Oconee Federal Financial Corp.
Form 10-Q
November 14, 2014

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 10-Q**

**x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the Quarterly Period ended September 30, 2014**

**Or**

**o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For transition period from to**

**Commission File Number 001-35033**

**Oconee Federal Financial Corp.**

(Exact Name of Registrant as Specified in Charter)

| | |
|---|---|
| **Federal** | **32-0330122** |
| (State of Other Jurisdiction of Incorporation) | (I.R.S Employer Identification Number) |
| **201 East North Second Street, Seneca, South Carolina** | **29678** |
| (Address of Principal Executive Officers) | (Zip Code) |

**(864) 882-2765**

Registrant's telephone number, including area code

**Not Applicable**

(Former name or former address, if changed since last report)

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 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 whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

| | |
|---|---|
| Large accelerated filer | Accelerated filer |
| Non-accelerated filer | Smaller reporting company 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

Indicate the number of shares outstanding of each of the Issuer's classes of common stock as of the latest practicable date.

There were 5,834,395 shares of Common Stock, par value $.01 per share, outstanding as of November 7, 2014.

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**OCONEE FEDERAL FINANCIAL CORP.**

Form 10-Q Quarterly Report

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OCONEE FEDERAL FINANCIAL CORP.

CONSOLIDATED BALANCE SHEETS

(Amounts in thousands, except share and per share data)

(Unaudited)

**PART I**

ITEM 1. FINANCIAL STATEMENTS

| | September 30, 2014 (Unaudited) | June 30, 2014 (*) |
|---|---|---|
| **ASSETS** | | |
| Cash and due from banks | $ 923 | $ 1,365 |
| Interest-bearing deposits | 7,366 | 10,525 |
| Total cash and cash equivalents | 8,289 | 11,890 |
| Securities available-for-sale | 100,830 | 103,806 |
| Loans, net of allowance for loan losses of $855 and $855 | 232,914 | 229,931 |
| Premises and equipment, net | 3,019 | 2,993 |
| Real estate owned, net | 596 | 744 |
| Accrued interest receivable | | |
| Loans | 846 | 811 |
| Investments | 344 | 251 |
| Restricted equity securities | 325 | 325 |
| Bank owned life insurance | 8,825 | 8,758 |
| Other assets | 1,108 | 992 |
| Total assets | $ 357,096 | $ 360,501 |
| | | |
| **LIABILITIES** | | |
| Deposits | | |
| Non-interest bearing | $ 8,360 | $ 7,075 |
| Interest bearing | 269,588 | 273,940 |
| Total deposits | 277,948 | 281,015 |
| Accrued interest payable and other liabilities | 1,717 | 2,505 |
| Total liabilities | 279,665 | 283,520 |
| | | |
| **SHAREHOLDERS' EQUITY** | | |

| | | |
|---|---|---|
| Common stock, $0.01 par value, 100,000,000 shares authorized; 5,834,395 shares outstanding | 64 | 64 |
| Treasury stock, at par 600,699 shares | (6 ) | (6 ) |
| Additional paid in capital | 12,281 | 12,186 |
| Retained earnings | 67,166 | 66,705 |
| Accumulated other comprehensive loss | (301 ) | (147 ) |
| Unearned ESOP shares | (1,773 ) | (1,821 ) |
| Total shareholders' equity | 77,431 | 76,981 |
| Total liabilities and shareholders' equity | $ 357,096 | $ 360,501 |

* Derived from audited consolidated financial statements

See accompanying notes to the consolidated financial statements

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OCONEE FEDERAL FINANCIAL CORP.

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(Amounts in thousands, except share and per share data)

(Unaudited)

| | Three Months Ended | |
|---|---|---|
| | **September 30, 2014** | **September 30, 2013** |
| Interest and dividend income: | | |
| Loans, including fees | $ 2,886 | $ 2,852 |
| Securities, taxable | 381 | 371 |
| Securities, tax-exempt | 36 | — |
| Interest-bearing deposits and other | 7 | 15 |
| Total interest income | 3,310 | 3,238 |
| | | |
| Interest expense: | | |
| Deposits | 308 | 429 |
| Total interest expense | 308 | 429 |
| Net interest income | 3,002 | 2,809 |
| Provision for loan losses | — | 81 |
| | | |
| Net interest income after provision for loan losses | 3,002 | 2,728 |
| Noninterest income: | | |
| Service charges on deposit accounts | 18 | 18 |
| Income on bank owned life insurance | 67 | 76 |
| Gain on sales of securities | 5 | — |
| Total noninterest income | 90 | 94 |
| | | |
| Noninterest expense: | | |
| Salaries and employee benefits | 910 | 861 |
| Occupancy and equipment | 167 | 155 |
| Data processing | 67 | 63 |
| Professional and supervisory fees | 113 | 112 |
| Office expense | 43 | 29 |
| Advertising | 23 | 21 |
| FDIC deposit insurance | 38 | 40 |
| Charitable contributions | — | — |

| | | | | |
|---|---|---|---|---|
| Provision for real estate owned and related expenses | | 19 | | 32 |
| Other | | 103 | | 77 |
| Total noninterest expense | | 1,483 | | 1,390 |
| | | | | |
| Income before income taxes | | 1,609 | | 1,432 |
| Income tax expense | | 565 | | 513 |
| Net income | $ | 1,044 | $ | 919 |
| | | | | |
| Other comprehensive income (loss) | | | | |
| Unrealized loss on securities available-for-sale | $ | (243 ) | $ | (9 ) |
| Tax effect | | 92 | | 3 |
| Reclassification adjustment for gains realized in net income | | (5 ) | | — |
| Tax effect | | 2 | | — |
| Total other comprehensive loss | | (154 ) | | (6 ) |
| Comprehensive income | $ | 890 | $ | 913 |
| | | | | |
| Basic net income per share: (Note 2) | $ | 0.18 | $ | 0.16 |
| Diluted net income per share: (Note 2) | $ | 0.18 | $ | 0.16 |
| Dividends declared per share: | $ | 0.10 | $ | 0.10 |

See accompanying notes to the consolidated financial statements

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OCONEE FEDERAL FINANCIAL CORP.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(Unaudited)

(Amounts in thousands, except share and per share data)

| | **Common Stock** | **Treasury Stock** | **Additional Paid-In Capital** | **Retained Earnings** |
|---|---|---|---|---|
| Balance at July 1, 2013 | $ 64 | $ (5 ) | $ 13,413 | $ 65,315 |
| Net income | — | — | — | 919 |
| Other comprehensive income | — | — | — | |
| Purchase of 89,900 shares of treasury stock | — | (1 ) | (1,423 ) | |
| Stock-based compensation expense | — | — | 57 | |
| Dividends | — | — | — | (584 |
| ESOP shares earned | — | — | 21 | |
| Balance at September 30, 2013 | $ 64 | $ (6 ) | $ 12,068 | $ 65,650 |
| | | | | |
| Balance at July 1, 2014 | $ 64 | $ (6 ) | $ 12,186 | $ 66,705 |
| Net income | — | — | — | 1,044 |
| Other comprehensive loss | — | — | — | |
| Stock-based compensation expense | — | — | 66 | |
| Dividends (1) | — | — | — | (583 |
| ESOP shares earned | — | — | 29 | |
| Balance at September 30, 2014 | $ 64 | $ (6 ) | $ 12,281 | $ 67,166 |

(1) Cash dividends declared on July 24, 2014 were paid on August 21, 2014.

See accompanying notes to the consolidated financial statements

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OCONEE FEDERAL FINANCIAL CORP.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Amounts in thousands, except share and per share data)

| | Three Months Ended | |
|---|---|---|
| | **September 30, 2014** | **September 30, 2013** |
| **Cash Flows From Operating Activities** | | |
| Net income | $ 1,044 | $ 919 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan losses | — | 81 |
| Depreciation and amortization, net | 221 | 252 |
| Deferred loan fees, net | 17 | 6 |
| Deferred income tax expense | 22 | — |
| Loss on sales of real estate owned | 8 | 14 |
| Gain on sales of securities | (5 ) | — |
| Increase in cash surrender value of bank owned life insurance | (67 ) | (76 ) |
| ESOP compensation expense | 77 | 67 |
| Stock based compensation expense | 66 | 57 |
| Net change in operating assets and liabilities: | | |
| Accrued interest receivable | (128 ) | (77 ) |
| Accrued interest payable | (309 ) | (1 ) |
| Other | 622 | 387 |
| Net cash provided by operating activities | 1,568 | 1,629 |
| | | |
| **Cash Flows From Investing Activities** | | |
| Purchases of premises and equipment | (84 ) | (19 ) |
| Purchases of securities held-to-maturity | — | (1,494 ) |
| Purchases of securities available-for-sale | (3,399 ) | (5,324 ) |
| Proceeds from maturities, paydowns and calls of securities available-for-sale | 3,323 | 2,218 |
| Proceeds from maturities, paydowns and calls of securities held-to-maturity | — | 797 |
| Proceeds from sales of securities available-for-sale | 1,501 | — |
| Proceeds from sale of real estate owned | 199 | 176 |
| Loan originations and repayments, net | (3,059 ) | (782 ) |
| Net cash used in investing activities | (1,519 ) | (4,428 ) |

| | | |
|---|---|---|
| **Cash Flows from Financing Activities** | | |
| Net change in deposits | (3,067 ) | (3,638 ) |
| Dividends paid | (583 ) | (584 ) |
| Purchase of treasury stock | — | (1,431 ) |
| Net cash used in financing activities | (3,650 ) | (5,653 ) |
| Change in cash and cash equivalents | (3,601 ) | (8,452 ) |
| Cash and cash equivalents, beginning of year | 11,890 | 37,942 |
| Cash and cash equivalents, end of period | $ 8,289 | $ 29,490 |

See accompanying notes to the consolidated financial statements

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

## (1) BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Oconee Federal Financial Corp., which include the accounts of its wholly owned subsidiary Oconee Federal Savings and Loan Association (the “Association”) (referred to herein as “the Company,” “we,” “us,” or “our”) have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Intercompany accounts and transactions are eliminated during consolidation. The Company is majority owned (70.74%) by Oconee Federal, MHC. These financial statements do not include the transactions and balances of Oconee Federal, MHC.

