in cost overruns experienced in Phase II of the project. Southwest also agreed to an \$11 million cost cap (with a maximum of \$3,800 per customer) for Phase III of the project. The Phase III project scope would be modified as requested in the July 1997 application. In addition, Southwest agreed not to file its next general rate case until the completion of Phase III. Based on the proposed settlement, Southwest recognized an \$8 million pretax charge in the fourth quarter of 1997.

In May 1998, the ALJ issued an unexpected Proposed Decision (PD) rejecting the January 1998 all-party settlement and directing Southwest to complete the project under the terms and conditions of the 1995 certificate. A PD that ignores an all-party settlement is rare and inconsistent with CPUC policies and procedures established in 1992. Subsequent to the PD, the Truckee Town Council took a formal position in opposition to the settlement, although they were not a party to the proceeding, and had not previously opposed the settlement.

In July 1998, the CPUC voted to adopt the PD and reject the all-party settlement, and ordered Southwest to proceed with all deliberate speed to complete the project under the terms and scope of the 1995 certificate. Southwest filed a Motion for Stay (Motion) of order and petitioned the CPUC for rehearing (Petition) in August 1998. The CPUC stated in its order that Southwest was required to show extraordinary circumstances to readjudicate the original settlement. Because no evidentiary hearings were conducted, management did not have the opportunity to demonstrate that such extraordinary circumstances exist; however, it believes that such circumstances do exist. In September 1998, the CPUC denied the Motion and in January 1999, the Petition was denied. As a result, in February 1999, Southwest petitioned the Supreme Court of the State of California for review of the July 1998 CPUC decision. Such a petition is discretionary with the Supreme Court, and if accepted, could take up to two years to be heard.

In September 1998, Southwest filed a civil lawsuit in the United States Federal District Court naming the Town of Truckee as a defendant for an indeterminate amount of damages. Southwest asserts that actions taken by the Town of Truckee resulted in unanticipated changes in project scope, which materially contributed to the cost overruns experienced during the construction of Phase II of the project.

In November 1998, Southwest, together with representatives from the town of Truckee, met before a federal mediator to reconcile the disputes and claims against each other. As a result of the mediation, Southwest and representatives of the town of Truckee are attempting to negotiate a Settlement Agreement and Mutual Release (Agreement). If an Agreement is reached, it would need to be ratified by the Truckee Town Council and approved by the CPUC, and likely would address the civil suit against the town of Truckee, the remaining project scope, and recovery of project costs among other items. An Agreement might also require Southwest to postpone the filing of its next California general rate case. If an Agreement is reached, it is anticipated that it will be presented to the Truckee Town Council at a town meeting. If ratified by the Truckee Town Council, Southwest would include the Agreement as part of a new application it plans to file with the CPUC to reopen the prior California general rate case and certificate proceeding in order to modify the original Settlement approved in December 1994.

Management believes that subsequent events may reduce the remaining scope and estimated costs of the project; however, preliminary estimates indicate that it could cost an additional \$23 million to \$25 million to complete the project under the terms of the 1995 certificate without modification. An additional pretax write-off of up to \$24 million could be recorded under this scenario. This estimate is comprised of approximately \$7 million related to costs incurred through Phase II, and up to \$17 million for the forecasted construction costs. However, Southwest will actively pursue the described regulatory and legal proceedings with the intent of reversing or mitigating the effects of the July 1998 CPUC action. Management believes that a reasonable possibility of modifying the existing CPUC orders pertaining to the expansion project exists through pursuit of the legal and regulatory remedies that have been outlined, although there can be no assurance of a favorable outcome. As a result, Southwest has not recorded any additional write-offs beyond the \$8 million recognized in the fourth quarter of 1997. Management also believes that civil litigation offers a reasonable possibility of recovering certain amounts spent to deal with changes in scope necessitated by unanticipated third party actions.

LNG STORAGE AND DISTRIBUTION SYSTEM. A subsidiary of the Company entered into an agreement to build Liquefied Natural Gas (LNG) storage and distribution systems to serve several small towns. The subsidiary contracted to provide project management services, materials, two gas distribution systems, and two LNG storage and vaporization systems. The project was completed in 1998. The total project cost exceeded the contract price by approximately \$5 million. A pretax charge of \$5 million was recorded in 1997 and was included in Other income (deductions), net on the Consolidated Statements of Income.

NOTE 12.

ACQUISITION OF NORTHERN PIPELINE CONSTRUCTION CO.

In April 1996, the Company acquired all of the outstanding stock of Northern Pipeline Construction Co. (Northern or the construction services segment) pursuant to a definitive agreement dated November 1995. The Company issued approximately 1,439,000 shares of common stock valued at \$24 million in connection with the acquisition. The acquisition was accounted for as a purchase. Goodwill in the amount of approximately \$10

million was recorded by Northern and is being amortized over 25 years. Northern provides utility companies with trenching and installation, replacement, and maintenance services for energy distribution systems.

