



**Jinhua City Industrial Zone**  
**Jinhua, Zhejiang Province**  
**People's Republic of China**  
**Post Code 321016**

(Address of principal executive offices)

**(86 - 579) 82239856**

(Registrant's telephone number, including area code)

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

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

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

|                                               |                           |
|-----------------------------------------------|---------------------------|
| Large accelerated filer                       | Accelerated filer         |
| Non-accelerated filer                         | Smaller reporting company |
| (Do not check if a smaller reporting company) | Emerging growth company   |

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

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

As of August 3, 2018, the registrant had 55,979,502 shares of common stock issued and 51,471,944 shares of common stock outstanding, par value \$0.001 per share.



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**PART I — FINANCIAL INFORMATION**

## Item 1. Financial Statements.

**KANDI TECHNOLOGIES GROUP, INC.  
AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEET**

|                                                                                                                                                | June 30,<br>2018<br>(Unaudited) | December 31,<br>2017 |
|------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------|----------------------|
| Current assets                                                                                                                                 |                                 |                      |
| Cash and cash equivalents                                                                                                                      | \$ 1,612,459                    | \$ 4,891,808         |
| Restricted cash                                                                                                                                | 7,878,200                       | 11,218,688           |
| Accounts receivable(net of allowance for doubtful accounts of \$331,362 and \$133,930 as of June 30, 2018 and December 31, 2017, respectively) | 34,071,931                      | 34,397,858           |
| Inventories (net of provision for slow moving inventory of \$938,624 and \$620,919 as of June 30, 2018 and December 31, 2017, respectively)    | 11,644,868                      | 15,979,794           |
| Notes receivable from JV Company and related party                                                                                             | -                               | 1,137,289            |
| Other receivables                                                                                                                              | 2,342,060                       | 2,650,668            |
| Prepayments and prepaid expense                                                                                                                | 6,099,704                       | 6,536,839            |
| Due from employees                                                                                                                             | 4,527                           | 7,070                |
| Advances to suppliers                                                                                                                          | 15,211,522                      | 14,908,385           |
| Amount due from JV Company, net                                                                                                                | 64,775,429                      | 146,422,440          |
| Amount due from related party                                                                                                                  | -                               | 162,048              |
| <b>TOTAL CURRENT ASSETS</b>                                                                                                                    | <b>143,640,700</b>              | <b>238,312,887</b>   |
| <br><b>LONG-TERM ASSETS</b>                                                                                                                    |                                 |                      |
| Property, Plant and equipment, net                                                                                                             | 12,806,094                      | 12,000,971           |
| Land use rights, net                                                                                                                           | 12,377,307                      | 12,666,047           |
| Construction in progress                                                                                                                       | 69,541,416                      | 53,083,925           |
| Deferred taxes assets                                                                                                                          | 3,301,698                       | 4,383,425            |
| Long Term Investment                                                                                                                           | -                               | 1,460,034            |
| Investment in JV Company                                                                                                                       | 154,866,326                     | 70,681,013           |
| Goodwill                                                                                                                                       | 24,156,275                      | 322,591              |
| Intangible assets                                                                                                                              | 4,811,077                       | 331,116              |
| Advances to suppliers                                                                                                                          | -                               | 21,592,918           |
| Other long term assets                                                                                                                         | 6,855,927                       | 7,590,734            |
| Amount due from JV Company, net                                                                                                                | -                               | 15,907,183           |
| <b>TOTAL Long-Term Assets</b>                                                                                                                  | <b>288,716,120</b>              | <b>200,019,957</b>   |

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|                                                                                                                                                                                                      |               |               |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------|---------------|
| TOTAL ASSETS                                                                                                                                                                                         | \$432,356,820 | \$438,332,844 |
| CURRENT LIABILITIES                                                                                                                                                                                  |               |               |
| Accounts payables                                                                                                                                                                                    | \$92,759,784  | \$111,595,540 |
| Other payables and accrued expenses                                                                                                                                                                  | 5,323,548     | 6,556,209     |
| Short-term loans                                                                                                                                                                                     | 32,482,003    | 33,042,864    |
| Customer deposits                                                                                                                                                                                    | 274,205       | 205,544       |
| Notes payable                                                                                                                                                                                        | 18,848,520    | 28,075,945    |
| Income tax payable                                                                                                                                                                                   | 1,181,776     | 2,902,699     |
| Due to employees                                                                                                                                                                                     | 10,521        | 35,041        |
| Deferred income                                                                                                                                                                                      | 1,404,431     | 2,191,143     |
| Total Current Liabilities                                                                                                                                                                            | 152,284,788   | 184,604,985   |
| LONG-TERM LIABILITIES                                                                                                                                                                                |               |               |
| Long term bank loans                                                                                                                                                                                 | 30,064,737    | 30,737,547    |
| Contingent liability                                                                                                                                                                                 | 5,345,985     | -             |
| Other long-term liability                                                                                                                                                                            | 549,568       | -             |
| Total Long-Term Liabilities                                                                                                                                                                          | 35,960,290    | 30,737,547    |
| TOTAL LIABILITIES                                                                                                                                                                                    | 188,245,078   | 215,342,532   |
| STOCKHOLDER'S EQUITY                                                                                                                                                                                 |               |               |
| Common stock, \$0.001 par value; 100,000,000 shares authorized; 54,257,312 and 48,036,538 shares issued and 51,297,475 and 48,036,538 outstanding at June 30,2018 and December 31,2017, respectively | 51,297        | 48,037        |
| Additional paid-in capital                                                                                                                                                                           | 254,193,380   | 233,055,348   |
| Retained earnings (the restricted portion is \$4,422,033 and \$4,422,033 at June 30,2018 and December 31,2017, respectively)                                                                         | 1,300,210     | (3,802,310 )  |
| Accumulated other comprehensive loss                                                                                                                                                                 | (11,433,145 ) | (6,310,763 )  |
| TOTAL STOCKHOLDERS' EQUITY                                                                                                                                                                           | 244,111,742   | 222,990,312   |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY                                                                                                                                                           | \$432,356,820 | \$438,332,844 |

