CHINA AUTOMOTIVE SYSTEMS INC
Form 10-Q/A
June 24, 2011

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

FORM 10-Q/A
Amendment No. 1

(Mark one)
x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2010

Or

¨ TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ________ to _________

Commission file number: 000-33123

China Automotive Systems, Inc.
(Exact name of registrant as specified in its charter)

Delaware	33-0885775
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification number)

No. 1 Henglong Road, Yu Qiao Development Zone, Shashi District,
Jing Zhou City, Hubei Province, People's Republic of China
(Address of principal executive offices)

Issuer's telephone number: (86) 716- 832- 9196

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ¨ No x

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

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

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer (Do not check if a smaller reporting company)	Smaller reporting company x

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

As of June 24, 2011, the Company had 28,083,534 shares of common stock issued and outstanding.

CHINA AUTOMOTIVE SYSTEMS, INC.

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EXPLANATORY NOTE
Restatement of Consolidated Financial Statements

On March 17, 2011, China Automotive Systems, Inc. (the "Company") announced that it had identified historical accounting errors relating to the accounting treatment of the Company's convertible notes issued on February 15, 2008 (the "Convertible Notes"). The accounting errors have resulted in the misstatement of certain charges arising from fair value adjustments and other changes to derivative liabilities since the first quarter of 2009. The Company has no evidence that the errors resulted from any fraud or intentional misconduct.

The Company undertook a review to determine the total amount of the errors and the accounting periods in which the errors occurred. The Company's review determined that the errors resulted from the Company's failure to properly apply the requirements of Accounting Standard Codification (ASC) 815 ("ASC 815"), which changed the accounting treatment of convertible notes effective January 1, 2009. Additionally, management also indentified accounting errors in accumulated depreciation and deferred tax assets reported and accrued payroll and related costs. These flaws represented material weaknesses in the Company's internal controls over financial reporting as of June 30, 2010, such as accounting error on compound embedded derivative financial instruments, which were mentioned in this amended quarterly report on Form 10-Q/A. Management identified the accounting errors in connection with the 2010 annual audit procedures undertaken by the Company's newly engaged independent registered public accounting firm, PricewaterhouseCoopers Zhong Tian CPAs Limited Company.

The Company's review was overseen by the audit committee of the board of directors of the Company (the "Audit Committee") with the assistance of management and accounting consultants engaged by management. The Audit Committee concluded on March 12, 2011 that the Company's previously issued audited consolidated financial statements as of and for the fiscal year ended December 31, 2009, and related auditors' report, and unaudited interim consolidated financial statements as of and for the quarterly periods ended March 31, June 30 and September 30, 2010 and 2009, should no longer be relied upon because of these errors in the financial statements. The Company's board of directors agreed with the Audit Committee's conclusions. After analyzing the size and timing of the errors, the Company determined that, in the aggregate, the errors were material and would require the Company to restate certain of its previously issued financial statements.

As more fully described in Note 2 to the accompanying restated consolidated financial statements for the three-month and six-month periods ended June 30, 2010 and 2009, the Company has restated its consolidated financial statements and the related disclosures for the three-month and six-month periods ended June 30, 2010 and 2009. Specifically, the Company has restated its consolidated balance sheets and the related consolidated statements of income, statements of stockholders' equity and statements of cash flows as of and for the three-month and six-month periods ended June 30, 2010 and 2009. The accompanying Management's Discussion and Analysis of Financial Condition and Results of Operations in Part I, Item 2, has been updated to reflect the effects of the restatement.

The effect of the adjustments included: (a) increases of $19,065,537 and $4,623,917, respectively, in net income attributable to parent company for the three-month and six-month periods ended June 30, 2010, including increases of $19,492,871 and $5,191,461, respectively, resulting from the gain on the change in fair value of derivative liabilities, and increases of $427,334 and $567,544 from adjustments to financial expenses related to the Convertible Notes; and (b) increases of $1,195,476 and decreases of $545,474, respectively, in net income attributable to parent company for the three-month and six-month periods ended June 30, 2009, including increases of $977,435 and $4,907,462, respectively, resulting from the gain on the change in fair value of derivative liabilities, and an increase of $218,041 and decrease of $5,452,936 from adjustments to financial expenses related to the Convertible Notes.

Except as discussed above, the Company has not modified or updated disclosures presented in its quarterly report on Form 10-Q for the three-month period ended June 30, 2010 filed with the Securities and Exchange Commission on August 9, 2010 (the "Original Filing"), except as required to reflect the effects of the restatement. Accordingly, this amended quarterly report does not reflect events occurring after the Original Filing or modify or update those disclosures affected by subsequent events, except as specifically referenced herein. Information not affected by the restatement is unchanged and reflects the disclosures made at the time of the Original Filing. References to this "quarterly report on Form 10-Q," this "quarterly report on Form 10-Q/A" and this "amended quarterly report on Form 10-Q/A" herein shall refer to the Original Filing as amended by this amended quarterly report on Form 10-Q/A. The following items have been amended as a result of the restatement:

Part I	Item 1.	Financial Statements and Supplementary Data;
Part I	Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations;
Part I	Item 1A.	Risk Factors
Part II	Item 4.	Controls and Procedures; and
Part II	Item 6.	Exhibits, Financial Statement Schedules.

Cautionary Statement

This Amendment No. 1 to the Quarterly Report on Form 10-Q/A contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. These statements relate to future events or the Company's future financial performance. The Company has attempted to identify forward-looking statements by terminology including "anticipates," "believes," "expects," "can," "continue," "co "estimates," "expects," "intends," "may," "plans," "potential," "predict," "should" or "will" or the negative of these ter comparable terminology. Such statements are subject to certain risks and uncertainties, including the matters set forth in this report or other reports or documents the Company files with the Securities and Exchange Commission from time to time, which could cause actual results or outcomes to differ materially from those projected. Although the Company believes that the expectations reflected in the forward-looking statements are reasonable, the Company cannot guarantee future results, levels of activity, performance or achievements. Undue reliance should not be placed on these forward-looking statements which speak only as of the date hereof. The Company's expectations are as of the date this Form 10-Q/A is filed, and the Company does not intend to update any of the forward-looking statements after the date this amended quarterly report on Form 10-Q/A is filed to confirm these statements to actual results, unless required by law.

PART 1 — FINANCIAL INFORMATION

Item 1. Financial Statements

China Automotive Systems, Inc.

Condensed Consolidated Statements of Operations (Unaudited)

	Three Months Ended June 30,	
	2010 (As Restated-Note 2)	2009 (As Restated-Note 2)
Net product sales, including $2,941,718 and $1,314,247 to related parties for the three months ended June 30, 2010 and 2009	$ 85,081,138	$ 62,484,279
Cost of product sold, including $5,248,896 and $2,812,741 purchased from related parties for the three months ended June 30, 2010 and 2009	65,270,878	46,178,351
Gross profit	19,810,260	16,305,928
Add: Gain on other sales	681,999	172,747
Less: Operating expenses-		
Selling expenses	2,903,125	1,620,497
General and administrative expenses	1,846,421	2,246,330
R&D expenses	1,741,405	444,226
Depreciation and amortization	288,352	507,341
Total Operating expenses	6,779,303	4,818,394
Income from operations	13,712,956	11,660,281
Add: Other income, net (note 23)	250,851	-
Financial income (expenses) net (note 24)	(840,683)	(260,187)
Gain on change in fair value of derivative (note 25)	19,587,135	—
Income before income taxes	32,710,259	11,400,094
Less: Income taxes (note 26)	2,291,292	1,474,618
Net income	$ 30,418,967	$ 9,925,476
Net income attributable to noncontrolling interest	2,811,362	2,653,651
Net income attributable to parent company	$ 27,607,605	$ 7,271,825
Allocation to convertible notes holders	(3,734,882)	(1,010,017)
Net income (loss) attributable to parent company’s common shareholders	$ 23,872,723	$ 6,261,808
Net income (loss) attributable to parent company’s common shareholders per share –		
Basic (note 27)	$ 0.88	$ 0.23
Diluted (note 27)	$ 0.28	$ 0.23
Weighted average number of common shares outstanding –		
Basic	27,075,607	26,983,244
Diluted	31,562,479	27,042,087

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

China Automotive Systems, Inc.
Condensed Consolidated Statements of Operations (Unaudited)

	Six Months Ended June 30,			
	2010		2009	
	(As Restated-Note 2)		(As Restated-Note 2)	
Net product sales, including $4,602,111 and $1,873,258 to related parties for the six months ended June 30, 2010 and 2009	$169,313,827	$	107,181,725	
Cost of product sold, including $9,596,184 and $4,986,222 purchased from related parties for the six months ended June 30, 2010 and 2009	126,968,550		79,972,452	
Gross profit	42,345,277		27,209,273	
Add: Gain on other sales	1,133,609		239,626	
Less: Operating expenses-				
Selling expenses	4,770,928		2,685,177	
General and administrative expenses	5,451,205		4,048,032	
R&D expenses	3,043,163		884,148	
Depreciation and amortization	610,145		1,078,754	
Total Operating expenses	13,875,441		8,696,111	
Income from operations	29,603,445		18,752,788	
Add: Other income, net (note 23)	266,379		-	
Financial income (expenses) net (note 24)	(1,348,904)		(6,370,644	)
Gain on change in fair value of derivative (note 25)	5,434,753		2,369,179	
Income before income taxes	33,955,673		14,751,323	
Less: Income taxes (note 26)	4,576,814		2,924,288	
Net income	$29,378,859	$	11,827,035	
Net income attributable to noncontrolling interest	5,877,705		4,037,348	
Net income attributable to parent company	$23,501,154	$	7,789,687	
Allocation to convertible notes holders	(3,180,834)		(1,144,465	)
Net income (loss) attributable to parent company's common shareholders	$20,320,320	$	6,645,222	
Net income (loss) attributable to parent company's common shareholders per share –				
Basic (note 27)	$0.75	$	0.25	
Diluted (note 27)	$0.62	$	0.25	
Weighted average number of common shares outstanding –				
Basic	27,060,925		26,983,244	
Diluted	31,558,848		27,012,665	

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

China Automotive Systems, Inc.
Condensed Consolidated Statements of Comprehensive Income (Unaudited)

	Three Months Ended June 30,	
	2010 (As Restated-Note 2)	2009 (As Restated-Note 2)
Net income	$ 30,418,967	$ 9,925,476
Other comprehensive income:		
Foreign currency translation gain (loss)	880,895	(187,728)
Comprehensive income	$ 31,299,862	$ 9,737,748
Comprehensive income attributable to non-controlling interest	2,955,278	2,667,215
Comprehensive income attributable to parent company	$ 28,344,584	$ 7,070,533

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

China Automotive Systems, Inc.
Condensed Consolidated Statements of Comprehensive Income (Unaudited)

	Six Months Ended June 30,	
	2010 (As Restated-Note 2)	2009 (As Restated-Note 2)
Net income	$29,378,859	$ 11,827,035
Other comprehensive income:		
Foreign currency translation gain (loss)	926,151	(202,314)
Comprehensive income	$30,305,010	$ 11,624,721
Comprehensive income attributable to non-controlling interest	6,029,175	4,046,488
Comprehensive income attributable to parent company	$24,275,835	$ 7,578,233

