

United States
Securities and Exchange Commission
Washington, D.C. 20549
FORM 10-Q

(Mark One)

- ☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2023
- ☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission File No.: 000-51821

LAKE SHORE BANCORP, INC.

(Exact name of registrant as specified in its charter)

United States

20-4729288

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification Number)

31 East Fourth Street, Dunkirk, New York

14048

(Address of principal executive offices)

(Zip code)

(716) 366-4070

(Registrant's telephone number, including area code)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common stock, par value \$0.01 per share	LSBK	The Nasdaq Stock Market LLC

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, 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 definition of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer <input type="checkbox"/>	Accelerated filer <input type="checkbox"/>
Non-accelerated filer <input checked="" type="checkbox"/>	Smaller reporting company <input checked="" type="checkbox"/>
Emerging growth company <input type="checkbox"/>	

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

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

Yes ☐ No ☒

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practical date:

There were 5,690,776 shares of the registrant's common stock, \$0.01 par value per share, outstanding at November 9, 2023.

TABLE OF CONTENTS

ITEM	PART I	PAGE
<u>1</u>	<u>FINANCIAL STATEMENTS</u>	
	- <u>Consolidated Statements of Financial Condition as of September 30, 2023 (Unaudited) and December 31, 2022</u>	1
	- <u>Consolidated Statements of Income for the Three and Nine Months Ended September 30, 2023 and 2022 (Unaudited)</u>	2
	- <u>Consolidated Statements of Comprehensive Income (Loss) for the Three and Nine Months Ended September 30, 2023 and 2022 (Unaudited)</u>	3
	- <u>Consolidated Statements of Stockholders' Equity for the Three Months Ended March 31, June 30, and September 30, 2023 and 2022 (Unaudited)</u>	4
	- <u>Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2023 and 2022 (Unaudited)</u>	5
	- <u>Notes to Unaudited Consolidated Financial Statements</u>	6
<u>2</u>	<u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	31
<u>3</u>	<u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	44
<u>4</u>	<u>CONTROLS AND PROCEDURES</u>	44
PART II		
<u>1A</u>	<u>RISK FACTORS</u>	45
<u>2</u>	<u>UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u>	46
<u>6</u>	<u>EXHIBITS</u>	47
	<u>SIGNATURES</u>	47

PART I Financial Information
Item 1. Financial Statements
Lake Shore Bancorp, Inc. and Subsidiary
Consolidated Statements of Financial Condition

	September 30, 2023 (Unaudited)	December 31, 2022
(Dollars in thousands, except share data)		
Assets		
Cash and due from banks	\$ 4,562	\$ 9,091
Interest earning deposits	41,437	542
Cash and Cash Equivalents	45,999	9,633
Securities	57,952	73,047
Federal Home Loan Bank stock, at cost	2,347	2,330
Loans receivable, net of allowance for credit losses 2023 \$6,642; 2022 \$7,065	564,848	573,537
Premises and equipment, net	8,043	8,286
Accrued interest receivable	2,889	2,796
Bank-owned life insurance	23,546	23,218
Other assets	7,939	7,067
Total Assets	\$ 713,563	\$ 699,914
Liabilities and Stockholders' Equity		
Liabilities		
Deposits:		
Interest bearing	\$ 484,287	\$ 464,441
Non-interest bearing	99,871	105,678
Total Deposits	584,158	570,119
Short-term borrowings	—	12,596
Long-term debt	36,450	24,950
Advances from borrowers for taxes and insurance	2,219	3,308
Other liabilities	8,879	7,757
Total Liabilities	631,706	618,730
Stockholders' Equity		
Common stock, \$0.01 par value per share, 25,000,000 shares authorized; 6,836,514 shares issued and 5,690,776 shares outstanding at September 30, 2023 and 6,836,514 shares issued and 5,705,225 shares outstanding at December 31, 2022	68	68
Additional paid-in capital	31,462	31,459
Treasury stock, at cost (1,145,738 shares at September 30, 2023 and 1,131,289 shares at December 31, 2022)	(13,717)	(13,571)
Unearned shares held by ESOP	(1,045)	(1,108)
Unearned shares held by compensation plans	(79)	(191)
Retained earnings	78,207	74,859
Accumulated other comprehensive loss	(13,039)	(10,332)
Total Stockholders' Equity	81,857	81,184
Total Liabilities and Stockholders' Equity	\$ 713,563	\$ 699,914

See notes to unaudited consolidated financial statements.

Lake Shore Bancorp, Inc. and Subsidiary
Consolidated Statements of Income

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2023	2022	2023	2022
	(Unaudited)			
	(Dollars in thousands, except per share data)			
Interest Income				
Loans, including fees	\$ 7,699	\$ 6,311	\$ 22,426	\$ 17,600
Investment securities, taxable	223	210	687	610
Investment securities, tax-exempt	240	309	815	935
Other	559	88	1,214	138
Total Interest Income	<u>8,721</u>	<u>6,918</u>	<u>25,142</u>	<u>19,283</u>
Interest Expense				
Deposits	2,104	419	5,332	1,095
Short-term borrowings	—	—	87	—
Long-term debt	309	141	884	354
Other	13	13	39	43
Total Interest Expense	<u>2,426</u>	<u>573</u>	<u>6,342</u>	<u>1,492</u>
Net Interest Income	<u>6,295</u>	<u>6,345</u>	<u>18,800</u>	<u>17,791</u>
(Credit) Provision for Credit Losses	<u>(199)</u>	<u>—</u>	<u>(1,011)</u>	<u>500</u>
Net Interest Income After (Credit) Provision for Credit Losses	<u>6,494</u>	<u>6,345</u>	<u>19,811</u>	<u>17,291</u>
Non-Interest Income				
Service charges and fees	256	277	792	834
Debit card fees	212	214	632	639
Increase in cash surrender value of bank-owned life insurance	114	66	328	262
Unrealized gain (loss) on equity securities	3	2	5	(7)
Unrealized gain (loss) on interest rate swap	—	91	(58)	344
Recovery on previously impaired investment securities	1	2	6	12
Loss on sale of securities available for sale	(3)	—	(52)	—
Net loss on sale of loans	—	—	—	(18)
Other	22	16	59	54
Total Non-Interest Income	<u>605</u>	<u>668</u>	<u>1,712</u>	<u>2,120</u>
Non-Interest Expense				
Salaries and employee benefits	2,773	2,504	8,363	7,371
Occupancy and equipment	715	738	2,212	2,273
Data processing	432	403	1,284	1,094
Professional services	389	562	2,087	1,196
Advertising	157	197	514	456
FDIC insurance	295	46	826	138
Postage and Supplies	59	54	189	168
Other	376	366	1,139	1,283
Total Non-Interest Expense	<u>5,196</u>	<u>4,870</u>	<u>16,614</u>	<u>13,979</u>
Income before Income Taxes	<u>1,903</u>	<u>2,143</u>	<u>4,909</u>	<u>5,432</u>
Income Tax Expense	<u>332</u>	<u>372</u>	<u>838</u>	<u>916</u>
Net Income	<u>\$ 1,571</u>	<u>\$ 1,771</u>	<u>\$ 4,071</u>	<u>\$ 4,516</u>
Basic and diluted earnings per common share	<u>\$ 0.27</u>	<u>\$ 0.30</u>	<u>\$ 0.69</u>	<u>\$ 0.77</u>
Dividends declared per share	<u>\$ —</u>	<u>\$ 0.18</u>	<u>\$ —</u>	<u>\$ 0.50</u>

See notes to unaudited consolidated financial statements.

Lake Shore Bancorp, Inc. and Subsidiary
Consolidated Statements of Comprehensive Income (Loss)

	Three Months Ended September 30,	
	2023	2022
	(Unaudited)	
	(Dollars in thousands)	
Net Income	\$ 1,571	\$ 1,771
Other Comprehensive (Loss), net of tax benefit:		
Unrealized holding (losses) on securities available for sale, net of tax benefit	(3,171)	(3,954)
Reclassification adjustments related to:		
Recovery on previously impaired investment securities included in net income, net of tax expense	(2)	(1)
Net loss on sale of securities included in net income, net of tax benefit	3	—
Total Other Comprehensive Loss	(3,170)	(3,955)
Total Comprehensive Loss	\$ (1,599)	\$ (2,184)

	Nine Months Ended September 30,	
	2023	2022
	(Unaudited)	
	(Dollars in thousands)	
Net Income	\$ 4,071	\$ 4,516
Other Comprehensive (Loss), net of tax benefit:		
Unrealized holding (losses) on securities available for sale, net of tax benefit	(2,744)	(13,517)
Reclassification adjustments related to:		
Recovery on previously impaired investment securities included in net income, net of tax expense	(5)	(9)
Net loss on sale of securities included in net income, net of tax benefit	42	—
Total Other Comprehensive Loss	(2,707)	(13,526)
Total Comprehensive Income (Loss)	\$ 1,364	\$ (9,010)

See notes to unaudited consolidated financial statements.

Lake Shore Bancorp, Inc. and Subsidiary
Consolidated Statements of Stockholders' Equity
Three Months Ended March 31, June 30, and September 30, 2023 and 2022 (Unaudited)

	Common Stock	Additional Paid-In Capital	Treasury Stock	Unearned Shares Held by ESOP	Unearned Shares Held by Compensation Plans	Retained Earnings	Accumulated Other Comprehensiv e Income (Loss)	Total
	(Dollars in thousands, except share data)							
Balance - January 1, 2022	\$ 68	\$ 31,350	\$ (13,660)	\$ (1,194)	\$ (157)	\$ 70,591	\$ 978	\$ 87,976
Net income	—	—	—	—	—	1,061	—	1,061
Other comprehensive loss, net of tax benefit of \$1,630	—	—	—	—	—	—	(6,134)	(6,134)
ESOP shares earned (1,984 shares)	—	8	—	22	—	—	—	30
Compensation plan shares granted (27,132 shares)	—	—	255	—	(255)	—	—	—
Compensation plan shares earned (2,749 shares)	—	16	—	—	26	—	—	42
Cash dividends declared (\$0.16 per share)	—	—	—	—	—	(312)	—	(312)
Balance - March 31, 2022	68	31,374	(13,405)	(1,172)	(386)	71,340	(5,156)	82,663
Net income	—	—	—	—	—	1,684	—	1,684
Other comprehensive loss, net of tax benefit of \$914	—	—	—	—	—	—	(3,437)	(3,437)
ESOP shares earned (1,984 shares)	—	7	—	21	—	—	—	28
Compensation plan shares forfeited (3,062 shares)	—	—	(29)	—	29	—	—	—
Compensation plan shares earned (4,942 shares)	—	29	—	—	45	—	—	74
Purchase of treasury stock, at cost (5,701 shares)	—	—	(85)	—	—	—	—	(85)
Cash dividends declared (\$0.16 per share)	—	—	—	—	—	(313)	—	(313)
Balance - June 30, 2022	68	31,410	(13,519)	(1,151)	(312)	72,711	(8,593)	80,614
Net income	—	—	—	—	—	1,771	—	1,771
Other comprehensive loss, net of tax benefit of \$1,051	—	—	—	—	—	—	(3,955)	(3,955)
ESOP shares earned (1,984 shares)	—	5	—	21	—	—	—	26
Compensation plan shares forfeited (3,192 shares)	—	—	(30)	—	30	—	—	—
Compensation plan shares earned (3,917 shares)	—	22	—	—	37	—	—	59
Cash dividends declared (\$0.18 per share)	—	—	—	—	—	(353)	—	(353)
Balance - September 30, 2022	68	31,437	(13,549)	(1,130)	(245)	74,129	(12,548)	78,162

	Common Stock	Additional Paid-In Capital	Treasury Stock	Unearned Shares Held by ESOP	Unearned Shares Held by Compensation Plans	Retained Earnings	Accumulated Other Comprehensiv e Loss	Total
	(Dollars in thousands, except share data)							
Balance - January 1, 2023	\$ 68	\$ 31,459	\$ (13,571)	\$ (1,108)	\$ (191)	\$ 74,859	\$ (10,332)	\$ 81,184
Cumulative change in accounting principle (Note 2)	—	—	—	—	—	(723)	—	(723)
Net Income	—	—	—	—	—	1,684	—	1,684
Other comprehensive income, net of tax expense of \$333	—	—	—	—	—	—	1,253	1,253
ESOP shares earned (1,984 shares)	—	1	—	21	—	—	—	22
Compensation plan shares granted (8,282 shares)	—	—	78	—	(78)	—	—	—
Compensation plan shares earned, net of forfeitures (2,510 shares)	—	(21)	—	—	(28)	—	—	(49)
Compensation plan shares forfeited (15,385 shares)	—	—	(144)	—	144	—	—	—
Common stock repurchased on vesting for payroll taxes (4,764 shares)	—	—	(56)	—	—	—	—	(56)
Balance - March 31, 2023	68	31,439	(13,693)	(1,087)	(153)	75,820	(9,079)	83,315
Net Income	—	—	—	—	—	816	—	816
Other comprehensive loss, net of tax benefit of \$209	—	—	—	—	—	—	(790)	(790)
ESOP shares earned (1,984 shares)	—	1	—	21	—	—	—	22
Compensation plan shares earned, net of forfeitures (2,328 shares)	—	9	—	—	22	—	—	31
Compensation plan shares forfeited (2,382 shares)	—	—	(22)	—	22	—	—	—
Balance - June 30, 2023	68	31,449	(13,715)	(1,066)	(109)	76,636	(9,869)	83,394
Net Income	—	—	—	—	—	1,571	—	1,571
Other comprehensive loss, net of tax benefit of \$843	—	—	—	—	—	—	(3,170)	(3,170)
ESOP shares earned (1,984 shares)	—	1	—	21	—	—	—	22
Compensation plan shares earned, net of forfeitures (2,933 shares)	—	12	—	—	28	—	—	40
Compensation plan shares forfeited (200 shares)	—	—	(2)	—	2	—	—	—
Balance - September 30, 2023	\$ 68	\$ 31,462	\$ (13,717)	\$ (1,045)	\$ (79)	\$ 78,207	\$ (13,039)	\$ 81,857

Lake Shore Bancorp, Inc. and Subsidiary
Consolidated Statements of Cash Flows

	Nine Months Ended September 30,	
	2023	2022
	(Unaudited)	
	(Dollars in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 4,071	\$ 4,516
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization of investment securities	42	73
Net amortization of deferred loan costs	392	323
(Credit) provision for credit losses	(1,011)	500
Recovery on previously impaired investment securities	(6)	(12)
Unrealized (gain) loss on equity securities	(5)	7
Loss on sale of investment securities	52	—
Unrealized loss (gain) on interest rate swap	58	(344)
Originations of loans held for sale	—	(1,309)
Proceeds from sales of loans held for sale	—	1,291
Loss on sale of loans held for sale	—	18
Depreciation and amortization	607	652
Increase in cash surrender value of bank-owned life insurance	(328)	(262)
ESOP shares committed to be released	66	84
Stock based compensation expense	22	175
Increase in accrued interest receivable	(93)	(104)
(Increase) decrease in other assets	(380)	635
Impairment of foreclosed real estate	16	9
Increase in other liabilities	1,122	99
Net Cash Provided by Operating Activities	<u>4,625</u>	<u>6,351</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Activity in debt securities:		
Sales	8,478	—
Maturities, prepayments and calls	3,107	6,495
Purchases	—	(6,141)
Purchases of Federal Home Loan Bank Stock	(1,314)	(157)
Redemptions of Federal Home Loan Bank Stock	1,297	—
Loan principal collections and origination, net	8,525	(45,003)
Proceeds from sale of interest rate swaps	214	—
Proceeds from sale of foreclosed real estate	—	143
Additions to premises and equipment	(364)	(298)
Net Cash Provided by (Used in) Investing Activities	<u>19,943</u>	<u>(44,961)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase (decrease) in deposits	14,039	(9,824)
Net decrease in advances from borrowers for taxes and insurance	(1,089)	(1,412)
Net decrease in short-term borrowings	(12,596)	—
Proceeds from issuance of long-term debt	15,250	5,000
Repayment of long-term debt	(3,750)	(2,000)
Purchase of treasury stock	(56)	(85)
Cash dividends paid	—	(978)
Net Cash Provided by (Used in) Financing Activities	<u>11,798</u>	<u>(9,299)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	<u>36,366</u>	<u>(47,909)</u>
CASH AND CASH EQUIVALENTS - BEGINNING	<u>9,633</u>	<u>67,585</u>
CASH AND CASH EQUIVALENTS - ENDING	<u>\$ 45,999</u>	<u>\$ 19,676</u>
SUPPLEMENTARY CASH FLOWS INFORMATION		
Interest paid	\$ 5,842	\$ 1,492
Income taxes paid	\$ 938	\$ 650
SUPPLEMENTARY SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES		
Foreclosed real estate acquired in settlement of loans	\$ 60	\$ 216

See notes to consolidated financial statements.