See accompanying notes to condensed consolidated financial statements

**KANDI TECHNOLOGIES GROUP, INC.  
AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS) AND  
COMPREHENSIVE INCOME (LOSS)  
(UNAUDITED)**

|                                                  | Three Months Ended |                  | Six Months Ended |                  |
|--------------------------------------------------|--------------------|------------------|------------------|------------------|
|                                                  | June 30,<br>2018   | June 30,<br>2017 | June 30,<br>2018 | June 30,<br>2017 |
| REVENUES FROM UNRELATED PARTY, NET               | 11,618,855         | 1,153,555        | \$17,351,318     | \$4,116,486      |
| REVENUES FROM JV COMPANY AND RELATED PARTY, NET  | 4,740,751          | 26,171,724       | 7,344,195        | 27,483,366       |
| REVENUES, NET                                    | 16,359,606         | 27,325,279       | 24,695,513       | 31,599,852       |
| COST OF GOODS SOLD                               | (14,301,594)       | (23,568,343)     | (21,291,550)     | (27,175,584)     |
| GROSS PROFIT                                     | 2,058,012          | 3,756,936        | 3,403,963        | 4,424,268        |
| OPERATING EXPENSES:                              |                    |                  |                  |                  |
| Research and development                         | (642,889 )         | (5,142,041 )     | (1,400,187 )     | (25,911,773)     |
| Selling and marketing                            | (228,173 )         | (402,253 )       | (976,398 )       | (760,562 )       |
| General and administrative                       | (3,861,263 )       | (1,558,652 )     | (3,463,092 )     | (9,877,946 )     |
| Total Operating Expenses                         | (4,732,325 )       | (7,102,946 )     | (5,839,677 )     | (36,550,281)     |
| (LOSS) FROM OPERATIONS                           | (2,674,313 )       | (3,346,010 )     | (2,435,714 )     | (32,126,013)     |
| OTHER INCOME(EXPENSE):                           |                    |                  |                  |                  |
| Interest income                                  | 456,784            | 559,425          | 1,399,777        | 1,090,067        |
| Interest expense                                 | (471,616 )         | (548,810 )       | (1,022,033 )     | (1,163,263 )     |
| Change in fair value of contingent consideration | 686,833            | -                | 3,367,012        | -                |
| Government grants                                | 15,558             | 262,137          | 110,813          | 5,329,611        |
| Share of income (loss) after tax of JV           | 2,372,696          | (8,738,254 )     | 3,167,751        | (13,899,967)     |
| Other income , net                               | 627,582            | 121,556          | 650,559          | 150,177          |
| Total other income (expense), net                | 3,687,837          | (8,343,946 )     | 7,673,879        | (8,493,375 )     |
| INCOME (LOSS) BEFORE INCOME TAXES                | 1,013,524          | (11,689,956)     | 5,238,165        | (40,619,388)     |
| INCOME TAX BENEFIT (EXPENSE)                     | 361,001            | 131,939          | (135,645 )       | 4,907,936        |
| NET INCOME (LOSS)                                | 1,374,525          | (11,558,017)     | 5,102,520        | (35,711,452)     |
| OTHER COMPREHENSIVE (LOSS) INCOME                |                    |                  |                  |                  |
| Foreign currency translation                     | (12,587,622)       | 3,118,462        | (5,122,382 )     | 4,910,278        |

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|                                                |                 |                 |              |                 |
|------------------------------------------------|-----------------|-----------------|--------------|-----------------|
| COMPREHENSIVE (LOSS)                           | \$ (11,213,097) | \$ (8,439,555 ) | \$ (19,862 ) | \$ (30,801,174) |
| WEIGHTED AVERAGE SHARES OUTSTANDING<br>BASIC   | 51,140,542      | 47,974,974      | 50,893,356   | 47,854,351      |
| WEIGHTED AVERAGE SHARES OUTSTANDING<br>DILUTED | 51,140,542      | 47,974,974      | 50,893,356   | 47,854,351      |
| NET INCOME (LOSS) PER SHARE, BASIC             | \$0.03          | \$ (0.24 )      | \$0.10       | \$ (0.75 )      |
| NET INCOME (LOSS) PER SHARE, DILUTED           | \$0.03          | \$ (0.24 )      | \$0.10       | \$ (0.75 )      |

See accompanying notes to condensed consolidated financial statements



KANDI TECHNOLOGIES GROUP, INC.  
AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

|                                                                                  | Six Months Ended |                 |
|----------------------------------------------------------------------------------|------------------|-----------------|
|                                                                                  | June 30,<br>2018 | June 30, 2017   |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                     |                  |                 |
| Net income (loss)                                                                | \$5,102,520      | \$(35,711,452 ) |
| Adjustments to reconcile net income to net cash provided by operating activities |                  |                 |
| Depreciation and amortization                                                    | 1,791,762        | 2,334,776       |
| Assets impairments                                                               | 341,261          | 38,548          |
| Allowance for doubtful accounts                                                  | (7,257 )         | -               |
| Deferred taxes                                                                   | -                | (5,415,959 )    |
| Share of income after tax of JV Company                                          | (3,167,751 )     | 13,899,967      |
| Reserve for fixed assets                                                         | (54,799 )        | -               |
| Change in fair value of contingent consideration                                 | (3,367,012 )     | -               |
| Stock compensation cost                                                          | 222,259          | 4,493,187       |
| Changes in operating assets and liabilities, net of effects of acquisition:      |                  |                 |
| (Increase) Decrease In:                                                          |                  |                 |
| Accounts receivable                                                              | (36,123,904)     | (2,826,433 )    |
| Deferred taxes assets                                                            | (53,330 )        | -               |
| Notes receivable                                                                 | 502,623          | -               |
| Notes receivable from JV Company and related party                               | 2,060,755        | 4,875,795       |
| Inventories                                                                      | 5,020,163        | (1,242,422 )    |
| Other receivables and other assets                                               | 927,544          | (498,376 )      |
| Due from employee                                                                | (22,355 )        | (23,344 )       |
| Advances to supplier and prepayments and prepaid expenses                        | (2,626,098 )     | 23,946,781      |
| Advances to suppliers-long term                                                  | -                | (4,099,879 )    |
| Amount due from JV Company                                                       | (39,263,079)     | (21,853,571 )   |
| Amount due from JV Company-Long term                                             | 15,907,183       | -               |
| Due from related party                                                           | 165,614          | -               |
| Increase (Decrease) In:                                                          |                  |                 |
| Accounts payable                                                                 | 41,319,755       | 25,017,146      |
| Other payables and accrued liabilities                                           | 25,636,794       | 127,252         |
| Notes payable                                                                    | (11,936,770)     | (2,731,692 )    |
| Customer deposits                                                                | 75,010           | 132,765         |
| Income tax payable                                                               | (1,837,147 )     | (31,314 )       |
| Deferred income                                                                  | (779,240 )       | (5,077,291 )    |
| Loss contingency-litigation                                                      | -                | 2,909,151       |
| Net cash used in operating activities                                            | \$(165,499 )     | \$(1,736,365 )  |

