CLEARONE COMMUNICATIONS INC
Form DEF 14A
October 17, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSIONWASHINGTON, DC 20549

SCHEDULE 14A

(Rule 14a-101)

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) ofthe Securities Exchange Act of 1934

Filed by the Registrant x

Filed by a Party other than the Registrant o

Check the appropriate box:

o

Preliminary Proxy Statement.

o

Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2)).

x

Definitive Proxy Statement.

o

Definitive Additional Materials.

o

Soliciting Material Pursuant to §240.14a-12.

ClearOne Communications, Inc.

(Name of Registrant as Specified in its Charter)

(Name of Person(s) Filing Proxy Statement, if other than Registrant)

Payment of Filing Fee (Check the appropriate box):

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No fee required.

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)(4) and 0-11.

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1)

Amount Previously Paid:

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Form, Schedule or Registration Statement No.:

3)

Filing Party:

4)

Date Filed:

CLEARONE COMMUNICATIONS, INC.

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

NOVEMBER 5, 2012

The Annual Meeting of Shareholders of ClearOne Communications, Inc., a Utah corporation, will be held at 9:00 a.m., local time, on Monday, November 5, 2012, at our corporate offices, 5225 Wiley Post Way, Suite 500, Salt Lake City, Utah 84116.

The following describes the purpose of the Annual Meeting:

1.

To elect five members of our Board of Directors;

2.

To ratify the appointment of the Company's independent public accountants;

3.

To amend the Articles of Incorporation to change the name of the Company from ClearOne Communications, Inc. to ClearOne, Inc.

4.

To transact such other business as may properly come before the meeting or any adjournment thereof.

The foregoing items of business are more fully described in the proxy statement accompanying this notice.

Only shareholders of record at the close of business on October 2, 2012 are entitled to notice of and to vote at the meeting.

All shareholders are cordially invited to attend the meeting and vote in person. However, to ensure your representation at the meeting, you are urged to vote as promptly as possible, whether via the Internet, by telephone, or, by marking, signing, dating, and returning the enclosed proxy in the postage-prepaid envelope enclosed for that

purpose. Any shareholder attending the meeting may vote in person even if such shareholder has previously submitted a proxy. If you need to obtain directions on how to attend the Annual Meeting and vote in person, please contact our corporate offices at (801) 975-7200.

Important Notice Regarding the Availability of Proxy Materials for the 2012 Annual Meeting of Shareholders to be held on November 5, 2012. Because we have elected to utilize the full set delivery option, we are delivering to all shareholders paper copies of all of our proxy materials, including a proxy card, as well as providing access to our proxy materials on a publicly accessible website. Our Proxy Statement and Annual Report for the fiscal year ended December 31, 2011 are available at our corporate website and may be accessed at www.clearone.com under Investor Relations .

Sincerely,

Narsi Narayanan

Corporate Secretary

Salt Lake City, Utah

October 3, 2012

CLEARONE COMMUNICATIONS, INC.

5225 Wiley Post Way, Suite 500

Salt Lake City, Utah 84116

PROXY STATEMENT

ANNUAL MEETING OF SHAREHOLDERS

NOVEMBER 5, 2012

General

The accompanying proxy is solicited on behalf of ClearOne Communications, Inc., a Utah corporation (the Company), by the Board of Directors for use at our 2012 Annual Meeting of Shareholders to be held at the corporate offices of the company, 5225 Wiley Post Way, Suite 500, Salt Lake City, Utah on November 5, 2012 at 9:00 a.m., local time, or at any postponement or adjournment thereof, for the purposes set forth herein and in the accompanying notice.

These proxy solicitation materials will be distributed on or about October 15, 2012 to all shareholders entitled to vote at the meeting.

Record Date and Shares Outstanding

Shareholders of record at the close of business on October 2, 2012 are entitled to notice of, and to vote at, the meeting. On the record date, 9,175,774 shares of common stock were issued and outstanding.

Voting of Proxies

By completing and submitting the proxy (whether over the internet, by telephone, or by signing, dating and mailing the accompanying proxy card), the shareholder authorizes Zeynep Hakimoglu, Chairman and Chief Executive Officer, and Narsi Narayanan, Corporate Secretary, as designated on the face of the proxy, to vote all shares for the shareholder. All proxies that are properly completed and submitted will be voted as the shareholder directs. If no direction is given, executed proxies will be voted FOR the election of each of the nominees set forth in this proxy statement, FOR the ratification of the appointment of the Company s independent public accountants and FOR amendment of the Articles of Incorporation to change the name of the Company from ClearOne Communications, Inc. to ClearOne, Inc.

Vote Required for Approval

A quorum must be present at the meeting in order for the shareholders to take official action. Under Utah law and our Articles of Incorporation and Bylaws, a quorum will exist if a majority of the total number of shares entitled to vote

are present, in person or by proxy. Abstentions and broker non-votes, which are indications by a broker that it does not have discretionary authority to vote on a particular matter, will be counted as represented for the purpose of determining the presence or absence of a quorum. The election of directors and the amendment of Articles of Incorporation are non-routine matters on which brokers are not allowed to vote unless they have received voting instructions from their customers. Accordingly, it is particularly important that beneficial owners instruct their brokers how they wish to vote their shares. The ratification of the appointment of the Company s independent public accountants is considered a routine matter for which brokerage firms may vote un-instructed shares.

Each holder of common stock will be entitled to one vote for each share of common stock held on the record date. In the election of directors, shareholders will not be allowed to cumulate their votes. Assuming that a quorum is present, the election of directors will be determined by plurality vote. The proposals to ratify the appointment of McGladrey LLP to serve as our independent public accountants for the year ending December 31, 2012 and to amend the Articles of Incorporation to change the name of the Company from ClearOne Communications, Inc. to ClearOne, Inc. requires that the votes cast in favor of the proposals must exceed the votes cast against the proposals. Abstentions and broker non-votes will not affect the outcome of the election of directors or the proposals to ratify the appointment of the Company s independent public accountants and amend the Articles of Incorporation. Any other matter properly presented for approval by the shareholders at the Annual Meeting will generally be approved if the number of votes cast in favor of a matter exceeds the number of votes cast in opposition. With respect to any such matter, abstentions and broker non-votes are not likely to affect the outcome of

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a vote on such matter. The Company is not currently aware of any other matters to be presented at the Annual Meeting.

The Board of Directors recommends that an affirmative vote be cast in favor of all nominees listed in this proxy statement, the ratification of the appointment of the Company s independent public accountants and the amendment of the Articles of Incorporation to change the name of the Company from ClearOne Communications, Inc. to ClearOne, Inc.

Revocability of Proxies

Any proxy given pursuant to this solicitation may be revoked by the person giving it at any time prior to its use by delivering to our Corporate Secretary a written notice of revocation or a duly executed proxy bearing a later date, or by attending the meeting and voting in person.

Solicitation

We will pay the cost of this solicitation. In addition, we may reimburse brokerage firms and other persons representing beneficial owners of shares for their expenses in forwarding solicitation material to such beneficial owners. Proxies may also be solicited by certain of our directors, officers, and employees, without additional compensation, personally or by telephone, facsimile, or e-mail.

Annual Report and Other Matters

Our 2011 Annual Report on Form 10-K, which was made available to shareholders with or preceding this proxy statement, contains financial and other information about our company, but is not incorporated into this proxy statement and is not to be considered a part of these proxy soliciting materials or subject to Regulations 14A or 14C or to the liabilities of Section 18 of the Securities Exchange Act of 1934, as amended. The information contained in the Audit and Compliance Committee Report shall not be deemed filed with the Securities and Exchange Commission or subject to Regulations 14A or 14C or to the liabilities of Section 18 of the Exchange Act.

We will provide, without charge, a printed copy of our 2011 Annual Report on Form 10-K, as filed with the Securities and Exchange Commission, to each shareholder of record as of the record date that requests a copy in writing. Any such requests should be directed to our Corporate Secretary at our corporate offices set forth in this proxy statement.

PROPOSAL ONE

ELECTION OF DIRECTORS

Our articles of incorporation and bylaws provide that our Board of Directors shall consist of not less than three nor more than nine members as the Board of Directors or our shareholders shall determine from time to time. The Board of Directors has currently fixed the number of directors at five. The term of each of our directors expires at the 2012 Annual Meeting. We have nominated all five existing directors for election at the meeting to serve until the next Annual Meeting of Shareholders or until their respective successors are duly elected and qualified. In the event any nominee is unable to serve, the proxies will be voted for a substitute nominee, if any, to be designated by our Board of Directors. The Board of Directors has no reason to believe any nominee will be unable or will decline to serve as a director.

The Board of Directors unanimously recommends a vote for election of the nominees named herein.

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Nominees for Director

The following table set forth certain information regarding our directors and nominees for directors.

Name	Age	Position	Director Since
Zeynep Zee Hakimoglu	59	Chairman, Chief Executive Officer, and President	2006
Brad R. Baldwin	57	Director (1)(2)(3)	1988
Larry R. Hendricks	69	Director (1)(2)(3)	2003
Scott M. Huntsman	47	Director (1)(2)(3)	2003
E. Bryan Bagley	48	Director	2009

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(1)

Member of the Audit and Compliance Committee

(2)

Member of the Compensation Committee

(3)

Member of the Nominating Committee

Zee Hakimoglu has served as a director of our company since April 2006. Ms. Hakimoglu joined our company in December 2003 with more than 15 years of executive and senior-level, high-tech management experience and was appointed as President and Chief Executive Officer in July 2004 and Chairman of the Board in July 2007. She served in a variety of executive business development, product marketing, and engineering roles including Vice President of Product Line Management for ClearOne from December 2003 to July 2004. Prior to joining ClearOne, Ms. Hakimoglu served as Vice President of Product Line Management for Oplink Communications, a publicly traded developer of fiber optic subsystems and components from December 2001 to December 2002; President of OZ Optics USA, a manufacturer of fiber optic test equipment and components from August 2000 to November 2001; and various management positions including Vice President of Wireless Engineering and Vice President of the Wireless Business Unit for Aydin Corp., a telecommunications equipment company, formerly traded on the New York Stock Exchange from May 1982 until it was acquired in September 1996. She also was Vice President of Business Development for Kaifa Technology from October 1998 to August 2000 and was instrumental in its acquisition by E-Tek Dynamics, then again acquired by JDS Uniphase. Through these acquisitions, she held the role of Deputy General Manager of the Kaifa Technology business unit. Ms. Hakimoglu earned a Bachelor of Science Degree in Physics from California State College, Sonoma, and a Master s Degree in Physics from Drexel University. In light of Ms. Hakimoglu s rich experience in the high-tech industry and her unique and extensive understanding of ClearOne s business, our Board has concluded that Ms. Hakimoglu should continue to serve as a director.

Brad R. Baldwin has served as a director of our company since October 1988. Mr. Baldwin is an attorney licensed to practice in Utah. Since April 2009, Mr. Baldwin has served as general counsel to the Wasatch Front Regional Multiple Listing Service (WFRMLS). The WFRMLS currently assists over 12,000 brokers, agents and appraisers with their MLS needs and services. From April 2001 to April 2009, he served as an attorney and investment real estate specialist with the commercial real estate business with Commerce CRG in Salt Lake City, Utah. From 1988 to 2000, he served as legal counsel and president of Bank One, Utah. He also practiced business, corporate and real

estate law for ten years in Salt Lake City. He has a degree in finance from the University of Utah and a law degree from the University of Washington. He has served on the board of many community organizations, including the Salt Lake Area Chamber of Commerce, the Utah Bankers Association, and the Economic Development Corporation of Utah. In light of Mr. Baldwin s legal background and unique understanding of our business due to his long service on our Board, the Board has concluded that Mr. Baldwin should continue to serve as a director.

