

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2022

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: 000-17363

LIFEWAY FOODS, INC.
(Exact name of registrant as specified in its charter)

Illinois
(State or other jurisdiction of
incorporation or organization)

36-3442829
(I.R.S. Employer
Identification No.)

6431 West Oakton St., Morton Grove, Illinois 60053
(Address of principal executive offices) (Zip Code)

(847) 967-1010
(Registrant's telephone number, including area code)

Securities registered under Section 12(b) of the Exchange Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, No Par Value	LWAY	Nasdaq Global Market

Securities registered under Section 12(g) of the Exchange Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer", "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

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

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. Yes No

If securities are registered pursuant to Section 12(b) of the Act, indicate by check mark whether the financial statements of the registrant included in the filing reflect the correction of an error to previously issued financial statements.

Indicate by check mark whether any of those error corrections are restatements that required a recovery analysis of incentive-based compensation received by any of the registrant's executive officers during the relevant recovery period pursuant to §240.10D-1(b).

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the stock was last sold as of June 30, 2022 (\$4.97 per share as quoted on the Nasdaq Global Market) was \$37,694,687.

As of March 20, 2023, 14,644,762 shares of the registrant's common stock, no par value, were outstanding.

Portions of the Registrant's Proxy Statement for the Annual Meeting of Shareholders to be held on June 15, 2023, are incorporated by reference into Part III.

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FORWARD LOOKING STATEMENTS

In connection with the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, readers are advised that this document, any document incorporated by reference herein, and other documents we file with the SEC, contain forward looking statements. In addition, we, or others on our behalf, may make forward looking statements in press releases or written statements, or in our communications and discussions with investors and analysts in the normal course of business through meetings, webcasts, phone calls, and conference calls. Forward looking statements are subject to certain risks and uncertainties, which could cause actual results to differ materially from those indicated by the forward looking statements. These statements use words, variations of words, and negatives of words such as “may,” “could,” “believe,” “future,” “depend,” “expect,” “will,” “result,” “can,” “remain,” “assurance,” “subject to,” “require,” “limit,” “impose,” “guarantee,” “restrict,” “continue,” “become,” “predict,” “likely,” “opportunities,” “effect,” “change,” “future,” “predict,” and “estimate.” Examples of forward looking statements include, but are not limited to, (i) projections of revenues, income or loss, earnings or losses per share, capital expenditures, dividends, capital structure and other financial items, (ii) statements of Lifeway Foods, Inc.’s (the “Company”, “Lifeway”, “we”, or “our”) plans and objectives, including the introduction of new products, or estimates or predictions of actions by customers, suppliers, competitors or regulatory authorities, (iii) statements of future economic performance, and (iv) statements of assumptions underlying other statements and statements about Lifeway or its business.

These forward looking statements are based on management’s beliefs, assumptions, estimates and observations of future events based on information available to our management at the time the statements are made and include any statements that do not relate to any historical or current fact. These statements are not guarantees of future performance and they involve certain risks, uncertainties and assumptions that are difficult to predict. Actual outcomes and results may differ materially from what is expressed, implied or forecast by our forward looking statements due in part to the risks, uncertainties, and assumptions that include:

- the actions of our competitors and suppliers, including those related to price competition;
- the actions and decisions of our customers or consumers;
- our ability to successfully implement our business strategy;
- changes in the pricing of commodities;
- the potential impact of material weaknesses in our internal control over financial reporting;
- the effects of government regulation;
- the impact of the novel coronavirus (“COVID-19”) outbreak on our business, suppliers, consumers, customers, and employees;
- disruptions to our supply chain, or our manufacturing and distribution capabilities, including those due to cybersecurity threats and the COVID-19 outbreak; and
- the other risks and uncertainties that are set forth in Item 1, “Business”, Item 1A “Risk Factors” and Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and that are described from time to time in our filings with the SEC.

These factors are not necessarily all of the important factors that could cause actual results to differ materially from those expressed in any of our forward looking statements. Other unknown or unpredictable factors could also have material adverse effects on future results. We intend these forward looking statements to speak only at the date made. Except as otherwise required to be disclosed in periodic reports required to be filed by public companies with the SEC pursuant to the SEC’s rules, we have no duty to update these statements, and we undertake no obligation to publicly update or revise any forward looking statements, whether as a result of new information, future events or otherwise.

PART I

ITEM 1. BUSINESS

OVERVIEW

Lifeway was founded in 1986 by Michael Smolyansky shortly after he and his wife, Ludmila Smolyansky, emigrated from Eastern Europe to the United States. Lifeway was the first to successfully introduce kefir to the U.S. consumer on a commercial scale, initially catering to ethnic consumers in the Chicago, Illinois metropolitan area. In the thirty-six years that have followed, Lifeway has grown to become the largest producer and marketer of kefir in the U.S. and an important player in the broader market spaces of probiotic-based products and natural, “better for you” foods.

PRODUCTS

Our primary product is drinkable kefir, a cultured dairy product. Lifeway Kefir is tart and tangy, high in protein, calcium and vitamin D. Thanks to our exclusive blend of kefir cultures, each cup of kefir contains 12 live and active cultures and 25 to 30 billion beneficial CFU (Colony Forming Units) at the time of manufacture.

We manufacture (directly or through co-packers) and market products under the Lifeway, Fresh Made and Glen Oaks Farms brand names, as well as under private labels on behalf of certain customers.

Our product categories are:

- Drinkable Kefir, sold in a variety of organic and non-organic sizes, flavors, and types;
- European-style soft cheeses, including farmer cheese, white cheese, and Sweet Kiss;
- Cream and other, which consists primarily of cream, a byproduct of making our kefir;
- ProBugs, a line of kefir products designed for children;
- Drinkable Yogurt, sold in a variety of sizes and flavors; and
- Other Dairy, which consists primarily of Fresh Made butter and sour cream.

Net sales of products by category were as follows for the years ended December 31:

In thousands	2022		2021	
	\$	%	\$	%
Drinkable Kefir other than ProBugs	\$ 110,247	78%	\$ 95,850	80%
Cheese	12,651	9%	12,612	11%
Cream and other	7,465	5%	3,582	3%
Drinkable Yogurt	6,105	4%	2,223	2%
Probugs Kefir	3,403	3%	3,178	3%
Other dairy	1,697	1%	1,620	1%
Net Sales	<u>\$ 141,568</u>	<u>100%</u>	<u>\$ 119,065</u>	<u>100%</u>

Product innovation and new product development

Lifeway is committed to maintaining its positions as the leading producer of kefir and a recognized leader in the market for probiotic products. We routinely evaluate opportunities for new product flavors and formulations, improved package design, new product configurations and other innovation avenues. Beyond our core drinkable kefir products, we have an ongoing effort to extend the strength of the Lifeway brand and leverage the capabilities of the Lifeway organization into fresh categories and into additional channels of trade, such as Convenience; Foodservice; Club; and Drug. In 2022, we maintained the level of focus on product innovations, packaging innovations, and growth opportunities. These product innovation and development efforts have led to additional revenue opportunities.

Lifeway considers research and development of new products to be a significant part of our overall business philosophy. Where possible, we leverage our existing staff and facilities to conduct our innovation, research, and development efforts, rather than maintaining a dedicated research and development staff and facilities or relying solely on third parties. Until the second half of 2021, in light of the COVID-19 outbreak, our focus was on expanding sales of our current products, and less on new product development. In August 2021, we purchased the Glen Oaks Farms drinkable yogurt product line, and launched our drinkable oat-based kefir product line in December 2021.

PRODUCTION

Manufacturing

During 2022 and 2021, approximately 96% and 98% of our revenue, respectively, was derived from products manufactured at our own facilities. We currently operate the following manufacturing and distribution facilities:

- Morton Grove, Illinois, which produces drinkable kefir, drinkable ProBugs kefir, and cheese products;
- Waukesha, Wisconsin, which produces drinkable kefir products and from which we store and distribute products;
- Niles, Illinois, which stores and serves as a distribution point for products; and
- Philadelphia, Pennsylvania, which produces drinkable kefir, cheese, and butter products, from which we store and distribute products.

We own these manufacturing facilities. All our fixed assets associated with manufacturing, storage, and distribution of our products are in the United States.

Co-Packers

In addition to the products manufactured in our own facilities, independent manufacturers (“co-packers”) manufacture some of our products. We have a co-packer agreement to manufacture drinkable yogurt in California. We have a co-packer agreement to manufacture drinkable kefir in Ireland, to serve our European markets. During 2022 and 2021, approximately 4% and 2% of our revenue, respectively, was derived from products manufactured by co-packers. Our domestic co-packer is Safe Quality Food (“SQF”) certified and follows Good Manufacturing Practices (GMPs). Additionally, the co-packers are required to ensure our products are manufactured in accordance with our quality specifications and that they are compliant with all applicable laws and regulations.

SALES AND DISTRIBUTION

Sales Organization

We sell our products primarily through our direct sales force, brokers, and distributors. Our sales organization strives to cultivate strong, collaborative relationships with our customers that facilitate favorable shelf placement for our products, which we believe will drive sales volumes when combined with our marketing efforts and our brand strength. Our relationships with food brokers provide additional customer coverage as a supplement to our direct sales force.

Distribution inside the United States

Lifeway's products reach the consumer through three primary "route-to-market" pathways:

- Retail-direct;
- Distributor; and
- Direct store delivery ("DSD").

Under the retail-direct channel, we sell our products to retailers and deliver it through either the retailers' carriers or third-party carriers that deliver to such retailers' distribution centers. In turn, our retailers then deliver the products to their respective stores. Customers in this route-to-market grouping include Kroger, Walmart and Trader Joe's. Under the retail direct-model, optimal product merchandising, assortment and product presentation are attended to by the retailer. Sales to our retail-direct customers represent approximately 50% of our total net sales for the year ended 2022.

Under the distributor channel, we sell our products to distributors and deliver it through either the distributors' carriers or third-party carriers that deliver to such distributors' designated warehouses. In turn, our distributors then sell and ship our products to their retail customers. Our distributors often use a DSD model of their own to make deliveries directly to individual stores, but they also make deliveries to retailers' distribution centers. Our distributor customers include United Natural Foods (UNFI), KeHE Distributors, and C&S Wholesale Grocers. The distributor attends to optimal product merchandising, assortment, and product presentations at the retail end of the channel, with support from Lifeway's direct sales force and broker network. Sales to our distributor customers represented approximately 48% of our total net sales for year ended 2022.

Under the direct store delivery (DSD) route to market, we sell our products to retailers and deliver it directly to the store using Company-owned vehicles and a team of Lifeway merchandisers who engage face-to-face with store management to ensure optimal product assortments and presentations. We operate our DSD model in the Chicago, Illinois metropolitan area only. Sales to our DSD customers represent approximately 2% of our total net sales for the year ended 2022.

Distribution outside of the U.S.

Substantially all of Lifeway's products are distributed within the United States; however, certain of our distributors sell our products to retailers in Mexico and portions of South America and the Caribbean. Additionally, Lifeway products reach consumers in the United Kingdom, Ireland, and the Middle East under third party co-manufacturing agreements and in-country broker and distributor arrangements. Sales outside the United States represented approximately 1% of net sales for the year ended 2022.

Channel- and Market-Specific Distribution and Broker Representation Arrangements

Lifeway's generally standardized agreements with independent distributors and food brokers allow us the latitude to establish new relationships as opportunities and needs arise. Where appropriate given the relationship, market, and business opportunity, we offer exclusive channels, markets, and/or territories to our distributors and brokers.

We provide our independent distributors with products at wholesale prices for distribution to their retail accounts. Lifeway believes that the prices at which we sell our products to distributors are competitive with the prices generally paid by distributors for similar products in the markets served. Due to the perishable nature of our products and the costs to return, we do not offer return privileges to any of our distributors or channel customers; however, from time to time we do provide our customers with allowances for non-saleable product.

Lifeway engages independent food brokers generally on a commission basis, subject in some cases to a minimum commission guarantee. The commissions vary based on the scope of services provided and customers served. Our brokers represent our products to a variety of prospective buyers. These buyers could be specialty stores, retail grocery chains, wholesalers, foodservice operators and distributors, drug chains, mass merchandisers, industrial users, schools and universities, or military installations. With support from our direct sales force, brokers may provide other value-added services. These may include scheduling and coordinating promotions, merchandising, centralized ordering, and data collection services.

MARKETING

We use a combination of sales incentives, trade promotions, and consumer promotions to market our products.

Sales Incentives and Trade Promotion Allowances

Lifeway offers various sales incentives and trade promotional programs to its retailer and distributor customers from time to time in the normal course of business. These sales incentives and trade promotion programs typically include rebates, in-store display and demo allowances, allowances for non-saleable product, coupons, and other trade promotional activities. Trade promotions support price features, displays, and other merchandising of our products by our retail and distributor customers. We record these arrangements as a reduction to net sales in our consolidated statements of operations.

Consumer Promotions and Marketing Campaigns

We engage in an ongoing and wide variety of marketing and media campaigns – primarily digital and social media, print advertising, television advertising, and event marketing. We complement these marketing and media efforts with industry-related trade shows and in-store promotional events. Our consumer marketing efforts also include cooperative advertising programs with our retail customers and various couponing campaigns, online consumer relationship programs, and other similar forms of promotions.

Our marketing efforts are aimed at stimulating demand with new and existing consumers by elevating awareness and consumption of kefir and probiotics, as well as enhancing our brand equity. Our awareness marketing seeks to promote the positive nutritional attributes and flavor of our products.

COMPETITION

Lifeway competes with a limited number of other domestic kefir producers and consequently faces a small amount of direct competition for kefir products. However, Lifeway's kefir-based products compete with other dairy products, such as spoonable and drinkable yogurt, and, increasingly, with non-dairy probiotic products. Many of our competitors are well-established and have significantly greater financial resources than Lifeway to promote their products.

SUPPLIERS

We purchase our ingredients such as milk, pectin, and other ingredients from unaffiliated suppliers. In addition, we purchase significant quantities of packaging materials to package our products and natural gas and electricity to operate our facilities. Purchases are made through purchase orders or contracts, and price, delivery terms, and product specifications vary. Although the prices for our principal inputs can fluctuate based on economic, weather, and other conditions, Lifeway believes it has ready access to alternative suppliers for all critical ingredients, packaging, and other input requirements.

MAJOR CUSTOMERS

During the year ended December 31, 2022, two customers collectively accounted for approximately 22% of our total net sales. Two customers collectively accounted for approximately 28% of net accounts receivable as of December 31, 2022.

SEGMENTS

Lifeway has determined that it has one reportable segment based on how our chief operating decision maker manages the business and, in a manner, consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing Company performance, has been identified as the Chief Executive Officer. Substantially all our consolidated revenues relate to the sale of cultured dairy products that we produce using the same processes and materials and are sold to consumers through a common network of distributors and retailers in the United States.

DANONE SA

Since October 1999, Danone SA, through subsidiaries (collectively “Danone”), has been the beneficial owner of approximately 24% of the outstanding common stock of Lifeway. Lifeway and Danone are parties to a Stockholders’ Agreement dated October 1, 1999, which as amended provides Danone the right to designate one director nominee, provides Danone with anti-dilutive rights relating to certain future offerings and issuances of capital stock, and grants Danone limited registration rights.

INTELLECTUAL PROPERTY

We believe that our rights in our trademarks and service marks are important to our marketing efforts to develop brand recognition and differentiate our brand from our competitors and are a valuable part of our business. We own many domestic and international trademarks and service marks. In addition, we own numerous registered and unregistered copyrights, registered domain names, and proprietary trade secrets, trade dress, technology, know-how, processes, and other proprietary rights that are not registered. Depending on the jurisdiction, trademarks are generally valid as long as they are in use and/or their registrations are properly maintained, and they have not been found to have become generic. Registrations of trademarks can also generally be renewed indefinitely as long as the trademarks are in use. We also have licenses to use certain trademarks inside and outside of the United States and to certain product formulas, all subject to the terms of the agreements under which such licenses are granted. Lifeway’s policy is to pursue registration of intellectual property whenever appropriate. We protect our intellectual property rights by relying on a combination of trademark, copyright, trade dress, trade secret and other intellectual property laws, and domain name dispute resolution systems; as well as licensing agreements, third-party confidentiality, nondisclosure, and assignment agreements; and by policing third-party misuses of our intellectual property. We regard the Lifeway family of trademarks and other intellectual property as having substantial value and as being an important factor in the marketing of our products. The loss of such protection would have a material adverse impact on our operations and share price.

REGULATION

Lifeway is subject to extensive regulation by federal, state, and local governmental authorities. In the United States, agencies governing the manufacture, marketing, and distribution of our products include, among others, the Federal Trade Commission (“FTC”), the United States Food & Drug Administration (“FDA”), the United States Department of Agriculture (“USDA”), the United States Environmental Protection Agency (“EPA”), the Occupational Safety and Health Administration (“OSHA”), and their state and local equivalents. Under various statutes, these agencies prescribe, among other things, the requirements and standards for quality, safety, and representation of our products to consumers. We are also subject to federal laws and regulations relating to our products and production. For example, as required by the National Organic Program (“NOP”), we rely on third parties to certify certain of our products and production locations as organic. Additionally, our facilities are subject to various laws and regulations regarding the release of material into the environment and the protection of the environment in other ways.

Internationally, we are subject to the laws and regulatory authorities of the foreign jurisdictions in which we manufacture and sell our products, including the Food Standards Agency in the United Kingdom; the National Service of Health, Food Safety and Agro-Food Quality (known by its Spanish-language acronym “SENASICA”) and the Federal Commission for the Protection from Sanitary Risks (“COFEPRIS”) in Mexico; the Food Safety Authority in Ireland; and the European Food Safety Authority, which supports the European Commission, as well as individual country, province, state, and local regulations.

Changes in these laws or regulations, or the introduction of new laws or regulations, could increase the costs of doing business for the Company, our customers, or suppliers, or restrict our actions, causing our results of operations to be adversely affected.

MILK INDUSTRY REGULATION

Our primary raw material is milk. The federal government establishes minimum prices for raw milk purchased in federally regulated areas. Some states have established their own rules for determining minimum prices. The federal government announces prices for raw milk each month. While we are subject to federal government regulations that establish minimum prices for milk, and we also pay producer (“over-order”) premiums, federal order administration costs, and other related charges that vary by milk product, location, and supplier.

FOOD SAFETY

Lifeway takes appropriate precautions to ensure the safety of our products. In addition to routine inspections by state and federal regulatory agencies, including the USDA and FDA, we have instituted Company-wide quality systems that address topics such as supplier control; ingredient, packaging, and product specifications; preventive maintenance; pest control; and sanitation. Each of our facilities also has in place a hazard analysis critical control points (“HACCP”) plan that identifies critical pathways for contaminants and mandates control measures that must be used to prevent, eliminate or reduce relevant food-borne hazards. To the extent that the federal Food Safety Modernization Act applies to Lifeway’s business, we develop food safety plans and implement preventive measures to protect against food contamination. We also maintain a product recall plan, including lot identifiability and traceability measures that allow us to act quickly to reduce the risk of consumption of any product that we suspect may pose a health issue.

We maintain various types of insurance, including product liability and product recall coverages, which we believe to be sufficient to cover potential product liabilities.

We have also implemented the SQF program at our Illinois and Wisconsin facilities. SQF is a fully integrated food safety and quality management protocol designed specifically for the food sector. The SQF Code, based on universally accepted CODEX Alimentarius, HACCP guidelines and the Global Food Safety Initiative (“GFSI”) standards, offers a comprehensive methodology to manage food safety and quality simultaneously. SQF certification provides an independent and external validation that a product, process or service complies with international, regulatory and other specified standards.

SEASONALITY

Lifeway’s business is not seasonal.

EMPLOYEES

As of December 31, 2022, we employed 289 full-time and two part-time employees, of which 103 were members of a union bargaining unit.

AVAILABLE INFORMATION

Lifeway maintains a corporate website for investors at www.lifewayfoods.com and makes available, free of charge, through this website its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports that we file with or furnish to the SEC as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

ITEM 1A. RISK FACTORS

In evaluating and understanding us and our business, you should carefully consider the risks described below, in conjunction with all of the other information included in this Annual Report on Form 10-K, including “Management’s Discussion and Analysis of Financial Condition and Results of Operations” contained in Part II, Item 7 and “Quantitative and Qualitative Disclosures About Market Risk” contained in Part II, Item 7A. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently believe are not material, may become important factors that adversely affect our business. If any of the events or circumstances described in the following risk factors actually occurs, our business, financial condition, results of operations, and future prospects could be materially and adversely affected.

RISKS RELATED TO OUR BUSINESS

Our product categories face a high level of competition, which could negatively impact our sales and results of operations.

We compete with a limited number of other domestic kefir producers and consequently face a small amount of direct competition for kefir products. However, our kefir-based products compete with other dairy products, notably spoonable and drinkable yogurt, and, increasingly, with non-dairy probiotic products that incorporate kefir cultures but are not kefir. We face significant competition for limited retailer shelf space in each of our product categories. Competition in our product categories is based on product innovation, product quality, price, brand recognition and loyalty, effectiveness of marketing, promotional activity, and our ability to identify and satisfy consumer tastes and preferences. We believe that our brands have benefited in many cases from being the first to introduce products in their categories, and their success has attracted competition from other food and beverage companies that produce branded products, as well as from private label competitors. Some of our competitors, such as Danone, General Mills, Chobani, Hain Celestial Group, and Nestle, have substantial financial and marketing resources. These competitors and others may be able to introduce innovative products more quickly or market their products more successfully than we can, which could cause our growth rate to be slower than we anticipate and could cause sales to decline.

We also compete with producers of non-dairy products, such as Millennium Products and PepsiCo, that have lower ingredient and production-related costs. As a result, these competing producers may be able to offer their products to customers at a lower price point. This could cause us to lower our prices, resulting in lower profitability or, in the alternative, cause us to lose market share if we fail to lower prices. Furthermore, private label competitors are generally able to sell their products at lower prices because private label products typically have lower marketing costs than their branded counterparts. If our products fail to compete successfully with other branded or private label offerings, demand for our products and our sales volumes could be negatively impacted.

Additionally, due to high levels of competition, certain of our key retailers may demand price concessions on our products or may become more resistant to price increases for our products. Increased price competition and resistance to price increases have had, and may continue to have, a negative effect on our results of operations.

We may not be able to successfully implement our business strategy for our brands on a timely basis or at all.

We believe that our future success depends, in part, on our ability to implement our strategy of leveraging our existing brands with our new products to maintain our market position in our product categories; drive increased sales; acquire or establish new brands; and create strategic alliances including potential joint ventures. Our ability to implement this strategy depends, among other things, on our ability to:

- enter into distribution and other strategic arrangements with third-party retailers and other potential distributors of our products;
- compete successfully in the product categories in which we choose to operate;
- introduce timely, new, cost-effective, and appealing products and innovate successfully within our existing product categories;
- develop and maintain consumer interest in and demand for our brands considering prevailing consumer tastes and preferences;
- increase our brand recognition and loyalty;
- enter into strategic arrangements with third-party suppliers to obtain necessary raw materials;
- identify suitable acquisition candidates or joint venture partners and accurately assess their value, growth potential, strengths, weaknesses, contingent and other liabilities, and potential profitability;
- negotiate acquisitions and joint ventures on terms acceptable to us; and
- integrate acquired brands, products, or joint ventures into our company and our business strategy.

If we fail to execute these and other important elements of our business strategy, our business and results of operations could be adversely affected.

One key element of our business strategy is to introduce timely, new, cost-effective, and appealing products and to innovate successfully within our existing product categories. However, consumer tastes and preferences change rapidly, and evolve over time. Factors that may affect consumer tastes and preferences include:

- dietary trends and increased attention to nutritional values, such as the sugar, fat, protein, fiber or calorie content of different foods and beverages;
- concerns regarding the health effects of specific ingredients and nutrients, such as sugar, other sweeteners, dairy, soybeans, nuts, oils, vitamins, fiber and minerals;
- concerns regarding the public health consequences associated with obesity, particularly among young people;
- decisions by yogurt and non-dairy beverage manufacturers to mislabel their products as “kefir” in order to benefit from our branding and marketing efforts, a marketing ploy that can cause significant confusion and misunderstanding among consumers; and
- increased awareness of the environmental and social effects of food processing.