**CASH FLOWS FROM INVESTING ACTIVITIES:**

|                                                                    |              |              |
|--------------------------------------------------------------------|--------------|--------------|
| Purchases of property, plant and equipment, net                    | (122,407 )   | (128,509 )   |
| Purchases of land use rights and other intangible assets           | (107,917 )   | -            |
| Acquisition of Jinhua An Kao (net of cash received)                | (3,694,275 ) | -            |
| Purchases of construction in progress                              | (48,042 )    | (1,029,516 ) |
| Reimbursement of capitalize interests for construction in progress | 1,860,287    | -            |
| Long Term Investment                                               | 1,492,162    | -            |
| Short term investment                                              | -            | 4,509,183    |
| Net cash (used in) provided by investing activities                | \$(620,192 ) | \$3,351,158  |

**CASH FLOWS FROM FINANCING ACTIVITIES:**

|                                                     |                |              |
|-----------------------------------------------------|----------------|--------------|
| Proceeds from short-term bank loans                 | 14,764,553     | 13,963,923   |
| Repayments of short-term bank loans                 | (14,764,553)   | (17,018,531) |
| Repayments of long-term bank loans                  | (157,070 )     | -            |
| Proceeds from notes payable                         | 34,702,510     | 5,713,368    |
| Repayment of notes payable                          | (40,349,566)   | -            |
| Net cash (used in) provided by financing activities | \$(5,804,126 ) | \$2,658,760  |

**NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS AND RESTRICTED CASH**

|                                                                           |                   |                   |
|---------------------------------------------------------------------------|-------------------|-------------------|
|                                                                           | (6,589,817 )      | 4,273,553         |
| Effect of exchange rate changes on cash                                   | (30,020 )         | 648,835           |
| <b>CASH AND CASH EQUIVALENTS AND RESTRICTED CASH AT BEGINNING OF YEAR</b> | <b>16,110,496</b> | <b>25,193,298</b> |

**CASH AND CASH EQUIVALENTS AND RESTRICTED CASH AT END OF PERIOD**

|  |           |            |
|--|-----------|------------|
|  | 9,490,659 | 30,115,686 |
|--|-----------|------------|

**SUPPLEMENTARY CASH FLOW INFORMATION**

|                   |           |           |
|-------------------|-----------|-----------|
| Income taxes paid | 1,815,156 | 1,001,501 |
| Interest paid     | 848,232   | 742,958   |

**SUPPLEMENTAL NON-CASH DISCLOSURES:**

|                                                                                                           |            |            |
|-----------------------------------------------------------------------------------------------------------|------------|------------|
| Advances to suppliers-long term transferred to construction in progress                                   | 22,068,080 | 8,712,000  |
| Advances to suppliers transferred to construction in progress                                             | 6,090,219  | -          |
| Purchase of construction in progress in accounts payable                                                  | -          | 5,974,383  |
| Settlement of due from JV Company and related parties with notes receivable                               | 36,310,747 | 22,819,847 |
| Settlement of accounts receivables with notes receivable from unrelated parties                           | 39,932,517 | 1,076,386  |
| Assignment of notes receivable from unrelated parties to supplier to settle accounts payable              | 12,570,974 | 1,076,386  |
| Assignment of notes receivable from JV Company and related parties to supplier to settle accounts payable | 35,176,703 | 18,348,424 |
| Settlement of accounts payable with notes payables                                                        | 19,480,843 | 18,839,444 |
| Deferred tax changed to other comprehensive income                                                        | -          | 24,486     |
| Acquisition of Jinhua An Kao by stock                                                                     | 20,718,859 | -          |
| Cancellation of notes payables                                                                            | 10,994,880 | -          |
| Amount due from JV Company converted to investment in JV Company                                          | 85,602,991 | -          |
| Adjustment of construction in progress with accounts payable                                              | 8,299,226  | -          |
| Adjustment of advance to supplier with accounts payable                                                   | 3,703,808  | -          |

See accompanying notes to condensed consolidated financial statements

**NOTE 1 - ORGANIZATION AND PRINCIPAL ACTIVITIES**

Kandi Technologies Group, Inc. (“Kandi Technologies”) was incorporated under the laws of the State of Delaware on March 31, 2004. Kandi Technologies changed its name from Stone Mountain Resources, Inc. to Kandi Technologies, Corp. on August 13, 2007, and on December 21, 2012, Kandi Technologies changed its name to Kandi Technologies Group, Inc. As used herein, the term the “Company” means Kandi Technologies and its operating subsidiaries, as described below.

Headquartered in Jinhua City, Zhejiang Province, People’s Republic of China, the Company is one of the People’s Republic of China’s (“China”) leading producers and manufacturers of electric vehicle (“EV”) products, EV parts, and off-road vehicles for sale in China and global markets. The Company conducts its primary business operations through its wholly-owned subsidiary, Zhejiang Kandi Vehicles Co., Ltd. (“Kandi Vehicles”) and Sportsman Country, LLC (“Sportsman Country”), and the partially and wholly-owned subsidiaries of Kandi Vehicles.

The Company’s organizational chart as of August 3, 2018 is as follows:

Operating Subsidiaries:

Pursuant to the agreements executed in January 2011, Kandi Vehicles is entitled to 100% of the economic benefits, voting rights and residual interests (100% of profits and losses) of Jinhua Kandi New Energy Vehicles Co., Ltd. (“Kandi New Energy”). Kandi New Energy currently holds battery pack production licensing rights and supplies battery packs to the JV Company (as such term is defined below).

In April 2012, pursuant to the agreement, the Company acquired 100% of Yongkang Scrou Electric Co, Ltd. (“Yongkang Scrou”), a manufacturer of automobile and EV parts. Yongkang Scrou currently manufactures and sells EV drive motors, EV controllers, air conditioners and other electric products to the JV Company.

