LIFEWAY FOODS INC
Form 10-Q/A
December 02, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q/A

AMENDMENT NO. 1

(Mark One)

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

For the quarterly period ended: June 30, 2009

o TRANSITION REPORT UNDER 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	36-3442829
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

6431 West Oakton, Morton Grove, IL 60053
(Address of Principal Executive Offices, Zip Code)

(847-967-1010)
(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or

15(d) of the Securities Exchange Act of 1934 during the past 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 o No x

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data file required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

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

Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller reporting company x

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

As of December 1, 2009, the issuer had 16,775,930 shares of common stock, no par value, outstanding.

EXPLANATORY NOTE

This amendment to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2009 of Lifeway Foods, Inc. (as originally filed on August 14, 2009, the "Form 10-Q") is being filed to correct typographical errors in the Form 10-Q. The Form 10-Q is restated herein in its entirety. The disclosures in this amendment (the "Form 10-Q/A") continue to speak as of the date of the Form 10-Q, and do not reflect events occurring after the filing of the Form 10-Q. Accordingly, this Form 10-Q/A should be read in conjunction with our other filings made with the Securities and Exchange Commission subsequent to the filing of the 10-Q, including any amendments to those filings. The filing of this Form 10-Q/A shall not be deemed an admission that the Form 10-Q when made included any untrue statement of a material fact or omitted to state a material fact necessary to make a statement not misleading.

LIFEWAY FOODS, INC.
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LIFEWAY FOODS, INC. AND SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2009 and 2008

AND DECEMBER 31, 2008

PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Financial Condition
June 30, 2009 and 2008 (Unaudited) and December 31, 2008

	(Unaudited) June 30 2009	(Unaudited) June 30 2008	December 31, 2008
ASSETS			
Current assets			
Cash and cash equivalents	$ 582,766	$ 342,039	$ 277,248
Marketable securities	4,659,161	6,472,027	5,262,168
Inventories	3,817,195	3,851,725	3,097,542
Accounts receivable, net of allowance for doubtful accounts of $110,011 and $35,011 at June 30, 2009 and 2008 and $110,011 at December 31, 2008	6,064,801	4,626,287	4,765,865
Prepaid expenses and other current assets	55,669	12,582	23,226
Other receivables	65,730	49,571	40,314
Deferred income taxes	638,372	602,227	919,649
Refundable income taxes	778,125	—	356,416
Total current assets	16,661,819	15,956,458	14,742,428
Property and equipment, net	13,793,929	10,769,676	11,062,714
Intangible assets			
Goodwill and other non amortizable brand asset	12,154,091	5,414,858	5,414,858
Other intangible assets, net of accumulated amortization of $1,260,810 and $761,699 at June 30, 2009 and 2008 and $921,422 at December 31, 2008	6,596,829	3,095,939	2,936,216
Total intangible assets	18,750,920	8,510,797	8,351,074
Other assets	500,000	500,000	500,000
Total assets	$ 49,706,668	$ 35,736,931	$ 34,656,216
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities			
Current maturities of notes payable	$ 6,219,788	$ 1,130,612	$ 928,444
Accounts payable	2,024,313	1,873,644	2,260,272
Accrued expenses	617,662	548,706	458,282
Margin payable	—	407,479	—
Accrued income taxes	—	395,093	—
Total current liabilities	8,861,763	4,355,534	3,646,998
Notes payable	7,907,847	3,517,841	3,108,014

Deferred income taxes		1,941,740		1,647,550		1,607,155
Stockholders' equity						
Common stock, no par value; 20,000,000 shares authorized; 17,273,776 shares issued; 16,812,955 shares outstanding at June 30, 2009; 17,273,776 shares issued; 16,740,407 shares outstanding at June 30, 2008; and 17,273,776 shares issued; 16,724,467 shares outstanding at December 31, 2008		6,509,267		6,509,267		6,509,267
Paid-in-capital		1,912,845		1,149,068		1,202,009
Treasury stock, at cost		(3,353,490)		(3,110,637)		(3,302,025)
Retained earnings		26,463,077		22,271,730		22,383,707
Accumulated other comprehensive loss, net of taxes		(536,381)		(603,422)		(498,909)
Total stockholders' equity		30,995,318		26,216,006		26,294,049
Total liabilities and stockholders' equity	$	49,706,668	$	35,736,931	$	34,656,216