Larry R. Hendricks has served as a director of our company since June 2003. Mr. Hendricks is a Certified Public Accountant who retired in December 2002 after serving as Vice President of Finance and General Manager of Daily Foods, Inc., a national meat processing company. During his 30-year career in accounting, he served as a self-employed CPA and worked for the international accounting firm Peat Marwick & Mitchell. Mr. Hendricks has served on the boards of eight other organizations, including Tunex International, Habitat for Humanity, Daily Foods, and Skin Care International. He earned a Bachelor s Degree in Accounting from Utah State University and a Master of Business Administration Degree from the University of Utah. In light of Mr. Hendricks background in finance and accounting and his deep understanding of our business after his service on our Board, the Board has concluded Mr. Hendricks should continue to serve as a director.

Scott M. Huntsman has served as a director of our company since June 2003. Mr. Huntsman has served as President of GlobalSim, a technology and simulation company, since February 2003, and as Chief Financial Officer from April 2002 to February 2003. Prior to joining GlobalSim, he spent 11 years on Wall Street as an investment banker, where he focused on mergers, acquisitions, and corporate finance transactions. Mr. Huntsman served at Donaldson, Lufkin and Jenrette Securities Corporation from August 1996 to 2000, when they merged with Credit Suisse First Boston where he served until October 2001. Mr. Huntsman earned a Bachelor s Degree from Columbia University and a Master of Business Administration Degree from The Wharton School at the University of Pennsylvania. He also studied at the London School of Economics as a Kohn Fellowship recipient. In light of Mr. Huntsman s background in finance and particularly in the areas of mergers and acquisitions and corporate finance, and in view of his experience as a leader of a technology company, the Board has concluded Mr. Huntsman should continue to serve as a director.

E. Bryan Bagley has served as a director of our company since November 2009. Mr. Bagley was a director of Nevada Chemicals from June 2000 until the company was sold in September 2008 and served as Chairman of the Board of Nevada Chemicals from December 2001 until September 2008. Since November 2002, Mr. Bagley has been a private investor managing accounts on his own behalf. From December 1991 to November 2002, Mr. Bagley served as a market maker for Wilson-Davis & Company. Prior to that position, he served as a trader for Covey & Co. and Bagley Securities. Mr. Bagley graduated from the University of Utah in 1987 with a Bachelor of Science degree in Economics. Mr. Bryan Bagley is the son of Edward D. Bagley, our former Chairman of the Board. Mr. Edward D. Bagley beneficially owns 23.3% of our issued and outstanding common stock. In light of Mr. Bagley s prior experience as the chairman of a public company and the benefit that may accrue to our company from his leadership experience, the Board has concluded that Mr. Bagley should continue to serve as a director.

Security holders who would like to send communications to any director or the entire Board may do so by submitting such communications to ClearOne Communications, Inc., 5225 Wiley Post Way, Suite 500, Salt Lake City, Utah 84116, Attention: Investor Relations or investor_relations@clearone.com. The communications will then be forwarded to the appropriate director or the entire Board. The Board suggests, but does not require, that such submissions include the name and contact information of the security holder making the submission and a description of the matter that is the subject of the communication.

CORPORATE GOVERNANCE

Information Relating to Corporate Governance and the Board of Directors

Our Board of Directors has determined, after considering all the relevant facts and circumstances, that Messrs. Baldwin, Hendricks, and Huntsman are independent directors, as independence is defined by the listing standards of NASDAQ, because they have no relationship with us that would interfere with their exercise of independent judgment.

Our Board of Directors has an Audit and Compliance Committee, a Compensation Committee, and a Nominating Committee, each consisting entirely of independent directors.

Our Board of Directors has adopted charters for the Audit and Compliance, Compensation and Nominating Committees describing the authority and responsibilities delegated to each committee by the Board. We post on our website at www.clearone.com the charters of our Audit and Compliance, Compensation and Nominating Committees, our Code of Ethics, and any amendments or waivers thereto and any other corporate governance materials contemplated by SEC or NASDAQ regulations. These documents are also available in print to any stockholder requesting a copy in writing from our Corporate Secretary at our corporate offices set forth in this proxy statement.

Board Leadership Structure

The Board has no formal policy on whether the role of the Chairman of the Board and Chief Executive Officer should be held by separate persons. We believe it is important to maintain flexibility to have either combined offices or a separate Chairman and Chief Executive Officer structure as circumstances dictate and to make that determination based on the strategic and operational position and direction of the company and the character of the membership of the Board.

The Board believes our current management structure, with Zeynep Hakimoglu serving as Chairman and Chief Executive Officer, is the optimal structure for us at this time. Ms. Hakimoglu possesses detailed and in-depth knowledge of the operational issues, opportunities and challenges facing the Company and its business, and also has a keen understanding of and ability to grasp our strategic position and opportunities. Given Ms. Hakimoglu s particular skills and knowledge, as well as our size and stage of development, we believe Ms. Hakimoglu is best positioned to identify strategic priorities, develop agendas that the Board s time and attention should be focused on as the most critical matters, and to lead the discussion and execution of strategy.

The Chief Executive Officer and the independent directors have different perspectives and roles in strategy development. The Chief Executive Officer brings Company-specific experience and expertise, while the Company s independent directors bring experience, oversight, and expertise from outside the Company and its industry. The Board believes its independent directors provide effective oversight of management, and that the combined role of Chief Executive Officer and Chairman promotes the development and execution of strategy and facilitates the flow of information between management and the Board, which is essential to effective corporate governance. Given the Board s confidence in the effectiveness of the current balance of positions and personalities, we have not appointed a lead independent director. The Board believes the combined role of Chief Executive Officer and Chairman, together with a Board whose majority of directors are independent, provides the appropriate balance between independent oversight of management and the development of strategy.

Board Role in Risk Oversight

The Board of Directors is responsible for overseeing the management of the business and affairs of the Company, but delegates day-to-day management of the Company to the Chief Executive Officer and our executive management team. The Board of Directors is generally responsible for risk oversight, and the Audit and Compliance Committee assists the Board in fulfilling its responsibilities for general oversight of risk assessment and risk management. In addition, the other Board committees are also tasked with specific risk oversight functions pursuant to the terms of the committee charters or applicable NASDAQ rules. The Board as a whole and the various standing committees, in performing their respective risk oversight functions, have access to our company s management team and external advisors, as necessary, and receive periodic presentations and reports from management, and incidental reports as matters arise, with respect to strategic, operational, financial, legal or other risks and the plans management has to control such risks.

Committees of the Board of Directors

Audit and Compliance Committee. The Audit and Compliance Committee meets to review and discuss our accounting practices and procedures with management and independent public accountants and to review our quarterly and annual financial statements. The Audit and Compliance Committee assists the Board of Directors in fulfilling its responsibility for oversight of the quality and integrity of our accounting, auditing, and reporting practices. The Audit and Compliance Committee s primary duties include reviewing the scope and adequacy of our internal accounting and financial controls; reviewing the independence of our independent registered public accounting firm; approving the scope of our independent registered public accounting firm s audit activities; approving the fees of our independent registered public accounting firm; approving any non-audit related services; reviewing the audit results; reviewing the objectivity and effectiveness of our internal audit function; and reviewing our financial reporting activities and the application of accounting standards and principles.

The members of the Audit and Compliance Committee are Scott M. Huntsman (Chairman), Brad R. Baldwin, and Larry R. Hendricks. Each member of the audit committee, in addition to being independent under the standards of

NASDAQ, is independent under the standards of the Securities and Exchange Commission s rules and regulations pertaining to listed company audit committees. The Board of Directors has determined that Scott M. Huntsman is an audit committee financial expert in accordance with applicable rules and regulations of the SEC.

Compensation Committee. The Compensation Committee is responsible for overseeing, reviewing, and approving our executive compensation and benefit programs and administers the Company s equity incentive plans for employees. Under its charter, the Compensation Committee may delegate authority to subcommittees of the Compensation Committee or to executive officers of the Company, particularly the President and CEO with respect to compensation determinations for persons who are not executive officers of the Company. The members of the Compensation Committee are Brad R. Baldwin (Chairman), Larry R. Hendricks and Scott M. Huntsman.

Our compensation objectives for executive officers are as follows:

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to attract and retain highly qualified individuals capable of making significant contributions to the long-term success of our company;

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to use incentive compensation to reinforce strategic performance objectives;

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to align the interest of our executives with the interests of our shareholders such that risks and rewards of strategic decisions are shared; and

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to reflect the value of each officer s position in the marketplace and within our company.

Policies and Practices Related to ClearOne s Compensation Program. We strive to create an overall compensation package for each executive officer that satisfies the aforementioned objectives, recognizing that certain elements of compensation are better suited to reflect different compensation objectives. For example, as base salaries are the only element of compensation that are fixed in amount in advance of the year in which the compensation will be earned, the Compensation Committee believes that it is most appropriate to determine base salaries with a focus on the market practices for similarly situated officers at comparable companies as adjusted to reflect the individual officer s performance during the preceding year. In contrast, cash bonuses and long-term incentives are better able to reflect our company s performance as measured by financial metrics and are well-suited to motivate officers to achieve specific performance goals that the Compensation Committee has determined are in the best interests of our company. Equity grants are also well-suited to drive long-term performance and align management s interests with those of shareholders. The Compensation Committee believes that as an officer s responsibility increases, so does his or her ability to influence the performance of our company and accordingly, the proportion of his or her compensation that consists of his or her salary and cash bonus should decrease while the proportion of equity incentives to total compensation should increase.

Comparable Companies. In making compensation decisions, including assessing the competitiveness of the total compensation structure for each named executive officer, the Compensation Committee considers compensation survey data from companies that the Compensation Committee has selected as comparable companies, namely comparable in terms of size and location. The Compensation Committee periodically reviews the companies that are included as comparable companies and makes revisions to the group as appropriate. During February 2010, the company obtained comparable compensation data from Equilar. The Compensation Committee reviewed the compensation data to ensure the company s compensation of executives is reasonable.

Equity Grant Practices. The Compensation Committee recognizes the importance of equity ownership in the alignment of shareholder and management interests. The exercise price of each stock option awarded to our executive officers under our incentive compensation programs is equal to the closing price of our common stock on the date of grant, which is the date when the Compensation Committee acts to approve equity awards for senior executives. Performance-based equity awards are also granted to our named executive officers at this time.

The Compensation Committee establishes the criteria, and directs the implementation, of all compensation program elements for the executive officers. Generally, the base salary for each named executive officer is set at the beginning of each fiscal year by our Board of Directors after review of the recommendation of the Compensation Committee. The Compensation Committee considers the Chief Executive Officer s appraisal of other executive officers general performance and looks especially to performance against predetermined goals before making its recommendation to the Board of Directors. In the past, the Compensation Committee has authorized the Chief Executive Officer to recruit executive officers and offer initial base salaries. The Chief Executive Officer recommends for the Compensation Committee s approval the stock option grants and compensation related to achievement of non-quantitative goals under non-equity based incentive plans for other executive officers. The Compensation Committee did not employ any compensation consultants during the year ended December 31, 2011.

Nominating Committee. The Nominating Committee is responsible for overseeing the nomination of our directors. The Nominating Committee selects, evaluates, and recommends to the full Board of Directors qualified candidates for election to the Board of Directors. The members of the Nominating Committee are Larry R. Hendricks (Chairman), Brad R. Baldwin, and Scott M. Huntsman.

The Board of Directors will consider recommendations by shareholders for director nominees if the names of those nominees and relevant biographical information are submitted in writing to our company s Secretary in the manner described for shareholder nominations below under the heading Shareholder Proposals. The Nominating Committee identifies and evaluates nominees for our Board of Directors, including nominees recommended by shareholders, based on numerous factors it considers appropriate, some of which may include strength of character,

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mature judgment, career specialization, relevant technical skills, diversity, and the extent to which the nominee would fill a present need on our Board of Directors. Although the Nominating Committee does not have a formal policy with regard to the consideration of diversity in identifying director nominees, the Nominating Committee strives to nominate directors with a variety of complementary skills so that, as a group, the Board will possess the appropriate talent, skills and expertise to oversee the Company s business. All director nominations, whether submitted by a shareholder, the Nominating Committee, or the Board of Directors, will be evaluated in the same manner. The current nominees for director were recommended by the Nominating Committee and nominated by the Board of Directors, including the independent members thereof.