In March 2013, pursuant to a joint venture agreement (the “JV Agreement”) entered into by Kandi Vehicles and Shanghai Maple Guorun Automobile Co., Ltd. (“Shanghai Guorun”), a 99%-owned subsidiary of Geely Automobile Holdings Ltd. (“Geely”), the parties established Zhejiang Kandi Electric Vehicles Co., Ltd. (the “JV Company”) to develop, manufacture and sell EV products and related auto parts. Each of Kandi Vehicles and Shanghai Guorun has 50% ownership interest in the JV Company. In March 2014, the JV Company changed its name to Kandi Electric Vehicles Group Co., Ltd. At present, the JV Company is a holding company and all products are manufactured by its subsidiaries. In an effort to improve the JV Company’s development, Zhejiang Geely Holding Group, the parent company of Geely, became a JV Company shareholder on October 26, 2016, through its purchase of the 50% equity of the JV Company held by Shanghai Guorun at a premium price (a price exceeding the cash amount of the aggregate of the original investment and the shared profits over the years). On May 19, 2017, due to business development, Zhejiang Geely Holding Group, Ltd. (Geely Holding) transferred its equity in the JV Company to Geely Group (Ningbo) Ltd., a company wholly owned by Mr. Li Shufu, Chairman of the Board of Geely Holding. On May 23, 2018, in order to obtain the manufacturing license, according to the recent notice (FGBCY[2018] No.547) from National Development and Reform Commission in China, the JV Company increased its registered capital by RMB 1.09 billion (approximately \$165 million), of which Kandi Vehicle increased its capital contribution to the JV Company by converting its RMB 545 million (approximately \$83 million) loans lent to the JV Company to the JV Company’s registered capital. Geely Group, Ltd. (“Geely Group”) became a new shareholder of the JV Company by investing RMB 545 million (approximately \$83 million). After this restructure, Kandi Vehicles, Geely Group and Geely Group (Ningbo) Ltd. owns 50%, 26.08%, and 23.92% of equity of the JV Company, respectively.

In March 2013, Kandi Vehicles formed Kandi Electric Vehicles (Changxing) Co., Ltd. (“Kandi Changxing”) in the Changxing (National) Economic and Technological Development Zone. Kandi Changxing is engaged in the production of EV products. In the fourth quarter of 2013, Kandi Vehicles entered into an ownership transfer agreement with the JV Company pursuant to which Kandi Vehicles transferred 100% of its ownership in Kandi Changxing to the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Kandi Changxing.

In July 2013, Zhejiang ZuoZhongYou Electric Vehicle Service Co., Ltd. (the “Service Company”) was formed. The Service Company is engaged in various pure EV leasing businesses, generally referred to as the Micro Public Transportation (“MPT”) and other EV share programs. Kandi Vehicle had a 9.5% ownership interest in the Service Company. After exploration and practice in the last five years, the Company realized a large sum of capital still needs to be invested in order to increase the size of EV share programs. Considering Geely Group has the abilities to grow the Service Company’s business to be stronger and bigger and a successful growth of the Service Company will have positive impact on the development of the JV Company’s business, Kandi Vehicle transferred its 9.5% of ownership interest in the Service Company to Geely Group in June 2018.

In November 2013, Kandi Electric Vehicles Jinhua Co., Ltd. (“Kandi Jinhua”) was formed by the JV Company. The JV Company has a 100% ownership interest in Kandi Jinhua, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Kandi Jinhua. In April 2017, Kandi Jinhua was reorganized to be owned directly by Kandi Jiangsu, which is 100% directly owned by the JV Company.

In November 2013, Zhejiang JiHeKang Electric Vehicle Sales Co., Ltd. (“JiHeKang”) was formed by the JV Company. JiHeKang is engaged in the car sales business. The JV Company has a 100% ownership interest in JiHeKang, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in JiHeKang. In April 2017, JiHeKang was reorganized to be owned directly by Kandi Jiangsu, which is 100% directly owned by the JV Company.

In December 2013, the JV Company entered into an ownership transfer agreement with Shanghai Guorun, pursuant to which the JV Company acquired a 100% ownership interest in Kandi Electric Vehicles (Shanghai) Co., Ltd. (“Kandi Shanghai”). As a result, Kandi Shanghai is a wholly-owned subsidiary of the JV Company, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Kandi Shanghai.

In January 2014, Kandi Electric Vehicles Jiangsu Co., Ltd. (“Kandi Jiangsu”) was formed by the JV Company. The JV Company has a 100% ownership interest in Kandi Jiangsu, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Kandi Jiangsu. Kandi Jiangsu is mainly engaged in EV research and development, manufacturing, and sales. As of the date of this report, Kandi Jiangsu directly owns 100% of JiHeKang, JiHeKang Service Company, Liuchuang and KandiJinhua.

In November 2015, Hangzhou Puma Investment Management Co., Ltd. (“Puma Investment”) was formed by the JV Company. Puma Investment provides investment and consulting services. The JV Company has a 50% ownership interest in Puma Investment (the other 50% is owned by Zuozhongyou Electric Vehicles Service (Hangzhou) Co., Ltd., a subsidiary of the Service Company), and the Company, indirectly through the JV Company, has a 25% economic interest in Puma Investment.

In November 2015, Hangzhou JiHeKang Electric Vehicle Service Co., Ltd. (the “JiHeKang Service Company”) was formed by the JV Company. The JiHeKang Service Company focuses on after-market services for EV products. In April 2017, JiHeKang Service Company was reorganized to be owned directly by Kandi Jiangsu, which is 100% directly owned by the JV Company. The JV Company has a 100% ownership interest in the JiHeKang Service Company, and the Company, indirectly through the JV Company, has a 50% economic interest in the JiHeKang Service Company.

In December 2015, Zhejiang JiHeKang Electric Vehicle Sales Co., Ltd. Tianjin Branch (“JiHeKang Tianjin”) was formed by JiHeKang. JiHeKang Tianjin is engaged in the car sales business. Since JiHeKang is 100% owned by the JV Company, the JV Company has a 100% ownership interest in JiHeKang Tianjin, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in JiHeKang Tianjin.

In January 2016, Kandi Electric Vehicles (Wanning) Co., Ltd. was renamed Kandi Electric Vehicles (Hainan) Co., Ltd. (“Kandi Hainan”). Kandi Hainan was originally formed in Wanning City in Hainan Province by Kandi Vehicles and Kandi New Energy in April 2013, and was transferred to Haikou City in January 2016. Kandi Vehicles has a 90% ownership interest in Kandi Hainan, and Kandi New Energy has the remaining 10% ownership interest. In fact, Kandi Vehicles is, effectively, entitled to 100% of the economic benefits, voting rights and residual interests (100% of the profits and losses) of Kandi Hainan as Kandi Vehicles is entitled to 100% of the economic benefits, voting rights and residual interests of Kandi New Energy.

In August 2016, Jiangsu JiDian Electric Vehicle Sales Co., Ltd. (“Jiangsu JiDian”) was formed by JiHeKang. Jiangsu JiDian is engaged in the car sales business. Since JiHeKang is 100% owned by the JV Company, the JV Company has a 100% ownership interest in Jiangsu JiDian, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Jiangsu JiDian.