Lake Shore Bancorp, Inc. and Subsidiary
Notes to Unaudited Consolidated Financial Statements

Note 1 – Basis of Presentation

The interim unaudited consolidated financial statements include the accounts of Lake Shore Bancorp, Inc. (the “Company”, “us”, “our”, or “we”) and Lake Shore Savings Bank (the “Bank”), its wholly owned subsidiary. All intercompany accounts and transactions of the consolidated subsidiary have been eliminated in consolidation.

The interim unaudited consolidated financial statements included herein as of September 30, 2023 and for the three and nine months ended September 30, 2023 and 2022 have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission, and therefore, do not include all information or footnotes necessary for a complete presentation of the consolidated statements of financial condition, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America (“GAAP”). The consolidated statement of financial condition at December 31, 2022 has been derived from the audited consolidated financial statements at that date, but does not include all of the information and footnotes required by GAAP for complete consolidated financial statements. The consolidated financial statements reflect all adjustments that are, in the opinion of management, necessary for a fair statement of such information and to make the financial statements not misleading. These interim unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the audited consolidated financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2022. The consolidated statements of income for the three and nine months ended September 30, 2023 and 2022 are not necessarily indicative of the results for any subsequent period or the entire year ending December 31, 2023.

To prepare these unaudited consolidated financial statements in conformity with GAAP, management of the Company made a number of estimates and assumptions relating to the reporting of assets and liabilities and the reporting of revenue and expenses. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for credit losses, securities valuation estimates, evaluation of impairment of securities, and income taxes.

Subsequent Events

The Company has evaluated events and transactions occurring subsequent to the statement of financial condition date of September 30, 2023 for items that should potentially be recognized or disclosed in the unaudited consolidated financial statements. The evaluation was conducted through the date these unaudited consolidated financial statements were issued.

Note 2 – New Accounting Standards

Adoption of New Accounting Standards

On January 1, 2023, the Company adopted the Financial Accounting Standards Board (“FASB”) Accounting Standard Update (“ASU”) 2016-13, *“Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments”* (“ASU 2016-13”), as amended. ASU 2016-13 (also known as Accounting Standard Codification 326 or “ASC 326”) replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (“CECL”) methodology. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loans receivable. It also applies to certain off-balance sheet credit exposures, such as loan commitments and standby letters of credit. In addition, ASU 2016-13 updated the accounting for available for sale debt securities to require credit losses to be presented as an allowance rather than a write-down on available-for-sale debt securities that management does not intend to sell or believes that it is more likely than not they will be required to sell.

The Company utilized the modified retrospective method for all financial assets measured at amortized cost, specifically loans receivable and off-balance sheet credit exposures. Upon adoption, the Company recorded a decrease to retained earnings of \$723,000 for the cumulative effect of adopting ASC 326. The transaction adjustment included a \$282,000 impact to reflect the expected credit losses inherent within the Company’s loan portfolio for the life of the loan portfolio

and a \$633,000 impact to reflect the expected credit losses inherent with the Company's off-balance sheet credit exposures, offset by a \$192,000 deferred tax entry relating to the additional expected loss.

The Company adopted ASC 326 using the prospective transition appropriate for available-for-sale debt securities for which other-than-temporary impairment had been recognized prior to January 1, 2023. As a result, the amortized cost basis remains the same before and after the effective date of ASC 326. The effective interest rate on the debt securities was not changed. Recoveries of amounts previously written-off relating to improvements in cash flows after January 1, 2023 will be recorded in earnings as received.

Allowance for Credit Losses – Loans: The allowance for credit losses is a valuation account that is deducted from or added to the loans receivable amortized cost basis to present the net amount expected to be collected on the loans. Loans are charged off against the allowance for credit losses when management believes the uncollectibility of a loan balance is confirmed. Expected recoveries recorded in the allowance for credit loss account should not exceed the aggregate of amounts previously charged-off and expected to be charged-off.

Management estimates the allowance for credit losses balance using relevant available information, from internal and external sources, relating to past events, current conditions, and reasonable and supportable forecasts. Historical credit loss experience provides the basis for the estimation of expected credit losses. Adjustments to historical information are made for differences in current loan-specific risk characteristics such as differences in underwriting standards, portfolio mix, delinquency level, or term as well as for changes in environmental conditions, such as change in unemployment rates, property values or other relevant factors. Changes in the allowance for credit losses are recorded as a provision for (or reversal of) credit loss.

The Company uses the vintage model to estimate expected credit losses for all loan segments. The vintage model measures the expected loss calculation for future periods based on the historical performance by the origination period of loans with similar life cycles and risk characteristics. For each loan segment, the Company utilizes historical loss data through the current period to calculate the actual loss percentage for each loan type by vintage year of loan origination. The calculated loss percentages are then applied to the remaining outstanding balance for each vintage year, for the estimated remaining life of the loans in the loan segment. In addition to this calculation, the Company applies qualitative factors for current conditions, including trends in the nature and volume of the loan portfolio, loan concentrations, changes in the experience, ability and depth of the Company's lending management, and national and local economic conditions. In addition, the Company utilizes an economic forecast factor consisting of unemployment data and changes in gross domestic production (GDP) to determine the impact to the Bank's loan portfolio. No reversion adjustments were necessary for our calculation as the starting point for the Company's estimate was a cumulative loss rate covering the expected contractual term of the loan portfolio.

The allowance for credit losses is measured on a collective (pool) basis when similar risk characteristics exist. Loans that do not share risk characteristics are evaluated on an individual basis. Loans evaluated individually are not included in the collective evaluation. When management determines that foreclosure is probable, expected credit losses are based on the fair value of the collateral at the reporting date, adjusted for selling costs as appropriate.

Accrued interest on loans of \$2.5 million at September 30, 2023 is included in accrued interest receivable on the consolidated statements of financial condition and is excluded from the estimate of credit losses.

The Company's determination as to the amount of expected credit losses are subject to review by bank regulators, which can require the establishment of additional expected credit losses. Although the allowance for credit losses is allocated by loan type, the allowance for credit losses is general in nature and is available to offset losses from any loan in the Company's portfolio.

Allowance for Credit Losses – Off Balance Sheet Credit Exposure: The Company estimates expected credit losses over the contractual period in which the Company is exposed to credit risk via a contractual obligation to extend credit, unless the obligation is unconditionally cancellable by the Company. Off-balance sheet credit exposure includes loan commitments in which the Company has extended terms and all parties have accepted. The Company's commercial overdraft line of credit and consumer overdraft line of credit products are unconditionally cancellable by the Company and therefore, the Company does not record an allowance for credit losses on these loan types. The allowance for credit losses for off balance

sheet credit exposure is derived through the use of the vintage model and a utilization rate concept, applied to those commitments which are not unconditionally cancellable. Changes in the allowance for credit losses are recorded as a provision for (or reversal of) credit loss.

Allowance for Credit Losses – Available-for-Sale Securities: For available-for-sale debt securities in an unrealized loss position, the Company first assesses whether it intends to sell, or if it is more likely than not that it will be required to sell the security before the recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security's amortized cost basis is written down to fair value through income. For available-for-sale debt securities that do not meet the aforementioned criteria, the Company will evaluate whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency, and adverse conditions specifically related to the security, among other factors. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected from the security are compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis, any excess cost is recorded as an allowance for credit losses. Any impairment that has not been recorded through an allowance for credit losses is recognized in other comprehensive income. The Company elected the practical expedient of zero loss estimates for securities issued by U.S. government entities and agencies. These securities are either explicitly or implicitly guaranteed by the U.S. government, are highly rated by major agencies and have a long history of no losses.

Changes in the allowance for credit losses are recorded as a provision for (or reversal of) credit loss. Losses are charged against the allowance when management believes the uncollectibility of an available-for-sale debt security is confirmed or when either of the criteria regarding intent or requirement to sell is met.

Accrued interest of \$358,000 as of September 30, 2023 on available-for-sale debt securities is included in accrued interest receivable on the consolidated statements of financial condition and is excluded from the estimate of credit losses.

In March 2022, the FASB issued ASU No. 2022-02, "*Financial Instruments – Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures*." This ASU eliminates the separate recognition and measurement guidance for Troubled Debt Restructurings ("TDRs") by creditors. The amendments in this update require the Company to apply the general loan modification guidance in Subtopic 310-20 to all loan modifications, including modifications for borrowers experiencing financial difficulty. The Company must evaluate whether the modification represents a new loan or a continuation of an existing loan. ASU 2022-02 may be adopted prospectively for loan modifications after adoption or on a modified retrospective basis, which would apply to loans previously modified, resulting in a cumulative effect adjustment to retained earnings in the period of adoption for changes in the allowance for credit losses. On January 1, 2023, the Company adopted ASU 2022-02 utilizing the prospective method, which did not have a material impact on its unaudited consolidated financial statements. The adoption of ASU-2022-02 required the Company to enhance the vintage disclosures to include gross charge-off by year of origination.

Note 3 – Investment Securities

The amortized cost and fair value of securities are as follows:

September 30, 2023				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(Dollars in thousands)				
SECURITIES				
<i>Debt Securities Available for Sale</i>				
U.S. government agencies	\$ 2,007	\$ —	\$ (234)	\$ 1,773
Municipal bonds	42,086	—	(10,939)	31,147
Mortgage-backed securities:				
Collateralized mortgage obligations-private label	10	—	(1)	9
Collateralized mortgage obligations-government sponsored entities	12,290	—	(1,787)	10,503
Government National Mortgage Association	58	—	(5)	53
Federal National Mortgage Association	12,125	—	(2,385)	9,740
Federal Home Loan Mortgage Corporation	5,865	—	(1,246)	4,619
Asset-backed securities-private label	—	92	—	92
Asset-backed securities-government sponsored entities	3	—	—	3
<i>Total Debt Securities Available for Sale</i>	<u>\$ 74,444</u>	<u>\$ 92</u>	<u>\$ (16,597)</u>	<u>\$ 57,939</u>
<i>Equity Securities</i>	22	—	(9)	13
Total Securities	<u><u>\$ 74,466</u></u>	<u><u>\$ 92</u></u>	<u><u>\$ (16,606)</u></u>	<u><u>\$ 57,952</u></u>

December 31, 2022				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(Dollars in thousands)				
SECURITIES				
<i>Debt Securities Available for Sale</i>				
U.S. government agencies	\$ 2,008	\$ —	\$ (175)	\$ 1,833
Municipal bonds	50,734	16	(8,336)	42,414
Mortgage-backed securities:				
Collateralized mortgage obligations-private label	12	—	(1)	11
Collateralized mortgage obligations-government sponsored entities	13,790	1	(1,636)	12,155
Government National Mortgage Association	61	—	(2)	59
Federal National Mortgage Association	13,232	1	(1,987)	11,246
Federal Home Loan Mortgage Corporation	6,277	—	(1,056)	5,221
Asset-backed securities-private label	—	96	—	96
Asset-backed securities-government sponsored entities	4	—	—	4
<i>Total Debt Securities Available for Sale</i>	<u>\$ 86,118</u>	<u>\$ 114</u>	<u>\$ (13,193)</u>	<u>\$ 73,039</u>
<i>Equity Securities</i>	22	—	(14)	8
Total Securities	<u><u>\$ 86,140</u></u>	<u><u>\$ 114</u></u>	<u><u>\$ (13,207)</u></u>	<u><u>\$ 73,047</u></u>

Debt Securities

All of the Company's collateralized mortgage obligations are backed by one- to four-family residential mortgages.

At September 30, 2023, no securities were pledged as collateral to the Federal Reserve Bank ("FRB"), and at December 31, 2022, thirty-eight municipal bonds with a cost of \$14.4 million and fair value of \$12.2 million were pledged under a collateral agreement with the FRB of New York for liquidity borrowing. In addition, at September 30, 2023 and December 31, 2022, twenty-four and twenty-two municipal bonds with a cost of \$6.9 million and \$6.6 million and fair value of \$4.8 million and \$5.6 million, respectively, were pledged as collateral for customer deposits in excess of the Federal Deposit Insurance Corporation ("FDIC") insurance limits.

The following table sets forth the Company's investment in securities with gross unrealized losses of less than twelve months and gross unrealized losses of twelve months or more and associated fair values for which an allowance for credit losses has not been recorded for the periods indicated:

	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
(Dollars in thousands)						
September 30, 2023						
U.S. government agencies	\$ —	\$ —	\$ 1,773	\$ (234)	\$ 1,773	\$ (234)
Municipal bonds	2,162	(300)	28,784	(10,639)	30,946	(10,939)
Mortgage-backed securities	162	(8)	24,751	(5,416)	24,913	(5,424)
	<u>\$ 2,324</u>	<u>\$ (308)</u>	<u>\$ 55,308</u>	<u>\$ (16,289)</u>	<u>\$ 57,632</u>	<u>\$ (16,597)</u>
December 31, 2022						
U.S. government agencies	\$ 1,833	\$ (175)	\$ —	\$ —	\$ 1,833	\$ (175)
Municipal bonds	12,227	(1,114)	23,259	(7,222)	35,486	(8,336)
Mortgage-backed securities	6,981	(410)	21,561	(4,272)	28,542	(4,682)
	<u>\$ 21,041</u>	<u>\$ (1,699)</u>	<u>\$ 44,820</u>	<u>\$ (11,494)</u>	<u>\$ 65,861</u>	<u>\$ (13,193)</u>

As of September 30, 2023, the Company determined that no individual securities in an unrealized loss position represented credit losses that would require an allowance for credit losses. The Company concluded that the unrealized losses were primarily attributed to increases in market interest rates since these securities were purchased and other market conditions.

As of September 30, 2023, the Company's investment portfolio included 18 securities in the "unrealized losses less than twelve months" category and 167 securities in the "unrealized losses twelve months or more" category.

As of December 31, 2022, the Company had the intent and ability to hold those securities in an unrealized loss position until maturity. Management believed the temporary impairments were due to declines in fair value resulting from changes in interest rates and/or increased credit liquidity spreads since the securities were purchased.

Therefore, under the accounting principles effective at December 31, 2022, the Company did not consider these securities to have other-than-temporary impairment.

The unrealized losses on debt securities shown in the previous tables were recorded as a component of other comprehensive loss, net of tax benefit on the Company's consolidated statements of stockholders' equity.

During the nine months ended September 30, 2023, the Company sold 35 municipal bonds and 2 mortgage-backed securities resulting in gross realized losses of \$52,000, with an amortized cost of \$8.4 million. During the three months ended September 30, 2023, the Company sold 12 municipal bonds resulting in gross realized losses of \$3,000, with an amortized cost of \$2.5 million. During the three and nine months ended September 30, 2022, the Company did not sell any debt securities.

Scheduled contractual maturities of debt securities are as follows:

	Amortized Cost	Fair Value
	(Dollars in thousands)	
September 30, 2023:		
Less than one year	\$ 230	\$ 228
After one year through five years	2,616	2,398
After five years through ten years	9,353	7,836
After ten years	31,894	22,458
Mortgage-backed securities	30,348	24,924
Asset-backed securities	3	95
	<u>\$ 74,444</u>	<u>\$ 57,939</u>

The Company's mortgage-backed securities and asset-backed securities have stated maturities that may differ from actual maturities due to the borrowers' ability to prepay obligations. Cash flows from such investments are dependent upon the performance of the underlying assets and are generally influenced by interest rates. In the table above, mortgage-backed securities and asset-backed securities are shown in one period.

Equity Securities

At September 30, 2023 and December 31, 2022, equity securities consisted of 22,368 shares of Federal Home Loan Mortgage Corporation ("FHLMC") common stock. During the three months ended September 30, 2023 and 2022, the Company recognized an unrealized gain of \$3,000 and \$2,000, respectively, on the equity securities, which was recorded in non-interest income in the consolidated statements of income. During the nine months ended September 30, 2023 and 2022, the Company recognized an unrealized gain of \$5,000 and an unrealized loss of \$7,000, respectively, on the equity securities, which was recorded in non-interest income in the consolidated statements of income. There were no sales of equity securities during the three and nine months ended September 30, 2023 and 2022.

Note 4 - Loans and Allowance for Credit Losses

Loans consisted of the following segments as of September 30, 2023 and December 31, 2022:

	September 30, 2023	December 31, 2022
	(Dollars in thousands)	
Real Estate Loans:		
Residential, one- to four-family ⁽¹⁾	\$ 172,974	\$ 175,904
Home Equity	51,276	53,057
Commercial ⁽²⁾	323,535	326,955
Total real estate loans	547,785	555,916
Other Loans:		
Commercial	18,749	19,576
Consumer	1,113	1,217
Total gross loans	567,647	576,709
Net deferred loan costs	3,843	3,893
Allowance for credit losses on loans	(6,642)	(7,065)
Loans receivable, net	\$ 564,848	\$ 573,537

⁽¹⁾ Includes one- to four-family construction loans.