In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments (consisting only of normal recurring accruals) necessary to present fairly the Company’s financial position as of September 30, 2014 and June 30, 2014 and the results of operations and cash flows for the interim periods ended September 30, 2014 and 2013. All interim amounts have not been audited, and the results of operations for the interim periods herein are not necessarily indicative of the results of operations to be expected for the year. These consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements and notes thereto included in the Form 10-K Annual Report of Oconee Federal Financial Corp. for the year ended June 30, 2014.

## (2) EARNINGS PER SHARE (“EPS”)

Basic EPS is determined by dividing net earnings available to common shareholders by the weighted average number of common shares outstanding for the period. ESOP shares are considered outstanding for this calculation unless unearned. The factors used in the earnings per common share computation follow:

| | Three Months Ended | |
|---|---|---|
| | September 30, 2014 | September 30, 2013 |
| Earnings per share | | |
| Net income | $ 1,044 | $ 919 |
| Less: distributed earnings allocated to participating securities | (7 ) | (7 ) |
| Less: (undistributed income) dividends in excess of earnings allocated to participating securities | (5 ) | (4 ) |
| Net earnings available to common shareholders | $ 1,032 | $ 908 |

| | | |
|---|---|---|
| Weighted average common shares outstanding including participating securities | 5,834,395 | 5,850,522 |
| Less: participating securities | (67,699 ) | (71,095 ) |
| Less: average unearned ESOP shares | (179,111 ) | (204,302 ) |
| Weighted average common shares outstanding | 5,587,585 | 5,575,125 |
| | | |
| Basic earnings per share | $ 0.18 | $ 0.16 |
| | | |
| Weighted average common shares outstanding | 5,587,585 | 5,575,125 |
| Add: dilutive effects of assumed exercises of stock options | 54,644 | 47,856 |
| Average shares and dilutive potential common shares | 5,642,229 | 5,622,981 |
| | | |
| Diluted earnings per share | $ 0.18 | $ 0.16 |

During the three months ended September 30, 2014, 7,700 shares were considered anti-dilutive. During the three months ended September 30, 2013, no shares were considered anti-dilutive.

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

**(3) SECURITIES AVAILABLE-FOR-SALE AND HELD-TO-MATURITY**

Debt, mortgage-backed and equity securities have been classified in the consolidated balance sheets according to management's intent. U.S. Government agency mortgage-backed securities consist of securities issued by U.S. Government agencies and U.S. Government sponsored enterprises. Investment securities at September 30, 2014 and June 30, 2014 are as follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| **September 30, 2014** | | | | |
| Available-for-sale: | | | | |
| FHLMC common stock | $ 20 | $ 195 | $ — | $ 215 |
| Preferred stock (1) | 271 | 27 | — | 298 |
| Certificates of deposit | 6,972 | 26 | (8 ) | 6,990 |
| Municipal securities | 6,087 | 12 | (31 ) | 6,068 |
| U.S. Government agency mortgage-backed securities | 59,520 | 327 | (805 ) | 59,042 |
| U.S. Government agency bonds | 28,448 | 151 | (382 ) | 28,217 |
| Total available-for-sale | $ 101,318 | $ 738 | $ (1,226 ) | $ 100,830 |
| | | | | |
| **June 30, 2014** | | | | |
| Available-for-sale: | | | | |
| FHLMC common stock | $ 20 | $ 294 | $ — | $ 314 |
| Preferred stock (1) | 271 | 27 | — | 298 |
| Certificates of deposit | 7,221 | 24 | (8 ) | 7,237 |
| Municipal securities | 5,846 | 2 | (39 ) | 5,809 |
| U.S. Government agency mortgage-backed securities | 60,742 | 428 | (730 ) | 60,440 |
| U.S. Government agency bonds | 29,946 | 181 | (419 ) | 29,708 |
| Total available-for-sale | $ 104,046 | $ 956 | $ (1,196 ) | $ 103,806 |

(1) Consists of 300 shares of Southern First Bancshares, Inc. cumulative perpetual preferred stock, series T.

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The following tables show the fair value and unrealized loss of securities that have been in unrealized loss positions for less than twelve months and for more than twelve months at September 30, 2014 and June 30, 2014. The table also shows the number of securities in an unrealized loss position for each category of investment security as of the respective dates.

| | Less than 12 Months | | | 12 Months or More | | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Loss | Number in Unrealized Loss (1) | Fair Value | Unrealized Loss | Numb Unrea Loss ( |
| **September 30, 2014** | | | | | | |
| Available for Sale: | | | | | | |
| Certificates of deposit | $ 992 | $ (4) | 2 | $ 494 | $ (4) | |
| Municipal securities | 3,254 | (31) | 9 | — | — | |
| U.S. Government agency mortgage-backed securities | 12,815 | (66) | 17 | 19,417 | (739) | |
| U.S. Government agency bonds | 5,459 | (18) | 7 | 11,626 | (364) | |
| | $ 22,520 | $ (119) | 35 | $ 31,537 | $ (1,107) | |

| | Less than 12 Months | | | 12 Months or More | | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Loss | Number in Unrealized Loss (1) | Fair Value | Unrealized Loss | Numbe in Unreali Loss (1) |
| **June 30, 2014** | | | | | | |
| Available for Sale: | | | | | | |
| Certificates of deposit | $ 1,237 | $ (8) | 5 | $ — | $ — | $ — |
| Municipal securities | 4,263 | (39) | 11 | — | — | — |
| U.S. Government agency mortgage-backed securities | 7,241 | (24) | 6 | 21,464 | (706) | 18 |
| U.S. Government agency bonds | 3,467 | (5) | 3 | 12,574 | (414) | 8 |
| | $ 16,208 | $ (76) | 25 | $ 34,038 | $ (1,120) | 26 |

(1) Actual amounts

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

None of the unrealized losses at September 30, 2014 were recognized into net income for the three months ended September 30, 2014 because the issuer's bonds are of high credit quality, management does not intend to sell and it is likely that management will not be required to sell the securities prior to their anticipated recovery, and the decline in fair value is largely due to changes in interest rates. The fair value of these securities is expected to recover as they approach their maturity date or reset date. None of the unrealized losses at June 30, 2014 were recognized as having other-than-temporary impairments ("OTTI") during the three months ended September 30, 2014.

The Company evaluates securities for OTTI at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. The Company considers the length of time and the extent to which the fair value has been less than cost and the financial condition and near-term prospects of the issuer. Additionally, the Company considers its intent to sell or whether it will be more likely than not it will be required to sell the security prior to the security's anticipated recovery in fair value. In analyzing an issuer's financial condition, the Company may consider whether the securities are issued by the federal Government agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition.

The amortized cost and fair value of debt securities classified available-for-sale at September 30, 2014 and June 30, 2014 by contractual maturity are summarized as follows:

| | September 30, 2014 | | June 30, 2014 | |
|---|---|---|---|---|
| | **Amortized Cost** | **Fair Value** | **Amortized Cost** | **Fair Value** |
| Less than one year | $ 3,998 | $ 4,015 | $ 4,002 | $ 4,029 |
| Due from one to five years | 18,183 | 18,296 | 18,717 | 18,836 |
| Due from five to ten years | 13,211 | 12,961 | 13,297 | 13,047 |
| Due after ten years | 6,115 | 6,003 | 6,997 | 6,842 |
| Mortgage backed securities | 59,520 | 59,042 | 60,742 | 60,440 |
| Total | $ 101,027 | $ 100,317 | $ 103,755 | $ 103,194 |

The following table presents the gross proceeds from sales of securities available-for-sale and held-to-maturity and gains or losses recognized for the three months ended September 30, 2014 and 2013:

| | Three Months Ended | |
|---|---|---|
| | **September 30, 2014** | **September 30, 2013** |
| **Available for Sale:** | | |
| Proceeds | $ 1,501 | $ — |

| | | |
|---|---|---|
| Gross gains | 5 | — |
| Gross losses | — | — |

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

**(4) LOANS**

The components of loans at September 30, 2014 and June 30, 2014 were as follows:

| | September 30, 2014 | June 30, 2014 |
|---|---|---|
| Real estate loans: | | |
| One-to-four family | $ 217,597 | $ 214,735 |
| Multi-family | 253 | 254 |
| Home equity | 214 | 227 |
| Nonresidential | 8,434 | 8,408 |
| Construction and land | 7,902 | 7,661 |
| Total real estate loans | 234,400 | 231,285 |
| Consumer and other loans | 632 | 747 |
| Total loans | 235,032 | 232,032 |
| Net deferred loan fees | (1,263 ) | (1,246 ) |
| Allowance for loan losses | (855 ) | (855 ) |
| Loans, net | $ 232,914 | $ 229,931 |

