RGC RESOURCES INC
Form 10-K
December 03, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended September 30, 2018
Commission file number 000-26591
RGC RESOURCES, INC.
(Exact name of registrant as specified in its charter)

Virginia	54-1909697
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

519 Kimball Avenue, N.E., Roanoke, VA 24016
(Address of principal executive offices) (Zip Code)
Registrant's telephone number, including area code (540) 777-4427
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, $5 Par Value	NASDAQ Global Market

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer as defined in Rule 405 of the Securities Act. Yes ¨ No x
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (Section 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See definition of "large accelerated filer", "accelerated filer", "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if smaller reporting company)	Smaller reporting company	x
		Emerging growth company	¨

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).   Yes ¨   No x

State the aggregate market value of the voting and non voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity as of the last business day of the registrant's most recently completed second fiscal quarter: March 31, 2018. $188,207,371

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

Class	Outstanding at November 23, 2018
COMMON STOCK, $5 PAR VALUE	8,003,606 SHARES

DOCUMENTS INCORPORATED BY REFERENCE:

Portions of the RGC Resources, Inc. Proxy Statement for the 2019 Annual Meeting of Shareholders are incorporated by reference into Part III hereof.

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Cautionary Note Regarding Forward Looking Statements

This report contains forward-looking statements that relate to future transactions, events or expectations. In addition, RGC Resources, Inc. (“Resources” or the “Company”) may announce or 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. These statements are based on management’s current expectations and information available at the time of such statements and are believed to be reasonable and are made in good faith. 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 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, but are not limited to those set forth in the following discussion and within Item 1A “Risk Factors” of this Annual Report on Form 10-K. 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,” “assu
similar words or future or conditional verbs such as “will,” “would,” “should,” “can,” “could” or “may” are intended to identif
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.

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PART I

Item 1. Business.

General and Historical Development
RGC Resources, Inc. ("Resources" or the "Company") was incorporated in the state of Virginia on July 31, 1998, for the primary purpose of becoming the holding company for Roanoke Gas Company (“Roanoke Gas”) and its subsidiaries. Effective July 1, 1999, Roanoke Gas and its subsidiaries were reorganized into the holding company structure. Resources is currently composed of the following subsidiaries: Roanoke Gas, Diversified Energy Company and RGC Midstream, LLC.

Roanoke Gas was organized as a public service corporation under the laws of the Commonwealth of Virginia in 1912. The principal service of Roanoke Gas is the distribution and sale of natural gas to residential, commercial and industrial customers within its service territory in Roanoke, Virginia and the surrounding localities. Roanoke Gas also provides certain non-regulated services which account for less than 2% of consolidated revenues.

In July 2015, the Company formed RGC Midstream, LLC, a limited liability company established for the purpose of becoming a 1% investor in Mountain Valley Pipeline, LLC (the "LLC"). Mountain Valley Pipeline, LLC was created for the purpose of constructing and operating interstate natural gas pipelines. Additional information regarding this investment is provided under Note 4 of the Company's annual consolidated financial statements and under the Equity Investment in Mountain Valley Pipeline section of Item 7.

Diversified Energy Company currently has no active operations.

Services
Roanoke Gas maintains an integrated natural gas distribution system to deliver natural gas purchased from suppliers to residential, commercial and industrial users in its service territory. The schedule below is a summary of customers, delivered volumes (expressed in decatherms), revenues and margin as a percentage of the total for each category. For the purposes of this schedule, margin for the utility operations is defined as revenues less cost of gas.

	2018							
	Customers		Volume		Revenue		Margin	
Residential	91.2	%	39	%	58	%	61	%
Commercial	8.7	%	32	%	33	%	25	%
Industrial	0.1	%	29	%	6	%	10	%
Other Utility	0.0	%	0	%	1	%	2	%
Other Non-Utility	0.0	%	0	%	2	%	2	%
Total Percent	100.0	%	100	%	100	%	100	%
Total Value	60,228		9,925,974		$65,534,736		$32,776,289	

	2017							
	Customers		Volume		Revenue		Margin	
Residential	91.2	%	37	%	57	%	61	%
Commercial	8.7	%	31	%	33	%	25	%
Industrial	0.1	%	32	%	7	%	10	%
Other Utility	0.0	%	0	%	1	%	2	%
Other Non-Utility	0.0	%	0	%	2	%	2	%
Total Percent	100.0	%	100	%	100	%	100	%
Total Value	59,847		8,562,582		$62,296,870		$32,809,157	

