VIRGINIA ELECTRIC & POWER CO
Form 10-Q
August 08, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark one)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended June 30, 2007

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission File Number 001-02255

VIRGINIA ELECTRIC AND POWER COMPANY

(Exact name of registrant as specified in its charter)

VIRGINIA	**54-0418825**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
120 TREDEGAR STREET	
RICHMOND, VIRGINIA	**23219**
(Address of principal executive offices)	*(Zip Code)*

(804) 819-2000

(Registrant s telephone number)

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

At June 30, 2007, the latest practicable date for determination, 198,047 shares of common stock, without par value, of the registrant were outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(millions)	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Operating Revenue	**$ 1,424**	$ 1,323	**$ 2,867**	$ 2,656
Operating Expenses				
Electric fuel and energy purchases	**661**	555	**1,336**	1,112
Purchased electric capacity	**107**	109	**223**	226
Other energy-related commodity purchases	**8**	8	**16**	18
Other operations and maintenance:				
External suppliers	**196**	207	**402**	396
Affiliated suppliers	**78**	81	**156**	158
Depreciation and amortization	**140**	135	**274**	267
Other taxes	**43**	43	**88**	88
Total operating expenses	**1,233**	1,138	**2,495**	2,265
Income from operations	**191**	185	**372**	391
Other income	**17**	17	**40**	41
Interest and related charges:				
Interest expense	**75**	63	**129**	133
Interest expense junior subordinated notes payable to affiliated trust	**7**	7	**15**	15
Total interest and related charges	**82**	70	**144**	148
Income before income tax expense	**126**	132	**268**	284
Income tax expense	**47**	46	**100**	101
Income before extraordinary item	**79**	86	**168**	183
Extraordinary item[1]	**(158)**		**(158)**	
Net Income (Loss)	**(79)**	86	**10**	183
Preferred dividends	**4**	4	**8**	8
Balance available for common stock	**$ (83)**	$ 82	**$ 2**	$ 175

(1) Net of income tax benefit of $101 million for the three and six months ended June 30, 2007.

The accompanying notes are an integral part of the Consolidated Financial Statements.

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VIRGINIA ELECTRIC AND POWER COMPANY

CONSOLIDATED BALANCE SHEETS

(Unaudited)

(millions)	June 30, 2007	December 31, 2006[1]
ASSETS		
Current Assets		
Cash and cash equivalents	**$ 25**	$ 18
Customer accounts receivable (less allowance for doubtful accounts of $8 and $7)	**743**	650
Other receivables (less allowance for doubtful accounts of $8 and $9)	**113**	98
Inventories (average cost method)	**457**	505
Prepayments	**54**	133
Other	**61**	51
Total current assets	**1,453**	1,455
Investments		
Nuclear decommissioning trust funds	**1,351**	1,293
Other	**22**	22
Total investments	**1,373**	1,315
Property, Plant and Equipment		
Property, plant and equipment	**21,207**	20,771
Accumulated depreciation and amortization	**(8,576)**	(8,353)
Total property, plant and equipment, net	**12,631**	12,418
Deferred Charges and Other Assets	**452**	495
Total assets	**$ 15,909**	$ 15,683

(1) The Consolidated Balance Sheet at December 31, 2006 has been derived from the audited Consolidated Financial Statements at that date.

The accompanying notes are an integral part of the Consolidated Financial Statements.

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VIRGINIA ELECTRIC AND POWER COMPANY

CONSOLIDATED BALANCE SHEETS (Continued)

(Unaudited)

(millions)	June 30, 2007	December 31, 2006[1]
LIABILITIES AND SHAREHOLDER S EQUITY		
Current Liabilities		
Securities due within one year	**$ 644**	$ 1,267
Short-term debt	**914**	618
Accounts payable	**458**	418
Other	**505**	638
Total current liabilities	**2,521**	2,941
Long-Term Debt		
Long-term debt	**3,492**	2,987
Junior subordinated notes payable to affiliated trust	**412**	412
Notes payable other affiliates	**220**	220
Total long-term debt	**4,124**	3,619
Deferred Credits and Other Liabilities		
Deferred income taxes and investment tax credits	**1,995**	2,308
Asset retirement obligations	**659**	641
Regulatory liabilities	**961**	430
Other	**262**	95
Total deferred credits and other liabilities	**3,877**	3,474
Total liabilities	**10,522**	10,034
Commitments and Contingencies (see Note 10)		
Preferred Stock Not Subject to Mandatory Redemption	**257**	257
Common Shareholder s Equity		
Common stock no par, 300,000 shares authorized; 198,047 shares outstanding	**3,388**	3,388
Other paid-in capital	**888**	887
Retained earnings	**821**	955
Accumulated other comprehensive income	**33**	162
Total common shareholder s equity	**5,130**	5,392
Total liabilities and shareholder s equity	**$ 15,909**	$ 15,683

(1) The Consolidated Balance Sheet at December 31, 2006 has been derived from the audited Consolidated Financial Statements at that date.

The accompanying notes are an integral part of the Consolidated Financial Statements.