Board and Committee Meetings

Our Board of Directors held a total of 10 meetings in 2011. No director attended fewer than 75% of the aggregate of (i) the total number of meetings of the Board of Directors; and (ii) the total number of meetings held by all committees of the Board of Directors on which such director was a member. Although we currently have no formal policy with respect to the attendance of members of the Board of Directors at the Annual Meetings of Shareholders, we encourage each of our directors to attend each annual meeting of shareholders. To that end, and to the extent reasonably practicable, we regularly schedule a meeting of the Board of Directors on the same day as our annual meeting of shareholders. All members of our Board of Directors attended the 2011 Annual Meeting of Shareholders.

In 2011, the Audit and Compliance Committee held 6 meetings, the Compensation Committee held 5 meetings, and the Nominating Committee held 2 meetings.

Code of Ethics

The Board of Directors adopted a code of ethics that applies to our Board of Directors, executive officers, and employees. The Company s Code of Ethics is posted on our website at www.clearone.com.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Exchange Act, as amended, requires our directors, executive officers and persons who own more than 10% of a registered class of our equity securities to file with the SEC initial reports of ownership on Form 3 and reports of changes of ownership of our equity securities on Forms 4 and 5. Officers, directors, and greater than 10% shareholders are required to furnish us with copies of all Section 16(a) reports they file. Based solely on a review of the reports and amendments to reports furnished to us for the year ended December 31, 2011, and written representations that no other reports were required, we believe that each person who, at any time during such fiscal year was a director, officer, or beneficial owner of more than 10% of our common stock, complied with all Section 16(a) filing requirements during such period , except that Edward Dallin Bagley, a beneficial owner of more than 10% of our common stock filed two Forms 4 late for one transaction each.

EXECUTIVE OFFICERS

The following table sets forth certain information regarding our executive officers.

Name	Age	Position
Zee Hakimoglu	59	President, Chief Executive Officer, and Chairman of the Board of Directors
Narsi Narayanan	42	Vice President of Finance and Corporate Secretary
Michael E. Braithwaite	44	Chief Strategy Officer

For the biography of Ms. Hakimoglu, see Nominees for Director.

Narsi Narayanan has served as our Vice President of Finance since July 2009 and has over 18 years of professional experience in the areas of accounting, finance and taxes. Prior to joining our company, he managed the SEC reporting, US GAAP accounting research, SOX compliance and other financial reporting functions from August 2007 through February 2009 at Solo Cup Company, a publicly reporting international consumer products company. Prior to that, Mr. Narayanan managed the accounting and finance functions, including SEC Reporting, SOX compliance and US GAAP accounting research, from June 2004 through August 2007 at eCollege.com,

a leading technology company serving private educational institutions which was also a publicly reporting company before being acquired by Pearson Education group. In addition to being a Chartered Accountant, Mr. Narayanan has extensive experience working in public accounting and in various senior finance positions in India with large public companies. He is a Certified Public Accountant with graduate degrees in accounting (M. Acc.) and business (MBA-Finance).

Michael Braithwaite joined us in November 2009 through the acquisition of NetStreams, Inc. where he was the co-founder and CTO since 2004. Mr. Braithwaite has led a distinguished twenty-plus-year career as a visionary, disruptive innovator, and proven leader in the professional audio and consumer electronics industries. He has authored more than twenty U.S. and International patents. Before NetStreams, Inc., Mr. Braithwaite was a product and market manager for Crestron Electronics where he worked on highly successful audio and video distribution products. He currently serves on the Consumer Electronics Association s R10 working group technical committees and the AVnu (AVB) marketing and technical committees and is a very active member in technology standard efforts for the CEA and other standard-setting bodies.

EXECUTIVE COMPENSATION

Summary Compensation

The following tables set forth for the periods indicated, the compensation paid or earned by each named executive officer for the years ended December 31, 2011 and 2010.

Name and Principal Position	Salary	Option Awards[1]	Non-Equity Incentive Plan Compensation[2]	All Other Compensation[3]	Total
Zee Hakimoglu - Chairman of the Board, Chief Executive Officer and President					
	$	$	$	$	
Year ended December 31, 2011	230,000	29,436	93,953	-	$353,389
Year ended December 31, 2010	225,000	12,400	73,523	-	310,923
Tracy A. Bathurst (4) - Chief Strategy Officer					
Year ended December 31, 2011	35,769	-	22,900	300	58,969
Year ended December 31, 2010	150,000	12,400	47,862	2,425	212,687
Narsi Narayanan Vice President of Finance and Corporate Secretary					
Year ended December 31, 2011	135,000	29,436	52,090	-	216,526
Year ended December 31, 2010	122,500	12,400	43,728	-	178,628
Michael Braithwaite Chief Strategy Officer					
Year ended December 31, 2011	155,000	29,436	59,539	2,200	246,175
Year ended December 31, 2010	152,500	12,400	49,548	9,275	223,723

(1)

The amounts in the Option Awards column reflect the aggregate grant date fair value of awards of stock options granted pursuant to our long-term incentive plans during the periods reported above, computed in accordance with FASB ASC Topic 718, *Compensation - Stock Compensation.* The assumptions made in the valuation of our option awards are disclosed in Note 9 - Share Based Payments in our Notes to Consolidated Financial Statements contained in our annual report on Form 10-K for the year ended December 31, 2011.

(2)

Non-Equity Incentive Plan Compensation is based upon the achievement of pre-determined quarterly goals, namely, quantitative financial goals comprising of revenue, gross margin and operating income, and non-quantitative performance goals. While quantitative financial goals are similar for all the executive officers, non-quantitative goals vary for each officer. Examples of non-quantitative goals include introduction of a new product, identification of a new distribution opportunity, implementing internal controls, and improving product quality. The Chief Executive Officer recommends to the Compensation Committee the compensation for achievement or partial achievement of any such predetermined goal. Compensation under the non-equity incentive plan is calculated by assigning 70% weight to quantitative financial goals (with revenue, gross margin and operating income having equal share) and 30% to non-quantitative goals.

Of the amounts included above, Ms. Hakimoglu s compensation for the year ended December 31, 2011 included $64,628 for achieving financial goals and $29,325 for achieving non-quantitative goals, and for the year ended December 31, 2010 included $56,273 for achieving financial goals and $17,250 for achieving non-quantitative goals. Mr. Bathurst s compensation for the year ended December 31, 2011 included $18,831 for achieving financial goals and $4,069 for achieving non-quantitative goals, and for the year ended December 31, 2010 included $37,923 for achieving financial goals and $9,939 for achieving non-quantitative goals. Mr. Narayanan s compensation for the year ended December 31, 2011 included $37,934 for achieving financial goals and $14,156 for achieving non-quantitative goals, and for the year ended December 31, 2010 included $33,030 for achieving financial goals and $10,698 for achieving non-quantitative goals. Mr. Braithwaite s compensation for the year ended December 31, 2011 included $43,554 for achieving financial goals and $15,985 for achieving non-quantitative goals, and for the year ended December 31, 2010 included $37,923 for achieving financial goals and $11,625 for achieving non-quantitative goals.

(3)

The amounts in the All Other Compensation column reflect the value of honorarium paid under a program to encourage the process of patenting process.

(4)

Mr. Bathurst left the company on May 13, 2011.

OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

The following table provides information on the holdings of stock options by the named executive officers as of December 31, 2011.

Name	Number of Securities Underlying Unexercised Options Exercisable	Number of Securities Underlying Unexercised Options Unexercisable (1)	Option Exercise Price	Option Grant Date	Option Expiration Date
Zee Hakimoglu	50,000	-	$ 6.40	03-24-04	03-24-14
	100,000	-	5.55	07-26-04	07-26-14
	150,000	-	3.65	09-18-06	09-18-16
	150,000	-	6.15	08-14-07	08-14-17
	50,000	-	4.03	11-14-08	11-14-18
	5,277	4,723	3.00	05-26-10	05-26-20
	-	10,000	5.48	08-05-11	08-05-21
Narsi Narayanan	23,333	6,667	2.78	08-27-09	08-27-19
	5,277	4,723	3.00	05-26-10	05-26-20
	-	10,000	5.48	08-05-11	08-05-21

Michael Braithwaite	10,833	19,167	2.65	11-30-09	11-30-19
	5,277	4,723	3.00	05-26-10	05-26-20
	-	10,000	5.48	08-05-11	08-05-21

(1)

Unvested options vest monthly over a three year period beginning on the date of grant.

Option Exercises

The following table provides information on the exercise of stock options by named executive officers during the year ended December 31, 2011.

Name	Number of shares acquired on exercise	Value realized on exercise [(1)]
Tracy A. Bathurst	95,138	$ 185,449

(1)

Value realized on exercise is the excess of market price of underlying shares on the date of exercise over exercise price for the options.

The following table sets forth information as of December 31, 2011 with respect to compensation plans under which equity securities of ClearOne are authorized for issuance.

	Number of securities to be issued upon exercise of outstanding options, warrants and rights	**Weighted-average exercise price of outstanding options, warrants and rights**	**Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))**
	(a)	(b)	(c)
Equity compensation plans approved by shareholders	1,160,933	$ 4.50	500,629
Equity compensation plans not approved by shareholders	-	-	-
Total	1,160,933	$ 4.50	500,629

Potential Payments Upon Termination or Change in Control

Employment Agreements. As of the year ended December 31, 2011, none of our named executive officers was party to an employment or severance agreement with us, and each named executive officer s employment was on an at-will basis, permitting either us or the executive to terminate his or her employment for any reason or for no reason.

Accelerated Stock Option Vesting Upon a Change in Control. For certain option grants to executive officers and directors, in the event of a change in control, all of such optionee s unvested stock options will vest and become exercisable immediately prior to the event or closing of the transaction causing the change in control.

Under the option grants, a *Change in Control* means a change in ownership or control of the Company effected through either of the following transactions:

(i) the acquisition, directly or indirectly, by any person or related group of persons (other than the Company or a person that directly or indirectly controls, is controlled by, or is under common control with, the Company), of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Company s outstanding securities pursuant to a tender or exchange offer made directly to the Company s shareholders, which the Board does not recommend such shareholders to accept, or

(ii) a change in the composition of the Board over a period of thirty-six (36) consecutive months or less, such that a majority of the Board members ceases, by reason of one or more contested elections for Board membership, to be comprised of individuals who either (A) have been Board members continuously since the beginning of such period or (B) have been elected or nominated for election as Board members during such period by at least a majority of the Board members described in clause (A) who were still in office at the time the Board approved such election or nomination.

Except as otherwise set forth in an option grant, in the event of a change in control of our company, the Board of Directors has the sole authority to elect that the vesting of each outstanding option automatically accelerate so that each such option shall, immediately prior to the effective date of the corporate transaction, become fully exercisable for all of the shares of common stock at the time subject to such option and may be exercised for any or all of those shares as fully vested shares of common stock.

At our current stock price of about $4.00, all the named executive officers would each benefit from any potential accelerated vesting of unvested stock options.

DIRECTOR COMPENSATION

Director Compensation

The following table summarizes the compensation paid by us to non-employee directors for the year ended December 31, 2011. Ms. Hakimoglu did not receive additional compensation for her service as a director.

Name	Fees Earned or Paid in Cash (1)	Option Awards (2) (3)	Total
	$	$	$
Brad R. Baldwin	24,000	14,718	38,718
Larry R. Hendricks	24,000	14,718	38,718
Scott M. Huntsman	24,000	14,718	38,718
E. Bryan Bagley	24,000	14,718	38,718

(1)

The base annual director s fee for the year ended December 31, 2011 was $24,000.

(2)

The amounts in the Option Awards column reflect the aggregate grant date fair value of awards of stock options granted pursuant to our long-term incentive plans during the periods reported above, computed in accordance with FASB ASC Topic 718, *Compensation - Stock Compensation*. The assumptions made in the valuation of our option awards are disclosed in Note 9 - Share Based Payments in our Notes to Consolidated Financial Statements contained in our annual report on Form 10-K for the year ended December 31, 2011.