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

China Automotive Systems, Inc.
Condensed Consolidated Balance Sheets

	June 30, 2010 (As Restated-Note 2) (Unaudited)	December 31, 2009 (As Restated-Note 2)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 45,246,219	$ 43,480,176
Pledged cash deposits (note 4)	19,340,337	12,742,187
Accounts and notes receivable, net, including $3,386,976 and $1,441,939 from related parties at June 30, 2010 and December 31, 2009 (note 5)	180,688,519	154,863,292
Advance payments and other, including $930,007 and $0 to related parties at June 30, 2010 and December 31, 2009	3,246,037	2,413,556
Inventories (note 7)	39,595,346	27,415,697
Current deferred tax assets (note 10)	4,185,875	3,866,353
Total current assets	$ 292,302,333	$ 244,781,261
Long-term Assets:		
Property, plant and equipment, net (note 8)	$ 60,673,902	$ 58,529,447
Intangible assets, net (note 9)	506,158	561,389
Other receivables, net, including $218,699 and $65,416 from related parties at June 30, 2010 and December 31, 2009 (note 6)	1,644,413	1,064,224
Advance payments for property, plant and equipment, including $5,676,085 and $2,579,319 to related parties at June 30, 2010 and December 31, 2009	13,508,244	6,369,043
Long-term investments	79,518	79,084
Non-current deferred tax assets (note 10)	3,111,251	2,998,124
Total assets	$ 371,825,819	$ 314,382,572
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Bank loans (note 11)	$ 8,835,353	$ 5,125,802
Accounts and notes payable, including $2,570,035 and $1,537,827 to related parties at June 30, 2010 and December 31, 2009 (note 12)	136,129,101	107,495,833
Convertible Notes payable (note 13)	30,000,000	30,000,000
Compound derivative liabilities (note 14)	40,008,753	45,443,506
Customer deposits	2,370,888	1,918,835
Accrued payroll and related costs	4,568,567	4,578,446
Accrued expenses and other payables(note 15)	20,920,549	22,472,452
Accrued pension costs (note 16)	3,814,440	3,778,187
Taxes payable (note 17)	10,700,504	11,482,177
Amounts due to shareholders/directors (note 18)	112,209	-
Total current liabilities	$ 257,460,364	$ 232,295,238
Long-term liabilities:		
Other long-term liabilities (note 19)	4,986,459	233,941
Total liabilities	$ 262,446,823	$ 232,529,179
Significant concentrations (note 28)		
Related party transactions (note 29)		
Commitments and contingencies (note 30)		

Stockholders' equity:				
Preferred stock, $0.0001 par value - Authorized - 20,000,000 shares Issued and outstanding – None	$	–	$	–
Common stock, $0.0001 par value - Authorized - 80,000,000 shares Issued and Outstanding – 27,110,693 and 27,046,244 shares at June 30, 2010 and December 31, 2009 (note 20)		2,711		2,704
Additional paid-in capital (note 20)		28,024,559		27,515,064
Retained earnings- (note 22)				
Appropriated		8,767,797		8,324,533
Unappropriated		30,742,892		7,685,002
Accumulated other comprehensive income		11,962,414		11,187,733
Total parent company stockholders' equity		79,500,373		54,715,036
Non-controlling interests (note 21)		29,878,623		27,138,357
Total stockholders' equity	$	109,378,996	$	81,853,393
Total liabilities and stockholders' equity	$	371,825,819	$	314,382,572

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

China Automotive Systems, Inc. and Subsidiaries
Consolidated Statements of Stockholders’ Equity
Period Ended June 30, 2010 (Unaudited) and December 31, 2009

	Common Stock	Additional Paid-in Capital	Retained Earnings Appropriated	Retained Earnings Unappropriated	Accumulated Other Comprehensive Income (Loss)	Total parent company stockholders ' Equity	Non-controlling interests	stoc E
Balance at January 1, 2009 restated	$ 2,698	$ 26,648,154	$ 7,525,777	$ 34,060,876	$ 11,127,505	$ 79,365,010	$ 23,270,820	$ 102
Accumulated effect of adoption of ASC 815-40 (note 23)	–	–	–	863,753	—	863,753	—	
Balance at January 1,2009 as further restated	2,698	26,648,154	7,525,777	34,924,629	11,127,505	80,228,763	23,270,820	103
Foreign currency translation gain	–	–	–	–	60,228	60,228	22,410	
Shares issued for stock options exercised	6	420,234	–	–	–	420,240	–	
Share-based compensation	-	446,676	–	–	–	446,676	–	
Appropriation of retained earnings	-	-	798,756	(798,756)	–	–	(3,944,619)	(3
Net income for the year ended December 31, 2009	–	–	–	(26,440,871)	–	(26,440,871)	7,789,746	(18
Balance at December 31, 2009 restated	$ 2,704	$ 27,515,064	$ 8,324,533	$ 7,685,002	$ 11,187,733	$ 54,715,036	$ 27,138,357	$ 81
Foreign currency translation gain	–	–	–	–	774,681	774,681	151,470	
Shares issued for stock options	7	259,469	–	–	–	259,476	–	

exercised								
Share-based compensation	–	250,026	–	–	–	250,026	–	
Appropriation of retained earnings	–	–	443,264	(443,264)	–	–	(3,288,909)	(3
Net income for the period ended June 30, 2010	–	–	–	23,501,154	–	23,501,154	5,877,705	29
Balance at June 30, 2010 restated	$ 2,711	28,024,559	8,767,797	30,742,892	11,962,414	79,500,373	29,878,623	109

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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China Automotive Systems, Inc.
Condensed Consolidated Statements of Cash Flows (Unaudited)

	Six Months Ended June 30, 2010 (As Restated-Note 2)	2009 (As Restated-Note 2)
Cash flows from operating activities:		
Net income	$29,378,859	$11,827,035
Adjustments to reconcile net income from continuing operations to net cash provided by operating activities:		
Stock-based compensation	250,026	125,013
Depreciation and amortization	4,909,679	3,886,332
Allowance for doubtful accounts (Recovered)	(599,863)	(1,117,881)
Deferred income taxes assets	(392,613)	(253,521)
Amortization for discount of Convertible Note payable	—	3,891,148
(Gain) loss on change in fair value of derivative	(5,434,753)	(2,369,179)
Other operating adjustments	14,275	(227,474)
Changes in operating assets and liabilities:		
(Increase) decrease in:		
Pledged deposits	(6,521,746)	(1,537,010)
Accounts and notes receivable	(24,024,295)	(23,776,920)
Advance payments and other	(814,827)	(813,196)
Inventories	(11,987,567)	(171,352)
Accounts and notes payable	27,953,517	19,639,466
Customer deposits	448,291	21,744
Accrued payroll and related costs	(35,015)	170,135
Accrued expenses and other payables	1,517,959	3,580,979
Accrued pension costs	15,083	(13,754)
Taxes payable	(852,725)	2,901,849
Net cash provided by operating activities	$13,824,285	$15,763,414
Cash flows from investing activities:		
(Increase) decrease in other receivables	(830,493)	(55,386)
Cash received from equipment sales	374,399	458,950
Cash paid to acquire property, plant and equipment	(14,134,717)	(6,341,035)
Cash paid to acquire intangible assets	(38,498)	(321,671)
Net cash (used in) investing activities	$(14,629,309)	$(6,259,142)
Cash flows from financing activities:		
Proceeds from bank loans	3,685,215	1,465,006
Dividends paid to the non-controlling interest holders of Joint-venture companies	(1,744,982)	(3,768,668)
Repayment of Convertible Note payable	-	(5,000,000)
Shares issued for stock options exercised	259,476	-
Increase in amounts due to shareholders/directors	110,271	226,717
Net cash provided by (used in) financing activities	$2,309,980	$(7,076,945)
Cash and cash equivalents affected by foreign currency	$261,087	$14,607
Net increase in cash and cash equivalents	1,766,043	2,441,934
Cash and cash equivalents at beginning of period	43,480,176	37,113,375
Cash and cash equivalents at end of period	$45,246,219	$39,555,309

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

China Automotive Systems, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited) (continued)

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

	Six Months Ended June 30,	
	2010	2009
Cash paid for interest	$ 407,296	$ 989,247
Cash paid for income taxes	$ 3,972,306	$ 1,403,715

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

China Automotive Systems, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
Three Months and Six Months Ended June 30, 2010 and 2009

1. Organization and Business

China Automotive Systems, Inc., “China Automotive”, was incorporated in the State of Delaware on June 29, 1999 under the name Visions-In-Glass, Inc. China Automotive, including, when the context so requires, its subsidiaries and the subsidiaries’ interests in the Sino-foreign joint ventures described below, is referred to herein as the “Company”. The Company is primarily engaged in the manufacture and sale of automotive systems and components, as described below.

Great Genesis Holdings Limited, a company incorporated on January 3, 2003 under The Companies Ordinance in Hong Kong as a limited liability company, “Genesis”, is a wholly-owned subsidiary of the Company.

Henglong USA Corporation, “HLUSA”, incorporated on January 8, 2007 in Troy, Michigan, is a wholly-owned subsidiary of the Company, and mainly engages in marketing of automotive parts in North America, and provides after sales service and research and development support accordingly.

The Company owns the following aggregate net interests in nine Sino-foreign joint ventures organized in the PRC as of June 30, 2010 and 2009.

	Percentage Interest			
Name of Entity	June 30, 2010		June 30, 2009	
Shashi Jiulong Power Steering Gears Co., Ltd., “Jiulong”	81.00	%	81.00	%
Jingzhou Henglong Automotive Parts Co., Ltd., “Henglong”	80.00	%	80.00	%
Shenyang Jinbei Henglong Automotive Steering System Co., Ltd., “Shenyang”	70.00	%	70.00	%
Zhejiang Henglong & Vie Pump-Manu Co., Ltd., “Zhejiang”	51.00	%	51.00	%
Universal Sensor Application Inc., “USAI”	83.34	%	83.34	%
Wuhan Jielong Electric Power Steering Co., Ltd., “Jielong”	85.00	%	85.00	%
Wuhu HengLong Automotive Steering System Co., Ltd., “Wuhu”	77.33	%	77.33	%
Jingzhou Hengsheng Automotive System Co., Ltd, “Hengsheng”	100.00	%	100.00	%
Jingzhou Henglong Automotive Technology (Testing) Center, “Testing Center”	80.00	%	-	%

Jiulong was established in 1993 and mainly engages in the production of integral power steering gear for heavy-duty vehicles.

Henglong was established in 1997 and mainly engages in the production of rack and pinion power steering gear for cars and light duty vehicles.

In December 2009, Henglong, a subsidiary of Genesis, formed Jingzhou Henglong Automotive Technology (Testing) Center, “Testing Center”, which is mainly engaged in research and development of new products. The registered capital of Testing Center is RMB 30,000,000 ($4,393,544 equivalent).

Shenyang was established in 2002 and focuses on power steering parts for light duty vehicles.

Zhejiang was established in 2002 to focus on power steering pumps.

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USAI was established in 2005 and mainly engages in production and sales of sensor modulars.

Jielong was established in 2006 and mainly engages in production and sales of electric power steering, “EPS”.

Wuhu was established in 2006 and mainly engages in production and sales of automobile steering systems.

Hengsheng was established in 2007 and mainly engages in production and sales of automobile steering systems.

On February 11, 2010, the registered capital of Hengsheng was increased to $16,000,000 from $10,000,000.

On January 24, 2010, Genesis entered into a sino-foreign equity joint venture contract with Beijing Hainachuan Auto Parts Co., Ltd., to establish a sino-foreign joint venture company, Beijing Henglong Automotive System Co., Ltd., “Beijing Henglong”, to design, develop and manufacture both hydraulic and electric power steering systems and parts. Under PRC laws, the establishment of Beijing Henglong and the effectiveness of the equity joint venture contract are subject to approval by the local Ministry of Commerce and the registration of the same with the local Administration of Industries and Commerce in Beijing.