See accompanying notes to financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Income and Comprehensive Income
For the Three and Six Months Ended June 30, 2009 and 2008 (Unaudited)
and the Year Ended December 31, 2008

	(Unaudited) Three Months Ended June 30,		(Unaudited) Six Months Ended June 30,		Year Ended December 31,
	2009	2008	2009	2008	2008
Sales	14,479,429	$ 11,523,393	$ 28,215,509	$ 22,645,631	44,461,455
Cost of goods sold	7,978,110	7,455,696	16,102,691	14,897,779	30,926,114
Depreciation expense	353,654	195,128	570,428	384,552	777,715
Total cost of goods sold	8,331,764	7,650,824	16,673,119	15,282,331	31,703,829
Gross profit	6,147,665	3,872,569	11,542,390	7,363,300	12,757,626
Selling Expenses	1,386,815	1,154,126	2,694,740	2,213,292	4,098,176
General and Administrative	1,437,505	1,092,420	2,810,103	2,077,466	4,149,010
Amortization expense	168,698	79,862	339,388	159,723	319,446
Total Operating Expenses	2,993,018	2,326,408	5,844,231	4,450,481	8,566,632
Income from operations	3,154,647	1,546,161	5,698,159	2,912,819	4,190,994
Other income (expense):					
Interest and dividend income	48,506	62,862	110,717	165,995	343,329
Rental Income	11,947	11,647	21,294	23,294	48,886
Interest expense	(110,090)	(68,969)	(264,473)	(154,924)	(298,619)
Impairment of marketable securities	—	—	—	—	(958,879)
Loss on Disposition of Equipment	(2,825)	—	(2,825)	—	—
Gain (loss) on sale of marketable securities, net	53,638	(87,174)	(96,152)	(36,145)	(733,647)
Total other income (Expense)	1,176	(81,634)	(231,439)	(1,780)	(1,598,930)
Income before provision for income taxes	3,155,823	1,464,527	5,466,720	2,911,039	2,592,064
Provision for income taxes	623,918	552,809	1,387,350	1,110,715	679,789
Net income	$ 2,531,905	$ 911,718	$ 4,079,370	$ 1,800,324	$ 1,912,275
	0.15	0.05	0.24	0.11	0.11

Basic and diluted earnings per common share									
Weighted average number of shares outstanding		16,823,691		16,765,094		16,823,691		16,789,727		16,765,080
COMPREHENSIVE INCOME										
Net income	$	2,531,905	$	911,718	$	4,079,370	$	1,800,324	$	1,912,275
Other comprehensive income (loss), net of tax: Unrealized gains (losses) on marketable securities (net of tax benefits)		306,293		(233,221)		(37,472)		(415,596)		(720,517)
Less reclassification adjustment for (gains) losses included in net income (net of taxes)				51,171				21,217		430,651
Comprehensive income	$	2,838,198	$	729,668	$	4,041,898	$	1,405,945	$	1,622,409

See accompanying notes to financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Changes in Stockholders Equity
For the Six Months Ended June 30, 2009 (Unaudited)
and the Year Ended December 31, 2008

	# of Shares Issued	Common Stock, No Par Value 20,000,000 Shares Authorized # of Shares Outstanding	# of Shares of Treasury Stock	Common Stock	Paid In Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss), Net of Tax
Balances at December 31, 2007	17,273,776	16,827,726	446,050	6,509,267	1,120,669	(2,078,165)	20,471,432	(209,043)
Redemption of stock	—	(112,009)	112,009	—	—	(1,239,488)	—	—
Issuance of treasury stock for compensation	—	8,750	(8,750)	—	81,340	15,628	—	—
Other comprehensive income (loss): Unrealized losses on securities, net of taxes and reclassification adjustment	—	—	—	—	—	—	—	(289,866)
Net income for the year ended December 31, 2008	—	—	—	—	—	—	1,912,275	—
Balances at December 31, 2008	17,273,776	16,724,467	549,309	6,509,267	1,202,009	(3,302,025)	22,383,707	(498,909)
Redemption of stock	—	(48,341)	48,341	—	—	(402,947)	—	—
	—	7,882	(7,882)	—	66,098	16,220	—	—