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The following tables present the activity in the allowance for loan losses for the three months ended September 30, 2014 and 2013 and the balances in the allowance for loan losses and the recorded investment in loans by portfolio segment based on impairment method at September 30, 2014 and 2013:

**Three Months Ended September 30, 2014**

| | Real estate | | | | | | |
|---|---|---|---|---|---|---|---|
| | **One-to-four family** | **Multi-family** | **Home Equity** | **Nonresidential** | **Construction and land** | **Consumer** | **Total** |
| Beginning balance | $ 736 | $ 4 | $ 1 | $ 52 | $ 59 | $ 3 | $ 855 |
| Provision | 35 | — | — | — | (33) | (2) | — |
| Charge-offs | — | — | — | — | — | — | — |
| Recoveries | — | — | — | — | — | — | — |
| Ending balance | $ 771 | $ 4 | $ 1 | $ 52 | $ 26 | $ 1 | $ 855 |
| | | | | | | | |
| **Allowance for loan losses:** | | | | | | | |
| Ending allowance attributed to loans: | | | | | | | |
| Individually evaluated for impairment | $ 45 | $ — | $ — | $ — | $ — | $ — | $ 45 |
| Collectively evaluated for impairment | 726 | 4 | 1 | 52 | 26 | 1 | 810 |
| Total ending allowance balance | $ 771 | $ 4 | $ 1 | $ 52 | $ 26 | $ 1 | $ 855 |
| | | | | | | | |
| **Loans:** | | | | | | | |
| Loans individually evaluated for impairment | $ 1,579 | $ — | $ — | $ — | $ — | $ — | $ 1,579 |
| Loans collectively evaluated for impairment | 216,018 | 253 | 214 | 8,434 | 7,902 | 632 | 233,453 |
| Total ending loans balance | $ 217,597 | $ 253 | $ 214 | $ 8,434 | $ 7,902 | $ 632 | $ 235,032 |

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

**Three Months Ended September 30, 2013**

| | Real estate One-to-four family | Multi-family | Home Equity | Nonresidential | Construction and land | Consumer | Total |
|---|---|---|---|---|---|---|---|
| Beginning balance | $ 665 | $ 4 | $ 1 | $ 52 | $ 27 | $ 2 | $ 751 |
| Provision | 82 | — | — | (2) | 1 | — | 81 |
| Charge-offs | — | — | — | — | — | — | — |
| Recoveries | — | — | — | — | — | — | — |
| Ending balance | $ 747 | $ 4 | $ 1 | $ 50 | $ 28 | $ 2 | $ 832 |
| | | | | | | | |
| **Allowance for loan losses:** | | | | | | | |
| Ending allowance attributed to loans: | | | | | | | |
| Individually evaluated for impairment | $ 110 | $ — | $ — | $ — | $ — | $ — | $ 110 |
| Collectively evaluated for impairment | 637 | 4 | 1 | 50 | 28 | 2 | 722 |
| Total ending allowance balance | $ 747 | $ 4 | $ 1 | $ 50 | $ 28 | $ 2 | $ 832 |
| | | | | | | | |
| **Loans:** | | | | | | | |
| Loans individually evaluated for impairment | $ 3,203 | $ — | $ — | $ — | $ — | $ — | $ 3,203 |
| Loans collectively evaluated for impairment | 202,068 | 256 | 268 | 8,365 | 8,818 | 932 | 220,707 |
| Total ending loans balance | $ 205,271 | $ 256 | $ 268 | $ 8,365 | $ 8,818 | $ 932 | $ 223,910 |

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The following table presents the balances in the allowance for loan losses and the recorded investment in loans by portfolio segment based on impairment method at June 30, 2014:

**June 30, 2014**

| | Real estate | | | | | | |
|---|---|---|---|---|---|---|---|
| | One-to-four family | Multi-family | Home Equity | Nonresidential | Construction and land | Consumer | Total |
| **Allowance for loan losses:** | | | | | | | |
| Ending allowance attributed to loans: | | | | | | | |
| Individually evaluated for impairment | $ 52 | $ — | $ — | $ — | $ — | $ — | $ 52 |
| Collectively evaluated for impairment | 684 | 4 | 1 | 52 | 59 | 3 | 803 |
| Total ending allowance balance | $ 736 | $ 4 | $ 1 | $ 52 | $ 59 | $ 3 | $ 855 |
| **Loans:** | | | | | | | |
| Loans individually evaluated for impairment | $ 1,647 | $ — | $ — | $ — | $ — | $ — | $ 1,647 |
| Loans collectively evaluated for impairment | 213,088 | 254 | 227 | 8,408 | 7,661 | 747 | 230,385 |
| Total ending loans balance | $ 214,735 | $ 254 | $ 227 | $ 8,408 | $ 7,661 | $ 747 | $ 232,032 |

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

The following table presents loans individually evaluated for impairment by portfolio segment at September 30, 2014 and June 30, 2014, including the average recorded investment balance and interest earned for the three months ended September 30, 2014 and year ended June 30, 2014:

| | September 30, 2014 | | | | | June 30, 2014 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **Unpaid Principal Balance** | **Recorded Investment** | **Related Allowance** | **Average Recorded Investment** | **Interest Income Recognized** | **Unpaid Principal Balance** | **Recorded Investment** | **Related Allowance** | **Average Recorded Investment** | **Interest Income Recognized** |
| **With no recorded allowance:** | | | | | | | | | | |
| Real estate loans: | | | | | | | | | | |
| One-to-four family | $ 680 | $ 680 | $ — | $ 527 | $ 4 | $ 374 | $ 374 | $ — | $ 1,054 | $ 8 |
| Multi-family | — | — | — | — | — | — | — | — | — | — |
| Home equity | — | — | — | — | — | — | — | — | — | — |
| Nonresidential | — | — | — | — | — | — | — | — | — | — |
| Construction and land | — | — | — | — | — | — | — | — | — | — |
| Total real estate loans | 680 | 680 | — | 527 | 4 | 374 | 374 | — | 1,054 | 8 |
| Consumer and other loans | — | — | — | — | — | — | — | — | — | — |
| Total | $ 680 | $ 680 | $ — | $ 527 | $ 4 | $ 374 | $ 374 | $ — | $ 1,054 | $ 8 |
| **With recorded allowance:** | | | | | | | | | | |
| Real estate loans: | | | | | | | | | | |
| One-to-four family | $ 899 | $ 899 | $ 45 | $ 1,086 | $ — | $ 1,273 | $ 1,273 | $ 52 | $ 763 | $ 9 |
| Multi-family | — | — | — | — | — | — | — | — | — | — |
| Home equity | — | — | — | — | — | — | — | — | — | — |
| Nonresidential | — | — | — | — | — | — | — | — | — | — |
| Construction and land | — | — | — | — | — | — | — | — | — | — |
| Total real estate loans | 899 | 899 | 45 | 1,086 | — | 1,273 | 1,273 | 52 | 763 | 9 |
| Consumer and other loans | — | — | — | — | — | — | — | — | — | — |
| Total | $ 899 | $ 899 | $ 45 | $ 1,086 | $ — | $ 1,273 | $ 1,273 | $ 52 | $ 763 | $ 9 |
| **Totals:** | | | | | | | | | | |
| Real estate loans | $ 1,579 | $ 1,579 | $ 45 | $ 1,613 | $ 4 | $ 1,647 | $ 1,647 | $ 52 | $ 1,817 | $ 17 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Consumer and other loans | — | — | — | — | — | — | — | — | — | — |
| Total | $ 1,579 | $ 1,579 | $ 45 | $ 1,613 | $ 4 | $ 1,647 | $ 1,647 | $ 52 | $ 1,817 | $ 17 |

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The following table presents the aging of the recorded investment in past due loans at September 30, 2014 and June 30, 2014 by portfolio segment of loans:

**September 30, 2014**

| | 30-59 Days Past Due | 60-89 Days Past Due | 90 Days or More Past Due | Total Past Due | Current | Total Loans | Accruing Loans Past Due 90 Days or More |
|---|---|---|---|---|---|---|---|
| Real estate loans: | | | | | | | |
| One-to-four family | $ 4,396 | $ 1,007 | $ 1,360 | $ 6,763 | $ 210,834 | $ 217,597 | $ — |
| Multi-family | — | — | — | — | 253 | 253 | — |
| Home equity | — | — | — | — | 214 | 214 | — |
| Nonresidential | 13 | — | — | 13 | 8,421 | 8,434 | — |
| Construction and land | — | — | — | — | 7,902 | 7,902 | — |
| Total real estate loans | 4,409 | 1,007 | 1,360 | 6,776 | 227,624 | 234,400 | — |
| Consumer and other loans | — | — | — | — | 632 | 632 | — |
| Total | $ 4,409 | $ 1,007 | $ 1,360 | $ 6,776 | $ 228,256 | $ 235,032 | $ — |