2. Restatement

The Company has restated its previously issued consolidated financial statements for the six months ended June 30, 2010 and 2009, for matters related to the following previously reported items: financial expenses and accrued interest; gain (loss) on the change in fair value of derivative liabilities; and derivative liabilities. The financial data set forth below as for the six months ended June 30, 2010 and 2009 have been restated to reflect those corrections. Also, retained earning and minority equity as at January 1, 2009, reduced by $1,965,640 and $48,254, respectively, as a result of adjustments to accumulated depreciation and deferred tax assets previously reported and previously unrecorded financial expenses in 2008.

Following is a summary of adjustments resulting from on the restatement for the three and six months ended June 30, 2010 (unaudited):

	Three Months Ended June 30, 2010	Six Months Ended June 30, 2010
Increase of previously reported financial expense	$ (427,334)	$ (567,544)
Increase of previously reported gain on change in fair value of derivative liabilities	$ 19,492,871	$ 5,191,461
Subtotal	19,065,537	4,623,917
Deferred tax assets related to accrued interest of Convertible Notes*	186,959	273,285
Valuation allowance*	(186,959)	(273,285)
Total increase in net earnings for the three and six months ended June 30, 2010	$ 19,065,537	$ 4,623,917

*The Company accrued valuation allowance against its deferred tax assets while it accrued and restated loss related to deferred income tax income.

Following is a summary of adjustment on the restatement for the three and six months ended June 30, 2009 (unaudited):

	Three Months Ended June 30, 2009	Six Months Ended June 30, 2009
Increase of previously reported financial expense, increase of related liabilities (Convertible Notes payable, accrued interest)	$ 218,041	$ (5,452,936)
Increase of previously reported gain on change in fair value of derivative liabilities, decrease of derivative liabilities	$ 977,435	$ 4,907,462
Subtotal	1,195,476	(545,474)
Deferred tax assets related to accrued interest of Convertible Notes*	58,309	724,070
Valuation allowance*	(58,309)	(724,070)
Total reduction in the three and six months ended June 30, 2009 net earnings	$ 1,195,476	$ (545,474)

*the Company accrued valuation allowance against its deferred tax assets while it accrued and restated loss related to deferred income tax income.

Due to the adjustments to restate the 2009 financial statements, the effect brought forward to the Company's previously issued balance sheet as of June 30, 2010 (unaudited) is summarized as follows:

	Previously Reported	Increase (Decrease)	Restated
Current Assets:			
Current deferred tax assets(a)	$2,617,570	$1,568,305	$4,185,875
Total current assets	290,734,028	1,568,305	292,302,333
Long-term Assets:			
Property, plant and equipment, net(b)	62,645,020	(1,971,118)	60,673,902
Non-current deferred tax assets(c)	1,351,409	1,759,842	3,111,251
Total Assets	370,468,790	1,357,029	371,825,819
Current Liabilities:			
Convertible notes payable(d)	28,854,024	1,145,976	30,000,000
Compound derivative liabilities(e)	636,717	39,372,036	40,008,753
Accrued payroll and related costs(f)	3,022,380	1,546,187	4,568,567
Accrued expenses and other payables(g)	15,375,965	5,544,584	20,920,549
Taxes payable(h)	10,582,698	117,806	10,700,504
Total current liabilities	209,733,775	47,726,589	257,460,364
Total Liabilities	214,720,234	47,726,589	262,446,823
Stockholders' equity			
Retained earnings-			
Unappropriated- January 1, 2009	36,026,516	(1,965,640)	34,060,876
Accumulated effect of adoption of ASC 815-40	—	863,753	863,753
Net income attributable to parent company- December 31, 2008	23,414,263	(49,855,134)	(26,440,871)
Unappropriated-December 31, 2009	58,642,023	(50,957,021)	7,685,002
Net income attributable to parent company- June 30, 2010	18,877,237	4,623,917	23,501,154
Unappropriated-June 30, 2010 (unaudited)	77,075,996	(46,333,104)	30,742,892

Accumulated other comprehensive income-December 31, 2009	11,187,744	(11)	11,187,733
Foreign currency translation gain –June 30, 2010 (unaudited)	776,167	(1,486)	774,681
Accumulated other comprehensive income- June 30, 2010 (unaudited)	11,963,911	(1,497)	11,962,414
Total parent company stockholders' equity	125,834,974	(46,334,601)	79,500,373
Non-controlling interests - January 1, 2009	23,222,566	48,254	23,270,820
Net income attributable to noncontrolling interest- December 31, 2009	7,872,813	(83,067)	7,789,746
Foreign currency translation gain (loss) - December 31, 2009	22,365	45	22,410
Non-controlling interests- December 31, 2009	27,173,125	(34,768)	27,138,357
Foreign currency translation gain – June 30, 2010 (unaudited)	151,661	(191)	151,470
Non-controlling interests- June 30, 2010 (unaudited)	29,913,582	(34,959)	29,878,623
Total stockholders' equity	155,748,556	(46,369,560)	109,378,996
Total liabilities and stockholders' equity	$370,468,790	$1,357,029	$371,825,819

(a) The adjustment represents the deferred tax assets arising from the provision for doubtful debt, prepaid income tax for unrealized profits for intra-group purchase and sale, accrued labour cost and accrued interest on the convertible notes payable, which were not previously accounted for.

(b) The adjustment represents the accumulated depreciation by which the depreciation expenses were understated in prior years.

(c) The adjustment represents the deferred tax assets arising from the timing difference associated with the depreciation expenses as noted in (b) above.

(d) The adjustment is to accrete the convertible note payable to its full face value in fiscal 2009 upon the WAP default.

(e) The adjustment represents valuation of the embedded derivative at its fair value as of December 31, 2009.

(f) The adjustment is to accrue the payroll and bonus expenses of certain of the Company's joint venture subsidiaries which were previously recorded under cash basis.

(g) The adjustment represents the make-whole redemption amount on the convertible note payable.

(h) The adjustment represents the withholding tax levied on dividends distributed by domestic companies to their foreign investors when the dividends are remitted out of China.

Statement of operations data for the six months ended June 30, 2010 (unaudited):

	Previously Reported	Increase (Decrease)	Restated
Financial income (expenses)	$(781,360)	$(567,544)	$(1,348,904)
Gain (loss) on change in fair value of derivative	243,292	5,191,461	5,434,753
Income (loss) before income taxes	29,331,756	4,623,917	33,955,673
Net income (loss)	24,754,942	4,623,917	29,378,859
Net income (loss) attributable to parent company	$18,877,237	$4,623,917	$23,501,154

Statement of operations data for the three months ended June 30, 2010 (unaudited):

	Previously Reported	Increase (Decrease)	Restated
Financial income (expenses)	$(413,349)	$(427,334)	$(840,683)
Gain (loss) on change in fair value of derivative	94,264	19,492,871	19,587,135
Income (loss) before income taxes	13,644,722	19,065,537	32,710,259
Net income (loss)	11,353,430	19,065,537	30,418,967
Net income (loss) attributable to parent company	$8,542,068	$19,065,537	$27,607,605

Statement of operations data for the six months ended June 30, 2009 (unaudited):

	Previously Reported	Increase (Decrease)	Restated
Financial income (expenses)	$(917,708)	$(5,452,936)	$(6,370,644)
Gain (loss) on change in fair value of derivative	(2,538,283)	4,907,462	2,369,179
Income (loss) before income taxes	15,296,797	(545,474)	14,751,323
Net income (loss)	12,372,509	(545,474)	11,827,035
Net income (loss) attributable to parent company	$8,335,161	$(545,474)	$7,789,687

Statement of operations data for the three months ended June 30, 2009 (unaudited):

	Previously Reported	Increase (Decrease)	Restated
Financial income (expenses)	$(478,228)	$218,041	$(260,187)
Gain (loss) on change in fair value of derivative	(977,435)	977,435	—
Income (loss) before income taxes	10,204,618	1,195,476	11,400,094
Net income (loss)	8,730,000	1,195,476	9,925,476
Net income (loss) attributable to parent company	$6,076,349	$1,195,476	$7,271,825

3. Basis of Presentation and Significant Accounting Policies

(a) Basis of Presentation

Basis of Presentation - For the three months and six months ended June 30, 2010 and 2009, the accompanying unaudited consolidated financial statements include the accounts of the Company and its subsidiaries. The subsidiaries include nine Sino-foreign Joint-ventures mentioned in Note 1. Significant inter-company balances and transactions have been eliminated upon consolidation. The unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America.

Comments - The accompanying interim condensed consolidated financial statements are unaudited, but in the opinion of the Company's management, contain all adjustments, which include normal recurring adjustments, necessary to present fairly the financial position, the results of operations and cash flows for the three months and six months ended June 30, 2010 and 2009 respectively.

The consolidated balance sheet as of December 31, 2009 is derived from the Company's audited financial statements.

Certain information and footnote disclosures normally included in financial statements that have been prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission, although the Company's management believes that the disclosures contained in these financial statements are adequate to make the information presented therein not misleading. For further information, refer to the financial statements and the notes thereto included in the Company's 2009 Annual Report on Form 10-K, as filed with the Securities and Exchange Commission.

The results of operations for the six months ended June 30, 2010 are not necessarily indicative of the results of operations to be expected for the full fiscal year ending December 31, 2010.

Estimation -The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(b) Recent Accounting Pronouncements

In June 2008, the FASB's Emerging Issues Task Force reached a consensus regarding ASC 815-40 (formerly EITF 07-5), "Determining Whether an Instrument (or Embedded Feature) Is Indexed to an Entity's Own Stock" (ASC 815-40, formerly EITF 07-5). ASC 815-40 (formerly EITF 07-5) outlines a two-step approach to evaluate the instrument's contingent exercise provisions, if any, and to evaluate the instrument's settlement provisions when determining whether an equity-linked financial instrument (or embedded feature) is indexed to an entity's own stock. ASC 815-40 (formerly EITF 07-5) is effective for fiscal years beginning after December 15, 2008 and must be applied to outstanding instruments as of the beginning of the fiscal year of adoption as a cumulative-effect adjustment to the opening balance of retained earnings. Early adoption is not permitted. The adoption of EITF 07-5 had a material impact on the Company's consolidated financial statements.

In June 2009, the Financial Accounting Standards Board (FASB) approved the "FASB Accounting Standards Codification" ("Codification", "FASB ASC") as the single source of authoritative generally accepted accounting principles (GAAP) and created a new Topic 105, Generally Accepted Accounting Principles , in the General Principles and Objective Section of the Codification. Topic 105 is effective for interim and annual periods ending after September 15, 2009, and its adoption did not have an impact on the Company's financial condition or results of operations.

In October 2009, the FASB issued ASU No. 2009-13, Revenue Recognition (ASC Topic 605) - Multiple-Deliverable Revenue Arrangements, a consensus of the FASB Emerging Issues Task Force. This guidance modifies the fair value requirements of ASC subtopic 605-25, Revenue Recognition-Multiple Element Arrangements by allowing the use of the "best estimate of selling price" in addition to vendor-specific objective evidence (VSOE) and verifiable objective evidence (VOE) (now referred to as TPE standing for third-party evidence) for determining the selling price of a deliverable. A vendor is now required to use its best estimate of the selling price when VSOE or TPE of the selling price cannot be determined. This update is effective for fiscal years beginning on or after June 15, 2010. However, early adoption is allowed. The Company has adopted this guidance. The adoption of this guidance did not have a material impact on the Company's consolidated results of operations and financial position.