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VIRGINIA ELECTRIC AND POWER COMPANY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(millions)	Six Months Ended June 30, 2007	2006
Operating Activities		
Net income	**$ 10**	$ 183
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**317**	307
Deferred income taxes and investment tax credits, net	**(2)**	(29)
Deferred fuel expenses, net	**69**	56
Extraordinary item, net of income taxes	**158**	
Other adjustments to net income	**(23)**	(45)
Changes in:		
Accounts receivable	**(99)**	37
Affiliated accounts receivable and payable	**1**	25
Inventories	**48**	(63)
Accounts payable	**61**	(60)
Accrued interest, payroll and taxes	**(18)**	152
Prepayments	**76**	13
Other operating assets and liabilities	**79**	98
Net cash provided by operating activities	**677**	674
Investing Activities		
Plant construction and other property additions	**(460)**	(421)
Purchases of nuclear fuel	**(66)**	(60)
Purchases of securities	**(279)**	(267)

Proceeds from sales of securities	**263**	256
Other	**9**	22
Net cash used in investing activities	**(533)**	(470)
Financing Activities		
Issuance (repayment) of short-term debt, net	**296**	(655)
Issuance (repayment) of affiliated current borrowings, net	**(140)**	190
Issuance of long-term debt	**600**	1,000
Repayment of long-term debt	**(726)**	(612)
Common dividend payments	**(142)**	(139)
Preferred dividend payments	**(8)**	(8)
Other	**(17)**	(14)
Net cash used in financing activities		

Conversion of First Federal MHC to Stock Form. Federal Reserve Board regulations permit First Federal MHC to convert from the mutual form of organization to the capital stock form of organization. In a conversion transaction, a new holding company would be formed as successor to First Federal MHC, its corporate existence would end, and certain depositors would receive the right to subscribe for additional shares of the new holding company. In a conversion transaction, each share of common stock held by stockholders other than First Federal MHC would be automatically converted into a number of shares of common stock of the new holding company based on an exchange ratio determined at the time of conversion that ensures that stockholders other than First Federal MHC own the same percentage of common stock in the new holding company as they owned in us immediately before conversion. Under Federal Reserve Board regulations, stockholders other than First Federal MHC would not be diluted because of any dividends waived by First Federal MHC (and waived dividends would not be considered in determining an appropriate exchange ratio, provided that the mutual holding company involved was formed, engaged in a minority offering and waived dividends prior to December 1, 2009), in the event First Federal MHC converts to stock form. First Federal MHC was formed, engaged in a minority stock offering and waived dividends prior to December 1, 2009. The total number of shares held by stockholders other than First Federal MHC after a conversion transaction also would be increased by any purchases by stockholders other than First Federal MHC in the stock offering conducted as part of the conversion transaction.

Acquisition of Control. Under the federal Change in Bank Control Act, a notice must be submitted to the Federal Reserve Board if any person (including a company), or group acting in concert, seeks to acquire "control" of a savings and loan holding company or savings association. An acquisition of "control" can occur upon the acquisition of 10% or more of the voting stock of a savings and loan holding company or savings institution or as otherwise defined by the Federal rd. Under the Change in Bank Control Act, the Federal Reserve Board has 60 days from the filing of a complete notice to act, taking into consideration certain factors, including the financial and managerial resources of the acquirer and the anti-trust effects of the acquisition. Any company that so acquires control would then be subject to regulation as a savings and loan holding company.

Federal and State Taxation

General. We report our income on a fiscal year basis using the accrual method of accounting.

Federal Taxation. The federal income tax laws apply to us in the same manner as to other corporations with some exceptions, including particularly the reserve for bad debts discussed below. The following discussion of tax matters is intended only as a summary and does not purport to be a comprehensive description of the tax rules applicable to us. Our federal income tax returns are subject to examination for years 2011 and later. For the 2015 fiscal year, First Federal of Hazard's and Frankfort First's maximum federal income tax rate was 34.0%.

For fiscal years beginning before June 30, 1996, thrift institutions that qualified under certain definitional tests and other conditions of the Internal Revenue Code were permitted to use certain favorable provisions to calculate their deductions from taxable income for annual additions to their bad debt reserve. A reserve could be established for bad debts on qualifying real property loans, generally secured by interests in real property improved or to be improved, under the percentage of taxable income method or the experience method. The reserve for nonqualifying loans was computed using the experience method. Federal legislation enacted in 1996 repealed the reserve method of accounting for bad debts and the percentage of taxable income method for tax years beginning after 1995 and require savings institutions to recapture or take into income certain portions of their accumulated bad debt reserves. First Federal of Hazard did not qualify for such favorable tax treatment for any years through 1996. Approximately $5.2 million of First Federal of Frankfort First's accumulated bad debt reserves would not be recaptured into taxable income unless Frankfort First makes a "non-dividend distribution" to Kentucky First as described below.