Issuance of treasury stock for compensation									
Issuance of treasury stock for Fresh Made acquisition	—	128,947	(128,947)	—	644,738	335,262	—	—	
Other comprehensive income (loss): Unrealized gains on securities, net of taxes and reclassification adjustment	—	—	—	—	—	—	—	(37,472)	
Net income for the six months ended June 30, 2009	—	—	—	—	—	—	4,079,370	—	
Balances at June 30, 2009	17,273,776	16,812,955	460,821	$ 6,509,267	$ 1,912,845	$ (3,353,490)	$ 26,463,077	$ (536,381)	$

See accompanying notes to financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Six Months Ended June 30, 2009 and 2008 (Unaudited)
and the Year Ended December 31, 2008

	(Unaudited) Six Months Ended June 30, 2009	June 30, 2008	December 31, 2008
Cash flows from operating activities:			
Net income	$ 4,079,370	$ 1,800,324	$ 1,912,275
Adjustments to reconcile net income to net cash flows from operating activities, net of acquisition:			
Depreciation and amortization	909,816	544,275	1,092,995
(Gain)Loss on sale of marketable securities, net	96,152	36,145	733,647
Loss on disposition of assets	2,825	—	—
Impairment of marketable securities	—	—	958,879
Deferred income taxes	179,796	(78,035)	(509,386)
Treasury stock issued for compensation	82,318	34,650	96,968
Increase (decrease) in allowance for doubtful accounts	—	(4,449)	70,551
(Increase) decrease in operating assets:			
Accounts receivable	(752,978)	(412,176)	(626,754)
Other receivables	(25,416)	(6,460)	2,797
Inventories	(346,800)	(345,171)	409,012
Refundable income taxes	(435,205)	240,880	(115,536)
Prepaid expenses and other current assets	5,029	8,950	(1,973)
Increase (decrease) in operating liabilities:			
Accounts payable	(440,911)	279,314	665,942
Accrued expenses	36,719	134,667	44,243
Margin payable	—	—	—
Accrued income taxes	—	395,093	—
Net cash provided by operating activities	3,390,715	2,628,007	4,733,660
Cash flows from investing activities:			
Purchases of marketable securities	(3,342,662)	(3,490,650)	(5,782,452)
Sale of marketable securities	4,127,666	3,299,791	5,323,423
Increase in margin	—	407,479	—
Purchases of property and equipment	(714,052)	(1,475,280)	(2,157,315)
Acquisition of Fresh Made, net of cash acquired	(2,898,224)	—	—
Net cash used in investing activities	(2,827,272)	(1,258,660)	(2,616,344)
Cash flows from financing activities:			
Proceeds of note payable	1,742,085	—	—
Purchases of treasury stock, net	(402,947)	(1,038,723)	(1,239,488)
Repayment of notes payable	(1,597,063)	(584,470)	(1,196,465)
Net cash provided (used) in financing activities	(257,925)	(1,623,193)	(2,435,953)
Net increase (decrease) in cash and cash equivalents	305,518	(253,846)	(318,637)
	277,248	595,885	595,885

Cash and cash equivalents at the beginning of the period						
Cash and cash equivalents at the end of the period	$	582,766	$	342,039	$	277,248

See accompanying notes to financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
June 30, 2009 and 2008
and December 31, 2008