	2016			
	Customers	Volume	Revenue	Margin
Residential	91.2 %	38 %	57 %	60 %
Commercial	8.7 %	31 %	33 %	25 %
Industrial	0.1 %	31 %	7 %	11 %
Other Utility	0.0 %	0 %	1 %	2 %
Other Non-Utility	0.0 %	0 %	2 %	2 %
Total Percent	100.0 %	100 %	100 %	100 %
Total Value	59,635	8,842,605	$59,063,291	$31,564,914

Roanoke Gas' regulated natural gas distribution business accounted for approximately 98% of Resources total revenues for fiscal years ending September 30, 2018, 2017 and 2016. The tables above indicate that residential customers represent over 91% of the Company's customer total; however, they represent less than 40% of the total gas volumes delivered and more than half of the Company's consolidated revenues and margin. Industrial customers include primarily transportation customers that purchase their natural gas requirements directly from a supplier other than the Company and utilize Roanoke Gas' natural gas distribution system for delivery to their operations. Most of the revenue billed for these customers relates only to transportation service, and not to the purchase of natural gas, causing total revenues generated by these deliveries to be approximately 6% of total revenues, even though they represent 29% of total natural gas deliveries for the year ended September 30, 2018 and approximately 10% to 11% of margin for each of the years presented.

The Company's revenues are affected by changes in gas costs as well as by changes in consumption volume due to weather and economic conditions and changes in the non-gas portion of customer billing rates. Increases or decreases in the cost of natural gas are passed on to customers through the purchased gas adjustment mechanism as explained in Note 1 of the Company's annual consolidated financial statements.

The Company's residential and commercial sales are seasonal and temperature-sensitive as the majority of the gas sold by Roanoke Gas to these customers is used for heating. For the fiscal year ended September 30, 2018, approximately 66% of the Company's total DTH of natural gas deliveries and 74% of the residential and commercial deliveries were made in the five-month period of November through March. These percentages are higher than in the prior two years as colder weather led to increased consumption by weather sensitive customers. Total natural gas deliveries were 9.9 million DTH, 8.6 million DTH and 8.8 million DTH in fiscal 2018, 2017 and 2016, respectively.

Suppliers

Roanoke Gas relies on multiple interstate pipelines including those operated by Columbia Gas Transmission Corporation, LLC and Columbia Gulf Transmission Corporation, LLC (together "Columbia"), and East Tennessee Natural Gas, LLC ("East Tennessee"), Tennessee Gas Pipeline, Midwestern Gas Transmission Company and Saltville Gas Storage Company, LLC to transport natural gas from the production and storage fields to Roanoke Gas' distribution system. Roanoke Gas is directly served by two pipelines, Columbia and East Tennessee. Columbia historically has delivered more than 60% of the Company's gas supply, while East Tennessee delivers the balance of the Company's requirements. The rates paid for natural gas transportation and storage services purchased from the interstate pipeline companies are established by tariffs approved by the Federal Energy Regulatory Commission ("FERC"). These tariffs contain flexible pricing provisions, which, in some instances, authorize these transporters to reduce rates and charges to meet price competition. The current pipeline contracts expire at various times from 2019 to 2027. The Company anticipates being able to renew these contracts or enter into other contracts to meet customers' continued demand for natural gas.

The Company manages its pipeline contracts and liquefied natural gas storage ("LNG") facility in order to provide for sufficient capacity to meet the natural gas demands of its customers. The maximum daily winter capacity available for delivery into Roanoke Gas' distribution system under the interstate pipelines is 78,606 DTH per day. The LNG facility is capable of storing up to 200,000 DTH of natural gas in a liquid state for use during peak demand. Combined, the pipelines and LNG facility may provide up to 105,000 DTH on a single winter day.

The Company uses multi-year contracts to meet its natural gas supply needs. The Company currently contracts with Sequent Energy Management, L.P. to manage its pipeline transportation, storage rights, gas supply inventories and deliveries and serve as the primary supplier of natural gas for Roanoke Gas. Natural gas purchased under the asset management agreement is priced at indexed-based market prices as reported in major industry pricing publications. The Company renewed its contract with the asset manager in March 2018. The new agreement expires March 31, 2021.

The Company uses summer storage programs to supplement gas supply requirements during the winter months. During the summer months, the Company injects gas into its LNG facility. In addition, the Company has contracted for storage capacity from Columbia, Tennessee Gas Pipeline and Saltville Gas Storage Company, LLC for a combined total of more than 2.4 million DTH of storage capacity. The balance of the Company’s annual natural gas requirements are met primarily through market purchases made by its asset manager.