If First Federal of Hazard or First Federal of Frankfort makes "non-dividend distributions" to us, the distributions will be considered to have been made from First Federal of Hazard's and First Federal of Frankfort's unrecaptured tax bad debt reserves, including the balance of their reserves as of December 31, 1987, to the extent of the "non-dividend distributions," and then from First Federal of Frankfort's supplemental reserve for losses on loans, to the extent of those reserves, and an amount based on the amount distributed, but not more than the amount of those reserves, will be included in First Federal of Frankfort's taxable income. Non-dividend distributions include distributions in excess of First Federal of Frankfort's current and accumulated earnings and profits, as calculated for federal income tax purposes, distributions in redemption of stock, and distributions in partial or complete liquidation. Dividends paid out of First Federal of Frankfort's current or accumulated earnings and profits will not be so included in First Federal of Frankfort's taxable income.

The amount of additional taxable income triggered by a non-dividend distribution is an amount that, when reduced by the tax attributable to the income, is equal to the amount of the distribution. Therefore, if First Federal of Frankfort makes a non-dividend distribution to us, approximately one and one-half times the amount of the distribution not in excess of the amount of the reserves would be includable in income for federal income tax purposes, assuming a 34% federal corporate income tax rate. First Federal of Frankfort does not intend to pay dividends in the future that would result in a recapture of any portion of its bad debt reserves.

State Taxation. Although First Federal MHC and Kentucky First are subject to the Kentucky corporation income tax and state corporation license tax (franchise tax), the corporation license tax is repealed effective for tax periods ending on or after December 31, 2005. Gross income of corporations subject to Kentucky income tax is similar to income reported for federal income tax purposes except that dividend income, among other income items, is exempt from taxation. For First Federal MHC and Kentucky First tax years beginning July 1, 2005, the corporations are subject to an alternative minimum income tax. Corporations must pay the greater of the income tax, the alternative tax or $175. The corporations can choose between two methods to calculate the alternative minimum; 9.5 cents per $100 of the corporation's gross receipts, or 75 cents per $100 of the corporation's Kentucky gross profits. Kentucky gross profits means Kentucky gross receipts reduced by returns and allowances attributable to Kentucky gross receipts, less Kentucky cost of goods sold. The corporations, in their capacity as holding companies for financial institutions, do not have a material amount of cost of goods sold. Although the corporate license tax rate is 0.21% of total capital employed in Kentucky, a bank holding company, as defined in Kentucky Revised Statutes 287.900, is allowed to deduct from its taxable capital, the book value of its investment in the stock or securities of subsidiaries that are subject to the bank franchise tax.

First Federal of Hazard and First Federal of Frankfort are exempt from both the Kentucky corporation income tax and corporation license tax. However, both institutions are instead subject to the bank franchise tax, an annual tax imposed on federally or state chartered savings and loan associations, savings banks and other similar institutions operating in Kentucky. The tax is 0.1% of taxable capital stock held as of January 1 each year. Taxable capital stock includes an institution's undivided profits, surplus and general reserves plus savings accounts and paid-up stock less deductible items. Deductible items include certain exempt federal obligations and Kentucky municipal bonds. Financial institutions which are subject to tax both within and without Kentucky must apportion their net capital.

Item 1A. Risk Factors

Rising interest rates may hurt our profits and asset values.

If interest rates rise, our net interest income would likely decline in the short term since, due to the generally shorter terms of interest-bearing liabilities, interest expense paid on interest-bearing liabilities, increases more quickly than interest income earned on interest-earning assets, such as loans and investments. In addition, a continuation of rising interest rates may hurt our income because of reduced demand for new loans, the demand for refinancing loans and the interest and fee income earned on new loans and refinancings. While we believe that modest interest rate increases will not significantly hurt our interest rate spread over the long term due to our high level of liquidity and the presence of a significant amount of adjustable-rate mortgage loans in our loan portfolio, interest rate increases may initially reduce our interest rate spread until such time as our loans and investments reprice to higher levels.

Changes in interest rates also affect the value of our interest-earning assets, and in particular our securities portfolio. Generally, the value of fixed-rate securities fluctuates inversely with changes in interest rates. Unrealized gains and losses on securities available for sale are reported as separate components of equity. Decreases in the fair value of securities available for sale resulting from increases in interest rates therefore could have an adverse effect on stockholders' equity.

A larger percentage of our loans are collateralized by real estate and further disruptions in the real estate market may result in losses and hurt our earnings.

Approximately 95.9% of our loan portfolio at June 30, 2015 was comprised of loans collateralized by real estate. The declining economic conditions have caused a decrease in demand for real estate, which has resulted in an erosion of some real estate values in our markets. Further disruptions in the real estate market could significantly impair the value of our collateral and our ability to sell the collateral upon foreclosure. The real estate collateral in each case provides an alternate source of repayment in the event of default by the borrower and may deteriorate in value during the time the credit is extended. If real estate values decline further, it will become more likely that we would be required to increase our allowance for loan losses. If during a period of reduced real estate values, we are required to liquidate the collateral securing a loan to satisfy the debt or to increase our allowance for loan losses, it could materially reduce our profitability and adversely affect our financial condition.

Strong competition within our market areas could hurt our profits and slow growth.

Although we consider ourselves competitive in our market areas, we face intense competition both in making loans and attracting deposits. Price competition for loans and deposits might result in our earning less on our loans and paying more on our deposits, which reduces net interest income. Some of the institutions with which we compete have substantially greater resources than we have and may offer services that we do not provide. We expect competition to increase in the future as a result of legislative, regulatory and technological changes and the continuing trend of consolidation in the financial services industry. Our profitability will depend upon our continued ability to compete successfully in our market areas.