(3)

As of the end of December 31, 2011, each non-employee director had outstanding options to purchase the following number of company shares of common stock: Mr. Baldwin, 140,000; Mr. Hendricks, 80,000; Mr. Huntsman, 90,000; and Mr. Bagley, 30,000.

All non-employee directors are paid a fixed fee at the rate of $2,000 per month and receive the same option grants. In August 2011, each non-employee director received a grant of options to purchase 5,000 shares of our common stock at an exercise price of $5.48. The fee is not dependent on the number of meetings attended by any directors. Directors are not paid additional compensation for chairing a committee. All directors are reimbursed by us for their out-of-pocket travel and related expenses incurred in attending all Board of Directors and committee meetings.

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

We recognize that transactions between us and any of our directors or executives can present potential or actual conflicts of interest and create the appearance that our decisions are based on considerations other than the best interests of our company and shareholders. Therefore, as a general matter and in accordance with our Code of Ethics, it is our preference to avoid such transactions. Nevertheless, we recognize that there are situations where such transactions may be in, or may not be inconsistent with, the best interests of our company. Under the terms of its charter, our Audit and Compliance Committee reviews and, if appropriate, approves or ratifies any such transactions.

Pursuant to the charter, the committee will review any transaction in which we are or will be a participant and the amount involved exceeds $120,000, and in which any of our directors or executives had, has or will have a direct or indirect material interest. After its review, the Committee will only approve or ratify those transactions that are in, or are not inconsistent with, the best interests of our company and our shareholders, as the committee determines in good faith.

Related Party Transactions: Indemnification of Officers and Directors

On July 25, 2007 and January 31, 2008, the U.S. Attorney for the District of Utah indicted two of our former officers, Frances Flood (Flood) and Susie Strohm (Strohm), for allegedly causing us to issue materially misstated financial statements for our 2001 and 2002 fiscal years and for perjury in connection with the investigation by the SEC into the alleged misstatements.

In December 2003, we entered into indemnification agreements with each former officer, requiring payment of all reasonable attorneys fees and costs incurred in defending against the charges in certain circumstances consistent with and subject to limitations imposed by our bylaws and applicable law. To date, we have paid approximately $2.9 million in attorneys fees and costs to defend ag="Times New Roman" SIZE="2">798,828798,311

Cash dividends paid

(1,959,765) (1,888,427)

Net cash used in continuing financing activities

(4,425,937) (5,115,116)

Net cash used in discontinued financing activities

(1,537,000) (960,000)

Net cash used in financing activities

(5,962,937) (6,075,116)

NET INCREASE IN CASH AND CASH EQUIVALENTS

3,302,258 3,593,870

CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR

1,490,141 1,349,518

CASH AND CASH EQUIVALENTS AT END OF YEAR

$4,792,399 $4,943,388

SUPPLEMENTAL INFORMATION:

Cash paid during the year for:

Interest	$2,039,238	$1,956,651
Income taxes net of refunds	1,952,794	1,897,415

See notes to condensed consolidated financial statements.

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1. In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly RGC Resources, Inc. s financial position as of June 30, 2007 and the results of its operations for the three months and nine months ended June 30, 2007 and 2006 and its cash flows for the nine months ended June 30, 2007 and 2006. The results of operations for the three months and nine months ended June 30, 2007 are not indicative of the results to be expected for the fiscal year ending September 30, 2007 as quarterly earnings are affected by the highly seasonal nature of the business and weather conditions generally result in greater earnings during the winter months.

2. The condensed consolidated interim financial statements and condensed notes are presented as permitted by Form 10-Q and do not contain certain information included in the Company s annual consolidated financial statements and notes thereto. The condensed consolidated financial statements and condensed notes should be read in conjunction with the financial statements and notes contained in the Company s Form 10-K.

3. Certain reclassifications were made to prior year financial statements to place them on a basis consistent with current year presentation with regard to discontinued operations as discussed below, utility property, nonutility property, accrued expenses and refunds from suppliers-due customers.

4. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

5. On February 16, 2007, RGC Resources, Inc. (Resources or Company) entered into a Purchase and Sale Agreement with ANGD LLC (ANGD) for the sale of all of the capital stock of Bluefield Gas Company (Bluefield Gas), a wholly owned subsidiary of Resources, to ANGD. The sales price will be equal to the book value of Bluefield Gas net assets on the date of closing, subject to mutually agreed upon or arbitrated purchase price adjustments determined subsequent to the closing date but no later than 230 days after Closing. In connection with the sale, (i) certain real estate will be distributed to the Company (or its designee) prior to Closing, (ii) inter-company receivables or payables existing between Bluefield Gas and the Company (including its other affiliates) will be settled as of Closing, and (iii) the Company will pay off Bluefield Gas outstanding debt at Closing out of the sales proceeds.

Also on February 16, 2007, Roanoke Gas entered into an Asset Purchase and Sale Agreement with Appalachian Natural Gas Distribution Company (Appalachian) for the sale of Roanoke Gas natural gas distribution assets located in the Town of Bluefield and the County

RGC RESOURCES, INC. AND SUBSIDIARIES

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of Tazewell, Virginia, (Bluefield division of Roanoke Gas Company) to Appalachian, which is a wholly owned subsidiary of ANGD. The sales price will be equal to the book value of net plant plus 1% and the book value of accounts receivable, natural gas inventory, and certain other listed current assets, subject to mutually agreed upon or arbitrated purchase price adjustments determined subsequent to the closing date but no later than 230 days after Closing. $1,300,000 of such sale price is payable in the form of a promissory note from ANGD with a 5-year term and a 15-year amortization schedule with annual principal payments and quarterly interest payments at a 10% interest rate.

Bluefield Gas and the Bluefield division of Roanoke Gas Company (Bluefield Operations) represent approximately 4,600 of Resources 60,200 customers and approximately $11,900,000 of the consolidated assets and $6,700,000 of the consolidated liabilities of the Company as reflected below.

The Board of Directors approved the Purchase and Sale Agreements of Bluefield Gas and the Bluefield division of Roanoke Gas Company for several reasons. The management time and effort required to oversee operations in West Virginia are significantly disproportionate to the size of the operation. The regulatory environment in West Virginia hindered the ability to recover increasing expenses on a timely basis resulting in net losses from those operations in each of the last four fiscal years. The economic conditions in southern West Virginia have lead to a loss of population and gas customers in the West Virginia service area. Management believes that the net proceeds realized from these transactions can be reinvested in the Roanoke Gas operations and ultimately provide a better return for the Company than could be realized in the Bluefield operations.

The transactions contemplated by the purchase agreements require the approval of the respective regulatory commissions: the West Virginia Public Service Commission (PSC) for the sale of Bluefield Gas and the Virginia State Corporation Commission (SCC) for the sale of Virginia assets. Furthermore, the closing of each of the purchase agreements is conditioned upon such approval of the other transaction. Therefore, the parties intend that either both transactions will close or neither will close. SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, requires that long-lived assets or disposal groups to be sold shall be classified as held for sale in the period in which certain criteria are met. Paragraph 30.d. of SFAS No. 144 specifies The sale of the asset (disposal group) is probable Although the Company has not received final approval for either transaction from the respective commissions, the Company has reached a stipulated agreement regarding the sales transaction and a pending request for increased non-gas rates with the West Virginia PSC staff and the West Virginia Consumer Advocate Division. Although an agreement has been reached with two of the key parties in the cases, final approval from the PSC is not assured; however, Company management does believe that such an agreement makes the ultimate approval of the sale probable. Furthermore, Company management believes that the SCC will likely approve the sale of the Bluefield division of Roanoke Gas Company. As a result, the Company believes that the pending sales transactions meet the definition of

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probable as required by SFAS No. 144, and the results of operations of both Bluefield Gas and the Bluefield division of Roanoke Gas Company are reflected as discontinued operations.

In July 2006, the company entered into an asset purchase and sale agreement for the sale of the assets relating to its Highland Energy gas marketing business. The assets sold included the gas supply contracts between Highland Energy and its customers and related business records. The operations associated with the energy marketing business were reclassified as Discontinued Operations in accordance with the provisions of SFAS No. 144. Under the agreement, a portion of the purchase price was deferred as realization of those revenues was subject to certain provisions. As these provisions had been achieved as of June 30, 2007, the Company recorded $160,000 revenue in final settlement of the sales contract as part of discontinued operations.

The components of discontinued operations from each of these transactions is reflected below:

	Three Months Ended June 30,		**Nine Months Ended June 30,**	
	2007	**2006**	**2007**	**2006**
Bluefield Operations				
Total Revenues	$ 1,653,605	$ 1,464,409	$ 10,268,630	$ 11,969,209
Gain on Sale of Assets				
Pretax Operating Income (Loss)	(179,427)	(216,285)	252,752	134,699
Continuing Costs	209,996	181,415	563,164	525,374
Income Tax (Expense) Benefit	(9,735)	17,838	(314,551)	(251,460)
Discontinued Operations	$ 20,834	$ (17,032)	$ 501,365	$ 408,613
Highland Energy				
Revenues	$	$ 4,603,741	$	$ 20,771,453
Gain on Sale of Assets	160,162		160,162	
Pretax Operating Income (Loss)		(125,599)		94,227
Continuing Costs		19,129		48,248
Income Tax (Expense) Benefit	(60,582)	40,416	(60,582)	(54,083)
Discontinued Operations	$ 99,580	$ (66,054)	$ 99,580	$ 88,392
Total				
Revenues	$ 1,653,605	$ 6,068,150	$ 10,268,630	$ 32,740,662
Gain on Sale of Assets	160,162		160,162	
Pretax Operating Income (Loss)	(179,427)	(341,884)	252,752	228,926
Continuing Costs	209,996	200,544	563,164	573,622
Income Tax (Expense) Benefit	(70,317)	58,254	(375,133)	(305,543)
Discontinued Operations	$ 120,414	$ (83,086)	$ 600,945	$ 497,005

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The carrying amounts of the major classes of assets and liabilities subject to the purchase agreements for the period ended June 30, 2007 and September 30, 2006 are as follows:

	June 30, 2007	September 30, 2006
Assets:		
Accounts receivable	$ 555,534	$ 658,551
Gas in storage	2,204,948	3,399,639
Other current assets	47,801	619,862
Net utility plant	9,061,407	8,962,113
Other assets	57,696	86,626
Total assets	$ 11,927,386	$ 13,726,791
Liabilities:		
Accounts payable	$ 1,177,390	$ 1,122,978
Accrued expenses	258,536	217,054
Other current liabilities	2,112,722	3,818,416
Non current liabilities	3,153,301	3,094,015
Total liabilities	$ 6,701,949	$ 8,252,463

Each of the purchase agreements provides at closing for a services agreement to be executed whereby Resources and Roanoke will provide certain customer billing, gas control, regulatory and other administrative services for Bluefield and Appalachian on mutually agreeable terms.

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Resources does not anticipate the closing of the purchase agreements to result in a material gain or loss in the consolidated results of operations.

6. Since 2003, Roanoke Gas Company has had in place a weather normalization adjustment tariff (WNA) based on a weather occurrence band around the most recent 30-year temperature average. The weather band provides approximately a 6 percent range around normal weather, whereby if the number of heating-degree days (an industry measure by which the average daily temperature falls below 65 degrees) falls within the weather band, no adjustment is made. However, if the number of heating-degree days is below the weather band, the Company will add a surcharge to customer bills equal to the equivalent margin lost beyond the weather band deficiency. Conversely, if the number of heating-degree days is above the weather band, the Company will credit customer bills equal to the excess margin realized above the weather band. The measurement period in determining the weather band extends from April through March. The total heating-degree days for the period April 2006 through March 2007 were approximately 12 percent less than the 30-year average. The Company recorded approximately $439,000 in additional revenues in continuing operations during the first two quarters to reflect the estimated impact of the WNA tariff for the difference in margin realized for weather between 12 percent and 6 percent warmer than the 30-year average. Roanoke Gas Company received approval for the WNA rate factors to be used in billing the surcharge to its customers and the WNA tariff was billed during the May billing cycle. For the measurement period of April 2005 through March 2006, the heating-degree days were approximately 11 percent less than the 30-year average. As a result, the income statement for the nine-month period ended June 30, 2006 included approximately $316,000 in additional revenues attributable to the WNA.