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**June 30, 2014**

| | **30-59 Days Past Due** | **60-89 Days Past Due** | **90 Days or More Past Due** | **Total Past Due** | **Current** | **Total Loans** | **Accruing Loans Past Due 90 Days or More** |
|---|---|---|---|---|---|---|---|
| Real estate loans: | | | | | | | |
| One-to-four family | $ 4,856 | $ 893 | $ 1,053 | $ 6,802 | $ 207,933 | $ 214,735 | $ — |
| Multi-family | — | — | — | — | 254 | 254 | — |
| Home equity | — | — | — | — | 227 | 227 | — |
| Nonresidential | 87 | — | — | 87 | 8,321 | 8,408 | — |
| Construction and land | — | — | — | — | 7,661 | 7,661 | — |
| Total real estate loans | 4,943 | 893 | 1,053 | 6,889 | 224,396 | 231,285 | — |
| Consumer and other loans | — | — | — | — | 747 | 747 | — |
| Total | $ 4,943 | $ 893 | $ 1,053 | $ 6,889 | $ 225,143 | $ 232,032 | $ — |

At September 30, 2014, nonaccrual loans were $ 1,579, of which $ 1,360 are classified in the "90 Days or More" category and $220 were classified in the "60-89 Days Past Due" category. Nonaccrual loans at June 30, 2014 were $1,647. All of these loans are disclosed by portfolio segment above in the "90 days or more past due" column at June 30, 2014, except one loan in the "60-89 days past due" category with a carrying amount of $220 and one loan in the "30-59 days past due" category with a carrying amount of $374. There were no troubled debt restructures at September 30, 2014 or June 30, 2014.

All loans graded pass, special mention, substandard and doubtful not specifically evaluated for impairment are collectively evaluated for impairment by portfolio segment. To develop and document a systematic methodology for determining the portion of the allowance for loan losses for loans evaluated collectively, the Company has divided the loan portfolio into six portfolio segments, each with different risk characteristics and methodologies for assessing risk and utilizes a loan grading system whereby all loans within each portfolio segment are assigned a grade based on the risk profile of each loan. Loan grades are determined based on an evaluation of relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. All loans, regardless of size, are analyzed and assigned a grade based upon management's assessment of the ability of borrowers to service their debts. The following describes each of the Company's loan grades and general information as to the risk profile of each of the Company's loan portfolio segments:

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**Loan Grades:**

Pass: Loans not meeting any of the criteria listed below for special mention, substandard, or doubtful are graded "Pass."

Special Mention: Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of repayment prospects for the loan or of the institution's credit position at some future date.

Substandard: Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful: Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

**Portfolio Segments:**

One-to-four family: One-to-four family residential loans consist primarily of loans secured by first or second deeds of trust on primary residences, and are originated as adjustable-rate or fixed-rate loans for the construction, purchase or refinancing of a one-to-four family residence. These loans are collateralized by owner-occupied properties located in the Company's market area. We currently originate residential mortgage loans for our portfolio with loan-to-value ratios of up to 80% for traditional owner-occupied homes.

Multi-family: Multi-family real estate loans generally have a maximum term of 5 years with a 30 year amortization period and a final balloon payment and are secured by properties containing five or more units in the Company's market area. These loans are generally made in amounts of up to 75% of the lesser of the appraised value or the purchase price of the property with an appropriate projected debt service coverage ratio. The Company's underwriting analysis includes considering the borrower's expertise and requires verification of the borrower's credit history, income and financial statements, banking relationships, independent appraisals, references and income projections for the property. The Company generally obtains personal guarantees on these loans.

Multi-family real estate loans generally present a higher level of risk than loans secured by one-to-four family residences. This greater risk is due to several factors, including the concentration of principal in a limited number of loans and borrowers, the effects of general economic conditions on income-producing properties and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by multi-family residential real estate is typically dependent upon the successful operation of the related real estate project.

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Home Equity: We originate fixed-rate home equity loans secured by a lien on the borrower's primary residence but only where we hold the first mortgage on the property. Our home equity loans are limited to an 80% loan-to-value ratio (including all prior liens), and have terms of up to 10 years with 10-year amortization periods. We use the same underwriting standards for home equity loans as we use for one- to four-family residential mortgage loans.

Nonresidential Real Estate: Our non-residential real estate loans are secured primarily by churches and, to a much lesser extent, office buildings, and retail and mixed-use properties located in our primary market area. The non-residential real estate loans that we originate generally have maximum terms of 5 years with amortization periods of 30 years. For loans secured by church property, our loans generally have maximum terms of 20 years with amortization periods of up to 20 years. The maximum loan-to-value ratio of our non-residential real estate loans is generally 75%.

Loans secured by non-residential real estate generally are larger than one- to four-family residential loans and involve greater credit risk. Non-residential real estate loans often involve large loan balances to single borrowers or groups of related borrowers. Repayment of these loans depends to a large degree on the results of operations and management of the properties securing the loans or the businesses conducted on such property, and may be affected to a greater extent by adverse conditions in the real estate market or the economy in general, including the current adverse conditions. In addition, because a church's financial stability often depends on donations from congregation members, some of whom may not reside in our market area, rather than income from business operations, repayment may be affected by economic conditions that affect individuals located both in our market area and in other market areas with which we are not as familiar. In addition, due to the unique nature of church buildings and properties, the real estate securing church loans may be less marketable than other non-residential real estate.

Construction and Land: We make construction loans to individuals for the construction of their primary residences and interim construction loans for non-residential properties. These loans generally have maximum terms of eight months, and upon completion of construction convert to conventional amortizing mortgage loans. These construction loans have rates and terms comparable to one- to four-family residential mortgage loans that we originate. During the construction phase, the borrower generally pays interest only. The maximum loan-to-value ratio of our owner-occupied construction loans is 80%. Residential construction loans are generally underwritten pursuant to the same guidelines used for originating permanent residential mortgage loans. Finally, we make loans secured by land to complement our construction and non-residential lending activities. These loans have terms of up to 10 years, and maximum loan-to-value ratios of 75% for improved lots and 65% for unimproved land.

To the extent our construction loans are not made to owner-occupants of single-family homes, they are more vulnerable to changes in economic conditions and the concentration of credit with a limited number of borrowers. Further, the nature of these loans is such that they are more difficult to evaluate and monitor. Our risk of loss on a construction or land loan is dependent largely upon the accuracy of the initial estimate of the property's value upon completion of the project and the estimated cost (including interest) of the project. If the estimate of value proves to be inaccurate, we may be confronted, at or prior to the maturity of the loan, with a project with a value which is insufficient to assure full repayment and/or the possibility of having to make substantial investments to complete and sell the project.  Because defaults in repayment may not occur during the construction period, it may be difficult to identify problem loans at an early stage.

Consumer and Other Loans:  We offer installment loans for various consumer purposes, including the purchase of automobiles, boats, appliances and recreational vehicles, and for other legitimate personal purposes.  The maximum terms of consumer loans is 18 months for unsecured loans, 12 months for loans secured by marketable securities and 18-60 months for loans secured by a vehicle, depending on the age of the vehicle.  We generally only extend consumer loans to existing customers or their immediate family members, and these loans generally have relatively low limits.

Consumer loans may entail greater credit risk than residential mortgage loans, particularly in the case of consumer loans that are unsecured or are secured by rapidly depreciable assets, such as automobiles.  In addition, consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be affected by adverse personal circumstances.  Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount which can be recovered on such loans.

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At September 30, 2014 and June 30, 2014, and based on the most recent analyses performed, the loan grade for each loan by portfolio segment is as follows:

| | Real estate | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | One-to-four family | | Multi-family | | Home Equity | | Nonresidential | |
| | September 30, 2014 | June 30, 2014 | September 30, 2014 | June 30, 2014 | September 30, 2014 | June 30, 2014 | September 30, 2014 | June 30, 2014 |
| Pass | $ 216,018 | $ 213,087 | $ 253 | $ 254 | $ 214 | $ 227 | $ 8,434 | $ 8,408 |
| Special mention | — | — | — | — | — | — | — | — |
| Substandard | 1,579 | 1,648 | — | — | — | — | — | — |
| Total | $ 217,597 | $ 214,735 | $ 253 | $ 254 | $ 214 | $ 227 | $ 8,434 | $ 8,408 |

| | Real estate | | | | | |
|---|---|---|---|---|---|---|
| | Construction and Land | | Consumer | | Total | |
| | September 30, 2014 | June 30, 2014 | September 30, 2014 | June 30, 2014 | September 30, 2014 | June 30, 2014 |
| Pass | $ 7,902 | $ 7,661 | $ 632 | $ 747 | $ 233,453 | $ 230,384 |
| Special mention | — | — | — | — | — | — |
| Substandard | — | — | — | — | 1,579 | 1,648 |
| Total | $ 7,902 | $ 7,661 | $ 632 | $ 747 | $ 235,032 | $ 232,032 |

Loans were evaluated for appropriate risk ratings as of September 30, 2014 on October 6, 2014.

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## (5) FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Investment Securities:

The fair values for investment securities are determined by quoted market prices, if available (Level 1). For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3). The Company's preferred stock investments are not actively traded; therefore, management estimates the fair value of its preferred stock using estimations provided by external dealer quotes.

Impaired Loans:

The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value.