The distressed economy in First Federal of Hazard's market area could hurt our profits and slow our growth.

First Federal of Hazard's market area consists of Perry and surrounding counties in eastern Kentucky. The economy in this market area has been distressed in recent years due to the decline in the coal industry on which the economy has been dependent. While the region has seen improvement in the economy from the influx of other industries, such as health care and manufacturing, and the competition provided by new methods of extracting natural gas has recently hurt the coal industry. As a consequence, the economy in First Federal of Hazard's market area continues to lag behind the economies of Kentucky and the United States and First Federal of Hazard has experienced insufficient loan demand in its market area. While First Federal of Hazard will seek to use excess funds to purchase loans from First Federal of Frankfort, we expect the redeployment of funds from securities into loans to take several years. Moreover, the slow economy in First Federal of Hazard's market area will limit our ability to grow our asset base in that market.

Regulation of the financial services industry is undergoing major changes, and we may be adversely affected by changes in laws and regulations.

We are subject to extensive government regulation, supervision and examination. Such regulation, supervision and examination governs the activities in which we may engage, and is intended primarily for the protection of the deposit insurance fund and our depositors.

In 2010 and 2011, in response to the financial crisis and recession that began in 2008, significant regulatory and legislative changes resulted in broad reform and increased regulation affecting financial institutions. The Dodd-Frank Act has created a significant shift in the way financial institutions operate and has restructured the regulation of depository institutions by merging the Office of Thrift Supervision, which previously regulated the Banks, into the Office of the Comptroller of the Currency, and assigning the regulation of savings and loan holding companies, including the Company and the MHC, to the Federal Reserve Board. The Dodd-Frank Act also created the Consumer Financial Protection Bureau to administer consumer protection and fair lending laws, a function that was formerly performed by the depository institution regulators. As required by the Dodd-Frank Act, the federal banking regulators have proposed new consolidated capital requirements that will limit our ability to borrow at the holding company level and invest the proceeds from such borrowings as capital in the Banks that could be leveraged to support additional growth. The Dodd-Frank Act contains various other provisions designed to enhance the regulation of depository institutions and prevent the recurrence of a financial crisis such as that which occurred in 2008 and 2009. The full impact of the Dodd-Frank Act on our business and operations may not be known for years until final regulations implementing the legislation are adopted. The Dodd-Frank Act may have a material impact on our operations, particularly through increased regulatory burden and compliance costs. Any future legislative changes could have a material impact on our profitability, the value of assets held for investment or the value of collateral for loans. Future legislative changes could also require changes to business practices and potentially expose us to additional costs, liabilities, enforcement action and reputational risk.

In addition to the enactment of the Dodd-Frank Act, the federal regulatory agencies recently have begun to take stronger supervisory actions against financial institutions that have experienced increased loan losses and other weaknesses as a result of the recent economic crisis. These actions include the entering into of written agreements and cease and desist orders that place certain limitations on their operations. Federal banking regulators recently have also been using with more frequency their ability to impose individual minimal capital requirements on banks, which requirements may be higher than those imposed under the Dodd-Frank Act or which would otherwise qualify the bank as being “well capitalized” under the Office of the Comptroller of the Currency’s prompt corrective action regulations. If we were to become subject to a supervisory agreement or higher individual capital requirements, such action may have a negative impact on our ability to execute our business plans, as well as our ability to grow, pay dividends, repurchase stock or engage in mergers and acquisitions and may result in restrictions in our operations. See *“Regulation and Supervision—Regulation of Federal Savings Institutions—Capital Requirements”* for a discussion of regulatory capital requirements.

We expect that our return on equity will be low compared to other companies as a result of our high level of capital.

Return on average equity, which equals net income divided by average equity, is a ratio used by many investors to compare the performance of a particular company with other companies. For the year ended June 30, 2015, our return on average equity was 3.1%. We also intend to continue managing excess capital through our stock repurchase program, which has been successful, given relatively low market prices of the Company’s common stock. However, this program could be curtailed or rendered less effective if the market price of our stock increases, or if the Company’s liquid funds are deployed elsewhere. Our goal of generating a return on average equity that is competitive with other publicly-held subsidiaries of mutual holding companies, by increasing earnings per share and book value per share, without assuming undue risk, could take a number of years to achieve, and we cannot assure that our goal will be attained. Consequently, you should not expect a competitive return on average equity in the near future. Failure to achieve a competitive return on average equity might make an investment in our common stock unattractive to some investors and might cause our common stock to trade at lower prices than comparable companies with higher returns on average equity.

Additional annual employee compensation and benefit expenses may reduce our profitability and stockholders’ equity.

We will continue to recognize employee compensation and benefit expenses for employees and executives under our benefit plans. With regard to the employee stock ownership plan, applicable accounting practices require that the expense be based on the fair market value of the shares of common stock at specific points in the future, therefore we will recognize expenses for our employee stock ownership plan when shares are committed to be released to participants’ accounts. We will also recognize expenses for restricted stock awards and options over the vesting periods of those awards. In addition, employees of both subsidiary Banks participate in a defined-benefit plan through Pentegra. Costs associated with the defined-benefit plans could increase or legislation could be enacted that would increase the Banks’ obligations under the plan or change the methods the Banks use in accounting for the plans. Those changes could adversely affect personnel expense and the Company’s balance sheet.