7. The Company s risk management policy allows management to enter into derivatives for the purpose of managing commodity and financial market risks of its business operations. The Company s risk management policy specifically prohibits the use of derivatives for speculative purposes. The key market risks that the Company would seek to hedge include the price of natural gas and the cost of borrowed funds.

The Company has historically entered into futures, swaps and caps for the purpose of hedging the price of natural gas in order to provide price stability during the winter months. The Company had settled all outstanding natural gas derivative arrangements in the prior quarter and had not entered into any new agreements during the current quarter.

The Company entered into an interest rate swap related to the $15,000,000 note issued in November 2005. The swap essentially converted the floating rate note based upon LIBOR into fixed rate debt with a 5.74 percent interest rate. The swap qualifies as a cash flow hedge with changes in fair value reported in other comprehensive income.

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A summary of other comprehensive income and derivative activity is provided below.

Three Months Ended June 30, 2007	**Interest Rate Swap**	**Minimum Pension Liability**	**Total**
Unrealized gains	$ 494,292	$	$ 494,292
Income tax expense	(187,633)		(187,633)
Net unrealized gains	306,659		306,659
Transfer of realized gains to income	(10,238)		(10,238)
Income tax expense	3,886		3,886
Net transfer of realized losses to income	(6,352)		(6,352)
Net other comprehensive income	$ 300,307	$	$ 300,307

Three Months Ended June 30, 2006	**Interest Rate Swap**	**Minimum Pension Liability**	**Total**
Unrealized gains	$ 315,566	$ 196,227	$ 511,793
Income tax expense	(119,789)	(74,566)	(194,355)
Net unrealized gains	195,777	121,661	317,438
Transfer of realized losses to income	2,590		2,590
Income tax benefit	(983)		(983)
Net transfer of realized losses to income	1,607		1,607
Net other comprehensive income	$ 197,384	$ 121,661	$ 319,045

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Nine Months Ended June 30, 2007	Interest Rate Swap	Minimum Pension Liability	Total
Unrealized gains	$ 459,265	$	$ 459,265
Income tax expense	(174,337)		(174,337)
Net unrealized gains	284,928		284,928
Transfer of realized losses to income	(30,819)		(30,819)
Income tax benefit	11,698		11,698
Net transfer of realized losses to income	(19,121)		(19,121)
Net other comprehensive income	$ 265,807	$	$ 265,807
Fair value of marked to market transactions	$ 423,887		$ 423,887
Accumulated comprehensive income	$ 262,979		$ 262,979

Nine Months Ended June 30, 2006	Interest Rate Swap	Minimum Pension Liability	Total
Unrealized gains	$ 602,555	$ 588,681	$ 1,191,236
Income tax expense	(228,730)	(223,699)	(452,429)
Net unrealized gains	373,825	364,982	738,807
Transfer of realized losses to income	22,731		22,731
Income tax benefit	(8,628)		(8,628)
Net transfer of realized losses to income	14,103		14,103
Net other comprehensive income	$ 387,928	$ 364,982	$ 752,910
Fair value of marked to market transactions	$ 638,892		$ 638,892
Accumulated comprehensive income (loss)	$ 396,369	(23,930)	$ 372,439

8. Basic earnings per common share for the three months and nine months ended June 30, 2007 and 2006 are calculated by dividing net income by the weighted average common shares outstanding during the period. Diluted earnings per common share for the three months and nine months ended June 30, 2007 and 2006 are calculated by dividing net income by the weighted average common shares outstanding during the period plus dilutive potential common shares. Dilutive potential common shares are calculated in accordance with the treasury stock method, which assumes that proceeds from the exercise of all options are used

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to repurchase common stock at market value. The amount of shares remaining after the proceeds are exhausted represents the potentially dilutive effect of the securities. A reconciliation of the weighted average common shares and the diluted average common shares is provided below:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2007	2006	2007	2006
Weighted average common shares	2,167,655	2,127,188	2,157,712	2,115,060
Effect of dilutive securities:				
Options to purchase common stock	11,428		10,452	10,455
Diluted average common shares	2,179,083	2,127,188	2,168,164	2,125,515

9. The Company has both a defined benefit pension plan (the pension plan) and a post - retirement benefit plan (the post-retirement plan). The pension plan covers substantially all of the Company s employees and provides retirement income based on years of service and employee compensation. The post-retirement plan provides certain healthcare and supplemental life insurance benefits to retired employees who meet specific age and service requirements. Net pension plan and post-retirement plan expense recorded by the Company is detailed as follows:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2007	2006	2007	2006
Components of net periodic pension cost:				
Service cost	$ 101,227	$ 119,320	$ 303,681	$ 357,960
Interest cost	185,228	173,896	555,684	521,688
Expected return on plan assets	(172,816)	(157,068)	(518,448)	(471,204)
Recognized (gain) loss	18,050	60,077	54,150	180,231
Net periodic pension cost	$ 131,689	$ 196,225	$ 395,067	$ 588,675

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	Three Months Ended June 30,		Nine Months Ended June 30,	
	2007	2006	2007	2006
Components of post-retirement benefit cost:				
Service cost	$ 36,923	$ 39,621	$ 110,769	$ 124,922
Interest cost	125,461	116,673	376,383	364,694
Expected return on plan assets	(59,724)	(52,842)	(179,172)	(162,185)
Amortization of unrecognized transition obligation	47,223	46,119	141,669	154,878
Recognized loss	2,472	18,153	7,416	60,818
Net post-retirement benefit cost	$ 152,355	$ 167,724	$ 457,065	$ 543,127

The Company contributed $600,000 to its pension plan for the nine-month period ended June 30, 2007. The Company expects to make a total contribution of approximately $800,000 to its pension plan and $700,000 to its post-retirement benefit plan during the fiscal year ending September 30, 2007.

10. Both Roanoke Gas Company and Bluefield Gas Company, subsidiaries of RGC Resources, Inc., operated manufactured gas plants (MGPs) as a source of fuel for lighting and heating until the late 1940s or early 1950s. A by-product of operating MGPs was coal tar, and the potential exists for on-site tar waste contaminants at the former plant sites. The extent of contaminants at these sites, if any, is unknown at this time. An analysis at the Bluefield Gas Company site indicates some soil contamination. The Company, with concurrence of legal counsel, does not believe any events have occurred requiring regulatory reporting. Further, the Company has not received any notices of violation or liabilities associated with environmental regulations related to the MGP sites and is not aware of any off-site contamination or pollution as a result of prior operations. Therefore, the Company has no plans for subsurface remediation at the MGP sites. Should the Company eventually be required to remediate either site, the Company will pursue all prudent and reasonable means to recover any related costs, including insurance claims and regulatory approval for rate case recognition of expenses associated with any work required. A stipulated rate case agreement between the Company and the West Virginia Public Service Commission recognized the right of Bluefield Gas Company to defer MGP clean-up costs, should any be incurred, and to seek rate recovery for such costs. While the Company is selling the stock of Bluefield Gas Company to ANGD, LLC, and retaining ownership of the former MPG site, an indemnification and cost sharing agreement that is part of the sales agreement obligates Bluefield Gas Company to seek rate recovery of any remediation costs not recovered through other means and to share in any such costs to the extent they are not recovered through rates. The former Bluefield Gas Company MPG site is currently in active use as a propane bulk storage and distribution facility under lease to a propane distributor. If the Company eventually incurs costs associated with a required clean-up of the Roanoke Gas Company MGP site, the Company anticipates recording a regulatory asset for such clean-up costs to be

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recovered in future rates. Based on anticipated regulatory actions and current practices, management believes that any costs incurred related to this matter will not have a material effect on the Company s financial condition or results of operations.

11. In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109*. This statement clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. This Interpretation prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The recognition threshold is based upon whether it is more-likely-than-not that a tax position taken by an enterprise will be sustained upon examination. The measurement attribute of a more-likely-than-not tax position is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. The effective date of this statement is for fiscal years beginning after December 15, 2006. The Company has not completed its evaluation of this statement but does not anticipate the adoption to have a material impact on the Company s financial position, results of operations or cash flows.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. This statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value methods. This statement does not require any new fair value measurements. Instead, it provides for increased consistency and comparability in fair value measurements and for expanded disclosure surrounding the fair value measurements. This statement is effective for fiscal years beginning after November 15, 2007. The Company does not anticipate the adoption of this statement to have a material impact on the Company s financial position, results of operations or cash flows.

In September 2006, the FASB issued SFAS No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132R.* This statement requires employers who sponsor one or more single-employer defined benefit plans to recognize the overfunded or underfunded position of such plan(s) as an asset or liability in its balance sheet and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. This statement also requires the measurement of the defined benefit plan assets and obligations as of the date of the employer s balance sheet date and additional disclosures in the financial statement footnotes. The effective date of this statement is for fiscal years ending after December 15, 2006. The requirement to measure plan assets and benefit obligations as of the fiscal year end balance sheet date is effective for fiscal years ending after December 15, 2008. The Company has not completed its evaluation of this statement and has not yet determined the full impact on the Company s financial position or results of operations in light of the current regulatory environment and the application of SFAS No. 71. In the absence of the considerations of SFAS No. 71 and using the most recent actuarial valuation

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as of June 30, 2006, the effect on the June 30, 2007 balance sheet would have been to increase accrued postretirement benefits and accumulated comprehensive loss by approximately $4,200,000 and $2,600,000, respectively, and decrease the deferred income tax liability by approximately $1,700,000. The Company does not expect the adoption of this statement to adversely affect the results of operations or cash flows on a going forward basis.

In June 2006, the FASB issued Emerging Issues Tax Force (EITF) Issue No. 06-3, *How Sales Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross Versus Net Presentation)*. EITF requires disclosure of accounting policy regarding the gross or net presentation of point-of-sales taxes such as sales tax and value-added tax. If taxes included in gross revenues are significant, the amount of such taxes for each period for which an income statement is presented should be disclosed. With the exception of the West Virginia Business and Occupation Taxes (B&O) imposed on sales by Bluefield Gas Company within the state of West Virginia, all such taxes encompassed by this EITF are recorded at net and not gross. As discussed above, the Bluefield Gas operations have been reclassified to discontinued operations.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities.* This statement permits, but does not require, entities to choose to measure selected financial assets and liabilities at fair value. Although SFAS No. 159 does not eliminate the fair value disclosure requirements included in other accounting standards, it does provide for additional presentation and disclosures designed to facilitate comparisons between companies that choose different measurement attributes for similar assets and liabilities. The effective date of this statement is for fiscal years beginning after November 15, 2007. The Company has not completed its evaluation of this statement, nor determined the potential effect on its financial position, results of operations or cash flows.