In January 2010, FASB issued ASU No. 2010-06, Fair Value Measurements and Disclosures (ASC Topic 820) — Improving Disclosures About Fair Value Measurements. The ASU requires new disclosures about transfers into and out of Levels 1 and 2 and separate disclosures about purchases, sales, issuances, and settlements relating to Level 3 measurements. It also clarifies existing fair value disclosures about the level of disaggregation and about inputs and valuation techniques used to measure fair value. The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. Other than requiring additional disclosures, the adoption of this new guidance will not have a material impact on the Company's consolidated results of operations and financial position.

In February 2010, FASB issued ASU 2010-09 Subsequent Event (Topic 855) Amendments to Certain Recognition and Disclosure Requirements. ASU 2010-09 removes the requirement for a SEC filer to disclose a date through which subsequent events have been evaluated in both issued and revised financial statements. Revised financial statements include financial statements revised as a result of either correction of an error or retrospective application of GAAP. All of the amendments in ASU 2010-09 are effective upon issuance of the final ASU, except for the use of the issued date for conduit debt obligors. That amendment is effective for interim or annual periods ending after June 15, 2010. The Company adopted ASU 2010-09 in February 2010 and did not disclose the date through which subsequent events have been evaluated.

(c) Significant Accounting Policies

Foreign Currencies - The Company’s subsidiaries based in China maintain their books and records in Renminbi, “RMB”, the currency of the PRC, its functional currency. In accordance with guidance now incorporated in ASC Topic 830 (formerly FAS 52), foreign currency transactions in RMB are reflected using the temporal method. Under this method, all monetary items are translated into the functional currency at the rate of exchange prevailing at the balance sheet date. Non-monetary items are translated at historical rates. Income and expenses are translated at the rate in effect on the transaction dates. Transaction gains and losses, if any, are included in the determination of net income for the period. The Parent Company (CAAS) and Henglong USA Corporation (HLUSA) maintain their books and records in United States Dollars, “USD”, the currency of the United States, its functional currency.

In translating the financial statements of the Company’s China subsidiaries from its functional currency into its reporting currency in United States dollars, balance sheet accounts are translated using the closing exchange rate in effect at the balance sheet date and income and expense accounts are translated using an average exchange rate prevailing during the reporting period. Adjustments resulting from the translation, if any, are included in cumulative other comprehensive income (loss) in stockholders’ equity.

Stock-Based Compensation - The Company may periodically issue shares of common stock for services rendered or for financing costs. Such shares will be valued based on the market price on the transaction date. The Company may periodically issue stock options to employees and stock options or warrants to non-employees in non-capital raising transactions for services and for financing costs.

In July 2004, the Company adopted a stock incentive plan. The maximum number of common shares for issuance under this plan is 2,200,000 with a period of 10 years. The stock incentive plan provides for the issuance, to the Company’s officers, directors, management and employees, of options to purchase shares of the Company’s common stock. Since the adoption of the stock incentive plan, the Company has issued 433,850 stock options under this plan, and there remain 1,766,150 stock options issuable in the future. As of June 30, 2010, the Company had 279,401 stock options outstanding.

The Company has adopted ASC Topic 718 (formerly SFAS 123R), “Accounting for Stock-Based Compensation”, which establishes a fair value method of accounting for stock-based compensation plans. In accordance with guidance now incorporated in ASC Topic 718, the cost of stock options and warrants issued to employees and non-employees is measured on the grant date based on the fair value. The fair value is determined using the Black-Scholes option pricing model. The resulting amount is charged to expense on the straight-line basis over the period in which the Company expects to receive benefit, which is generally the vesting period.

Comprehensive Income - The Company has adopted ASC Topic 220 (formerly SFAS No. 130), “Reporting Comprehensive Income”. ASC Topic 220 establishes standards for the reporting and display of comprehensive income, its components and accumulated balances in a full set of general purpose financial statements. ASC Topic 220 defines comprehensive income to include all changes in equity except those resulting from investments by owners and distributions to owners, including adjustments to minimum pension liabilities, accumulated foreign currency translation, and unrealized gains or losses on marketable securities.

Derivatives – Effective January 1, 2009, the Company adopted and applied the amendments to ASC 815 Derivatives and Hedging Activities that revised the definition of “indexed to a company’s own stock” for purposes of continuing classification of the Company’s derivative financial instruments that are linked to the Company’s common stock. Derivative financial instruments, including those that are embedded in other financial instruments, may be classified in equity only when they both are indexed to the Company’s common stock and meet certain conditions for equity classification. Under the revised definition, an instrument (or embedded feature) is indexed to an entity's own stock if its settlement amount will equal the difference between the fair value of a fixed number of the entity's equity shares and a fixed monetary amount. On the effective date of the amendment, the embedded conversion option that is embedded in the Company’s Convertible Notes Payable (see Note 15) no longer met the definition because it embodied certain anti-dilution protections that did not achieve the fixed-for-fixed criteria described above. As a result, the embedded conversion feature required bifurcation, classification in liabilities and measurement at fair value. The Company will be required to re-measure the bifurcated derivative at fair value, with changes reflected in the Company’s income, until the Convertible Notes are settled.

The Company has accounted for this change in accounting principle by reflecting the cumulative effect as an adjustment to the Company’s beginning retained earnings during the Company’s year ended December 31, 2009. The cumulative effect adjustment that the Company made is the difference between the amounts that the Company recognized related to the Convertible Notes Payable before the initial application of the amended principle and the amounts that would have been recognized if the amended guidance had been applied from the issuance date of the Convertible Notes Payable, which was February 15, 2008. The following table illustrates the differences that comprise the cumulative effect:

	(Effective Date January 1, 2009)		
Financial Instrument:	As Recorded	As Adjusted	Cumulative Effect
Convertible Notes Payable	$ 34,339,807	$ 31,108,852	$ 3,230,955
Derivative liabilities	—	2,367,202	(2,367,202)
	$ 34,339,807	$ 33,476,054	$ 863,753

The cumulative effect gives effect to the reallocation of proceeds that arose from the February 15, 2008 financing transaction discussed in Note 14 on the financing date. The following table illustrates the reallocation as if the amended provisions of ASC 815 had been in effect on the financing date:

	(Financing Date February 15, 2008)		
Financial Instrument:	Original	Amended	Difference

	Allocation	Allocation	
Convertible Notes Payable	$ 34,201,374	$ 28,379,704	$ 5,821,670
Derivative liabilities	—	5,821,670	(5,821,670)
Warrants	798,626	798,626	—
	$ 35,000,000	$ 35,000,000	$ —

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The cumulative effect change in accounting principle on the effective date reflects (i) the difference in the financing date allocation of proceeds, (ii) the resulting change in the amortization of the debt discount that results from the revised allocation and (iii) the changes in the fair values in the derivative liabilities that would have been recorded had the amended standard been in effect since the financing date.

Financial Instruments – Financial instruments consist of cash, evidence of ownership in an entity, and contracts that both (i) impose on one entity a contractual obligation to deliver cash or another financial instrument to a second entity, or to exchange other financial instruments on potentially unfavorable terms with the second entity, and (ii) conveys to that second entity a contractual right (a) to receive cash or another financial instrument from the first entity, or (b) to exchange other financial instruments on potentially favorable terms with the first entity. Inputs to the valuation methodology for Level I are quoted prices (unadjusted) for identical assets or liabilities in active markets. Inputs to the valuation methodology Level 2 include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the assets or liability, either directly or indirectly, for substantially the full term of the financial instruments. Inputs to the valuation methodology for Level 3 are unobservable and significant to the fair value. Consideration is also given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model.

Fair Value Measurements - The Company has adopted the provisions of ASC Topic 820 (formerly SFAS 157), “Fair Value Measurements”, except as it applies to those nonfinancial assets and nonfinancial liabilities. ASC Topic 820 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This statement does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. In February 2008, FASB Staff delayed the effective date of ASC Topic 820 for all nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually).

Noncontrolling Interests in Consolidated Financial Statements - In December 2007, the FASB issued guidance now incorporated in ASC Topic 810 “Consolidation” (formerly Statement of Financial Accounting Standards (“SFAS”) 160). The guidance clarifies the accounting for noncontrolling interests and establishes accounting and reporting standards for the noncontrolling interest in a subsidiary, including classification as a component of stockholders’ equity. This guidance was effective for the Company’s fiscal year beginning January 1, 2009. The Company has adopted this guidance in its consolidated financial statements for the period ended June 30, 2010.

4. Pledged cash deposits

Pledged as guarantee for its notes payable, the Company regularly pays some of its suppliers by bank notes. The Company has to deposit a cash deposit, equivalent to 30% - 40% of the face value of the relevant bank note, at a bank in order to obtain the bank note.

5. Accounts and notes receivable

The Company's accounts receivable at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010	December 31, 2009
Accounts receivable	$109,097,616	$ 104,120,926
Notes receivable	75,954,136	56,062,744
	185,051,752	160,183,670
Less: allowance for doubtful accounts	(4,363,233)	(5,320,378)
Balance at the end of the period	$180,688,519	$ 154,863,292

Notes receivable represent accounts receivable in the form of bills of exchange whose acceptances and settlements are handled by banks.

The activity in the Company's allowance for doubtful accounts during the six months ended June 30, 2010 (unaudited) and the year ended December 31, 2009 are summarized as follows:

	June 30, 2010	December 31, 2009
Balance at beginning of period	$ 5,320,378	$ 4,910,478
Amounts provided (recovered) during the period	(876,872)	406,228
Foreign currency translation gain (loss)	(80,273)	3,672
Balance at the end of the period	$ 4,363,233	$ 5,320,378

6. Other receivables

The Company's other receivables at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010	December 31, 2009
Other receivables	$ 2,556,150	$ 1,804,334
Less: allowance for doubtful accounts	(911,737)	(740,110)
Balance at the end of the period	$ 1,644,413	$ 1,064,224

Other receivables consist of amounts advanced to both related and unrelated parties, primarily as unsecured demand loans, with no stated interest rate or due date.

The activity in the Company's allowance for doubtful accounts of other receivable during the six months ended June 30, 2010 (unaudited) and the year ended December 31, 2009 are summarized as follows:

	June 30, 2010	December 31, 2009
Balance at beginning of the period	$ 740,110	$ 659,837
Amounts provided during the period	260,720	79,618
Foreign currency translation gain (loss)	(89,093)	655
Balance at the end of the period	$ 911,737	$ 740,110

7. Inventories

The Company's inventories at June 30, 2010 (Unaudited) and December 31, 2009 consisted of the following:

	June 30, 2010	December 31, 2009
Raw materials	$ 15,154,343	$ 10,683,448
Work in process	8,231,247	6,824,137
Finished goods	18,356,069	12,017,195
	41,741,659	29,524,780
Less: provision for loss	(2,146,313)	(2,109,083)
Balance at the end of the period	$ 39,595,346	$ 27,415,697

8. Property, plant and equipment

The Company's property, plant and equipment at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010 As Restated– note 2	December 31, 2009 As Restated– note 2
Land use rights and buildings	$ 33,659,604	$ 33,100,702
Machinery and equipment	68,538,569	62,982,885
Electronic equipment	5,299,803	5,054,502
Motor vehicles	2,773,265	2,634,696
Construction in progress	2,564,378	1,939,256
	112,835,619	105,712,041
Less: Accumulated depreciation	(52,161,717)	(47,182,594)
Balance at the end of the period	$ 60,673,902	$ 58,529,447

Depreciation charge for the six months ended June 30, 2010 and the year ended December 31, 2009 are $4,861,101 and $8,429,863, respectively.