First Federal MHC owns a majority of our common stock and is able to exercise voting control over most matters put to a vote of stockholders, including preventing

sale or merger transactions you may like or a second-step conversion by First Federal MHC.

First Federal MHC owns a majority of our common stock and, through its Board of Directors, is able to exercise voting control over most matters put to a vote of stockholders. As a federally chartered mutual holding company, the board of directors of First Federal MHC must ensure that the interests of depositors of First Federal of Hazard are represented and considered in matters put to a vote of stockholders of Kentucky First. Therefore, the votes cast by First Federal MHC may not be in your personal best interests as a stockholder. For example, First Federal MHC may exercise its voting control to prevent a sale or merger transaction in which stockholders could receive a premium for their shares, prevent a second-step conversion transaction by First Federal MHC or defeat a stockholder nominee for election to the Board of Directors of Kentucky First. However, implementation of a stock-based incentive plan will require approval of Kentucky First's stockholders other than First Federal MHC. Federal Reserve Board regulations would likely prevent an acquisition of Kentucky First other than by another mutual holding company or a mutual institution.

There may be a limited market for our common stock which may lower our stock price.

Although our shares of common stock are listed on the Nasdaq Global Market, there is no guarantee that the shares will be regularly traded. If an active trading market for our common stock does not develop, you may not be able to sell all of your shares of common stock on short notice and the sale of a large number of shares at one time could temporarily depress the market price.

Our ability to pay dividends is subject to the ability of First Federal of Hazard and First Federal of Frankfort to make capital distributions to Kentucky First and the waiver of dividends by First Federal MHC.

Our long-term ability to pay dividends to our stockholders is based primarily upon the ability of the Banks to make capital distributions to Kentucky First, and also on the availability of cash at the holding company level in the event earnings are not sufficient to pay dividends according to the cash dividend payout policy. Under Office of the Comptroller of the Currency safe harbor regulations, the Banks may each distribute to Kentucky First capital not exceeding net retained income for the current calendar year and the prior two calendar years. First Federal MHC owns a majority of Kentucky First’s outstanding stock. First Federal MHC has historically waived its right to dividends on the Kentucky First common shares it owns, in which case the amount of dividends paid to public stockholders is significantly higher than it would be if First Federal MHC accepted dividends. First Federal MHC is not required to waive dividends, but Kentucky First expects this practice to continue, subject to member and regulatory approval annually. First Federal MHC is required to obtain a waiver from the Federal Reserve Board allowing it to waive its right to dividends.

The Federal Reserve Board in 2011 issued regulations that govern the activities of Kentucky First and First Federal MHC and the regulations were implemented in the fourth quarter of 2011. Under Section 239.8(d) of the Federal Reserve Board’s Regulation MM governing dividend waivers, a mutual holding company may waive its right to dividends on shares of its subsidiary if the mutual holding company gives written notice of the waiver to the Federal Reserve Board and the Federal Reserve Board does not object. For a company such as First Federal MHC that waived dividends prior to December 1, 2009, the Federal Reserve Board may not object to a dividend waiver if such waiver would not be detrimental to the safety and soundness of the savings association subsidiary and the board of directors of the mutual holding company expressly determines that such dividend waiver is consistent with the board’s fiduciary duties to the members of the mutual holding company.

To address concerns with respect to the conflict of interest created by dividend waivers, Regulation MM requires the board of directors of the mutual holding company to adopt a resolution that describes the conflict of interest that exists because of a director's ownership of stock in the subsidiary declaring the dividends and any actions the mutual holding company board have taken to eliminate the conflict of interest, such as the directors' waiving their right to receive dividends. Also, the resolution must contain an affirmation that a majority of the mutual members eligible to vote have, within the 12 months prior to the declaration date of the dividend, voted to approve the waiver of dividends.

Federal MHC has received Federal Reserve Board approval to waive quarterly dividends totaling $0.40 per share annually beginning with the dividend paid on September 28, 2012 and continuing through the dividend payable in the 3rd quarter of 2016. It is expected that First Federal MHC will continue to waive future dividends, except to the extent dividends are needed to fund First Federal MHC's continuing operations, subject to the ability of First Federal MHC to obtain regulatory approval of its requests to waive dividends and to its ability to obtain member approval of dividend waivers.

We cannot predict whether members will continue to approve annual dividend waiver requests or whether the Federal Reserve Board will grant future dividend waiver requests and, if granted, there can be no assurance as to the conditions, if any, the Federal Reserve Board will place on future dividend waiver requests by grandfathered mutual holding companies such as First Federal MHC. If First Federal MHC is unable to waive the receipt of dividends, our ability to pay dividends to our stockholders may be substantially impaired and the amounts of any such dividends may be significantly reduced.

We are subject to certain risks in connection with our use of technology.