Note 1 – NATURE OF BUSINESS

Lifeway Foods, Inc. (The "Company") commenced operations in February 1986 and incorporated under the laws of the state of Illinois on May 19, 1986. The Company's principal business activity is the production of dairy products. Specifically, the Company produces Kefir, a drinkable product which is similar to but distinct from yogurt, in several flavors sold under the name "Lifeway's Kefir;" a plain farmer's cheese sold under the name "Lifeway's Farmer's Cheese;" a fruit sugar-flavored product similar in consistency to cream cheese sold under the name of "Sweet Kiss;" and a dairy beverage, similar to Kefir, with increased protein and calcium, sold under the name "Basics Plus." The Company also produces several soy-based products under the name "Soy Treat" and a vegetable-based seasoning under the name "Golden Zesta." The Company currently distributes its products throughout the Chicago Metropolitan area and various cities in the East Coast through local food stores. In addition, the products are sold throughout the United States and Ontario, Canada by distributors. The Company also distributes some of its products to Eastern Europe.

Note 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies applied in the preparation of the accompanying financial statements follows:

Principles of consolidation
The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, LFI Enterprises, Inc., Helios Nutrition, Ltd., Pride of Main Street, L.L.C., Starfruit, L.L.C. and Fresh Made, Inc. All significant intercompany accounts and transactions have been eliminated.

Use of estimates
The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates made in preparing the consolidated financial statements include the allowance for doubtful accounts, the valuation of goodwill, intangible assets and deferred taxes.

Revenue Recognition
Sales represent sales of Company produced dairy products that are recorded at the time of shipment and the following four criteria have been met: (i) The product has been shipped and the Company has no significant remaining obligations; (ii) Persuasive evidence of an agreement exists; (iii) The price to the buyer is fixed or determinable and (iv) Collection is probable. In addition, shipping costs invoiced to the customers are included in net sales and the related cost in cost of sales.

Cash and cash equivalents
All highly liquid investments purchased with an original maturity of three months or less are considered to be cash equivalents.

The Company maintains cash deposits at several institutions located in the greater Chicago, Illinois and Philadelphia, Pennsylvania metropolitan areas.

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LIFEWAY FOODS, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
June 30, 2009 and 2008
and December 31, 2008

Note 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Bank balances of amounts reported by financial institutions are categorized as follows:

	June 30, 2009	June 30, 2008	December 31, 2008
Amounts insured	$ 1,411,079	$ 251,589	$ 847,711
Uninsured and uncollateralized amounts	402,977	889,463	—
Total bank balances	$ 1,814,056	$ 1,141,052	$ 847,711

Marketable securities
All investment securities are classified as available-for-sale, are carried at fair value or quoted market prices. Unrealized gains and losses on available-for-sale securities are reported as a separate component of stockholders' equity. Amortization, accretion, interest and dividends, realized gains and losses, and declines in value judged to be other-than-temporary on available-for-sale securities are recorded in other income. All of the Company's securities are subject to a periodic impairment evaluation. This evaluation depends on the specific facts and circumstances. Factors that we consider in determining whether an other-than-temporary decline in value has occurred include: the market value of the security in relation to its cost basis; the financial condition of the investee; and the intent and ability to retain the investment for a sufficient period of time to allow for possible recovery in the market value of the investment.

Accounts receivable
Credit terms are extended to customers in the normal course of business. The Company performs ongoing credit evaluations of its customers' financial condition and generally requires no collateral.

Accounts receivable are recorded at invoice amounts, and reduced to their estimated net realizable value by recognition of an allowance for doubtful accounts. The Company's estimate of the allowance for doubtful accounts is based upon historical experience, its evaluation of the current status of specific receivables, and unusual circumstances, if any. Accounts are considered past due if payment is not made on a timely basis in accordance with the Company's credit terms. Accounts considered uncollectible are charged against the allowance.

Inventories
Inventories are stated at the lower of cost or market, cost being determined by the first-in, first-out method.

Property and equipment
Property and equipment are stated at depreciated cost or fair value where depreciated cost is not recoverable. Depreciation is computed using the straight-line method. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is charged to income as incurred; significant renewals and betterments are capitalized.