Our future investments may not produce the results we expect when we expect them for a variety of reasons including those described herein. Our future product development and innovation will be reliant on our ability to identify and develop potential new growth opportunities. This process is inherently risky and will result in investments of substantial time and resources for which we may not achieve any return or value. Successful product development and innovation is also affected by our ability to launch new or improved products successfully and on a timely and cost-effective basis.

We may have to pay cash, incur debt, or issue equity, equity-linked, or debt securities to fund our business strategy, or may be unable to fund that strategy. Any of these events could adversely affect our financial results and our business. We could experience similar effects if we invest resources in a strategy that ultimately proves unsuccessful. If, due to a failure of our strategy or any other reason, consumer demand for our products declines, our sales volumes, results of operations, and our business could be negatively affected, and we may not be able to create or sustain growth or successfully implement our business strategy.

Interruption of our supply chain could affect our ability to manufacture or distribute products, could adversely affect our business and sales, and/or could increase our operating costs and capital expenditures.

We have several supply agreements with suppliers and co-packers that require them to provide us with specific finished goods, including packaging and kefir. For some of these products, we essentially rely on a single supplier or co-packer as our sole source for the item. The failure for any reason of any such sole source or other co-packer to fulfill its obligations under the applicable agreements with us or the termination or renegotiation of any such sourcing agreement could result in disruptions to our supply of finished goods and have an adverse effect on our results of operations. Additionally, our suppliers and co-packers are subject to risk, including labor disputes, union organizing activities, financial liquidity, inclement weather, natural disasters, supply constraints, and general economic and political conditions that could limit their ability to timely provide us with acceptable products, which could disrupt our supply of finished goods, or require that we incur additional expense by providing financial accommodations to the supplier or co-packer or taking other steps to seek to minimize or avoid supply disruption, such as establishing new arrangements with other providers. A new arrangement may not be available on terms as favorable to us as our existing arrangements, if at all.

Our inability to maintain sufficient internal capacity or establish satisfactory co-packing, warehousing and distribution arrangements could limit our ability to operate our business or implement our strategic plan and could negatively affect our sales volumes and results of operations.

Disruption of our manufacturing or distribution chains or information technology systems, including disruption due to cybersecurity threats, could adversely affect our business.

The success of our business depends, in part, on maintaining a strong production platform and we rely primarily on internal production resources to fulfill our manufacturing needs. Our ongoing initiatives to expand our production platform and our productive capacity could fail to achieve such objectives and, in any case, could increase our operating costs beyond our expectations and could require significant additional capital expenditures. If we cannot maintain sufficient production, warehousing, and distribution capacity, either internally or through third party agreements, we may be unable to meet customer demand and/or our manufacturing, distribution, and warehousing costs may increase, which could negatively affect our business.

Furthermore, damage or disruption to our manufacturing or distribution capabilities due to weather, natural disaster, fire, environmental incident, terrorism, cybersecurity threats and other security breaches, pandemic, strikes, the financial or operational instability of key distributors, warehousing, and transportation providers, or other reasons could impair our ability to manufacture or distribute our products.

We rely on a limited number of production and distribution facilities. A disruption in operations at any of these facilities or any other disruption in our supply chain relating to common carriers, supply of raw materials and finished goods, or otherwise, whether as a result of casualty, natural disaster, power loss, telecommunications failure, cybersecurity threat, terrorism, labor shortages, contractual disputes or other causes, could significantly impair our ability to operate our business and adversely affect our relationship with our customers. Furthermore, our insurance coverage may not be adequate to cover all related costs.

Our information technology systems are also critical to the operation of our business and essential to our ability to successfully perform day-to-day operations. These systems include, without limitation, networks, applications, and outsourced services in connection with the operation of our business. A failure of our information technology systems to perform as we anticipate could disrupt our business and result in transaction errors, processing inefficiencies, and sales losses, causing our business to suffer. In addition, our information technology systems may be vulnerable to damage or interruption from circumstances beyond our control, including fire, natural disasters, systems failures, and cybersecurity threats. Cybersecurity threats in particular are persistent, evolve quickly and include, without limitation, computer viruses, unauthorized attempts to access information, denial of service attacks, and other electronic security breaches. Like our customers, suppliers, subcontractors and other third parties with whom we do business generally, we expect that we will continue to be the subject of cybersecurity threats. In some cases, we must rely on the safeguards put in place by the third parties with whom we do business to protect against security threats. We believe we have implemented appropriate measures and controls and have invested in sufficient resources to appropriately identify and monitor these threats and mitigate potential risks, including risks involving our customers and suppliers. However, there can be no assurance that any such actions will be sufficient to prevent cybersecurity breaches, disruptions to mission critical systems, the unauthorized release of sensitive information or corruption of data, or harm to facilities or personnel.

These threats and other events could disrupt our operations, or the operations of our customers, suppliers, subcontractors and other third parties; could require significant management attention and resources; could result in the loss of business, regulatory actions and potential liability; and could negatively impact our reputation among our customers and the public. Any of these outcomes could have a negative impact on our financial condition, results of operations, or liquidity.

Our debt and financial obligations could adversely affect our financial condition, our ability to obtain future financing, and our ability to operate our business.

We have outstanding debt obligations that could adversely affect our financial condition and limit our ability to successfully implement our business strategy. Furthermore, from time to time, we may need additional financing to support our business and pursue our business strategy, including strategic acquisitions. Our ability to obtain additional financing, if and when required, will depend on investor demand, our operating performance, the condition of the capital markets, and other factors. We cannot assure that additional financing will be available to us on favorable terms when required, or at all. If we raise additional funds through the issuance of equity, equity-linked, or debt securities, those securities may have rights, preferences, or privileges senior to those of our common stock, and, in the case of equity and equity-linked securities, our existing stockholders may experience dilution.

As of December 31, 2022, we had \$2.77 million outstanding under the Revolving Credit Facility and \$3.72 million outstanding under the note payable, net of \$25 thousand of unamortized deferred financing. Our loan agreements contain certain restrictions and requirements that among other things:

- require us to maintain a quarterly fixed charge coverage ratio and minimum working capital ratio;
- limit our ability to obtain additional financing in the future for working capital, capital expenditures and acquisitions, to fund growth or for general corporate purposes;
- limit our future ability to refinance our indebtedness on terms acceptable to us or at all;
- limit our flexibility in planning for or reacting to changes in our business and market conditions or in funding our strategic growth plan; and
- impose on us financial and operational restrictions.

Our ability to meet our debt service obligations will depend on our future performance, which will be affected by the other risk factors described in this Annual Report on Form 10-K. If we do not generate enough cash flow to pay our debt service obligations, we may be required to refinance all or part of our existing debt, sell our assets, borrow more money or raise equity. There is no guarantee that we will be able to take any of these actions on a timely basis, on terms satisfactory to us, or at all.

Our Revolving Credit Facility and term loan bear interest at variable rates. If market interest rates increase, it will increase our debt service requirements, which could adversely affect our cash flow.

Our loan agreements also contain provisions that restrict our ability to:

- borrow money or guarantee debt;
- create liens;
- make specified types of investments and acquisitions;
- pay dividends on or redeem or repurchase stock;
- enter into new lines of business;
- enter into transactions with affiliates; and
- sell assets or merge with other companies.

These restrictions on the operation of our business could harm our ability to execute on our business strategy by, among other things, limiting our ability to take advantage of financing, merger and acquisition opportunities, and other corporate opportunities. Various risks, uncertainties, and events beyond our control could affect our ability to comply with these covenants. Unless cured or waived, a default would permit lenders to accelerate the maturity of the debt under the credit agreement and to foreclose upon the collateral securing the debt.

Loss of our key management or other personnel, or an inability to attract such management and other personnel, could negatively impact our business.

We depend on the skills, working relationships, and continued services of key personnel, including our experienced senior management team. We also depend on our ability to attract and retain qualified personnel to operate and expand our business. If we lose one or more members of our senior management team whose responsibilities cannot otherwise be distributed among our other officers, or if we fail to attract talented new employees, our business and results of operations could be negatively affected.

Employee strikes and other labor-related disruptions may adversely affect our operations.

We have a union contract governing the terms and conditions of employment for a significant portion of our workforce. Although we believe union relations since the union's certification as the exclusive bargaining representative of this portion of our workforce have been amicable, there is no assurance that this will continue in the future or that we will not be subject to future union organizing activity. There are potential adverse effects of labor disputes with our own employees or by others who provide warehousing, transportation, and distribution, both domestic and foreign, of our raw materials or other products. Strikes or work stoppages or other business interruptions could occur if we are unable to renew collective bargaining agreements on satisfactory terms or enter into new agreements on satisfactory terms, which could impair manufacturing and distribution of our products or result in a loss of sales, which could adversely impact our business, financial condition, or results of operations. The terms and conditions of existing, renegotiated, or new collective bargaining agreements could also increase our costs or otherwise affect our ability to fully implement future operational changes to enhance our efficiency or to adapt to changing business needs or strategy.

Our intellectual property rights are valuable, and any inability to protect them could reduce the value of our products and brands.

We consider our intellectual property rights, particularly our trademarks, but also our copyrights, registered domain names, and proprietary trade secrets, technology, know-how, processes and other proprietary rights to be a significant and valuable aspect of our business. We attempt to protect our intellectual property rights by relying on a combination of trademark, copyright, trade dress, trade secret, and other intellectual property laws, and domain name dispute resolution systems; as well as licensing agreements, third-party confidentiality, nondisclosure, and assignment agreements; and by policing third-party misuses of our intellectual property. Our failure to obtain or maintain adequate protection of our intellectual property rights, or any change in law or other changes that serve to lessen or remove the current legal protections of our intellectual property, may diminish our competitiveness and could materially harm our business.

We also face the risk of claims that we have infringed third parties' intellectual property rights. Any claims of intellectual property infringement, even those without merit, could be expensive and time consuming to defend, cause us to cease making, licensing, or using products that incorporate the challenged intellectual property, require us to redesign or rebrand our products or packaging, divert management's attention and resources, or require us to enter into royalty or licensing agreements to obtain the right to use a third party's intellectual property. Any royalty or licensing agreements, if required, may not be available to us on acceptable terms or at all. Additionally, a successful claim of infringement against us could result in our being required to pay significant damages, enter into costly license or royalty agreements, or stop the sale of certain products, any of which could have a negative effect on our results of operations.

The Smolyansky family controls a substantial portion of our common stock and has the ability to control the outcome of matters submitted for stockholder approval.

Although the members of the Smolyansky family together control less than 50% of our common stock collectively, they could significantly influence any matter requiring approval by our stockholders, including the election of all of our directors and the approval or rejection of any merger, change of control, or other significant corporate transaction. It is unlikely that any person interested in acquiring Lifeway will be able to do so without obtaining the consent of some members of the Smolyansky family. The Smolyansky family's interests may not always be aligned with other stockholders' interests. By exercising their influence, members of the Smolyansky family could cause Lifeway to take actions that are at odds with the investment goals of institutional, short-term, non-voting, or other non-controlling investors, or that have a negative effect on our stock price.

Our business could be negatively affected as a result of the actions of stockholders.

Our business could be negatively affected as a result of stockholder actions, which could cause us to incur significant expense, hinder execution of our business strategy, and impact the trading value of our securities. Stockholder actions, including potential proxy contests, requires significant time and attention by management and our Board, potentially interfering with our ability to execute our strategic plan. We may be required to incur significant legal fees and other expenses related to stockholder actions, and the attention of our management may be diverted by such actions. While we welcome our stockholders' constructive input, there can be no assurance that stockholder actions would not result in negative impacts to the Company. Any of these impacts could materially and adversely affect our business and operating results, and the market price of our Common Stock could be subject to significant fluctuation or otherwise be adversely affected by stockholder actions.

RISKS RELATED TO OUR INDUSTRY

The consolidation of our customers or the loss of any of our largest customers could negatively impact our sales and results of operations.

Customers, such as supermarkets and food distributors, continue to consolidate. This consolidation has produced larger, more sophisticated organizations with increased negotiating and buying power that are able to resist price increases or demand increased promotional programs, as well as operate with lower inventories, decrease the number of brands that they carry and increase their emphasis on private label products, all of which could negatively impact our business. The consolidation of retail customers also increases the risk that a significant adverse impact on their business could have a corresponding material adverse impact on our business.

Two of our customers together accounted for 22% of our net sales in the fiscal year ended December 31, 2022. Where we enter into written agreements with our customers, they are generally terminable after short notice periods by the customer. In addition, our customers sometimes award contracts based on competitive bidding, which could result in lower profits for contracts we win and the loss of business for contracts we lose. The loss of any large customer, the reduction of purchasing levels, or the cancellation of any business from a large customer for an extended period of time could negatively affect our sales and results of operations.

We rely on sales made by or through our independent distributors to customers. Distributors purchase directly for their own account for resale. The loss of, or business disruption at, one or more of these distributors may harm our business. If we are required to obtain additional or alternative distribution agreements or arrangements in the future, we cannot be certain that we will be able to do so on satisfactory terms or in a timely manner. Our inability to enter into satisfactory distribution agreements may inhibit our ability to implement our business plan or to establish markets necessary to expand the distribution of our products successfully.

We are subject to the risk of product contamination and product liability claims, which could harm our reputation, force us to recall products and incur substantial costs.

The sale of food products for human consumption involves the risk of injury to consumers. Such injuries may result from tampering by unauthorized third parties, inadvertent mislabeling, product contamination or spoilage, including the presence of foreign objects, substances, chemicals, other agents, or residues introduced during the storage, processing, handling or transportation phases. We also may be subject to liability if our products or production processes violate applicable laws or regulations, including environmental, health, and safety requirements, or in the event our products cause injury, illness, or death.

Under certain circumstances, we may be required to recall or withdraw products, suspend production of our products, or cease operations, which may lead to a material adverse effect on our business. In addition, customers may cancel orders for such products as a result of such events. Even if a situation does not necessitate a recall or market withdrawal, and even if we and each of our co-packers and suppliers comply in all material respects with all applicable laws and regulations, we may become subject to claims or lawsuits relating to such matters. Even if a product liability claim is unsuccessful or is not fully pursued, the negative publicity surrounding any assertion that our products caused illness or physical harm, including the risk of reputational harm being magnified and/or distorted through the rapid dissemination of information over the Internet, including through news articles, blogs, chat rooms, and social media, could adversely affect our reputation with existing and potential customers and consumers and our corporate and brand image. Moreover, claims or liabilities of this type might not be covered by our insurance or by any rights of indemnity or contribution that we may have against others. We maintain product liability and product recall insurance in amounts that we believe to be adequate. However, we cannot be sure that we will not incur claims or liabilities for which we are not insured or that exceed the amount of our insurance coverage. A product liability judgment against us or a product recall could have a material adverse effect on our business, consolidated financial condition, results of operations or liquidity.

We rely on independent certification for several of our products and facilities.

We rely on independent certification, such as certifications of our products as “organic,” or “gluten-free,” to differentiate our products from others. The loss of any independent certifications could adversely affect our market position as a probiotic-based product and natural, “better for you” foods company, which could harm our business. We rely on independent SQF certification at some of our facilities, a certification that some of our customers require us to maintain.

We must comply with the requirements of independent organizations or certification authorities in order to label our products as certified. For example, we can lose our “organic” certification if a manufacturing plant becomes contaminated with non-organic materials, or if it is not properly cleaned after a production run. In addition, all organic raw materials must be certified organic or organic compliant. Our products could lose their organic certifications if our raw material suppliers lose their organic certifications. Similarly, we could lose our SQF certification if we do not meet the requirements of the SQF Code. The loss of these certifications could cause us to lose customers that require Lifeway products and/or facilities to carry some or all of them, which could negatively affect our sales and results of operations.

Increases in the cost of raw milk could reduce our gross margin and profit.

Conventional and organic raw milk, our primary raw material, is an agricultural commodity that is subject to price fluctuations. Both conventional and organic milk prices in fiscal 2022 were higher than the prior year, and there can be no assurance that such prices will remain at these levels in the future. The supply and price of raw milk may be impacted by, among other things, weather, natural disasters, real or perceived supply shortages, lower dairy and crop yields, general increases in farm inputs and costs of production, political and economic conditions, labor actions, government actions, and trade barriers. Increases in the market price for raw milk or over-order premiums charged by producers may also impact our ability to enter into purchase commitments at a fixed price. There can be no assurance that our purchasing practices will mitigate future price risk. As a result, increases in the cost of raw milk could have an adverse impact on our profitability.

In addition, the dairy industry continues to experience periodic imbalances between supply and demand for organic raw milk. Industry regulation and the costs of organic farming compared to costs of conventional farming can impact the supply of organic raw milk in the market. Oversupply levels of organic raw milk can increase competitive pressure on our products and pricing, while supply shortages can cause higher input costs and reduce our ability to deliver product to our customers. Cost increases in raw materials and other inputs could cause our profits to decrease significantly compared to prior periods, as we may be unable to increase our prices to offset the increased cost of these raw materials and other inputs. If we are unable to obtain raw materials and other inputs for our products or offset any increased costs for such raw materials and inputs, our business could be negatively affected.

Reduced availability of raw materials and other inputs, as well as increased costs for them, could adversely affect us.

Our business depends heavily on raw materials and other inputs in addition to conventional and organic raw milk, such as sweeteners, diesel fuel, packaging material, resin, and other commodities. Our raw materials are generally sourced from third-party suppliers, and we are not assured of continued supply, pricing, or exclusive access to raw materials from any of these suppliers. In 2022, costs to us increased primarily due to inflationary price increases of other ingredients, packaging materials, and freight. However, for market conditions or competitive reasons, our pricing actions may also lag input cost changes, or we may not be able to pass along the full effect of increases in raw materials and other input costs as we incur them.

The organic ingredients we use in some of our products are less plentiful and available from a fewer number of suppliers than their conventional counterparts. Competition with other manufacturers in the procurement of organic product ingredients may increase in the future if consumer demand for organic products increases.

Our business is subject to various food, environmental, and health and safety laws and regulations, which may increase our compliance costs, subject us to liabilities, or otherwise adversely affect our business.

Our business operations are subject to numerous requirements in the United States relating to food safety, production, and marketing, as well as the protection of the environment, and health and safety matters. The food production and marketing industry is subject to a variety of federal, state, local, and foreign laws and regulations, including food safety requirements related to the ingredients, manufacture, processing, storage, marketing, advertising, labeling, and distribution of our products, as well as those related to worker health and workplace safety. Our activities, both in and outside of the United States, are subject to extensive regulation. We are regulated by, among other federal and state authorities, the FDA, USDA, the U.S. Federal Trade Commission (“FTC”), and the U.S. Departments of Commerce, and Labor, as well as by similar authorities in the foreign countries in which we do business. Environmental laws including the Clean Air Act, the Clean Water Act, the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended, and the National Organic Standards of the U.S. Department of Agriculture, as well as similar state and local statutes and regulations in the United States and in each of the foreign countries in which we do business apply to our business operations as well. These laws and regulations govern, among other things, air emissions and the discharge of wastewater and other pollutants, the use of refrigerants, the handling and disposal of hazardous materials, and the cleanup of contamination in the environment.

In addition, the marketing and advertising of our products could make us the target of claims relating to alleged false or deceptive advertising under federal, state, and foreign laws and regulations, and we may be subject to initiatives that limit or prohibit the marketing and advertising of our products to children.

We are also subject to federal laws and regulations relating to our organic products and production. For example, as required by the National Organic Program (“NOP”), we rely on third parties to certify certain of our products and production locations as organic. Regulations and formal and informal positions taken by the NOP pursuant to the Organic Foods Production Act of 1990, which created the NOP, are subject to continued review and scrutiny.

Changes in these laws or regulations or the introduction of new laws or regulations could increase our compliance costs, increase other costs of doing business for us, our customers, or our suppliers, or restrict our actions, which could adversely affect our results of operations. In some cases, new laws and regulations or other federal and state regulatory initiatives could interrupt distribution of our products or force changes in our production processes and our products. Governmental regulations also affect taxes and levies, healthcare costs, energy usage, immigration, and other labor issues, all of which may have a direct or indirect effect on our business or those of our customers or suppliers. These costs could negatively affect our results of operations and financial condition. Further, if we are found to be in violation of applicable laws and regulations in these areas, we could be subject to civil remedies, including third-party claims for property damage or personal injury, fines, injunctions, recalls, cleanup costs, and other civil sanctions, as well as potential criminal sanctions, any of which could have a material adverse effect on our business.

RISKS RELATED TO COVID-19 AND OTHER PANDEMIC OR DISEASE OUTBREAKS

Pandemics or disease outbreaks, such as the COVID-19 pandemic, may disrupt consumption and trade patterns, supply chains, available labor supply, and production processes, which could materially affect our operations and results of operations.

The ultimate impact that the COVID-19 pandemic or any future pandemic or disease outbreak will have on our business and our consolidated results of operations is uncertain.

To date we have seen increased customer and consumer demand for our products. We have not experienced significant supply chain disruptions or labor supply shortages and we have continued to be able to satisfy customer and consumer demand for our products. However, the COVID-19 pandemic, or any future pandemic, may limit the availability of, or increase the cost of, employees, ingredients, packaging and other inputs necessary to produce our products, and our operations may be negatively impacted. In 2022, our costs increased primarily due to inflationary price increases of milk, other ingredients, packaging materials, and freight. However, because of market conditions or for competitive reasons, our pricing actions may sometimes lag input cost changes, or we may not be able to pass along the full effect of increases in raw materials and other input costs as we incur them.

In 2022, social distancing, shelter-in-place and work-from-home mandates and recommendations have begun to be reduced or eliminated. The increased customer demand we have realized over the past two years as consumers increased their at-home consumption and e-commerce purchasing during the COVID-19 pandemic may change or decrease due to the decrease in social distancing and stay-at-home and work-from-home mandates and recommendations. We are unable to predict the nature and timing of when such change may occur, if at all.

The ultimate impact of the COVID-19 pandemic on our business will depend on many factors, including, among others, whether additional waves of COVID-19 or different variants of COVID-19 will affect the United States and other markets and the duration of any social distancing and stay home and work from home mandates or recommendations that may occur as a result of such COVID-19 wave or variant; our ability and the ability of our suppliers to continue to maintain production despite unprecedented demand in the food industry, supply chain disruptions, tight labor markets and increased raw materials and packaging costs; and the extent to which macroeconomic conditions resulting from the pandemic and the pace of the subsequent recovery impact consumer eating and shopping habits. We cannot predict the duration or scope of the disruption or the impact of any recovery from the impacts of COVID-19. Therefore, the financial impact cannot be reasonably estimated at this time.

Future pandemics or disease outbreaks could similarly adversely affect economies and financial markets, consumer spending and confidence levels and result in an economic downturn that affects customer demand for our products. Our efforts to manage and mitigate these risks may be unsuccessful, and the effectiveness of these efforts depends on factors beyond our control, including the duration and severity of any pandemic or disease outbreak, as well as third party actions taken to contain its spread and mitigate public health effects.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We operate the following facilities:

Location	Owned / Leased	Principal Use
Morton Grove, Illinois	Owned	Production of kefir and cheese, principal executive offices
Waukesha, Wisconsin	Owned	Production of kefir, administrative offices
Niles, Illinois	Owned	Distribution center, administrative offices
Philadelphia, Pennsylvania	Owned	Production of kefir and cheese, administrative offices

Lifeway believes that its facilities are adequate for its current needs and that suitable additional space will be available on commercially acceptable terms as required. We believe that we have adequate insurance coverage for all our properties.

ITEM 3. LEGAL PROCEEDINGS

From time to time, we are engaged in litigation matters arising in the ordinary course of business. While the results of litigation and claims cannot be predicted with certainty, Lifeway believes that no such matter is reasonably likely to have a material adverse effect on our financial position or results of operations.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is listed on the Nasdaq Global Market under the symbol "LWAY." Trading commenced on March 29, 1988. As of March 14, 2023, there were approximately 49 holders of record of Lifeway's Common Stock, one of which was Cede & Co., a nominee for Depository Trust Company, or DTC, and 73 financial institutions as nominees for beneficial owners or in "street name" the shares of which were deposited into participant accounts at DTC and are considered to be held of record by Cede & Co. as one stockholder.