9. Intangible assets

The activities in the Company's intangible asset account at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010	December 31, 2009
Costs:		
Patent technology	$ 1,391,639	$ 1,384,037
Management software license	476,134	438,359
	1,867,773	1,822,396
Less: Amortization	(1,361,615)	(1,261,007)
Balance at the end of the period	$ 506,158	$ 561,389

10. Deferred Income Tax Assets

In accordance with the provisions of ASC Topic 740 "Income Taxes" (formerly SFAS 109), the Company assesses, on a quarterly basis, its ability to realize its deferred tax assets. Based on the more likely than not standard in the guidance and the weight of available evidence, the Company believes a valuation allowance against its deferred tax assets is necessary. In determining the need for a valuation allowance, the Company considered the following significant factors: an assessment of recent years' profitability and losses; the Company's expectation of profits based on margins and volumes expected to be realized (which are based on current pricing and volume trends); the long period - ten years or more in all significant operating jurisdictions — before the expiry of net operating losses, noting further that a portion of the deferred tax asset is composed of deductible temporary differences that are subject to an expiry period until realized under tax law. The Company will continue to evaluate the provision of valuation allowance in future periods.

The components of estimated deferred income tax assets at June 30, 2010 (unaudited) and December 31, 2009 were as follows:

	June 30, 2010 As Restated– note 2	December 31, 2009 As Restated– note 2
Losses carryforward (U.S.)	$ 2,127,176	$ 2,089,985
Losses carryforward (PRC)	711,734	659,774
Product warranties and other reserves	3,612,888	3,164,674
Property, plant and equipment	3,226,305	3,112,550
Accrued make-whole interest expense for convertible notes	1,940,604	1,667,320
Share-based compensation	379,927	289,705
Bonus accrual	190,687	306,030
Other	382,300	395,649
	12,571,621	11,685,687
Valuation allowance 1	(5,274,495)	(4,821,210)
Total deferred tax assets 2	$ 7,297,126	$ 6,864,477

1 As of June 30, 2010, valuation allowance was $5,274,495, including $4,447,708 allowance for the Company's deferred tax assets in the U.S. and $826,787 allowance for the Company's non-U.S. deferred tax assets. Based on the Company's current operations in the U.S., the management believes that the deferred tax assets in the U.S. are not likely to be realized in the future. For the non-U.S. deferred tax assets, pursuant to certain tax laws and regulations in China, the management believes such amount will not be used to offset future taxable income.

2 Approximately $3,111,251 and $2,998,124 of deferred income tax asset as of June 30, 2010 and December 31, 2009, respectively, is included in non-current deferred tax assets in the accompanying consolidated balance sheets. The remaining $4,185,875 and $3,866,353 of deferred income tax asset as of June 30, 2010 and December 31, 2009, respectively, is included in the current deferred tax assets.

11. Bank loans

At June 30, 2010, the Company, through its Sino-foreign joint ventures, had outstanding fixed-rate short-term bank loans of $8,835,353, with weighted average interest rate at 5.31% per annum. These loans are secured with some of the property and equipment of the Company, and are repayable within one year.

At December 31, 2009, the Company, through its Sino-foreign joint ventures, had outstanding fixed-rate short-term bank loans of $5,125,802, with weighted average interest rate at 5.68% per annum. These loans are secured with some of the property and equipment of the Company and are repayable within one year.

12. Accounts and notes payable

The Company's accounts and notes payable at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010	December 31, 2009
Accounts payable	$91,399,792	$ 69,454,231
Notes payable	44,729,309	38,041,602
Balance at the end of the period	$136,129,101	$ 107,495,833

Notes payable represent accounts payable in the form of bills of exchange whose acceptances and settlements are handled by banks.

The Company has pledged cash deposits, notes receivable and certain property plant and machinery to secure trade financing granted by banks.

13. Convertible Notes payable

In February 2008, the Company sold to two accredited institutional investors $35 million of convertible notes, the "Convertible Notes", with a scheduled maturity date of February 15, 2013. The Convertible Notes, including any accrued but unpaid interest, are convertible into common shares of the Company at a conversion price of $8.8527 per share, subject to adjustment upon the occurrence of certain events.

The Convertible Notes bear annual interest rates of 3%, 3.5%, 4%, 4.5% and 5% for each year of 2008, 2009, 2010, 2011 and 2012. The interest on the Convertible Notes shall be computed commencing from the issuance date and will be payable in cash in arrears semi-annually on January 15, and July 15 of each year with the first interest payable date being July 15, 2008. From and after the occurrence and during the continuance of an Event of Default defined in the relevant Convertible Note agreements, the interest rate then in effect shall be increased by two percent (2%) until the event of default is remedied.

The holders of the Convertible Notes will be entitled to convert any portion of the conversion amount into shares of common stock at the conversion price at any time or times on or after the thirtieth (30th) day after the issuance date and prior to the thirtieth (30th) Business Day prior to the expiry date of the Convertible Notes. A damage penalty will be paid if share certificates are not delivered timely after any conversion.

The Company will have the right to require the Convertible Note holders to convert all or any portion of the conversion amount then remaining under the Convertible Note obligation into shares of common stock, " Mandatory Conversion", if at any time during a six-month period, the beginning day of each such six-month period, a "Mandatory Conversion Period Start Date", the arithmetic average of the weighted average price of the common stock for a period of at least thirty (30) consecutive trading days following the Mandatory Conversion Period Start Date equals or exceeds the percentage of $8.8527 set forth in the chart below as applicable to the indicated six month period:

0-6 months:	125 %
6-12 months:	125 %
12-18 months:	135 %
18-24 months:	135 %
24-30 months:	145 %
30-36 months:	145 %
36-42 months:	155 %

42-48 months:	155 %

The Company will not effect a Mandatory Conversion of more than twelve percent (12%) of the original principal amount of the Convertible Notes, with the applicable accrued but unpaid interest, in any six month period or twenty-four percent (24%) of the original principal amount of the Convertible Notes, with the applicable accrued but unpaid interest, in any twelve (12) month period.

On each six month anniversary of the issuance date beginning August 15, 2008, the conversion price will be adjusted downward to the Reset Reference Price, as defined below, if the weighted average price for the twenty (20) consecutive trading days immediately prior to the applicable six month anniversary, the “Reset Reference Price”, is less than 95% of the conversion price in effect as of such applicable six month anniversary date. The foregoing notwithstanding, the conversion price will not be reduced via such reset provision to less than $7.0822. The conversion price is also subject to weighted-average antidilution adjustments, but in no event will the conversion price be reduced to less than $6.7417. If and whenever on or after the issuance date, the Company issues or sells its shares of Common Stock or other convertible securities, except for certain defined exempt issuances, for a consideration per share less than a price equal to the conversion price in effect on the issuance date immediately prior to such issue or sale, the original conversion price then in effect shall be adjusted by a weighted-average antidilution formula, but in no event to a new conversion price less than $6.4717.

The Company will not effect any conversion of the Convertible Notes, and each holder of the Convertible Notes will not have the right to convert any portion of the Convertible Notes to the extent that after giving effect to such conversion, such holders would beneficially own in excess of 4.99% of the number of shares of Common Stock outstanding immediately after giving effect to such conversion.

As indicated above, according to the terms of the Convertible Notes, the conversion price was reset to $7.0822 as of August 15, 2008 based on the weighted average price of the stock on that date. In accordance with ASC Topic 470 (formerly EITF 00-27), a contingency feature that cannot be measured at inception of the instrument should be recorded when the contingent event occurs. Therefore, on the date of the reset, the difference in the number of indexed shares prior to the reset was compared to the indexed shares subsequent to the reset and this incremental number of shares was multiplied by the commitment date stock price to determine the incremental intrinsic value that resulted from the adjustment to the conversion price. At the commitment date, as the effective conversion price was higher than the market value of the stock, no beneficial conversion feature was present and therefore, no beneficial conversion charge was recorded.

As of August 15, 2008, the number of indexed shares was 3,953,596 and 4,941,967 at the inception conversion price and reset conversion price, respectively. At the commitment date, the stock price was $6.09, and the “effective” conversion price was $6.93. Accordingly, since the effective conversion price was higher than the market value of the stock, the debt instruments are not considered "in the money" and no beneficial conversion feature is present.

Upon the occurrence of an event of default with respect to the Convertible Notes, the Convertible Note holders may require the Company to redeem all or any portion of the Convertible Notes. Each portion of the Convertible Notes subject to redemption by the Company will be redeemed by the Company at a price equal to the sum of (i) the conversion amount to be redeemed and (ii) the Other Make Whole Amount. The “Other Make Whole Amount” will mean a premium to the conversion amount such that the total amount received by the Convertible Note holder upon redemption represents a gross yield to the Convertible Note holders on the original principal amount as of the redemption date equal to thirteen percent (13%), with interest computed on the basis of actual number of days elapsed over a 360-day year. The events of default includes the Company’s failure to cure a conversion failure by delivery of the required number of shares of Common Stock, the Company’s failure to pay to the Convertible Note holder any amount of principal, interest, late charges or other amounts when and as due under the Convertible Notes and other events as defined in the Convertible Note agreements. Any amount of principal, interest or other amount due under the Convertible Notes which is not paid when due shall result in a late charge of 18% being incurred and payable by the

Company until such amount has been paid.

Upon the consummation of a change of control as defined in the Convertible Note agreements, the Convertible Note holder may require the Company to redeem all or any portion of the Convertible Notes. The portion of the Convertible Notes subject to redemption shall be redeemed by the Company in cash at a price equal to the sum of the conversion amount of being redeemed and the Other Make Whole Amount as defined above.

On each of February 15, 2010 and February 15, 2011, the Convertible Note holders will have the right, in their sole discretion, to require that the Company redeem the Convertible Notes in whole but not in part, by delivering written notice thereof to the Company. The portion of this Convertible Note subject to redemption pursuant to this annual redemption right will be redeemed by the Company in cash at a price equal to the sum of the conversion amount being redeemed and the Annual Redemption Make Whole Amount. The “Annual Redemption Make Whole Amount” will mean a premium to the conversion amount such that the total amount received by the Convertible Note holder upon any annual redemption represents a gross yield on the original principal amount of eleven percent (11%), with interest computed on the basis of actual number of days elapsed over a 360-day year.

In the event that the Company has not completed the necessary filings to list the conversion shares on its principal market by the date that is ninety (90) days after the issuance date or has not so listed the conversion shares by the date that is ninety (90) days after the issuance date or the shares of the Company’s common stock are terminated from registration under the Securities Act of 1933, the Convertible Note holders will have the right, in its sole discretion, to require that the Company redeem all or any portion of the Convertible Notes. The portion of the Convertible Notes subject to redemption in connection with this listing default will be redeemed by the Company in cash at a price equal to the sum of the conversion amount being redeemed and the Other Make Whole Amount as mentioned above.

At any time following February 15, 2009, if the Weighted Average Price (WAP) for twenty (20) consecutive trading days is less than 45% of the Conversion Price in effect on the Issuance Date, as adjusted, namely $3.187, the Convertible Note holder shall have the right, in its sole discretion, to require that the Company redeem all or any portion of the Convertible Notes. The portion of this Convertible Note subject to redemption in connection with the share price change of the underlying common stock will be redeemed by the Company in cash at a price equal to the sum of the conversion amount being redeemed and the Other Make Whole Amount as mentioned above.

Since the Company’s stock Weighted Average Price for twenty (20) consecutive trading days ended on March 16, 2009 was below $3.187, which is less than 45% of the Conversion Price in effect as of the Issuance Date, as adjusted, the “ WAP Default” , each Convertible Note holder had the right, at its sole discretion, to require that the Company redeem all or any portion of the Convertible Notes by delivering written redemption notice to the Company within five (5) business days after the receipt of the Company’s notice of the WAP Default.