⁽²⁾ Includes commercial construction loans.

Real estate loans of approximately \$57.4 million and \$147.4 million were pledged as collateral for Federal Home Loan Bank (FHLB) advances as of September 30, 2023 and December 31, 2022, respectively.

Loans are stated at the principal amounts outstanding, net of unamortized loan fees and costs, with interest income recognized on the interest method based upon the terms of the loan. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method. Loans are reported by the portfolio segments identified above and are analyzed by management on this basis. All loan policies identified below apply to all segments of the loan portfolio.

Allowance for Credit Losses for Loans

The Company adopted ASU 2016-13 on January 1, 2023 at which time the Company implemented the current expected credit loss model in estimating the allowance for credit losses valuation account. Adjustments to the allowance for credit losses on loans is recognized in (credit) provision for credit losses on the unaudited consolidated statements of income. As part of the CECL calculation, the loan portfolio is segmented into the following loan types by risk level:

Real Estate Loans:

- One- to Four-Family – are loans secured by first lien collateral on residential real estate primarily held in the Western New York region. These loans can be affected by economic conditions and the value of underlying properties. Western New York’s housing market has consistently demonstrated stability in home prices despite economic conditions. Furthermore, the Company has conservative underwriting standards and its residential lending policies and procedures verify that its one- to four-family residential mortgage loans generally conform to secondary market guidelines.
- Home Equity - are loans or lines of credit secured by first or second liens on owner-occupied residential real estate primarily held in the Western New York region. These loans can also be affected by economic conditions and the values of underlying properties. Home equity loans may have increased risk of loss if the Company does not hold the first mortgage resulting in the Company being in a secondary position in the event of collateral liquidation. The Company does not originate interest only home equity loans.
- Commercial Real Estate – are loans used to finance the purchase of real property, which generally consists of developed real estate that is held as first lien collateral for the loan. These loans are secured by real estate properties that are primarily held in the Western New York region. Commercial real estate lending involves additional risks compared with one- to four-family residential lending, because payments on loans secured by commercial real estate properties are often dependent on the successful operation or management of the properties, and/or the collateral value of the commercial real estate securing the loan, and repayment of such loans may be subject to adverse conditions in the real estate market or economic conditions to a greater extent than one- to four-family residential mortgage loans. Also, commercial real estate loans typically involve relatively large loan balances concentrated with single borrowers or groups of related borrowers.

Other Loans:

- Commercial – includes business installment loans, lines of credit, and other commercial loans. Most of our commercial loans are for terms generally not in excess of 5 years. Whenever possible, we collateralize these loans with a lien on business assets and equipment and require the personal guarantees from principals of the borrower. Commercial loans generally involve a higher degree of credit risk, as commercial loans can involve relatively large loan balances to a single borrower or groups of related borrowers, with the repayment of such loans typically dependent on the successful operation of the commercial business and the income stream of the borrower. Such risks can be significantly affected by economic conditions. Although commercial loans may be collateralized by equipment or other business assets, the liquidation of collateral in the event of a borrower default may be an insufficient source of repayment because the equipment or other business assets may be obsolete or of limited use, among other things. Accordingly, the repayment of a commercial loan depends primarily on the credit worthiness of the borrowers (and any guarantors), while liquidation of collateral is a secondary and often insufficient source of repayment.
- Consumer – consist of loans secured by collateral such as an automobile or a deposit account, unsecured loans and lines of credit. Consumer loans tend to have a higher credit risk due to the loans being either unsecured or secured by rapidly depreciable assets. Furthermore, consumer loan payments are dependent on the borrower’s continuing financial stability, and therefore are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy.

Included in the Real Estate Loans for one-to four-family and commercial real estate are loans to finance the construction of either a one- to four-family owner occupied home or commercial real estate. At the end of the construction period, the loan automatically converts to either a one- to four-family residential mortgage or a commercial real estate mortgage, as applicable. Risk of loss on a construction loan depends largely upon the accuracy of the initial estimate of the value of the property at completion compared to the actual cost of construction. The Company limits its risk during construction as disbursements are not made until the required work for each advance has been completed and an updated lien search is performed. The completion of the construction progress is verified by a Company loan officer or inspections performed by an independent appraisal firm or other third party. Construction loans also expose us to the risk of construction delays which may impair the borrower's ability to repay the loan.

The following table details the changes in the allowance for credit losses by loan segment for the three and nine months ended September 30, 2023.

	Real Estate Loans			Other Loans			
	One- to Four-Family ⁽¹⁾	Home Equity	Commercial Real Estate ⁽²⁾	Commercial	Consumer	Unallocated	Total
	(Dollars in thousands)						
September 30, 2023							
Allowance for Credit Loss: on Loans							
Balance – July 1, 2023	\$ 541	\$ 257	\$ 5,422	\$ 520	\$ 18	\$ —	\$ 6,758
Charge-offs	—	—	—	—	(16)	—	(16)
Recoveries	—	—	35	—	2	—	37
(Credit) provision	(6)	(47)	(122)	25	13	—	(137)
Balance – September 30, 2023	<u>\$ 535</u>	<u>\$ 210</u>	<u>\$ 5,335</u>	<u>\$ 545</u>	<u>\$ 17</u>	<u>\$ —</u>	<u>\$ 6,642</u>
Balance - January 1, 2023	\$ 411	\$ 217	\$ 5,746	\$ 509	\$ 47	\$ 135	\$ 7,065
Impact of adopting ASC 326	201	114	55	72	(25)	(135)	282
Charge-offs	—	—	—	—	(47)	—	(47)
Recoveries	—	—	35	29	7	—	71
(Credit) provision	(77)	(121)	(501)	(65)	35	—	(729)
Balance – September 30, 2023	<u>\$ 535</u>	<u>\$ 210</u>	<u>\$ 5,335</u>	<u>\$ 545</u>	<u>\$ 17</u>	<u>\$ —</u>	<u>\$ 6,642</u>
Ending balance: individually evaluated for impairment	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>
Ending balance: collectively evaluated for impairment	<u>\$ 535</u>	<u>\$ 210</u>	<u>\$ 5,335</u>	<u>\$ 545</u>	<u>\$ 17</u>	<u>\$ —</u>	<u>\$ 6,642</u>
Gross Loans Receivable⁽³⁾:							
Ending balance	<u>\$ 172,974</u>	<u>\$ 51,276</u>	<u>\$ 323,535</u>	<u>\$ 18,749</u>	<u>\$ 1,113</u>	<u>\$ —</u>	<u>\$ 567,647</u>
Ending balance: individually evaluated for impairment	<u>\$ 142</u>	<u>\$ —</u>	<u>\$ 1,242</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 1,384</u>
Ending balance: collectively evaluated for impairment	<u>\$ 172,832</u>	<u>\$ 51,276</u>	<u>\$ 322,293</u>	<u>\$ 18,749</u>	<u>\$ 1,113</u>	<u>\$ —</u>	<u>\$ 566,263</u>

(1) Includes one- to four-family construction loans.

(2) Includes commercial construction loans of \$23.9 million.

(3) Gross Loans Receivable does not include allowance for credit losses of \$(6,642) or deferred loan costs of \$3,843.

Prior to the adoption of ASC 326 on January 1, 2023, the Company calculated the allowance for loan losses using the incurred loss methodology. The following tables summarize the activity in the allowance for loan losses for the three and nine months ended September 30, 2022 and the distribution of the allowance for loan losses and loans receivable by loan portfolio class and impairment method as of September 30, 2022 and December 31, 2022:

	Real Estate Loans				Other Loans				Total
	One- to Four-Family ⁽²⁾	Home Equity	Commercial	Construction - Commercial	Commercial	Consumer	Unallocated		
(Dollars in thousands)									
September 30, 2022									
Allowance for Loan Losses:									
Balance – July 1, 2022	\$ 449	\$ 330	\$ 4,908	\$ 373	\$ 479	\$ 24	\$ 184	\$ 6,747	
Charge-offs	—	—	-	—	—	(17)	—	(17)	
Recoveries	-	—	115	—	—	4	—	119	
Provision (credit)	17	(62)	35	10	(1)	23	(22)	-	
Balance – September 30, 2022	<u>\$ 466</u>	<u>\$ 268</u>	<u>\$ 5,058</u>	<u>\$ 383</u>	<u>\$ 478</u>	<u>\$ 34</u>	<u>\$ 162</u>	<u>\$ 6,849</u>	
Balance – January 1, 2022	\$ 383	\$ 211	\$ 4,377	\$ 360	\$ 531	\$ 32	\$ 224	\$ 6,118	
Charge-offs	—	—	(4)	—	—	(58)	—	(62)	
Recoveries	17	1	269	—	—	6	—	293	
Provision (credit)	66	56	416	23	(53)	54	(62)	500	
Balance – September 30, 2022	<u>\$ 466</u>	<u>\$ 268</u>	<u>\$ 5,058</u>	<u>\$ 383</u>	<u>\$ 478</u>	<u>\$ 34</u>	<u>\$ 162</u>	<u>\$ 6,849</u>	
Ending balance: individually evaluated for impairment	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	
Ending balance: collectively evaluated for impairment	<u>\$ 466</u>	<u>\$ 268</u>	<u>\$ 5,058</u>	<u>\$ 383</u>	<u>\$ 478</u>	<u>\$ 34</u>	<u>\$ 162</u>	<u>\$ 6,849</u>	
Gross Loans Receivable⁽¹⁾:									
Ending balance	<u>\$ 171,570</u>	<u>\$ 50,633</u>	<u>\$ 295,582</u>	<u>\$ 23,241</u>	<u>\$ 21,950</u>	<u>\$ 1,171</u>	<u>\$ —</u>	<u>\$ 564,147</u>	
Ending balance: individually evaluated for impairment	<u>\$ 216</u>	<u>\$ 14</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 230</u>	
Ending balance: collectively evaluated for impairment	<u>\$ 171,354</u>	<u>\$ 50,619</u>	<u>\$ 295,582</u>	<u>\$ 23,241</u>	<u>\$ 21,950</u>	<u>\$ 1,171</u>	<u>\$ —</u>	<u>\$ 563,917</u>	

(1) Gross Loans Receivable does not include allowance for loan losses of \$(6,849) or deferred loan costs of \$3,872.

(2) Includes one- to four- family construction loans.

	Real Estate Loans				Other Loans			Total
	One- to Four-Family ⁽²⁾	Home Equity	Commercial	Commercial - Construction	Commercial	Consumer	Unallocated	
(Dollars in thousands)								
December 31, 2022								
Allowance for Loan Losses:								
Balance – December 31, 2022	\$ 411	\$ 217	\$ 5,398	\$ 348	\$ 509	\$ 47	\$ 135	\$ 7,065
Ending balance: individually evaluated for impairment	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Ending balance: collectively evaluated for impairment	\$ 411	\$ 217	\$ 5,398	\$ 348	\$ 509	\$ 47	\$ 135	\$ 7,065
Gross Loans Receivable ⁽¹⁾ :								
Ending Balance	\$ 175,904	\$ 53,057	\$ 304,037	\$ 22,918	\$ 19,576	\$ 1,217	\$ —	\$ 576,709
Ending balance: individually evaluated for impairment	\$ 153	\$ 14	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 167
Ending balance: collectively evaluated for impairment	\$ 175,751	\$ 53,043	\$ 304,037	\$ 22,918	\$ 19,576	\$ 1,217	\$ —	\$ 576,542

(1) Gross Loans Receivable does not include allowance for loan losses of \$(7,065) or deferred loan costs of \$3,893.

(2) Includes one- to four-family construction loans.

Unfunded Loan Commitments

The Company's allowance for credit losses on unfunded loan commitments is recognized as a liability and included within other liabilities on the unaudited consolidated statement of financial condition, with adjustments to the reserve recognized in (credit) provision for credit losses on the unaudited consolidated statements of income. The Company did not record an allowance on unfunded loan commitments prior to January 1, 2023. The Company's activity in the allowance for credit losses on unfunded loan commitments for the three and nine months ended September 30, 2023 was as follows:

	For the Three and Nine Months Ended September 30, 2023
	(Dollars in thousands)
Balance at December 31, 2022	\$ —
Impact of CECL Adoption	633
Balance at March 31, 2023	633
Provision for Credit Losses	(220)
Balance at June 30, 2023	413
Provision for Credit Losses	(62)
Balance at September 30, 2023	\$ 351

Non-accrual Loans and Delinquency Status

The following table presents the amortized cost basis of loans on non-accrual status, loans on non-accrual status with no allowance for credit losses recorded and loans past due 90 days or more and still accruing by loan segment as of the periods indicated.

	Total Non-accrual		Non-accrual with no Allowance for Credit Losses		90 Days or More Past Due and Accruing	
	September 30, 2023	December 31, 2022	September 30, 2023	December 31, 2022	September 30, 2023	December 31, 2022
	(Dollars in thousands)					
Real Estate Loans:						
Residential, one- to four-family ⁽¹⁾	\$ 2,004	\$ 2,295	\$ 2,004	\$ 2,295	\$ —	\$ 1
Home Equity	319	602	319	602	—	—
Commercial Real Estate ⁽²⁾	1,226	—	1,226	—	—	—
Other Loans:						
Commercial	—	—	—	—	—	—
Consumer	8	34	8	34	—	—
Total loans	\$ 3,557	\$ 2,931	\$ 3,557	\$ 2,931	\$ —	\$ 1

⁽¹⁾ Includes one- to four-family construction loans.

⁽²⁾ Includes commercial construction loans.

There was no interest income recognized on non-accrual loans during the three and nine months ended September 30, 2023 and there was \$4,000 of interest income recognized during the three and nine months ended September 30, 2022, respectively. The accrual of interest on loans is discontinued when in management's opinion, the borrower may be unable to meet payments as they become due. A loan does not have to be 90 days delinquent in order to be classified as non-accrual. When interest accrual is discontinued, all unpaid accrued interest is reversed. If ultimate collection of principal is in doubt, all cash receipts on non-accrual loans are applied to reduce the principal balance.

The following tables provide an analysis of past due loans as of the dates indicated:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current Due	Total Loans Receivable
(Dollars in thousands)						
September 30, 2023:						
Real Estate Loans:						
Residential, one- to four-family ⁽¹⁾	\$ 1,103	\$ 123	\$ 538	\$ 1,764	\$ 171,210	\$ 172,974
Home equity	45	68	107	220	51,056	51,276
Commercial ⁽²⁾	203	1,039	—	1,242	322,293	323,535
Other Loans:						
Commercial	117	—	—	117	18,632	18,749
Consumer	—	2	5	7	1,106	1,113
Total	<u>\$ 1,468</u>	<u>\$ 1,232</u>	<u>\$ 650</u>	<u>\$ 3,350</u>	<u>\$ 564,297</u>	<u>\$ 567,647</u>
	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current Due	Total Loans Receivable
(Dollars in thousands)						

December 31, 2022:

Real Estate Loans:						
Residential, one- to four-family ⁽¹⁾	\$ 1,173	\$ 380	\$ 1,649	\$ 3,202	\$ 172,702	\$ 175,904
Home equity	137	287	468	892	52,165	53,057
Commercial ⁽²⁾	—	—	—	—	326,955	326,955
Other Loans:						
Commercial	—	—	—	—	19,576	19,576
Consumer	15	—	17	32	1,185	1,217
Total	<u>\$ 1,325</u>	<u>\$ 667</u>	<u>\$ 2,134</u>	<u>\$ 4,126</u>	<u>\$ 572,583</u>	<u>\$ 576,709</u>

⁽¹⁾ Includes one- to four-family construction loans.

⁽²⁾ Includes commercial real estate construction loans.

Collateral-Dependent Loans

Collateral-dependent loans are loans for which the repayment is expected to be provided substantially through the operation or sale of the collateral and the borrower is experiencing financial difficulty. These loans do not share common risk characteristics and are not included within the collectively evaluated loans for determining the allowance for credit losses. Under CECL, for collateral-dependent loans, the Company has adopted the practical expedient to measure the allowance for credit losses based on the fair value of collateral. The allowance for credit losses is measured on an individual loan basis based on the difference between the fair value of the loan's collateral, which is adjusted for liquidation costs, and the amortized cost. If the fair value of the collateral exceeds the amortized cost, no allowance for credit losses is required. Refer to Note 8 - Fair Value of Financial Instruments for additional information.

The following table presents an analysis of the amortized cost of collateral-dependent loans of the Company as of September 30, 2023 by collateral type and loan segment:

	Residential Properties	Business Assets	Land	Commercial Property	Other	Total Loans
(Dollars in thousands)						
Real Estate Loans:						
Residential, one- to four-family	\$ 145	\$ —	\$ —	\$ —	\$ —	\$ 145
Home Equity	—	—	—	—	—	—
Commercial	200	—	1,026	—	—	1,226
Total	<u>\$ 345</u>	<u>\$ —</u>	<u>\$ 1,026</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 1,371</u>

There was no allowance recorded on the above noted collateral-dependent loans as of September 30, 2023.