Common stock price

The following table shows the high and low sale prices per share of our common stock as reported on the Nasdaq Global Market for each quarter during the two most recent fiscal years:

	Common Stock Price Range	
	2021	
	Low	High
First Quarter	\$ 5.21	\$ 6.90
Second Quarter	\$ 4.56	\$ 5.71
Third Quarter	\$ 5.15	\$ 7.04
Fourth Quarter	\$ 4.60	\$ 5.85
	2022	
	Low	High
First Quarter	\$ 4.55	\$ 8.42
Second Quarter	\$ 4.56	\$ 7.22
Third Quarter	\$ 4.60	\$ 7.86
Fourth Quarter	\$ 5.26	\$ 7.66

Dividend Policy

Lifeway does not routinely declare and pay dividends. From time to time however our Board of Directors may declare and pay dividends depending on our operating cash flow, financial condition, capital requirements and such other factors as the Board of Directors may deem relevant.

There were no dividends declared or paid in fiscal 2022 or 2021.

Issuer Purchases of Equity Securities

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of a publicly announced program (a)	Approximate Dollar Value of Shares that may yet be Purchased Under the Plans or Programs (\$ in thousands)
7/1/2021 to 7/31/2021	250,000	\$ 6.33	250,000	\$ —
Fiscal Year 2021	250,000	\$ 6.33	250,000	\$ —
11/1/2022 to 11/30/2022	850,340 (b)	\$ 4.70	—	\$ —
Fiscal Year 2022	850,340	\$ 4.70	—	\$ —

- (a) During the fourth quarter of 2015, Lifeway publicly announced a share repurchase program. On November 1, 2017, our Board of Directors amended the 2015 stock repurchase program (the “2017 amendment”), by adding to (i.e., exclusive of the shares previously authorized under the 2015 stock program repurchase) the authorization the lesser of \$5,185 or 625 shares. The program has no expiration date. As of April 2020, the Company had reached the amended threshold of 625 shares and therefore no shares of common stock remain available to be purchased under the 2017 Repurchase Plan Amendment. On June 24, 2021, our Board authorized a plan to repurchase up to 250 shares of Common Stock in the open market within 24 months at no more than \$10 per share (the “2021 Repurchase Plan”). As of December 31, 2021, the Company had reached the threshold of 250 shares and therefore no shares of common stock remain available to be purchased under the 2021 Repurchase Plan Amendment.
- (b) On November 7, 2022, the Company entered into a Stock Purchase Agreement with Ludmila Smolyansky (“Ms. Smolyansky”), to purchase 850,340 shares of Lifeway common stock from Ms. Smolyansky in a privately negotiated share repurchase (the “Share Repurchase”). The Share Repurchase closed on November 30, 2022.

ITEM 6. [RESERVED]

ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of the financial condition and results of operations as of and for the years ended December 31, 2022 and 2021 should be read in conjunction with the audited consolidated financial statements and the notes to those statements that are included elsewhere in this Annual Report on Form 10-K. In addition to historical information, the following discussion contains certain forward-looking statements within the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. These statements relate to our future plans, objectives, expectations and intentions. These statements may be identified by the use of words such as “may,” “could,” “believe,” “future,” “depend,” “expect,” “will,” “result,” “can,” “remain,” “assurance,” “subject to,” “require,” “limit,” “impose,” “guarantee,” “restrict,” “continue,” “become,” “predict,” “likely,” “opportunities,” “effect,” “change,” “future,” “predict,” and “estimate,” and similar terms or terminology, or the negative of such terms or other comparable terminology. Although we believe the expectations expressed in these forward-looking statements are based on reasonable assumptions within the bounds of our knowledge of our business, our actual results could differ materially from those discussed in these statements. Factors that could contribute to such differences include, but are not limited to, those discussed in the “Risk Factors” section in Part I, Item 1A. We undertake no obligation to update publicly any forward-looking statements for any reason even if new information becomes available or other events occur in the future.

Recent Developments

COVID-19 Pandemic Impact

We have seen increased customer and consumer demand for our products during the pandemic as consumers increased their food purchases for in-home consumption. We have not experienced significant supply chain disruptions or labor supply shortages and have continued to satisfy customer and consumer demand for our products. Management continues to proactively manage the supply and transportation of materials used to make and package our products, staffing, and transportation of our products to customers. This proactive planning has allowed the Company to avoid disruption to its manufacturing facilities and production, transportation, and sales and to meet the increased demand. The Company has maintained full production capacity available at all locations and does not anticipate manufacturing or staffing disruptions in the near term.

However, the COVID-19 pandemic, or any future pandemic, may limit the availability of, or increase the cost of, employees, ingredients, packaging and other inputs necessary to produce our products, and our operations may be negatively impacted. In 2022, our costs increased primarily due to inflationary price increases of milk, other ingredients, packaging materials, and transportation to our customers. However, because of market conditions or for competitive reasons, our pricing actions may sometimes lag input cost changes, or we may not be able to pass along the full effect of increases in raw materials and other input costs as we incur them.

During 2022, social distancing, shelter-in-place and work-from-home mandates and recommendations have continued to be reduced or eliminated. The increased customer demand for our products as consumers increased their at-home consumption and e-commerce purchasing during the COVID-19 pandemic may change or decrease due to the decrease in social distancing and stay-at-home and work-from-home mandates and recommendations. We are unable to predict the nature and timing of when such change may occur, if at all.

Results of Operations

Comparison of Year Ended December 31, 2022 to Year Ended December 31, 2021 (in 000's)

	December 31,			
	2022		2021	
	\$	%	\$	%
Net sales	141,568	100.0%	119,065	100.0%
Cost of goods sold	112,350	79.4%	87,604	73.6%
Depreciation expense	2,432	1.7%	2,751	2.3%
Total cost of goods sold	114,782	81.1%	90,355	75.9%
Gross profit	26,786	18.9%	28,710	24.1%
Selling expenses	11,304	8.0%	11,097	9.3%
General & administrative expenses	12,593	8.9%	11,611	9.8%
Amortization expense	540	0.4%	122	0.1%
Total operating expenses	24,437	17.2%	22,830	19.2%
Income from operations	2,349	1.7%	5,880	4.9%
Other income (expense):				
Interest expense	(267)	(0.2%)	(116)	(0.1%)
Gain on investments	–	0.0%	2	0.0%
Loss on sale of property and equipment	(241)	(0.2%)	(88)	(0.1%)
Other Income, net	–	0.0%	(62)	0.0%
Total other income (expense)	(508)	(0.4%)	(264)	(0.2%)
Income before provision for income taxes	1,841	1.3%	5,616	4.7%
Provision for income taxes	917	0.6%	2,305	1.9%
Net income	924	0.7%	3,311	2.8%

Net Sales

Net sales were \$141,568 for the year ended December 31, 2022, an increase of \$22,503 or 18.9% versus prior year. The net sales increase was primarily driven by higher volumes of our branded drinkable kefir and the impact of price increases implemented during the year, and to a lesser extent, the favorable impact of our acquisition of Glen Oaks Farms during the third quarter of 2021. Approximately 18% of the net sales increase results from the full year 2022 impact of our acquisition of Glen Oaks Farms during the third quarter of 2021.

Gross Profit

Gross profit as a percentage of net sales decreased to 18.9% during the year ended December 31, 2022 from 24.1% during the same period in 2021. The decrease versus the prior year was primarily due to the unfavorable impact of milk pricing, and the inflationary price increases of other ingredients, packaging materials, and freight, partially offset by the decrease in depreciation expense and favorable labor efficiency due to increased volumes. We took favorable pricing actions during 2022 to recover a portion of the input and freight cost inflation. However, for market conditions or competitive reasons, our pricing actions may also lag input cost changes, or we may not be able to pass along the full effect of increases in raw materials and other input costs as we incur them.

Selling Expenses

Selling expenses increased by \$207 to \$11,304 during the year ended December 31, 2022 from \$11,097 during the same period in 2021. The increase versus prior year is primarily due to increased investment in advertising and marketing programs, increased broker expense, partially offset by lower compensation expense.

General and Administrative Expenses

General and administrative expenses increased \$982 to \$12,593 during the year ended December 31, 2022 from \$11,611 during the same period in 2021. The increase is primarily a result of increased legal and professional fees, which include expense related to non-routine stockholder action, the fiscal year 2020 Form 10-K restatement, and incentive compensation, partially offset by lower consulting expense to our former Chairperson of the Board of Directors.

Provision for Income Taxes

The provision for income taxes includes federal, state and local income taxes. The provision for income taxes was \$917 and \$2,305 during the year ended December 31, 2022 and 2021, respectively.

Our effective income tax rate was 49.1% in 2022 compared to 41.0% in 2021. The statutory Federal and state tax rates remained consistent from 2021 to 2022. The Company has a number of items that are nondeductible or are discrete adjustments to tax expense. The Company consistently reflects non-deductible officer compensation expense, non-deductible compensation expense related to equity incentive awards and separate state tax rates from year to year. Although similar items were reflected in 2022, the percentage effect is different due to the difference in pre-tax income in 2022 compared to 2021.

Our effective tax rate may change from period to period based on recurring and non-recurring factors including the relative mix of pre-tax earnings (or losses), the underlying income tax rates applicable to various state and local taxing jurisdictions, enacted tax legislation, the impact of non-deductible items, changes in valuation allowances, and the expiration of the statute of limitations in relation to unrecognized tax benefits. We record discrete income tax items such as enacted tax rate changes in the period in which they occur.

Section 162(m) of the Internal Revenue Code (the "Code") limits the deductibility of compensation paid to certain of our executives to the extent their total compensation exceeds \$1 million in any taxable year.

Income taxes are discussed in Note 10 in the Notes to the Consolidated Financial Statements.

Net Income (Loss)

We reported net income of \$924 or \$0.06 per basic and diluted common share for the year ended December 31, 2022 compared to net income of \$3,311 or \$0.21 per basic and diluted common share in the same period in 2021.

Liquidity and Capital Resources

Management assesses the Company's liquidity in terms of its ability to generate cash to fund its operating, investing, and financing activities. The Company remains in a strong financial position, and while it has been impacted by the macroeconomic challenges with commodity inflation and other input cost increases, the Company believes that its cash flow from operations, revolving credit and term loan facility, and cash and cash equivalents will continue to provide sufficient liquidity for its working capital needs, capital resource requirements, and growth initiatives and to ensure the continuation of the Company as a going concern.

If additional borrowings are needed, \$2,223 was available under the Revolving Credit Facility as of December 31, 2022 (see Note 7, Debt). We are in compliance with the terms of the Credit Agreement and expect to meet foreseeable financial requirements. The success of our business and financing strategies will continue to provide us with the financial flexibility to take advantage of various opportunities as they arise. To date, we have been successful in generating cash and obtaining financing as needed. However, if a serious economic or credit market crisis ensues, it could have a negative effect on our liquidity, results of operations and financial condition.

The Company's most significant ongoing short-term cash requirements relate primarily to funding operations (including expenditures for raw materials, labor, manufacturing and distribution, trade and promotions, advertising and marketing, and income tax liabilities) as well as expenditures for property, plant, and equipment.

Long-term cash requirements primarily relate to funding long-term debt repayments (see Note 7, Debt) and deferred income taxes (see Note 10, Income Taxes).

The following table is derived from our Consolidated Statement of Cash Flows:

	Year Ended December 31,	
	2022	2021
Net Cash Flows Provided By (Used In):		
Operating activities	\$ 3,987	\$ 5,564
Investing activities	\$ (4,029)	\$ (7,142)
Financing activities	\$ (4,747)	\$ 2,885

Operating Activities

Net cash provided by operating activities was \$3,987 in 2022 compared to \$5,564 in 2021. The decrease was primarily due to lower cash earnings, which reflect the impact of input and freight cost inflation in 2022, and the change in working capital.

Investing Activities

Net cash used in investing activities was \$4,029 in 2022 compared to \$7,142 in 2021. The decrease in cash used reflects the August 2021 acquisition of GlenOaks Farms, Inc., partially offset by increased capital spending in 2022. Our capital spending is focused in three core areas: growth, cost reduction, and facility improvements. Growth capital spending supports new product innovation and enhancements. Cost reduction and facility improvements support manufacturing efficiency, safety, and productivity.

Financing Activities

Net cash used in financing activities was \$4,747 during 2022 compared to net cash provided by financing activities of \$2,885 in 2021. The decrease in cash used relates to the term loan entered into during August 2021 in connection with the acquisition of GlenOaks Farms, Inc., partially offset by the quarterly principal payments under the term loan.

On June 24, 2021, Lifeway's Board authorized a plan to repurchase up to 250 shares of Common Stock in the open market within 24 months at no more than \$10 per share. We repurchased all 250 shares of common stock at a cost of \$1,583 during the three-month period ended September 30, 2021. We intend to hold repurchased shares in treasury for general corporate purposes, including issuances under our 2015 Omnibus Incentive Plan. Treasury shares are accounted for using the cost method.

On November 7, 2022, the Company entered into a Stock Purchase Agreement with Ludmila Smolyansky ("Ms. Smolyansky"), to purchase 850,340 shares of Lifeway common stock from Ms. Smolyansky, Board of Director member. The shares were repurchased during the fourth quarter of 2022.

Pursuant to the Stock Purchase Agreement, the Company and Ms. Smolyansky have agreed, among other things, that (i) Ms. Smolyansky will sell the shares at a purchase price of \$4.70 per share, which represents a twenty percent (20.0%) discount to the average closing price of the common stock on Nasdaq over the five (5) trading day period ended on the trading day immediately preceding the date of the Stock Purchase Agreement and (ii) Ms. Smolyansky will use a portion of the proceeds to satisfy in full certain obligations of Ms. Smolyansky, which are secured by previously disclosed pledges of common stock, causing all such pledges to be released. The purchased shares will be held in treasury by the Company.

Debt Obligations

On August 18, 2021, Lifeway entered into the Fourth Modification (the "Fourth Modification") to the Amended and Restated Loan and Security Agreement (as amended and modified from time to time, the "Credit Agreement") with its existing lender and certain of its subsidiaries. The Fourth Modification amends the Credit Agreement to provide for, among other things, a \$5 million term loan by the existing lender to the borrowers to be repaid in quarterly installments of principal and interest over a term of five years (the "Term Loan"). The termination date of the Term Loan is August 18, 2026, unless earlier terminated. Except for the addition of the Term Loan, the Credit Agreement remains substantively unchanged and in full force and effect.

As of December 31, 2022, we had \$2,777 outstanding under the Revolving Credit Facility and \$3,727 outstanding under the note payable, net of \$23 of unamortized deferred financing fees. We had \$2,223 available for future borrowings under the Revolving Credit Facility as of December 31, 2022. As amended, all outstanding amounts under the Loans bear interest, at Lifeway's election, at either the lender Base Rate (the Prime Rate minus 1.00%) or the LIBOR plus 1.95%, payable monthly in arrears. Lifeway is also required to pay a quarterly unused line fee of 0.20% on the Revolving Credit Facility and, in conjunction with the issuance of any letters of credit, a letter of credit fee of 0.20%.

The Company's interest rate on debt outstanding under the revolving line of credit and note payable as of December 31, 2022 was 6.17% and 6.29%, respectively.

We are in compliance with all applicable financial debt covenants as of December 31, 2022. See Note 7 to our Consolidated Financial Statements for additional information regarding our indebtedness and related agreements.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet financing arrangements as defined in Item 303(a)(4) of Regulation S-K.

Contractual Obligations

Not applicable.

Critical Accounting Estimates

Critical accounting estimates are those estimates made in accordance with U.S. GAAP that involve a significant level of estimation uncertainty and have had or are reasonably likely to have a material impact on the financial condition or results of operations of the registrant. In many cases, the accounting treatment of a particular transaction is specifically dictated by U.S. GAAP with no need for the application of our judgement. In certain circumstances, the preparation of our Consolidated Financial Statements in conformity with U.S. GAAP requires us to use our judgment to make certain estimates and assumptions. These estimates affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the Consolidated Financial Statements and the reported amounts of net sales and expenses during the reporting period. We believe in the quality and reasonableness of our critical accounting estimates; however, materially different amounts might be reported under different conditions or using assumptions, estimates or making judgments different from those that we have applied. Management has discussed the development and selection of these critical accounting policies, as well as our significant accounting policies (see Note 2 to the Consolidated Financial Statements), with the Audit Committee of our Board of Directors. We have identified the policies described below as our critical accounting policies.

Goodwill impairment

Goodwill totaled \$11,704 as of December 31, 2022. The Company completed its annual goodwill impairment analysis as of December 31, 2022. Our assessment did not result in an impairment. Goodwill represents the excess purchase price over the fair value of the net tangible and other identifiable intangible assets acquired. We estimate the fair value of our one reporting unit annually (as of December 31), or more frequently if certain conditions exist, using a combination of the fair values derived from both the income approach and the market approach. Under the income approach, we calculate the fair value of a reporting unit based on the present value of estimated future cash flows. Cash flow projections are based on our estimates of revenue growth rates and operating margins, taking into consideration industry and market conditions. The discount rate used to determine the present value of future cash flows is based on the weighted-average cost of capital adjusted for the relevant risk associated with business-specific characteristics and the uncertainty related to the business's ability to execute on the projected cash flows. The market approach estimates fair value based on market multiples of revenue and earnings derived from comparable publicly-traded companies with similar operating and investment characteristics. The resulting fair value, based on the income and market approaches, is then compared to the carrying value to determine if impairment is necessary.

Sales discounts & allowance

We offer various trade promotions and sales incentive programs to customers and consumers. From time to time, we grant certain sales discounts to customers which are classified as a reduction in sales. The measurement and recognition of discounts and allowances involve the use of judgment and our estimates are made based on historical experience and specific customer program accruals. Differences between estimated and actual discount and allowance costs are normally not material and are recognized in earnings in the period such differences are determined. The process for analyzing trade promotion programs could impact our results of operations and trade spending accruals depending on how actual results of the programs compare to original estimates. As of December 31, 2022, we had \$1,800 of accrued discounts and allowances.

Share-based compensation

Certain employees and non-employee directors receive various forms of share-based payment awards, and we recognize compensation expense for these awards based on their grant date fair values. The grant fair value of Restricted Stock Units ("RSUs") and Performance Share Unit ("PSUs") awards is equal to the Company's closing stock price on the grant date. The Company granted RSU and PSU awards during 2022 to employees under the 2022 long-term incentive-based plan, and RSU awards to non-employee Directors under the 2022 Non-Employee Director Equity and Deferred Compensation Plan. We do not estimate forfeitures in measuring the grant date fair value, but rather account for forfeitures as they occur. See Note 11 to our consolidated financial statements for further detail.

Income taxes

We pay income taxes based on tax statutes, regulations, and case law of the various jurisdictions in which we operate. At any given time, multiple tax years are subject to audit by the various taxing authorities. Income taxes are accounted for under the asset and liability method. Deferred income tax assets and liabilities are recognized for the future tax effects of temporary differences between financial and income tax reporting using tax rates in effect for the years in which the differences are expected to reverse. The assumptions about future taxable income require the use of significant judgment and are consistent with the plans and estimates we are using to manage our underlying businesses.

We recognize an income tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities based on the technical merits of the position. The income tax benefit recognized in our financial statements from such a position is measured based on the largest estimated benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. These judgments and estimates made at a point in time may change based on the outcome of tax audits and changes to, or further interpretations of, regulations. If such changes take place, there is a risk that our tax rate may increase or decrease in any period, which would impact our earnings. Future business results may affect deferred tax liabilities or the valuation of deferred tax assets over time.

Recent Accounting Pronouncements.

See Note 2, Summary of Significant Accounting Policies, in the Notes to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K for information regarding recent accounting pronouncements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and
Stockholders of Lifeway Foods, Inc. and Subsidiaries:

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheet of Lifeway Foods, Inc. and Subsidiaries (the "Company") as of December 31, 2021, the related consolidated statement of operations, stockholders' equity, and cash flows for the year ended December 31, 2021, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2021, and the results of its operations and its cash flows for the year ended December 31, 2021, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audit we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audit included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audit provide a reasonable basis for our opinion.

/s/ Mayer Hoffman McCann P.C.

We have served as the Company's auditor since 2015, which ended in 2022
Chicago, Illinois
July 21, 2022

Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Lifeway Foods, Inc.

Opinion on the financial statements

We have audited the accompanying consolidated balance sheet of Lifeway Foods, Inc. and subsidiaries (the “Company”) as of December 31, 2022, the related consolidated statements of operations, stockholders’ equity, and cash flows for the year ended December 31, 2022, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2022, and the results of its operations and its cash flows for the year ended December 31, 2022, in conformity with accounting principles generally accepted in the United States of America.

Basis for opinion

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audit. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audit we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audit included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audit also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Critical audit matters

Critical audit matters are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. We determined that there are no critical audit matters.

/s/ GRANT THORNTON LLP

We have served as the Company’s auditor since 2022.