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Forward-Looking Statements

From time to time, RGC Resources, Inc. (Resources or the Company) may publish forward-looking statements relating to such matters as anticipated financial performance, business prospects, technological developments, new products, research and development activities and similar matters. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. In order to comply with the terms of the safe harbor, the Company notes that a variety of factors could cause the Company s actual results and experience to differ materially from the anticipated results or other expectations expressed in the Company s forward-looking statements. The risks and uncertainties that may affect the operations, performance, development and results of the Company s business include the following: (i) failure to earn on a consistent basis an adequate return on invested capital; (ii) ability to retain and attract professional and technical employees; (iii) price competition from alternative fuels; (iv) volatility in the price and availability of natural gas; (v) uncertainty in the projected rate of growth of natural gas requirements in the Company s service area; (vi) general economic conditions both locally and nationally (for instance, southern West Virginia); (vii) increases in interest rates; (viii) increased customer delinquencies and conservation efforts resulting from high fuel costs and/or colder weather; (ix) developments in electricity and natural gas deregulation and associated industry restructuring; (x) variations in winter heating degree-days from normal; (xi) changes in environmental requirements, pipeline operating requirements and cost of compliance; (xii) impact of potential increased regulatory oversight and compliance requirements due to financial, environmental, safety and system integrity laws and regulations; (xiii) failure to obtain timely rate relief for increasing operating or gas costs from regulatory authorities; (xiv) ability to raise debt or equity capital; (xv) impact of terrorism; (xvi) volatility in actuarially determined benefit costs; (xvii) impact of natural disasters (such as hurricanes) on production and distribution facilities and the related effect on supply availability and price; and (xviii) new accounting standards issued by the Financial Accounting Standards Board, which could change the accounting treatment for certain transactions. All of these factors are difficult to predict and many are beyond the Company s control. Accordingly, while the Company believes its forward-looking statements to be reasonable, there can be no assurance that they will approximate actual experience or that the expectations derived from them will be realized. When used in the Company s documents or news releases, the words, anticipate, believe, intend, plan, estimate, expect, objective, projection, forecast , budget or similar words or future or conditional verbs such as will, would, should, could or may identify forward-looking statements.

Forward-looking statements reflect the Company s current expectations only as of the date they are made. The Company assumes no duty to update these statements should expectations change or actual results differ from current expectations except as required by applicable laws and regulations.

The three-month and nine-month earnings presented herein should not be considered as reflective of the Company s consolidated financial results for the fiscal year ending September 30, 2007.

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The total revenues and margins realized during the first nine months reflect higher billings due to the weather sensitive nature of the gas business. Improvement or decline in earnings for the balance of the year will depend primarily on the level of operating and maintenance costs and, to a lesser extent, weather.

Overview

Resources is an energy services company primarily engaged in the regulated sale and distribution of natural gas to approximately 60,200 residential, commercial and industrial customers in Roanoke, Virginia and Bluefield, Virginia and West Virginia and the surrounding areas through its Roanoke Gas Company (Roanoke Gas) and Bluefield Gas Company (Bluefield Gas) subsidiaries. Natural gas service is provided at rates and for the terms and conditions set forth by the State Corporation Commission (SCC) in Virginia and the Public Service Commission (PSC) in West Virginia.

On February 16, 2007, Resources entered into a Purchase and Sale Agreement with ANGD for the sale of all of the capital stock of Bluefield Gas to ANGD and Roanoke Gas entered into an Asset Purchase and Sale Agreement with Appalachian Natural Gas Distribution Company (Appalachian) for the sale of Roanoke s natural gas distribution assets located in the Town of Bluefield and the County of Tazewell, Virginia, (Bluefield division of Roanoke Gas Company) to Appalachian, which is a wholly owned subsidiary of ANGD. Resources management believes that both of these agreements will be approved by the respective commissions and the sale will be completed. As such, these two operations have been reclassified as discontinued operations. See Discontinued Operations section below and Note 5 for more information on these transactions.

Resources also provides certain unregulated natural gas related services through Roanoke Gas Company and information system services to software providers in the utility industry through RGC Ventures, Inc. of Virginia, which operates as Application Resources. Such operations represent less than one percent of total revenues and income of Resources.

Winter weather conditions and volatility in natural gas prices both have a direct influence on the quantity of natural gas sales to the Company s customers and management believes each factor has the potential to significantly impact earnings. A majority of natural gas sales are for space heating during the winter season. Consequently, during warmer than normal winters, customers may significantly reduce their purchase of natural gas. Furthermore, rising natural gas commodity prices could also affect customer usage through conservation or use of alternative fuels.

Because the SCC authorizes billing rates for the natural gas operations based upon normal weather, warmer than normal weather may result in the Company failing to earn its authorized rate of return. The Company has been able to mitigate a portion of the risk associated with warmer than normal winter weather by the inclusion of a weather normalization adjustment

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(WNA) factor as part of Roanoke Gas rate structure, which allows the company to recover revenues equivalent to the margin that would be realized at approximately 6 percent warmer than the 30-year normal. The Company recorded approximately $439,000 in additional revenues for the nine-month period ended June 30, 2007. In the prior fiscal year, the Company recorded approximately $316,000 in additional revenues for the nine-month period ended June 30, 2006.

Management also has concerns regarding the volatility of natural gas prices and the potential for reduced sales in response to increasing prices. Rising natural gas prices may influence the level of sales due to conservation efforts by customers or may result in customers switching to an alternative fuel. In addition, increasing prices may lead to a higher level of bad debts due to customers inability to afford the higher prices. After natural gas prices spiked in December 2005 following the impact of hurricanes on natural gas supplies and prices, the Company experienced reduced consumption in the following two quarters by customers in what appeared to be a response to the high energy prices. Based on the level of sales for the current year, the Company believes that much of the conservation it encountered last year has declined and natural gas consumption has returned to its prior trends as natural gas prices have stabilized. Although natural gas production facilities and pipelines are better prepared for the impact of severe weather in the Gulf of Mexico, the forecast of a more active 2007 hurricane season still is a cause for concern regarding the potential impact on natural gas production and prices if another hurricane entered the Gulf of Mexico and caused significant damage to natural gas production facilities.

Results of Operations

Consolidated net income (loss) from continuing and discontinued operations is as follows:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2007	**2006**	**2007**	**2006**
Net Income				
Continuing Operations	$ 236,520	$ 26,127	$ 4,034,208	$ 3,055,292
Discontinued Operations	120,414	(83,086)	600,945	497,005
Net Income (Loss)	$ 356,934	$ (56,959)	$ 4,635,153	$ 3,552,297

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Continuing Operations

Three Months Ended June 30, 2007:

The table below reflects volume activity and heating degree-days.

	Three Months Ended June 30,		Increase/	
	2007	2006	(Decrease)	Percentage
Delivered Volumes				
Regulated Natural Gas (DTH)				
Tariff Sales	995,678	861,186	134,492	16%
Transportation	623,258	652,665	(29,407)	-5%
Total	1,618,936	1,513,851	105,085	7%
Heating Degree Days (Unofficial)	384	279	105	38%

The table below reflects operating revenues.

	Three Months Ended June 30,		Increase/	
	2007	2006	(Decrease)	Percentage
Operating Revenues				
Gas Utilities	$ 15,001,023	$ 11,258,506	$ 3,742,517	33%
Other	130,352	236,542	(106,190)	-45%
Total Operating Revenues	$ 15,131,375	$ 11,495,048	$ 3,636,327	32%

Total operating revenues from continuing operations for the three months ended June 30, 2007 compared to the same period last year increased due to higher natural gas commodity prices, increased sales volumes due to a colder spring and the implementation of a non-gas cost rate increase in October. The total average unit cost of natural gas for the quarter increased by more than 26 percent compared to the same period last year. Total regulated natural gas delivered volumes increased by 7 percent as the total number of heating degree-days increased by 105, or 38 percent, from the same period last year. Other revenues declined due to the services provided under the Company s master meter services program last year.

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	Three Months Ended June 30,		Increase/	
	2007	2006	(Decrease)	Percentage
Gross Margin				
Gas Utilities	$ 4,868,437	$ 4,337,655	$ 530,782	12%
Other	78,841	49,809	29,032	58%
Total Gross Margin	$ 4,947,278	$ 4,387,464	$ 559,814	13%

Regulated natural gas margins from gas utilities increased due to a 7 percent increase in total delivered natural gas volumes (both tariff and transporting) and the implementation of a non-gas cost rate increase. The increase in firm sales resulted from an increase in heating degree-days and a partial lessening of customer conservation efforts begun in 2006 in response to the high energy prices and high customer bills incurred in the first quarter of fiscal 2006. Total heating degree-days increased by 38 percent while total tariff volumes (most of which are weather dependent) increased by 16 percent. The relationship between heating degree-days and sales volumes is not high during the spring months as it is during the winter months due to the much greater proportion of base load volumes (non weather sensitive sales) to total volumes in the spring and summer as compared to the winter months. In addition, Roanoke placed increased rates into effect during the first quarter. Roanoke s rates were placed into effect subject to refund pending a final order from the Virginia SCC. See Regulatory Affairs section for more information regarding the rate award. As a result of these rate awards and the increase in total natural gas deliveries, the Company realized approximately $127,000 in additional margin from customer base charges, which is a flat monthly fee billed to each natural gas customer, and approximately $431,000 associated with increase in the volumetric margin of natural gas. Carrying cost revenues, as explained below, decreased by approximately $45,000 due to lower average investment in natural gas storage during the period. The components of the gas utility margin increase are summarized below:

Net Margin Increase

Customer Base Charge including rate increase	$ 127,418
WNA	22,862
Carrying Cost	(44,920)
Volumetric (rate and volume increase)	430,539
Other	(5,117)
Total	$ 530,782

Roanoke had an approved rate structure in place during the quarter that allowed it to accrue revenue to cover the financing costs related to the level of investment in natural gas inventory.

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During times of rising gas costs and rising inventory levels, Roanoke recognizes revenues to offset the higher financing costs. Conversely, Roanoke passes along savings to customers during times of declining gas costs and lower inventories. Other margins increased over last year primarily due to billings related to temporary work performed in the unregulated operations of Roanoke Gas.

Operations expenses increased by $123,538, or 5 percent, compared to the same period last year. Increases in operations labor and contractor expenses combined with lower capitalized overheads more than offset reductions in bad debt expense and employee benefit costs. Operations labor and contractor expenses increased by $320,000 due to a focus on various operations tasks including the timing of distribution pipeline leak survey work, salary increases, network support functions and performance accruals. The Company also reduced the level of capital activity resulting in a $51,000 reduction of capitalized overheads. Bad debt expense declined by $119,000 due to strong collection efforts and improved aging due to the warm heating season and stable energy prices. Employee benefit expenses decreased due to a $70,000 reduction in pension and other post employment benefit costs attributable to an increase in the discount rate used to determine the actuarial expense for the current year. The balance of the difference is attributable to small reductions in other expenses. Maintenance expenses increased $48,246, or 16 percent, from the same period last year. The increase in maintenance primarily relates to timing of repairs of pipeline leaks in the Company s distribution system determined through leak surveys.

General taxes increased by $13,923, or 5 percent, due to higher payroll and property taxes. Depreciation expense increased $66,720, or 7 percent, on a corresponding increase in utility plant associated with extending service to new customers and replacing cast iron and bare steel pipe. Other income, net increased by $30,032 due to a higher level of investment earnings.

Interest expense increased by $10,286, or 2 percent, primarily due to increased level of customer deposits and a higher deposit interest rate as annually reset by the SCC. Declines in borrowings under the Company s line-of-credit arrangements offset the impact of higher interest rates on the variable rate debt. The overall average borrowing requirements for the quarter were nearly unchanged from the same period last year, declining by $80,000, while the effective average interest rate on the Company s line-of-credit increased from 5.6 percent last year to 6.0 percent for the current period.

Income tax expense increased by $116,740, which corresponds to the increase in pre-tax income on continuing operations for the quarter.

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Nine Months Ended June 30, 2007:

The table below reflects volume activity and heating degree-days.

	Nine Months Ended June 30,		Increase/	
	2007	2006	(Decrease)	Percentage
Delivered Volumes				
Regulated Natural Gas (DTH)				
Tariff Sales	6,242,356	6,052,889	189,467	3%
Transportation	2,148,347	2,227,196	(78,849)	-4%
Total	8,390,703	8,280,085	110,618	1%
Heating Degree Days (Unofficial)	3,714	3,649	65	2%

The table below reflects operating revenues.