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
June 30, 2009 and 2008
and December 31, 2008

Note 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

Property and equipment are being depreciated over the following useful lives:

Category	Years
Buildings and improvements	31 and 39
Machinery and equipment	5 – 12
Office equipment	5 – 7
Vehicles	5

Intangible assets
The Company accounts for intangible assets at historical cost. Intangible assets acquired in a business combination are recorded under the purchase method of accounting at their estimated fair values at the date of acquisition. Goodwill represents the excess purchase price over the fair value of the net tangible and other intangible assets acquired. Goodwill is not amortized and is reviewed for impairment at least annually. Brand assets represent the fair value of brands acquired. Brand assets have an indefinite life, therefore are not amortized, rather are reviewed periodically for impairment. The Company amortizes other intangible assets over their estimated useful lives, as disclosed in the table below.

The Company reviews intangible assets and their related useful lives at least once a year to determine if any adverse conditions exist that would indicate the carrying value of these assets may not be recoverable. The Company conducts more frequent impairment assessments if certain conditions exist, including: 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 the Company's products or changes in the size of the market for the Company's products.

If the estimate of an intangible asset's remaining useful life is changed, the remaining carrying amount of the intangible asset is amortized prospectively over the revised remaining useful life.

Intangible assets are being amortized over the following useful lives:

Category	Years
Recipes	4
Customer lists and other customer related intangibles	7-10
Lease agreement	7
Trade names	15
Formula	10
Customer relationships	12

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
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Note 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

Income taxes
Deferred income taxes arise from temporary differences resulting from income and expense items reported for financial accounting and tax purposes in different periods. Deferred taxes are classified as current or non-current, depending on the classification of the assets and liabilities to which they relate. Deferred taxes arising from temporary differences that are not related to an asset or liability are classified as current or non-current depending on the periods in which the temporary differences are expected to reverse.

The principal sources of temporary differences are different depreciation and amortization methods for financial statement and tax purposes, unrealized gains or losses related to marketable securities, capitalization of indirect costs for tax purposes, and the recognition of an allowance for doubtful accounts for financial statement purposes.

As of January 1, 2007, the Company adopted FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109" (FIN 48), which clarifies the accounting and disclosure for uncertainty in tax positions, as defined. Pursuant to FIN 48, the Company has analyzed filing positions in all of 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 only periods subject to examination for the Company's federal return are the 2004 through 2007 tax years. The Company believes that its income tax filing positions and deductions would be sustained on audit and does not anticipate any adjustments that would result in a material change to its financial position. Therefore, no reserves for uncertain income tax positions have been recorded pursuant to FIN 48. In addition, the Company did not record a cumulative effect adjustment related to the adoption of FIN 48.

The Company's policy for recording interest and penalties associated with audits is to record such items as a component of income before taxes. There were no such items during the periods covered in this report.

Treasury stock
Treasury stock is recorded using the cost method.

Advertising costs
The Company expenses advertising costs as incurred. During the year ended December 31, 2008 and for the six months ended June 30, 2009 and 2008, approximately $1,530,207, $780,116 and $893,710 of such costs respectively, were expensed.

Earning per common share
Earnings per common share were computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period. For the six months ended June 30, 2009 and 2008 and the year ended December 31, 2008, diluted and basic earnings per share were the same, as the effect of dilutive securities options outstanding was not significant.

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
June 30, 2009 and 2008
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Note 3 – ACQUISITION

On February 6, 2009, Lifeway Foods, Inc., a Illinois corporation (“Lifeway”) completed a Stock Purchase Agreement (the “Stock Agreement”) by and among Lifeway, Ilya Mandel, an individual and Michael Edelson, an individual (each a “Seller” and collectively “Sellers”).

Lifeway purchased from Sellers all of the issued and outstanding stock (the “Shares”) of Fresh Made, Inc., a Pennsylvania corporation (“Fresh”). The consideration for the Shares was an aggregate of $8,048,000, less certain offsets for any selling expenses in excess of certain limits set forth in the Stock Agreement and other payments and funded debt all as set forth in the Stock Agreement, a note in the principal amount of $2,735,000, due on February 6, 2011, 128,948 shares of common stock of Lifeway valued at a total of $980,000 (“Lifeway’s Common Stock”), the cancellation of a loan in the principal amount of $265,000 and not more than $98,000 in funds held in Fresh’s two accounts with Vist Financial Corp. The issuance of Lifeway’s Common Stock was exempted from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended.