Chicago, Illinois
March 27, 2023

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
December 31, 2022 and 2021
(In thousands)

	December 31,	
	2022	2021
Current assets		
Cash and cash equivalents	\$ 4,444	\$ 9,233
Accounts receivable, net of allowance for doubtful accounts and discounts & allowances of \$1,820 and \$1,170 at December 31, 2022 and 2021, respectively	11,414	9,930
Inventories, net	9,631	8,285
Prepaid expenses and other current assets	1,445	1,254
Refundable income taxes	44	344
Total current assets	26,978	29,046
Property, plant and equipment, net	20,905	20,130
Operating lease right-of use asset	174	216
Goodwill	11,704	11,704
Intangible assets, net	7,438	7,978
Other assets	1,800	1,800
Total assets	\$ 68,999	\$ 70,874
Current liabilities		
Current portion of note payable	\$ 1,250	\$ 1,000
Accounts payable	7,979	6,614
Accrued expenses	3,813	3,724
Accrued income taxes	–	725
Total current liabilities	13,042	12,063
Line of credit	2,777	2,777
Note payable	2,477	3,470
Operating lease liabilities	104	85
Deferred income taxes, net	3,029	3,201
Other long-term liabilities	–	147
Total liabilities	21,429	21,743
Commitments and contingencies (Note 9)		
Stockholders' equity		
Preferred stock, no par value; 2,500 shares authorized; none issued	–	–
Common stock, no par value; 40,000 shares authorized; 17,274 shares issued; 14,645 and 15,435 shares outstanding at 2022 and 2021	6,509	6,509
Paid-in capital	3,624	2,552
Treasury stock, at cost	(16,993)	(13,436)
Retained earnings	54,430	53,506
Total stockholders' equity	47,570	49,131
Total liabilities and stockholders' equity	\$ 68,999	\$ 70,874

See accompanying notes to consolidated financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Operations
For the Years Ended December 31, 2022 and 2021
(In thousands, except per share data)

	<u>2022</u>	<u>2021</u>
Net sales	\$ 141,568	\$ 119,065
Cost of goods sold	112,350	87,604
Depreciation expense	2,432	2,751
Total cost of goods sold	<u>114,782</u>	<u>90,355</u>
Gross profit	26,786	28,710
Selling expenses	11,304	11,097
General and administrative	12,593	11,611
Amortization expense	540	122
Total operating expenses	24,437	22,830
Income from operations	2,349	5,880
Other income (expense):		
Interest expense	(267)	(116)
Realized gain on investments, net	-	2
Loss on sale of property and equipment	(241)	(88)
Other (expense) income	-	(62)
Total other income (expense)	<u>(508)</u>	<u>(264)</u>
Income before provision for income taxes	1,841	5,616
Provision for income taxes	917	2,305
Net income	\$ 924	\$ 3,311
Basic earnings per common share	\$ 0.06	\$ 0.21
Diluted earnings per common share	\$ 0.06	\$ 0.21
Weighted average number of shares outstanding - Basic	15,396	15,537
Weighted average number of shares outstanding - Diluted	15,718	15,773

See accompanying notes to consolidated financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Stockholders' Equity
For the Years Ended December 31, 2022 and 2021
(In thousands)

	<u>Common Stock</u>				<u>Paid-In Capital</u>	<u>Retained Earnings</u>	<u>Total Equity</u>
	<u>Issued</u>		<u>In treasury</u>				
	<u>Shares</u>	<u>\$</u>	<u>Shares</u>	<u>\$</u>			
Balance, January 1, 2021	17,274	\$ 6,509	(1,669)	\$ (12,450)	\$ 2,600	\$ 50,195	\$ 46,854
Treasury stock purchased	–	–	(250)	(1,583)	–	–	(1,583)
Issuance of common stock in connection with stock-based compensation	–	–	80	597	(721)	–	(124)
Stock-based compensation	–	–	–	–	673	–	673
Net income	–	–	–	–	–	3,311	3,311
Balance, December 31, 2021	17,274	\$ 6,509	(1,839)	\$ (13,436)	\$ 2,552	\$ 53,506	\$ 49,131
Treasury stock purchased	–	–	(850)	(3,997)	–	–	(3,997)
Issuance of common stock in connection with stock-based compensation	–	–	60	440	(558)	–	(118)
Stock-based compensation	–	–	–	–	1,630	–	1,630
Net Income	–	–	–	–	–	924	924
Balance, December 31, 2022	17,274	\$ 6,509	(2,629)	\$ (16,993)	\$ 3,624	\$ 54,430	\$ 47,570

See accompanying notes to consolidated financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Years Ended December 31, 2022 and 2021
(In thousands)

	2022	2021
Cash flows from operating activities:		
Net income	\$ 924	\$ 3,311
Adjustments to reconcile net income to operating cash flow:		
Depreciation and amortization	2,972	2,873
Non-cash interest expense	6	11
Non-cash rent expense	–	1
Bad debt expense	–	2
Deferred revenue	(28)	(30)
Stock-based compensation	1,109	1,144
Deferred income taxes	(172)	257
Loss on sale of property and equipment	241	88
(Increase) decrease in operating assets:		
Accounts receivable	(1,483)	(1,931)
Inventories	(1,345)	(1,356)
Refundable income taxes	300	(313)
Prepaid expenses and other current assets	(191)	(91)
Increase (decrease) in operating liabilities:		
Accounts payable	1,945	1,022
Accrued expenses	434	504
Accrued income taxes	(725)	72
Net cash provided by operating activities	3,987	5,564
Cash flows from investing activities:		
Purchases of property and equipment	(3,449)	(1,922)
Acquisition, net of cash acquired	(580)	(5,220)
Net cash used in investing activities	(4,029)	(7,142)
Cash flows from financing activities:		
Purchase of treasury stock	(3,997)	(1,583)
Payment of deferred financing cost	–	(32)
Proceeds from note payable	–	5,000
Repayment of note payable	(750)	(500)
Net cash (used in) provided by financing activities	(4,747)	2,885
Net (decrease) increase in cash and cash equivalents	(4,789)	1,307
Cash and cash equivalents at the beginning of the period	9,233	7,926
Cash and cash equivalents at the end of the period	\$ 4,444	\$ 9,233
Supplemental cash flow information:		
Cash paid for income taxes, net of (refunds)	\$ 1,121	\$ 2,288
Cash paid for interest	\$ 247	\$ 102
Non-cash investing activities		
Increase in right-of-use assets and operating lease obligations	\$ 83	\$ 45
Business acquisition escrow payable	\$ –	\$ 580

See accompanying notes to consolidated financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
December 31, 2022 and 2021
(In thousands)

Note 1 – Basis of presentation

The consolidated financial statements and accompanying notes have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”). The consolidated financial statements include all of the assets, liabilities and results of operations of Lifeway Foods, Inc. and its wholly owned subsidiaries (collectively “Lifeway” or the “Company”). All inter-company balances and transactions have been eliminated in the consolidated financial statements.

Note 2 – Summary of significant accounting policies

Use of estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to use judgement to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of net sales and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates made in preparing the consolidated financial statements include the reserve for promotional allowances, the valuation of goodwill and intangible assets, stock-based and incentive compensation, and deferred income taxes.

During the fourth quarter of 2021, the Company completed an assessment of the useful life of its \$3,700 indefinite-lived brand name intangible asset and determined that it should adjust the estimated useful life from an indefinite length to 15 years. The change in accounting estimate was effective January 1, 2022, at which time the Company began amortizing the asset over 15 years. The future amortization expense is included in the five-year intangible asset amortization table in Note 5 – Goodwill and Intangible Assets.

Going Concern

The Company follows the guidance in Accounting Standards Codification (“ASC”) 205-40, Presentation of Financial Statements - Going Concern which requires management to assess an entity’s ability to continue as a going concern and to provide related disclosure in certain circumstances. There were no conditions or events, when considered in the aggregate, that raise substantial doubt about the Company’s ability to continue as a going concern within one year after the date the financial statements are issued.

Cash and cash equivalents

Lifeway considers cash and all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Cash and cash equivalents are stated at cost, which approximates or equals fair value due to their short-term nature.

Lifeway from time to time may have bank deposits in excess of insurance limits of the Federal Deposit Insurance Corporation. The Company places its cash and cash equivalents with high credit quality financial institutions. Lifeway has not experienced any losses in such accounts and believes the financial risks associated with these financial instruments are minimal.

The Company has no restricted cash as of December 31, 2022. The Restricted cash escrow funds of \$580 were deposited by Lifeway in connection with the September 18, 2021 acquisition of certain assets of Glen Oaks Farms, Inc. The funds are security for the liability and indemnity obligations of seller as defined under the asset purchase agreement. The escrow funds were remitted to the sellers in August 2022.

Revenue Recognition

Lifeway sells food and beverage products across select product categories to customers predominantly within the United States (see Note 12 - Segments, Products and Customers). The Company also sells bulk cream, a byproduct of its fluid milk manufacturing process. In accordance with ASC 606, Revenue from Contracts with Customers, Lifeway recognizes revenue when control over the products transfers to its customers, which generally occurs upon delivery to its customers or their common carriers. The amount of revenue recognized reflects the consideration to which the Company expects to be entitled to receive in exchange for these goods or services, using the five-step method required by ASC 606.

For the Company, the contract is the approved sales order, which may also be supplemented by other agreements that formalize various terms and conditions with customers. The Company applies judgment in determining the customer's ability and intention to pay, which is based on a variety of factors including the customer's historical payment experience or, in the case of a new customer, published credit and financial information pertaining to the customer.

Performance obligations promised in a contract are identified based on the goods or services that will be transferred to the customer, which is the delivery of food and beverage products which provide immediate benefit to the customer.

Lifeway accounts for product shipping and handling as fulfillment activities with revenues for these activities recorded within net revenue and costs recorded within cost of goods sold. Any taxes collected on behalf of government authorities are excluded from net revenues.

Variable consideration, which includes known or expected pricing or revenue adjustments, such as trade discounts, allowances for non-saleable products, product returns, trade incentives and coupon redemption, is estimated utilizing the most likely amount method.

Key sales terms, such as pricing and quantities ordered, are established on a frequent basis such that most customer arrangements and related incentives have a one year or shorter duration. As such, the Company does not capitalize contract inception costs and it capitalizes product fulfillment costs in accordance with U.S. GAAP and its inventory policies. It generally does not receive noncash consideration for the sale of goods, nor does it grant payment financing terms greater than one year.

Accounts Receivable

Lifeway provides credit terms to customers in-line with industry standards and maintain allowances for potential credit losses based on historical experience. Customer balances are written off after all collection efforts are exhausted. Estimated product returns, which have not been material, are deducted from sales at the time of revenue recognition. The Company does not charge interest on past due accounts receivable.

Inventories

Inventories are stated at the lower of cost or net realizable value, valued on a first in, first out basis ("FIFO"). The costs of finished goods inventories include raw materials, direct labor, and overhead costs. Inventories are stated net of reserves for excess or obsolete inventory.

Property, plant and equipment

Property, plant and equipment are recorded at cost. Depreciation and amortization are calculated using the straight-line method over the estimated useful lives of the assets as follows:

Asset	Useful Life
Buildings and improvements	10 – 39 years
Machinery and equipment	5 – 12 years
Office equipment	3 – 7 years
Vehicles	5 years
Leasehold improvements	Shorter of expected useful life or lease term

The Company performs impairment tests when circumstances indicate that the carrying value of an asset may not be recoverable. Expenditures for repairs and maintenance, which do not improve or extend the life of the assets, are expensed as incurred.

Intangible Assets

Goodwill

Goodwill represents the excess purchase price over the fair value of the net tangible and other identifiable intangible assets acquired. Lifeway estimates the fair value of its one reporting unit annually (as of December 31), or more frequently if certain conditions exist, using a combination of the fair values derived from both the income approach and the market approach. Under the income approach, it calculates the fair value of a reporting unit based on the present value of estimated future cash flows. Cash flow projections are based on the Company's estimates of revenue growth rates and operating margins, taking into consideration industry and market conditions. The discount rate used to determine the present value of future cash flows is based on the weighted-average cost of capital adjusted for the relevant risk associated with business-specific characteristics and the uncertainty related to the business's ability to execute on the projected cash flows. The market approach estimates fair value based on market multiples of revenue and earnings derived from comparable publicly traded companies with similar operating and investment characteristics. The resulting fair value, based on the income and market approaches, is then compared to the carrying value to determine if impairment is necessary.

Intangible assets

Intangible assets acquired in a business combination are recorded at their estimated fair values at the date of acquisition. Identifiable intangible assets with finite lives are amortized over their estimated useful lives as follows:

Asset	Useful Life
Recipes	4 years
Brand names	8-15 years
Formula	10 years
Customer lists	5-10 years
Customer relationships	15 years

All amortization expense related to intangible assets is recorded in Amortization expense in the consolidated statements of operations.

Amortizable intangible assets are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Lifeway conducts more frequent impairment assessments if certain conditions exist, such as a change in the competitive landscape, any internal decisions to pursue new or different strategies, a loss of a significant customer, or a significant change in the market place including changes in the prices paid for its products or changes in the size of the market for its products. If an evaluation of the undiscounted cash flows indicates impairment, the asset is written down to its estimated fair value, which is generally based on discounted future cash flows. If the estimated remaining useful life of an intangible asset is changed, the remaining carrying amount of the intangible asset is amortized prospectively over the revised remaining useful life.

Fair value measurements

Fair value is estimated by applying the following hierarchy, which prioritizes the inputs used to measure fair value into three levels and bases the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Inputs that are generally unobservable and typically reflect management’s estimate of assumptions that market participants would use in pricing the asset or liability.

Lifeway’s financial assets and liabilities that are not carried at fair value on a recurring basis include cash and cash equivalents, accounts receivable, other receivables, accounts payable, accrued expenses and revolving line of credit for which carrying value approximates fair value.

The Company records its investments in equity securities without a readily determinable fair value at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. As of December 31, 2022, and 2021, the Company has one investment without a readily determinable fair value which is recorded at \$1,800 in other assets on the consolidated balance sheet. The investment cost of \$1,800 includes a cumulative unrealized gain of \$1,731 resulting from an observable price change in 2019. There were no upward or downward adjustments to the investment cost during 2022 or 2021.

Income taxes

The Provision for income taxes includes federal, state, local and foreign income taxes currently payable, and those deferred because of temporary differences between the financial statement and tax bases of assets and liabilities. Deferred tax assets or liabilities are computed based on the difference between the financial statement and income tax bases of assets and liabilities using enacted tax rates expected to apply to taxable income in the year in which the deferred tax assets or liabilities are expected to be realized or settled. The principal sources of temporary differences are different depreciation and amortization methods for financial statement and tax purposes, incentive compensation, unrealized gain, capitalization of indirect inventory costs for tax purposes, reserves for excess and obsolete inventory and the allowance for doubtful accounts. Valuation allowances are recorded to reduce deferred tax assets when it is more likely not that a tax benefit will not be realized. Deferred income tax expense or benefit is based on the changes in the asset or liability from period to period.

Lifeway analyzes filing positions in all the federal and state jurisdictions where it is required to file income tax returns, as well as all open tax years in these jurisdictions. The Company recognizes the income tax benefit from an uncertain tax position when it is more likely than not that, based on technical merits, the position will be sustained upon examination, including resolutions of any related appeals or litigation processes. It applies a more likely than not threshold to the recognition and derecognition of uncertain tax positions. Accordingly, Lifeway recognizes the amount of tax benefit that has a greater than 50% likelihood of being ultimately realized upon settlement. Future changes in judgment related to the expected ultimate resolution of uncertain tax positions will affect earnings in the period of such change. For those income tax positions where it is not more likely than not that a tax benefit will be sustained, no tax benefit has been recognized in the financial statements. The total amount of unrecognized tax benefits can change due to audit settlements, tax examination activities, statute expirations and the recognition and measurement criteria under accounting for uncertainty in income taxes. Lifeway recognizes penalties and interest related to unrecognized tax benefits in the provision (benefit) for income taxes in the consolidated statements of operations.

Share-based compensation

Share-based compensation expense is recognized for equity awards over the vesting period based on their grant date fair value. The fair value of restricted stock awards is equal to the closing price of Lifeway's stock on the date of grant. The Company does not estimate forfeitures in measuring the grant date fair value, but rather account for forfeitures as they occur. The Company issues share based equity awards from treasury shares.

Treasury stock

Treasury stock is recorded using the cost method.

Advertising costs

Advertising costs are expensed as incurred and reported in Selling expense in the Company's consolidated statements of operations. Expenditures totaled \$3,353 and \$3,267 for the years ended December 31, 2022 and 2021, respectively.

Earnings (loss) per common share

Basic earnings (loss) per common share is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares issued and outstanding during the reporting period. Diluted earnings (loss) per common share is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares issued and outstanding and the effect of all dilutive common stock equivalents related to the Company's outstanding stock-based compensation awards outstanding during the reporting period. For the years ended December 31, 2022 and 2021, there were 322 and 236 common stock equivalents outstanding, respectively.

Segments

The Company is managed as a single reportable segment. The Chief Executive Officer, who is the Company's Chief Operating Decision Maker ("CODM"), reviews financial information on an aggregate basis for purposes of allocating resources and assessing financial performance, as well as for making strategic operational decisions and managing the organization. Substantially all of Lifeway's consolidated revenues relate to the sale of cultured dairy products that it produces using the same processes and materials and are sold to consumers through a common network of distributors and retailers in the United States.

Recent accounting pronouncements

Issued but not yet effective

In October 2021, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2021-08, Business Combinations (Topic 805): Accounting for Contract Assets and Contract Liabilities from Contracts with Customers. The new guidance provides a single comprehensive accounting model on revenue recognition for contracts with customers and requires that the acquirer in a business combination recognize and measure contract assets and liabilities acquired in a business combination in accordance with Topic 606 (Revenue from Contracts with Customers). The amendments in this ASU are effective for fiscal years beginning after December 15, 2022. Early adoption is permitted, including adoption in an interim period. With early adoption, the amendments are applied retrospectively to all business combinations for which the acquisition date occurs on or after the beginning of the fiscal year that includes the interim period of adoption and prospectively to all business combinations that occur on or after the date of initial application. Management does not expect the adoption of this ASU to have a material impact on its consolidated financial statements.

In March 2020, the FASB issued ASU No. 2020-04, Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting. The new guidance provides optional expedients and exceptions for applying U.S. GAAP to contracts, hedging relationships, and other transactions that reference LIBOR or another reference rate expected to be discontinued because of reference rate reform. The guidance will be effective prospectively as of March 12, 2020 through December 31, 2022 and interim periods within those fiscal years. Management will adopt this new guidance effective January 1, 2023, and does not expect the adoption of this ASU to have a material impact on its consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, in November 2018 issued an amendment, ASU 2018-19, Codification Improvements to Topic 326, Financial Instruments - Credit Losses, and in November 2019 issued two amendments, ASU 2019-10, Financial Instruments – Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates, and ASU 2019-11, Codification Improvements to Topic 326, Financial Instruments – Credit Losses. The series of new guidance amends the impairment model by requiring entities to use a forward-looking approach based on expected losses rather than incurred losses to estimate credit losses on certain types of financial instruments, including trade receivables. This may result in the earlier recognition of allowances for losses. The guidance should be applied on either a prospective transition or modified-retrospective approach depending on the subtopic. The guidance is effective for annual periods beginning after December 15, 2022, including interim periods within those fiscal years, with early adoption permitted. Management does not expect the adoption of this ASU to have a material impact on its consolidated financial statements.

Note 3 – Inventories, net

	December 31,	
	2022	2021
Ingredients	\$ 2,859	\$ 2,279
Packaging	3,233	2,723
Finished goods	3,539	3,283
Total inventories, net	<u>\$ 9,631</u>	<u>\$ 8,285</u>

Note 4 – Property, Plant and Equipment, net

	December 31,	
	2022	2021
Land	\$ 1,565	\$ 1,565
Buildings and improvements	19,341	17,920
Machinery and equipment	32,786	32,073
Vehicles	640	640
Office equipment	979	900
Construction in process	1,180	417
	<u>56,491</u>	<u>53,515</u>
Less accumulated depreciation	(35,586)	(33,385)
Total property, plant and equipment, net	<u>\$ 20,905</u>	<u>\$ 20,130</u>

Note 5 – Goodwill and Intangible Assets*Goodwill*

Goodwill consisted of the following:

	Total
Balance at December 31, 2021, before accumulated impairment losses	\$ 12,948
Accumulated impairment losses	(1,244)
Balance at December 31, 2021	<u>\$ 11,704</u>
Balance at December 31, 2022	<u>\$ 11,704</u>

Goodwill

The Company performed the annual impairment assessment of goodwill for its single reporting unit as of December 31, 2022 and 2021, noting no impairment loss. Considerable management judgment is necessary to evaluate goodwill for impairment. Lifeway estimates fair value using widely accepted valuation techniques including discounted cash flows and market multiples analysis with respect to its single reporting unit. These valuation approaches are dependent upon a number of factors, including estimates of future growth rates, its cost of capital, capital expenditures, income tax rates, and other variables. Assumptions used in the Company's valuations were consistent with its internal projections and operating plans. Lifeway's discounted cash flows forecast could be negatively impacted by a change in the competitive landscape, any internal decisions to pursue new or different strategies, a loss of a significant customer, or a significant change in the market place including changes in the prices paid for its products or changes in the size of the market for its products. Additionally, under the market approach analysis, the Company used significant other observable inputs including various guideline company comparisons. Lifeway bases its fair value estimates on assumptions it believes to be reasonable, but which are unpredictable and inherently uncertain. Changes in these estimates or assumptions could materially affect the determination of fair value and the conclusions of the quantitative goodwill test for the Company's one reporting unit.

Approximately \$1,664 of goodwill is deductible for income tax purposes.

Intangible Assets

The gross carrying amounts and accumulated amortization of intangible assets consisted of the following:

	December 31, 2022			December 31, 2021		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Recipes	\$ 44	\$ (44)	\$ –	\$ 44	\$ (44)	\$ –
Customer lists and other customer related intangibles	4,529	(4,529)	–	4,529	(4,529)	–
Customer relationship	3,385	(1,212)	2,173	3,385	(1,052)	2,333
Brand names	7,948	(2,683)	5,265	7,948	(2,303)	5,645
Formula	438	(438)	–	438	(438)	–
Total intangible assets, net	<u>\$ 16,344</u>	<u>\$ (8,906)</u>	<u>\$ 7,438</u>	<u>\$ 16,344</u>	<u>\$ (8,366)</u>	<u>\$ 7,978</u>

Estimated amortization expense on intangible assets for the next five years is as follows:

Year	Amortization
2023	\$ 540
2024	\$ 540
2025	\$ 540
2026	\$ 540
2027	\$ 540

Note 6 – Accrued Expenses

Accrued expenses consisted of the following:

	December 31,	
	2022	2021
Payroll and incentive compensation	\$ 2,925	\$ 2,951
Real estate taxes	394	359
Current portion of operating lease liabilities	70	131
Other	424	283
Total accrued expenses	\$ 3,813	\$ 3,724

Note 7 – Debt

Note payable consisted of the following:

	December 31,	
	2022	2021
Term loan due August 18, 2026. Interest (6.29% at December 31, 2022) payable monthly.	\$ 3,750	\$ 4,500
Unamortized deferred financing costs	(23)	(30)
Total note payable	3,727	4,470
Less current portion	(1,250)	(1,000)
Total long-term portion	\$ 2,477	\$ 3,470

The scheduled maturities of the term loan, excluding deferred financing costs, at December 31, 2022 are as follows:

2023	\$ 1,250
2024	1,000
2025	1,000
2026	500
Total term loan	\$ 3,750

Credit Agreement

On August 18, 2021, Lifeway entered into the Fourth Modification (the “Fourth Modification”) to the Amended and Restated Loan and Security Agreement (as amended and modified from time to time, the “Credit Agreement” and, as amended and modified by the Fourth Modification, the “Modified Credit Agreement”) with its existing lender and certain of its subsidiaries. The Fourth Modification amends the Credit Agreement to provide for, among other things, a \$5 million term loan by the existing lender to the borrowers to be repaid in quarterly installments of principal and interest over a term of five years (the “Term Loan”). The termination date of the Term Loan is August 18, 2026, unless earlier terminated. The Amended and Restated Loan and Security Agreement continues to provide Lifeway with a revolving line of credit up to a maximum of \$5 million (the “Revolving Loan”) and provides the Borrowers with an incremental facility not to exceed \$5 million (the “Incremental Facility” and together with the Revolving Loan, the “Loans”). The Termination Date of the Revolving Loan was extended to June 30, 2025, unless earlier terminated.

As amended, all outstanding amounts under the revolving line of credit and term loan bear interest, at Lifeway's election, at either the lender Base Rate (the Prime Rate minus 1.00%) or the LIBOR plus 1.95%, payable monthly in arrears. Lifeway is also required to pay a quarterly unused revolving line of credit fee of 0.20% and, in conjunction with the issuance of any letters of credit, a letter of credit fee of 0.20%.

The Modified Credit Agreement includes customary representations, warranties, and covenants, including financial covenants requiring the Company to maintain a fixed charge coverage ratio of no less than 1.25 to 1.00, and a minimum working capital financial covenant, as defined, of no less than \$11.25 million, in each of the fiscal quarters ending through the expiration date. The Modified Credit Agreement continues to provide for events of default, including failure to repay principal and interest when due and failure to perform or violation of the provisions or covenants of the agreement, as a result of which amounts due under the Modified Credit Agreement may be accelerated. The loans and all other amounts due and owed under the Credit Agreement and related documents are secured by substantially all of the Company's assets.

Lifeway was in compliance with the fixed charge coverage ratio and minimum working capital covenants at December 31, 2022.

Revolving Credit Facility

As of December 31, 2022, the Company had \$2,777 outstanding under the Revolving Credit Facility. Lifeway had \$2,223 available for future borrowings under the Revolving Credit Facility as of December 31, 2022. Lifeway's interest rate on debt outstanding under the Revolving Credit Facility as of December 31, 2022 was 6.17%.

Deferred Financing Costs

As of December 31, 2022, net unamortized deferred financing costs of \$23 related to the term loan were included as a direct deduction from outstanding long-term debt.

Note 8 – Leases

The Company leases certain machinery and equipment with fixed base rent payments and variable costs based on usage. Remaining lease terms for these leases range from less than one year to five years. The Company includes lease extension options, if applicable and reasonably certain to be exercised, in the calculation of the right-of-use asset and lease liabilities. Lifeway includes only fixed payments for lease components in the measurement of the right-of-use asset and lease liability. Variable lease payments are those that vary because of changes in facts or circumstances occurring after the commencement date, other than the passage of time. There are no residual value guarantees. Lifeway does not currently have leases which meet the finance lease classification as defined under ASC 842.

Lifeway treats contracts as a lease when the contract conveys the right to use a physically distinct asset for a period of time in exchange for consideration, it directs the use of the asset and obtain substantially all the economic benefits of the asset.