Pre-Adoption of ASC 326 – Impaired Loans

For periods prior to the adoption of ASC 326, a loan was considered impaired when, based on current information and events, it was probable that the Company would not be able to collect the scheduled payments of principal and interest when due according to the contractual terms of the loan agreement. Factors considered in determining impairment include payment status, collateral value and the probability of collecting scheduled payments when due. Impairment was measured on a loan-by-loan basis for commercial real estate loans and commercial loans. Larger groups of smaller balance homogeneous loans were collectively evaluated for impairment. Accordingly, the Company did not separately identify individual consumer, home equity, or one- to four-family loans for impairment disclosure, unless they were subject to a troubled debt restructuring.

The following is a summary of information pertaining to impaired loans at or for the periods indicated:

	Recorded Investment	Unpaid Principal Balance	Related Allowance
At December 31, 2022			
(Dollars in thousands)			
With no related allowance recorded:			
Residential, one- to four-family	\$ 153	\$ 153	\$ —
Home equity	14	14	—
Commercial real estate ⁽¹⁾	—	—	—
Total impaired loans with no related allowance	167	167	—
		Average Recorded Investment	Interest Income Recognized
		For the Nine Months Ended September 30, 2022	
With no related allowance recorded:			
Residential, one- to four-family	\$	252	\$ 9
Home equity		22	—
Commercial real estate ⁽²⁾		3,262	—
Total impaired loans	\$	3,536	\$ 9

⁽¹⁾ Commercial Real Estate loans consisted of one loan which was paid off during the year ended December 31, 2022.

⁽²⁾ Average Commercial Real Estate loans consisted of one loan which was paid off during the nine months ended September 30, 2022.

Credit Quality Indicators

The Company's policies provide for the classification of loans as follows:

- Pass/Performing;
- Special Mention – does not currently expose the Company to a sufficient degree of risk but does possess credit deficiencies or potential weaknesses deserving the Company's close attention;
- Substandard – has one or more well-defined weaknesses and are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. A substandard asset would be one inadequately protected by the current net worth and paying capacity of the obligor or pledged collateral, if applicable;
- Doubtful – has all the weaknesses inherent in substandard loans with the additional characteristic that the weaknesses present make collection or liquidation in full on the basis of currently existing facts, conditions and values questionable, and there is a high possibility of loss; and
- Loss – loan is considered uncollectible and continuance without the establishment of a specific valuation reserve is not warranted.

Each commercial loan is individually assigned a loan classification. The Company's consumer loans, including residential one- to four-family loans and home equity loans, are classified by using the delinquency status as the basis for classifying

these loans. Generally, all consumer loans more than 90 days past due are classified and placed in non-accrual. Such loans that are well-secured and in the process of collection will remain in accrual status.

Asset quality indicators for all loans and the Company's risk rating process are reviewed on a monthly basis. Risk ratings are updated as circumstances that could affect the repayment of individual loans are brought to management's attention through an established monitoring process. Written action plans are maintained and reviewed on a quarterly basis for all classified commercial loans. In addition to the Company's internal process, an outsourced independent credit review function is in place for commercial loans to further assess assigned risk classifications and monitor compliance with internal lending policies and procedures.

The following table presents loans by credit quality indicator by origination year at September 30, 2023:

	YTD 2023	2022	2021	2020	2019	Prior	Revolving Loans	Total
(Dollars in thousands)								
Residential, one-to four-family⁽¹⁾:								
Pass	\$ 9,050	\$ 36,486	\$ 30,209	\$ 18,234	\$ 10,245	\$ 66,389	\$ —	\$ 170,613
Substandard	—	266	40	94	275	1,686	—	2,361
Doubtful	—	—	—	—	—	—	—	—
Total	<u>\$ 9,050</u>	<u>\$ 36,752</u>	<u>\$ 30,249</u>	<u>\$ 18,328</u>	<u>\$ 10,520</u>	<u>\$ 68,075</u>	<u>\$ —</u>	<u>\$ 172,974</u>
Current period gross chargeoffs	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>
Home Equity:								
Pass	\$ 3,492	\$ 3,212	\$ 109	\$ 50	\$ 301	\$ 532	\$ 43,174	\$ 50,870
Substandard	—	—	—	—	—	—	406	406
Doubtful	—	—	—	—	—	—	—	—
Total	<u>\$ 3,492</u>	<u>\$ 3,212</u>	<u>\$ 109</u>	<u>\$ 50</u>	<u>\$ 301</u>	<u>\$ 532</u>	<u>\$ 43,580</u>	<u>\$ 51,276</u>
Current period gross chargeoffs	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>
Commercial Real Estate⁽²⁾:								
Pass	\$ 13,995	\$ 85,751	\$ 54,080	\$ 42,579	\$ 39,196	\$ 75,789	\$ —	\$ 311,390
Special mention	—	—	—	989	689	—	—	1,678
Substandard	—	—	—	1,242	5,439	3,786	—	10,467
Doubtful	—	—	—	—	—	—	—	—
Total	<u>\$ 13,995</u>	<u>\$ 85,751</u>	<u>\$ 54,080</u>	<u>\$ 44,810</u>	<u>\$ 45,324</u>	<u>\$ 79,575</u>	<u>\$ —</u>	<u>\$ 323,535</u>
Current period gross chargeoffs	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>
Commercial Loans:								
Pass	\$ 1,223	\$ 2,571	\$ 800	\$ 665	\$ 1,965	\$ 7,108	\$ —	\$ 14,332
Special mention	—	—	287	—	790	—	—	1,077
Substandard	—	—	—	—	3,015	325	—	3,340
Doubtful	—	—	—	—	—	—	—	—
Total	<u>\$ 1,223</u>	<u>\$ 2,571</u>	<u>\$ 1,087</u>	<u>\$ 665</u>	<u>\$ 5,770</u>	<u>\$ 7,433</u>	<u>\$ —</u>	<u>\$ 18,749</u>
Current period gross chargeoffs	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>
Consumer Loans:								
Pass	\$ 218	\$ 280	\$ 89	\$ 152	\$ 3	\$ 133	\$ 205	\$ 1,080
Substandard	—	—	3	1	—	—	29	33
Doubtful	—	—	—	—	—	—	—	—
Total	<u>\$ 218</u>	<u>\$ 280</u>	<u>\$ 92</u>	<u>\$ 153</u>	<u>\$ 3</u>	<u>\$ 133</u>	<u>\$ 234</u>	<u>\$ 1,113</u>
Current period gross chargeoffs	<u>\$ —</u>	<u>\$ 8</u>	<u>\$ 3</u>	<u>\$ 3</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 33</u>	<u>\$ 47</u>

(1) Includes one- to four-family construction loans.

(2) Includes commercial construction loans.

The following table presents loans by credit quality indicator at December 31, 2022:

	<u>Pass/Performing</u>	<u>Special Mention</u>	<u>Substandard</u>	<u>Doubtful</u>	<u>Loss</u>	<u>Total</u>
	(Dollars in thousands)					
<u>December 31, 2022</u>						
Real Estate Loans:						
Residential, one- to four-family ⁽¹⁾	\$ 173,857	\$ —	\$ 2,047	\$ —	\$ —	\$ 175,904
Home equity	52,269	—	788	—	—	53,057
Commercial ⁽²⁾	314,218	3,272	9,465	—	—	326,955
Other Loans:						
Commercial	14,926	1,112	3,538	—	—	19,576
Consumer	1,183	—	24	—	10	1,217
Total	\$ 556,453	\$ 4,384	\$ 15,862	\$ —	\$ 10	\$ 576,709

⁽¹⁾ Includes one- to four- family construction loans.

⁽²⁾ Includes commercial construction loans.

Modifications with Borrowers Experiencing Financial Difficulty:

Occasionally, the Company modifies loans to borrowers in financial distress by providing modifications to loans that it would not normally grant. Such modifications could include principal forgiveness, term extension, a significant payment delay, an interest rate reduction or the addition of a co-borrower or guarantor. When principal forgiveness is provided, the amount of the forgiveness is charged-off against the allowance for credit losses.

Because the effect of most modifications made to borrowers experiencing financial difficulty is already included in the allowance for credit losses, a change to the allowance for credit losses is generally not recorded upon modification.

In some cases, the Company provides multiple types of modifications on one loan. Typically, one type of concession, such as a term extension, is granted initially. If the borrower continues to experience financial difficulty, another modification may be granted, such as principal forgiveness.

The following table presents the amortized cost basis of loans at September 30, 2023 that were experiencing financial difficulty and were modified during the three and nine months ended September 30, 2023, by loan class and by type of modification. The percentage of the amortized cost basis of loans that were modified to borrowers in financial distress as compared to the amortized cost basis of each class of financing receivables is also presented.

	<u>Principal Forgiveness</u>	<u>Payment Delay</u>	<u>Term Extension</u>	<u>Interest Rate Reduction</u>	<u>Add Co- Borrower/ Guarantor</u>	<u>Combination Term Extension and Add Co- Borrower</u>	<u>Percentage of Total Class of Financing Receivable</u>
	(Dollars in thousands)						
Real Estate Loans							
Commercial real estate	\$ —	\$ —	\$ —	\$ —	\$ 4,935	\$ —	1.53 %
Other loans							
Commercial	—	—	—	—	—	1,114	5.94 %
Total	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 4,935</u>	<u>\$ 1,114</u>	

The following table describes the financial effect of the modifications made to borrowers experiencing financial difficulty:

Loan Type	Term Extension and Added Co-Borrower
	Financial Effect
Commercial Real Estate	Added a co-borrower with financial ability to strengthen the credit risk related to this particular loans. No other modification was made to this loan that had a financial effect on the borrower(s).
Other - Commercial	Added a weighted-average of 5 years to the life of the loans, which reduced the monthly payment amount for the borrowers. Added a co-borrower with financial ability to strengthen the credit risk related to these particular loans.

There were no modified loans past due or on non-accrual as of September 30, 2023.

There were no modified loans made during the three and nine months ended September 30, 2023 that subsequently defaulted.

The Company has not committed to lending additional amounts to the borrowers included in the previous tables.

Foreclosed real estate consists of property acquired in settlement of loans which is carried at its fair value less estimated selling costs. Write-downs from cost to fair value less estimated selling costs are recorded at the date of acquisition or repossession and are charged to the allowance for credit losses. Foreclosed real estate was \$100,000 and \$95,000 at September 30, 2023 and December 31, 2022, respectively, and was included as a component of other assets on the consolidated statements of financial condition. The recorded investment of consumer mortgage loans secured by residential real estate properties for which formal foreclosure proceedings are in process according to local requirements of the applicable jurisdiction was \$0.2 million at September 30, 2023 and \$1.8 million at December 31, 2022.

Note 5 – Earnings per Share

Earnings per share was calculated for the three and nine months ended September 30, 2023 and 2022. Basic earnings per share is based upon the weighted average number of common shares outstanding, exclusive of unearned shares held by the Employee Stock Ownership Plan of Lake Shore Bancorp, Inc. (the “ESOP”) and by the Lake Shore Bancorp, Inc. 2012 Equity Incentive Plan (“EIP”). Diluted earnings per share is based upon the weighted average number of common shares outstanding and common share equivalents that would arise from the exercise of dilutive securities. Stock options are regarded as potential common stock and are considered in the diluted earnings per share calculations to the extent they would be dilutive and computed using the treasury stock method.

The calculated basic and diluted earnings per share are as follows:

	Three Months Ended September 30,	
	2023	2022
Numerator – net income	\$ 1,571,000	\$ 1,771,000
Denominator:		
Basic weighted average shares outstanding	5,846,333	5,889,615
Increase in weighted average shares outstanding due to:		
Stock options ⁽¹⁾	—	—
Diluted weighted average shares outstanding ⁽¹⁾	5,846,333	5,889,615
Earnings per share:		
Basic	\$ 0.27	\$ 0.30
Diluted	\$ 0.27	\$ 0.30

	Nine Months Ended September 30,	
	2023	2022
Numerator – net income	\$ 4,071,000	\$ 4,516,000
Denominator:		
Basic weighted average shares outstanding	5,858,054	5,875,155
Increase in weighted average shares outstanding due to:		
Stock options ⁽¹⁾	—	483
Diluted weighted average shares outstanding ⁽¹⁾	5,858,054	5,875,638
Earnings per share:		
Basic	\$ 0.69	\$ 0.77
Diluted	\$ 0.69	\$ 0.77

- (1) Stock options to purchase 58,857 shares under the Company's 2006 Stock Option Plan and 13,101 shares under the EIP at \$14.38 were outstanding during the three and nine months ended September 30, 2023 but were not included in the calculation of diluted earnings per share because to do so would have been anti-dilutive.

Note 6 – Commitments to Extend Credit

The Company has commitments to extend credit with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated statements of financial condition.

The Company's exposure to credit loss is represented by the contractual amount of these commitments. There was a \$351,000 and \$0 allowance for credit losses on these commitments at September 30, 2023 and December 31, 2022, respectively. The Company follows the same credit policies in making commitments as it does for on-balance sheet instruments.

The following commitments to extend credit were outstanding as of the dates specified:

	Contract Amount	
	September 30, 2023	December 31, 2022
	(Dollars in thousands)	
Commitments to grant loans	\$ 13,873	\$ 26,334
Unfunded commitments to fund loans and lines of credit	77,581	74,848
Commercial and Standby letters of credit	762	—

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses. The commitments for lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Company, is based on management's credit evaluation of the customer.

Note 7 – Stock-based Compensation

As of September 30, 2023, the Company had three active stock-based compensation plans, which are described below. The compensation cost that has been recorded under salary and benefits expense in the non-interest expense section of the consolidated statements of income for these plans was \$62,000 and \$85,000 for the three months ended September 30, 2023 and 2022, respectively. The compensation cost that has been recorded for the nine months ended September 30, 2023 and 2022 was \$88,000 and \$259,000, respectively.

2006 Stock Option Plan

The Company's 2006 Stock Option Plan (the "Stock Option Plan"), which was approved by the Company's stockholders, permitted the grant of options to its employees and non-employee directors for up to 297,562 shares of common stock. The Stock Option Plan expired on October 24, 2016, and grants of options can no longer be awarded.

Both incentive stock options and non-qualified stock options have been granted under the Stock Option Plan. The exercise price of each stock option equals the market price of the Company's common stock on the date of grant and an option's maximum term is ten years. The stock options generally vest over a five year period.

A summary of the status of the Stock Option Plan during the nine months ended September 30, 2023 and 2022 is presented below:

	2023			2022		
	Options	Weighted Average Exercise Price	Remaining Contractual Life	Options	Weighted Average Exercise Price	Remaining Contractual Life
Outstanding at beginning of year	58,857	\$ 14.38		64,548	\$ 14.38	
Granted	—	—		—	—	
Exercised	—	—		—	—	
Forfeited	—	—		—	—	
Outstanding at end of period	58,857	\$ 14.38	3.0 years	64,548	\$ 14.38	4.0 years
Options exercisable at end of period	58,857	\$ 14.38	3.0 years	64,548	\$ 14.38	4.0 years
Fair value of options granted	—	—		—	\$ —	

At September 30, 2023, stock options had no intrinsic value and there were no remaining options available for grant under the Stock Option Plan. At September 30, 2023 and 2022, respectively, all compensation cost and expense related to the Stock Option Plan has been recognized in prior periods.

2012 Equity Incentive Plan

The Company's 2012 Equity Incentive Plan (the "EIP"), which was approved by the Company's stockholders on May 23, 2012, authorizes the issuance of up to 180,000 shares of common stock pursuant to grants of restricted stock awards and up to 20,000 shares of common stock pursuant to grants of incentive stock options and non-qualified stock options, subject to permitted adjustments for certain corporate transactions. Employees and non-employee directors of Lake Shore Bancorp or its subsidiaries are eligible to receive awards under the EIP, except that non-employees may not be granted incentive stock options.