	Nine Months Ended June 30,		Increase/	
	2007	2006	(Decrease)	Percentage
Operating Revenues				
Gas Utilities	$ 78,648,958	$ 82,856,760	$ (4,207,802)	-5%
Other	472,174	510,841	(38,667)	-8%
Total Operating Revenues	$ 79,121,132	$ 83,367,601	$ (4,246,469)	-5%

Total operating revenues from continuing operations for the nine months ended June 30, 2007 compared to the same period last year decreased due to lower gas costs in the first quarter, partially offset by the implementation of non-gas cost rate increases and higher level of natural gas sales. Although total tariff sales of the gas utilities increased slightly by 3 percent, the average unit cost of natural gas delivered to customers decreased for the period by 12 percent as energy prices spiked in December 2005 due to the combination of cold weather and production issues in the Gulf of Mexico attributable to damage caused by hurricanes in 2005. Other revenues decreased by 8 percent due to the reduction in services provided under the Company s master meter services program last year.

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	Nine Months Ended June 30,		Increase/	
	2007	2006	(Decrease)	Percentage
Gross Margin				
Gas Utilities	$ 20,484,455	$ 18,772,222	$ 1,712,233	9%
Other	246,373	212,402	33,971	16%
Total Gross Margin	$ 20,730,828	$ 18,984,624	$ 1,746,204	9%

Regulated natural gas margins increased even though total delivered volume (tariff and transporting) remained virtually unchanged from last year s volumes. A majority of the increase is attributable to the implementation of non-gas cost rate increases and to a much lesser extent, a 3 percent increase in the higher margin tariff sales and a greater level of WNA revenues. The components of the regulated margin increase are summarized below:

Net Margin Increase	
Customer Base Charge including rate increase	$ 360,346
WNA	122,882
Carrying Cost	(75,808)
Volumetric (rate and volume increase)	1,312,671
Other	(7,858)
Total	$ 1,712,233

Operations expenses increased by $132,473, or 2 percent, for the nine-month period ended June 30, 2007 compared to the same period last year. Increases in audit fees, contracted services and operations labor more than offset reductions in bad debt expense and employee benefit expenses. Audit fees increased by $54,000 primarily due to timing of internal audit services and additional fees associated with the Company s prior auditors providing their consent to the fiscal 2006 year end financial statements. Contract services and labor increased approximately $525,000 related to timing of distribution pipeline leak surveys, network support services, other operations projects, salary increases and performance accruals. Bad debt expense declined by $252,000 due to strong collection efforts and improved aging due to the warm heating season and lower energy prices. Employee benefit expenses decreased by $234,000 due to reductions in pension and other post employment benefit costs. Maintenance expenses remained consistent with the same period last year, decreasing by $5,440, or 1 percent.

General taxes remained nearly unchanged for the nine-month period ended June 30, 2007 compared to the same period last year. Increases in property taxes offset reductions in payroll taxes resulting in a net increase in general taxes of $3,148, or less than 1 percent change.

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Depreciation expense increased $183,725, or 6 percent, due to the growth in utility plant associated with extending service to new customers and replacing cast iron and bare steel pipe. Other income, net, increased $44,788 due to a higher level of investment earnings associated with reduced borrowing requirements during the spring and early summer.

Interest expense decreased by $81,512, or 5 percent, as significant reductions in borrowings under the Company s line-of-credit agreements more than offset the impact of higher interest rates on variable rate debt. The combination of lower natural gas inventories, higher customer credit balances under the budget payment program and improved earnings all contributed to reducing the overall average borrowing requirements for the quarter by nearly $3,700,000, while the effective average interest rate on the Company s line-of-credit increased from 4.9 percent last year to 5.8 percent for the current period. The lower borrowing levels and the corresponding reduction in interest expense experienced by the Company are the result of a combination of multiple factors as discussed above. The continuation of these factors in future periods is not expected, and the Company anticipates borrowings under its line-of-credit agreements will return to higher levels next year.

Income tax expense increased $579,682, or 31 percent, which corresponds to the rise in pre-tax income on continuing operations. The effective tax rate was 38.0 percent compared to 38.2 percent for the same period last year.

Discontinued Operations

As discussed in Note 5 of the financial statements, Resources entered into a Purchase and Sale Agreement with ANGD for the sale of all of the capital stock of Bluefield Gas to ANGD and Roanoke Gas entered into an Asset Purchase and Sale Agreement with Appalachian Natural Gas Distribution Company (Appalachian) for the sale of Roanoke Gas natural gas distribution assets located in the Town of Bluefield and the County of Tazewell, Virginia, (Bluefield division of Roanoke Gas Company) to Appalachian, which is a wholly owned subsidiary of ANGD. All of the 3,500 customers of Bluefield Gas and 1,100 Bluefield division of Roanoke Gas customers are represented by these sale agreements. The sales price of the Virginia assets will be equal to the book value of net plant plus 1% plus the book value of accounts receivable, natural gas inventory, and certain other listed current assets, subject to mutually agreed upon or arbitrated purchase price adjustments determined subsequent to the closing date but no later than 230 days after closing. $1,300,000 of such sale price is payable in the form of a subordinated promissory note from ANGD with a 5-year term and a 15-year amortization schedule with annual principal payments and quarterly interest payments at a 10% interest rate. Estimated net proceeds from both agreements will be approximately $5,200,000 less the $1,300,000 promissory note received. The Company anticipates using the proceeds from both sales to reduce debt and provide additional capital investment for Roanoke Gas.

The Board of Directors approved the Purchase and Sale Agreements of Bluefield Gas and the Bluefield division of Roanoke Gas for several reasons. The management time and effort

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required to oversee operations in West Virginia are significantly disproportionate to the size of the operation. The regulatory environment in West Virginia hindered the Company s ability to recover increasing expenses on a timely basis resulting in net losses from those operations in each of the last four fiscal years. The economic conditions in southern West Virginia have lead to a loss of population and gas customers in our West Virginia service area. Management believes that the net proceeds realized from these transactions can be reinvested in the Roanoke Gas operations and ultimately provide a better return for the Company than could be realized in the Bluefield Gas operations.

The transactions contemplated by the purchase agreements require the approval of the respective regulatory commissions: the West Virginia Public Service Commission for the sale of Bluefield Gas and the Virginia State Corporation Commission for the sale of the assets of the Bluefield Division of Roanoke Gas Company. Furthermore, the closing of each of the purchase agreements is conditioned upon such approval of the other transaction. Each of the purchase agreements provides at closing for a services agreement to be executed whereby Resources and Roanoke Gas will provide certain customer billing, gas control, regulatory and administrative services for Bluefield Gas and Appalachian on mutually agreeable terms. The length of time this services agreement will be in place will be dependent on the time it takes Bluefield Gas and Appalachian to assume these processes in their own operations; however, management expects most of the services to be fully assumed within one year of closing.

If both commissions approve the proposed transaction and the agreements are executed, the sale of Bluefield Gas and the Bluefield Division of Roanoke Gas could result in lower earnings for Resources in the near term. Even though the combined annual losses for both of these operations were approximately $142,000 and $195,000 for the fiscal years ended September 30, 2006 and 2005, these operations also included $729,000 and $683,000, respectively, in allocated costs from Resources and Roanoke Gas that will be retained by the Company. A portion of these retained costs will be recovered under the services agreement with ANGD discussed above. In addition, the promissory note from ANGD will generate interest income, and the Company expects to reinvest the approximately $2,000,000 of net proceeds from the sale of Bluefield Gas stock into Roanoke Gas to be used to reduce company debt and interest expense. In Roanoke Gas next non-gas cost rate filing, the Company will file for a return on the $2,000,000 equity investment resulting from the Bluefield sale as well as for recovery of the balance of those costs retained by the Company after the sale, net of any service agreement revenue. Under this scenario, operating results could improve by more than $200,000 as Bluefield s net loss would be replaced by a return on the $2,000,000 equity investment into Roanoke. Based on the most recent rate filing, the Company could earn a 10 percent return on this equity investment.

In July 2006, the Company entered into an asset purchase and sale agreement for the sale of the assets relating to its Highland Energy gas marketing business. The assets sold included the gas supply contracts between Highland Energy and its customers and related business records. The operations associated with the energy marketing business were reclassified as Discontinued Operations in accordance with the provisions of SFAS No. 144. Under the agreement, a portion of the sales price was deferred as realization of those revenues was subject to certain provisions.

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As these provisions had been met as of June 30, 2007, the Company recorded $160,000 revenue as part of discontinued operations in final settlement of the sales contract. The Company expects to receive payment in August 2007.

Critical Accounting Policies

The consolidated financial statements of Resources are prepared in accordance with accounting principles generally accepted in the United States of America. The amounts of assets, liabilities, revenues and expenses reported in the Company s financial statements are affected by accounting policies, estimates and judgments that are necessary to comply with generally accepted accounting principles. Estimates used in the financial statements are derived from prior experience, statistical analysis and professional judgments. Actual results could differ from the estimates, which would affect the related amounts reported in the Company s financial statements. The following policies and estimates are important to understanding certain key components of the financial statements.

Revenue recognition Regulated utility sales and transportation revenues are based upon rates approved by the SCC for Roanoke and the PSC for Bluefield. The non-gas cost component of rates may not be changed without a formal rate increase application and corresponding authorization by the appropriate regulatory commission; however, the gas cost component of rates may be adjusted periodically through the PGA mechanism with approval from the respective commission. Roanoke also utilizes a WNA, which is designed to partially offset the impact of weather that is either more than approximately 6 percent warmer than normal or approximately 6 percent colder than normal over a 12 month period. The calculation of the WNA requires the use of estimates. Without the WNA, the Company s operating revenues and gross margins would have been reduced by approximately $439,000 and $316,000 for the nine-month periods ended June 30, 2007 and 2006, respectively.

The Company bills its regulated natural gas customers on a monthly cycle. The billing cycle periods for most customers do not coincide with the accounting periods used for financial reporting. The Company accrues estimated revenue for natural gas delivered to customers not yet billed during the accounting period. Determination of unbilled revenue relies on the use of estimates and current and historical data. The financial statements included unbilled revenues of $1,278,635 and $1,462,878 at June 30, 2007 and September 30, 2006, respectively. Roanoke also accrues a provision for rate refund during periods in which it has implemented new billing rates pending the results of a final review and hearing on the increases by the SCC. The Company s estimated refund provision is based upon historical experience, discussions with the SCC and other relevant factors.

Bad debt reserves The Company evaluates the collectibility of its accounts receivable balances based upon a variety of factors including loss history, level of delinquent account balances and general economic climate.

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Retirement plans The Company offers a defined benefit pension plan (pension plan) and a postretirement medical and life insurance plan (postretirement plan) to eligible employees. The expenses and liabilities associated with these plans are determined through actuarial means requiring the use of estimates and assumptions. In regard to the pension plan, these factors include assumptions regarding discount rate, expected long-term rate of return on plan assets, compensation increases and life expectancies, among others. Similarly, the postretirement plan also requires the estimation of many of the same factors as the pension plan in addition to assumptions regarding rate of medical inflation and Medicare availability. Actual results may differ materially from the results expected from the actuarial assumptions due to changing economic conditions, volatility in interest rates and changes in life expectancy. Such differences may result in a material impact on the amount of expense recorded in future periods or the value of the obligations on the balance sheet.

Derivatives As discussed in the Item 3 - Qualitative and Quantitative Disclosures about Market Risk section below, the Company may hedge certain risks incurred in the normal operation of business through the use of derivative instruments. The Company applies the requirements of Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities,* which requires the recognition of all derivative instruments as assets or liabilities in the Company s balance sheet at fair value. In most instances, fair value is based upon quoted futures prices for the natural gas commodities and interest rate futures for interest rate swaps. Changes in the commodity and futures markets will impact the estimates of fair value in the future. Furthermore, the actual market value at the point of realization of the derivative may be significantly different from the values used in determining fair value in prior financial statements.

Regulatory accounting The Company s regulated operations follow the accounting and reporting requirements of Statement of Financial Accounting Standards No. 71, *Accounting for the Effects of Certain Types of Regulation.* The economic effects of regulation can result in a regulated company deferring costs that have been or are expected to be recovered from customers in a period different from the period in which the costs would be charged to expense by an unregulated enterprise. When this results, costs are deferred as assets in the consolidated balance sheet (regulatory assets) and recorded as expenses when such amounts are reflected in rates. Additionally, regulators can impose liabilities upon a regulated company for the amounts previously collected from customers and for current collection in rates of costs that are expected to be incurred in the future (regulatory liabilities).