On March 17, 2009, the Company delivered two WAP Default notices to the Convertible Note holders. On March 27, 2009, the Company received a letter from YA Global, one of the Convertible Note holders, electing to require the Company to redeem all the three Convertible Notes it held in the total principal amount of $5,000,000, together with interest, late charges, and the Other Make Whole Amount as defined in Section 5(d) of the Convertible Notes. After negotiation, the Company and YA Global reached a settlement agreement on April 8, 2009 and under the terms of the settlement agreement, the Company paid on April 15, 2009 a redemption amount of $5,041,667 to YA Global and YA Global waived its entitlement to the Other Make Whole Amount.

Following the WAP Default notices, the Company received a letter from the provisional liquidator acting on behalf of Lehman Brothers Commercial Corporation Asia Limited, the “LBCCA Liquidator”, the other Convertible Note holder, requesting an extension until April 24, 2009 to consider its rights under the Convertible Notes. The Company granted an extension to April 15, 2009. The LBCCA Liquidator further requested another extension to April 24, 2009. On April 24, 2009, LBCCA’s lawyers sent three Holder Redemption Notices via fax electing to redeem the entire outstanding principal of $30,000,000, together with interest, late charges, if any, and the Other Make Whole Amount, to be paid on July 23, 2009. The Company discussed settlement with the LBCCA Liquidator, and on or about July 22, 2009, the Company and the LBCCA Liquidator agreed to extend the applicable holder mandatory redemption date for two months to September 23, 2009 to give more time to pursue settlement discussion. The Company received a letter dated September 22, 2009 from the LBCCA Liquidator stating that upon the Company’s acceptance of the revocation, all holder redemption notices dated April 24, 2009 shall be immediately revoked as if they were never issued, and the letter and the revocation did not purport to amend, restate or supplement any other terms and conditions under the three Notes and the Securities Purchase Agreement dated 1 February 2008 between the Company and LBCCA Liquidator. The Company accepted such revocation on September 23, 2009.

In connection with the Convertible Notes, the Company issued 1,317,864 detachable warrants, the “Warrants,” to purchase from the Company shares of common stock of the Company at the exercise price of $8.8527 per share. The Warrants are exercisable immediately and expired on February 15, 2009. The Warrants require net cash settlement in the event that there is a fundamental transaction, contractually defined as a merger, sale of substantially all assets, tender offer or share exchange. Due to this contingent redemption provision, in accordance with guidance now incorporated in ASC Topic 480 (formerly SFAS 150), the warrants require liability classification and must be recorded at fair value each reporting period. As of the issuance date, i.e., February 15, 2008, the fair value of warrants was $798,626, which was determined using the Black-Scholes option pricing model.

On the issuance date, February 15, 2008, the Company has evaluated the convertible notes for terms and conditions that are not clearly and closely associated with the risks of the debt-type host instrument. Generally, such features require separation from the host contract and treatment as derivative financial instruments. Certain features, such as the conversion option, were found to be exempt, as they satisfied the conditions in ASC Topic 815 (formerly the paragraph 11(a) of SFAS 133) for instruments (1) indexed with the Company’s own stock, and (2) classified as equity in financial position statement. Other features, such as puts features were also found to be exempt based on the provision of ASC Topic 815 (formerly the paragraph 61(d) of SFAS 133), when they are clearly and closely associated with the risk of the debt-type host instrument, except (1) debt involve a substantial discount, and (2) put only contingently exercisable. Put feature that were embedded in the Company’s hybrid debt instrument satisfied the exemption conditions as (1) they are clearly and closely related to the host debt instrument, (2) the debt does not involve a substantial discount, and that debt discount that the Company calculated was only 2% which is not considered a substantial discount.

When a financial instrument contains embedded derivatives that require bifurcation, such as the conversion option, redemption put, and freestanding instruments that are recorded at fair value each period, such as the warrants, the accounting is to record the embedded derivative and the freestanding instruments at fair value on inception and the residual proceeds are allocated to the debt instrument. Therefore, upon inception of the debt instruments, the Company recorded the warrants at fair value of $798,626. The remaining proceeds were then allocated to the debt instrument.

As more fully discussed in Note 3, in January 1, 2009, the Company adopted and applied the amendments to ASC 815 Derivatives and Hedging Activities (effective on January 1, 2009), and changed its accounting to conform to the amended rules in ASC 815-40 (formerly was EITF 07-5) relating o the classification of derivative financial instruments. As a result of adopting the amended provisions of ASC 815-40, the Company was required to bifurcate the embedded conversion feature from the Convertible Debt and classify the liabilities of the financial instrument at fair value. Accounting for the cumulative effect change in this accounting principle required the Company to record an adjustment to its beginning retained earnings during the year ended December 31, 2009 which is the difference between the amounts that it recognized related to the Convertible Notes Payable before the initial application of the amended principle and the amounts that would have been recognized if the amended guidance had been applied from the issuance date of the Convertible Notes Payable, which was February 15, 2008. The following table illustrates the differences that comprise the cumulative effect:

	Convertible notes payable	
	Original Allocation	Amended Allocation
Value allocated to debt	$34,201,374	$28,379,704
Warrants	798,626	798,626
Compound Embedded Derivative	-	5,821,670
Face value of Convertible Notes payable	$35,000,000	$35,000,000
Unamortized discount	660,193	3,891,148
Unamortized value as of December 31, 2008	$34,339,807	-
Fair value as of January 1, 2009	-	$31,108,852

As indicated above, on the date of inception, allocation of basis in the financing arrangement to the warrants has resulted in an original issue discount to the face value of the convertible notes in the amount of $798,626, which amount is subject to amortization over the Convertible Note’s term using the effective interest method. As of December 31, 2008, the amortization expense recorded by the Company was $138,433, and unamortized discount was $660,193. On January 1, 2009, the Company adopted and applied the amendments to ASC 815 Derivatives and Hedging Activities (effective on January 1, 2009), accounting for the cumulative effect change in this accounting principle resulting in $6,620,296, including $798,626 discount resulted from Warrants and $5,821,670 from embedded conversion feature of the original unamortized discount and the subsequent amortization using the effective interest method. On January 1, 2009, unamortized discount was $3,891,148.

As indicated above, on March 17, 2009, as a result of the Company’s WAP Default, the Convertible Note holders elected to exercise their rights to require the Company to redeem the Convertible Notes. The remaining amount of $3,891,148 unamortized discount was recorded to full face value of the Convertible Notes including the make-whole redemption amount. On April 8, 2009, the Company and YA Global reached a settlement agreement, and the Company paid a redemption amount of $5,000,000 of the principal and $41,667 of interest to YA Global. On September 22, 2009, LBCCA Liquidator revoked the redemption notices that were sent on April 24, 2009, and continued to hold the Company’s Convertible Notes, of which the face value was $30,000,000. The Company accepted such revocation on September 23, 2009.

On each of June 30, 2010 and December 31, 2009, the carrying value of the Company’s Convertible Notes payable was $30,000,000.

14. Compound derivative liabilities

Effective January 1, 2009, the Company adopted the provisions of ASC 815 Derivatives and Hedging Activities that addresses the determination of whether an instrument meets the definition of a derivative being indexed to a company's own stock for purposes of applying the scope exception as provided for in accordance with ASC 815-15. Upon adoption of the standard on the effective date, the embedded conversion option that is embedded in the Company's Convertible Notes Payable (see Note 13) no longer met the definition because it embodied certain anti-dilution protections that is not based on input to the fair value of a fixed-for-fixed option. As a result, the embedded conversion feature required bifurcation, classification in liabilities and measurement at fair value at each reporting period, with changes reflected in earnings, until the Convertible Notes are settled.

The Company's derivative financial instruments (liabilities) consisted of a compound embedded derivative that originated in connection with the Company's Convertible Note Payable and Warrant Financing Arrangement. Derivative liabilities are carried at fair value.

The following table summarizes the compound derivative liabilities as of June 30, 2010 (unaudited) and December 31, 2009:

Financial Instrument	June 30, 2010 As Restated– note 2	December 31, 2009 As Restated– note 2
Compound derivative liability	$ 40,008,754	$ 45,443,506
Common shares to which the derivative liability is linked	4,235,972	4,235,972

Changes in the fair value of compound derivative liabilities are recorded in gain (loss) on change in fair value of derivative column in the income statement. The following tables summarize the components of gain (loss) on change in fair value of derivative arising from fair value adjustments and other changes to compound derivative liabilities during the six months ended June 30, 2010 and 2009:

	Six Months Ended June 30,	
	2010 As Restated– note 2	2009 As Restated– note 2
Balances at January 1	$ 45,443,506	$ -
Cumulative effect change in accounting principal	-	2,367,202
Subtotal	45,443,506	2,367,202
Redemptions and settlements:		
Redemption		(2,367,202)
Increase (decrease) in fair value adjustments	(5,434,753)	-
Balances at June 30	$ 40,008,753	$ -

Estimating fair values of derivative financial instruments requires the development of significant and subjective estimates that may, and are likely to, change over the duration of the instrument with related changes in internal and external market factors. In addition, option-based techniques are highly volatile and sensitive to changes in the trading market price of the Company's common stock, which has a high estimated volatility. Since derivative financial instruments are initially and subsequently carried at fair values, the Company's income will reflect the volatility in these estimate and assumption changes.

The Company's embedded conversion option derivative represents the conversion option, term-extending option, certain redemption and put features in the Company's Convertible Notes payable. See Note 13 for additional information about the Company's Convertible Notes payable. The features embedded in the Senior Convertible Notes were combined into one compound embedded derivative that the Company fair valued using the Monte Carlo valuation technique. Monte Carlo was believed by the Company's management to be the best available technique for this compound derivative because, in addition to providing for inputs such as trading market values, volatilities and risk free rates, Monte Carlo also embodies assumptions that provide for credit risk, interest risk and redemption behaviors (i.e. assumptions market participants exchanging debt-type instruments would also consider). Monte Carlo simulates multiple outcomes over the period to maturity using multiple assumption inputs also over the period to maturity. The following table sets forth (i) the range of inputs for each significant assumption and (ii) the equivalent, or averages, of each significant assumption as of March 31, 2010, December 31, 2009 and January 1, 2009 (effective date of accounting principle change):

	Range					
June 30, 2010 Assumptions:	Low		High		Equivalent	
Volatility	72.93	%	80.36	%	76.88	%
Market adjusted interest rates	2.75	%	21.13	%	10.15	%
Credit risk adjusted rates	16.42	%	17.35	%	16.59	%
Implied expected life (years)	—		—		1.78	

	Range					
December 31, 2009 Assumptions:	Low		High		Equivalent	
Volatility	68.86	%	81.94	%	76.71	%
Market adjusted interest rates	6.40	%	7.87	%	7.05	%
Credit risk adjusted rates	13.39	%	14.20	%	13.63	%
Implied expected life (years)	—		—		1.96	

	Range					
January 1, 2009 Assumptions:	Low		High		Equivalent	
Volatility	63.09	%	91.15	%	74.02	%
Market adjusted interest rates	4.14	%	17.01	%	7.15	%
Credit risk adjusted rates	21.58	%	24.97	%	23.20	%
Implied expected life (years)	—		—		4.27	

The Monte Carlo Simulations technique requires the use of inputs that range across all levels in the fair value hierarchy. As a result, the technique is a Level 3 valuation technique in its entirety. The calculations of fair value utilized the Company's trading market values on the calculation dates. The contractual conversion prices were adjusted to give effect to the value associated with the down-round, anti-dilution protection. Expected volatility for each interval in the Monte Carlo Simulations process was established based upon the Company's historical volatility for historical periods consistent with the term of each interval in the calculation. Market adjusted interest rates give effect to expected trends or changes in market interest rates by reference to historical trends in LIBOR. Credit risk adjusted rates, or yields, were developed using bond curves, risk free rates, market and industry adjustment factors for companies with similar credit standings as the Company's.