Our security measures may not be sufficient to mitigate the risk of a cyber attack. Communications and information systems are essential to the conduct of our business, as we use such systems to manage our customer relationships, our general ledger and virtually all other aspects of our business. Our operations rely on the secure processing, storage, and transmission of confidential and other information in our computer systems and networks. Although we take protective measures and endeavor to modify them as circumstances warrant, the security of our computer systems, software, and networks may be vulnerable to breaches, unauthorized access, misuse, computer viruses, or other malicious code and cyber attacks that could have a security impact. If one or more of these events occur, this could jeopardize our or our customers' confidential and other information processed and stored in, and transmitted through, our computer systems and networks, or otherwise cause interruptions or malfunctions in our operations or the operations of our customers or counterparties. We may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures, and we may be subject to litigation and financial losses that are either not insured against or not fully covered through any insurance maintained by us. We could also suffer significant reputational damage.

Security breaches in our Internet banking activities could further expose us to possible liability and damage our reputation. Any compromise of our security also could deter customers from using our Internet banking services that involve the transmission of confidential information. We rely on standard Internet security systems to provide the security and authentication necessary to effect secure transmission of data. These precautions may not protect our systems from compromises or breaches of our security measures, which could result in significant legal liability and significant damage to our reputation and our business.

Our security measures may not protect us from systems failures or interruptions. While we have established policies and procedures to prevent or limit the impact of systems failures and interruptions, there can be no assurance that such events will not occur or that they will be adequately addressed if they do. In addition, we outsource certain aspects of our data processing and other operational functions to certain third-party providers. If our third-party providers encounter difficulties, or if we have difficulty in communicating with them, our ability to adequately process and account for transactions could be affected, and our business operations could be adversely impacted. Threats to information security also exist in the processing of customer information through various other vendors and their personnel.

The occurrence of any failures or interruptions may require us to identify alternative sources of such services, and we cannot assure you that we could negotiate terms that are as favorable to us, or could obtain services with similar functionality as found in our existing systems without the need to expend substantial resources, if at all. Further, the occurrence of any systems failure or interruption could damage our reputation and result in a loss of customers and business, could subject us to additional regulatory scrutiny, or could expose us to legal liability. Any of these occurrences could have a material adverse effect on our financial condition and results of operations.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We conduct our business through seven offices. The following table sets forth certain information relating to our offices at June 30, 2015.

	Year Opened/Acquired	Owned or Leased	Net Book Value at June 30, 2015	Approximate Square Footage
	(Dollars in thousands)			
First Federal of Hazard				
Main Office: 479 Main Street Hazard, Kentucky 41701	1960	Owned	$ 255	15,000
First Federal of Frankfort Main Office: 216 West Main Street Frankfort, Kentucky 40601	2005	Owned	1,105	14,000
1980 Versailles Road Frankfort, Kentucky 40601	2005	Owned	509	1,800
1220 US 127 South Frankfort, Kentucky 40601	2005	Owned	477	2,480
340 West Main Street Danville, Kentucky 40422	2012	Owned	517	8,700
120 Skywatch Drive Danville, Kentucky 40422	2012	Owned	774	2,300
208 Lexington Street Lancaster, Kentucky 40444	2012	Owned	526	4,300

The net book value of our investment in premises and equipment was $5.2 million at June 30, 2015. See Note E of Notes to Consolidated Financial Statements.

Item 3. Legal Proceedings

From time to time, we may be defendants in claims and lawsuits against us, such as claims to enforce liens, condemnation proceedings on properties in which we hold security interests, claims involving the making and servicing of real property loans and other issues incident to our business. We are not a party to any pending legal proceedings that we believe could have a material adverse effect on our financial condition, results of operations or cash flows.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

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

(a) The information contained under the sections captioned "*Market Information*" in the Company's Annual Report to Stockholders for the Fiscal Year Ended June 30, 2015 (the "Annual Report") filed as Exhibit 13 hereto is incorporated herein by reference.

(b) Not applicable.

(c) The Company repurchased the following equity securities registered under the Securities Exchange Act of 1934, as amended, during the fourth quarter of the fiscal year ended June 30, 2015.

Period	**(a) Total Number of Shares Purchased**	**(b) Average Price Paid per Share**	**(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs**	**(d) Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs (1)**
April 2015 Beginning date: April 1 Ending date: April 30	—	—	—	60,323
May 2015 Beginning date: May 1 Ending date: May 31	—	—	—	60,323
June 2015 Beginning date: June 1 Ending date: June 30	—	—	—	60,323

Total	—	—	—

(1) On January 16, 2014, the Company announced a program (its seventh) to repurchase up to 150,000 shares of its Common Stock.

Item 6. Selected Financial Data

This item is not applicable, as the Company is a smaller reporting company.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The information contained in the section captioned "*Management's Discussion and Analysis of Financial Condition and Results of Operations*" in the Annual Report, is incorporated herein by reference.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

This item is not applicable, as the Company is a smaller reporting company.

Item 8. Financial Statements and Supplementary Data

The Consolidated Financial Statements, Notes to Consolidated Financial Statements, Report of Independent Registered Public Accounting Firm and Selected Financial Data, which are listed under Item 15 herein, are included in the Annual Report and are incorporated herein by reference.