The Company does not record leases with an initial term of 12 months or less on the balance sheet. Expense for these short-term leases is recorded on a straight-line basis over the lease term. Total lease expense was \$229 and \$304 (including short term leases) for the years ended December 31, 2022 and 2021, respectively.

Right-of-use assets and lease liabilities are measured and recognized based on the present value of the future minimum lease payments over the lease term at the commencement date. Lifeway has elected the practical expedient to combine lease and non-lease components into a single component for all of its leases. When the Company is unable to determine an implicit interest rate, it uses its incremental borrowing rate based on the information available at the commencement date in determining the present value of future payments for those leases. Lifeway includes options to extend or terminate the lease in the measurement of the right-of-use asset and lease liability when it is reasonably certain that it will exercise such options. Lease expense for minimum lease payments is recognized on a straight-line basis over the lease term.

Future maturities of lease liabilities were as follows:

Year	Operating Leases
2023	\$ 86
2024	67
2025	33
2026	10
2027	3
Total lease payments	199
Less: Interest	(25)
Present value of lease liabilities	\$ 174

The weighted-average remaining lease term for its operating leases was 2.7 years as of December 31, 2022. The weighted average discount rate of its operating leases was 11.70% as of December 31, 2022. Cash paid for amounts included in the measurement of lease liabilities was \$151 and \$198 for the year ended December 31, 2022 and 2021, respectively.

Note 9 – Commitments and Contingencies

Litigation

Lifeway is involved in various legal proceedings, claims, disputes, regulatory matters, audits, and proceedings arising in the ordinary course of, or incidental to the Company's business, including commercial disputes, product liabilities, intellectual property matters and employment-related matters.

Lifeway records provisions in the consolidated financial statements for pending legal matters when it believes it is probable that a loss will be incurred and the amount of such loss can be reasonably estimated. The Company evaluates, on a periodic basis, developments in legal matters that could affect the amount of any accrual and developments that would make a loss contingency both probable and reasonably estimable. If a loss contingency is not both probable and estimable, it does not establish an accrued liability. Currently, none of its accruals for outstanding legal matters are material individually or in the aggregate to its financial position and it is management's opinion that the ultimate resolution of these outstanding legal matters will not have a material adverse effect on its business, financial condition, results of operations, or cash flows. However, if the Company is ultimately required to make payments in connection with an adverse outcome, it is possible that such contingency could have a material adverse effect on the Company's business, financial condition, results of operations or cash flows.

Note 10 – Income taxes

The provision for income taxes consists of the following:

	For the Years Ended December 31,	
	2022	2021
Current:		
Federal	\$ 645	\$ 1,097
State and local	444	951
Total current	1,089	2,048
Deferred	(172)	257
Provision for income taxes	<u>\$ 917</u>	<u>\$ 2,305</u>

The following is a reconciliation of income tax expense computed at the U.S. federal statutory tax rate to income tax expense reported in the consolidated statement of operations:

	2022		2021	
	Amount	Percentage	Amount	Percentage
Federal income tax at statutory rate	\$ 392	21.0%	\$ 1,179	21.0%
State and local tax, net	287	15.4%	440	7.8%
Other permanent differences	8	0.4%	6	0.1%
Section 162m	229	12.2%	206	3.7%
Stock based compensation	127	6.8%	100	1.8%
Uncertain tax positions	–	–%	218	3.9%
Change in tax rates	(83)	(4.4%)	198	3.4%
Other	(43)	(2.3%)	(42)	(0.7%)
Provision for income taxes	<u>\$ 917</u>	<u>49.1%</u>	<u>\$ 2,305</u>	<u>41.0%</u>

The tax effects of temporary differences giving rise to deferred income tax assets and liabilities were:

	December 31,	
	2022	2021
Deferred tax liabilities attributable to:		
Accumulated depreciation and amortization	\$ (3,394)	\$ (3,401)
Unrealized gains	(472)	(473)
Total deferred tax liabilities	<u>(3,866)</u>	<u>(3,874)</u>
Deferred tax assets attributable to:		
Net operating losses	6	6
Accrued compensation	287	170
Incentive compensation	194	164
Inventory	328	324
Allowances for doubtful accounts and discounts	5	5
Deferred revenue	–	10
Other	17	(6)
Total net deferred tax assets	<u>837</u>	<u>673</u>
Net deferred tax liabilities	<u>\$ (3,029)</u>	<u>\$ (3,201)</u>

The following table details the Company's tax attributes related to net operating losses for which it has recorded deferred tax assets.

Tax Attributes	Gross Amount	Net Amount	Expiration Years
State net operating losses	\$ 116	\$ 6	2035
		<u>\$ 6</u>	

During the year, the Company recorded adjustments to its unrecognized tax benefits. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

	2022	2021
Balance at January 1	\$ 396	\$ 95
Additions based on tax positions of prior years	–	301
Settlement for tax positions of prior years	(396)	–
Balance at December 31	<u>\$ –</u>	<u>\$ 396</u>

Lifeway is subject to U.S. federal income tax as well as income tax in multiple state and city jurisdictions. With limited exceptions, Lifeway's calendar year 2019 and subsequent federal and state tax years remain open by statute. As of December 31, 2022, the unrecognized tax benefit is \$0.

The amount of interest and penalties recognized in the consolidated statements of operations was \$0 during 2022 and 2021, respectively. The amount of accrued interest and penalties recognized in the consolidated balance sheets was \$0 at December 31, 2022 and 2021, respectively.

Note 11 – Stock-based and Other Compensation

Omnibus Incentive Plan

In December 2015, Lifeway stockholders approved the 2015 Omnibus Incentive Plan, which authorized the issuance of an aggregate of 3.5 million shares to satisfy awards of stock options, stock appreciation rights, unrestricted stock, restricted stock, restricted stock units, performance shares and performance units to qualifying employees. Under the Plan, the Board or its Audit and Corporate Governance Committee approves stock awards to executive officers and certain senior executives, generally in the form of restricted stock or performance shares. The number of performance shares that participants may earn depends on the extent to which the corresponding performance goals have been achieved. Stock awards generally vest over a three-year performance or service period. At December 31, 2022, no shares remain available for award under the 2015 Omnibus Incentive Plan as it was terminated on August 31, 2022. However, any outstanding awards under the 2015 Omnibus Incentive Plan are unaffected by the termination of the 2015 Omnibus Incentive Plan or by the approval of the 2022 Omnibus Incentive Plan (the "2022 Plan") as described below.

On August 31, 2022, Lifeway stockholders approved the 2022 Plan. Under the 2022 Plan, the Compensation Committee of the Board of Directors may grant awards of various types of compensation, including, nonqualified stock options, incentive stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units, cash-based awards and other stock-based awards. The maximum number of shares authorized to be awarded under the 2022 Plan is 3.25 million shares of common stock, which includes shares that remained available under the now terminated 2015 Omnibus Incentive Plan.

Awards granted under the 2022 Plan are generally subject to a minimum vesting period of at least one year. Awards may be subject to cliff-vesting or graded-vesting conditions, with graded vesting starting no earlier than one year after the grant date. The Plan Administrator may provide for shorter vesting periods in an award agreement for no more than five percent of the maximum number of shares authorized for issuance under the 2022 Plan. As of December 31, 2022, 3.00 million shares remain available to award under the 2022 Plan.

Stock Options

The following table summarizes stock option activity during the year ended December 31, 2022:

	Options	Weighted average exercise price	Weighted average remaining contractual life	Aggregate intrinsic value
Outstanding at December 31, 2021	41	\$ 10.42	4.22	\$ —
Granted	—	—	—	—
Exercised	—	—	—	—
Forfeited	—	—	—	—
Outstanding at December 31, 2022	<u>41</u>	<u>\$ 10.42</u>	<u>3.22</u>	<u>\$ —</u>
Exercisable at December 31, 2022	41	\$ 10.42	3.22	\$ —

Lifeway measures the fair value of stock options using the Black-Scholes option pricing model. The expected term of options granted was based on the weighted average time of vesting and the end of the contractual term. The Company utilized this simplified method as it did not have sufficient historical exercise data to provide a reasonable basis upon which to estimate the expected term.

Restricted Stock Awards

A Restricted Stock Award (“RSA”) represents the right to receive one share of common stock in the future. RSAs have no exercise price. The grant date fair value of the awards is equal to the Company’s closing stock price on the grant date. The following table summarizes RSA activity during the year ended December 31, 2022.

	Restricted Stock Awards	Weighted Average Grant Date Fair Value
Outstanding at December 31, 2021	94	\$ 4.50
Granted	97	6.25
Shares issued upon vesting	(27)	3.43
Forfeited	—	—
Outstanding at December 31, 2022	<u>164</u>	<u>\$ 5.69</u>
Vested and deferred at December 31, 2022	<u>37</u>	<u>\$ 5.60</u>

Lifeway expenses RSAs over the service period. For the years ended December 31, 2022 and 2021 total stock-based compensation expense recognized in the consolidated statements of operations was \$279 and \$264, respectively. For the years ended December 31, 2022 and 2021 tax-related benefits of \$78 and \$76, respectively, were also recognized. As of December 31, 2022, the total remaining unearned compensation related to non-vested RSAs was \$520, which is expected to be amortized over the weighted-average remaining service period of 1.55 years.

Long-Term Incentive Plan Compensation

Lifeway has established long-term incentive-based compensation programs for certain senior executives and key employees pursuant to the terms of its incentive plans.

2020 CEO Incentive Award

During the fourth quarter 2020, Lifeway awarded a long-term equity-based incentive of \$750 to its Chief Executive Officer (the “2020 CEO Award”) depending on Lifeway’s 2020 performance levels compared to the respective targets. The equity-based incentive compensation is payable in restricted stock that vests one-third in April 2022, one-third in April 2023, and one-third in April 2024. The issuance of vested equity awards is subject to approval under the Stock Purchase Agreement dated October 1, 1999. For the years ended December 31, 2022 and 2021, \$229 and \$342 was expensed as stock-based compensation expense in the consolidated statements of operations. As of December 31, 2022, the total remaining unearned compensation was \$129, of which \$105 will be recognized in 2023, and \$24 in 2024, respectively, subject to vesting. During Q2 2021, the number of shares became fixed and determinable. Therefore, the award liability was reclassified from long-term liabilities to paid in capital.

2021 Equity Award

The 2021 long-term equity incentive plan compensation is based on Lifeway’s achievement of adjusted EBITDA performance versus the respective target established by the Board for 2021. Under the 2021 plan, collectively the participants earned equity-based incentive compensation of \$1,069 based on Lifeway’s achievement of the respective financial target. The equity-based incentive compensation is payable in restricted stock that vests one-third in April 2022, one-third in April 2023, and one-third in April 2024. For the years ended December 31, 2022 and 2021, \$449 and \$386 was expensed as stock-based compensation expense in the consolidated statements of operations, respectively. As of December 31, 2022, the total remaining unearned compensation was \$234, of which \$194 will be recognized in 2023, and \$40 in 2024, respectively, subject to vesting. During Q2 2022, the number of shares awarded became fixed and determinable. Therefore, the award liability was reclassified from long-term liabilities to paid in capital.

2022 Equity Award

Under the 2022 long-term incentive plan, participants can earn a specified number of target level Performance Share Units (“PSUs”) contingent upon the achievement of strategic milestones during the three-year measurement period, which is fiscal year 2022 to 2024. The strategic milestones are 1) 3-year cumulative net revenue, and 2) 3-year cumulative adjusted EBITDA. The target number of PSU awards are weighted 50% on net revenue and 50% on adjusted EBITDA. Collectively, the participants can earn 125,066 PSUs at the target level. Participants may earn more or less than the target number of shares based on actual results, however the minimum and maximum number of shares that can be earned are bound by minimum and maximum thresholds of net revenue and adjusted EBITDA. The PSU awards will be earned and will vest, if at all, after the end of the three-year measurement period based on achievement of the milestones. The PSU awards do not vest during the three-year measurement period. The PSUs have a grant date fair value of \$6.25 dollars per share. For the twelve months ended December 31, 2022, \$151 was expensed as stock-based compensation expense in the consolidated statements of operations, respectively.

The 2022 long-term incentive plan also granted restricted stock unit awards that contain only a service condition and vest on the passage of time in three equal installments on each of the first three anniversaries of the August 31, 2022 grant date. The stock-based compensation expense for these awards is included in the Restricted Stock Award section above.

Non-Employee Director Plan

On August 31, 2022, Lifeway stockholders approved the 2022 Non-Employee Director Equity and Deferred Compensation Plan (the “2022 Director Plan”), which authorizes the grant of restricted stock units (“RSUs”), which will vest on such schedule as the Company, in its sole discretion, shall determine. Each non-employee director of the Company is eligible to be a participant in the 2022 Director Plan until they no longer serve as a non-employee director. As of the date of each annual shareholder meeting, the Company may grant each director a number of RSUs for such year and set the vesting schedule for the RSUs granted. Whether and how many RSUs the Company will grant to directors in any year is subject to the sole discretion of the Company and shall in any event be subject to the 2022 Director Plan’s overall share limits. The maximum aggregate number of shares of common stock that may be issued under the 2022 Directors Plan is 500 thousand shares. As of December 31, 2022, 466 thousand shares remain available to award under the 2022 Director Plan. The aggregate fair market value of shares underlying RSU compensation that may be issued as RSU compensation to a director in any year shall not exceed \$170. In addition to the grant of RSUs, the 2022 Director Plan also provides for the deferral by electing participants of all or part of their cash compensation (in 10% increments) into a deferred cash account, and they may defer all or part of their cash and/or RSU compensation (in 10% increments) into a deferred RSU account. Deferred benefits are paid in a lump sum upon the applicable director’s departure from the Board of Directors.

Retirement Benefits

Lifeway has a defined contribution plan which is available to substantially all full-time employees. Under the terms of the plan we match employee contributions under a prescribed formula. For the years ended December 31, 2022 and 2021 total contribution expense recognized in the consolidated statements of operations was \$446 and \$432, respectively.

Note 12 – Segments, Products and Customers

Lifeway’s primary product is drinkable kefir. The Company manufactures (directly or through a co-manufacturer) and markets products under the Lifeway, Fresh Made, and GlenOaks Farms brand names, as well as under private labels on behalf of certain customers.

The Company’s product categories are:

- Drinkable Kefir, a cultured dairy product sold in a variety of organic and non-organic sizes, flavors, and types.
- European-style soft cheeses, including farmer cheese, white cheese, and Sweet Kiss.
- Cream and other, which primarily consists of cream, a byproduct of raw milk processing.
- Drinkable Yogurt, sold in a variety of sizes and flavors.
- ProBugs, a line of kefir products designed for children.
- Other Dairy, which primarily consists of Fresh Made butter and sour cream.

Lifeway has determined that it has one reportable segment based on how its chief operating decision maker manages the business and, in a manner, consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing the Company’s performance, has been identified as the Chief Executive Officer. Substantially all of Lifeway’s consolidated revenues relate to the sale of cultured dairy products that it produces using the same processes and materials and are sold to consumers through a common network of distributors and retailers in the United States.

Net sales of products by category were as follows for the years ended December 31:

In thousands	2022		2021	
	\$	%	\$	%
Drinkable Kefir other than ProBugs	110,247	78%	95,850	80%
Cheese	12,651	9%	12,612	11%
Cream and other	7,465	5%	3,582	3%
Drinkable Yogurt	6,105	4%	2,223	2%
ProBugs Kefir	3,403	3%	3,178	3%
Other dairy	1,697	1%	1,620	1%
Net Sales	141,568	100%	119,065	100%

Significant Customers – Sales are predominately to companies in the retail food industry located within the United States. Two major customers accounted for approximately 22% and 23% of net sales for the years ended December 31, 2022 and 2021, respectively. Two major customers accounted for 28% and 32% of accounts receivable as of December 31, 2022 and 2021, respectively.

Note 13 – Share repurchase program

Pursuant to the share repurchase program, during the year ended December 31, 2020, the Company repurchased 179 shares at a cost of \$405 or approximately \$2.27 per share. During 2020, the Company reached the amended threshold of 625 shares and therefore no shares of common stock remain available to be purchased under the 2017 Repurchase Plan Amendment as of December 31, 2020.

On June 24, 2021, the Lifeway’s Board authorized a plan to repurchase up to 250 shares of Common Stock in the open market within 24 months at no more than \$10 per share (the “2021 Repurchase Plan”). The Company repurchased all 250 shares of common stock at a cost of \$1,583 during the three-month period ended September 30, 2021. Lifeway intends to hold repurchased shares in treasury for general corporate purposes, including issuances under its 2015 Omnibus Incentive Plan. Treasury shares are accounted for using the cost method.

Stock Purchase Agreement

On November 7, 2022, the Company entered into a Stock Purchase Agreement with Ludmila Smolyansky (“Ms. Smolyansky”), to purchase 850,340 shares of Lifeway common stock from Ms. Smolyansky. The shares were repurchased during the fourth quarter of 2022.

Pursuant to the Stock Purchase Agreement, the Company and Ms. Smolyansky have agreed, among other things, that (i) Ms. Smolyansky will sell the shares at a purchase price of \$4.70 per share, which represents a twenty percent (20.0%) discount to the average closing price of the common stock on Nasdaq over the five (5) trading day period ended on the trading day immediately preceding the date of the Stock Purchase Agreement and (ii) Ms. Smolyansky will use a portion of the proceeds to satisfy in full certain obligations of Ms. Smolyansky, which are secured by previously disclosed pledges of common stock, causing all such pledges to be released. The purchased shares will be held in treasury by the Company.

As a closing condition to the Stock Purchase Agreement, Ms. Smolyansky and Mr. Smolyansky delivered an executed amendment (the “Amendment”) to that certain Settlement Agreement dated as of July 27, 2022 (the “Settlement Agreement”), between the Company and Ms. Smolyansky and Mr. Smolyansky. Pursuant to the Amendment, Ms. Smolyansky and Mr. Smolyansky each agree, among other things, to (i) grant the Company a right of first refusal, subject to Danone North America Public Benefit Corporation’s (“Danone”) right of first refusal, on substantially similar terms as Danone (ii) extend the standstill and all related terms under the Proxy Settlement Agreement through the date of the 2024 annual meeting of the Company’s shareholders (the “Standstill”); and (iii) to appear in person or by proxy and vote their respective remaining shares of common stock beneficially owned, individually or otherwise, and controlled by either of them and over which they have power and authority to vote during the Standstill (a) in accordance with the recommendations of the Board at any special meeting or annual meeting of the shareholders with respect to any proposal(s) not related to the sale of the Company or all or substantially all of the assets of the Company; and (b) in proportion to the vote of the other shareholders with respect to any proposal relating to any vote on the sale of the Company or all or substantially all of the assets of the Company.

Note 14 – Related party transactions

Consulting Services

Lifeway obtains consulting services from Ludmila Smolyansky, a member of the Company's Board of Directors and former Chairperson of its Board of Directors. On December 28, 2020, Lifeway entered into an amended and restated consulting agreement (the "Agreement"), effective as of December 31, 2020, with Ms. Smolyansky. Under the terms and conditions of the Agreement, Ms. Smolyansky will continue to provide consulting services with respect to, among other things, the Company's business strategy, international expansion and product management and expansion. For the services, the Company will pay an annual service fee of \$500, and Ms. Smolyansky will also be eligible for an annual performance fee target of \$500 based on the achievement of specified performance criteria. The annual service fee and target bonus amounts are subject to periodic change by the Compensation Committee of the Company's Board of Directors on 30 days' prior written notice to the Chairperson. The Agreement shall continue until either party provides at least a 10-day written notice of termination.

On January 4, 2022, the Company notified Ms. Smolyansky that it was terminating the Agreement effective January 17, 2022. Service fees earned are included in general and administrative expenses in the accompanying consolidated statements of operations and were \$22 and \$500 during the years ended December 31, 2022 and 2021, respectively.

Endorsement Agreement

Lifeway is also a party to an endorsement agreement, dated as March 14, 2016, by and between the Company and Ludmila Smolyansky, a member of the Company's Board of Directors and former Chairperson of its Board of Directors (the "Endorsement Agreement") under which it pays the Chairperson a royalty based on the sale of certain Lifeway products, not to exceed \$50 in any fiscal month.

On September 6, 2022, the Company entered into an agreement (the "Termination Agreement") with Ms. Smolyansky that terminated the Endorsement Agreement as of September 6, 2022.

Pursuant to the Termination Agreement, the Company and Ms. Smolyansky have agreed, among other things, that (i) the Company will pay Ms. Smolyansky a lump sum payment of \$400,000, (ii) Ms. Smolyansky will no longer have any further claims against the Company under the Endorsement Agreement, and (iii) the Endorsement Agreement was terminated and of no further force or effect except for the provisions thereof that expressly survive termination.

Royalties earned are included in selling expenses in the accompanying consolidated statements of operations and were \$400 and \$600 during the years ended December 31, 2022 and 2021, respectively.

Stock Purchase Agreement

See the November 2022 stock purchase agreement between Ms. Smolyansky and the Company in Note 13.

Note 15 – Business Acquisition

On August 18, 2021, the Company completed the acquisition of certain assets of Glen Oaks Farms Inc. for a purchase price of \$5,800 in cash. Glen Oaks is engaged in the manufacture, development, and sale of probiotic drinkable yogurt. The acquisition of Glen Oaks Farms initiates Lifeway's expansion outside of kefir and into drinkable yogurt. The current distribution of Glen Oaks Farms in western U.S. retailers is strategically significant for Lifeway as the Company seeks to further grow its presence in this region. From a portfolio perspective, it complements the Company's eastern U.S. presence with the Fresh Made brand and national strength with Lifeway. The acquisition was funded through the proceeds of a \$5,000 note payable (see Note 7) and the Company's existing cash resources.

Management considers the purchase of Glen Oaks Farms Inc. to consist of inputs, processes and outputs and has accounted for the purchase as a business combination. The acquisition was accounted for under the acquisition method of accounting and the results of operations were included in the Company's consolidated statement of operations from the date of acquisition. Included in the Company's consolidated statements of operations are the acquisition's net sales of \$2,223 and income before income taxes of approximately \$384 from the date of acquisition through December 31, 2021. The Company incurred approximately \$83 in acquisition-related costs which are expensed as incurred and included in general and administrative expense on the consolidated statement of operations. Pro-forma results of operation have not been presented as the effect would not be material to the Company's results of operations for any periods presented.

The following table summarizes the preliminary purchase price allocation of the fair value of intangible assets acquired and liabilities assumed:

	<u>\$</u>
Customer relationships	2,400
Brand name	2,000
Goodwill	1,400
Assets acquired	<u>5,800</u>
Liabilities assumed	<u>—</u>
Total purchase price	<u><u>5,800</u></u>

The fair value for the customer relationships at the acquisition date were determined using the excess earnings method under the income approach. The brand name fair value was determined using the relief from royalty method. The customer relationship and brand name intangible assets have an estimated life of 15 years and will be amortized over that period. The fair value measurements of intangible assets are based on significant unobservable inputs, and thus represent Level 3 inputs. Significant assumptions used in assessing the fair values of intangible assets include discounted future cash flows, customer attrition rates, and royalty rates. Goodwill arises principally from category expansion opportunities to better serve its regional and national customers. The goodwill resulting from the acquisition is tax deductible.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure material information required to be disclosed in our reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer, principal financial officer and principal accounting officer, as appropriate, to allow timely decisions regarding required financial disclosure. In designing and evaluating the disclosure controls and procedures, we recognize that a control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

As of December 31, 2022 (the "Evaluation Date"), we conducted an evaluation, under the supervision and with the participation of our principal executive officer and principal financial officer, of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15 and 15d-15 of the Securities Exchange Act of 1934 (the "Exchange Act")). Based on this evaluation, our principal executive officer and principal financial officer have concluded that, as of the Evaluation Date, our disclosure controls and procedures were effective at the reasonable assurance level as of December 31, 2022 in ensuring that information required to be disclosed by us under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified under the Exchange Act rules.