Real estate owned:

Nonrecurring adjustments to certain commercial and residential real estate properties classified as real estate owned are measured at the lower of carrying amount or fair value, less costs to sell. Fair values are generally based on third party appraisals of the property, resulting in a Level 3 classification. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized.

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Assets and liabilities measured at fair value on a recurring basis at September 30, 2014 and June 30, 2014 are summarized below:

| | Fair Value Measurements | |
|---|---|---|
| | **(Level 2)** | **(Level 2)** |
| | **September 30, 2014** | **June 30, 2014** |
| Financial assets: | | |
| Securities available-for-sale | $ 100,830 | $ 103,806 |
| Total financial assets | $ 100,830 | $ 103,806 |

Presented in the table below are assets measured at fair value on a non-recurring basis using level 3 inputs at September 30, 2014 and June 30, 2014:

| | Fair Value Measurements | |
|---|---|---|
| | **(Level 3)** | **(Level 3)** |
| | **September 30, 2014** | **June 30, 2014** |
| Financial assets: | | |
| Impaired real estate loans, with specific allocations: | | |
| One-to-four-family | $ 899 | $ 1,221 |
| | | |
| Non-financial assets: | | |
| Real estate owned, net: | | |
| One-to-four-family | 596 | 744 |
| Total non-financial assets | 596 | 744 |
| Total assets measured at fair value on a non-recurring basis | $ 1,495 | $ 1,965 |

The Company's impaired loans at September 30, 2014 and June 30, 2014, which were measured for impairment using the fair value of collateral less costs to sell, had carrying amounts of $899 and $1,221, respectively. The carrying value included a valuation allowance of $45 and $52, respectively. The impact to the provision to loan losses from the change in the valuation allowance for the three months ended September 30, 2014 was a decrease of $7.

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Real estate owned is carried at the lower of carrying value or fair value less costs to sell. The outstanding balances of real estate owned and their respective valuation allowances at September 30, 2014 and June 30, 2014 were $ 596 and $80 and $ 744 and $164, respectively. There were no write downs of real estate owned for the three months ended September 30, 2014.

The table below presents the valuation methodology and unobservable inputs for Level 3 assets measured at fair value on a non-recurring basis at September 30, 2014 and June 30, 2014.

| | Level 3 Quantitative Information | | | | |
|---|---|---|---|---|---|
| | **September 30, 2014 Fair Value** | **June 30, 2014 Fair Value** | **Valuation Technique** | **Unobservable Inputs** | **R (We Av** |
| Impaired real estate loans net, with specific allocations: | | | | | |
| One-to-four family | $ 899 | $ 1,221 | Sales comparison approach | Adjustment for differences between the comparable sales | 0% t (15% |
| Real estate owned: | | | | | |
| One-to-four family | $ 596 | $ 744 | Sales comparison approach | Adjustment for differences between the comparable sales | 0% t (10% |

Many of the Company's assets and liabilities are short-term financial instruments whose carrying amounts reported in the consolidated balance sheet approximate fair value. These items include cash and cash equivalents, accrued interest receivable and payable balances, variable rate loan and deposits that re-price frequently and fully. The estimated fair values of the Company's remaining on-balance sheet financial instruments at September 30, 2014 and June 30, 2014 are summarized below:

| September 30, 2014 | | | | |
|---|---|---|---|---|
| **Carrying Amount** | **Fair Value (Level 1)** | **(Level 2)** | **(Level 3)** | **Total** |

| | Carrying Amount | (Level 1) | (Level 2) | (Level 3) | Total |
|---|---|---|---|---|---|
| Financial assets | | | | | |
| Securities available-for-sale | $ 100,830 | $ — | $ 100,830 | $ — | $ 100,830 |
| Loans, net | 232,914 | — | — | 237,488 | 237,488 |
| Restricted equity securities (1) | 325 | N/A | N/A | N/A | N/A |
| | | | | | |
| Financial liabilities | | | | | |
| Deposits | $ 277,948 | $ 81,650 | $ 196,674 | $ — | $ 278,324 |

| | June 30, 2014 | | | | |
|---|---|---|---|---|---|
| | Carrying | Fair Value | | | |
| | Amount | (Level 1) | (Level 2) | (Level 3) | Total |
| Financial assets | | | | | |
| Securities available-for-sale | $ 103,806 | $ — | $ 103,806 | $ — | $ 103,806 |
| Loans, net | 229,931 | — | — | 233,176 | 233,176 |
| Restricted equity securities (1) | 325 | N/A | N/A | N/A | N/A |
| | | | | | |
| Financial liabilities | | | | | |
| Deposits | $ 281,015 | $ 80,904 | $ 200,662 | $ — | $ 281,566 |

(1) It was not practicable to determine fair value of restricted equity securities due to restrictions placed on transferability.

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**(6) EMPLOYEE STOCK OWNERSHIP PLAN**

Employees participate in an Employee Stock Ownership Plan ("ESOP"). The ESOP borrowed from the Company to purchase 248,842 shares of the Company's common stock at $ 10 per share during 2011. The Company makes discretionary contributions to the ESOP, and pays dividends on unallocated shares to the ESOP, and the ESOP uses funds it receives to repay the loan. When loan payments are made, ESOP shares are allocated to participants based on relative compensation and expense is recorded. Dividends on allocated shares increase participant accounts.

Participants receive the shares at the end of employment. No contributions to the ESOP were made during the three months ended September 30, 2014. ESOP compensation expense recognized for the three months ended September 30, 2014 and 2013 was $77 and $ 67, respectively.

Shares held by the ESOP at September 30, 2014 and June 30, 2014 were as follows:

| | September 30, 2014 | June 30, 2014 |
|---|---|---|
| Committed to be released to participants | 14,195 | 9,464 |
| Allocated to participants | 57,902 | 57,902 |
| Unearned | 176,745 | 181,476 |
| Total ESOP shares | 248,842 | 248,842 |
| | | |
| Fair value of unearned shares | $ 3,269,783 | $ 3,277,457 |

**(7) STOCK BASED COMPENSATION**

On April 5, 2012, the shareholders of Oconee Federal Financial Corp. approved the Oconee Federal Financial Corp. 2012 Equity Incentive Plan (the "Plan") for employees and directors of the Company. The Plan authorizes the issuance of up to 435,472 shares of the Company's common stock, with no more than 124,420 of shares as restricted stock awards and 311,052 as stock options, either incentive stock options or non-qualified stock options. The exercise price of options granted under the Plan may not be less than the fair market value on the date the stock option is granted. The compensation committee of the board of directors has sole discretion to determine the amount and to whom equity incentive awards are granted.

On April 27, 2012, the compensation committee of the board of directors approved the issuance of 62,208 stock options to purchase Company stock and 24,884 shares of restricted stock to its directors. In addition, a total of 171,078 stock options and 62,210 shares of restricted stock were granted to officers. Stock options and restricted stock have vesting periods of 5 years or 7 years, a percentage of which vests annually on each anniversary date of grant. The weighted average vesting period of stock options and restricted stock granted was 5.7 years and 5.6 years, respectively. Stock options expire ten years after issuance. Apart from the vesting schedule for both stock options and restricted stock, there are no performance-based conditions or any other material conditions applicable to the awards issued.

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On November 13, 2013, the compensation committee of the board of directors approved the issuance of 7,700 stock options to purchase Company stock and 12,600 shares of restricted stock to one of the Company's officers. Stock options and restricted stock have vesting periods of 7 years, a percentage of which and vests annually at each anniversary date of grant. Stock options expire ten years after issuance. Apart from the vesting schedule for both stock options and restricted stock, there are no performance-based conditions or any other material conditions applicable to the awards issued.

The following table summarizes stock option activity for the three months ended September 30, 2014:

| | **Options** | **Weighted-Average Exercise Price/Share** | **Weighted-Average Remaining Contractual Life (in years)** | **Aggregate Intrinsic Value (1)** |
|---|---|---|---|---|
| Outstanding - July 1, 2014 | 240,986 | $ 11.58 | | |
| Granted | — | — | | |
| Exercised | — | — | | |
| Forfeited | — | — | | |
| Outstanding - September 30, 2014 | 240,986 | $ 11.58 | 7.62 | $ 1,667,623 |
| Fully vested and exercisable at September 30, 2014 | 84,428 | $ 11.58 | 7.62 | $ 584,242 |
| Expected to vest in future periods | 156,558 | | | |
| Fully vested and expected to vest - September 30, 2014 | 240,986 | $ 11.58 | 7.62 | $ 1,667,623 |

(1) The intrinsic value for stock options is defined as the difference between the current market value and the exercise price. The current market price was based on the closing price of common stock of $18.50 per share on September 30, 2014

The fair value for each option grant is estimated on the date of grant using the Black-Scholes-Merton option pricing model that uses the following assumptions. The Company uses the U.S. Treasury yield curve in effect at the time of the grant to determine the risk-free interest rate. The expected dividend yield is estimated using the projected annual dividend level and recent stock price of the Company's common stock at the date of grant. Expected stock volatility is based on historical volatilities of the SNL Financial Index of Thrifts. The expected life of the options is calculated based on the "simplified" method as provided for under Staff Accounting Bulletin No.110.

