

SOUTHWEST GAS STORAGE COMPANY

Statement of the Nature, Reasons and Basis for the Filing Including Summary of Changes or Additions to Tariff and Explanation of Need for Changes

Southwest Gas Storage Company ("Southwest Gas Storage") is filing a general rate increase applicable to storage services provided under Rate Schedules FSS and ISS of its FERC Gas Tariff, First Revised Volume No. 1.

A. Nature of the Filing

The changes in rate levels in this filing are designed based on the filed billing determinants and throughput levels for storage services. The principal factors supporting the increase in cost of service are:

- (a) an increase in rate base resulting from additional plant and recoverable base gas that will be acquired pursuant to Commission authorization in Docket No. CP07-69-000.;
- (b) a reclassification of base gas inventory from recoverable (Account No. 117) to non-recoverable (Account No. 101);
- (c) an increase in operating and maintenance expenses resulting primarily from third party storage costs;
- (d) an increase in return and associated income taxes; and
- (e) a decrease in depreciation rates and the establishment of a negative salvage rate.

The primary reason for the filing is to adjust Southwest Gas Storage's rates for storage services. The computed cost of service herein, when compared with the cost of service underlying the currently effective rates, indicates an annual increase of approximately \$5.0 million.

In compliance with Section 154.7(a)(6) of the Commission's regulations, 18 CFR §154.7(a)(6), the following table compares the cost of service, rate base and throughput underlying this filing with the same information underlying the last rate found just and reasonable by the Commission:

	<u>Instant Filing</u>	<u>CP97-237¹</u>
Storage Revenues	\$50,449,002	\$42,824,612
Cost of Service	\$50,448,945	\$44,222,552
Rate Base	\$141,570,520	\$140,101,034

¹ Docket No. CP97-237-000 was settled.

Billing Determinants (MMBtu)		
Capacity	60,917,892	56,988,737
Deliverability	8,696,536	8,130,684
Injection/Withdrawal	74,322,954	56,988,737

Southwest Gas Storage's overall cost-of-service, as detailed in Statement A, for the Base Period ending April 30, 2007, adjusted for known and measurable changes through January 31, 2008, justify the rate increase. Southwest Gas Storage is controlling expenses, and taking a conservative approach in its rate proposals, while striving to match cost incurrence with cost causation.

1. Unchanged Rate Components

A number of components of Southwest Gas Storage's proposed rates represent a continuation of existing practices. Southwest Gas Storage generally has retained the methods of cost classification, cost allocation and rate design that underlie its currently effective rates. Southwest Gas Storage utilizes the Equitable Gas Company methodology preferred by the Commission for the derivation of its storage rates. As more fully explained in Southwest Gas Storage's testimony:

a. Straight-fixed Variable Method. Southwest Gas Storage continues to design rates using the Commission-preferred straight fixed variable ("SFV") method.

b. ISS Rate Design. Southwest Gas Storage has continued the design of its interruptible storage rate for service under Rate Schedule ISS, which reflects a one-part inventory rate with billing on the average daily balance per month. Southwest Gas Storage recognizes the Commission's preference for the derivation of interruptible storage rates, and believes that circumstances continue to exist to warrant such design.

2. Proposed Changes

Southwest Gas Storage's proposed rates are supported by the statements and schedules enclosed with this filing pursuant to Section 154.312 of the Commission's regulations, including the prepared testimony of Southwest Gas Storage's witnesses. As more fully explained therein, Southwest Gas Storage's proposed changes include the following:

a. Cost of capital. The proposed rates incorporate an overall cost of capital of 10.41 percent, based on the Test Period capitalization of its parent, Panhandle Eastern Pipe Line Company, LP ("Panhandle"). This cost of capital reflects the decision by Southwest Gas Storage to file for an equity return commensurate with Southwest Gas Storage's risks in the highly competitive market environment in which it operates. Thus, Southwest Gas Storage's filed cost of capital is as follows:

<u>Capital Component</u>	<u>Weight</u>	<u>Cost</u>	<u>Wgtd. Cost</u>
Long-Term Debt	39.85%	6.51%	2.59%
Cost of Common Equity Requested by Southwest Gas Storage	60.15%	13.00%	7.82%
Overall Cost of Capital Requested by Southwest Gas Storage			10.41%

b. Depreciation Rates. Southwest Gas Storage has filed to lower its storage depreciation rates to 1.95 percent from 3.60 percent, which is the currently effective depreciation rates that were included in Southwest Gas Storage's Stipulation and Agreement in Docket No. CP97-237-000, as approved by the Commission on December 2, 1998. In addition, Southwest Gas Storage is proposing to establish a negative salvage rate of 0.97 percent. Southwest Gas Storage also has made an adjustment to its General Plant – Computer Equipment depreciation rates to better reflect the useful life of such assets and is proposing to utilize a 20 percent annual depreciation rate for those facilities.