Also on February 6, 2009, Lifeway entered into and consummated a Real Property Purchase Agreement (the “Real Property Agreement”) by and among Sellers and Lifeway. Pursuant to the Real Property Agreement, Lifeway acquired 1.1355 acres of land in Philadelphia, PA (the “Property”) from Sellers. The consideration for the Property was approximately $2,000,000.

The acquisition was accounted for using the purchase accounting method of accounting, and accordingly, the purchase price was allocated to assets acquired and the liabilities assumed based on the fair value as of the merger date. Acquisition costs for legal and professional fees have been included in General and Administrative costs.

The estimated fair value of assets acquired, including the real property, and liabilities assumed consisted of the following:

Cash and cash equivalents	$ 226,000
Accounts receivable (contractual amounts totaling $546,000)	546,000
Other current assets	361,000
Building and other fixed assets	2,617,000
Customer list	4,000,000
Non amortizable goodwill and brand asset	6,739,000
Current liabilities	(461,000)
Total fair value of assets acquired and liablities assumed	$ 14,028,000

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
June 30, 2009 and 2008
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Note 4 – INTANGIBLE ASSETS

Intangible assets, and the related accumulated amortization, consist of the following:

	June 30, 2009		June 30, 2008		December 31, 2008	
	Cost	Accumulated Amortization	Cost	Accumulated Amortization	Cost	Accumulated Amortization
Recipes	$ 43,600	$ 43,600	$ 43,600	$ 40,420	$ 43,600	$ 43,600
Customer lists and other customer related intangibles	4,305,200	385,166	305,200	162,228	305,200	182,938
Lease acquisition	87,200	61,245	87,200	48,790	87,200	55,019
Other	6,638	6,638	6,638	3,984	6,638	4,647
Customer relationship	985,000	239,410	985,000	157,327	985,000	198,368
Contractual backlog	12,000	12,000	12,000	12,000	12,000	12,000
Trade names	1,980,000	385,000	1,980,000	253,000	1,980,000	319,000
Formula	438,000	127,750	438,000	83,950	438,000	105,850
	$ 7,857,638	$ 1,260,809	$ 3,857,638	$ 761,699	$ 3,857,638	$ 921,422

Amortization expense is expected to be as follows for the 12 months ending June 30:

2010	$ 672,250
2011	669,707
2012	658,288
2013	627,275
2014	624,550
Thereafter	3,344,759
	$ 6,596,829

Amortization expense during the six months ended June 30, 2009 and 2008 and for the year ended December 31, 2008 was $339,388, $159,723 and $319,446, respectively.

Goodwill and brand assets increased during the period ending June 30, 2009 due to the acquisition of Fresh Made (See Note 3).

Note 5 – MARKETABLE SECURITIES

The cost and fair value of marketable securities classified as available for sale are as follows:

June 30, 2009	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Equities	$ 1,536,976	$ 57,665	$ (178,926)	$ 1,415,715
Mutual Funds	617,082	842	(267,818)	350,106
Preferred Securities	680,527	14,361	(207,218)	487,670
Corporate Bonds	506,165	5,836	(7,781)	504,220
Government agency Obligations	1,889,963	15,201	(3,714)	1,901,450
Total	$ 5,230,713	$ 93,905	$ (665,457)	$ 4,659,161

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Note 5 – MARKETABLE SECURITIES - Continued

June 30, 2008	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Equities	$ 3,190,184	$ 58,147	$ (569,316)	$ 2,679,015
Mutual Funds	827,737	4,371	(138,044)	694,064
Preferred Securities	1,657,944	4,395	(304,967)	1,357,372
Corporate Bonds	1,288,708	387	(73,012)	1,216,083
Municipal Bonds	4,586	352	—	4,938
Government agency Obligations	530,845	—	(10,290)	520,555
Total	$ 7,500,004	$ 67,652	$ (1,095,629)	$ 6,472,027