Competition
The Company’s natural gas utility operates in a regulated, monopolistic environment. Roanoke Gas currently holds the only franchises and/or certificates of public convenience and necessity ("CPCN") to distribute natural gas in its Virginia service areas. These franchises generally extend for multi-year periods and are renewable by the municipalities, including exclusive franchises in the cities of Roanoke and Salem and the Town of Vinton, Virginia. All three franchise agreements were recently renewed for a term of 20 years and will expire December 31, 2035. The Company has filed an application with the Virginia State Corporation Commission ("SCC") to obtain a CPCN for portions of Franklin County that are not currently certificated. A final decision is pending on this request. Roanoke Gas plans to tap into the Mountain Valley Pipeline and provide natural gas service to portions of Franklin County.

Management anticipates that the Company will be able to renew all of its franchises when they expire. There can be no assurance, however, that a given jurisdiction will not refuse to renew a franchise or will not, in connection with the renewal of a franchise, attempt to impose restrictions or conditions that could adversely affect the Company’s business operations or financial condition. CPCN, issued by the SCC, are generally of perpetual duration and subject to compliance with regulatory standards. If the SCC issues a CPCN for the currently uncertified sections of Franklin County, the CPCN would have a 5-year term if natural gas service was not extended into those areas.

Although Roanoke Gas has exclusive rights for the distribution of natural gas in its service area, the Company competes with suppliers of other forms of energy such as fuel oil, electricity, propane, coal and solar. Competition can be intense among the other energy sources with the primary driver being price in most instances. This is particularly true for those industrial applications that have the ability to switch to alternative fuels. The relationship between supply and demand has the greatest impact on the price of natural gas. Greater demand for natural gas for electric generation and other uses can provide upward pressure on the price of natural gas. Currently, a plentiful supply of natural gas, mostly due to improved drilling and extraction processes in shale formations, has served to maintain prices at lower levels. The Company continues to see a demand for its product. Construction activity for new business has improved over this past year and growth in residential service has remained steady over the last few years as the Company continues to grow its customer base through a combination of extending service by new construction and converting existing alternative energy source users to natural gas.

Regulation
In addition to the regulatory requirements generally applicable to all companies, Roanoke Gas is also subject to additional regulation at the federal, state and local levels. At the federal level, the Company is subject to pipeline safety regulations issued by the Department of Transportation and the Pipeline and Hazardous Materials Safety Administration.

At the state level, the SCC performs regulatory oversight including the approval of rates and other charges for natural gas sold to customers, the approval of agreements between or among affiliated companies involving the provision of goods and services, pipeline safety, and certain other corporate activities of the Company, including mergers and acquisitions related to utility operations.

At the local level, Roanoke Gas is further regulated by the municipalities and localities that grant franchises for the placement of gas distribution pipelines and the operation of gas distribution networks within their jurisdictions.

Employees

At September 30, 2018, Resources had 110 full-time employees and 112 total employees. As of that date, 32 employees, or 29%, belonged to the United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied-Industrial International Union, Local No. 515 and were represented under a collective bargaining agreement. The union has been in place at the Company since 1952. The current collective bargaining agreement will expire on July 31, 2020. Management maintains an amicable relationship with the union.

Website Access to Reports
The Company's website address is www.rgcresources.com. Information appearing on this website is not incorporated by reference in and is not a part of this annual report. The Company files reports with the Securities and Exchange Commission ("SEC"). A copy of this annual report, as well as other recent annual and quarterly reports are available on the Company's website. You may read and copy these filings with the SEC at the SEC public reference room at 100 F Street, NE, Washington, D.C. 20549. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding the Company's filings at www.sec.gov, which is hyper-linked on the Company's website where you may obtain other Company filings with the SEC.

Item 1A. Risk Factors

Please carefully consider the risks described below regarding the Company. These risks are not the only ones faced by the Company. Additional risks not presently known to the Company or that the Company currently believes are immaterial may also impair business operations and financial results. If any of the following risks actually occur, the Company's business, financial condition or results of operations could be adversely affected. In such case, the trading price of the Company's common stock could decline and investors could lose all or part of their investment. The risk factors below are categorized by operational, regulatory and financial:

OPERATIONAL RISKS

Availability of sufficient and reliable pipeline capacity.

The Company is currently served directly by two interstate pipelines. These two pipelines carry 100% of the natural gas transported to the Company's distribution system. Depending on weather conditions and the level of customer demand, failure of one or both of these interstate transmission pipelines could have a major impact on the Company's ability to meet customer demand for natural gas and adversely affect the Company's earnings as a result of lost revenue and the cost of service restoration. If the failure is frequent or prolonged, it could lead customers to switch to alternative energy sources. Capacity limitations on existing pipeline and storage infrastructure could impact the Company's ability to obtain additional natural gas supplies, thereby limiting the ability to meet customer demand and thus decreasing future earnings potential.