Management's Annual Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting as such term is identified in Exchange Act Rules 13a-15(f). Internal control over financial reporting is a process designed by, or under the supervision of, our principal executive officer, principal financial officer and principal accounting officer, and effected by the Board of Directors, management, and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Our internal control over financial reporting includes those policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect our transactions and dispositions of our assets;
- provide reasonable assurance that our transactions are recorded as necessary to permit preparation of our consolidated financial statements in accordance with accounting principles generally accepted in the United States of America, and that our receipts and expenditures of the Company are being made only in accordance with authorizations of our management and our directors; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on our consolidated financial statements.

Internal control over financial reporting has inherent limitations which may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or because the level of compliance with related policies or procedures may deteriorate.

Management, including our Chief Executive Officer and our Chief Financial Officer, assessed the effectiveness of our internal control over financial reporting as of December 31, 2022. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) in Internal Control - Integrated Framework (2013). Based on this assessment, management has concluded that our internal control over financial reporting was effective as of December 31, 2022.

Remediation of the Material Weakness

During 2022, management evaluated our policies and procedures related to accounting for deferred income taxes and goodwill of acquired intangible assets. We have implemented controls to ensure that (i) the goodwill allocation associated with any acquired intangible assets are properly accounted for and disclosed in the period of acquisition, and (ii) the deferred income tax effects of acquired intangible assets are properly accounted for and disclosed in the period of acquisition.

Changes in Internal Control over Financial Reporting

Except as discussed above, there were no changes in our internal control over financial reporting that occurred during 2022 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

ITEM 9C. DISCLOSURE REGARDING FOREIGN JURISDICTIONS THAT PREVENT INSPECTIONS

Not applicable.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Corporate Governance Guidelines and Code of Ethics

Information required by this Item 10 will be included in our definitive Proxy Statement to be filed no later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K and is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

Information required by this Item 11 will be included in our definitive Proxy Statement to be filed no later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.

Information required by this Item 12 will be included in our definitive Proxy Statement to be filed no later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE.

Information required by this Item 13 will be included in our definitive Proxy Statement to be filed no later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.

Information required by this Item 14 will be included in our definitive Proxy Statement to be filed no later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

1. A list of the Financial Statements and Financial Statement Schedules filed as part of this Report is set forth in Part II, Item 8, which list is incorporated herein by reference.
2. Financial Statement Schedules – Separate financial statement schedules have been omitted either because they are not applicable or because the required information is included in the consolidated financial statements
3. Exhibits.

No.	Description	Form	Period Ending	Exhibit	Filing Date
3.1	Amended and Restated Bylaws	Filed Herewith			
3.2	Articles of Incorporation, as amended and currently in effect	10-K	12/31/2013	3.2	4/2/2014
10.1	Stockholders' Agreement dated October 1, 1999 by and among Danone Foods, Inc., Lifeway Foods, Inc., Michael Smolyansky and certain other parties	8-K	10/1/1999	10.11	10/12/1999
10.2	Letter Agreement dated December 24, 1999	8-K	12/24/1999	10.12	1/12/2000
10.3+	Employment Agreement, dated September 12, 2002, between Lifeway Foods, Inc. and Julie Smolyansky	10-QSB/A No. 2	9/30/2002	10.14	4/30/2003
10.4	Endorsement Agreement by and between the Company and Ludmila Smolyansky, dated as of March 14, 2016	10-K	12/31/2015	10.24	3/16/2016
10.5	Termination Agreement dated as of August 30, 2022, between the Company and Ludmila Smolyansky	8-K	9/6/2022	10.2	9/13/2022
10.6	Amended and Restated Loan and Security Agreement dated as of May 7, 2018 among Lifeway Foods, Inc., Fresh Made, Inc., The Lifeway Kefir Shop, LLC, Lifeway Wisconsin, Inc., and CIBC Bank USA, as Lender.	8-K	5/7/2018	10.1	5/11/2018
10.7+	Employment Agreement by and between the Company and Amy Feldman, dated as of October 29, 2018	8-K	10/26/2018	10.1	11/1/2018
10.8+	Employment Agreement by and between the Company and Eric Hanson, dated as of January 18, 2019	8-K	1/1/2019	10.1	1/23/2019
10.9	First Modification to Amended and Restated Loan and Security Agreement dated as of April 10, 2019 among Lifeway Foods, Inc., Fresh Made, Inc., The Lifeway Kefir Shop, LLC, Lifeway Wisconsin, Inc., and CIBC Bank USA, as Lender.	10-K	12/31/2018	10.10	4/15/2019

10.10	Second Modification to Amended and Restated Loan and Security Agreement, effective as of December 10, 2019 by and among Lifeway Foods, Inc., Fresh Made, Inc., The Lifeway Kefir Shop, LLC, Lifeway Wisconsin, Inc., and CIBC Bank USA, as Lender.	8-K	12/10/2019	10.1	12/10/2019
10.11	Third Modification to Amended and Restated Loan and Security Agreement dated as of September 30, 2020 among Lifeway Foods, Inc., Fresh Made, Inc., The Lifeway Kefir Shop, LLC, Lifeway Wisconsin, Inc., and CIBC Bank USA, as Lender.	10-Q	9/30/2020	10.1	10/6/2020
10.12	Fourth Modification to Amended and Restated Loan and Security Agreement, dated as of August 18, 2021, by and among Lifeway Foods, Inc., Fresh Made, Inc., The Lifeway Kefir Shop, LLC, Lifeway Wisconsin, Inc., and CIBC Bank USA, as Lender	8-K	8/18/2021	10.1	8/20/2021
10.13+	Amended and Restated Consulting Agreement dated December 28, 2020 by and between the Company and Ludmila Smolyansky	8-K	12/28/2020	10.1	12/28/2020
10.14+	Lifeway Foods, Inc. Omnibus Incentive Plan	8-K	12/14/2015	10.2	12/18/2015
10.15+	Notice of Restricted Stock Unit Award	8-K	12/14/2015	10.3	12/18/2015
10.16+	Notice of Performance Unit Award	8-K	12/14/2015	10.4	12/18/2015
10.17+	Notice of Restricted Stock Award	8-K	12/14/2015	10.5	12/18/2015
10.18+	Notice of Non-Qualified Stock Option Award	8-K	12/14/2015	10.6	12/18/2015
10.19	Settlement Agreement dated as of July 27, 2022, between the Company and Edward Smolyansky and Ludmila Smolyansky	8-K	7/27/2022	10.1	7/29/2022
10.20	Amendment to Settlement Agreement dated as of July 27, 2022, between the Company and Edward Smolyansky and Ludmila Smolyansky	Filed Herewith			
10.21+	Lifeway Foods, Inc. 2022 Omnibus Incentive Plan	8-K	8/31/2022	10.1	9/2/2022
10.22+	Form of Notice of Restricted Stock Award under the Lifeway Foods, Inc. 2022 Non-Employee Director Equity and Deferred Compensation Plan	10-Q	9/30/2022	10.6	11/14/2022
10.23+	Form of Notice of Restricted Stock Unit Award under the Lifeway Foods, Inc. 2022 Omnibus Incentive Plan	10-Q	9/30/2022	10.7	11/14/2022
10.24+	Form of Notice of Performance-Based Restricted Stock Unit Award under the 2022 Omnibus Incentive Plan	10-Q	9/30/2022	10.8	11/14/2022

10.25+	Lifeway Foods, Inc. 2022 2022 Non-Employee Director Equity and Deferred Compensation Plan	8-K	8/31/2022	10.2	9/2/2022
10.26+	Form of Notice of Restricted Stock Unit Award under the Lifeway Foods, Inc. 2022 Non-Employee Director Equity and Deferred Compensation Plan	10-Q	9/30/2022	10.6	11/14/2022
10.27	Settlement Agreement dated as of September 1, 2022, between the Company and Edward Smolyansky	8-K	9/6/2022	10.1	9/13/2022
10.28	Stock Purchase Agreement dated as of November 7, 2022, between the Company and Ludmila Smolyansky	8-K	11/7/2022	10.1	11/9/2022
10.29	Restricted Stock Unit Award Agreement, dated as of April 27, 2022, by and between the Company and Jason Scher	Filed Herewith			
21	List of Subsidiaries of the Registrant				
23.1	Consent of Grant Thornton LLP				
23.2	Consent of Mayer Hoffman McCann P.C.				
31.1	Rule 13a-14(a)/15d-14(a) Certification of Julie Smolyansky				
31.2	Rule 13a-14(a)/15d-14(a) Certification of Eric Hanson				
32.1*	Section 1350 Certification of Julie Smolyansky				
32.2*	Section 1350 Certification of Eric Hanson				
99.1*	Press release dated March 27, 2023 reporting the Company's financial results for year ended December 31, 2022.				
101*	The following financial statements from the Company's Annual Report on Form 10-K for the year ended December 31, 2022, formatted in inline XBRL, include: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations, (iii) Consolidated Statements of Stockholders' Equity, (iv) Consolidated Statements of Cash Flows and (v) the Notes to the Consolidated Financial Statements.				

+ Indicates a management contract or compensatory plan or arrangement.

* This exhibit is furnished and not deemed filed with the Securities and Exchange Commission, and is not incorporated by reference into any filing of Lifeway Foods, Inc. under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of filing this Form 10-K and irrespective of any general incorporation language contained in such filing.

ITEM 16. FORM 10-K SUMMARY

Not applicable.

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.

LIFEWAY FOODS, INC.

Date: March 27, 2023

By: /s/ Julie Smolyansky
Julie Smolyansky
Chief Executive Officer, President, and
Director

Date: March 27, 2023

By: /s/ Eric Hanson
Eric Hanson
Chief Financial & Accounting 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.

Date: March 27, 2023

/s/ Julie Smolyansky
Julie Smolyansky
Chief Executive Officer, President, and Director
(Principal Executive Officer)

Date: March 27, 2023

/s/ Eric Hanson
Eric Hanson
Chief Financial & Accounting Officer
(Principal Financial & Accounting Officer)

Date: March 27, 2023

Ludmila Smolyansky
Ludmila Smolyansky
Director

Date: March 27, 2023

/s/ Jason Scher
Jason Scher
Director

Date: March 27, 2023

/s/ Pol Sikar
Pol Sikar
Director

Date: March 27, 2023

/s/ Jody Levy
Jody Levy
Director

Date: March 27, 2023

/s/ Dorri McWhorter
Dorri McWhorter
Director

Date: March 27, 2023

/s/ Juan Carlos Dalto
Juan Carlos Dalto
Director

Date: March 27, 2023

/s/ Perfecto Sanchez
Perfecto Sanchez
Director

**SECOND AMENDED AND RESTATED BY-LAWS
OF
LIFEWAY FOODS, INC.**

These Amended and Restated Bylaws (the “Bylaws”) are hereby amended and restated as of this 24th day of March 2023, by the Board of Directors of Lifeway Foods, Inc. (the “Board”).

RECITALS

WHEREAS, Lifeway Foods, Inc. has heretofore been formed as a corporation under the Illinois Business Corporation Act of 1983 (805 ILCS § 5/1.01, et seq.), as amended, pursuant to the Articles of Incorporation filed in the office of the Illinois Secretary of State on May 19, 1986, and thereafter amended;

WHEREAS, the Board desires to amend and restate the by-laws of the corporation in their entirety; and

WHEREAS, the Board has the authority to amend the by-laws pursuant to Section 12.1 hereof.

NOW, THEREFORE, the Board, hereby amends and restates the by-laws in their entirety as follows:

ARTICLE I

OFFICES

1.1. The corporation shall continuously maintain in the State of Illinois a registered office and a registered agent whose business office is identical with such registered office, and may have other offices within or without the state.

1.2. Books and Records. Any records maintained by the corporation in the regular course of its business, including its stock ledger, books of account, and minute books, may be maintained on any information storage device or method; provided that the records so kept can be converted into clearly legible paper form within a reasonable time. The corporation shall so convert any records so kept on the reasonable request of any person entitled to inspect such records pursuant to applicable law.

ARTICLE II

SHAREHOLDERS

2.1. Annual Meeting. An annual meeting of the shareholders shall be held on the first Monday in June of each year or at such time as the Board may designate for the purpose of electing directors and for the transaction of such other business as may come before the meeting. If the day fixed for the annual meeting shall be a legal holiday, such meeting shall be held on the next succeeding business day.

2.1.1 Failure to hold the annual meeting at the designated time does not result in the winding up or dissolution of the corporation. If the Board fails to call the annual meeting, any shareholder may make demand in writing to any officer of the corporation that an annual meeting be held.

2.1.2 Nominations of persons for election to the Board and the proposal of business to be considered by the stockholders at an annual meeting of stockholders may be made (a) pursuant to the corporation's notice of meeting, (b) by or at the direction of the Board or (c) by any stockholder of the corporation who was a stockholder of record at the time of giving notice provided for in this Section 2.1, who is entitled to vote at the meeting and who complied with the notice procedures set forth in this Section 2.1.

2.1.3 For nominations or other business to be properly brought before an annual meeting by a stockholder pursuant to Section 2.1.2, such business, as determined by the Chairperson of the meeting, must be a proper subject for stockholder action under the Illinois Business Corporation Act of 1983, and the stockholder must have given timely notice thereof in writing to the Secretary of the corporation. To be timely, a stockholder's notice shall be delivered to the Secretary at the principal executive offices of the corporation not less than ninety (90) days nor more than one hundred and twenty (120) days prior to the first anniversary of the preceding year's annual meeting; provided, however, that in the event that the date of the annual meeting is advanced by more than thirty (30) days or delayed by more than sixty (60) days from such anniversary date, notice by the stockholder to be timely must be so delivered not earlier than the one hundred and twentieth (120th) day prior to such annual meeting and not later than the close of business on the later of the ninetieth (90th) day prior to such annual meeting or the tenth (10th) day following the date on which public announcement of the date of such meeting is first made. Such stockholder's notice shall set forth (a) as to each person whom the stockholder proposes to nominate for election or reelection as a director, all information relating to such person that is required to be disclosed in solicitations of proxies for election of directors, or is otherwise required, in each case pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended (the "Exchange Act") (including such person's written consent to being named as a nominee in any proxy statement and accompanying proxy card and to serving as a director if elected) and a representation as to whether such stockholder, any of their respective affiliates or associates, and any other person intends or is part of a group which intends to solicit proxies in support of any proposed nominee in accordance with Rule 14a-19 promulgated under the Exchange Act; (b) as to any other business that the stockholder proposes to bring before the meeting, a brief description of the business desired to be brought before the meeting, the reasons for conducting such business at the meeting, any material interest in such business of such stockholder and the beneficial owner, if any, on whose behalf the proposal is made, and a representation as to whether or not the stockholder intends to solicit proxies in support of such proposal; and (c) as to the stockholder giving the notice and the beneficial owner, if any, on whose behalf the nomination or proposal is made (i) the name and address of such stockholder, as they appear on the corporation's books, and of such beneficial owner and (ii) the class and number of shares of the corporation which are owned beneficially and of record by such stockholder and such beneficial owner.

2.1.4 Notwithstanding anything in the second sentence of paragraph 2.1.3 to the contrary, in the event that the number of directors to be elected to the Board is increased and there is no public announcement naming all of the nominees for Directors or specifying the size of the increased Board made by the corporation at least one hundred (100) days prior to the first anniversary of the preceding year's annual meeting, a stockholder's notice required by this Section 2 shall also be considered timely, but only with respect to nominees for any new positions created by such increase, if it shall be delivered to the Secretary at the principal executive offices of the corporation not later than the close of business on the tenth (10th) day following the day on which such public announcement is first made by the Corporation.

2.2. Special Meetings. Special meetings of the shareholders may be called either by the president, by the Board or by the holders of not less than one-fifth of all the outstanding shares of the corporation entitled to vote, for the purpose or purposes stated in the call of the meeting.

2.3. Place of Meeting. The Board may designate any place, as the place of meeting for any annual meeting or for any special meeting called by the Board. If no designation is made, or if a special meeting be otherwise called, the place of meeting shall be at Lifeway Foods, Inc., 6431 West Oakton St., Morton Grove, Illinois 60053. The Board may, in its discretion, determine that shareholder meetings may be held solely by means of remote communication. If authorized by the Board, and subject to any guidelines and procedures adopted by the Board, shareholders not physically present at a meeting of shareholders may participate in a meeting of shareholders by means of remote communication; and, may be considered present in person and may vote at a meeting of shareholders held at a designated place or held solely by means of remote communication, subject to the conditions imposed by applicable law.

2.4. Notice of Meetings. Written notice stating the place, date, and hour of the meeting and, in the case of a special meeting, the purpose or purposes for which the meeting is called, shall be delivered not less than 10 nor more than 60 days before the date of the meeting, or in the case of a merger, consolidation, share exchange, dissolution or sale, lease or exchange of assets not less than 20 nor more than 60 days before date of the meeting, either personally or by mail, by or at the direction of the president, or the secretary, or the officer or persons calling the meeting, to each shareholder of record entitled to vote at such meeting. If mailed, such notice shall be deemed to be delivered when deposited in the United States mail addressed to the shareholder at his or her address as it appears on the records of the corporation, with postage thereon prepaid. When a meeting is adjourned to another time or place, notice need not be given of the adjourned meeting if the time and place thereof are announced at the meeting at which the adjournment is taken.

2.5. Fixing of Record Date. For the purpose of determining the shareholders entitled to notice of or to vote at any meeting of shareholders, or shareholders entitled to receive payment of any dividend, or in order to make a determination of shareholders for any other proper purpose, the Board of the corporation may fix in advance a date as the record date to any such determination of shareholders, such date in any case to be not more than 60 days and for a meeting of shareholders, less than 10 days, or in the case of a merger, consolidation, share exchange, dissolution or sale, lease or exchange of assets, less than 20 days before the date of such meeting. If no record date is fixed for the determination of shareholders entitled to notice of or to vote at a meeting of shareholders, or shareholders entitled to receive payment of a dividend, the date on which notice of the meeting is mailed or the date on which the resolution of the Board declaring such dividend is adopted, as the case may be, shall be the record date for such determination of shareholders. A determination of shareholders shall apply to any adjournment of the meeting.

2.6. Voting Lists. The officer or agent having charge of the transfer book for shares of the corporation shall make, within 20 days after the record date for a meeting of shareholders or 10 days before such meeting, whichever is earlier, a complete list of the shareholders entitled to vote at such meeting, arranged in alphabetical order, with the address of and the number of shares held by each, which list, for a period of 10 days prior to such meeting, shall be kept on file at the registered office of the corporation and shall be subject to inspection by any shareholder, and to copying at the shareholder's expense, at any time during usual business hours. Such list shall also be produced and kept open at the time and place of the meeting and shall be subject to the inspection of any shareholder during the whole time of the meeting. The original share ledger or transfer book, or a duplicate thereof kept in this State, shall be prima facie evidence as to who are the shareholders entitled to examine such list or share ledger or transfer book or to vote at any meeting of shareholders.

2.6.1 If any shareholders are participating in the meeting by means of remote communication, the list must be open to examination by the shareholders for the duration of the meeting on a reasonably accessible electronic network, and the information required to access the list must be provided to shareholders with the notice of the meeting.

2.7. Quorum. The holders of a majority of the outstanding shares of the corporation entitled to vote on a matter, represented in person or by proxy, shall constitute a quorum for consideration of such matter at any meeting of shareholders, but in no event shall a quorum consist of less than one-third of the outstanding shares entitled so to vote; provided that if less than a majority of the outstanding shares are represented at said meeting, a majority of the shares so represented may adjourn the meeting at any time without further notice. If a quorum is present, the affirmative vote of the majority of the shares represented at the meeting shall be the act of the shareholders, unless the vote of a greater number or voting by classes is required by the Business Corporation Act, the articles of incorporation or these by-laws. At any adjourned meeting at which a quorum shall be present, any business may be transacted which might have been transacted at the original meeting. Withdrawal of shareholders from any meeting shall not cause failure of a duly constituted quorum at that meeting.

2.8. Proxies. Each shareholder may appoint a proxy to vote or otherwise act for him or her by signing an appointment form and delivering it to the person so appointed, but no such proxy shall be valid after 11 months from the date of its execution, unless otherwise provided in the proxy.

2.9. Voting of Shares. Each outstanding share, regardless of class, shall be entitled to one vote in each matter submitted to vote at a meeting of shareholders, and in all elections for directors every shareholder shall have the right to vote the number of shares owned by such shareholder for as many persons as there are directors to be elected and for whose election the shareholder has a right to vote. Each shareholder may vote either in person or by proxy as provided in Section 2.8 hereof.

2.10. Voting of Shares By Certain Holders. Shares held by the corporation in a fiduciary capacity may be voted and shall be counted in determining the total number of outstanding shares entitled to vote at any given time.

2.10.1 Shares registered in the name of another corporation, domestic or foreign, may be voted by any officer, agent, proxy or other legal representative authorized to vote such shares under the law of incorporation of such corporation. Shares registered in the name of a deceased person, a minor ward or a person under legal disability, may be voted by his or her administrator, executor or court appointed guardian, either in person or by proxy without a transfer of such shares into the name of such administrator, executor or court appointed guardian. Shares registered in the name of a trustee may be voted by him or her, either in person or by proxy.

2.10.2 Shares registered in the name of a receiver may be voted by such receiver, and shares held by or under the control of a receiver may be voted by such receiver without the transfer thereof into his or her name if authority to do so is contained an appropriate order of the court by which such receiver was appointed.

2.10.3 A shareholder whose shares are pledged shall be entitled to vote such shares until the shares have been transferred into the name of the pledgee, and thereafter the pledgee shall be entitled to vote the shares so transferred.

2.10.4 Any number of shareholders may create a voting trust for the purpose of conferring upon a trustee or trustees the right to vote or otherwise represent their shares, for a period not to exceed 10 years, by entering into a written voting trust agreement specifying the terms and conditions of the voting trust, and by transferring their shares to such trustee or trustees for the purpose of the agreement. Any such trust agreement shall not become effective until a counterpart of the agreement is deposited with the corporation at its registered office. The counterpart of the voting trust agreement so deposited with the corporation shall be subject to the same right of examination by a shareholder of the corporation, in person or by agent or attorney, as are the books and records of the corporation, and shall be subject to examination by any holder of a beneficial to rest in the voting trust, either in person or by agent or attorney, at any reasonable time for any proper purpose. Shares of its own stock belonging to this corporation shall not be voted, directly or indirectly, at any meeting and shall not be counted in determining the total number of outstanding shares at any given time, but shares of its own stock held by it in a fiduciary capacity may be voted and shall be counted in determining the total number of outstanding shares at any given time.

2.11. Cumulative Voting. In all elections for directors there shall be no right of cumulative voting.

2.12. Inspectors. At any meeting of shareholders, presiding officer may, or upon the request of any shareholder, shall appoint one or more persons as inspectors for such meeting.

2.12.1 Such inspectors shall ascertain and report the number of shares represented at the meeting, based upon their determination of the validity and effect of proxies; count all votes and report the results; and do such other acts as are proper to conduct the election and voting with impartiality and fairness to all the shareholders.

2.12.2 Each report of an inspector shall be in writing and signed by him or her or by a majority of them if there be more than one inspector acting at such meeting. If there is more than one inspector, the report of a majority shall be the report of the inspectors. The report of the inspector or inspectors on the number of shares represented at the meeting and the results of the voting shall be prima facie evidence thereof.

2.13. Informal Action By Shareholders. Any action required to be taken at a meeting of the shareholders, or any other action which may be taken at a meeting of the shareholders, taken without a meeting and without a vote, if a consent in writing, setting forth the action so taken shall be signed (a) if 5 days prior notice of the proposed action is given in writing to all of the shareholders entitled to vote with respect to the subject matter hereof, by the holders of outstanding shares having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting at which all shares entitled to vote thereon were present and voting or (b) by all of the shareholders entitled to vote with respect to the subject matter thereof.

2.13.1 Prompt notice of the taking of the corporate action without a meeting by less than unanimous written consent shall be given in writing to those shareholders who have not consented in writing. In the event that the action which is consented to is such as would have required the filing of a certificate under any section of the Business Corporation Act if such action had been voted on by the shareholders at a meeting thereof, the certificate filed under such section shall state, in lieu of any statement required by such section concerning any vote of shareholders, that written consent has been given in accordance with the provisions of Section 7.10 of the Business Corporation Act and that written notice has been given as provided in such Section 7.10.