During 1998, Northern recognized \$38 million of revenues generated from contracts with Southwest, and \$36 million in 1997. During the period from the acquisition date through December 31, 1996, the construction services segment recognized \$36 million of revenues generated from contracts with Southwest. These revenues and associated profits are included in the consolidated financial statements of the Company and were not eliminated during consolidation. SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation," provides that intercompany profits on sales to regulated affiliates should not be eliminated in consolidation if the sales price is reasonable and if future revenues approximately equal to the sales price will result from the rate-making process. Management believes these two criteria are being met. At December 31, 1998 and 1997, consolidated accounts receivable included \$5 million and \$3.6 million, respectively, which were not eliminated during consolidation.

NOTE 13.

MERGER AGREEMENT WITH ONEOK, INC.

In December 1998, the Boards of Directors of the Company and ONEOK, Inc. (ONEOK), headquartered in Tulsa, Oklahoma, announced a definitive agreement for the Company to be merged into ONEOK. The agreement calls for ONEOK to pay cash of \$28.50 for each share of Company common stock outstanding. The transaction is subject to customary conditions, including approvals from shareholders of the Company and state regulators in Arizona, California, and Nevada. ONEOK expects to account for the merger using the purchase method of accounting. If the merger is consummated, the Company would operate as a division of ONEOK.

In connection with the proposed merger into ONEOK, the Company incurred approximately \$1.1 million (pretax) of financial advisor and legal costs, which were included in Other income (deductions), net, during the fourth quarter of 1998. Additional amounts of financial advisor, legal, and accounting-related expenses will be incurred during the merger process and, depending on the successful completion of the merger, are estimated at \$2 million to \$5 million.

In February 1999, the Company announced that it had received an unsolicited proposal from Southern Union Company (Southern Union), headquartered in Austin, Texas, offering to acquire the Company for \$32.00 per share in cash. The proposal is preliminary in nature and subject to a number of contingencies and uncertainties. Under the terms of the agreement with ONEOK, as a result of certain preliminary determinations made by the Board of Directors of the Company, the Board of Directors has authorized management to commence substantive discussions with Southern Union regarding its proposal. No assurances can be given that any agreement will be reached with Southern Union. The merger agreement with ONEOK remains in full force and effect.

NOTE 14.

SEGMENT INFORMATION

The Company's 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.

The financial information pertaining to the Company's natural gas operations and construction services segments for each of the three years in the period ended December 31, 1998, is as follows (thousands of dollars):

| | 1998 | | | |
|--|----------------|-----------------------|-------------|-------------|
| | Gas Operations | Construction Services | Adjustments | Total |
| Revenues from unaffiliated customers.... | \$ 799,597 | \$ 79,736 | | \$ 879,333 |
| Intersegment sales..... | -- | 37,976 | | 37,976 |
| Total..... | \$ 799,597 | \$117,712 | | \$ 917,309 |
| Interest expense..... | \$ 62,284 | \$ 1,070 | | \$ 63,354 |
| Depreciation and amortization..... | \$ 80,231 | \$ 8,573 | | \$ 88,804 |
| Income tax expense..... | \$ 33,995 | \$ 2,419 | | \$ 36,414 |
| Segment income..... | \$ 44,830 | \$ 2,707 | | \$ 47,537 |
| Segment assets..... | \$1,772,418 | \$ 59,285 | \$(1,009) | \$1,830,694 |
| Capital expenditures..... | \$ 179,361 | \$ 15,260 | | \$ 194,621 |

| | 1997 | | | |
|--|----------------|-----------------------|-------------|-------------|
| | Gas Operations | Construction Services | Adjustments | Total |
| Revenues from unaffiliated customers.... | \$ 614,665 | \$ 81,421 | | \$ 696,086 |
| Intersegment sales..... | -- | 35,924 | | 35,924 |
| Total..... | \$ 614,665 | \$117,345 | | \$ 732,010 |
| Interest expense..... | \$ 61,751 | \$ 1,467 | | \$ 63,218 |
| Depreciation and amortization..... | \$ 74,528 | \$ 10,133 | | \$ 84,661 |
| Income tax expense..... | \$ 4,217 | \$ 642 | | \$ 4,859 |
| Segment income..... | \$ 15,825 | \$ 644 | | \$ 16,469 |
| Segment assets..... | \$1,717,025 | \$ 52,919 | \$(885) | \$1,769,059 |
| Capital expenditures..... | \$ 164,528 | \$ 5,086 | | \$ 169,614 |

| | 1996 | | | |
|--|----------------|-----------------------|-------------|------------|
| | Gas Operations | Construction Services | Adjustments | Total |
| Revenues from unaffiliated customers.... | \$ 546,361 | \$ 61,646 | | \$ 608,007 |
| Intersegment sales..... | -- | 36,054 | | 36,054 |
| Total..... | \$ 546,361 | \$ 97,700 | | \$ 644,061 |

| | 1996 | | | |
|------------------------------------|----------------|-----------------------|-------------|-------------|
| | Gas Operations | Construction Services | Adjustments | Total |
| Interest expense..... | \$ 53,003 | \$ 1,910 | | \$ 54,913 |
| Depreciation and amortization..... | \$ 67,443 | \$ 6,256 | | \$ 73,699 |
| Income tax expense..... | \$ 1,661 | \$ 2,213 | | \$ 3,874 |
| Segment income..... | \$ 3,919 | \$ 2,655 | | \$ 6,574 |
| Segment assets..... | \$1,498,099 | \$ 62,315 | \$(145) | \$1,560,269 |
| Capital expenditures..... | \$ 210,743 | \$ 8,092 | | \$ 218,835 |

Construction services segment interest expense and income tax expense, for the year ended December 31, 1996, include allocations of \$968,000 and \$(387,000), respectively, from the gas operations segment. For the years ended December 31, 1998 and 1997, no allocations from the gas operations segment to the construction services segment were made.