Risks associated with the operation of a natural gas distribution pipeline and LNG storage facility.

Numerous potential risks are inherent in the operation of a natural gas distribution system and LNG storage facility, including unanticipated or unforeseen events that are beyond the control of the Company. Examples of such events include adverse weather conditions, acts of terrorism or sabotage, accidents and damage caused by third parties, equipment failure, failure of upstream pipelines and storage facilities, as well as catastrophic events such as explosions, fires, earthquakes, floods, or other similar events. These risks could result in injury or loss of life, property damage, pollution and customer service disruption resulting in potentially significant financial losses. The Company maintains insurance coverage to protect against many of these risks. However, if losses result from an event that is not fully covered by insurance, the Company's financial condition could be significantly impacted if it were unable to recover such losses from customers through the regulatory rate making process. Even if the Company did not incur a direct financial loss as a result of any of the events noted above, it could encounter significant reputational damage from a reliability, safety, integrity or similar viewpoint, potentially resulting in a longer-term negative earnings impact.

Supply disruptions due to weather or other forces.

Hurricanes, floods and other natural or man-made disasters could damage or inhibit production and/or pipeline transportation facilities, which could result in decreased natural gas supplies. Decreased supplies could result in an inability to meet customer demand or lead to higher prices and/or service disruptions. Disasters could also lead to additional governmental regulations that may limit production activity and/or increase production and transportation costs.

Security incident or cyber-attacks on the Company’s computer or information technology systems.

The Company’s business operations and information technology systems may be vulnerable to an attack by individuals or organizations intending to disrupt the operations of the Company. Such an attack or cyber-security incident on the Company’s information technology systems could result in corruption of the Company’s financial information; the unauthorized release of confidential customer, employee or vendor information; the interruption of natural gas deliveries to our customers; or compromise the safety of our distribution, transmission and storage systems. The Company has implemented policies, procedures and controls to prevent and detect these activities; however, there are no guarantees that Company processes will adequately protect against unauthorized access. In the event of a successful attack, the Company could be exposed to material financial and reputational risks, possible disruptions in natural gas deliveries or a compromise of the safety of the natural gas distribution system, as well as be exposed to claims by persons harmed by such an attack. which could materially increase the Company's costs to protect against such risks.

General downturn in the economy or prolonged period of slow economic recovery.

A weak or poorly performing economy can negatively affect the Company’s profitability. An economic downturn can result in loss of commercial and industrial customers due to plant closings, a loss of residential customers as well as slow or declining growth in new customer additions, all of which would result in reduced sales volumes and lower revenues. An economic downturn could also result in rising unemployment and other factors that could lead to a loss of customers and an increase in customer delinquencies and bad debt expense.

Inability to attract and retain professional and technical employees.

The ability to implement the Company’s business strategy and serve customers is dependent upon employing talented professionals and attracting, training, developing and retaining a skilled workforce. As the Company will be facing retirements of key personnel over the next several years, the failure to replace those departing employees with skilled and qualified employees could increase operating costs and expose the Company to other operational and financial risks.

Geographic concentration of business activities.

The Company's business activities are concentrated in the Roanoke Valley. Changes in the local economy, politics, regulations and weather patterns could negatively impact the Company's existing customer base, leading to declining usage patterns and financial condition of customers, both of which could adversely affect earnings.

Volatility in the price and availability of natural gas.

Natural gas purchases represent the single largest expense of the Company. Even with increasing demand from other areas, including electricity generation, natural gas prices are currently expected to remain stable in the near term, although there can be no guarantee to that effect. If demand for natural gas increases at a rate in excess of current expectations, natural gas prices could face upward pressure. Increasing natural gas prices could result in declining sales as well as increases in bad debt expense.

Impact of weather conditions and related regulatory mechanisms.

The Company’s revenues and earnings are dependent upon weather conditions, specifically winter weather. The Company’s rate structure currently has a weather normalization adjustment factor that results in either a recovery or refund of revenues due to any variation from the 30-year average for heating degree-days. If the provision for the weather normalization adjustment were removed from its rate structure, the Company would be exposed to a much greater risk related to weather variability resulting in earnings volatility. A colder than normal winter could cause the Company to incur higher than normal operating and maintenance costs.

Inability to complete necessary or desirable pipeline expansion or infrastructure development projects.

In order to serve new customers or expand service to existing customers, the Company needs to install new pipeline and maintain, expand or upgrade its existing distribution, transmission and/or storage infrastructure. Various factors may prevent or delay the completion of such projects or make them more costly, such as the inability to obtain required approval from local, state and/or federal regulatory and governmental bodies, public opposition to the projects, inability to obtain adequate financing, competition for labor and materials, construction delays, cost overruns, and an inability to negotiate acceptable agreements relating to rights-of-way, construction or other material development components. As a result, the Company may not be able to adequately serve existing customers or expand its distribution system to support customer growth. This could include any potential customer growth or system reliability enhancement resulting from connection to the Mountain Valley Pipeline ("MVP"). Any of these factors could negatively impact earnings.