In October 2016, JiHeKang acquired Tianjin BoHaiWan Vehicle Sales Co., Ltd. (“Tianjin BoHaiWan”), which is engaged in the car sales business. Since JiHeKang is 100% owned by the JV Company, the JV Company has a 100% ownership interest in Tianjin BoHaiWan, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Tianjin BoHaiWan.

In November 2016, Changxing Kandi Vehicle Maintenance Co., Ltd. (“Changxing Maintenance”) was formed by Kandi Changxing. Changxing Maintenance is engaged in the car repair and maintenance business. In December 2017, the Service Company entered into an agreement with the JV Company to acquire 100% of Changxing Maintenance for RMB 1,089,887 or approximately \$167,501. The transaction was completed in April 2018.

In November 2016, Guangdong JiHeKang Electric Vehicle Sales Co., Ltd. (“Guangdong JiHeKang”) was formed by JiHeKang. Guangdong JiHeKang is engaged in the car sales business. Since JiHeKang is 100% owned by the JV Company, the JV Company has a 100% ownership interest in Guangdong JiHeKang, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Guangdong JiHeKang.

In March 2017, Hangzhou Liuchuang Electric Vehicle Technology Co., Ltd. (“Liuchuang”) was formed by Kandi Jiangsu. Since Kandi Jiangsu is 100% owned by the JV Company, the JV Company has a 100% ownership interest in Liuchuang, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Liuchuang.

In April 2017, in order to promote business development, Kandi Jinhua, JiHeKang, and the JiHeKang Service Company were reorganized to become subsidiaries of Kandi Jiangsu. As the JV Company has a 100% ownership interest in Kandi Jiangsu, the JV Company has 100% ownership interests in Kandi Jinhua, JiHeKang, and the JiHeKang Service Company; the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Kandi Jinhua, JiHeKang, and the JiHeKang Service Company.

In December 2017, Zhejiang Chang Dian Technology Co., Ltd. (“Zhejiang Chang Dian”) was formed by the JV Company. Zhejiang Chang Dian is primarily engaged in the battery replacement business. Since Zhejiang Chang Dian is 100% owned by the JV Company, and the Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Zhejiang Chang Dian.

On December 18, 2017, Kandi Vehicles and the sole shareholder of Jinhua An Kao Power Technology Co., Ltd. (“Jinhua An Kao”) entered into a Share Transfer Agreement and a Supplementary Agreement, pursuant to which Kandi Vehicles acquired Jinhua An Kao. The two agreements were signed on December 12, 2017 and the closing took place on January 3, 2018. Kandi Vehicles acquired 100% of the equity interests of Jinhua An Kao for a purchase price of

approximately RMB 25.93 million (approximately \$3.9 million) in cash. In addition, pursuant to the Supplementary Agreement by and between the two parties, the Company issued a total of 2,959,837 shares of restrictive stock, or 6.2% of the Company's total outstanding shares of the common stock to the shareholder of Jinhua An Kao. An additional 2,959,837 shares are placed as make good shares for the undertaking of Jinhua An Kao to achieve no less than a total of RMB 120,000,000 (approximately \$18.1 million) net income over the course of the following three years. The Supplementary Agreement sets forth the terms and conditions of the issuance of these shares, including that the Company has the voting rights of the make good shares until conditions for vesting those shares are satisfied.

In April 2018, Zhejiang Chang Dian Technology Co., Ltd. Hangzhou Tonglu Branch (“Chang Dian Tonglu”) was formed by Zhejiang Chang Dian. Chang Dian Tonglu is primarily engaged in the battery replacement business..

In April 2018, Zhejiang Chang Dian Technology Co., Ltd. Changxing Branch (“Chang Dian Changxing”) was formed by Zhejiang Chang Dian. Chang Dian Changxing is primarily engaged in the battery replacement business.

On May 31, 2018, the Company entered into a Membership Interests Transfer Agreement (the “Transfer Agreement”) with the two members of Sportsman Country under which the Company acquired 100% of the ownership of Sportsman Country. Sportsman Country is a Dallas based sales company primarily engaged in the wholesale of off-road vehicle products, with a small percentage of business in off-road vehicle parts wholesale and retail. According to the terms of the Transfer Agreement, the Company shall transfer \$10.0 million worth of restricted shares to acquire 100% membership interests in Sportsman Country, of which the Company was required to issue \$1.0 million worth of corresponding restricted shares within 30 days from the signing date of the Transfer Agreement, and the remaining \$9.0 million worth of corresponding restricted shares will be released from escrow based on Sportsman Country’s pre-tax profit performance over the course of the following three years. The transaction closed in July 2018.

The Company’s primary business operations are designing, developing, manufacturing and commercializing EV products, EV parts and off-road vehicles. As part of its strategic objective of becoming a leading manufacturer of EV products (through the JV Company) and related services, the Company has increased its focus on pure EV-related products, and actively expanded China market and international market.

## **NOTE 2 - LIQUIDITY**

The Company had a working capital deficit of \$8,644,088 as of June 30, 2018, a decrease of \$62,351,990 from a working capital surplus of \$53,707,902 as of December 31, 2017.

As of June 30, 2018, the Company had credit lines available from commercial banks of \$32,482,003. Although the Company expects that most of its outstanding trade receivables from customers will be collected in the next twelve months, there are uncertainties about the timing in collecting these receivables, especially the receivables due from the JV Company, because most of them are indirectly impacted by the progress of the receipt of government subsidies. Since the amount due from the JV Company accounts for the majority of the Company’s outstanding receivables, and since the Company cannot control the timing of the receipt of government subsidies, the Company believes that its internally-generated cash flows may not be sufficient to support the growth of future operations and to repay short-term bank loans for the next twelve months. However, the Company believes its access to existing financing sources and its good credit will enable it to meet its obligations and fund its ongoing operations for the next twelve

months. The Company expects to approximately maintain the current debt level for the next twelve months given the Company's current financial position and business development needs.

The Company's primary need for liquidity is to fund working capital requirements of the Company's businesses, capital expenditures and for general operational purposes, including debt repayment. The Company has incurred losses and experienced negative operating cash flows for the past years, and accordingly, the Company has taken a number of actions to continue to support its operations and meet its obligations. The Company has historically financed its operations through short-term commercial bank loans from Chinese banks. The term of these loans is typically for one year, and upon the payment of all outstanding principal and interest on a particular loan, the banks have typically rolled over the loan for an additional one-year term, with adjustments made to the interest rate to reflect prevailing market rates. This practice has been ongoing and the Company believes that short-term bank loans will remain available on normal trade terms if needed. For the remainder of 2018, the management will take measures to grow the business and further improve the Company's liquidity. The Company acknowledges that it continues to face a challenging competitive environment and expects to take actions that will enhance the Company's liquidity and financial flexibility to support the Company's operation needs.