The weighted-average fair value of options granted and assumptions used in the Black-Scholes-Merton option pricing model in the fiscal years granted are listed below:

| | Fiscal Years Granted | |
|---|---|---|
| | **2014** | **2012** |
| Risk-free interest rate | 2.32 % | 1.54 % |
| Expected dividend yield | 2.33 % | 3.45 % |
| Expected stock volatility | 15.5 | 15.3 |
| Expected life (years) | 8 | 8 |
| Fair value | $ 2.46 | $ 1.00 |

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Stock options are assumed to be earned ratably over their respective vesting periods and charged to compensation expense based upon their grant date fair value and the number of options assumed to be earned. There were 11,332 and 10,640 options that were earned during the three months ended September 30, 2014 and 2013, respectively. Stock-based compensation expense for stock options for the three months ended September 30, 2014 and 2013 was $11 and $10, respectively. Total unrecognized compensation cost related to stock options was $144 at September 30, 2014 and is expected to be recognized over a weighted-average period of 3.3 years.

The following table summarizes non-vested restricted stock activity for the three months ended September 30, 2014:

| | **September 30, 2014** |
|---|---|
| Balance - beginning of year | 67,699 |
| Granted | — |
| Forfeited | — |
| Vested | — |
| Balance - end of period | 67,699 |
| Weighted average grant date fair value | $ 12.29 |

The fair value of the restricted stock awards is amortized to compensation expense over their respective vesting periods and is based on the market price of the Company's common stock at the date of grant multiplied by the number of shares granted that are expected to vest. The weighted-average grant date fair value of restricted stock granted on April 27, 2012 was $11.58 per share or $1,009. The weighted-average grant date fair value of restricted stock granted on November 13, 2013 was $17.16 per share or $216. Stock-based compensation expense for restricted stock included in noninterest expense for the three months ended September 30, 2014 and 2013 was $55 and $47, respectively. Unrecognized compensation expense for nonvested restricted stock awards was $734 at September 30, 2014 and is expected to be recognized over a weighted-average period of 3.5 years.

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OCONEE FEDERAL FINANCIAL CORP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Amounts in thousands, except share and per share data)

**(8) SUPPLEMENTAL CASH FLOW INFORMATION**

Supplemental cash flow information for the three months ended September 30, 2014 and 2013:

| | September 30, 2014 | September 30, 2013 |
|---|---|---|
| Cash paid during the period for: | | |
| Interest paid | $ 309 | $ 430 |
| Income taxes paid | $ 100 | $ 200 |
| Supplemental noncash disclosures: | | |
| Transfers from loans to real estate owned | $ 59 | $ — |
| Unrealized gains (losses) on securities available-for-sale, net | $ (154 ) | $ (6 ) |

**(9) MERGER**

On February 26, 2014, the Company, the Association and Oconee Federal, MHC ("Oconee MHC"), the Company's parent, and Stephens Federal Bank, a federally chartered mutual savings bank ("Stephens Federal"), entered into a definitive merger agreement (as amended, the "Merger Agreement"). On May 6, 2014, the Merger Agreement was amended to change the contemplated structure of the Merger Agreement. The Merger Agreement's terms stipulate that Stephens Federal will undergo a full Supervisory Conversion from a federally chartered mutual savings association to a federally chartered stock savings association. Concurrent with the Supervisory Conversion, Stephens Federal will merge with and into the Association with the Association as the surviving institution (the "Merger"), and the separate existence of Stephens Federal will cease. Additionally, at the time of the Merger, the Company will issue to Oconee MHC a number of shares of the Company's common stock equal to the quotient of (i) the Valuation of Stephens Federal as prepared by an independent third party, *divided by* (ii) the average of the closing sales price of a share of the Company's common stock, as reported on the Nasdaq stock market, for the twenty (20) consecutive trading days ending on the second trading day preceding the effective time of the Merger, and each share of the common stock of Stephens Federal issued pursuant to the Supervisory Conversion and outstanding immediately prior to the Effective Time shall cease to be outstanding and shall immediately be canceled and retired and cease to exist.

The Office of the Comptroller of Currency (the "OCC") approved Stephens Federal's application for Supervisory Conversion on August 29, 2014 and our application for Merger on September 3, 2014. The Federal Reserve Board approved our application to acquire Stephens Federal on September 9, 2014. The Supervisory Conversion approval requires the Supervisory Conversion to be completed by September 29, 2014, and the Merger approval requires the Merger to be completed by December 9, 2014.

On October 24, 2014, the OCC approved Stephen Federal's request for an extension to December 9, 2014 to consummate the Supervisory Conversion. We expect to close the Merger on or before that date. Based on preliminary estimates, the Merger is expected to increase total assets by approximately $150 million, although final amounts are subject to change.  The Merger will be accounted for as an acquisition of a business using acquisition accounting, which requires that all identifiable assets and liabilities to be recorded at fair value, including any intangible assets and liabilities.

**(10) SUBSEQUENT EVENTS**

On October 23, 2014, the Board of Directors of Oconee Federal Financial Corp. (the “Company”) declared a quarterly cash dividend of $0.10 per share of the Company’s common stock. The dividend is payable to stockholders of record as of November 6, 2014, and will be paid on or about November 20, 2014.

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

This Quarterly Report contains forward-looking statements, which can be identified by the use of such words as estimate, project, believe, intend, anticipate, plan, seek, expect and similar expressions. These forward-looking statements include:

- statements of our goals, intentions and expectations;
- statements regarding our business plans and prospects and growth and operating strategies;
- statements regarding the asset quality of our loan and investment portfolios; and
- estimates or our risks and future costs and benefits.

These forward-looking statements are based on our current beliefs and expectations and are inherently subject to significant business, economic, and competitive uncertainties and contingencies, many of which are beyond our control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change. We are under no duty to and do not take any obligation to update any forward-looking statements after the date of this Quarterly Report.

The following factors, among others, could cause actual results to differ materially from the anticipated results or other expectations expressed in the forward-looking statements:

- our ability to manage our operations under the current adverse economic conditions (including real estate values, loan demand, inflation, commodity prices and employment levels) nationally and in our market areas;
- adverse changes in the financial industry, securities, credit and national and local real estate markets (including real estate values);
- significant increases in our delinquencies and loan losses, including as a result of our inability to resolve classified assets, changes in the underlying cash flows of our borrowers, and management's assumptions in determining the adequacy of the allowance for loan losses;
- credit risks of lending activities, including changes in the level and trend of loan delinquencies and write-offs and in our allowance and provision for loan losses;
- use of estimates for determining the fair value of certain of our assets, which may prove to be incorrect and result in significant declines in valuations;
- increased competition among depository and other financial institutions;
- our ability to attract and maintain deposits, including attracting and maintaining deposits and introducing new deposit products;
- changes in interest rates generally, including changes in the relative differences between short term and long term interest rates and in deposit interest rates, that may affect our net interest margin and funding sources;

- fluctuations in the demand for loans, which may be affected by the number of unsold homes, land and other properties in our market areas and by declines in the value of real estate in our market area;

- declines in the yield on our assets resulting from the current low interest rate environment;

- our ability to successfully implement our business strategies, including attracting and maintaining deposits and introducing new financial products;

- risks related to high concentration of loans secured by real estate located in our market areas;

- changes in the level of government support of housing finance;

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- the results of examinations by our regulators, including the possibility that our regulators may, among other things, require us to increase our reserve for loan losses, write down assets, change our regulatory capital position, limit our ability to borrow funds or maintain or increase deposits, or prohibit us from paying dividends, which could adversely affect our dividends and earnings;

- our ability to enter new markets successfully and capitalize on growth opportunities;

- our businesses may not be combined successfully, or such combination may take longer to accomplish than expected;

- the growth opportunities and cost savings from the acquisition of Stephens Federal may not be fully realized or may take longer to realize than expected;

- our ability to manage increased expenses following the acquisition of Stephens Federal, including salary and employee benefit expenses and occupation expenses;

- operating costs, customer losses and business disruption following the acquisition of Stephens Federal, including adverse effects of relationships with employees, may be greater than expected;

- our ability to attract and maintain deposits, including former depositors of Stephens Federal;

- changes in laws or government regulations or policies affecting financial institutions, including the Dodd-Frank Act and the JOBS Act, which could result in, among other things, increased deposit insurance premiums and assessments, capital requirements (particularly the new capital regulations), regulatory fees and compliance costs and the resources we have available to address such changes;

- our reliance on a small executive staff;

- changes in our compensation and benefit plans, and our ability to retain key members of our senior management team and to address staffing needs to implement our strategic plan;

- changes in consumer spending, borrowing and savings habits;

- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board, the Securities and Exchange Commission and the Public Company Accounting Oversight Board;

- our ability to control costs and expenses, particularly those related to operating as a publicly traded company;

- other changes in our financial condition or results of operations that reduce capital available to pay dividends;

- other changes in the financial condition or future prospects of issuers of securities that we own, including our stock in the FHLB of Atlanta; and

- other economic, competitive, governmental, regulatory and operational factors affecting our operations, pricing, products and services.

Because of these and a wide variety of other uncertainties, our actual future results may be materially different from the results indicated by these forward-looking statements.

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**Critical Accounting Policies**

There are no material changes to the critical accounting policies disclosed in the Annual Report on Form 10-K for Oconee Federal Financial Corp. for the year ended June 30, 2014, as filed with the Securities and Exchange Commission.