Competition from other energy providers.

The Company competes with other energy providers in its service territory, including those that provide electricity, propane, coal, fuel oil and solar. Price is a significant competitive factor. Higher natural gas costs or decreases in the price of other energy sources may enhance competition and encourage customers to convert their natural gas-fueled equipment to systems that use alternative energy sources, thus lowering natural gas deliveries and earnings. Price considerations could also inhibit customer and revenue growth if builders and developers do not perceive natural gas to be a better value than other energy options and elect to install heating systems that use an energy source other than natural gas.

Inability to renew or obtain new franchise agreements or certificates of public convenience

Roanoke Gas Company holds either franchises or certificates of public convenience (“CPC”) to provide natural gas to customers in its service territory. The franchises are granted by the local municipalities and the CPCs are granted by the State Corporation Commission of Virginia. The ability to renew such agreements is important to the long-term operations of the Company and the ability to obtain new franchises or CPCs is fundamental to expanding the Company’s service territory. Failure to renew these agreements could result in significant impact to future earnings and the inability to obtain new franchises or CPCs for new service areas could negatively impact future earnings growth.

REGULATORY RISKS

Increased compliance and pipeline safety requirements and fines.

The Company is committed to the safe and reliable delivery of natural gas to its customers. Working in concert with this commitment are numerous federal and state laws and regulations. Failure to comply with these laws and regulations could result in the levy of significant fines. There are inherent risks that may be beyond the Company’s control, including third party actions, which could result in damage to pipeline facilities, injury and even death. Such incidents could subject the Company to lawsuits, large fines, increased scrutiny and loss of customers, all of which could have a significant effect on the Company’s financial position and results of operations.

Environmental laws or regulations associated with global warming and climate change.

Several federal and state legislative and regulatory initiatives have been proposed in recent years in an attempt to limit the effects of global warming and climate change, including greenhouse gas emissions such as those created by the combustion of fossil fuels such as natural gas. Passage of new environmental legislation or implementation of regulations that mandate reductions in greenhouse gas emissions or other similar restrictions could have a negative effect on the Company’s core operations and its investment in the LLC. Such legislation could impose limitations on greenhouse gas emissions, require funding of new energy efficiency objectives, impose new operational requirements or lead to other additional costs to the Company. Regulations restricting or prohibiting the use of coal as a fuel for electric power generation has increased the demand for natural gas, and could at some point potentially result in natural gas supply concerns and higher costs for natural gas. Legislation or regulations could limit the exploration and development of natural gas reserves, making the price of natural gas less competitive and less attractive as a fuel source for consumers, resulting in reduced deliveries and earnings. The current Presidential administration is de-emphasizing climate change initiatives; however, future administrations might prioritize climate change and greenhouse gas emissions, which could lead to new and stricter environmental laws.

Regulatory actions or failure to obtain timely rate relief.

The Company’s natural gas distribution operations are regulated by the SCC. The SCC approves the rates that the Company charges its customers. If the SCC did not allow rates that provided for the timely recovery of costs or a reasonable rate of return on investment in natural gas distribution facilities, earnings could be negatively impacted. Issuance of debt and equity by our subsidiaries are also subject to SCC regulation and approval. Delays or lack of approvals could inhibit the ability to access capital markets and negatively impact liquidity or earnings.

FINANCIAL RISKS

Access to capital to maintain liquidity.

The Company relies on a variety of capital sources to operate its business and fund capital expenditures, including internally generated cash from operations, short-term borrowings under its line-of-credit, proceeds from the issuance of additional shares of its common stock and other sources. Access to a line-of-credit is essential to provide seasonal funding of natural gas operations and provide capital budget bridge financing. Access to capital markets and other long-term funding sources is important for capital outlays and funding of the LLC investment. The ability of the Company to maintain and renew its line-of-credit and to secure longer-term financing is critical to operations. Adverse market trends, market disruptions or deterioration in the financial condition of the Company could increase the cost of borrowing, restrict the Company's ability to issue additional shares of its common stock or otherwise limit the Company’s ability to secure adequate funding.

Investment in Mountain Valley Pipeline.

The success of the Company's investment in the LLC is predicated on several key factors including but not limited to the ability of all investors to meet their capital calls when due, timely state and federal approvals and completing the construction of the pipeline within the targeted time frame and budget. Any significant delay, cost over-run or the failure to receive the requisite approvals on a timely basis, or at all, could have a significant effect on the Company's earnings and financial position.