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

(a) Disclosure Controls and Procedures

The Company's management, including the Company's principal executive officer and principal financial officer, have evaluated the effectiveness of the Company's "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, (the "Exchange Act"). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the Securities and Exchange Commission (the "SEC") (1) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

(b) Internal Control Over Financial Reporting

Parent Company of First Federal Savings and Loan of Hazard and First Federal Savings Bank of Frankfort

MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL

OVER FINANCIAL REPORTING

Management of Kentucky First Federal Bancorp (the "Company") is responsible for the preparation, integrity, and fair presentation of the consolidated financial statements included in this annual report. The Company's consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and, as such, include some amounts that are based on the best estimates and judgments of management.

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting. The internal control system is designed to provide reasonable assurance to management and the Board of Directors regarding the reliability of the company's financial reporting and the preparation and presentation of financial statements for external reporting purposes in conformity with accounting principles generally accepted in the United States of America, as well as to safeguard assets from unauthorized use or disposition. The system of internal control over financial reporting is evaluated for effectiveness by management and tested for reliability through a program of internal audit with actions taken to correct potential deficiencies as they are identified. Because of inherent limitations in any internal control system, no matter how well designed, misstatements due to error or fraud may occur and not be detected, including the possibility of the circumvention or overriding controls. Accordingly, even an effective internal control system can provide only reasonable assurance with respect to financial statement preparation. Further, because of changes in conditions, internal control effectiveness may vary over time.

Management assessed the effectiveness of the company's internal control over financial reporting as of June 30, 2015, based upon criteria set forth in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission – 1992 ("COSO").

Based on this assessment and on the forgoing criteria, management has concluded that, as of June 30, 2015, the Company's internal control over financial reporting is effective.

This annual report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to the exemption provided to issuers that are not "large accelerated filers" or "accelerated filers" under the Dodd-Frank Wall Street Reform and Consumer Protection Act.

/s/ Don D. Jennings	/s/ R. Clay Hulette
Don D. Jennings	R. Clay Hulette
Chief Executive Officer	Vice President and Chief Financial Officer

(c) Changes to Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the quarter ended June 30, 2015 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

Not applicable.

PART III

Item 10. Directors, Executive Officers, and Corporate Governance

Directors

The information contained under the section captioned "*Proposal I Election of Directors*" in the Company's definitive proxy statement for the Company's 2015 Annual Meeting of Stockholders (the "Proxy Statement") is incorporated herein by reference.

Executive Officers

The information regarding the Company's executive officers is incorporated herein by reference to *"Proposal I – Election of Directors"* in the Proxy Statement.

Corporate Governance

Information regarding the Company's Audit Committee and Audit Committee financial expert is incorporated herein by reference to the section captioned *"Proposal I Election of Directors Committees of the Board of Directors"* in the Proxy Statement.

Compliance with Section 16(a) of the Exchange Act

Information regarding compliance with Section 16(a) of the Exchange Act is incorporated by reference to section captioned *"Section 16(a) Beneficial Ownership Reporting Compliance"* in the Proxy Statement.

Disclosure of Code of Ethics

Kentucky First has adopted a Code of Ethics and Business Conduct that applies to all of its directors, officers and employees. To obtain a copy of this document at no charge, please write to Kentucky First Federal Bancorp, P.O. Box 535, Frankfort, Kentucky 40602-0535, or call toll-free (888) 818-3372 and ask for Investor Relations.

Item 11. Executive Compensation

The information contained under the section captioned "*Executive Compensation*" in the Proxy Statement is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

(a) **Security Ownership of Certain Beneficial Owners.** Information required by this item is incorporated herein by reference to the section captioned "*Voting Securities and Security Ownership*" in the Proxy Statement.

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(b) **Security Ownership of Management.** Information required by this item is incorporated herein by reference to the sections captioned "*Voting Securities and Security Ownership*" in the Proxy Statement.

(c) **Changes in Control.** Management of the Company knows of no arrangements, including any pledge by any person of securities of the Company, the operation of which may at a subsequent date result in a change in control of the Company.

(d) **Equity Compensation Plans.** The following table sets forth certain information with respect to the Company's equity compensation plans as of June 30, 2015.

	(a) **Number of securities to be issued upon exercise of outstanding options, warrants and rights**	(b) **Weighted-average exercise price of outstanding options, warrants and rights**	(c) **Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))**
Equity compensation plans approved by security holders	325,800	$ 10.10	95,416
Equity compensation plans not approved by security holders	—	—	—
Total	325,800	$ 10.10	95,416

Item 13. Certain Relationships and Related Transactions, and Director Independence

Certain Relationships and Related Transactions

The information required by this item is incorporated herein by reference to the section captioned "*Transactions with Related Persons*" in the Proxy Statement.

Corporate Governance

For information regarding director independence, the section captioned *"Proposal I – Election of Directors"* is incorporated herein by reference.