**Comparison of Financial Condition at September 30, 2014 and June 30, 2014**

Our total assets decreased by $3.4 million, or 0.9%, to $357.1 million at September 30, 2014 from $360.5 million at June 30, 2014. The decrease is primarily reflective of a decrease in total cash and cash equivalents of $3.6 million, or 30.3%, to $8.3 million at September 30, 2014 from $11.9 million at June 30, 2014. The decrease in total cash and cash equivalents is primarily reflective of the decrease in total deposits of $3.1 million, or 1.1%, to $277.9 million at September 30, 2014 from $281.0 million at June 30, 2014. Total equity increased $450 thousand, or 0.6%, to $77.4 million at September 30, 2014 compared to $76.9 million at June 30, 2014.

Total gross loans increased by $3.0 million, or 1.3%, to $235.0million at September 30, 2014 from $232.0 million at June 30, 2014. Our one-to-four family real estate loans increased by $2.9 million, or 1.3%, to $217.6 million at September 30, 2014 from $214.7million at June 30, 2014. Construction and land loans increased by $241 thousand, or 3.1%, to $7.9 million at September 30, 2014 from $7.7 million at June 30, 2014. These increases are a reflection of an increased demand in our market for one-to-four family residential real estate loans, resulting from modest improvements in the economy and competitive rates that we offer on these one-to-four family loan products. The Oconee County area remains a very attractive market for second home and retirement home construction and purchases.

Deposits decreased by $3.1 million, or 1.1%, to $277.9 million at September 30, 2014 from $281.0 million at June 30, 2014. The decrease was primarily attributed to a decrease in interest bearing deposit accounts of $4.4 million, or 1.6%, offset partially by an increase in non-interest bearing deposits of $1.3 million, or 18.2%. The decline in interest bearing deposits, primarily our certificates of deposits, is reflective of depositors moving their deposits into higher yielding investments in the market. Oconee Federal, MHC’s cash is held on deposit with the Company. We generally do not accept brokered deposits and no brokered deposits were accepted during the three months ended September 30, 2014.

We had no advances from the Federal Home Loan Bank of Atlanta as of September 30, 2014 or June 30, 2014. We have credit available under a loan agreement with the Federal Home Loan Bank of Atlanta in the amount of 11% of total assets (as of September 30, 2014), or approximately $39.6 million.

Total equity increased $450 thousand, or 0.6%, to $77.4 million at September 30, 2014 compared to $76.9 million at June 30, 2014. The increase in total equity is primarily reflective of net income of $1.0 million, net of dividends paid of $583 thousand and net accumulated other comprehensive loss of $154 thousand for the three months ended September 30, 2014. Additionally, total equity increased $143 thousand from the recognition of compensation related expenses associated with the ESOP and equity compensation plans for the three months ended September 30, 2014.

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**Nonperforming Assets**

The table below sets forth the amounts and categories of our nonperforming assets at the dates indicated.

| | September 30, 2014 | June 30, 2013 |
|---|---|---|
| | (Dollars in thousands) | |
| Nonaccrual loans: | | |
| Real estate loans: | | |
| One-to-four family | $ 1,579 | $ 1,647 |
| Multi-family | — | — |
| Home equity | — | — |
| Non-residential | — | — |
| Construction and land | — | — |
| Total real estate loans | 1,579 | 1,647 |
| Consumer and other loans | — | — |
| Total nonaccrual loans | $1,579 | $ 1,647 |
| Accruing loans past due 90 days or more: | | |
| Real estate loans: | | |
| One-to-four family | $ — | $ — |
| Multi-family | — | — |
| Home equity | — | — |
| Non-residential | — | — |
| Construction and land | — | — |
| Total real estate loans | — | — |
| Consumer and other loans | — | — |
| Total accruing loans past due 90 days or more | — | — |
| Total of nonaccrual and 90 days or more past due loans | $ 1,579 | $ 1,647 |
| Real estate owned, net: | | |
| One-to-four family | $ 596 | $ 744 |
| Multi-family | — | — |
| Home equity | — | — |
| Non-residential | — | — |
| Other | — | — |
| Other nonperforming assets | — | — |
| Total nonperforming assets | $ 2,175 | $ 2,391 |
| Troubled debt restructurings | — | — |
| Troubled debt restructurings and total nonperforming assets | $ 2,175 | $ 2,391 |
| | | |
| Total nonperforming loans to total loans | 0.67% | 0.71% |
| Total nonperforming assets to total assets | 0.61% | 0.66% |
| Total nonperforming assets to loans and real estate owned | 0.92% | 1.03% |

Interest income that would have been recorded had our non-accruing loans been current in accordance with their original terms was $28 thousand and $68 thousand for the three months ended September 30, 2014 and 2013, respectively. Interest of $4 thousand and $16 thousand was recognized on these loans and is included in net income for the three months ended September 30, 2014 and 2013, respectively.

The decrease in the ratio of nonperforming loans to total loans is a reflection of a decrease of $68 thousand, or 4.1%, in nonperforming loans to $1.6 million at September 30, 2014. This decrease is a reflection of improvements in the credit quality of our loan portfolio. All nonperforming loans, regardless of size, are evaluated by management for impairment. In cases where there is more than one loan under the same relationship, all loans within that relationship are evaluated for impairment. Therefore, total impaired loans may exceed total nonperforming loans. Additionally, any loan or loan relationship exhibiting signs of potential impairment are evaluated for impairment, even if those loans are currently performing.

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**Analysis of Net Interest Margin**

The following tables set forth average balance sheets, average yields and rates, and certain other information at and for the periods indicated. No tax-equivalent yield adjustments were made, as the effect thereof was not material. All average balances are daily average balances. Nonaccrual loans were included in the computation of average balances, but have been reflected in the tables as loans carrying a zero yield. The yields set forth below include the effect of net deferred costs, discounts and premiums that are amortized or accreted to income.

| | For the Three Months Ended | | | | | |
|---|---|---|---|---|---|---|
| | September 30, 2014 | | | September 30, 2 | | |
| | Average Balance | Interest and Dividends | Yield/ Cost | Average Balance | Interest and Dividends | Y |
| | (Dollars in Thousands) | | | | | |
| **Assets:** | | | | | | |
| Interest-earning assets: | | | | | | |
| Loans | $233,035 | $2,886 | 4.95% | $221,611 | $2,852 | |
| Investment securities, taxable | 97,122 | 381 | 1.57 | 99,060 | 371 | |
| Investment securities, tax-free | 5,911 | 36 | 2.44 | — | — | |
| Interest-bearing deposits and other | 12,726 | 7 | 0.22 | 31,178 | 15 | |
| Total interest-earning assets | 348,794 | 3,310 | 3.80 | 351,849 | 3,238 | |
| Noninterest-earning assets | 9,499 | | | 15,022 | | |
| Total assets | $358,293 | | | $366,871 | | |
| **Liabilities and equity:** | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| NOW and demand deposits | $ 18,184 | $ 4 | 0.09% | $ 18,872 | $ 3 | |
| Money market deposits | 12,605 | 6 | 0.20 | 12,271 | 6 | |
| Regular savings and other deposits | 42,362 | 38 | 0.35 | 39,391 | 38 | |
| Certificates of deposit | 198,946 | 260 | 0.52 | 215,474 | 382 | |
| Total interest-bearing deposits | 272,097 | 308 | 0.45 | 286,008 | 429 | |
| Total interest-bearing liabilities | 272,097 | | | 286,008 | | |
| Noninterest bearing deposits | 7,450 | | | 3,781 | | |
| Other noninterest-bearing liabilities | 1,700 | | | 1,416 | | |
| Total liabilities | 281,247 | | | 291,205 | | |
| Equity | 77,046 | | | 75,666 | | |
| Total liabilities and equity | $358,293 | | | $366,871 | | |
| Net interest income | | $3,002 | | | $2,809 | |
| Interest rate spread | | | 3.35% | | | |
| Net interest margin | | | 3.44% | | | |
| Average interest-earning assets to average interest-bearing liabilities | 1.28 X | | | 1.23 X | | |

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**Comparison of Operating Results for the Three Months Ended September 30, 2014 and September 30, 2013**

***General.*** We recognized net income of $1.0 million for the three months ended September 30, 2014 as compared to net income of $919 thousand for the three months ended September 30, 2013. The $125 thousand increase was primarily attributable to an increase in net interest income after the provision for loan losses of $274 thousand, offset partially by an increases in noninterest expense of $99 thousand and income tax expense of $51 thousand for the three months ended September 30, 2014.

***Interest Income.*** Interest income increased by $72 thousand, or 2.2%, to $3.3 million for the three months ended September 30, 2014 from $3.2 million for the three months ended September 30, 2013. The increase reflected an increase on the yield of interest-earning assets of 12 basis points to 3.80% for the three months ended September 30, 2014 as compared to 3.68% for the three months ended September 30, 2013. The increase in yield offset the decrease in the average balance of interest-earning assets of $3.1 million to $348.8 million from $351.8 million. The overall increase in yield is a reflection of the shift in investment from lower interest yielding interest-bearing deposits and other to higher yielding investment securities and loans. The average balance of interest-bearing deposits decreased $18.4 million, or 59.2%, to $12.7 million for the three months September 30, 2014 from $31.2 million at September 30, 2013. The average balances of loans and investment securities increased to $233.0 million and $103.0 million, respectively, for the three months ended September 30, 2014 from $221.6 million and $99.1 million, respectively, for the three months ended September 30, 2013.