Although the LLC initially received the necessary federal and state permits to begin construction on the pipeline, progress on the MVP has been hindered by several legal and regulatory obstacles as both the U.S, Fourth Circuit Court of Appeals (“Fourth Circuit”) and FERC have issued stays or stop orders affecting portions or all of the project pending resolution of issues or concerns raised as the project has progressed. For example, in July 2018, the Fourth Circuit challenged the adequacy of alternative route evaluations for the permits issued by the US Forest Service and the Bureau of Land Management for the right-of-way granted for the 3.5 mile section of the 303 mile pipeline through the Jefferson National Forest. In August 2018, FERC issued a project wide stop work order related to the Fourth Circuit’s stay issued for the right-of-way in the National Forest. At the end of August, FERC issued a Modified Stop Work Order that allowed construction activities to restart in all locations except for the Jefferson National Forest and a section in West Virginia. The Fourth Circuit also lifted a stay order which had stopped construction through streams and wetland crossings in West Virginia thereby allowing construction to proceed in these areas. In October, the Fourth Circuit issued an order to vacate the stream and wetland crossing permit issued by the US. Army Corps of Engineers, which impacts approximately 160 miles of the project in West Virginia.

The LLC continues to respond to the issues and concerns raised. However, these ongoing starts and stops have caused delays in construction and resulted in significantly higher projected costs and an extended targeted in-service date for the pipeline. Cost overruns may not be approved for recovery or be recovered through regulatory mechanisms that may otherwise be available, and the LLC could be obligated to make delay or termination payments or responsible for other contractual damages. They could also experience the loss of tax credits or tax incentives, or delayed or diminished returns, and could be required to write-off all or a portion of its investment in the project. New or extended regulatory, legislative or judicial actions could lead to further delays and even higher costs all of which could significantly impact future returns for the LLC and ultimately impact Resources consolidated financial position and results of operation.

In addition, there are numerous risks facing the LLC, which can adversely affect the Company's earnings and financial performance through its 1% investment. The LLC's ability to obtain and keep contract crews to complete construction of the pipeline, the inability to obtain or renew ancillary licenses, rights-of-way, permits or other approvals and opposition from pipeline opponents and environmental groups could all influence the successful completion of the pipeline. Should the LLC be unable to adequately address these issues, the LLC’s business, financial condition, results of operations and prospects could be materially adversely affected, which could materially impact the financial condition and results of operations of the Company. Any failure to negotiate successful project development agreements for new facilities with third parties could have similar results.

Once in operation, the LLC’s gas infrastructure facilities and other facilities are subject to many operational risks. Operational risks could result in, among other things, lost revenues due to prolonged outages, increased expenses due to monetary penalties or fines for compliance failures, liability to third parties for property and personal injury damage, a failure to perform under applicable sales agreements and associated loss of revenues from terminated agreements or liability for liquidated damages under continuing agreements. The consequences of these risks could have a material adverse effect on the LLC’s business, financial condition, results of operations and prospects. Uncertainties and risks inherent in operating and maintaining the LLC's facilities include, but are not limited to, risks associated with facility start-up operations, such as whether the facility will achieve projected operating performance on schedule and otherwise as planned. The LLC’s business, financial condition, results of operations and prospects can be materially adversely affected by weather conditions, including, but not limited to, the impact of severe weather. Threats of terrorism and catastrophic events resulting from terrorism, cyber-attacks, or individuals and/or groups attempting to disrupt the LLC’s business, or the businesses of third parties, may materially adversely affect the LLC’s business, financial condition, results of operations and prospects.

Insurance coverage may not be sufficient.

The Company currently has liability and property insurance to cover a variety of exposures and perils. The insurance policies supporting said coverages are subject to certain limits and deductibles. Insurance coverage for risks against which the Company and its industry peers typically insure may not be offered in the future or such policies may expand exclusions that limit the amount of coverage or remove certain risks completely as insured events. Furthermore, litigation awards continue to increase and the limits of insurance may not keep pace accordingly. The proceeds received from any such insurance may not be paid in a timely manner. The occurrence of any of the foregoing could have a material adverse effect on the Company’s financial position, results of operations and cash flows.

Post-retirement benefits and related funding of obligations.

The costs of providing defined benefit pension and retiree medical plans are dependent on a number of factors such as the rates of return on plan assets, discount rates used in determining plan liabilities, the level of interest rates used to measure the required minimum funding levels of the plan, future government regulation, changes in life expectancy, and required or voluntary contributions made to the plan. Changes in actuarial assumptions and differences between the assumptions and actual results, as well as a significant decline in the value of investments that fund these plans, if not offset or mitigated by a decline in plan liabilities, could increase the expense of these plans and require significant additional funding. Both funding obligations and increased expense could have a material impact on the Company's financial position, results of operation and cash flows.