Item 14. Principal Accountant Fees and Services

The information required by this item is incorporated herein by reference to the section captioned *"Audit and Other Fees Paid to Independent Accountant"* in the Proxy Statement.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) List of Documents Filed as Part of This Report

(1) ***Financial Statements*****.** The following consolidated financial statements are incorporated by reference from Item 8 hereof (see Exhibit 13):

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of June 30, 2015 and 2014

Consolidated Statements of Income for the Years Ended June 30, 2015 and 2014

Consolidated Statements of Comprehensive Income for the Years Ended June 30, 2015 and 2014

Consolidated Statements of Changes in Shareholders' Equity for the Years Ended June 30, 2015 and 2014

Consolidated Statements of Cash Flows for the Years Ended June 30, 2015 and 2014

Notes to Consolidated Financial Statements

(2) ***Financial Statement Schedules*.** All schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission are omitted because of the absence of conditions under which they are required or because the required information is included in the consolidated financial statements and related notes thereto.

(3) ***Exhibits*.** The following is a list of exhibits filed as part of this Annual Report on Form 10-K and is also the Exhibit Index.

No.	**Description**
3.1[1]	Charter of Kentucky First Federal Bancorp
3.2[6]	Amended and Restated Bylaws of Kentucky First Federal Bancorp
4.1[1]	Specimen Stock Certificate of Kentucky First Federal Bancorp
10.1[2]	Employment Agreement between Kentucky First Federal Bancorp and Don D. Jennings, as amended†
10.2[2]	Employment Agreement between First Federal Savings Bank of Frankfort and Don D. Jennings, as amended†
10.3[2]	Employment Agreement between Kentucky First Federal Bancorp and R. Clay Hulette, as amended†
10.4[2]	Employment Agreement between First Federal Savings Bank of Frankfort and R. Clay Hulette, as amended†
10.5[2]	Employment Agreement between First Federal Savings Bank of Frankfort and Teresa Kuhl, as amended†
10.6[2]	Amended and Restated First Federal Savings and Loan Association of Hazard Change in Control Severance Compensation Plan†
10.7[2]	Amended and Restated First Federal Savings Bank of Frankfort Change in Control Severance Compensation Plan†
10.8[2]	

	Amended and Restated First Federal Savings and Loan Association Supplemental Executive Retirement Plan†
10.9[3]	Kentucky First Federal Bancorp 2005 Equity Incentive Plan†
10.10[4]	Form of Restricted Stock Award Agreement†
10.11[4]	Form of Incentive Stock Option Award Agreement†
10.12[4]	Form of Non-Statutory Option Award Agreement†
10.13[5]	Employment Agreement by and between Kentucky First Federal Bancorp and William H. Johnson†
10.14[5]	Employment Agreement by and between First Federal Savings Bank of Frankfort and William H. Johnson†
13	Annual Report to Stockholders for the year ended June 30, 2015
21	Subsidiaries
23.1	Consent of Crowe Horwath LLP
31.1	Rule 13a-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a) Certification of Chief Financial Officer
32	Section 1350 Certifications
101*	The following materials from the Company’s Annual Report on Form 10-K for the year ended June 30, 2015, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Changes in Shareholders’ Equity, (v) the Consolidated Statements of Cash Flows and the (vi) Notes to Consolidated Financial Statements.

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† Management contract or compensation plan or arrangement.

* Furnished, not filed.

(1) Incorporated herein by reference to the Company's Registration Statement on Form S-1 (File No. 333-119041).

(2) Incorporated herein by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended December 31, 2008 (File No. 0-51176).

(3) Incorporated herein by reference to the Company's definitive additional proxy solicitation materials filed with the Securities and Exchange Commission on October 24, 2005.

(4) Incorporated herein by reference to the Company's Registration Statement on Form S-8 (File No. 333-130243).

(5) Incorporated herein by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended December 31, 2012 (File No. 0-51176).

(6) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended June 30, 2012 (File No. 0-51176).

(b) **Exhibits.** The exhibits required by Item 601 of Regulation S-K are either filed as part of this Annual Report on Form 10-K or incorporated by reference herein.

(c) **Financial Statements and Schedules Excluded from Annual Report.** There are no other financial statements and financial statement schedules which were excluded from the Annual Report to Stockholders pursuant to Rule 14a-3(b) which are required to be included herein.

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SIGNATURES

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

KENTUCKY FIRST
FEDERAL BANCORP

September 28, 2015 By: /s/ Don D. Jennings
Don D. Jennings
Chief Executive Officer

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

/s/ Don D. Jennings Don D. Jennings Chief Executive Officer and Director (Principal Executive Officer)	September 28, 2015
/s/ R. Clay Hulette R. Clay Hulette Vice President, Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer)	September 28, 2015
/s/ Tony D. Whitaker Tony D. Whitaker Chairman of the Board	September 28, 2015
/s/ Stephen G. Barker Stephen G. Barker Director	September 28, 2015
/s/ C. Michael Davenport. C. Michael Davenport Director	September 28, 2015
/s/ Walter G. Ecton, Jr.	September 28, 2015

Walter G. Ecton, Jr.
Director

/s/ William D. Gorman, Jr.	September 28, 2015
William D. Gorman, Jr.	
Director	

/s/ David R. Harrod David R. Harrod Director	September 28, 2015
/s/ William H. Johnson William H. Johnson Director	September 28, 2015
/s/ W. Banks Hudson W. Banks Hudson Director	September 28, 2015

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