Interest income on loans increased by $34 thousand, or 1.2%, to $2.9 million for the three months ended September 30, 2014 from $2.8 million for the three months ended September 30, 2013. The slight increase reflected an increase of $11.4 million, or 5.1%, in average balance of loans to $233.0 million for the three months ended September 30, 2014 from $221.6 million for the three months ended September 30, 2013, offset partially by a decrease in the yield on loans of 20 basis points to 4.95% from 5.15% for the same periods ended. Interest income on investment securities increased by $46 thousand, or 12.4%, to $417 thousand for the three months ended September 30, 2014 from $371 thousand for the three months ended September 30, 2013. The increase reflected an increase in the average balance of securities of $4.0 million, or 4.01%, to $103.0 million for the three months ended September 30, 2014 from $99.1 million for the three months ended September 30, 2013 and an increase of 8 basis points in the yield on securities to 1.58% from 1.50%. The increase in average balances of our investment securities is reflective of our efforts to continue to invest in high-quality investment securities during this period of low loan demand.

***Interest Expense.*** Interest expense decreased $121 thousand, or 28.2%, to $308 thousand for the three months ended September 30, 2014 from $429 thousand for the three months ended September 30, 2013. The decrease reflected a decrease of 15 basis points in the average rate paid on deposits for the three months ended September 30, 2014 to 0.45% from 0.60% for the three months ended September 30, 2013 and a decrease in the average balances of interest-bearing deposits of $13.9 million, or 4.9%, to $272.1million for the three months ended September 30, 2014 from $286.0 million for the three months ended September 30, 2013. The largest decrease in interest expense came from certificates of deposit, which decreased $122 thousand, or 31.9%, to $260 thousand for the three months ended September 30, 2014 from $382 thousand for the same period in 2013. The decrease is reflective of a decrease of $16.5 million, or 7.7%, in the average balance of certificates of deposit to $198.9 million for the three months ended September 30, 2014 from $215.5 million for the three months ended September 30, 2013 and a decrease of 18 basis points in the average rate paid on such deposits to 0.52% from 0.70% for the same periods ended.

***Net Interest Income.*** Net interest income before the provision for loan losses increased by $193 thousand, or 6.9%, to $3.0 million for the three months ended September 30, 2014from $2.8 million for the three months ended September 30, 2012. Our interest rate spread and net interest margin for the three months ended September 30, 2014 increased to 3.35% and 3.44%, respectively, from 3.09% and 3.19%, respectively, for the three months ended September 30, 2013.

The increase in interest rate spread and net interest margin are reflective of both higher yields on interest-earning assets and lower cost of funds on interest-bearing liabilities.

***Provision for Loan Losses.*** We recorded no provision for loan losses for the three months ended September 30, 2014, compared with a provision of $81 thousand for the three months ended September 30, 2013. There were no charges offs recorded for the three months ended September 30, 2014 or the three months ended September 30, 2013. We recorded no provision for the three months ended September 30, 2014 due to continued high credit quality within our loan portfolio as can be evidenced by improved credit quality metrics. Our nonperforming loans to total loans and nonperforming assets to total assets were 0.67% and 0.61%, respectively, at September 30, 2014 compared to 0.71% and 0.66%, respectively, at June 30, 2014. Our allowance for loan losses was $855 thousand at September 30,2014 and June 30, 2014, 0.36% and 0.37% of gross loans, respectively.

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We used the same methodology in assessing the allowances for both periods. To the best of our knowledge, we have recorded all losses that are both probable and reasonably estimable for the three months ended September 30, 2014 and 2013.

***Noninterest Income.*** Noninterest income for the three months ended September 30, 2014 remained relatively unchanged at $82 thousand for the three months ended September 30, 2014 compared to $80 thousand for the same period in 2013.

***Noninterest Expense.*** Noninterest expense for the three months ended September 30, 2014 increased by $93 thousand, or 6.7%, to $1.5 million from $1.4 million for the same period in 2013. The increase in noninterest expenses is primarily reflective of increases in salaries and employee benefits of $49 thousand, or 5.7%, to $910 thousand for the three months ended September 30, 2014 from $861 thousand for the three months ended September 30, 2013. Additionally, there were increases in occupancy and equipment of $12 thousand, or 7.7%, to $167 thousand for the three months ended September 30, 2014 from $155 thousand for the same period in 2013, office expense of $14 thousand, or 48.3%, to $43 thousand for the three months ended September 30, 2014 from $29 thousand for the same period in 2013, and other noninterest expenses of $26 thousand, or 33.7%, to $103 thousand for the three months ended September 30, 2014 from $77 thousand for the same period in 2013. The increase in salaries and employee benefits is due to an increase during the third and fourth quarters of fiscal year 2014 in salaries related to several officer promotions as well as normal annual pay increases. Additionally, compensation expense associated with our ESOP and equity incentive plans increased to $143 thousand for the three months ended September 30, 2014 from $124 thousand for the same period in 2013. The increase in equity compensation expense resulted from additional shares of restricted stock and stock options granted in the second quarter of fiscal year 2013. ESOP compensation expense increased due to the increasing price of our stock used in the calculation of compensation expense. The increase in other noninterest expense resulted from slight increases in miscellaneous expenses for insurance, dues and subscriptions, and filing fees.

***Income Tax Expense.*** Income tax expense for the three months ended September 30, 2014 was $565 thousand compared with $513 thousand for the three months ended September 30, 2013. Our effective income tax rate remained relatively unchanged at35.1% for the three months ended September 30, 2014 and 35.8% for the three months ended September 30, 2013.

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**Liquidity and Capital Resources**

Our primary sources of funds are deposits and the proceeds from principal and interest payments on loans and investment securities. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and mortgage prepayments are greatly influenced by general interest rates, economic conditions and competition. We generally manage the pricing of our deposits to be competitive within our market and to increase core deposit relationships.

Liquidity management is both a daily and long-term responsibility of management. We adjust our investments in liquid assets based upon management's assessment of (i) expected loan demand, (ii) expected deposit flows, (iii) yields available on interest-earning deposits and investment securities, and (iv) the objectives of our asset/liability management program. Excess liquid assets are invested generally in interest-earning overnight deposits, federal funds sold, and short and intermediate-term U.S. Government sponsored agencies and mortgage-backed securities of short duration. If we require funds beyond our ability to generate them internally, we have credit available under a loan agreement with the Federal Home Loan Bank of Atlanta in the amount of 11% assets (as of September 30, 2014), or approximately $39.6 million.

***Common Stock Dividend Policy.*** On August 21, 2014, the Company paid a $0.10 per share cash dividend on its common stock for a total of $583 thousand.

***Equity Compensation Plans.*** There were no new shares of restricted stock or stock options issued during the three months ended September 30, 2014.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Disclosures of quantitative and qualitative market risk are not required by smaller reporting companies, such as the Company.

**ITEM 4. CONTROLS AND PROCEDURES**

An evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) promulgated under the Securities and Exchange Act of 1934, as amended) as of September 30, 2014. Based on that evaluation, the Company's management, including the Chief Executive Officer and the Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective.

During the quarter ended September 30, 2014, there have been no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) under the Securities and Exchange Act of 1934, amended) that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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## PART II

### ITEM 1. LEGAL PROCEEDINGS

There are various claims and lawsuits in which the Company is periodically involved incidental to the Company's business. In the opinion of management, no material loss is expected from any of such pending claims or lawsuits.

### ITEM 1A. RISK FACTORS

Disclosures of risk factors are not required by smaller reporting companies, such as the Company.

### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) None.

(b) Not applicable.

(c) ***Issuer Repurchases.*** On June 19, 2013, the Board of Directors authorized the repurchase of up to 150,000 shares of the Company's common stock. The repurchase authorization has no expiration date. No shares were repurchased during the three months ended September 30, 2014. The total number of shares remaining that may be purchased under this plan is 48,500.

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**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

The exhibits required by Item 601 of Regulation S-K are included with this Form 10-Q and are listed on the "Index to Exhibits" immediately following the Signatures.

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## SIGNATURES

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

Oconee Federal Financial Corp.

Date: November 14, 2014

/s/ T. Rhett Evatt
T. Rhett Evatt
Chairman and Chief Executive Officer

/s/ H. Allen Salter
H. Allen Salter
Senior Vice President and Chief Financial Officer

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**INDEX TO EXHIBITS**

| Exhibit number | Description |
|---|---|
| 31.1 | Certification of T. Rhett Evatt, Chairman and Chief Executive Officer, Pursuant to Rule 13a-14(a) and Rule 15d-14(a). |
| 31.2 | Certification of H. Allen Salter, Senior Vice President and Chief Financial Officer, Pursuant to Rule 13a-14(a) and Rule 15d-14(a). |
| 32.1 | Certification of T. Rhett Evatt, Chairman and Chief Executive Officer, and H. Allen Salter Senior Vice President and Chief Financial Officer, Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101 | The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2014, formatted in XBRL (Extensible Business Reporting Language):<br>(i) Consolidated Balance Sheets<br>(ii) Consolidated Statements of Income and Comprehensive Income<br>(iii) Consolidated Statements of Changes In Shareholders' Equity<br>(iv) Consolidated Statements of Cash Flows, and<br>(v) Notes to The Consolidated Financial Statements |