c. Reclassification of Base Gas. Southwest Gas Storage has analyzed the base gas inventory to determine how much of storage base gas inventory is economically recoverable when the storage fields are no longer operating. Southwest Gas Storage's analysis and evaluation demonstrates that 26.5 Bcf of storage base gas can no longer be considered as recoverable and should be reclassified to Account 352.3 as non-recoverable.

d. Acquisition of additional North Hopeton Base Gas. On January 26, 2007, Southwest Gas Storage requested certificate authorization under Section 7(b) and 7(c) of the Natural Gas Act to purchase an additional 3 Bcf of base gas and adjust the maximum working storage capacity from 10 Bcf to 3.5 Bcf of the North Hopeton Storage field located in Woods County, Oklahoma. The 3 Bcf of base gas is needed to sustain the working storage capability of this field. Upon Commission authorization Southwest Gas Storage will purchase 3 Bcf of gas for the additional base gas at North Hopeton. At today's price, Southwest Gas Storage estimates that the base gas will cost \$22.5 million. Market prices are expected to be similar at the time Southwest Gas Storage would acquire the gas following Commission approval of the certificate application in CP07-69-000. Once acquired, the cost of the base gas will be included in Account No. 117.

B. Reasons for the Filing

Southwest Gas Storage is submitting this rate filing to incorporate into its storage rates the current operating conditions related to the pending partial abandonment of a portion of its North Hopeton Storage Field and the replacement of that lost capacity with third party storage service, which will allow Southwest Gas Storage to continue to meet its contractual obligations to its customer. The revised rates reflect: (1) increases in rate base and operating and maintenance expenses, (2) decreases in depreciation expense; and (3) increases in overall rate of return and related taxes.

1. Rate Base

The revised tariff sheets reflect a rate base of \$141.6 million. This includes the facilities transferred pursuant to Commission authorization in Docket No. CP97-237-000.

Southwest Gas Storage's rate base also reflects test period capital additions and changes to the accumulated reserve for depreciation.

2. Rate of Return

The revised tariff sheets reflect an overall rate of return on rate base of 10.41 percent. Southwest Gas Storage has utilized the actual capital structure of its parent, Panhandle Eastern Pipe Line Company, LP ("Panhandle"), for the purposes of calculating Southwest Gas Storage's rate of return allowance. Using Panhandle's capital structure (consisting of 60.15 percent equity and 39.85 percent debt) is appropriate because Southwest Gas Storage does not issue its own non-guaranteed debt, and has no bond rating separate from its parent. Southwest Gas Storage has based its return allowance on its weighted average cost of debt, which is 6.51 percent. Southwest Gas Storage is requesting a return on equity of 13.00 percent, which reflects Southwest Gas Storage's risks which justify the requested return on equity.

3. Billing Determinants

The billing determinants used in this filing reflect actual volumes for the twelve months ended April 30, 2007. Southwest Gas Storage only has one firm customer, Panhandle. Its storage capacity is fully subscribed under Rate Schedule FSS. Southwest Gas Storage has not provided any interruptible storage service during the Base Period.

C. Basis for the Filing

The basis for Southwest Gas Storage's proposed changes are fully detailed in Statements A through J, L, M and O, submitted as part of this rate filing, and as described in Section 154.312 of the Commission's regulations [18 CFR §154.312]. In addition, Statement P, submitted herewith, contains prepared direct testimony setting forth the evidence that supports Southwest Gas Storage's case-in-chief. The testimony of Southwest Gas Storage's witnesses are as follows:

<u>Witness</u>	<u>Testimony</u>
Michael T. Langston	Background Information Related to Filing, Capital Structure, Including Selection of Equity Return, Proposed Base Rates, Acquisition of Base Gas, Reclassification of Storage Base Gas, and Overall Business Risks
Karen G. Benson	Non-recoverable Storage Base Gas
Lawrence J. Biediger	Overall Cost of Service, Rate Base, Accumulated Deferred Income Taxes, Operating Costs, Depreciation Expense, Income Taxes, Revenue Credits, and Gas Balance
Rickey J. Brocato	Gas Plant, Accumulated Provision for Depreciation, Working Capital and Other Taxes
Edward H. Feinstein	Depreciation Rates

William W. Grygar	Billing Determinants, Classification, Cost Allocations, and Rate Design for Storage Services
Robert B. Hevert	Range of Return on Equity
James S. Taylor	Negative Salvage