The Board of Directors granted restricted stock awards under the EIP during the nine months ended September 30, 2023 as follows:

Grant Date	Number of Restricted Stock Awards	Vesting	Fair Value per Share of Award on Grant Date	Awardees
January 17, 2023	2,709	100% on January 17, 2024	\$ 12.92	Non-employee directors
January 18, 2023	4,573	100% on January 18, 2024	\$ 12.90	Non-employee directors
January 18, 2023	1,000	20% per year with first vesting date on January 18, 2024	\$ 12.90	Employees

A summary of the status of unvested restricted stock awards under the EIP for the nine months ended September 30, 2023 and 2022 is as follows:

	At September 30, 2023	Weighted Average Grant Price (per Share)	At September 30, 2022	Weighted Average Grant Price (per Share)
Unvested shares outstanding at beginning of year	43,866	\$ 15.02	29,495	\$ 15.24
Granted	8,282	12.91	27,132	14.97
Vested	(11,734)	15.39	—	—
Forfeited	(17,967)	14.91	(6,254)	15.12
Unvested shares outstanding at end of period	22,447	\$ 14.13	50,373	\$ 15.11

As of September 30, 2023, there were 109,620 shares of restricted stock that vested or were distributed to eligible participants under the EIP and 47,933 remaining shares available for grant. Compensation expense related to unvested

restricted stock awards under the EIP amounted to \$40,000 and \$59,000 for the three months ended September 30, 2023 and 2022, respectively. Compensation expense related to unvested restricted stock awards under the EIP amounted to \$22,000 and \$175,000 for the nine months ended September 30, 2023 and 2022, respectively. At September 30, 2023, \$119,000 of unrecognized compensation cost related to unvested restricted stock awards is expected to be recognized over a period of 13.2 months.

A summary of the status of stock options under the EIP for the nine months ended September 30, 2023 and 2022 is presented below:

	2023			2022		
	Options	Exercise Price	Remaining Contractual Life	Options	Exercise Price	Remaining Contractual Life
Outstanding at beginning of year	20,000	\$ 14.38		20,000	\$ 14.38	
Granted	—	—		—	—	
Exercised	—	—		—	—	
Forfeited	—	—		—	—	
Expired	(6,899)	\$ 14.38				
Outstanding at end of period	<u>13,101</u>		3.0 years	<u>20,000</u>	\$ 14.38	4.0 years
Options exercisable at end of period	<u>13,101</u>	\$ 14.38	3.0 years	<u>20,000</u>	\$ 14.38	4.0 years
Fair value of options granted	<u>—</u>	—		<u>—</u>	—	

At September 30, 2023, stock options had no intrinsic value and there were 6,899 remaining options available for grant under the EIP. At September 30, 2023 and 2022, all compensation cost and expense related to the stock options granted under the EIP has been recognized in prior periods.

Employee Stock Ownership Plan (“ESOP”)

The Company established the ESOP for the benefit of eligible employees of the Company and Bank. All Company and Bank employees meeting certain age and service requirements are eligible to participate in the ESOP. Participants’ benefits become fully vested after five years of service once the employee is eligible to participate in the ESOP. The Company utilized \$2.6 million of the proceeds of its 2006 stock offering to extend a loan to the ESOP and the ESOP used such proceeds to purchase 238,050 shares of stock on the open market at an average price of \$10.70 per share, plus commission expenses. As a result of the purchase of shares by the ESOP, total stockholders’ equity of the Company was reduced by \$2.6 million. As of September 30, 2023, the balance of the loan to the ESOP was \$1.4 million and the fair value of unallocated shares was \$1.0 million. As of September 30, 2023, there were 76,815 allocated shares and 103,154 unallocated shares compared to 77,475 allocated shares and 111,089 unallocated shares at September 30, 2022. The ESOP compensation expense was \$22,000 for the three months ended September 30, 2023 and \$26,000 for the three months ended September 30, 2022 based on 1,984 shares earned in each of those quarters. The ESOP compensation expense was \$66,000 for the nine months ended September 30, 2023 and \$84,000 for the nine months ended September 30, 2022 based on 5,952 shares earned in each of those nine month periods.

Note 8 - Fair Value of Financial Instruments

Management uses its best judgment in estimating the fair value of the Company’s financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Company could have realized in a sale transaction on the dates indicated. The estimated fair value amounts have been measured as of September 30, 2023 and December 31, 2022 and have not been re-evaluated or updated for purposes of these unaudited consolidated financial statements subsequent to those respective dates. The estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported here.

GAAP establishes a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities measurements (Level 1) and the lowest priority to unobservable input measurements (Level 3). The three levels of the fair value hierarchy are as follows:

Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.

Level 2: Inputs other than quoted prices included in Level 1 that are observable for the asset or liability either directly or indirectly.

Level 3: Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

An asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The Company's consolidated statements of financial condition contain investment securities and derivative instruments that are recorded at fair value on a recurring basis. For financial instruments measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at September 30, 2023 and December 31, 2022 were as follows:

	Fair Value Measurements at September 30, 2023			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
	(Dollars in thousands)			
Measured at fair value on a recurring basis:				
Securities:				
Debt Securities				
U.S. government agencies	\$ 1,773	\$ —	\$ 1,773	\$ —
Municipal bonds	31,147	—	31,147	—
Mortgage-backed securities:				
Collateralized mortgage obligations-private label	9	—	9	—
Collateralized mortgage obligations-government sponsored entities	10,503	—	10,503	—
Government National Mortgage Association	53	—	53	—
Federal National Mortgage Association	9,740	—	9,740	—
Federal Home Loan Mortgage Corporation	4,619	—	4,619	—
Asset-backed securities:				
Private label	92	—	92	—
Government sponsored entities	3	—	3	—
Total Debt Securities	\$ 57,939	\$ —	\$ 57,939	\$ —
Equity securities	13	13	—	—
Total Securities	\$ 57,952	\$ 13	\$ 57,939	\$ —

		Fair Value Measurements at December 31, 2022			
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)	
	Fair Value	(Dollars in thousands)			
Measured at fair value on a recurring basis:					
Securities:					
Debt Securities					
U.S. government agencies	\$ 1,833	\$ —	\$ 1,833	\$ —	
Municipal bonds	42,414	—	42,414	—	
Mortgage-backed securities:					
Collateralized mortgage obligations-private label	11	—	11	—	
Collateralized mortgage obligations-government sponsored entities	12,155	—	12,155	—	
Government National Mortgage Association	59	—	59	—	
Federal National Mortgage Association	11,246	—	11,246	—	
Federal Home Loan Mortgage Corporation	5,221	—	5,221	—	
Asset-backed securities:					
Private label	96	—	96	—	
Government sponsored entities	4	—	4	—	
Total Debt Securities	\$ 73,039	\$ —	\$ 73,039	\$ —	
Equity securities	8	8	—	—	
Total Securities	\$ 73,047	\$ 8	\$ 73,039	\$ —	
Interest Rate Swap ⁽¹⁾	\$ 273	\$ —	\$ 273	\$ —	

⁽¹⁾ Included in Other Assets on the consolidated statements of financial condition.

Level 2 inputs for assets or liabilities measured at fair value on a recurring basis might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment projections, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means. The following is a description of valuation methodologies used for financial assets recorded at fair value on a recurring basis:

- Investment securities - the fair values are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1) or matrix pricing (Level 2), which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted prices. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution date, market consensus prepayment projections, credit information, and the security' terms and conditions, among other things. Level 2 securities which are fixed income instruments that are not quoted on an exchange, but are traded in active markets, are valued using prices obtained from our custodian, who use third party data service providers.
- Interest Rate Swap – the fair value is based on a discounted cash flow model. The model's key assumptions include the contractual term of the derivative contract, including the period to maturity, and the use of observable market based inputs, such as interest rates, yield curves, nonperformance risk and implied volatility.

Assets Measured at Fair Value on a Non-Recurring Basis

In addition to disclosure of the fair value of assets on a recurring basis, GAAP requires disclosures for assets and liabilities measured at fair value on a non-recurring basis. The following is a description of the valuation methods used for assets measured at fair value on a non-recurring basis.

Collateral-Dependent Loans. Loans for which repayment is substantially expected to be provided through the operations or sale of collateral are considered collateral dependent. They are held at the lower of cost or fair value, and are considered

to be measured at fair value when recorded below cost. Collateral-dependent loans are valued based on the estimated fair value of the collateral, less estimated costs to sell at the reporting date, based on either a recent appraisal or discounted cash flows based on current market conditions. Accordingly, collateral dependent loans are classified within Level 3 of the fair value hierarchy. As of September 30, 2023 and December 31, 2022, the Company did not record any non-recurring adjustments on collateral dependent loans.

Foreclosed Real Estate and Repossessed Assets. Foreclosed real estate and repossessed assets are held at the lower of cost or fair value and are considered to be measured at fair value when recorded below cost. The fair value of foreclosed real estate is calculated using independent appraisals, less estimated selling costs. Certain repossessed assets may require assumptions about factors that are not observable in an active market when determining fair value. Accordingly, foreclosed real estate and repossessed assets are classified within Level 3 of the fair value hierarchy. Foreclosed real estate was \$100,000 and \$95,000 at September 30, 2023 and December 31, 2022, respectively and was included as a component of other assets on the consolidated statements of financial condition. No non-recurring adjustments were made to foreclosed real estate at September 30, 2023 or December 31, 2022.

Mortgage Servicing Rights. Mortgage servicing rights do not trade in an active market with readily observable market data. As a result, the Company estimates the fair value of loan servicing rights by using a discounted cash flow model to calculate the present value of estimated future net servicing income. The key assumptions used in the model include the estimated life of loans sold with servicing retained and the estimated cost to service the loans. Loan servicing rights are classified as Level 3 measurements due to the use of unobservable inputs, as well as management judgment and estimation. Mortgage servicing rights are included as a component of other assets on the consolidated statements of financial condition.

For assets subject to measurement at fair value on a non-recurring basis, the fair value measurements by level within the fair value hierarchy used at September 30, 2023 and December 31, 2022 were as follows:

	Fair Value	Fair Value Measurements		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
		(Dollars in thousands)		
Measured at fair value on a non-recurring basis:				
<u>At September 30, 2023</u>				
Collateral-dependent loans	\$ 1,371	\$ —	\$ —	\$ 1,371
Foreclosed real estate	100	—	—	100
Mortgage servicing rights	199	—	—	199
<u>At December 31, 2022</u>				
Mortgage servicing rights	209	—	—	209

The following table presents additional quantitative information about assets measured at fair value on a non-recurring basis and for which the Company has utilized Level 3 inputs to determine fair value:

(Dollars in thousands)	Quantitative Information about Level 3 Fair Value Measurements				
	Fair Value Estimate	Valuation Technique	Unobservable Input	Range	Weighted Average
At September 30, 2023					
Collateral-dependent loans \$	1,371	Appraisal of collateral ⁽¹⁾	Direct Disposal Costs ⁽³⁾	8.00-10.00%	9.75 %
Foreclosed real estate	100	Appraisal of collateral ⁽¹⁾	Direct Disposal Costs ⁽³⁾	7.00-8.00%	7.69 %
Mortgage servicing rights	199	Discounted Cash Flow Model ⁽²⁾	Servicing Fees	0.25 %	0.25 %
			Servicing Costs	0.09 %	0.09 %
			Estimated Life of Loans	5.31 years	5.31 years
At December 31, 2022					
Mortgage servicing rights	209	Discounted Cash Flow Model ⁽²⁾	Servicing Fees	0.25 %	0.25 %
			Servicing Costs	0.15 %	0.15 %
			Estimated Life of Loans	5.0 years	5.0 years

- (1) Fair value is generally determined through independent third-party appraisals of the underlying collateral or by a purchase offer for the related property, which generally includes various Level 3 inputs which are not observable.
- (2) The fair value is based on a discounted cash flow model. The model's key assumptions are the estimated life of loans sold with servicing retained and the estimated cost to service the loans.
- (3) The fair value basis may be adjusted to reflect management estimates of disposal costs including, but not necessarily limited to, real estate brokerage commissions, legal fees, and delinquent property taxes.

The carrying amount and estimated fair value of the Company's financial instruments, whether carried at cost or fair value, are as follows:

	Fair Value Measurements at September 30, 2023				
	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
(Dollars in thousands)					
Financial assets:					
Cash and cash equivalents	\$ 45,999	\$ 45,999	\$ 45,999	\$ —	\$ —
Securities	57,952	57,952	13	57,939	—
Federal Home Loan Bank stock	2,347	2,347	—	2,347	—
Loans receivable, net	564,848	546,849	—	—	546,849
Accrued interest receivable	2,889	2,889	—	2,889	—
Bank-owned life insurance	23,546	23,546	—	23,546	—
Mortgage servicing rights	199	199	—	—	199
Financial liabilities:					
Deposits	584,158	580,216	—	580,216	—
Long-term debt	36,450	35,602	—	35,602	—
Accrued interest payable	566	566	—	566	—

	Fair Value Measurements at December 31, 2022				
	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
(Dollars in thousands)					
Financial assets:					
Cash and cash equivalents	\$ 9,633	\$ 9,633	\$ 9,633	\$ —	\$ —
Securities	73,047	73,047	8	73,039	—
Federal Home Loan Bank stock	2,330	2,330	—	2,330	—
Loans receivable, net	573,537	546,278	—	—	546,278
Accrued interest receivable	2,796	2,796	—	2,796	—
Interest rate swap	273	273	—	273	—
Mortgage servicing rights	209	209	—	—	209
Financial liabilities:					
Deposits	570,119	571,521	—	571,521	—
Short-term borrowings	12,596	12,596	—	12,596	—
Long-term debt	24,950	23,946	—	23,946	—
Accrued interest payable	66	66	—	66	—

Note 9 – Treasury Stock

During the three and nine months ended September 30, 2023, the Company did not repurchase any shares of common stock under the existing stock repurchase program. As of September 30, 2023, there were 30,626 shares remaining to be repurchased under the existing stock repurchase program. During the nine months ended September 30, 2023, the Company transferred 8,282 shares of common stock out of treasury stock reserved for the 2012 Equity Incentive Plan, at an average cost of \$9.39 per share to fund awards that had been granted under the plan. During the nine months ended September 30, 2023, there were 17,967 shares transferred back into treasury stock reserved for the 2012 Equity Incentive Plan at an average cost of \$9.39 per share due to forfeitures. The Company repurchased 4,764 shares upon vesting of shares under the 2012 Equity Incentive Plan for the purpose of remitting payroll taxes on behalf of awardees who were employees, at an average cost of \$11.63 per share, during the nine months ended September 30, 2023.

During the three months ended September 30, 2022, the Company did not repurchase any shares of common stock. During the nine months ended September 30, 2022, the Company repurchased 5,701 shares of common stock at an average cost of \$14.91 per share. These shares were repurchased pursuant to the Company's publicly announced common stock repurchase program. As of September 30, 2022, there were 30,626 shares remaining to be repurchased under the existing stock repurchase program. During the nine months ended September 30, 2022, the Company transferred 27,132 shares of common stock out of treasury stock reserved for the 2012 Equity Incentive Plan, at an average cost of \$9.39 per share to fund awards that had been granted under the plan. During the nine months ended September 30, 2022, there were 6,254 shares transferred back into treasury stock reserved for the 2012 Equity Incentive Plan at an average cost of \$9.39 per share due to forfeitures.

Note 10 – Other Comprehensive Loss

In addition to presenting the consolidated statements of comprehensive income (loss) herein, the following table shows the tax effects allocated to the Company's single component of other comprehensive loss for the periods presented:

	For the Three Months Ended September 30, 2023			For The Three Months Ended September 30, 2022		
	Pre-Tax Amount	Tax Benefit (Expense)	Net of Tax Amount	Pre-Tax Amount	Tax Benefit	Net of Tax Amount
	(Unaudited) (Dollars in thousands)					
Net unrealized losses on securities available for sale:						
Net unrealized losses arising during the period	\$ (4,014)	\$ 843	\$ (3,171)	\$ (5,004)	\$ 1,050	\$ (3,954)
Less: reclassification adjustment related to:						
Loss on sale of securities included in net income	3	—	3	—	—	—
Recovery on previously impaired investment securities included in net income	(2)	—	(2)	(2)	1	(1)
Total Other Comprehensive Loss	<u>\$ (4,013)</u>	<u>\$ 843</u>	<u>\$ (3,170)</u>	<u>\$ (5,006)</u>	<u>\$ 1,051</u>	<u>\$ (3,955)</u>

	For the Nine Months Ended September 30, 2023			For The Nine Months Ended September 30, 2022		
	Pre-Tax Amount	Tax Benefit (Expense)	Net of Tax Amount	Pre-Tax Amount	Tax Benefit	Net of Tax Amount
	(Unaudited) (Dollars in thousands)					
Net unrealized losses on securities available for sale:						
Net unrealized losses arising during the period	\$ (3,473)	\$ 729	\$ (2,744)	\$ (17,109)	\$ 3,592	\$ (13,517)
Less: reclassification adjustment related to:						
Loss on sale of securities included in net income	52	(10)	42	—	—	—
Recovery on previously impaired investment securities included in net income	(6)	1	(5)	(12)	3	(9)
Total Other Comprehensive Loss	<u>\$ (3,427)</u>	<u>\$ 720</u>	<u>\$ (2,707)</u>	<u>\$ (17,121)</u>	<u>\$ 3,595</u>	<u>\$ (13,526)</u>

The following table presents the amounts reclassified out of the single component of the Company's accumulated other comprehensive loss for the indicated periods:

Details about Accumulated Other Comprehensive Loss Components	Amounts Reclassified from Accumulated Other Comprehensive Loss for the three months ended September 30,		Affected Line Item on the Consolidated Statements of Income
	2023	2022	
	(Dollars in thousands)		
Net unrealized losses on securities available for sale:			
Loss on sale of securities included in net income	\$ 3	\$ —	Loss on sale of securities available for sale
Recovery on previously impaired investment securities	(2)	(2)	Recovery on previously impaired investment securities
Provision for income tax expense	—	1	Income tax expense
Total reclassification for the period	<u>\$ 1</u>	<u>\$ (1)</u>	Net Income

Details about Accumulated Other Comprehensive Loss Components	Amounts Reclassified from Accumulated Other Comprehensive Loss for the nine months ended September 30,		Affected Line Item on the Consolidated Statements of Income
	2023	2022	
(Dollars in thousands)			
Net unrealized losses on securities available for sale:			
Loss on sale of securities included in net income	\$ 52	\$ —	Loss on sale of securities available for sale
Recovery on previously impaired investment securities	(6)	(12)	Recovery on previously impaired investment securities
Provision for income tax expense	(9)	3	Income tax expense
Total reclassification for the period	<u>\$ 37</u>	<u>\$ (9)</u>	Net Income

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
Forward-Looking Statements

Safe-Harbor

This Quarterly Report on Form 10-Q contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, that are based on current expectations, estimates and projections about the Company's and the Bank's industry, and management's beliefs and assumptions. Words such as anticipates, expects, intends, plans, believes, estimates and variations of such words and expressions are intended to identify forward-looking statements. Such statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to forecast. Therefore, actual results may differ materially from those expressed or forecast in such forward-looking statements.