We finance our ongoing operating activities by using funds from our operations and external credit or financing arrangements. We routinely monitor current and expected operational requirements and financial market conditions to evaluate the use of available financing sources. Considering our existing working capital position and our ability to access debt funding sources, we believe that our operations and borrowing resources are sufficient to provide for our current and foreseeable capital requirements to support our ongoing operations for the next twelve months.

### **NOTE 3 - BASIS OF PRESENTATION**

The Company maintains its general ledger and journals using the accrual method of accounting for financial reporting purposes. The Company's financial statements and notes are the representations of the Company's management. Accounting policies adopted by the Company conform to generally accepted accounting principles in the United States and have been consistently applied in the Company's presentation of its financial statements.

### **NOTE 4 - PRINCIPLES OF CONSOLIDATION**

The Company's consolidated financial statements reflect the accounts of the Company and its ownership interests in the following subsidiaries:

- (1) Continental Development Limited ("Continental"), a wholly-owned subsidiary of the Company incorporated under the laws of Hong Kong;
- (2) Kandi Vehicles, a wholly-owned subsidiary of Continental;

- Kandi New Energy, a 50%-owned subsidiary of Kandi Vehicles (Mr. Hu Xiaoming owns the other 50%). Pursuant to agreements executed in January 2011, Mr. Hu Xiaoming contracted with Kandi Vehicles for the operation and management of Kandi New Energy and put his shares of Kandi New Energy into escrow. As a result, Kandi Vehicles is entitled to 100% of the economic benefits, voting rights and residual interests of Kandi New Energy;
- (3)
- (4) Yongkang Scrou, a wholly-owned subsidiary of Kandi Vehicles;
- (5) Kandi Hainan, a subsidiary, 10% owned by Kandi New Energy and 90% owned by Kandi Vehicles; and
- (6) Jinhua An Kao, a wholly-owned subsidiary of Kandi Vehicles.

## Equity Method Investees

The Company's consolidated net income also includes the Company's proportionate share of the net income or loss of its equity method investees as follows:

- (1) The JV Company, a 50% owned subsidiary of Kandi Vehicles;
- (2) Kandi Changxing, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Kandi Changxing;  
  
Kandi Jinhua, a wholly-owned direct subsidiary of Kandi Jiangsu, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Kandi Jinhua;
- (3) JiHeKang, a wholly-owned direct subsidiary of Kandi Jiangsu, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in JiHeKang;
- (4) Kandi Shanghai, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Kandi Shanghai;
- (5) Kandi Jiangsu, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Kandi Jiangsu;  
  
The JiHeKang Service Company, a wholly-owned direct subsidiary of Kandi Jiangsu, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in the JiHeKang Service Company.
- (6) Tianjin BoHaiWan, a wholly-owned direct subsidiary of JiHeKang, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Tianjin BoHaiWan;
- (7) Liuchuang, a wholly-owned direct subsidiary of Kandi Jiangsu, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Liuchuang;
- (8) Jiangsu JiDian, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Jiangsu JiDian;
- (9) (10)

JiHeKang Tianjin, a wholly-owned direct subsidiary of Kandi Jiangsu, a wholly-owned subsidiary of the JV (11) Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in JiHeKang Tianjin;

Guangdong JiHeKang, a wholly-owned direct subsidiary of JiHeKang, a wholly-owned subsidiary of the JV (12) Company. The Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Guangdong JiHeKang; and

Zhejiang Chang Dian, a wholly-owned subsidiary of the JV Company. The Company, indirectly through its 50% (13) ownership interest in the JV Company, has a 50% economic interest in Zhejiang Chang Dian.

Chang Dian Tonglu, branch of Zhejiang Chang Dian, a wholly-owned subsidiary of the JV Company. The (14) Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Chang Dian Tonglu.

Chang Dian Changxing, a branch of Zhejiang Chang Dian, a wholly-owned subsidiary of the JV Company. The (15) Company, indirectly through its 50% ownership interest in the JV Company, has a 50% economic interest in Chang Dian Changxing.

All intra-entity profits and losses with regards to the Company's equity method investees have been eliminated.

## **NOTE 5 - USE OF ESTIMATES**

The preparation of financial statements in conformity with generally accepted accounting principles in the United States requires the Company's management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. Management makes these estimates using the best information available at the time the estimates are made; however actual results when ultimately realized could differ from those estimates.

## **NOTE 6 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

### **(a) Economic and Political Risks**

The Company's operations are conducted in China. As a result, the Company's business, financial condition and results of operations may be influenced by the political, economic and legal environments in China, and by the general state



of the Chinese economy. In addition, the Company's earnings are subject to movements in foreign currency exchange rates when transactions are denominated in Renminbi ("RMB"), which is the Company's functional currency. Accordingly, the Company's operating results are affected by changes in the exchange rate between the U.S. dollar and the RMB.

The Company's operations in China are subject to special considerations and significant risks not typically associated with companies in North America and Western Europe. These include risks associated with, among others, the political, economic and legal environment and foreign currency exchange restrictions. The Company's performance may be adversely affected by changes in the political and social conditions in China, and by changes in governmental policies with respect to laws and regulations, anti-inflationary measures, currency conversion, remittances abroad, and rates and methods of taxation, among other things.

(b) Fair Value of Financial Instruments

ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market.

These tiers include:

Level 1—defined as observable inputs such as quoted prices in active markets;

Level 2—defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and

Level 3—defined as unobservable inputs for which little or no market data exists, therefore requiring an entity to develop its own assumptions.

The Company's financial instruments primarily consist of cash and cash equivalents, restricted cash, accounts receivable, notes receivable, other receivables, accounts payable, other payables and accrued liabilities, short-term bank loans, notes payable, and warrants.

The carrying value of cash and cash equivalents, restricted cash, accounts receivable, notes receivable, other receivables, accounts payable, other payables and accrued liabilities, and notes payable approximate fair value because of the short-term nature of these items. The estimated fair values of short-term bank loans were not materially different from their carrying value as presented due to the brief maturities and because the interest rates on these

borrowings approximate those that would have been available for loans of similar remaining maturities and risk profiles. As the carrying amounts are reasonable estimates of fair value, these financial instruments are classified within Level 1 of the fair value hierarchy. The Company identified notes payable as Level 2 instruments due to the fact that the inputs to valuation are primarily based upon readily observable pricing information. The balance of notes payable, which was measured and disclosed at fair value, was \$18,848,520 and \$28,075,945 at June 30, 2018 and December 31, 2017, respectively.