Failure to comply with debt covenant requirements.

The Company's long-term debt obligations and bank line of credit contain financial covenants. Noncompliance with any of these covenants could result in an event of default which, if not cured or waived, could accelerate payment on outstanding debt obligations or cause prepayment penalties. In such an event, the Company may not be able to refinance or repay all of its indebtedness, pay dividends or have sufficient liquidity to meet operating and capital expenditure requirements. Any such acceleration would cause a material adverse change in our financial condition.

Item 1B. Unresolved Staff Comments.

Not applicable.

Item 2. Properties.

Included in “Utility Property” on the Company’s consolidated balance sheet are storage plant, transmission plant, distribution plant and general plant of Roanoke Gas as categorized by natural gas utilities. The Company has approximately 1,141 miles of transmission and distribution pipeline with transmission and distribution plant representing more than 87% of the total utility plant investment. The transmission and distribution pipelines are located on or under public roads and highways or private property for which the Company has obtained the legal authorization and rights to operate.

Roanoke Gas currently owns and operates eight metering stations through which it measures and regulates the gas being delivered by its suppliers. These stations are located at various points throughout the Company's distribution system.

Roanoke Gas also owns a liquefied natural gas storage facility located in its service territory that has the capacity to store up to 200,000 DTH of natural gas.

The Company's executive, accounting and business offices, along with its maintenance and service departments, are located on Kimball Avenue in Roanoke, Virginia.

Although the Company considers its present properties to be adequate, management continues to evaluate the adequacy of its current facilities as additional needs arise.

Item 3. Legal Proceedings.

The Company is not known to be a party to any pending legal proceedings.

Item 4. Mine Safety Disclosures.

Not applicable.

PART II

Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market Information

Resources' common stock is listed on the NASDAQ Global Market under the trading symbol RGCO. Payment of dividends is within the discretion of the Board of Directors and depends on, among other factors, earnings, capital requirements, and the operating and financial condition of the Company.

	Range of Bid Prices			Cash Dividends
Year Ending September 30, 2018	High	Low		Declared
First Quarter	$31.57	$	25.01	$0.1550
Second Quarter	27.49	22.16		0.1550
Third Quarter	29.46	23.61		0.1550
Fourth Quarter	31.33	25.85		0.1550
Year Ending September 30, 2017				
First Quarter	$20.04	$	15.81	$0.1450
	$ 705,000	$ 149,000	$ 1,847,000	$ 149,000

Stock-based compensation consists of the fair value of shares issued to outside consultants for services provided. Professional fees consists primarily of legal, audit and accounting costs related to the Merger and public company compliance costs. Labor consists of compensation costs attributable to Ampio s administrative employees. The increase in expenses in 2010 relates to the increase in business activity as Ampio did not begin incurring operating expenses until April 2009.

Net Cash Used in Operating Activities

During the six months ended June 30, 2010, our operating activities used $1,250,000 of cash. The use of cash reflected a $2,628,000 net loss, a non-cash charge of $1,014,000 for stock based compensation, an increase in accounts payables of $278,000 relating to professional fees incurred in conjunction with the Merger and other expenses, an increase in accrued salaries of $123,000 resulting from deferral of salaries by our management team, and changes in other assets and current liabilities which provided net cash of $36,000.

Net Cash from Financing Activities

Net cash provided by our financing activities was $1,312,000 for the six months ended June 30, 2010. During this period, we received $200,000 in loans from shareholders and $1,367,000 from the sale and subscription of common stock. Immediately prior to the Merger, we made advances of $150,000 to stockholders. Pursuant to the terms of the Merger Agreement, we were also required to place $125,000 in restricted cash into an escrow account, $20,000 of which was released in June and $75,000 was released in July 2010. The remaining escrowed funds are to be released to us on closing of a Qualified Financing (as defined) during the escrow period, or will be released to the principal stockholders of Chay if we do not obtain such financing during the escrow period, subject to adjustment for any sales of our common stock made by the Chay principal stockholders.

Liquidity and Capital Resources

We had unrestricted cash of $131,000 at June 30, 2010, and an additional $75,000 was released from restricted cash subsequent to June 30, 2010. We raised approximately $1,500,000 in a private placement of common stock conducted from November 2009 to March, 2010 and are actively seeking to raise additional capital. As of June 30, 2010 we had $400,000 in notes payable to stockholders, which mature on the earlier of a minimum financing of $5,000,000 or September 2, 2010. During August 2010, stockholders loaned us an additional $430,000. The loans mature at the earlier of a minimum financing of $10,000,000 or January 31, 2011. Additional loans from our stockholders may be a source of short-term liquidity. However, there is currently no formal commitment from our stockholders to provide additional short-term financing. In order to execute on our business plan, it will be necessary for us to raise additional capital.