Potential risks and uncertainties that could cause our actual results to differ from those anticipated in any forward-looking statements include, but are not limited to, those described in Part I, Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2022, Part II, Item 1A of this Quarterly Report on Form 10-Q and the following:

- compliance with the Consent Order and Individual Minimum Capital Requirement from the Office of the Comptroller of the Currency;
- compliance with the Written Agreement with the Federal Reserve Bank of Philadelphia;
- risks from data loss or other security breaches, including a breach of our operational or security systems, policies, or procedures, including cyber-attacks on us or on our third-party vendors or service providers;
- recent events involving the failure of financial institutions may adversely affect our business, and the market price of our common stock;
- the strength of the United States economy in general and of the local economies in which we conduct operations;
- the effect of change in monetary and fiscal policy, including changes in interest rate policies of the Board of Governors of the Federal Reserve System;
- inflation, and market and monetary fluctuations;
- climate change;
- deterioration in the credit quality of our loan portfolio and/or the value of the collateral securing repayment of loans;
- unanticipated changes in our liquidity position;
- reduction in the value of our investment securities;
- the cost and ability to attract and retain key employees;
- regulatory or legal developments, tax policy changes;
- our ability to implement and execute our business plan and strategy and expand our operations;
- the ability of our customers to make loan payments;
- the effect of competition on rates of deposit and loan growth and net interest margin;
- our ability to continue to control costs and expenses;
- any future FDIC insurance premium increases, or special assessment may adversely affect our earnings;
- risks relating to the COVID-19 pandemic;
- changes in accounting principles, policies, or guidelines;
- our success in managing the risks involved in our business; and
- other economic, competitive, governmental, regulatory and technological factors affecting our operations, pricing, products and services.

Any and all of our forward-looking statements in this Quarterly Report on Form 10-Q and in any other public statements we make may differ from actual outcomes. They can be affected by inaccurate assumptions we might make or known or unknown risks and uncertainties. Consequently, no forward-looking statement can be guaranteed. We undertake no obligation to publicly update any forward-looking statement, whether as a result of new information, future events or otherwise.

Overview

The following discussion and analysis is presented to assist in the understanding and evaluation of our consolidated financial condition, results of operations and other relevant statistical data. It is intended to complement the unaudited consolidated financial statements and notes thereto appearing elsewhere in this Form 10-Q and should be read in conjunction therewith. The detailed discussion focuses on our consolidated financial condition as of September 30, 2023 compared to the consolidated financial condition as of December 31, 2022 and the consolidated results of operations for the three and nine months ended September 30, 2023 and 2022.

Our results of operations depend primarily on our net interest income, which is the difference between the interest income we earn on loans and investments and the interest expense we pay on deposits, borrowings and other interest-bearing liabilities. Net interest income is affected by the relative amounts of interest-earning assets and interest-bearing liabilities and the interest rates we earn or pay on these balances.

Our operations are also affected by non-interest income, such as service charges and fees, debit card fees, earnings on bank owned life insurance, and gains and losses on interest rate swaps and the sales of securities and loans, our provision for credit losses and non-interest expenses which include salaries and employee benefits, occupancy and equipment costs, data processing, professional services, advertising, FDIC insurance and other general and administrative expenses.

Financial institutions like us, in general, are significantly affected by economic conditions, competition, and the monetary and fiscal policies of the federal government. Lending activities are influenced by the demand for and supply of housing and commercial real estate, competition among lenders, interest rate conditions, and funds availability. Our operations and lending are principally concentrated in the Western New York area, and our operations and earnings are influenced by local economic conditions. Deposit balances and cost of funds are influenced by prevailing market rates on competing investments, customer preferences, and levels of personal income and savings in our primary market area. Operations are also significantly impacted by government policies and actions of regulatory authorities. Future changes in applicable law, regulations or government policies may materially impact the Company.

Recent Events

As previously reported on a [Current Report on Form 8-K](#) filed on June 28, 2023 with the SEC, Lake Shore, MHC and Lake Shore Bancorp, Inc. (collectively, the “Companies”), the parent savings and loan holding companies of Lake Shore Savings Bank, entered into a written agreement (the “Agreement”) with the Federal Reserve Bank of Philadelphia (the “Reserve Bank”), the Companies’ regulator. The Agreement provides, among other things, that the Companies take appropriate steps to fully utilize the Companies’ financial and managerial resources to serve as a source of strength to the Bank, including, but not limited to, taking steps to ensure that the Bank complies with the Consent Order (described below) and not, directly or indirectly, declare or pay dividends, increase or guarantee any debt. We expect that our non-interest expenses will continue at their increased levels as a result of the Agreement and the Order, which may adversely affect our financial performance.

As previously reported on a [Current Report on Form 8-K](#) filed on February 9, 2023 with the SEC, the Bank consented to the issuance of a Consent Order (the “Order”) by the Office of the Comptroller of the Currency (the “OCC”), the Bank’s primary federal regulator. The Order requires the Bank to correct deficiencies related to information technology, security, automated clearing house program, audit, management and BSA/AML. Management and the Bank’s Board of Directors are committed to promptly addressing the action items included in the Order. We expect that our non-interest expenses will continue at their increased levels as a result of remediation actions we will take in order to comply with the requirements of the Order which may adversely affect our financial performance.

Management Strategy

There have been no material changes in the Company’s management strategy from what was disclosed in the Company’s Annual Report on Form 10-K for the year ended December 31, 2022.

Critical Accounting Estimates

Disclosure of the Company's significant accounting estimates is included in the notes to the consolidated financial statements of the Company's Annual Report on Form 10-K for the year ended December 31, 2022. Some of these estimates require significant judgment, estimates and assumptions to be made by management, most particularly in connection with determining securities valuation, impairment of securities and income taxes. The Company adopted ASU 2016-13 - *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, as amended, ("CECL") for all financial assets measured at amortized cost using the modified retrospective method on January 1, 2023 and replaced the allowance for loan losses "incurred loss" model discussed in the Form 10-K for the year ended December 31, 2022 with the allowance for credit losses model. Refer to Notes 2 and 4 in the unaudited consolidated financial statements for additional information and accounting policies related to the CECL model.

Analysis of Net Interest Income

Net interest income represents the difference between the interest we earn on our interest-earning assets, such as commercial and residential mortgage loans and investment securities, and the expense we pay on interest-bearing liabilities, such as deposits and borrowings. Net interest income depends on both the volume of our interest-earning assets and interest-bearing liabilities and the interest rates we earn or pay on them.

Average Balances, Interest and Average Yields. The following tables set forth certain information relating to our average balance sheets and reflects the average yield on interest-earning assets and average cost of interest-bearing liabilities, interest earned and interest paid for the periods indicated. Such yields and costs are derived by dividing income or expense by the average balance of interest-earning assets or interest-bearing liabilities, respectively, for the periods presented. Average balances are derived from daily balances over the periods indicated. The average balances for loans are net of allowance for credit losses but include non-accrual loans. The loan yields include net amortization of certain deferred fees and costs that are considered adjustments to yields. The net amortization of deferred loan fees and costs were \$77,000 and \$176,000 for the three months ended September 30, 2023 and 2022, respectively. The net amortization of deferred loan fees and costs

were \$392,000 and \$323,000 for the nine months ended September 30, 2023 and 2022, respectively. Interest income on securities does not include a tax equivalent adjustment for tax exempt securities.

	For the Three Months Ended September 30, 2023			For the Three Months Ended September 30, 2022		
	Average Balance	Interest Income/ Expense	Yield/ Rate ⁽²⁾	Average Balance	Interest Income/ Expense	Yield/ Rate ⁽²⁾
(Dollars in thousands)						
Interest-earning assets:						
Interest-earning deposits & federal funds sold	\$ 43,374	\$ 559	5.16 %	\$ 16,461	\$ 88	2.14 %
Securities ⁽¹⁾	65,019	463	2.85 %	79,350	519	2.62 %
Loans, including fees	565,011	7,699	5.45 %	552,320	6,311	4.57 %
Total interest-earning assets	673,404	8,721	5.18 %	648,131	6,918	4.27 %
Other assets	45,506			49,188		
Total assets	\$ 718,910			\$ 697,319		
Interest-bearing liabilities						
Demand & NOW accounts	\$ 76,171	\$ 19	0.10 %	\$ 85,323	\$ 18	0.08 %
Money market accounts	123,998	405	1.31 %	166,250	110	0.26 %
Savings accounts	69,327	13	0.08 %	78,798	11	0.06 %
Time deposits	214,282	1,667	3.11 %	138,464	280	0.81 %
Borrowed funds & other interest-bearing liabilities	36,953	322	3.49 %	25,530	154	2.41 %
Total interest-bearing liabilities	520,731	2,426	1.86 %	494,365	573	0.46 %
Other non-interest bearing liabilities	114,152			120,758		
Stockholders' equity	84,027			82,196		
Total liabilities & stockholders' equity	\$ 718,910			\$ 697,319		
Net interest income		\$ 6,295			\$ 6,345	
Interest rate spread			3.32 %			3.81 %
Net interest margin			3.74 %			3.92 %

- (1) The tax equivalent adjustment for bank qualified tax exempt municipal securities results in rates of 3.24% and 3.03% for the three months ended September 30, 2023 and 2022, respectively.
- (2) Annualized.

	For the Nine Months Ended September 30, 2023			For the Nine Months Ended September 30, 2022		
	Average Balance	Interest Income/ Expense	Yield/ Rate ⁽²⁾	Average Balance	Interest Income/ Expense	Yield/ Rate ⁽²⁾
	(Dollars in thousands)					
Interest-earning assets:						
Interest-earning deposits & federal funds sold	\$ 34,214	\$ 1,214	4.73 %	\$ 24,931	\$ 138	0.74 %
Securities ⁽¹⁾	70,268	1,502	2.85 %	84,015	1,545	2.45 %
Loans, including fees	569,977	22,426	5.25 %	537,825	17,600	4.36 %
Total interest-earning assets	674,459	25,142	4.97 %	646,771	19,283	3.98 %
Other assets	45,690			51,244		
Total assets	\$ 720,149			\$ 698,015		
Interest-bearing liabilities						
Demand & NOW accounts	\$ 77,948	\$ 57	0.10 %	\$ 87,988	\$ 57	0.09 %
Money market accounts	133,491	1,091	1.09 %	174,156	296	0.23 %
Savings accounts	72,111	35	0.06 %	77,109	31	0.05 %
Time deposits	203,527	4,149	2.72 %	134,792	711	0.70 %
Borrowed funds & other interest-bearing liabilities	39,451	1,010	3.41 %	23,646	397	2.24 %
Total interest-bearing liabilities	526,528	6,342	1.61 %	497,691	1,492	0.40 %
Other non-interest bearing liabilities	110,108			116,524		
Stockholders' equity	83,513			83,800		
Total liabilities & stockholders' equity	\$ 720,149			\$ 698,015		
Net interest income		\$ 18,800			\$ 17,791	
Interest rate spread			3.36 %			3.58 %
Net interest margin			3.72 %			3.67 %

- (1) The tax equivalent adjustment for bank qualified tax exempt municipal securities results in rates of 3.26% and 2.85% for the nine months ended September 30, 2023 and 2022, respectively.
- (2) Annualized.

Rate Volume Analysis. The following tables analyze the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities. The tables show the amount of the change in interest income or expense caused by either changes in outstanding balances (volume) or changes in interest rates. The effect of a change in volume is measured by applying the average rate during the first period to the volume change between the two periods. The effect of changes in rate is measured by applying the change in rate between the two periods to the

average volume during the first period. Changes attributable to both rate and volume, which cannot be segregated, have been allocated proportionately to the absolute value of the change due to volume and the change due to rate.

Three Months Ended September 30, 2023 Compared to Three Months Ended September 30, 2022			
	Rate	Volume (Dollars in thousands)	Net Change
Interest-earning assets:			
Interest-earning deposits & federal funds sold	\$ 218	\$ 253	\$ 471
Securities	43	(99)	(56)
Loans, including fees	1,240	148	1,388
Total interest-earning assets	1,501	302	1,803
Interest-bearing liabilities:			
Demand & NOW accounts	3	(2)	1
Money market accounts	330	(35)	295
Savings accounts	3	(1)	2
Time deposits	1,164	223	1,387
Total deposits	1,500	185	1,685
Other interest-bearing liabilities:			
Borrowed funds & other interest-bearing liabilities	88	80	168
Total interest-bearing liabilities	1,588	265	1,853
Total change in net interest income	\$ (87)	\$ 37	\$ (50)

Nine Months Ended September 30, 2023 Compared to Nine Months Ended September 30, 2022			
	Rate	Volume (Dollars in thousands)	Net Change
Interest-earning assets:			
Interest-earning deposits & federal funds sold	\$ 1,007	\$ 69	\$ 1,076
Securities	230	(273)	(43)
Loans, including fees	3,725	1,101	4,826
Total interest-earning assets	4,962	897	5,859
Interest-bearing liabilities:			
Demand & NOW accounts	7	(7)	—
Money market accounts	878	(84)	795
Savings accounts	6	(2)	4
Time deposits	2,919	519	3,438
Total deposits	3,810	427	4,237
Other interest-bearing liabilities:			
Borrowed funds & other interest-bearing liabilities	294	319	613
Total interest-bearing liabilities	4,104	746	4,850
Total change in net interest income	\$ 858	\$ 151	\$ 1,009

As shown in the above tables, the decrease in net interest income for three months ended September 30, 2023 was primarily impacted by an increase in the average interest rate paid on interest-bearing liabilities when compared to the prior year period, partially offset by an increase in the average interest rate earned on interest-earning assets. The average interest rate paid on interest-bearing liabilities increased 140 basis points from 0.46% during the three months ended September 30, 2022 to 1.86% during three months ended September 30, 2023. The increase in the average interest rate paid on interest-bearing liabilities during three months ended September 30, 2023 was primarily due to a 230 basis points increase in the average interest rate paid on time deposits and a \$75.8 million increase in the average balance of time deposits in comparison to the prior year period. The increase in average interest rate paid on time deposits and average time deposit balances was primarily due to an increase in customer demand for these types of deposit products due to the rising and competitive interest rate environment. The average yield on interest-earning assets for the three months ended September 30, 2023 increased by 91 basis points when compared to the prior year period primarily due to an increase in market interest rates and a \$12.7

million, or 2.3%, increase in average loans during the three months ended September 30, 2023. Net interest margin decreased to 3.74% for the three months ended September 30, 2023 as compared to 3.92% for the same period of the prior year.

As shown in the above tables, the increase in net interest income for the nine months ended September 30, 2023 was primarily due to an increase in the average yield of interest-earning assets when compared to the prior year period. The average yield of interest-earning assets increased 99 basis points from 3.98% during the nine months ended September 30, 2022 to 4.97% during the nine months ended September 30, 2023. The increase in the average yield of interest-earning assets was primarily driven by an 89 basis points increase in the average yield of average loans and a \$32.2 million increase in the average balance of loans. The increase in the average yield of interest-earning assets during the nine months ended September 30, 2023 was partially offset by a \$28.8 million increase in the average balance of interest-bearing liabilities in comparison to the prior year period. The increase in the average balance of interest-bearing deposits was primarily driven by an increase in the average balance of time deposit accounts. The average interest rate paid on interest-bearing liabilities for the nine months ended September 30, 2023 increased by 121 basis points when compared to the prior year period primarily due to an increase in market interest rates during the first nine months of 2023. Net interest margin increased to 3.72% for the nine months ended September 30, 2023 as compared to 3.67% for the nine months ended September 30, 2022.