December 31, 2008	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Equities	$ 2,116,004	$ 75,333	$ (279,487)	$ 1,911,850
Mutual Funds	888,182	202	(339,970)	548,414
Preferred Securities	1,541,423	13,075	(308,963)	1,245,535
Corporate Bonds	783,761	1,559	(19,289)	766,031
Municipal Bonds	4,586	414	—	5,000
Government agency Obligations	778,140	8,668	(1,470)	785,338
Total	$ 6,112,096	$ 99,251	$ (949,179)	$ 5,262,168

Proceeds from the sale of marketable securities were $5,323,423, $4,127,666 and $3,299,791 during the year ended December 31, 2008 and for the six months ended June 30, 2009 and 2008 respectively.

Gross gains of $384,574, $235,408 and $279,278 and gross losses of $1,118,221, $331,562 and $366,452 were realized on these sales during the year ended December 31, 2008 and for the six months ended June 30, 2009 and 2008, respectively.

The following table shows the gross unrealized losses and fair value of Company's investments with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at June 30, 2009:

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Note 5 – MARKETABLE SECURITIES - Continued

	Less Than 12 Months		12 Months or Greater		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Equities	$ 537,047	$ (113,772)	$ 270,700	$ (65,154)	$ 807,747	$ (178,926)
Mutual Funds	95,391	(33,238)	248,327	(234,580)	343,718	(267,818)
Preferred Securities	21,527	(3,368)	365,740	(203,850)	387,267	(207,218)
Corporate Bonds	—	—	212,531	(7,781)	212,531	(7,781)
Government Agency Obligations	—	—	202,046	(3,714)	202,046	(3,714)
	$ 653,965	$ (150,378)	$ 1,299,344	$ (515,079)	$ 1,953,309	$ (665,457)

For the year ended December 31, 2008, we recorded other than temporary impairments related to investments in marketable securities in certain investments of $958,879. The impairments recognized relate to securities that were in an unrealized loss position at December 31, 2008 that were subsequently sold and equity holdings that we consider other than temporarily impaired due to the recent performance of the issuers of those securities.

Equities, Mutual Funds, Corporate Bonds and Government Agency Obligations - The Company's investments in equity securities, mutual funds, corporate bonds and government agency obligations consist of investments in common stock, preferred stock and debt securities of companies in various industries. The Company evaluated the near-term prospects of the issuer in relation to the severity and duration of the impairment. Based on that evaluation and the Company's ability and intent to hold these investments for a reasonable period of time sufficient for a forecasted recovery of fair value, the Company does not consider any material investments to be other-than-temporarily impaired at June 30, 2009.

Preferred Securities - The Company's investments in preferred securities consist of investments in preferred stock of companies in various industries. The Company evaluated the continuing performance of the securities, the credit worthiness of the issuers as well as the near-term prospects of the security in relation to the severity and duration of the impairment. Based on that evaluation and the Company's ability and intent to hold these investments for a reasonable period of time sufficient for a forecasted recovery of fair value, the Company does not consider any material investments to be other-than-temporarily impaired at June 30, 2009.

Note 6 – INVENTORIES

Inventories consist of the following:

	June 30,		December 31,
	2009	2008	2008
Finished goods	$ 1,500,090	$ 1,276,812	$ 1,343,811
Production supplies	1,704,240	1,476,944	1,291,484
Raw materials	612,865	1,097,969	462,247

Total inventories	$	3,817,195	$	3,851,725	$	3,097,542

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Note 7 – PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	June 30, 2009	June 30, 2008	December 31, 2008
Land	$ 1,178,160	$ 969,232	$ 969,232
Buildings and improvements	9,769,348	7,054,840	7,138,042
Machinery and equipment	12,213,069	8,199,914	8,229,202
Vehicles	961,245	581,458	610,558
Office equipment	208,213	116,203	180,351
Construction in process	—	1,828,582	2,309,045
	24,330,035	18,750,229	19,436,430
Less accumulated depreciation	10,536,106	7,980,553	8,373,716
Total property and equipment	$ 13,793,929	$ 10,769,676	$ 11,062,714

Depreciation expense during the year ended December 31, 2008 and for the six months ended June 30, 2009 and 2008 was $777,715, $570,428 and $384,552, respectively.