Contingent consideration related to the acquisition of Jinhua An Kao, which is accounted for as liabilities, are measured at each reporting date for their fair value using Level 3 inputs. The fair value of contingent consideration was \$5,345,985 and \$0 at June 30, 2018 and December 31, 2017, respectively. Also see Note 26.

(c) Cash and Cash Equivalents

The Company considers highly-liquid investments purchased with original maturities of three months or less to be cash equivalents.

As of June 30, 2018, and December 31, 2017, the Company's restricted cash was \$7,878,200 and \$11,218,688, respectively.

(d) Inventories

Inventories are stated at the lower of cost or net realizable value (market value). The cost of raw materials is determined on the basis of weighted average. The cost of finished goods is determined on the basis of weighted average and comprises direct materials, direct labor and an appropriate proportion of overhead.

Net realizable value is based on estimated selling prices less selling expenses and any further costs expected to be incurred for completion. Adjustments to reduce the cost of inventory to net realizable value are made, if required, for estimated excess, obsolescence, or impaired balances.

(e) Accounts Receivable

Accounts receivable are recognized and carried at net realizable value. An allowance for doubtful accounts is recorded for periods in which the Company determines a loss is probable, based on its assessment of specific factors, such as troubled collections, historical experience, accounts aging, ongoing business relations and other factors. Accounts are written off after exhaustive collection efforts. If accounts receivable are to be provided for, or written off, they are recognized in the consolidated statement of operations within the operating expenses line item. If accounts receivable previously written off is recovered in later period or when facts subsequently become available to indicate that the amount provided as an allowance for doubtful accounts was incorrect, an adjustment is made to restate allowance for doubtful accounts.

As of June 30, 2018 and December 31, 2017, credit terms with the Company's customers were typically 180 to 360 days after delivery. As of June 30, 2018 and December 31, 2017, the Company had a \$331,362 and \$133,930

allowance for doubtful accounts, as per the Company management's judgment based on their best knowledge. The Company conducts quarterly assessments of the state of the Company's outstanding receivables and reserves any allowance for doubtful accounts if it becomes necessary.

(f) Notes receivable

Notes receivable represent short-term loans to third parties with maximum terms of six months. Interest income is recognized according to each agreement between a borrower and the Company on an accrual basis. For notes receivable with banks, the interest rates are determined by banks. For notes receivable with other parties, the interest rates are based on agreements between the parties. If notes receivable are paid back, that transaction will be recognized in the relevant year. If notes receivable are not paid back, or are written off, that transaction will be recognized in the relevant year if default is probable, reasonably assured, and the loss can be reasonably estimated. The Company will recognize income if the written-off loan is recovered at a future date. In case of any foreclosure proceedings or legal actions, the Company provides an accrual for the related foreclosure and litigation expenses. The Company also receives notes receivable from the JV Company and other parties to settle accounts receivable. If the Company decides to discount notes receivable for the purpose of receiving immediate cash, the current discount rate is approximately in the range of 4.80% to 5.00% annually. As of June 30, 2018 and December 31, 2017, the Company had notes receivable from JV Company and other related parties of \$0 and \$1,137,289, respectively, which notes receivable typically mature within six months.

(g) Advances to Suppliers

Advances to suppliers represent cash paid in advance to suppliers, and include advances to raw material suppliers, mold manufacturers, and equipment suppliers.

As of June 30, 2018, the Company had made a total advance payments of RMB 744 million (approximately \$112 million) to Nanjing Shangtong Auto Technologies Co., Ltd. (“Nanjing Shangtong”) as an advance to purchase a production line and develop a new EV model for Kandi Hainan. Nanjing Shangtong is a total solutions contractor for Kandi Hainan and provides all the equipment and EV product design and research services used by Kandi Hainan. After part of such advances were transferred to construction in progress and expensed for R&D purposes, the Company had \$8,637,681 left in Advance to Suppliers in current assets related to the purchases from Nanjing Shangtong as of June 30, 2018.

Advances for raw material purchases are typically settled within two months of the Company’s receipt of the raw materials. Prepayment is offset against the purchase price after the equipment or materials are delivered.

(h) Property, Plants and Equipment

Property, plants and equipment are carried at cost less accumulated depreciation. Depreciation is calculated over the asset’s estimated useful life using the straight-line method. Leasehold improvements are amortized over the life of the asset or the term of the lease, whichever is shorter. Estimated useful lives are as follows:

|                         |          |
|-------------------------|----------|
| Buildings               | 30 years |
| Machinery and equipment | 10 years |
| Office equipment        | 5 years  |
| Motor vehicles          | 5 years  |
| Molds                   | 5 years  |

The costs and related accumulated depreciation of assets sold or otherwise retired are eliminated from the Company’s accounts and any gain or loss is included in the statements of income. The cost of maintenance and repairs is charged to expenses as incurred, whereas significant renewals and betterments are capitalized.

(i) Construction in Progress

Construction in progress (“CIP”) represents the direct costs of construction, and the acquisition costs of buildings or machinery. Capitalization of these costs ceases, and construction in progress is transferred to plants and equipment, when substantially all the activities necessary to prepare the assets for their intended use are completed. No depreciation is provided for until the assets are completed and ready for their intended use. As of June 30, 2018, \$2,854,673 of interest expenses previously capitalized for CIP have been reimbursed by the government.

(j) Land Use Rights

Land in China is owned by the government and land ownership rights cannot be sold to an individual or to a private company. However, the Chinese government grants the user a “land use right” to use the land. The land use rights granted to the Company are amortized using the straight-line method over a term of fifty years.

(k) Accounting for the Impairment of Long-Lived Assets

The Company periodically evaluates the carrying value of long-lived assets to be held and used, including intangible assets subject to amortization, when events and circumstances warrant such a review, pursuant to the guidelines established in Statement of Financial Accounting Standards (“SFAS”) No. 144 (now known as “ASC 360”). The carrying value of a long-lived asset is considered impaired when the anticipated undiscounted cash flow from such asset is separately identifiable and is less than its carrying value. In that event, a loss is recognized based on the amount by which the carrying value exceeds the fair market value of the long-lived asset. Fair market value is determined primarily using the anticipated cash flows discounted at a rate commensurate with the risk involved. Losses on long-lived assets to be disposed of are determined in a similar manner, except that fair market values are reduced for disposal costs.