Comparison of Financial Condition at September 30, 2023 and December 31, 2022

Total assets at September 30, 2023 were \$713.6 million, an increase of \$13.6 million, or 2.0%, from \$699.9 million at December 31, 2022. The increase in total assets was primarily due to a \$36.4 million increase in cash and cash equivalents, partially offset by a decrease in securities of \$15.0 million, or 20.7% and a decrease in loans receivable, net of \$8.7 million, or 1.5%.

Cash and cash equivalents increased by \$36.4 million, or 377.5%, from \$9.6 million at December 31, 2022 to \$46.0 million at September 30, 2023. The increase was primarily due to an increase in deposits and the sale of \$8.5 million of securities during the nine months ended September 30, 2023.

Securities decreased by \$15.0 million, or 20.7%, from \$73.0 million at December 31, 2022 to \$58.0 million at September 30, 2023, primarily due to the sale of \$8.5 million of securities, a \$3.4 million increase in the unrealized losses on the mark to market value of the available-for-sale securities, and securities paydowns of \$3.1 million.

Net loans receivable decreased during the nine months ended September 30, 2023 as shown in the table below:

	At September 30, 2023	At December 31, 2022	Change	
			\$	%
	(Dollars in thousands)			
Real Estate Loans:				
Residential, one- to four-family ⁽¹⁾	\$ 172,974	\$ 175,904	\$ (2,930)	(1.7) %
Home equity	51,276	53,057	(1,781)	(3.4) %
Commercial ⁽²⁾	323,535	326,955	(3,420)	(1.0) %
Total real estate loans	547,785	555,916	(8,131)	(1.5) %
Other Loans:				
Commercial	18,749	19,576	(827)	(4.2) %
Consumer	1,113	1,217	(104)	(8.5) %
Total gross loans	567,647	576,709	(9,062)	(1.6) %
Allowance for credit losses	(6,642)	(7,065)	423	(6.0) %
Net deferred loan costs	3,843	3,893	(50)	(1.3) %
Loans receivable, net	\$ 564,848	\$ 573,537	\$ (8,689)	(1.5) %

⁽¹⁾ Includes one- to four-family construction loans.

⁽²⁾ Includes commercial construction loans.

The loans receivable, net balance decreased \$8.7 million, or 1.5%, from \$573.5 million at December 31, 2022 to \$564.8 million at September 30, 2023. The decrease was primarily due to decreases in commercial, one- to four-family loans, and

home equity loans. During the nine months ended September 30, 2023, we remained strategically focused on originating shorter duration, adjustable-rate loans to diversify our asset mix and to manage interest rate risk.

Asset Quality. The following table sets forth activity in our allowance for credit losses on loans and other ratios at or for the dates indicated:

	At or for the Nine Months Ended September 30,	
	2023	2022
	(Dollars in thousands)	
Beginning balance, prior to adoption of ASC 326	\$ 7,065	\$ 6,118
Impact of adopting ASC 326	282	—
(Credit) provision for credit losses	(729)	500
Charge-offs:		
Real estate loans:		
Commercial	—	(4)
Other loans:		
Consumer	(47)	(58)
Total charge-offs	(47)	(62)
Recoveries:		
Real estate loans:		
Residential, one- to four-family	—	17
Home equity	—	1
Commercial	35	269
Other loans:		
Commercial	29	—
Consumer	7	6
Total recoveries	71	293
Net recoveries	24	231
Balance at end of period	\$ 6,642	\$ 6,849
Average loans outstanding	\$ 569,977	\$ 537,825
Allowance for credit losses as a percent of total net loans	1.18 %	1.22 %
Allowance for credit losses as a percent of non-performing loans	188.32 %	231.46 %

	For the Nine Months Ended September 30,	
	2023	2022
Ratio of net recoveries (charge-offs) to average loans outstanding by loan type, annualized:		
Real estate loans:		
Residential, one- to four-family	— %	0.01 %
Home equity	— %	— %
Commercial	0.02 %	0.12 %
Construction – Commercial	— %	— %
Other loans:		
Commercial	0.20 %	— %
Consumer	(4.58) %	(5.29) %
Ratio of net recoveries to average loans outstanding	0.01 %	0.06 %

	At September 30, 2023	At December 31, 2022
	(Dollars in thousands)	
Loans past due 90 days or more but still accruing:		
Real estate loans:		
Residential, one- to four-family	\$ —	\$ 1
Home equity	—	—
Commercial	—	—
Other loans:		
Commercial	—	—
Consumer	—	—
Total	\$ —	\$ 1
Loans accounted for on a non-accrual basis:		
Real estate loans:		
Residential, one- to four-family ⁽¹⁾	\$ 2,004	\$ 2,295
Home equity	319	602
Commercial ⁽²⁾	1,226	—
Other loans:		
Commercial	—	—
Consumer	8	34
Total non-accrual loans	3,557	2,931
Total non-performing loans	3,557	2,932
Foreclosed real estate	100	95
Total non-performing assets	\$ 3,657	\$ 3,027
Ratios:		
Non-performing loans as a percent of total net loans:	0.62 %	0.51 %
Non-performing assets as a percent of total assets:	0.51 %	0.43 %

(1) Includes one- to four- family construction loans.

(2) Includes Commercial construction loans.

Total non-performing assets increased by \$630,000, or 20.8%, to \$3.7 million at September 30, 2023 from \$3.0 million at December 31, 2022, primarily due to an increase in non-accrual loans, including one commercial relationship comprised of two loans which were moved to non-accrual status during the third quarter of 2023.

Other assets increased \$872,000, or 12.3%, to \$7.9 million at September 30, 2023 from \$7.1 million at December 31, 2022 primarily due to the increase in the Company's deferred tax assets related to the unrealized mark-to-market losses on the available for sale securities portfolio as a result of the increase in market interest rates.

The table below shows changes in deposit balances by type of deposit account between September 30, 2023 and December 31, 2022:

	At September 30, 2023	At December 31, 2022	Change	
			\$	%
	(Dollars in thousands)			
Core Deposits				
Demand deposits and NOW accounts:				
Non-interest bearing	\$ 99,871	\$ 105,678	\$ (5,807)	(5.5) %
Interest bearing	76,869	85,033	(8,164)	(9.6) %
Money market	123,103	149,250	(26,147)	(17.5) %
Savings	68,428	77,200	(8,772)	(11.4) %
Total core deposits	368,271	417,161	(48,890)	(11.7) %
Non-core Deposits				
Time deposits	215,887	152,958	62,929	41.1 %
Total deposits	\$ 584,158	\$ 570,119	\$ 14,039	2.5 %

The increase in total deposits was primarily due to a 41.1% increase in time deposits, partially offset by a decrease in core deposits. The increase in time deposits was primarily due to a \$46.9 million increase in customer time deposits, and a \$16.0 million increase in brokered time deposits. The increase in customer time deposits was primarily due to an increase in customer demand for these types of deposit products due to the rising and competitive interest rate environment. The increase in brokered time deposits was a result of management's strategy to lock in liquidity during a rising interest rate environment, and increased competition for deposits in our market area. The Company's strategic focus is centered on organic growth of deposits among its retail and commercial customers to reduce the reliance on wholesale funding and to strengthen customer relationships. At September 30, 2023 and December 31, 2022, the Company's percentage of uninsured deposits to total deposits was 12.4% and 16.6%, respectively.

During the nine months ended September 30, 2023, short term borrowings decreased by \$12.6 million, as the Company transferred its borrowings into long-term debt with the Federal Home Loan Bank of New York ("FHLBNY") to lock in interest rates and repaid \$2.8 million of debt. Long-term debt with the FHLBNY increased to \$36.5 million at September 30, 2023 from \$25.0 million at December 31, 2022.

Stockholders' equity at September 30, 2023 was \$81.9 million, a \$0.7 million increase, or 0.8%, as compared to \$81.2 million at December 31, 2022. The increase in stockholders' equity was primarily attributed to \$4.1 million in net income earned during the first nine months of 2023, partially offset by a \$2.7 million unrealized mark-to-market loss on the available for sales securities portfolio recognized in other comprehensive loss, and the initial entry of \$0.7 million recorded to retained earnings upon the adoption of CECL.

Comparison of Results of Operations for the Three Months Ended September 30, 2023 and 2022

General. Net income was \$1.6 million for the three months ended September 30, 2023, or \$0.27 per diluted share, a decrease of \$0.2 million, or 11.3%, compared to net income of \$1.8 million, or \$0.30 per diluted share, for the three months ended September 30, 2022. Net income for the three months ended September 30, 2023 reflected a \$0.3 million increase in non-interest expense, a \$1.9 million increase in interest expense, and a \$63,000 decrease in non-interest income, partially offset by a \$1.8 million increase in interest income and a \$0.2 million credit to the provision for credit losses.

Interest Income. Interest income increased by \$1.8 million, or 26.1%, to \$8.7 million for the three months ended September 30, 2023, when compared to the three months ended September 30, 2022. Loan interest income increased by \$1.4 million, or 22.0%, to \$7.7 million for the three months ended September 30, 2023, as compared to the prior year period primarily due to an increase in the average yield on loans and an increase in the average balance of the loan portfolio of \$12.7 million, or 2.3%, from \$552.3 million for the three months ended September 30, 2022, to \$565.0 million for the three months ended September 30, 2023. The increase in the average balance of the loan portfolio was primarily driven by growth in commercial real estate loans. The average yield on loans, including fees was 5.45% for the three months ended September 30, 2023, as compared to 4.57% for the three months ended September 30, 2022, primarily due to the impact of higher interest rates on variable rate loans, new loan originations, and portfolio composition.

Investment securities interest income decreased \$56,000, or 10.8%, to \$463,000 for the three months ended September 30, 2023, compared to the three months ended September 30, 2022, primarily due to a \$14.3 million decrease in the average balance of investment securities, partially offset by a 23 basis points increase in the average yield of investment securities.

Interest Expense. Interest expense increased \$1.9 million, or 323.4%, to \$2.4 million for the three months ended September 30, 2023, compared to \$573,000 for the three months ended September 30, 2022, primarily due to an increase in interest paid on deposits. Interest paid on deposits increased by \$1.7 million, or 402.1%, to \$2.1 million for the three months ended September 30, 2023, when compared to the three months ended September 30, 2022. The increase in interest expense on deposits was primarily due to a 138 basis points increase in the average interest rate paid on deposit accounts as the deposit mix shifted towards higher cost time deposits. The average balance of deposits increased by \$15.0 million, or 3.2%, from \$468.8 million for the three months ended September 30, 2022, to \$483.8 million for the three months ended September 30, 2023 primarily due to an increase in the average balance of time deposits. Interest expense on borrowed funds and other interest-bearing liabilities increased by \$168,000, or 109.1%, for the three months ended September 30, 2023 when compared to the three months ended September 30, 2022, primarily due to a \$11.4 million increase in average borrowed funds and other interest-bearing liabilities outstanding, and a 108 basis points increase in the average rate paid on

borrowings. The increase in borrowings was a result of management's strategy to add liquidity to the balance sheet as a result of economic volatility, anticipated loan growth, and increased competition for deposits in the current rising interest rate environment.

(Credit) Provision for Credit Losses. The provision for credit losses represents a charge or credit made to earnings to maintain a sufficient allowance for credit losses. The allowance for credit losses is management's estimate of expected lifetime losses in the loan portfolio as of the balance sheet date and is measured using the vintage method. The allowance for credit losses also applies to off-balance sheet credit exposures, including loan commitments and standby letters of credit, as well as available-for-sale debt securities. Management considers past events, current conditions, and reasonable and supportable forecasts as the basis for the estimation of expected credit losses.

The Company recorded a \$199,000 credit to the provision for credit losses on loans and unfunded commitments during the three months ended September 30, 2023, as compared to no provision for loan losses during the three months ended September 30, 2022. The current period (credit) provision for credit losses was primarily due to a decrease in the loan portfolio and loan commitments during the three months ended September 30, 2023.

Non-Interest Income. Non-interest income decreased by \$63,000, or 9.4%, to \$605,000 for the three months ended September 30, 2023, as compared to \$668,000 for the three months ended September 30, 2022. The decrease was primarily due to a \$91,000 decrease in unrealized gains on the interest rate swap products as a result of their unwind in the second quarter of 2023 and a \$21,000 decrease in service charges and fees during the three months ended September 30, 2023.

Non-Interest Expense. Non-interest expense increased by \$326,000, or 6.7%, to \$5.2 million for the three months ended September 30, 2023, as compared to \$4.9 million for the three months ended September 30, 2022. Salary and employee benefits expense increased \$269,000, or 10.7%, during the third quarter of 2023 primarily due to the addition of staffing resources, annual salary increases, and an increase in employee benefits. FDIC insurance expense increased by \$249,000, or 541.3%, during the current quarter due to an increase in premium assessments. Data processing costs increased \$29,000, or 7.2%, primarily due to an increase in costs related to core system maintenance and enhancements to existing IT security protocols. These increases were partially offset by a decrease in professional services of \$173,000, or 30.8%, primarily due to consulting costs incurred in the prior year quarter associated with remediation activities related to regulatory matters and a decrease in advertising costs of \$40,000, or 20.3%, with a decrease in marketing activity.

Income Taxes Expense. Income tax expense was \$332,000 for the three months ended September 30, 2023, a decrease of \$40,000, or 10.8%, as compared to \$372,000 for the three months ended September 30, 2022. The decrease in income tax expense was primarily due to a decrease in income before taxes. The effective tax rate was 17.4% for each of the three months ended September 30, 2023 and 2022.

Comparison of Results of Operations for the Nine Months Ended September 30, 2023 and 2022

General. Net income was \$4.1 million for the nine months ended September 30, 2023, or \$0.69 per diluted share, a decrease of \$445,000, or 9.9%, compared to net income of \$4.5 million, or \$0.77 per diluted share, for the nine months ended September 30, 2022. Net income for the nine months ended September 30, 2023 reflected a \$4.9 million increase in interest expense, a \$2.6 million increase in non-interest expenses and a \$408,000 decrease in non-interest income, partially offset by a \$5.9 million increase in interest income and a \$1.0 million (credit) provision for credit losses.

Interest Income. Interest income increased by \$5.9 million, or 30.4%, to \$25.1 million for the nine months ended September 30, 2023, when compared to the nine months ended September 30, 2022. Loan interest income increased by \$4.8 million, or 27.4%, to \$22.4 million for the nine months ended September 30, 2023, as compared to the prior year period primarily due to an increase in the average yield on loans and an increase in the average balance of the loan portfolio of \$32.2 million, or 6.0%, from \$537.8 million for the nine months ended September 30, 2022, to \$570.0 million for the nine months ended September 30, 2023. The increase in the average balance of the loan portfolio was primarily driven by growth in commercial real estate loans. The average yield on loans was 5.25% for the nine months ended September 30, 2023, as compared to 4.36% for the nine months ended September 30, 2022, primarily due to the impact of higher interest rates on variable rate loans, new loan originations, and portfolio composition.

Investment securities interest income decreased \$43,000, or 2.8%, to \$1.5 million for the nine months ended September 30, 2023, compared to the nine months ended September 30, 2022, primarily due to a decrease in the average balance of securities, from \$84.0 million for the nine months ended September 30, 2022, to \$70.3 million for the nine months ended September 30, 2023. This was partially offset by a 40 basis points increase in the average yield of investment securities.

Interest Expense. Interest expense increased \$4.9 million, or 325.1%, to \$6.3 million for the nine months ended September 30, 2023, compared to \$1.5 million for the nine months ended September 30, 2022, primarily due to an increase in interest paid on deposits. Interest paid on deposits increased by \$4.2 million, or 386.9%, to \$5.3 million for the nine months ended September 30, 2023, when compared to the nine months ended September 30, 2022. The increase in interest expense on deposits was primarily due to a 115 basis points increase in the average interest rate paid on deposit accounts as the deposit mix shifted towards higher cost time deposits. The average balance of deposits increased by \$13.1 million, or 2.7%, from \$474.0 million for the nine months ended September 30, 2022, to \$487.1 million for the nine months ended September 30, 2023 primarily due to an increase in the average balance of time deposits. Interest expense on borrowed funds and other interest-bearing liabilities for the nine months ended September 30, 2023 increased by \$613,000, or 154.4%, when compared to the nine months ended September 30, 2022, primarily due to a \$15.8 million increase in average borrowed funds and other interest-bearing liabilities outstanding, and a 117 basis points increase in the average rate paid on borrowings. The increase in borrowings was a result of management's strategy to add liquidity to the balance sheet as a result of economic volatility, anticipated loan growth, and increased competition for deposits in the current rising interest rate environment.