On February 15, 2009, the warrants expired unexercised and the warrants were forfeited. Accordingly, the fair value of the warrants of $1,977 at the beginning of 2009 decreased to 0 at March 31, 2009 and the change has been recorded in the income statement as a gain of $1,977 for the six months ended June 30, 2009.

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15. Accrued expenses and other payables

The Company’s accrued expenses and other payables at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010 As Restated– note 2	December 31, 2009 As Restated– note 2
Accrued expenses	$ 2,747,434	$ 4,160,433
Accrued interest (1)	6,057,085	5,751,270
Other payables	1,945,914	1,706,946
Warranty reserves 2	6,841,601	9,092,464
Dividend payable to non-controlling interest shareholders of Joint-ventures	3,328,515	1,761,339
Balance at the end of the period	$ 20,920,549	$ 22,472,452

1 On June 30, 2010 and December 31, 2009, the Company’s balance of accrued interest was $6,057,085 and $5,751,270, respectively, and the Company’s accrued provision on make-whole redemption interest pursuant to the terms of the Convertible Notes was approximately $5,500,000 and $4,800,000, respectively.

2 The Company provides for the estimated cost of product warranties when the products are sold. Such estimates of product warranties were based on, among other things, historical experience, product changes, material expenses, service and transportation expenses arising from the manufactured product. Estimates will be adjusted on the basis of actual claims and circumstances.

For the six months ended June 30, 2010 (unaudited) and the year ended December 31, 2009, the warranties activities were as follows:

	June 30, 2010 As Restated– note 2	December 31, 2009 As Restated– note 2
Balance at the beginning of period	$ 9,092,462	$ 6,335,613
Additions during the period-	5,765,935	10,192,749
Settlement within period, by cash or actual material	(3,322,294)	(7,442,982)
Foreign currency translation gain (loss)	56,730	7,084
Balance at end of period	$ 11,592,833	$ 9,092,464

Approximately $6,841,601 and $9,092,464 of warranty reserves, respectively, are included in accrued expenses and other payables in the accompanying consolidated balance sheets. The remaining $4,751,232 of warranty reserves as of June 30, 2010 is included in the other long-term liabilities.

16. Accrued pension costs

Since the Company’s operations are all located in China, all the employees are located in China. The Company records pension costs and various employment benefits in accordance with the relevant Chinese social security laws, which is substantially based on a total of 31% of base salary as required by local governments. Base salary levels are the average salary determined by the local governments.

The activities in the Company's pension account during the six months ended June 30, 2010 (unaudited) and the year ended December 31, 2009 are summarized as follows:

	June 30, 2010	December 31, 2009
Balance at beginning of the period	$ 3,778,187	$ 3,806,519
Amounts provided during the period	2,391,155	3,738,373
Settlement during the period	(2,376,072)	(3,770,220)
Foreign currency translation gain (loss)	21,170	3,515
Balance at end of period	$ 3,814,440	$ 3,778,187

17. Taxes payable

The Company's taxes payable at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010 As Restated– note 2	December 31, 2009 As Restated– note 2
Income tax payable	$ 2,819,884	$ 1,851,103
Value-added tax payable	7,711,055	9,290,149
Other tax payable	169,565	340,925
Balance at end of the period	$ 10,700,504	$ 11,482,177

18. Amounts due to shareholders/ directors

The activities in the amounts due to shareholders/directors at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010	December 31, 2009
Balance at the beginning of period	$ -	$ 337,370
Increase (decrease) during the period	110,271	(337,915)
Foreign currency translation gain (loss)	1,938	545
Balance at end of period	$ 112,209	$ -

The amounts due to shareholders/directors were unsecured, interest-free and repayable on demand.

19. Other long-term liabilities

The Company's other long-term liabilities at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010	December 31, 2009
Advances payable 1	$ 235,227	$ 233,941
Warranty reserves	4,751,232	-
Balance at end of the period	$ 4,986,459	$ 233,941

1 The amounts mainly represent advances made by the Chinese government to the Company as subsidy on interest on loans related to production facilities expansion.

The balances are unsecured, interest-free and will be repayable to the Chinese government if the usage of such advance does not continue to qualify for the subsidy (see notes 22).

20. Share Capital and Additional paid-in capital

The activities in the Company's share capital and additional paid-in capital account during the six months ended June 30, 2010 (unaudited) and the year ended December 31, 2009 are summarized as follows:

	Share Capital			
	Shares	Par Value	Additional paid-in capital	
Balance at January 1, 2009	26,983,244	$2,698	$	26,648,154
Shares issued for stock options exercised	63,000	6		420,234
Share-based compensation 1	-	-		446,676
Balance at December 31, 2009	27,046,244	$2,704	$	27,515,064
Shares issued for stock options exercised	64,449	7		259,469
Share-based compensation 1	-	-		250,026
Balance at June 30, 2010 (unaudited)	27,110,693	$2,711	$	28,024,559

1 The stock options granted during 2009 were exercisable immediately, the fair value on the grant date using the Black-Scholes option pricing model was $196,650, and have been recorded as compensation costs.

The stock options granted during 2008 were partially exercisable immediately, and partially exercisable pro rata during the grant term. The stock options' fair value on the grant date using the Black-Scholes option pricing model was $845,478, of which $345,426 and $250,026 have been recorded as compensation costs in 2008 and 2009. The remaining of $250,026 has been recognized in June 2010.

21. Non-controlling interests

The Company's activities in respect of the amounts of the non-controlling interests' equity at June 30, 2010 (unaudited) and December 31, 2009 are summarized as follows:

	June 30, 2010 As Restated– note 2			December 31, 2009 As Restated– note 2		
Balance at beginning of the period	$	27,138,357		$	23,270,820	
Add: Additions during the period –						
Income attributable to non-controlling interests		5,877,705			7,789,746	
Less: Decreases during the period						
Dividends declared to the non-controlling interest holders of Joint-venture companies		(3,288,909	)		(3,944,619	)
Foreign currency translation gain		151,470			22,410	
Balance at end of period	$	29,878,623		$	27,138,357	

22. Retained earnings—

Appropriated

Pursuant to the relevant PRC laws and regulations of Sino-foreign joint venture enterprises, the profits distribution of the Company's Sino-foreign subsidiaries, which are based on their PRC statutory financial statements, other than based on the financial statement that was prepared in accordance with generally accepted accounting principles in the United States of America, are available for distribution in the form of cash dividends after these subsidiaries have paid all relevant PRC tax liabilities, provided for losses in previous years, and made appropriations to statutory surplus at 10%.

When the statutory surplus reserve reaches 50% of the registered capital of a company, additional reserve is no longer required. However, the reserve cannot be distributed to joint venture partners. Based on the business licenses of the Sino-foreign joint ventures, the registered capital of Henglong, Jiulong, Shenyang, Zhejiang, USAI, Jielong, Wuhu, and Hengsheng are $10,000,000, $4,283,170 (RMB35,000,000), $8,132,530 (RMB67,500,000), $7,000,000, $2,600,000, $6,000,000, $3,750,387 (RMB30,000,000), and $10,000,000 respectively.

The Company recorded $443,264 and $798,756 statutory surplus reserve for the six months ended June 30, 2010 (unaudited) and the year ended December 31, 2009, respectively.

Unappropriated

Following is the change in unappropriated retained earning as of June 30, 2010 (unaudited) and December 31, 2009:

	June 30, 2010 As Restated– note 2	December 31, 2009 As Restated– note 2
Balance at beginning of the year	$ 7,685,002	$ 34,060,876
Accumulated effect of adoption of ASC 815-40 (1)	—	863,753
Net income (loss)	23,501,154	(26,440,871)
Distribution of retained earnings	(443,264)	(798,756)
Balance at end of period	$ 30,742,892	$ 7,685,002

1 As discussed in Note 3, effective on January 1, 2009, the Company adopted and applied the amendments to ASC 815 Derivatives and Hedging Activities, the accumulated effect of adoption of ASC 815-40 was $863,753.

23. Other Income

During the three months and six months ended June 30, 2010 (unaudited), the other income was $250,851 and $266,379, mainly from Government subsidies. During the three months and six months ended June 30, 2009 (unaudited), there was no such income.

Government subsidies represent refunds by the Chinese Government of interest paid to banks by companies entitled to such subsidies. This applies only to interest on loans related to production facilities expansion. The Company recorded the refunded interest on projects which achieved their goals into Other income, and refunded interest on projects which have not achieved their goals into advances payable.

24. Financial (income) expenses

During the three months and six months ended June 30, 2010 and 2009 (unaudited), the Company recorded financial expenses which are summarized as follows:

	Three Months Ended June 30,	
	2010 As Restated– note 2	2009 As Restated– note 2
Interest expenses, net	$ 775,359	$ 395,734
Foreign exchange (gain) loss, net	57,571	(257,484)
(Income) loss of note discount, net	(28,268)	94,545
Amortization for discount of Convertible Note payable	—	—
Bank charges	36,021	27,392
Total	$ 840,683	$ 260,187

During the six months ended June 30, 2010 and 2009 (unaudited), the Company recorded financial expenses which are summarized as follows:

	Six Months Ended June 30,	
	2010 As Restated– note 2	2009 As Restated– note 2
Interest expenses, net 1	$ 1,233,966	$ 2,586,190
Foreign exchange (gain) loss, net	67,393	(242,916)
(Income) loss of note discount, net	(13,077)	94,655
Amortization for discount of Convertible Note payable 2	—	3,891,148
Bank charges	60,622	41,567
Total	$ 1,348,904	$ 6,370,644

(1) Decreased interest expenses as a result of the Company's WAP Default on March 17, 2009, and the Convertible Note holders required Make Whole redemption by the Company, thus, the Company recorded about $1,200,000 of default interest.
(2) On March 17, 2009, due to the Company's WAP Default, the Convertible Note holders required Make Whole redemption by the Company and the remaining amount of $3,891,148 unamortized discount was fully amortized (see note 13).

25. Gain (loss) on change in fair value of derivative

During the three months ended June 30, 2010 (unaudited) and 2009, the Company recorded gain (loss) on change in fair value of derivatives, which is summarized as follows:

	Three Months Ended June 30,	
	2010	2009
	As Restated– note 2	As Restated– note 2
Income from adjustment of fair value of compound derivative liabilities	$ 19,587,135	—
Total	$ 19,587,135	$ —

During the six months ended June 30, 2010 (unaudited) and 2009, the Company recorded gain (loss) on change in fair value of derivatives, which is summarized as follows:

	Six Months Ended June 30,	
	2010	2009
	As Restated– note 2	As Restated– note 2
Income from adjustment of fair value of liabilities in connection with warrants	$ -	$ 1,977
Income from adjustment of fair value of compound derivative liabilities	5,434,753	2,367,202
Total	$ 5,434,753	$ 2,369,179

During the six months ended June 30, 2009, the gain on change in fair value of the compound derivative liabilities was due to the Company's WAP Default on March 17, 2009, and the Convertible Note holders required Make Whole redemption by the Company, thus, the embedded conversion feature in Convertible Notes was forfeited, thus, the fair value of derivative liability was $0. (see note 13)

During the six months ended June 30, 2010, the Company's common stock market price dropped to $17.6 from $18.71, thus, decreased the intrinsic value of embedded conversion feature in financial instruments, decreased the fair value of compound derivative liabilities, and increased the gain on change in fair value of derivatives. (see note 14)

26. Income taxes

The Company's subsidiaries registered in the PRC, whose enterprise income tax exemption has ceased, are subject to state and local income taxes within the PRC at the applicable tax rate of 25% on the taxable income as reported in their PRC statutory financial statements in accordance with the relevant income tax laws applicable to foreign invested enterprise. The Company's PRC subsidiaries, which are in the stage of its enterprise income tax exemption currently, are to remain subject to enterprise fixed income tax at a statutory rate of 33%, which comprises 30% national income tax and 3% local income tax.