Off Balance Sheet Arrangements

We do not have off-balance sheet arrangements, financings, or other relationships with unconsolidated entities or other persons, also known as variable interest entities.

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Contractual Obligations

As condition of the Merger, Ampio and certain of its shareholders (the Guarantors) and the Chay Control Shareholders entered into a Securities Put and Guarantee Agreement, or the Put Agreement. The Put Agreement provides that if Ampio is not successful in obtaining a minimum of $5.0 million in financing, within 150 days after the closing of the Merger, the Chay Control Shareholders will have the right to put back to Ampio all of the Chay common stock then owned by the Chay Control Shareholders for a put price of $250,000, subject to adjustment. Under the Put Agreement, the Guarantors agreed to jointly guarantee the payment of the put price by DMI if the put right becomes exercisable in accordance with its terms. In addition, Ampio placed into escrow a cash deposit of $125,000 that will be paid to the Chay Control Shareholders in the event the put right becomes exercisable by its terms. The Chay Control Shareholders have since released $95,000 of the funds in escrow. If any amounts are paid to the Chay Control Shareholders in accordance with the escrow agreement, such payment will reduce the amount the Guarantors would be required to pay on exercise of the put right.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

The Company is not currently exposed to material market risk arising from financial instruments, changes in interest rates or commodity prices, or fluctuations in foreign currencies. The Company has no need to hedge against any of the foregoing risks and therefore currently engages in no hedging activities. Our outstanding indebtedness is limited currently to fixed rate instruments.

Item 4T. Controls and Procedures.

As of the end of the period covered by this Quarterly Report on Form 10-Q, an evaluation was carried out by the Company s management, with the participation of the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company s disclosure controls and procedures, as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934. Based on such evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports the Company files or furnishes under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and regulations, and are operating in an effective manner.

The Company made no significant changes in its internal controls over financial reporting or in other factors that materially affected, or are reasonably likely to materially affect, these controls during the six months ended June 30, 2010.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

The Company is currently not party to any material pending legal proceedings, whether routine or non-routine.

Item 1A. Risk Factors.

Certain factors exist which may affect the Company s business and could cause actual results to differ materially from those expressed in any forward-looking statements. The Company has not experienced any material changes from those risk factors as previously disclosed in the Company s Current Report on Form 8-K filed with the Securities and Exchange Commission on March 8, 2010 (the Form 8-K). However, the Company continues to require additional capital, the receipt of which is not assured.

Item 2. Unregistered Sales of Securities and Use of Proceeds.

The Company previously furnished the information required by Item 701 of Regulation S-K in the Form 8-K. The Company incorporates by reference herein the information included in Item 3.02 of the Form 8-K.

The Company issued 47,000 shares of stock in June 2010. The Company did not provide the information required by Item 701 of Regulation S-K on Form 8-K for reasons of materiality.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. [Removed and Reserved].

Item 5. Other Information.

On April 22, 2010, the Company issued a press release announcing the execution of a letter of intent under which the Company intends to acquire DMI BioSciences, Inc. On April 27, 2010, a report of current event was filed with respect to the letter of intent.

On July 21 and 27, we issued two press releases, the first of which concerned the initiation of a Phase II clinical trial for one of our produt candidates, and the second of which concerned the finalization of negotiations concerning the terms of a definitive agreement to acquire DMI BioSciences, Inc. The July 27 press release contained an error in the title of the release which was corrected in a press release issued on August 3, 2010.

Item 6. Exhibits

Exhibit Number	Description
10.1	Notes Payable dated June 23, 2010, by and between DMI BioSciences, Inc. and Ampio Pharmaceuticals, Inc.
31.1	Certificate of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2	Certificate of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certificate of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.1	Press release by Ampio Pharmaceuticals, Inc. dated July 21, 2010.
99.2	Press release by Ampio Pharmaceuticals, Inc. dated July 21, 2010.
99.3	Correction to press release by Ampio Pharmaceuticals, Inc. dated August 3, 2010.

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SIGNATURES

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

AMPIO PHARMACEUTICALS, INC.

By: /s/ DONALD B. WINGERTER, JR.
Donald B. Wingerter, Jr.

Chief Executive Officer

Date: August 16, 2010

By: /s/ BRUCE G. MILLER
Bruce G. Miller

Chief Financial Officer

Date: August 16, 2010