2.14. Voting By Ballot. Voting on any question or in any election may be by voice unless the presiding officer shall order or any shareholder shall demand that voting be by ballot.

2.15. Abstentions and Broker Non-Votes. Outstanding shares represented in person or by proxy (including Broker Non-Votes and shares that abstain with respect to one or more proposals presented for shareholder approval) will be counted for purposes of determining whether a quorum is present at a meeting. Except as otherwise provided by law, Abstentions and Broker Non-Votes will be treated as shares that are present and entitled to vote for purposes of determining the number of shares that are present and entitled to vote with respect to any particular proposal, but will not be counted as a vote cast on such proposal. Abstentions and Broker Non-Votes, therefore, will have no effect on proposals which require a plurality or majority of votes cast for approval, but will have the same effect as a vote “against” proposals requiring any percentage of the outstanding voting securities for approval.

ARTICLE III

DIRECTORS

3.1. General Powers. The business of the corporation shall be managed by or under the direction of its Board.

3.2. Number, Tenure and Qualifications. The number of directors of the corporation shall not be less than three (3). The number of directors may be set by the Board by resolution from time to time. Each director shall hold office until the next annual meeting of shareholders; or until his or her successor shall have been elected and qualified. Directors need not be residents of Illinois or shareholders of the corporation. The number of directors may be increased or decreased from time to time by the amendment of this section. No decrease shall have the effect of shortening the term of any incumbent director.

3.3. Election Procedures. At each annual meeting, the shareholders shall elect the directors. If the directors shall not have been elected at any annual meeting, they may be elected at a special meeting of shareholders called for that purpose in the manner provided by these Bylaws.

3.3.1 Except as provided in this Section, each director shall be elected by the vote of the majority of the votes cast. A majority of votes cast means that the number of shares cast “for” a director’s election exceeds the number of votes cast “against” that director. The following shall not be votes cast: (a) a share whose ballot is marked as withheld; (b) a share otherwise present at the meeting but for which there is an abstention; and (c) a share otherwise present at the meeting for which a shareholder gives no authority or direction (“Broker Non-Votes”). In a contested election, the directors shall be elected by the vote of a plurality of the votes cast.

3.3.2 A nominee in an uncontested election who does not receive a majority vote shall not be elected. An incumbent director not elected because he or she does not receive a majority vote shall continue to serve as a holdover director until the earliest of (a) the date on which the Board either (i) appoints an individual to fill the office held by such director, (ii) by resolution, leaves the office vacant, or (iii) by resolution, eliminates the directorship by reducing the number of directors; or (b) the date of the incumbent director’s resignation.

3.3.3 Any vacancy resulting from the non-election of a director under this Section may be filled by the Board as provided in Section 3.9. If no director receives a majority vote in an uncontested election, then the incumbent directors (a) will nominate a slate of directors and hold a special meeting for the purpose of electing those nominees as soon as practicable, and (b) may in the interim fill one or more offices with the same director(s) who will continue in office until their successors are elected.

3.4. Regular Meetings. A regular meeting of the Board shall be held without other notice than this by-law, immediately after the annual meeting of shareholders. The Board may provide, by resolution, the time and place for holding of additional regular meetings without other notice than such resolution.

3.5. Special Meetings. Special meetings of the Board may be called by or at the request of the president or any two directors. The person or persons authorized to call special meetings of the Board may fix any as the place for holding any special meeting of the Board called by them.

3.6. Notice. Notice of any special meeting shall be given at least 2 days previous thereto by written notice to each director at the address provided to the Corporation by each director. If mailed, such notice shall be deemed to be delivered when deposited in the United States mail so addressed, with postage thereon prepaid. If notice is given by facsimile transmission, such notice shall be deemed to be delivered upon the day the facsimile transmission is sent. If notice is given by electronic mail transmission, such notice shall be deemed to be delivered upon the day the electronic mail transmission is sent. The attendance of a director at any meeting shall constitute a waiver of notice of such meeting, except where a director attends a meeting for the express purpose of objecting to the transaction of any business because the meeting is not lawfully called or convened. Neither the business to be transacted at, nor the purpose of, any regular or special meeting of the Board need be specified in the notice or waiver of notice of such meeting.

3.7. Quorum. A majority of the number of directors fixed by these by-laws shall constitute a quorum for transaction of business at any meeting of the Board, provided that if less than a majority of such number of directors are present at said meeting, a majority of the directors present may adjourn the meeting at any time without further notice.

3.8. Manner of Acting. The act of the majority of the directors present at a meeting at which a quorum is present shall be the act of the Board, unless the act of a greater number is required by statute, these by-laws, or the articles of incorporation.

3.9. Vacancies. Any vacancy or new office on the Board may be filled by election at the next annual or special meeting of shareholders. A majority of the Board may fill any vacancy or new office prior to such annual or special meeting of shareholders.

3.10. Resignation and Removal of Directors. A director may resign at any time upon written notice to the Board. A director may be removed with or without cause, by a majority of shareholders if the notice of the meeting names the director or directors to be removed at said meeting.

3.11. Informal Action By Directors. The authority of the Board may be exercised without a meeting if a consent in writing, setting forth the action taken, is signed by all of the directors entitled to vote.

3.12. Compensation. The Board, by the affirmative vote of a majority of directors then in office, and irrespective of any personal interest of any of its members shall have authority to establish reasonable compensation of all directors for services to the corporation as directors, officers or otherwise notwithstanding any director conflict of interest. By resolution of the Board, the directors may be paid their expenses, if any, of attendance at each meeting of the board. No such payment previously mentioned in this section shall preclude any director from serving the corporation in any other capacity and receiving compensation therefor.

3.13. Presumption of Assent. A director of the corporation who is present at a meeting of the Board at which action on any corporate matter is taken shall be conclusively presumed to have assented to the action taken unless his or her dissent shall be entered in the minutes of the meeting or unless he or she shall file his or her written dissent to such action with the person acting as the secretary of the meeting before the adjournment thereof or shall forward such dissent by registered or certified mail to the secretary of the corporation immediately after the adjournment of the meeting. Such right to dissent shall not apply to a director who voted in favor of such action.

3.14. Committees. A majority of the Board may create one or more committees of two or more members to exercise appropriate authority of the Board. A majority of such committee shall constitute a quorum for transaction of business. A committee may transact business without a meeting by unanimous written consent.

3.14.1 For so long as the corporation is subject to continued listing requirements of The Nasdaq Capital Market or another stock exchange, trading platform or marketplace (the "Exchange"), the corporation shall maintain an audit committee, compensation committee and nominating committee that meet the requirements of the relevant Exchange, subject to any exemptions available therefrom.

ARTICLE IV

OFFICERS

4.1. Number. The officers of the corporation shall be a president, one or more vice-presidents, a treasurer, a secretary, and such other officers as may be elected or appointed by the Board. Any two or more offices may be held by the same person.

4.2. Election and Term of Office. The officers of the corporation shall be elected annually by the Board at the first meeting of the Board held after each annual meeting of shareholders. If the election of officers shall not be held at such meeting, such election shall be held as soon thereafter as conveniently may be. Vacancies may be filled or new offices created and filled at any meeting of the Board. Each officer shall hold office until his or her successor shall have been duly elected and shall have qualified or until his or her death or until he or she shall resign or shall have

4.3. Removal. Any officer elected or appointed by the Board may be removed by the Board whenever in its judgment the best interest of the corporation would be served thereby, but such removal shall be without prejudice to the contract rights, if any, of the person so removed.

4.4. President. The president shall be the principal executive officer of the corporation. Subject to the direction and control of the Board, he/she shall be in charge of the business of the corporation; he/she shall see that the resolutions and directions of the Board are carried into effect except in those instances in which that responsibility is specifically assigned to some other person by the Board; and, in general, he/she shall discharge all duties incident to the office of president and such other duties as may be prescribed by the Board from time to time. He/She shall preside at all meetings of the shareholders and of the Board. Except in those instances in which the authority to execute is expressly delegated to another officer or agent of the corporation or a different mode of execution is expressly prescribed by the Board or these by-laws, he/she may execute for the corporation certificates for its shares, and any contracts, deeds, mortgages, bonds, or other instruments which the Board has authorized to be executed, and he/she may accomplish such execution either under or without the seal of the corporation and either individually or with the secretary, any assistant secretary, or any other officer thereunto authorized by the Board, according to the requirements of the form of the instrument. He or she may vote all securities which the corporation is entitled to vote except as and to the extent such authority shall be vested in a different officer or agent of the corporation by the Board.

4.5. The Vice-Presidents. The vice-president (or in the event there be more than one vice-president, each of the vice-presidents) shall assist the president in the discharge of his/her duties as the president may direct and shall perform such other duties as from time to time may be assigned to him/her by the president or by the Board. In the absence of the president or in the event of his/her inability or refusal to act, the vice-president (or in the event there be more than one vice-president, the vice-presidents in the order designated by the Board, or by the president if the Board has not made such a designation, or in the absence of any designation, then in the order of seniority of tenure as vice-president) shall perform the duties of the president, and when so acting, shall have all the powers of and be subject to all the restrictions upon the president. Except in those instances in which the authority to execute is expressly delegated to another officer or agent of the corporation or a different mode of execution is expressly prescribed by the Board or these by-laws, the vice-president (or each of them if there are more than one) may execute for the corporation certificates for its shares and any contracts, deed, mortgages, bonds or other instruments which the Board has authorized to be executed, and he/she may accomplish such execution either under or without the seal of the corporation and either individually or with the secretary, any assistant secretary, or any other officer thereunto authorized by the Board, according to the requirements of the form of the instrument.

4.6. The Treasurer. The treasurer shall be the principal accounting and financial officer of the corporation. He/She shall: (a) have charge of and be responsible for the maintenance of adequate books of account for the corporation; (b) have charge and custody of all funds and securities of the corporation, and be responsible therefor and for the receipt and disbursement thereof; and (c) perform all the duties incident to the office of treasurer and such other duties as from time to time may be assigned to him by the president or by the Board. If required by the Board, the treasurer shall give a bond for the faithful discharge of his/her duties in such sum and with such surety or sureties as the Board may determine.

4.7. The Secretary. The secretary shall: (a) record the minutes of the shareholders' and of the Board' meetings in one or more books provided for that purpose; (b) see that all notices are duly given in accordance with the provisions of these by-laws or as required by law; (c) be custodian of the corporate records and of the seal of the corporation; (d) keep a register of the post-office address of each shareholder which shall be furnished to the secretary by such shareholder; (e) sign with the president, or a vice-president, or any other officer thereunto authorized by the Board, certificates for shares of the corporation, the issue of which shall have been authorized by the Board, and any contracts, deeds, mortgages, bonds, or other instruments which the Board has authorized to be executed, according to the requirements of the form of the instrument, except when a different mode of execution is expressly prescribed by the Board or these by laws; (f) have general charge of the stock transfer books of the corporation; (g) have authority to certify the by- laws, resolutions of the shareholders and Board and committees thereof, and other documents of the corporation as true and correct copies thereof, and (h) perform all duties incident to the office of secretary and such other duties as from time to time may be assigned to him/her by the president or by the Board.

4.8. Assistant Treasurers and Assistant Secretaries. The assistant treasurers and assistant secretaries shall perform such duties as shall be assigned to them by the treasurer or the secretary, respectively, or by the president or the Board. The assistant secretaries may sign with the president, or a vice-president, or any other officer thereunto authorized by the Board, certificates for shares of the corporation, the issue of which shall have been authorized by the Board, and any contracts, deeds, mortgages, bonds, or other instruments which the Board has authorized to be executed, according to the requirements of the form of the instrument, except when a different mode of execution is expressly prescribed by the Board or these by-laws. The assistant treasurers shall respectively, if required by the Board, give bonds for the faithful discharge of their duties in such sums and with such sureties as the Board shall determine.

4.9. Salaries. The salaries of the officers shall be fixed from time to time by the Board or any committee thereof and no officer shall be prevented from receiving such salary by reason of the fact that he or she is also a director of the corporation.

ARTICLE V

CONTRACTS, LOANS, CHECKS AND DEPOSITS

5.1. Contracts. The Board may authorize any officer or officers, agent or agents, to enter into any contract or execute and deliver any instrument in the name of and on behalf of the corporation, and such authority may be general or confined to specific instances.

5.2. Loans. No loans shall be contracted on behalf of the corporation and no evidences of indebtedness shall be issued in its name unless authorized by a resolution of the Board.

5.3. Checks, Drafts, Etc. All checks, drafts or other orders for the payment of money, notes or other evidences of Indebtedness is issued in the name of the corporation, shall be signed by such officer or officers, agent or agents of the corporation and in such manner as shall from time to time be determined by dissolution of the Board.

5.4. Deposits. All funds of the corporation not otherwise employed shall be deposited from time to time to the credit of the corporation in such banks, trust companies or other depositories as the Board may select.

ARTICLE VI

SHARES AND THEIR TRANSFER,

6.1. Shares Represented By Certificates and Uncertificated Shares. Shares either shall be represented by certificates or shall be uncertificated shares.

6.1.1 Certificates representing shares of the corporation shall be signed by the appropriate officers and may be sealed with the seal or a facsimile of the seal of the corporation. If a certificate is countersigned by a transfer agent or registrar, other than the corporation or its employee, any other signatures may be facsimile. Each certificate representing shares shall be consecutively numbered or otherwise identified, and shall also state the name of the person to whom issued, the number and class of shares (with designation of series, if any), the date of issue, and that the corporation is organized under Illinois law. If the corporation is authorized to issue shares of more than one class or of series within a class, the certificate shall also contain such information or statement as may be required by law. Unless prohibited by the articles of incorporation, the Board may provide by resolution that some or all of any class or series of shares shall be uncertificated shares. Any such resolution shall not apply to shares represented by a certificate until the certificate has been surrendered to the corporation. Within a reasonable time after the issuance or transfer of uncertificated shares, the corporation shall send the registered owner thereof a written notice of all information that would appear on a certificate. Except as otherwise expressly provided by law, the rights and obligations of the holders of uncertificated shares shall be identical to those of the holders of certificates representing shares of the same class and series.

6.1.2 The name and address of each shareholder, the number and class of shares held and the date on which the shares were issued shall be entered on the books of the corporation. The person in whose name shares stand on the books of the corporation shall be deemed the owner thereof for all purposes as regards the corporation.

6.2. Lost Certificates. If a certificate representing shares has allegedly been lost or destroyed the Board may in its discretion, except as may be required by law, direct that a new certificate be issued upon such indemnification and other reasonable requirements as it may impose.

6.3. Transfers of Shares. Transfer of shares of the corporation shall be recorded on the books of the corporation. Transfer of shares represented by a certificate, except in the case of a lost or destroyed certificate, shall be made on surrender for cancellation of the certificate for such shares. A certificate presented for transfer must be duly endorsed and accompanied by proper guaranty of signature and other appropriate assurances the endorsement is effective. Transfer of an uncertificated share shall be made on receipt by the corporation of an instruction from the registered owner or other appropriate person. The instruction shall be in writing or a communication in such form as may be agreed upon in writing by the corporation.

ARTICLE VII

FISCAL YEAR

7.1. The fiscal year of the corporation shall be fixed by resolution of the Board. In the absence of such a resolution, the fiscal year of the corporation shall be the calendar year.

ARTICLE VIII

DISTRIBUTIONS

8.1. The Board may authorize, and the corporation may make, distributions to its shareholders, subject to any restrictions in its articles of incorporation or provided by law.

ARTICLE IX

SEAL

9.1. The corporate seal shall have inscribed thereon the name of the corporation and the words Corporate Seal, Illinois. The seal may be used by causing it or a facsimile thereof to be impressed or affixed or in any other manner reproduced, provided that affixing of the corporate seal to an instrument shall not give the instrument additional force or effect, or change the construction thereof, and the use of the corporate seal is not mandatory.

ARTICLE X

WAIVER OF NOTICE

10.1. Whenever any notice is required to be given under the provisions of these by-laws or under the provisions of the articles of incorporation or under the provisions of The Business Corporation Act of the State of Illinois, a waiver thereof in writing, signed by the person or persons entitled to such notice, whether before or after the time stated therein, shall be deemed equivalent to the giving of such notice. Attendance at any meeting shall constitute waiver of notice thereof unless the person at the meeting objects to the holding of the meeting because proper notice was not given.

ARTICLE XI

INDEMNIFICATION OF OFFICERS, DEBTORS, EMPLOYEES AND AGENTS,

11.1. The corporation shall indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action by or in the right of the corporation) by reason of the fact that such person is or was a director, officer, employee or agent of the corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by such person in connection with such action, suit or proceeding if he or she acted in good faith and in a manner he or she reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe his or her conduct was unlawful. The termination of any action, suit or proceeding by judgment or settlement, conviction or upon a plea of nolo contendere or its equivalent, shall not, of itself, create a presumption that the person did not act in good faith and in a manner which he or she reasonably believed to be in or not opposed to the best interest of the corporation, and with respect to any criminal action or proceeding, had reasonable cause to believe that his or her conduct was unlawful.

11.2. The corporation shall indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action or suit by or in the right of the corporation to procure a judgment in its favor any reason of the fact that such person is or was a director, officer, employee or agent of the corporation, or is or was serving at the request of the corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise against expenses (including attorneys' fees) actually and reasonably incurred by such person in connection with the defense or settlement of such action or suit if he or she acted in good faith and in a manner he or she reasonably believed to be in or not opposed to the best interests of the corporation and except that no indemnification shall be made in respect of any claim, issue or matter as to which such person shall have been adjudged to be liable for negligence or misconduct in the performance of his or her duty to the corporation unless and only to the extent that the court in which such action or suit was brought shall determine upon application that despite the adjudication of liability but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses which the court shall deem proper.

11.3. To the extent that a director, officer, employee or agent of a corporation has been successful, on the merits or otherwise, in the defense of any action, suit or proceeding referred to in sections 1 and 2, or in defense of any claim, or matter therein, such person shall be indemnified against expenses actually and reasonably incurred by such person in connection therewith.

11.4. Any indemnification under sections 1 and 2 shall be made by the corporation only as authorized in the specific case upon a determination that indemnification of the director, officer, employee or agent is proper in the circumstances because he or she has met the applicable standard of conduct set forth in sections 1 and 2. Such determination shall be made (a) by the Board by a majority vote of a quorum consisting of directors who were not parties to such action, suit or proceeding, or (b) if such a quorum is not obtainable, or, even if obtainable, a quorum of disinterested directors so directs, by independent legal counsel in a written opinion, or (c) by the shareholders.

11.5. Expenses incurred in defending a civil or criminal action, suit or proceeding may be paid by the corporation in advance of the final disposition of such action, suit or proceeding, as authorized by the Board in the specific case, upon receipt of an undertaking by or on behalf of the director, officer, employee or agent to repay such amount, unless it shall ultimately be determined that he or she is entitled to be indemnified by the corporation as authorized in this article.

11.6. The indemnification provided by this article shall not be deemed exclusive of any other rights to which those seeking indemnification may be entitled under any by-law, agreement, vote of shareholders or disinterested directors or otherwise, both as to action in his or her official capacity and as to action in another capacity while holding such office, and shall continue as to a person who has ceased to be a director, officer, employee or agent and shall inure to the benefit of the heirs, executors and administrators of such a person.

11.7. The corporation shall have power to purchase and maintain insurance on behalf of any person who is or was a director, officer, employee or agent of the corporation, or is or was serving at the request of the corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise against any liability asserted against such person and incurred by such person in any such capacity, or arising out of his or her status as such, whether or not the corporation would have the power to indemnify such person against such liability under the provisions of these sections.

11.8. If the corporation has paid indemnity or has advanced expenses to a director, officer, employee or agent, the corporation shall report the indemnification or advance in writing to the shareholders with or before the notice of the next shareholders' meeting.

11.9. References to "the corporation" shall include, in addition to the surviving corporation, any merging corporation, including any corporation having merged with a merging corporation, absorbed in a merger which otherwise would have lawfully been entitled to indemnify its directors, officers, and employees or agents.

ARTICLE XII

AMENDMENTS

12.1. Unless the power to make, alter, amend or repeal the by-laws is reserved to the shareholders by the articles of incorporation, the by-laws of the corporation may be made, altered, amended or repealed by the shareholders or the Board, but no by-law adopted by the shareholders may be altered, amended or repealed by the Board if the by-laws so provide. The by-laws may contain any provisions for the regulation and management of the affairs of the corporation not inconsistent with the law or the articles of incorporation.

Amendment to Settlement Agreement

This Amendment to the Settlement Agreement, dated November 7, 2022 (including all exhibits hereto, this "Amendment"), is by and among Lifeway Foods, Inc. (the "Company") on the one hand and Edward Smolyansky ("Mr. Smolyansky") and Ludmila Smolyansky ("Mrs. Smolyansky") and, together with Mr. Smolyansky, the "Shareholders") on the other hand (each, a "Party" and, collectively, the "Parties").

WHEREAS, the Parties have previously entered into that certain Settlement Agreement, dated as of July 27, 2022 (the "Agreement"); and

WHEREAS, the Company and Mrs. Smolyansky desire to enter into that certain Common Stock Purchase Agreement, dated as of November 7, 2022 (the "Purchase Agreement"), pursuant to which Mrs. Smolyansky will sell to the Company, and the Company will purchase from Mrs. Smolyansky, certain shares of the Company's common stock held by Mrs. Smolyansky and the Shareholders will execute and deliver this Amendment; and

WHEREAS, the Parties desire to, among other things, amend the terms of the Agreement as provided below.

NOW, THEREFORE, in consideration of the mutual covenants and agreements set forth herein and in the Purchase Agreement, and in consideration of other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, and intending to be legally bound hereby, the Parties hereby covenant and agree as follows:

1. All capitalized terms not otherwise defined herein shall have the meanings ascribed to such terms in the Agreement except that all references to the "2022 Annual Meeting" shall deemed to be references to the "Annual Meetings".

2. Section 1 of the Agreement is hereby amended by deleting in its entirety the phrase "at the 2022 annual meeting of the shareholders (together with any postponements, adjournments or other delays thereof, the "2022 Annual Meeting")" and replacing it with the following:

"at each annual meeting of the shareholders during the Term (as defined below) (together with any postponements, adjournments or other delays thereof, each an "Annual Meeting")"

3. Section 1 of the Agreement is hereby amended by deleting in its entirety the phrase ", which approvals shall not be unreasonably withheld" and replacing it with the following:

", which approvals shall not be unreasonably withheld, and the Board shall promptly thereafter appoint such substitute person as a director of the Company"

4. Section 2 of the Agreement is hereby deleted in its entirety and replaced with the following:

“The Shareholders agree to appear in person or by proxy and vote (a) all shares of common stock of the Company (the “Common Stock”) beneficially owned (in accordance with Rule 13d-3 promulgated under the Securities Exchange Act of 1934, as amended), individually or otherwise, and controlled by each of the Shareholders and over which the Shareholders have power and authority to vote (“Voting Shares”) in accordance with the recommendations of the Board at any special or annual meeting of the shareholders of the Company with respect to each proposal not related to the sale of the Company or all or substantially all of the assets of the Company and (b) their Voting Shares in proportion to the vote of the other shareholders of the Company with respect to any proposal related to the sale of the Company or all or substantially all of the assets of the Company, or, in case of either (a) or (b) of this Section 2, at the request of the Company delivered at least five (5) business days prior to the date of the applicable special or annual meeting of the shareholders of the Company, to appear in person and to give their proxy to the Company-appointed proxies to be voted in accordance with this Section 2 in their capacities as such attaching without instruction as to how to vote on any such proposal. Mr. Smolyansky hereby agrees to consent to and approve the voting of shares of Common Stock held by Smolyansky Holding LLC in a manner such that fifty percent (50.0%) of such shares are voted in accordance with the preceding sentence, and the remaining fifty percent (50.0%) of such shares are voted in accordance with the direction of the other manager(s) of Smolyansky Holding LLC.”