(Credit) Provision for Credit Losses. The Company recorded a \$1.0 million credit to the provision for credit losses on loans and unfunded commitments during the nine months ended September 30, 2023, as compared to a \$500,000 provision for loan losses during the nine months ended September 30, 2022. The current period (credit) provision for credit losses was primarily due to a change in the qualitative economic forecasting factor and a decrease in the loan portfolio and loan commitments during the first nine months of 2023.

Non-Interest Income. Non-interest income decreased by \$408,000, or 19.2%, to \$1.7 million for the nine months ended September 30, 2023, as compared to the nine months ended September 30, 2022. The decrease was primarily due to a \$402,000 net decrease in unrealized gains on interest rate swap products as a result of market interest rate movements and a \$52,000 loss on the sale of \$8.5 million of securities during the nine months ended September 30, 2023 to reposition the Bank's balance sheet.

Non-Interest Expense. Non-interest expense increased by \$2.6 million, or 18.8%, to \$16.6 million for the nine months ended September 30, 2023, as compared to \$14.0 million for the nine months ended September 30, 2022. Salary and employee benefits expense increased \$992,000, or 13.5%, during the first nine months of 2023 primarily due to the addition of staffing resources, annual salary increases, and an increase in employee benefits. Professional services increased by \$891,000, or 74.5%, primarily due to an increase in legal, auditing services, regulatory assessments, and consulting costs during the first nine months of 2023 associated with remediation activities related to regulatory matters. FDIC insurance expense increased by \$688,000, or 498.6%, during the first nine months of 2023 due to an increase in premium assessments. Data processing costs increased \$190,000, or 17.4%, during the first nine months of 2023 primarily due to an increase in costs related to core system maintenance and enhancements to existing IT security protocols. Advertising expense increased \$58,000, or 12.7%, primarily due to an increase in marketing costs during the first nine months of 2023. The increases were partially offset by a decrease in other costs of \$144,000, or 11.2%, primarily due to a one-time, insurance-related expense being recorded in the first nine months of 2022.

Income Taxes Expense. Income tax expense was \$838,000 for the nine months ended September 30, 2023, a decrease of \$78,000, or 8.5%, as compared to \$916,000 for the nine months ended September 30, 2022. The decrease in income tax expense was primarily due to a decrease in income before taxes, partially offset by an increase in the effective tax rate. The effective tax rate for the nine months ended September 30, 2023 and 2022 was 17.1% and 16.9%, respectively.

Liquidity and Capital Resources

Liquidity describes our ability to meet the financial obligations that arise during the ordinary course of business. Liquidity is primarily needed to fund loan commitments, to pay the deposit withdrawal requirements of our customers as well as to

fund current and planned expenditures. Our primary sources of funds consist of deposits, scheduled amortization and prepayments of loans and securities, maturities and sales of investments and loans, excess cash, interest earning deposits at other financial institutions, and funds provided from operations. We have written agreements with the FHLBNY, which allows us to borrow the maximum lending values designated by the type of collateral pledged. As of September 30, 2023, the maximum remaining amount that we can borrow from the FHLBNY, based on the market value of certain fixed-rate residential, one- to four-family loans pledged to FHLBNY, was \$3.5 million. At September 30, 2023, we had outstanding advances under this agreement of \$36.5 million. We have a written agreement with the Federal Reserve Bank discount window for overnight borrowings which is collateralized by a pledge of our securities and allows us to borrow up to the value of the securities pledged. As of September 30, 2023, we had no securities pledged to the Federal Reserve Bank and we had no balances outstanding. We have also established lines of credits with correspondent banks for \$27.0 million, of which \$25.0 million is unsecured and the remaining \$2.0 million will be secured by a pledge of our securities when a draw is made. There were no borrowings on these lines as of September 30, 2023.

As a result of the Order previously disclosed herein, the Company's ability to access available sources of funds from the FHLB has been curtailed to short-term advances (i.e., 30 days or less) and the residential loans pledged as collateral for these borrowings are subject to reductions in value. The availability of lines of credit with one other correspondent bank was terminated, while the availability of lines of credit with other correspondent banks may also be reduced or eliminated. The Bank is not eligible to access the new Bank Term Funding Program created by the Federal Reserve Board on March 12, 2023. The Bank is ineligible to participate in the program due to the Consent Order. Lastly, the unsecured line of credit for our Master Account at the Federal Reserve has been withdrawn at this time.

While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit outflows, calls of investment securities, and prepayments of loans and mortgage-backed securities are strongly influenced by interest rates, general and local economic conditions, and competition in the marketplace. These factors reduce the predictability of the timing of these sources of funds.

Our primary investing activities include the origination of loans and the purchase of investment securities. For the nine months ended September 30, 2023, we originated loans of approximately \$47.6 million as compared to approximately \$124.6 million of loans originated during the nine months ended September 30, 2022. Loan principal repayments and other deductions exceeded originations during the nine months ended September 30, 2023 by \$8.5 million. The Company did not make any purchases of investment securities during the nine months ended September 30, 2023 and purchases of investment securities totaled \$6.1 million during the nine months ended September 30, 2022. During the nine months ended September 30, 2023, the Company sold investment securities amounting to \$8.5 million. The Company did not sell any investment securities during the nine months ended September 30, 2022.

As described elsewhere in this report, the Company has loan commitments to borrowers and borrowers have unused overdraft lines of protection, unused home equity lines of credit and unused commercial lines of credit that may require funding at a future date. The Company believes it has sufficient funds to fulfill these commitments, including sources of funds available through the use of FHLBNY advances or other liquidity sources. Total deposits were \$584.2 million at September 30, 2023, as compared to \$570.1 million at December 31, 2022. Approximately \$160.4 million of time deposit accounts are scheduled to mature within one year as of September 30, 2023. Based on our deposit retention experience, and current pricing strategy, we anticipate that a significant portion of these time deposits will remain with us following their maturity.

We are committed to maintaining a strong liquidity position; therefore, we monitor our liquidity position on a daily basis. We anticipate that we will have sufficient funds to meet our current funding commitments. The marginal cost of new funding, however, whether from deposits or borrowings from the FHLBNY, will be carefully considered as we monitor our liquidity needs. Therefore, in order to manage our cost of funds, we may consider additional borrowings from the FHLBNY in the future.

We do not anticipate any material capital expenditures in 2023. We do not have any balloon or other payments due on any long-term obligations, other than the borrowing agreements noted above.

Regulatory Capital

Federal regulations require a federal savings bank to meet certain capital standards, as discussed in the “Supervision and Regulation” section included in our Annual Report on Form 10-K for the year ended December 31, 2022.

The federal banking agencies have developed a “Community Bank Leverage Ratio” (bank’s tier 1 capital to average total consolidated assets) for financial institutions with assets of less than \$10 billion and limited amounts of off-balance-sheet exposures and trading assets and liabilities. A “qualifying community bank” may elect to utilize the Community Bank Leverage Ratio in lieu of the general applicable risk-based capital requirements under Basel III. If the community bank exceeds this ratio it will be deemed to be in compliance with all other capital and leverage requirements, including the capital requirements to be considered “well capitalized” under Basel III. The federal banking agencies may consider a financial institution’s risk profile when evaluating whether it qualifies as a community bank for purposes of the capital ratio requirement. The federal banking agencies set the minimum capital for the Community Bank Leverage Ratio at 9.0%. The Bank elected to be subject to this new definition when it became effective on January 1, 2020. As of September 30, 2023, the Bank’s Community Bank Leverage Ratio was 12.49%.

Pursuant to an Individual Minimum Capital Requirement, the Bank has been directed by the OCC to maintain a Tier 1 Leverage capital ratio of 10% and a Total Risk-Based capital ratio of 13%. In order to be considered “well-capitalized” by the OCC, a savings bank must maintain a Tier 1 Leverage capital ratio of 5% and a Total Risk-Based capital ratio of 10%. At September 30, 2023, the Bank’s Tier 1 Leverage capital ratio was 12.49% and its Total Risk-Based capital ratio was 17.61% and accordingly the Bank was in compliance with its Individual Minimum Capital Requirement and was considered well-capitalized.

Off-Balance Sheet Arrangements

Other than loan commitments, we do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources that is material to investors. Refer to Note 6 in the Notes to our unaudited consolidated financial statements for a summary of loan commitments outstanding as of September 30, 2023.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Disclosure is not required as the Company is a smaller reporting company.

Item 4. Controls and Procedures.

Disclosure Controls and Procedures

The Company’s management, with the participation of its Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company’s disclosure controls and procedures (as defined in Rules 13(a)-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based upon such evaluation, the Company’s Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company’s disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting

There have not been any changes in the Company’s internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) during the quarter ended September 30, 2023 that have materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

PART II

Item 1A. Risk Factors.

In addition to the other information contained in this Quarterly Report on Form 10-Q, the following risk factors represents a material update and addition to the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2022. Additional risks not presently known to us, or that we currently deem immaterial, may also adversely affect our business, financial condition or results of operations. Further, to the extent that any of the information contained in this Quarterly Report on Form 10-Q constitutes forward-looking statements, the risk factors set forth below also are a cautionary statement identifying important factors that could cause our actual results to differ materially from those expressed in any forward-looking statements made by or on behalf of us.

The Companies have entered into an Agreement with the Federal Reserve Bank of Philadelphia. Failure to comply with the Agreement may result in further regulatory enforcement actions. We expect that our non-interest expense will increase as a result of remediation actions we will take in order to comply with the requirements of the Agreement which may adversely affect our financial performance.

Effective as of June 28, 2023, the Companies entered into an Agreement with the Federal Reserve Bank of Philadelphia (the “Reserve Bank”). The Agreement provides, among other things, that the Companies and/or their Board of Directors:

- take appropriate steps to fully utilize the Companies’ financial and managerial resources to serve as a source of strength to the Bank, including, but not limited to, taking steps to ensure that the Bank complies with the Consent Order entered into with the Office of the Comptroller of the Currency on February 9, 2023, and any other supervisory action taken by the Bank’s federal regulator;
- not, directly or indirectly, declare or pay dividends, engage in share repurchases, or make any other capital distribution in respect of common shares, preferred shares, or other capital instruments, including, without limitation, any interest payments due on subordinated debentures, without the prior written approval of the Reserve Bank and the Director of Supervision and Regulation of the Board of Governors. All requests for prior approval must be received in writing at least 30 days prior to the earlier of the proposed declaration, payment, or distribution date, or required notice of deferral;
- not, directly or indirectly, incur, increase, or guarantee any debt without the prior written approval of the Reserve Bank. All requests for prior approval must be received at least 30 days prior to the proposed transaction date;
- comply with the prior notice requirements to the Reserve Bank in accordance with applicable federal law and regulation prior to appointing any new director or senior executive officer, or changing the responsibilities of any senior executive officer so that the officer would assume a different senior executive officer position;
- comply with the restrictions on indemnification and severance payments under applicable federal law and regulation; and
- within 45 days after the end of each calendar quarter following the date of the Agreement, submit to the Reserve Bank written progress reports detailing the form and manner of all actions taken to secure compliance with the provisions of the Agreement and the results thereof.

Management and the Companies’ Board of Directors are committed to promptly addressing the action items included in the Agreement. In the event we are in material non-compliance with the terms of the Agreement, the Reserve Bank has the authority to subject us to additional enforcement actions, such as civil money penalties and removal of directors and officers from their positions with the Companies. We expect that our non-interest expense will increase as a result of remediation actions we will take in order to comply with the requirements of the Agreement which may adversely affect our financial performance.

Recent events involving the failure of financial institutions may adversely affect our business, and the market price of our common stock.

Recent developments and events in the financial services industry, including the large-scale deposit withdrawals over a short period of time at Silicon Valley Bank, Signature Bank and First Republic Bank that resulted in the failure of those institutions have resulted in decreased confidence in banks among depositors, other

counterparties and investors, as well as significant disruption, volatility and reduced valuations of equity and other securities of banks in the capital markets. These events have occurred against the backdrop of a rapidly rising interest rate environment which, among other things, has resulted in unrealized losses in longer duration securities and loans held by banks, more competition for bank deposits and may increase the risk of a potential recession. These events and developments could materially and adversely impact our business or financial condition, including through potential liquidity pressures, reduced net interest margins, and potential increased credit losses. These recent events and developments have, and could continue to, adversely impact the market price and volatility of our common stock. These recent events may also result in changes to laws or regulations governing banks, savings bank and bank and savings and loan holding companies or result in the impositions of restrictions through supervisory or enforcement activities, including higher capital requirements, which could have a material impact on our businesses. The cost of resolving the recent failures may prompt the FDIC to increase its premiums above the recently increased levels or to issue additional special assessments.

Item 2. Unregistered Sales of Equity Securities, Use of Proceeds, and Issuer Purchases of Equity Securities

The following table reports information regarding repurchases by Lake Shore Bancorp of its common stock in each month of the quarter ended September 30, 2023. The Company has suspended its stock repurchase program.

COMPANY PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet be Purchased Under the Plans or Programs ⁽¹⁾
July 1 through July 31, 2023	—	\$ —	—	30,626
August 1 through August 31, 2023	—	—	—	30,626
September 1 through September 30, 2023	—	—	—	30,626
Total	—	\$ —	—	30,626

- ⁽¹⁾ On August 13, 2021, our Board of Directors (the “Company”) adopted a new stock repurchase program. The stock repurchase program authorizes the Company to repurchase up to an aggregate of 106,327 shares, or approximately 5% of its outstanding shares, excluding the shares held by Lake Shore, MHC. The repurchase program permits shares to be repurchased in open market or private transactions, through block trades, and pursuant to any trading plan that may be adopted in accordance with Rule 10b5-1 of the Securities and Exchange Commission. The repurchase plan does not have an expiration date and superseded all of the prior stock repurchase programs.

Item 6. Exhibits

31.1	<u>Certification by the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*</u>
31.2	<u>Certification by the Chief Financial Officer Pursuant to Section 302 of the Sarbanes- Oxley Act of 2002*</u>
32.1	<u>Certification by the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*</u>
32.2	<u>Certification by the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*</u>
101.INS	Inline XBRL Instance Document*
101.SCH	Inline XBRL Taxonomy Extension Schema Document*
101.CAL	Inline XBRL Taxonomy Calculation Linkbase Document*
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document*
101.LAB	Inline XBRL Taxonomy Label Linkbase Document*
101.PRE	Inline XBRL Taxonomy Presentation Linkbase Document*
104	Cover Page Interactive Data File (formatted as inline XBRL and contained in Exhibit 101)*

* Filed herewith.

SIGNATURES

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

LAKE SHORE BANCORP, INC.

(Registrant)

November 13, 2023

By: /s/ Kim C. Liddell
Kim C. Liddell
President and Chief Executive Officer
(Principal Executive Officer)

November 13, 2023

By: /s/ Taylor M. Gilden
Taylor M. Gilden
Chief Financial Officer
(Principal Financial and Accounting Officer)

**CERTIFICATION
PURSUANT TO 17 CFR 240.13a-14
PROMULGATED UNDER
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Kim C. Liddell, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lake Shore Bancorp, 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 consolidated financial statements, and other financial information included in this report, fairly present in all material respects the consolidated 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 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 consolidated 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 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 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 or material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial data; 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.

November 13, 2023

/s/ Kim C. Liddell

Kim C. Liddell

President and Chief Executive Officer

**CERTIFICATION
PURSUANT TO 17 CFR 240.13a-14
PROMULGATED UNDER
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Taylor M. Gilden, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lake Shore Bancorp, 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 consolidated financial statements, and other financial information included in this report, fairly present in all material respects the consolidated 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 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 consolidated 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 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 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 or material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial data; 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.

November 13, 2023

/s/ Taylor M. Gilden
Taylor M. Gilden
Chief Financial Officer

**CERTIFICATE 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 Quarterly Report of Lake Shore Bancorp, Inc. (the “Company”) on Form 10-Q for the quarter ended September 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Kim C. Liddell, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- 1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and
- 2) The information contained in the Report fairly presents, in all material respects, the consolidated financial condition and results of operations of the Company as of the dates and for the periods covered by the Report.

November 13, 2023

/s/ Kim C. Liddell

Kim C. Liddell

President and Chief Executive Officer

**CERTIFICATE 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 Quarterly Report of Lake Shore Bancorp, Inc. (the “Company”) on Form 10-Q for the quarter ended September 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Taylor M. Gilden, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- 1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and
- 2) The information contained in the Report fairly presents, in all material respects, the consolidated financial condition and results of operations of the Company as of the dates and for the periods covered by the Report.

November 13, 2023

/s/ Taylor M. Gilden
Taylor M. Gilden
Chief Financial Officer