On January 1, 2007, Jiulong has used up its enterprise income tax exemption. During 2008, Jiulong was subject to enterprise income tax at a rate of 25%. During 2009, Jiulong was awarded the title of Advanced Technology Enterprises, and subject to enterprise income tax at a rate of 15% for 2008, 2009 and 2010.

On January 1, 1999, Henglong was granted an enterprise income tax holiday of a 100% enterprise income tax exemption for two years commencing from 1999, and a 50% enterprise national income tax deduction and a 100% local income tax deduction for the next nine years thereafter, from 2001 to 2009, for income tax purposes. During

2008, Henglong was awarded the title of Advanced Technology Enterprises, and subject to enterprise income tax at a rate of 15% for 2008, 2009 and 2010.

On January 1, 2003, Shenyang was granted an enterprise income tax holiday of a 100% enterprise income tax exemption for two years commencing from 2003, a 75% enterprise national income tax deduction and a 100% local income tax deduction for the next three years thereafter, from 2005 to 2007, and a 50% enterprise national income tax deduction, from January 1, 2008, for income tax purposes and was subject to enterprise income tax at a rate of 18%. During 2009, Shenyang was awarded the title of Advanced Technology Enterprises, and subject to enterprise income tax at a rate of 15% for 2009 and 2010.

On January 1, 2004, Zhejiang was granted an enterprise income tax holiday of a 100% enterprise income tax exemption for two years commencing from 2004, and a 50% enterprise national income tax deduction, and a 50% local income tax deduction for the next three years thereafter, from 2006 to 2008, for income tax purposes. During 2008, Zhejiang is subject to enterprise income tax at a rate of 16.5%, which is comprised of 15% enterprise national income tax and 1.5% local income tax. During 2009, Zhejiang was awarded the title of Advanced Technology Enterprise, and is subject to enterprise income tax at a rate of 15% for 2009 and 2010.

Wuhu, Jielong and Hengsheng have an enterprise income tax exemption in 2008 and 2009, and are subject to income tax at a rate of 15% for the next three years thereafter, from 2010 to 2012, and a 25% enterprise national income tax commencing from January 1, 2013.

There is no assessable profit for USAI and Testing Center in 2009 and 2010. Based on PRC income tax laws, USAI and Testing Center have an enterprise income tax exemption in 2009, and are subject to income tax at a rate of 15% for the next three years thereafter, from 2010 to 2012, and a 25% enterprise national income tax for the years commencing from January 1, 2013.

No provision for Hong Kong tax is made as Genesis is an investment holding company, and has no assessable income in Hong Kong for the six months ended June 30, 2010 and 2009. The enterprise income tax of Hong Kong is 16.5%.

No provision for US tax is made as the Company has no assessable income in the US for the six months ended June 30, 2010 and 2009. The enterprise income tax of US is 35%.

27. Income per share

Basic income per share attributable to Parent company is calculated by dividing net income by the weighted average number of common shares outstanding during the period using the two-class method. Diluted income per share is calculated based on the treasury stock method, assuming the issuance of common shares, if dilutive, resulting from the exercise of warrants. The dilutive effect of convertible securities is reflected in diluted earnings per share by application of the “if converted” method.

The calculations of income per share attributable to Parent company were:

	Three Months Ended June 30, 2010 As Restated (unaudited)	2009 As Restated (unaudited)
Numerator:		
Net income attributable to Parent company	$ 27,607,605	$ 7,271,825
Allocation to convertible notes holders	(3,734,882)	(1,010,017)
Net income (loss) attributable to the parent Company’s common shareholders – Basic	23,872,723	6,261,808
Dilutive effect of:		
Add back allocation to convertible notes holders	3,734,882	1,010,017
Interest expenses of Convertible Notes payable	834,167	
Gain on change in fair value of derivative	(19,587,134)	
Net income (loss) attributable to the parent Company’s common shareholders - Diluted	$ 8,854,638	$ 7,271,825
Denominator:		
Weighted average shares outstanding	27,075,607	26,983,244
Shares issuable under stock options	250,900	58,843
Shares issuable pursuant to convertible senior notes	4,235,972	-
	31,562,479	27,042,087
Net income per common share attributable to Parent company – basic	$ 0.88	$ 0.23
Net income per common share attributable to Parent company – diluted	$ 0.28	$ 0.23

	Six Months Ended June 30, 2010 As Restated (unaudited)	2009 As Restated (unaudited)
Numerator:		
Net income attributable to Parent company	$23,501,154	$7,789,687
Allocation to convertible notes holders	(3,180,834)	(1,144,465)
Net income (loss) attributable to the parent Company’s common shareholders – Basic	20,320,320	6,645,222
Dilutive effect of:		
Add back allocation to convertible notes holders	3,180,834	1,144,465
Interest expenses of Convertible Notes payable	1,362,063	-
Gain on change in fair value of derivative	(5,434,752)	-
Net income attributable to the parent Company’s common shareholders - Diluted	$19,428,465	$7,789,687
Denominator:		
Weighted average shares outstanding - basic and diluted	27,060,925	26,983,244
Shares issuable under stock options	261,950	29,421
Shares issuable pursuant to convertible senior notes	4,235,972	—
	31,558,847	27,012,665
Net income per common share attributable to Parent company –		
Basic	$0.75	$0.25
Diluted	$0.62	$0.25

The following table summarizes potential common shares outstanding excluded from the calculation of diluted earnings (loss) per share for the three months ended June 30, 2010 and 2009 (unaudited), because such inclusion would have had an anti-dilutive effect.

	Three Months Ended June 30, 2010	2009
Shares issuable under stock options	-	90,000
Shares issuable pursuant to convertible senior notes	-	4,235,972
	-	4,352,345

The following table summarizes potential common shares outstanding excluded from the calculation of diluted earnings (loss) per share for the six months ended June 30, 2010 and 2009 (unaudited), because such inclusion would have had an anti-dilutive effect.

	Six Months Ended June 30,	
	2010	2009
Shares issuable under stock options	-	90,000
Shares issuable pursuant to convertible senior notes	-	4,235,972
	-	4,352,345

28. Significant concentrations

The Company grants credit to its customers, generally on an open account basis. The Company's customers are all located in the PRC.

During the six months ended June 30, 2010 (unaudited), the Company's ten largest customers accounted for 83.8% of its consolidated net sales, with each of two customers individually accounting for more than 10% of consolidated net sales, i.e. 17.9%, and 11.3% individually, or an aggregate of 29.2%. At June 30, 2010, approximately 17.0% of accounts receivable were from trade transactions with the aforementioned two customers.

During the six months ended June 30, 2009 (unaudited), the Company's ten largest customers accounted for 80.1% of its consolidated net sales, with each of five customers individually accounting for more than 10% of consolidated net sales, i.e. 13.0%, 12.9%, 12.1%, 10.6%, and 10.5% individually, or an aggregate of 59.2%. At June 30, 2009, approximately 44.1% of accounts receivable were from trade transactions with the aforementioned five customers.

29. Related party transactions and balances

Related party transactions with companies with common directors are as follows:

Related sales (unaudited):

	Three Months Ended June 30,	
	2010	2009
Merchandise Sold to Related Parties	$ 2,941,718	$ 1,314,247

	Six Months Ended June 30,	
	2010	2009
Merchandise Sold to Related Parties	$ 4,602,111	$ 1,873,258

Related purchases (unaudited):

	Three Months Ended June 30 ,	
	2010	2009
Materials Purchased from Related Parties	$ 5,248,896	$ 2,812,741
Technology Purchased from Related Parties	132,530	29,274
Equipment Purchased from Related Parties	207,646	427,391
Total	$ 5,589,072	$ 3,269,406

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	Six Months Ended June 30 , 2010	2009
Materials Purchased from Related Parties	$ 9,596,184	$ 4,986,222
Technology Purchased from Related Parties	176,478	73,186
Equipment Purchased from Related Parties	1,334,947	1,503,726
Total	$ 11,107,609	$ 6,563,134

Related receivables (June 30, 2010, unaudited):

	June 30, 2010	December 31, 2009
Accounts receivable	$ 3,386,976	$ 1,441,939
Other receivables	218,699	65,416
Total	$ 3,605,675	$ 1,507,355

Related advances (June 30, 2010, unaudited):

	June 30, 2010	December 31, 2009
Advanced Equipment Payment to Related Parties	$ 5,676,085	$ 2,579,319
Advanced Expenses and Others to Related Parties	930,007	-
Total	$ 6,606,092	$ 2,579,319

Related payables (June 30, 2010 unaudited)

	June 30, 2010	December 31, 2009
Accounts payable	$ 2,570,035	$ 1,537,827

These transactions were consummated under similar terms as those with the Company's customers and suppliers.

As of August 9, 2010, the date the Company issued this financial statement, Hanlin Chen, Chairman, owns 55.76% of the common stock of the Company and has the effective power to control the vote on substantially all significant matters without the approval of other stockholders.

30. Commitments and contingencies

Legal Proceedings - The Company is not currently a party to any threatened or pending legal proceedings, other than incidental litigation arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

The following table summarizes the Company's major contractual payment obligations and commitments as of June 30, 2010 (unaudited):

	Payment Obligations by Period					
	2010 (a)	2011	2012	2013	Thereafter	Total
Obligations for service agreements	$110,000	$110,000	$-	$-	$-	$220,000
Interest and make-whole on Convertible Notes	2,107,085	5,912,500	-	-		8,019,585
Obligations for purchasing agreements	14,238,674	3,557,421	$-	$-	-	17,796,095
Total	$16,455,759	$9,579,921	$-	$-	$-	$26,035,680

(a) Remaining 6 months in 2010

31. Off-balance sheet arrangements

At June 30, 2010 and 2009 (unaudited), the Company did not have any transactions, obligations or relationships that could be considered off-balance sheet arrangements.

32. Segment reporting

The accounting policies of the product sectors are the same as those described in the summary of significant accounting policies except that the disaggregated financial results for the product sectors have been prepared using a management approach, which is consistent with the basis and manner in which management internally disaggregates financial information for the purposes of assisting them in making internal operating decisions. Generally, the Company evaluates performance based on stand-alone product sector operating income and accounts for inter segment sales and transfers as if the sales or transfers were to third parties, at current market prices.

During the six months ended June 30, 2010 and 2009 (unaudited), the Company had nine product sectors, five of them were principal profit makers, which were reported as separate sectors which engaged in the production and sales of power steering (Henglong), power steering (Jiulong), power steering (Shenyang), power pumps (Zhejiang), and power steering (Wuhu). The other four sectors which were established in 2005, 2006 and 2007 respectively, engaged in the production and sales of sensor modular (USAI), electronic power steering (Jielong), power steering (Hengsheng), and provider of after sales and R&D services (HLUSA). Since the revenues, net income and net assets of these four sectors are less than 10% of its segment in the consolidated financial statements, the Company incorporated these four sectors into "other sectors".

The Company's product sectors information is as follows:

	Henglong	Jiulong	Shenyang	Zhejiang	Wuhu	Other sectors	Other *	Total
For the Three Months Ended June 30, 2010 (unaudited-restated):								
Revenue								
Net product sales – external	$39,261,293	$25,214,971	$7,361,646	$5,502,059	$5,470,844	$2,270,325	$-	$85,081,138
	8,692,999	753,536	1,875,804					

Net product sales –
internal