5. The introductory language in Section 6 of the Agreement is hereby deleted in its entirety and replaced with the following:

“From the date hereof through and including the date that is the earlier of (i) the day of the Company’s 2024 annual meeting of shareholders and (ii) the date of any material breach by the Company of its obligations under Sections 1 and 5 of this Agreement, other than a breach resulting from any Shareholder, provided that (if such breach is curable) the Company has received ten days prior written notice of such breach and such breach has not been cured prior to the expiration of such ten day period (the “Term”), other than in their respective capacities as a director of the Company or otherwise in accordance with this Agreement, the Shareholders shall not, without the prior written consent of the Company:”

6. A new Section 22 as set forth below is hereby included in the Agreement:

“22. Subject to the expiration or waiver of the right of first refusal (the “Danone ROFR”) of Danone North America PBC and its affiliates (collectively, “Danone”) pursuant to that certain Stockholders’ Agreement, dated as of October 1, 1999, as amended from time to time (the “Stockholder Agreement”), by and among Danone, the Company and certain members of the Smolyansky family, including the Shareholders, no Shareholder shall, directly or indirectly, sell, transfer, assign, pledge, hypothecate or otherwise dispose of (“Transfer”) shares of Common Stock except in accordance with the provisions of this Section 22.

(a) On or after the date on which a Shareholder contemplating a Transfer of Common Stock (in such case, a “Selling Shareholder”) provides notice to Danone of a proposed transfer pursuant to Section 4.01 of the Stockholders Agreement (a “Transfer Notice”), the Selling Shareholder shall provide a copy of the Transfer Notice to the Company.

(b) Subject to the Danone ROFR, the Company shall have the right (the “Company ROFR”), exercisable by written notice given to the Selling Shareholder within 16 business days after its receipt of such Transfer Notice, to purchase (or to cause another person designated by the Company to purchase) all, but not less than all, of the Common Stock specified in the Transfer Notice, at the purchase price and on the other terms set forth therein. If the consideration specified in the Transfer Notice includes any property other than cash, such purchase price shall be deemed to be the amount of any cash included as part of such consideration plus the value (as jointly determined by internationally recognized independent public accountancy firms selected by each of the Company and the Selling Shareholder or, in the event such firms are unable to agree, a third internationally recognized independent public accountancy firm to be selected by the first two such firms) of such other property included in such consideration, and the date by which the Company must exercise the Company ROFR shall be extended until five business days after the determination of the value of the property included in the consideration.

(c) If the Company exercises the Company ROFR, the closing of the purchase of the Common Stock with respect to which such right has been exercised shall take place within 10 business days after the Company gives notice of such exercise; provided that if any approval of or notice to any governmental agency or the Company's shareholders is required in connection with such purchase of Common Stock, the Selling Shareholder and the Company shall use all reasonable efforts to obtain such approvals or to provide such notices and the closing shall take place within five business days after receipt of the last such approval and expiration of any required waiting periods.

(d) If Danone does not exercise the Danone ROFR under the Stockholder Agreement and the Company does not exercise the Company ROFR within the time specified for such exercise, the Selling Shareholder shall be free during the 90-day period following the expiration the Danone ROFR, but only during such period, to sell the Common Stock specified in the applicable Transfer Notice to the person specified therein (the "Purchaser") for the consideration (or at any price in excess thereof) and on substantially the same terms (or on other terms more favorable to the Selling Shareholder) specified therein; provided, however, that (i) such Purchaser's offer constituted a bona fide, arm's length offer, (ii) at the request of the Company, the Selling Shareholder shall have obtained an opinion from an internationally recognized investment bank, selected jointly by the Company and the Selling Shareholder, to the effect that the consideration to be paid by such Purchaser per share of Common Stock falls within a reasonable range of valuations therefor, (iii) such Purchaser's ownership of the Common Stock could reasonably be expected, in the opinion of the Board, to materially disadvantage the business of the Company and its subsidiaries or could reasonably be expected to have an adverse effect on the future profitability of the Company and its subsidiaries, taken as a whole.

(e) The Company's ROFR shall not apply to (i) any proposed Transfer by a Shareholder if the amount of shares to be so Transferred when combined with all other Transfers of Common Stock by the Shareholders during the calendar year does not equal or exceed 2% of the shares of Common Stock issued and outstanding as of the date of the Transfer Notice delivered in connection with such proposed Transfer, (ii) any proposed Transfer by a Shareholder to an immediate family member or a trust in which the beneficiary is the Shareholder or an immediate family member of such Shareholder; (iii) any proposed Transfer by a Shareholder to a charitable organization; provided that in the case of clauses (ii) and (iii) the transferee shall have agreed to be bound by the terms of this Agreement; or (iv) any proposed Transfer to Danone.

No transferee (other than a Shareholder) of Common Stock be entitled to any of the rights set forth under this Agreement by virtue of its ownership of such Common Stock.

(f) Any attempted Transfer in violation of this Section 22 shall be null, void and of no force and effect, and the Company shall not give effect to any such attempted Transfer."

7. All references to the Agreement in future correspondence or notices shall be deemed to refer to the Agreement as modified by this Amendment.

8. Except as expressly modified or amended by this Amendment, all of the terms, covenants and conditions of the Agreement are hereby ratified and confirmed.

9. This Amendment may be executed in one or more counterparts, each of which shall be considered an original instrument, but all of which shall be considered one and the same agreement, and shall become binding when one or more counterparts have been signed by each of the Parties hereto and delivered to each of the other Parties hereto. Delivery of an executed counterpart of this Amendment by facsimile or electronic mail in portable document format (pdf) shall be equally as effective as delivery of an original executed counterpart of this Amendment.

[SIGNATURE PAGES FOLLOW]

IN WITNESS WHEREOF, each of the Parties hereto has executed this Amendment to Settlement Agreement or caused the same to be executed by its duly authorized representative as of the date first above written.

LIFEWAY FOODS, INC

By: /s/ Julie Smolyansky

Name: Julie Smolyansky

Title: Chief Executive Officer

SHAREHOLDERS

/s/Edward Smolyansky
Edward Smolyansky

/s/ Ludmila Smolyansky
Ludmila Smolyansky

RESTRICTED STOCK UNIT AGREEMENT

LIFEWAY FOODS, INC.

This Agreement is made as of April 27, 2022 and is by and between Lifeway Foods, Inc., an Illinois corporation (the “Company”) and Jason Scher (“Director”), a non-employee director.

Restricted Stock Units

1. **Grant Date.** After compensation to the board of directors (the “Board”) on August 12, 2021 was approved by the Board, the Company hereby grants Director as of April 27, 2022 (the “Grant Date”), an award (“Award”) in the form of 40,625 restricted stock units (the “Units”), subject to the terms and conditions set forth herein.
2. **Accounts.** The Units granted to Director shall be credited to an account (the “Account”) established and maintained for Director. The Account shall be the record of Units granted to the Director pursuant to this Agreement, is solely for accounting purposes and shall not require a segregation of any Company assets.
3. **Terms and Conditions.** Except as otherwise provided herein, the Units shall remain non-vested and subject to substantial risk of forfeiture.

Valuation of Restricted Stock Units

4. **Value of Units.** The value of each Unit on any date shall be equal to the value of one share of the Company’s common stock (“Company Stock”) on such date.
5. **Value of Stock.** For purposes of this Agreement, the value of the Company’s Common Stock is the closing price of the Company Stock on the relevant date.

Vesting of Restricted Stock Units

6. **Vesting.** Of the 40,625 Units, Director’s interest in 35,268 Units is fully vested and non-forfeitable as of the date hereof. With respect to remaining 5,357 Units, Director’s interest in 1,786 Units will vest and become non-forfeitable on August 12, 2022; 1,786 Units will vest and become non-forfeitable on August 12, 2023 and the remaining 1,785 Units shall vest and become non-forfeitable on August 12, 2024. In the event of a change of control of the Company, the unvested Units shall become fully vested.

Termination of Service During the Vesting Period

7. **Death or Disability.** Anything in this Agreement to the contrary notwithstanding, if Director dies or becomes Disabled while serving as a director for the Company or an Affiliate and prior to the forfeiture of the Units under Section 8, all Units that are forfeitable shall become non-forfeitable as of the date of Director's death or Disability, as the case may be and shall be paid in accordance with the provisions contained herein. For purposes of this Agreement, "Disability" or "Disabled" means Director's permanent and total disability within the meaning of Section 22(e)(3) of the Code.
8. **Forfeiture.** If Director's service as a director for the Company or an Affiliate terminates for any reason other than Director's death or Disability, all unvested Units at such time shall be forfeited.

Payment of Awards

9. **Time of Payment.** Payment of Director's vested Units shall only be made as soon as practicable after Director no longer serves as a director for the Company.
10. **Form of Payment.** If previously approved by the Company's shareholders, the vested Units shall be paid in whole shares of the Company's Common Stock and if not previously approved by the Company's shareholders, the vested Units shall be paid in cash equal to the number of vested Units multiplied by the value of the Company Stock (as determined in accordance with Section 5) on the last day that the Director serves as a director of the Company.
11. **Death of Director.** If Director dies prior to the payment of his or her non-forfeitable Units, such Units shall be paid to his or her beneficiary or his estate. The Company shall pay the amounts due hereunder to the beneficiary designated by Director or his executor. If Director fails to designate a beneficiary, or if at the time of the Director's death there is no surviving beneficiary, any amounts payable will be paid to the Director's estate.

General Provisions

12. **No Right to Continued Service.** Neither this Award nor the granting or vesting of Units shall confer upon Director any right with respect to continuance of service as a director for the Company or an Affiliate.

13. **Change in Capital Structure.** The terms of this grant shall be adjusted as the Compensation Committee determines is equitable in the event the Company effects one or more stock dividends, stock split-ups, subdivisions or consolidations of shares or other similar changes in capitalization.
14. **Section 409A.** This Agreement is intended to comply with, or satisfy an exemption from, the provisions of Section 409A of the Code. To that end this Agreement shall at all times be interpreted in a manner that is consistent with Section 409A of the Code. Notwithstanding any other provision in this Agreement to the contrary, the Company shall have the right, in its sole discretion, to adopt such amendments to this Agreement or take such other actions (including amendments and actions with retroactive effect) as it determines is necessary or appropriate for this Agreement to comply with Section 409A of the Code or an exemption therefrom.
15. **Governing Law.** This Award shall be governed by the laws of the State of Illinois and applicable Federal law. All disputes arising under this Award shall be adjudicated solely within the state or Federal courts located within the State of Illinois.
16. **Binding Effect.** Subject to the limitations stated above, this Award shall be binding upon and inure to the benefit of the legatees, distributees, and personal representatives of Director and the successors of the Company.

IN WITNESS WHEREOF, the Company has caused this Award to be signed on its behalf.

LIFEWAY FOODS, INC

By: /s/ Julie Smolyansky

JASON SCHER

/s/ Jason Scher

Exhibit 21**Subsidiaries of Lifeway Foods, Inc.**

Below is a list of the subsidiaries of Lifeway Foods, Inc. All of the voting stock of each subsidiary is 100% owned directly by Lifeway Foods, Inc.

Name of Subsidiary	Jurisdiction of Incorporation or Organization
Lifeway Wisconsin, Inc.	Illinois
The Lifeway Kefir Shop, LLC	Illinois
Fresh Made, Inc.	Pennsylvania
Lifeway Foods Europe Limited	Ireland

Exhibit 23.1

Consent of Independent Registered Public Accounting Firm

We have issued our report dated March 27, 2023, with respect to the consolidated financial statements included in the Annual Report of Lifeway Foods, Inc. on Form 10-K for the year ended December 31, 2022. We consent to the incorporation by reference of said report in the Registration Statement of Lifeway Foods, Inc. on Form S-8 (No. 333-210463).

/s/ Grant Thornton LLP

Chicago, Illinois
March 27, 2023

Exhibit 23.2

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in the Registration Statement on Form S-8 (No. 333-210463) of our report dated July 21, 2022, with respect to the consolidated financial statements of Lifeway Foods, Inc. and Subsidiaries as of December 31, 2021 and for the year then ended, included in this annual report on Form 10-K of Lifeway Foods, Inc. and Subsidiaries as of and for the year ended December 31, 2022.

/s/ Mayer Hoffman McCann P.C.

Chicago, Illinois
March 27, 2023

Exhibit 31.1

SECTION 302 CERTIFICATION OF CHIEF EXECUTIVE OFFICER

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Julie Smolyansky, certify that:

1. I have reviewed this annual report on Form 10-K of Lifeway Foods, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 27, 2023

By: /s/ Julie Smolyansky

Julie Smolyansky
Chief Executive Officer, President and Director
(Principal Executive Officer)

Exhibit 31.2

SECTION 302 CERTIFICATION OF CHIEF FINANCIAL OFFICER

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Eric Hanson, certify that:

1. I have reviewed this annual report on Form 10-K of Lifeway Foods, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 27, 2023

By: /s/ Eric Hanson

Eric Hanson
Chief Financial & Accounting Officer

Exhibit 32.1

SECTION 906 CERTIFICATION OF CHIEF EXECUTIVE OFFICER

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT
TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report on Form 10-K of Lifeway Foods, Inc. (the "Company") for the period ended December 31, 2022 as filed with the SEC (the "Report"), the undersigned, in the capacity and on the date indicated below, hereby certifies pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to her knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operation of the Company.

Date: March 27, 2023

By: /s/ Julie Smolyansky
Julie Smolyansky
Chief Executive Officer, President and Director
(Principal Executive Officer)

Exhibit 32.2

SECTION 906 CERTIFICATION OF CHIEF FINANCIAL OFFICER

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT
TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report on Form 10-K of Lifeway Foods, Inc. (the "Company") for the period ended December 31, 2022 as filed with the SEC (the "Report"), the undersigned, in the capacity and on the date indicated below, hereby certifies pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operation of the Company.

Date: March 27, 2023

By: /s/ Eric Hanson
Eric Hanson
Chief Financial & Accounting Officer



Lifeway Foods® Announces Results for the Fourth Quarter and Record Full Year Ended December 31, 2022

Record annual net sales of \$141.5 million, up 18.9% year-over-year and 51.1% compared to 2019

Delivers 13th straight quarter of year-over-year net sales growth

Morton Grove, IL — March 27, 2023 — Lifeway Foods, Inc. (Nasdaq: LWAY) (“Lifeway” or “the Company”), a leading U.S. supplier of kefir and fermented probiotic products to support the microbiome, today reported financial results for the fourth quarter and full year ended December 31, 2022.

“Culminated by our thirteenth straight quarter of year-over-year topline growth, I am thrilled to report the highest recorded year of sales in Lifeway’s history, up 18.9% compared to a very strong year in 2021, and up 51.1% when compared to 2019,” commented Julie Smolyansky, President and Chief Executive Officer of Lifeway Foods. “What we accomplished in 2022 was a remarkable feat, reflecting our team’s year-round execution of the Lifeway 2.0 strategy, and driven by the continued dominance of our core Lifeway Kefir product. Throughout 2022 we strategically invested behind our core products to expand awareness and drive velocities, and our efforts clearly paid dividends. Despite facing broader macro headwinds that affected our industry, our premium, better-for-you offerings grew in both consumption and dollars. In the year ahead, we aim to assess further distribution opportunities in current and new channels such as convenience, where we have seen positive initial results. We will look to pursue incremental brand awareness and exposure for our category-leading, core Lifeway Kefir behind continued investments in marketing. I am extremely happy with our performance in this record-breaking year and look forward to continuing this momentum in 2023.”

Full Year 2022 Results

Net sales were \$141.5 million for the year ended December 31, 2022, an increase of \$22.5 million or 18.9% from the prior year. The net sales increase was primarily driven by higher volumes of our branded drinkable kefir and the impact of price increases implemented during the year, and to a lesser extent, the favorable impact of our acquisition of Glen Oaks Farms during the third quarter of 2021.

Gross profit as a percentage of net sales was 18.9% for the year ended December 31, 2022.

Selling, general and administrative expenses as a percentage of net sales were 16.9% for the year ended December 31, 2022, compared to 19.1% in the prior year.

The Company reported net income of \$0.9 million or \$0.06 per basic and diluted common share for the year ended December 31, 2022 compared to net income of \$3.3 million or \$0.21 per basic and diluted common share during the same period in 2021.

Conference Call and Webcast

A pre-recorded conference call and webcast with Julie Smolyansky discussing these results with additional comments and details is available through the "Investor Relations" section of the Company's website at <https://lifewaykefir.com/webinars-reports/> and will also be available for replay.

About Lifeway Foods, Inc.

Lifeway Foods, Inc., which has been recognized as one of Forbes' Best Small Companies, is America's leading supplier of the probiotic, fermented beverage known as kefir. In addition to its line of drinkable kefir, the company also produces cheese, probiotic oat milk, and a ProBugs line for kids. Lifeway's tart and tangy fermented dairy products are now sold across the United States, Mexico, Ireland and France. Learn how Lifeway is good for more than just you at lifewayfoods.com.

Forward-Looking Statements

This release (and oral statements made regarding the subjects of this release) contains "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995 regarding, among other things, future operating and financial performance, product development, market position, business strategy and objectives. These statements use words, and variations of words, such as "continue," "build," "future," "increase," "drive," "believe," "look," "ahead," "confident," "deliver," "outlook," "expect," and "predict." Other examples of forward-looking statements may include, but are not limited to, (i) statements of Company plans and objectives, including the introduction of new products, or estimates or predictions of actions by customers or suppliers, (ii) statements of future economic performance, and (iii) statements of assumptions underlying other statements and statements about Lifeway or its business. You are cautioned not to rely on these forward-looking statements. These statements are based on current expectations of future events and thus are inherently subject to uncertainty. If underlying assumptions prove inaccurate or known or unknown risks or uncertainties materialize, actual results could vary materially from Lifeway's expectations and projections. These risks, uncertainties, and other factors include: price competition; the decisions of customers or consumers; the actions of competitors; changes in the pricing of commodities; the effects of government regulation; possible delays in the introduction of new products; and customer acceptance of products and services. A further list and description of these risks, uncertainties, and other factors can be found in Lifeway's Annual Report on Form 10-K for the fiscal year ended December 31, 2022, and the Company's subsequent filings with the SEC. Copies of these filings are available online at <https://www.sec.gov>, <http://lifewaykefir.com/investor-relations/>, or on request from Lifeway. Information in this release is as of the dates and time periods indicated herein, and Lifeway does not undertake to update any of the information contained in these materials, except as required by law. Accordingly, YOU SHOULD NOT RELY ON THE ACCURACY OF ANY OF THE STATEMENTS OR OTHER INFORMATION CONTAINED IN ANY ARCHIVED PRESS RELEASE.

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LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
December 31, 2022 and 2021
(In thousands)

	December 31,	
	2022	2021
Current assets		
Cash and cash equivalents	\$ 4,444	\$ 9,233
Accounts receivable, net of allowance for doubtful accounts and discounts & allowances of \$1,820 and \$1,170 at December 31, 2022 and 2021, respectively	11,414	9,930
Inventories, net	9,631	8,285
Prepaid expenses and other current assets	1,445	1,254
Refundable income taxes	44	344
Total current assets	26,978	29,046
Property, plant and equipment, net		
	20,905	20,130
Operating lease right-of use asset	174	216
Goodwill	11,704	11,704
Intangible assets, net	7,438	7,978
Other assets	1,800	1,800
Total assets	\$ 68,999	\$ 70,874
Current liabilities		
Current portion of note payable	\$ 1,250	\$ 1,000
Accounts payable	7,979	6,614
Accrued expenses	3,813	3,724
Accrued income taxes	–	725
Total current liabilities	13,042	12,063
Line of credit	2,777	2,777
Note payable	2,477	3,470
Operating lease liabilities	104	85
Deferred income taxes, net	3,029	3,201
Other long-term liabilities	–	147
Total liabilities	21,429	21,743
Commitments and contingencies (Note 9)		
Stockholders' equity		
Preferred stock, no par value; 2,500 shares authorized; none issued	–	–
Common stock, no par value; 40,000 shares authorized; 17,274 shares issued; 14,645 and 15,435 shares outstanding at 2022 and 2021	6,509	6,509
Paid-in capital	3,624	2,552
Treasury stock, at cost	(16,993)	(13,436)
Retained earnings	54,430	53,506
Total stockholders' equity	47,570	49,131
Total liabilities and stockholders' equity	\$ 68,999	\$ 70,874

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Operations
For the three months and twelve months ended December 31, 2022 and 2021
(In thousands, except per share data)

	Three Months Ended December 31,		Twelve months Ended December 31,	
	2022	2021	2022	2021
Net sales	\$ 35,838	\$ 30,974	\$ 141,568	\$ 119,065
Cost of goods sold	27,318	24,331	112,350	87,604
Depreciation expense	599	652	2,432	2,751
Total cost of goods sold	<u>27,917</u>	<u>24,983</u>	<u>114,782</u>	<u>90,355</u>
Gross profit	7,921	5,991	26,786	28,710
Selling expenses	2,777	2,587	11,304	11,097
General and administrative	3,047	2,909	12,593	11,611
Amortization expense	135	89	540	122
Total operating expenses	5,959	5,585	24,437	22,830
Income from operations	1,962	406	2,349	5,880
Other income (expense):				
Interest expense	(96)	(44)	(267)	(116)
Realized gain on investments, net	-	-	-	2
Loss on sale of property and equipment	(241)	-	(241)	(88)
Other (expense) income	10	(1)	-	(62)
Total other (expense) income	<u>(327)</u>	<u>(45)</u>	<u>(508)</u>	<u>(264)</u>
Income before provision for income taxes	1,635	361	1,841	5,616
Provision for income taxes	919	454	917	2,305
Net income (loss)	\$ 716	\$ (93)	\$ 924	\$ 3,311
Earnings (loss) per common share:				
Basic	<u>\$ 0.05</u>	<u>\$ (0.01)</u>	<u>\$ 0.06</u>	<u>\$ 0.21</u>
Diluted	<u>\$ 0.05</u>	<u>\$ (0.01)</u>	<u>\$ 0.06</u>	<u>\$ 0.21</u>
Weighted average common shares:				
Basic	<u>15,199</u>	<u>15,435</u>	<u>15,396</u>	<u>15,537</u>
Diluted	<u>15,557</u>	<u>15,686</u>	<u>15,718</u>	<u>15,773</u>

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Years Ended December 31, 2022 and 2021
(In thousands)

	2022	2021
Cash flows from operating activities:		
Net income	\$ 924	\$ 3,311
<i>Adjustments to reconcile net income to operating cash flow:</i>		
Depreciation and amortization	2,972	2,873
Non-cash interest expense	6	11
Non-cash rent expense	–	1
Bad debt expense	–	2
Deferred revenue	(28)	(30)
Stock-based compensation	1,109	1,144
Deferred income taxes	(172)	257
Loss on sale of property and equipment	241	88
<i>(Increase) decrease in operating assets:</i>		
Accounts receivable	(1,483)	(1,931)
Inventories	(1,345)	(1,356)
Refundable income taxes	300	(313)
Prepaid expenses and other current assets	(191)	(91)
<i>Increase (decrease) in operating liabilities:</i>		
Accounts payable	1,945	1,022
Accrued expenses	434	504
Accrued income taxes	(725)	72
Net cash provided by operating activities	3,987	5,564
Cash flows from investing activities:		
Purchases of property and equipment	(3,449)	(1,922)
Acquisition, net of cash acquired	(580)	(5,220)
Net cash used in investing activities	(4,029)	(7,142)
Cash flows from financing activities:		
Purchase of treasury stock	(3,997)	(1,583)
Payment of deferred financing cost	–	(32)
Proceeds from note payable	–	5,000
Repayment of note payable	(750)	(500)
Net cash (used in) provided by financing activities	(4,747)	2,885
Net (decrease) increase in cash and cash equivalents	(4,789)	1,307
Cash and cash equivalents at the beginning of the period	9,233	7,926
Cash and cash equivalents at the end of the period	\$ 4,444	\$ 9,233
Supplemental cash flow information:		
Cash paid for income taxes, net of (refunds)	\$ 1,121	\$ 2,288
Cash paid for interest	\$ 247	\$ 102
Non-cash investing activities		
Increase in right-of-use assets and operating lease obligations	\$ 83	\$ 45
Business acquisition escrow payable	\$ –	\$ 580