If any portion of the current regulated operations ceases to meet the criteria for application of the provisions of SFAS No. 71, the Company would remove the corresponding regulatory assets or liabilities from the consolidated balance sheets and reflect them within the consolidated statement of income for the period in which the discontinuance occurred.

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Asset Management

Both Roanoke and Bluefield use a third party as an asset manager to manage their pipeline transportation and storage rights and gas supply inventories and deliveries. In return for being able to utilize the excess capacities of the transportation and storage rights, the third party pays both Roanoke and Bluefield a monthly utilization fee, which is used to reduce the cost of gas for their customers. The current agreements expire October 31, 2007. The Company is currently in the process of reviewing proposals for a new three-year asset management agreement to begin in November 2007.

Energy Costs

Natural gas prices were relatively stable with commodity prices between $7.50 and $8.00 per decatherm for much of the quarter. Prices dropped near the end of the quarter with the NYMEX (New York Mercantile Exchange) closing price at June 30, 2007 under $7.00 a decatherm with prices falling to below $6.00 a decatherm in July. The lack of tropical storm and hurricane activity has been a contributing factor for the reduction in natural gas prices. However, the forecast for 2007 continues to predict a very active hurricane season with an above-average number of hurricanes to develop in the Atlantic. If these predictions prove accurate and if a hurricane makes its way into the Gulf of Mexico and strikes natural gas production facilities, natural gas prices could again experience sharp increases similar to the price spikes that occurred in late 2005.

Management believes that it has planned for adequate supplies to fulfill projected customer needs. In addition, the Company uses various hedging mechanisms, including summer storage injections and financial instruments, to mitigate volatility in energy prices. Prudently incurred natural gas costs are fully recoverable under the present regulatory Purchased Gas Adjustment (PGA) mechanisms, and increases and decreases in the cost of gas are passed through to the Company s customers. Although rising energy prices are recoverable through the PGA mechanism for the regulated operations, high energy prices may have a negative impact on earnings through increases in bad debt expense and higher interest costs because the delay in recovering higher gas costs requires borrowing to temporarily fund receivables from customers. The Company s rate structure provides a level of protection against the impact that rising energy prices may have on bad debts and carrying costs of gas in storage by allowing for more timely recovery of these costs. However, the rate structure will not protect the Company from increased rate of bad debts or increases in interest rates.

Regulatory Affairs

On September 14, 2006, Roanoke filed an application with the Virginia SCC for an expedited increase in non-gas rates to provide approximately $1,750,000 in additional revenues. The requested rates were placed into effect on October 23, 2006 subject to refund for any differences between the implemented rates and the final rates approved by the SCC. In March 2007,

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Roanoke reached a stipulated agreement with the SCC staff for a rate award of $1,667,940. In April 2007, Roanoke received the final rate order approving the stipulated agreement. In June 2007, the Company completed the refunding of approximately $53,000 in billings and interest for billings in excess of the final approved rates.

On January 4, 2007, Bluefield filed a new rate application with the PSC for an increase in non-gas rates of approximately $456,000. On February 20, 2007, Bluefield Gas and ANGD filed a Joint Petition for Consent and Approval of the Purchase of the Common Stock of Bluefield Gas Company (Joint Petition) requesting the PSC s consent and approval of the sale of Bluefield Gas stock. On May 10, 2007, the Administrative Law Judge issued a Procedural Order consolidating the cases and establishing a public comment hearing on June 26, 2007 and an evidentiary hearing on July 6, 2007. Prior to the public comment hearing, representatives from Bluefield Gas, ANGD, PSC staff, City of Bluefield and the Consumer Advocate Division of West Virginia (CAD) met to discuss settlement negotiations for the combined case. On July 6, 2007, the evidentiary hearing was held in Bluefield and a Stipulation dated July 6, 2007 was submitted and signed by representatives of Bluefield Gas, ANGD, PSC staff and the CAD and set forth several conditions for the sale. The Stipulation provided for a non-gas rate increase providing for additional annual revenues of $323,853 if the sale is not approved and a non-gas rate increase providing for additional annual revenues of $176,242 if the sale is approved. The increased rates would be effective for service rendered on or after November 1, 2007. The Administrative Law Judge s report is due September 18, 2007.

Simultaneous with the Bluefield Gas filing on February 20, 2007, Roanoke Gas and Appalachian filed a request with the SCC for approval of the transfer of certain assets located in Bluefield, Virginia. The only other party to this proceeding was the SCC; and, on July 23, 2007, the SCC staff issued a report supporting the transfer of those assets. A final decision from the SCC is expected in early fall.

Capital Resources and Liquidity

Due to the capital intensive nature of Resources utility business, as well as the related weather sensitivity, Resources primary capital needs are the funding of its continuing construction program and the seasonal funding of its natural gas inventories and accounts receivable. The Company s construction program is composed of a combination of replacing aging bare steel and cast iron pipe with new plastic or coated steel pipe and expansion of its natural gas system to meet the demands of customer growth. Total capital expenditures from continuing operations were $4,557,706 and $5,109,452 for the nine-month periods ended June 30, 2007 and 2006, respectively. Roanoke Gas total capital budget for the current year is more than $5,500,000. It is anticipated that future capital expenditures will be funded with the combination of operating cash flow, sale of Company equity securities through the Dividend Reinvestment and Stock Purchase Plan and issuance of debt.

The level of borrowing under the Company s line-of-credit agreements can fluctuate significantly due to the time of the year, changes in the wholesale price of energy and weather

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outside the normal temperature ranges. As the wholesale price of natural gas increases, short-term debt generally increases because the payment to the Company s energy suppliers is due before the Company can recover its costs through the monthly billing of its customers. In addition, colder weather requires the Company to purchase greater volumes of natural gas, the cost of which is recovered from customers on a delayed basis. As discussed under the Results of Operations section above, several factors combined to reduce borrowings under the lines-of-credit below both expected and historical levels. The continuation of these reduced levels of borrowing is not expected, and borrowing levels should return to higher levels next winter.

On March 20, 2007, the Company renewed its line-of-credit agreements. The new agreements maintain the same variable interest rates based upon 30-day LIBOR and continue the multi-tier level for borrowing limits to accommodate the Company s seasonal borrowing demands. Effective with the execution of the new agreements, the Company s total available limits under the lines-of-credit including Bluefield Gas which will be terminated at closing are as follows:

Beginning	Total Available Line of Credit	Bluefield Gas Line of Credit	Continuing Operations
April 1, 2007	$ 10,000,000	$ 4,000,000	$ 6,000,000
July 16, 2007	15,000,000	4,000,000	11,000,000
September 16, 2007	23,000,000	6,000,000	17,000,000
November 16, 2007	27,000,000	6,000,000	21,000,000
February 16, 2008	22,000,000	6,000,000	16,000,000

These lines-of-credit expire March 31, 2008, unless extended. The Company anticipates being able to extend or replace the lines-of-credit upon expiration.

Stockholders equity increased by $3,720,934 for the nine months ended June 30, 2007, primarily due to earnings and proceeds from stock issued under the Dividend Reinvestment and Stock Purchase Plan (DRIP). The activity is summarized below:

Net income	$ 4,635,153
Dividends	(1,978,854)
DRIP	667,916
Restricted stock and stock options	130,912
Net comprehensive income	265,807
Increase in stockholders equity	$ 3,720,934

At June 30, 2007, the Company s consolidated long-term capitalization was 61 percent equity and 39 percent debt exclusive of Bluefield Gas $2,000,000 note classified as liabilities of assets available for sale.

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ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risks associated with interest rates and commodity prices. Interest rate risk is related to the Company s outstanding long-term and short-term debt. Commodity price risk is experienced by the Company s regulated natural gas operations and energy marketing business. The Company s risk management policy, as authorized by the Company s Board of Directors, allows management to enter into derivatives for the purpose of managing commodity and financial market risks of its business operations.

Interest Rate Risk

The Company is exposed to market risk related to changes in interest rates associated with its borrowing activities. At March 31, 2007, the Company had $88,000 outstanding under its lines of credit from continuing operations at a weighted-average interest rate of 6.02%. Included in the liabilities of assets available for sale are $1,723,000 in lines-of-credit balance and $2,000,000 outstanding on an intermediate-term variable-rate note for Bluefield Gas. A hypothetical 100 basis point increase in market interest rates applicable to the Company s variable rate debt would have resulted in an increase in the nine month interest expense from continuing operations of approximately $19,000. The impact on interest expense for the three month period ended June 30, 2007 would have been negligible. The Company also has a $15,000,000 intermediate term variable rate note that is currently being hedged by a fixed rate interest swap. The balance of the long-term debt is at fixed rates.

Commodity Price Risk

The Company manages the price risk associated with purchases of natural gas by using a combination of fixed price contracts, gas storage injections and derivative commodity instruments including futures, price caps, swaps and collars. During the quarter, the Company did not use or enter into any derivative arrangements for the purpose of hedging the price of natural gas. However, under the Company s regulated natural gas operations, any cost incurred or benefit received from the derivative arrangements is recoverable or refunded through the regulated natural gas purchased gas adjustment (PGA) mechanism. The SCC currently allows for full recovery of prudent costs associated with natural gas purchases, and any additional costs or benefits associated with the settlement of derivative contracts will be passed through to customers when realized. As of June 30, 2007, all natural gas derivative contracts had been settled.

ITEM 4 CONTROLS AND PROCEDURES

Based on their evaluation of the Company s disclosure controls and procedures (as defined by Rule 13a-15(e) under the Securities Exchange Act of 1934) as of June 30, 2007, the Company s Chief Executive Officer and principal financial officer have concluded that these disclosure controls and procedures are effective. Management routinely reviews the Company s internal controls over financial reporting and from time to time makes changes intended to enhance the effectiveness of internal controls over financial reporting. There has been no change

during the quarter ended June 30, 2007, in the Company s internal control over financial reporting or in other factors that has materially affected, or is reasonably likely to materially affect, this internal control over financial reporting.

Part II Other Information

ITEM 2 UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Pursuant to the RGC Resources Restricted Stock Plan for Outside Directors (the Restricted Stock Plan), 40% of the monthly retainer fee of each non-employee director of the Company is paid in shares of unregistered common stock and is subject to vesting and transferability restrictions (restricted stock). A participant can, subject to approval of Directors of the Company (the Board), elect to receive up to 100% of his retainer fee in restricted stock. The number of shares of restricted stock is calculated each month based on the closing sales price of the Company s common stock on the Nasdaq-NMS on the first day of the month. The shares of restricted stock are issued in reliance on Section 3(a)(11) and Section 4(2) exemptions under the Securities Act of 1933 (the Act) and will vest only in the case of the participant s death, disability, retirement or in the event of a change in control of the Company. Shares of restricted stock will be forfeited to the Company upon (i) the participant s voluntary resignation during his term on the Board or (ii) removal for cause. During the quarter ended June 30, 2007, the Company issued a total of 763.176 shares of restricted stock pursuant to the Restricted Stock Plan as follows:

Investment Date	**Price**	**Number of Shares**
4/2/2007	$ 28.000	251.637
5/1/2007	$ 28.010	251.548
6/1/2007	$ 27.100	259.991

On April 2, 2007, the Company issued a total of 2,250.000 shares of its common stock as bonuses to certain employees and management personnel as rewards for performance and service. The 2,250.000 shares were not issued in a transaction constituting a sale within the meaning of section 2(3) of the Act.

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ITEM 6 EXHIBITS

Number	**Description**
31.1	Rule 13a 14(a)/15d 14(a) Certification of Principal Executive Officer.
31.2	Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer.
32.1	Section 1350 Certification of Principal Executive Officer.
32.2	Section 1350 Certification of Principal Financial Officer.

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SIGNATURES

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

RGC Resources, Inc.

Date: August 10, 2007

By: /s/ Howard T. Lyon

Howard T. Lyon
Vice-President, Treasurer and Controller
(Principal Financial Officer)