Construction services segment assets include deferred tax assets of \$1 million in 1998, \$885,000 in 1997, and \$145,000 in 1996, which were netted against gas operations segment deferred tax liabilities during consolidation.

NOTE 15.
QUARTERLY FINANCIAL DATA (UNAUDITED)

| Quarter Ended | March 31 | June 30 | September 30 | December 31 |
|--|-----------|-----------|--------------|-------------|
| (Thousands of dollars, except per share amounts) | | | | |
| 1998 | | | | |
| Operating revenues..... | \$292,601 | \$192,897 | \$162,508 | \$269,303 |
| Operating income (loss)..... | 75,502 | 12,951 | (529) | 66,246 |
| Net income (loss)..... | 35,953 | (2,514) | (10,945) | 25,043 |
| Basic earnings (loss) per common share*..... | 1.31 | (0.09) | (0.38) | 0.83 |
| Diluted earnings (loss) per common share*..... | 1.30 | (0.09) | (0.38) | 0.82 |
| 1997 | | | | |
| Operating revenues..... | \$235,231 | \$136,938 | \$128,698 | \$231,143 |
| Operating income (loss)..... | 51,515 | (3,982) | (7,248) | 61,976 |
| Net income (loss)..... | 21,568 | (12,748) | (15,686) | 23,335 |
| Basic earnings (loss) per common share*..... | 0.80 | (0.47) | (0.58) | 0.85 |
| Diluted earnings (loss) per common share*..... | 0.80 | (0.47) | (0.58) | 0.85 |
| 1996 | | | | |
| Operating revenues..... | \$188,352 | \$123,611 | \$125,255 | \$206,843 |
| Operating income (loss)..... | 38,539 | (4,747) | (8,404) | 46,185 |
| Net income (loss)..... | 14,859 | (11,943) | (14,638) | 18,296 |
| Basic earnings (loss) per common share*..... | 0.60 | (0.46) | (0.55) | 0.69 |
| Diluted earnings (loss) per common share*..... | 0.60 | (0.46) | (0.55) | 0.68 |

* 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 management's opinion that comparisons of earnings for the interim periods do not reliably reflect overall trends and changes in the Company's operations. 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.

NOTE 16.

DISCONTINUED OPERATIONS -- FINANCIAL SERVICES ACTIVITIES

In July 1996, the Company completed the sale of the assets and liabilities of PriMerit Bank (the Bank) to Norwest Corporation for \$191 million. Proceeds from the sale were used by the Company to retire debt incurred in connection with its investment in the Bank. The loss on disposition was included in the 1995 results of operations.

SOUTHWEST GAS CORPORATION
LIST OF SUBSIDIARIES OF THE REGISTRANT
AT DECEMBER 31, 1998

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

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation of our report dated March 26, 1999, incorporated by reference in this Form 10-K, into Southwest Gas Corporation's previously filed registration statements on Form S-8 (File No. 33-58135), Form S-3 (File No. 333-14605), Form S-3 (File No. 333-17667), Form S-8 (File No. 333-31223), and Form S-8 (File No. 333-31267).

ARTHUR ANDERSEN LLP

Las Vegas, Nevada
March 26, 1999

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM SOUTHWEST GAS CORPORATION'S FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 1998 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

1,000

| YEAR | DEC-31-1998 | DEC-31-1998 |
|-----------|-------------|-------------|
| | | PER-BOOK |
| | 1,459,362 | |
| | 73,926 | |
| | 247,386 | |
| | 0 | |
| | | 50,020 |
| | | 1,830,694 |
| | | 32,040 |
| | 424,840 | |
| | | 19,520 |
| 476,400 | | 0 |
| | | 0 |
| | | 812,906 |
| | | 52,000 |
| | | 0 |
| | 0 | |
| 5,270 | | |
| | | 0 |
| | | 0 |
| | | 0 |
| 484,118 | | |
| 1,830,694 | | |
| | 917,309 | |
| | | 36,414 |
| | 763,139 | |
| | 763,139 | |
| | 154,170 | |
| | | (6,865) |
| 147,305 | | |
| | 63,354 | |
| | | 47,537 |
| | 0 | |
| 47,537 | | |
| | 23,676 | |
| | | 0 |
| | 203,517 | |
| | | 1.66 |
| | | 1.65 |

Includes: trust originated preferred securities of \$60,000, current liabilities, net of current long-term debt maturities and short-term debt, of \$193,524 and deferred income taxes and other credits of \$230,594. Includes distributions related to trust originated preferred securities of \$5,475.