Note 8 – ACCRUED EXPENSES

Accrued expenses consist of the following:

	June 30, 2009	June 30, 2008	December 31, 2008
Accrued payroll and payroll taxes	$ 219,842	$ 243,876	$ 98,089
Accrued property tax	300,446	293,712	291,819
Other	97,374	11,118	68,374
	$ 617,662	$ 548,706	$ 458,282

Note 9 – NOTES PAYABLE

Notes payable consist of the following:

	June 30, 2009	June 30, 2008	December 31, 2008
Mortgage note payable to a bank, payable in monthly installments of $3,273 including interest at 7%, with a balloon payment of $416,825 due September 25, 2011. Collateralized by real estate.	—	$ 443,275	$ 438,926
Mortgage note payable to a bank, payable in monthly installments of $19,513 including interest at 5.6%, with a balloon payment of $2,652,143 due July 14, 2010. Collateralized by real estate.	—	2,798,264	2,760,288

Note payable to Amani Holding LLC, payable in quarterly installments of $262,500 plus interest at the floating prime rate per annum (7.25% at December 31, 2007) due September 1, 2010 secured by letter of credit.	—	1,406,914	837,244
Note payable to Private Bank in monthly installments of $42,222, plus variable interest rate, currently at 2.945%, with a balloon payment of $5,066,667 due February 6, 2014. Collateralized by substantially all assets of the Company.	7,388,889	—	—
Line of credit with Private Bank at variable interest rate, currently at 2.945%, due on February 6, 2010. Collateralized by real estate.	2,400,000	—	—
Line of credit with Morgan Stanley at variable interest rate, currently at 2.40%. Secured by marketable securities.	1,945,621	—	—
Subordinated notes payable to Ilya Mandel & Michael Edelson, payable in quarterly installments of $341,875, plus interest at the floating rate per annum (3.3% at June 30, 2009) due February 6, 2011.	2,393,125	—	—
Total notes payable	14,127,635	4,648,453	4,036,458
Less current maturities	6,219,788	1,130,612	928,444
Total long-term portion	$ 7,907,847	$ 3,571,841	$ 3,108,014

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Note 9 – NOTES PAYABLE - Continued

Maturities of notes payables are as follows:

For the Period Ended June 30,		
2010	$	6,219,788
2011		1,532,292
2012		506,667
2013		506,667
2014		5,362,221
Total	$	14,127,635

Note 10 – PROVISION FOR INCOME TAXES

The provision for income taxes consists of the following:

	For the Six Months Ended June 30, 2009	For the Six Months Ended June 30, 2008	For the Year Ended December 31, 2008
Current:			
Federal	$ 974,424	$ 969,123	$ 1,005,159
State and local	233,131	219,627	184,016
Total current	1,207,555	1,188,750	1,189,175
Deferred	179,795	(78,035)	(509,386)
Provision for income taxes	$ 1,387,350	$ 1,110,715	$ 679,789

A reconciliation of the provision for income taxes and the income tax computed at the statutory rate is as follows:

	For the Six Months Ended June 30, 2009	For the Six Months Ended June 30, 2008	For the Year Ended December 31, 2008
Federal income tax expense computed at the statutory rate	$ 1,858,685	$ 989,753	$ 881,302
State and local tax expense, net	262,403	139,730	124,419
Permanent differences	(733,738)	(18,768)	(150,772)
Other	—	—	(175,160)
Provision for income taxes	$ 1,387,350	$ 1,110,715	$ 679,789

LIFEWAY FOODS, INC. AND SUBSIDIARIES
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Note 10 – PROVISION FOR INCOME TAXES - Continued

Amounts for deferred tax assets and liabilities are as follows:

	June 30,		December 31,
	2009	2008	