The Company recognized no impairment loss during the reporting period.

(l) Revenue Recognition

The Company adopted ASC Topic 606 Revenue from Contracts with Customers with a date of the initial application of January 1, 2018 using the modified retrospective method. As a result, the Company has changed its accounting policy for revenue recognition. The impact of the adoption of ASC Topic 606 on the Company’s condensed consolidated financial statements is not material.

The Company recognizes revenue when goods or services are transferred to customers in an amount that reflects the consideration which it expects to receive in exchange for those goods or services. In determining when and how revenue is recognized from contracts with customers, the Company performs the following five-step analysis: (i) identification of contract with customer (ii) determination of performance obligations (iii) measurement of the transaction price (iv) allocation of the transaction price to the performance obligations and (v) recognition of revenue when (or as) the Company satisfies each performance obligation.



The Company generates revenue through the sale of EV products, EV parts and off-road vehicles. The revenue is recognized at a point in time once the Company has determined that the customer has obtained control over the product. Control is typically deemed to have been transferred to the customer when the performance obligation is fulfilled, usually at the time of delivery, at the net sales price (transaction price). Estimates of variable consideration, such as volume discounts and rebates, are determined, reviewed and revised periodically by management. Revenue is recognized net of any taxes collected from customers, which are subsequently remitted to governmental authorities. Shipping and handling costs for product shipments occur prior to the customer obtaining control of the goods are accounted for as fulfillment costs rather than separate performance obligations and recorded as sales and marketing expenses.

The Company's contracts are predominantly short-term in nature with a contract term of one year or less. For those contracts, the Company has utilized the practical expedient in ASC Topic 606 exempting the Company from disclosure of the transaction price allocated to remaining performance obligations if the performance obligation is part of a contract that has an original expected duration of one year or less.

Receivables are recorded when the Company has an unconditional right to consideration.

See Note 24 "Segment Reporting" for disaggregation of revenue by reporting segments. The Company believes this disaggregation best depicts how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

(m) Research and Development

Expenditures relating to the development of new products and processes, including improvements to existing products, are expensed as incurred. Research and development expenses were \$642,889 and \$5,142,041 for the three months ended June 30, 2018, and June 30, 2017, respectively. Research and development expenses were \$1,400,187 and \$25,911,773 for the six months ended June 30, 2018, and June 30, 2017, respectively.

(n) Government Grants

Grants and subsidies received from the Chinese government are recognized when the proceeds are received or collectible and related milestones have been reached and all contingencies have been resolved.

For the three months ended June 30, 2018 and June 30, 2017, \$15,558 and \$262,137, respectively, were received by the Company's subsidiaries from the Chinese government. For the six months ended June 30, 2018 and June 30, 2017, \$110,813 and \$5,329,611, respectively, were received by the Company's subsidiaries from the Chinese government.

(o) Income Taxes

The Company accounts for income tax using an asset and liability approach, which allows for the recognition of deferred tax benefits in future years. Under the asset and liability approach, deferred taxes are provided for the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The accounting for deferred tax calculation represents the Company management's best estimate of the most likely future tax consequences of events that have been recognized in our financial statements or tax returns and related future anticipation. A valuation allowance is provided for deferred tax assets if it is more likely than not these items will either expire before the Company is able to realize their benefits, or that future realization will be uncertain.

## (p) Foreign Currency Translation

The accompanying consolidated financial statements are presented in United States dollars. The functional currency of the Company is the Renminbi (RMB). Capital accounts of the consolidated financial statements are translated into United States dollars from RMB at their historical exchange rates when the capital transactions occurred.

Assets and liabilities are translated at the exchange rates as of balance sheet date. Income and expenditures are translated at the average exchange rate of the reporting period, which rates are obtained from the website: <http://www.oanda.com>

|                                    | June 30,<br>2018 | December 31,<br>2017 | June 30,<br>2017 |
|------------------------------------|------------------|----------------------|------------------|
| Period end RMB : USD exchange rate | 6.61905          | 6.5067               | 6.779400         |
| Average RMB : USD exchange rate    | 6.3666           | 6.7568               | 6.874859         |

## (q) Comprehensive Income

Comprehensive income is defined to include all changes in equity except those resulting from investments by owners and distributions to owners. Among other disclosures, all items that are required to be recognized under current accounting standards as components of comprehensive income are required to be reported in a financial statement that is presented with the same prominence as other financial statements. Comprehensive income includes net income and the foreign currency translation changes.

## (r) Segments

In accordance with ASC 280-10, Segment Reporting, the Company's chief operating decision makers rely upon the consolidated results of operations when making decisions about allocating resources and assessing the performance of the Company. As a result of the assessment made by the Company's chief operating decision makers, the Company has only one operating segment. The Company does not distinguish between markets or segments for the purpose of internal reporting.

## (s) Stock Option Expenses

The Company's stock option expenses are recorded in accordance with ASC 718 and ASC 505.

The fair value of stock options is estimated using the Black-Scholes-Merton model. The Company's expected volatility assumption is based on the historical volatility of the Company's common stock. The expected life assumption is primarily based on the expiration date of the option. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

The recognition of stock option expenses is based on awards expected to vest. ASC standards require forfeitures to be estimated at the time of grant and revised in subsequent periods, if necessary, if actual forfeitures differ from those estimates.

The stock-based option expenses for the three months ended June 30, 2018 and June 30, 2017, were \$589,430 and \$1,994,993. The stock-based option expenses for the six months ended June 30, 2018 and June 30, 2017, were \$1,586,926 net of a reversal for forfeited stock option of \$2,644,877 and \$3,128,512, respectively. See Note 19. There were no forfeitures estimated during the reporting period.

(t) Goodwill

The Company allocates goodwill from business combinations to reporting units based on the expectation that the reporting unit is to benefit from the business combination. The Company evaluates its reporting units on an annual basis and, if necessary, reassigns goodwill using a relative fair value allocation approach. Goodwill is tested for impairment at the reporting unit level on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. These events or circumstances could include a significant change in the business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit.

Application of the goodwill impairment test requires judgments, including the identification of reporting units, assignment of assets and liabilities to reporting units, assignment of goodwill to reporting units, and the determination of the fair value of each reporting unit. The Company first assesses qualitative factors to determine whether it is more likely than not that goodwill is impaired. If the more likely than not threshold is met, the Company performs a quantitative impairment test.

As of June 30, 2018 and June 30, 2017, the Company determined that its goodwill was not impaired.

(u) Intangible assets

Intangible assets consist of patent, trade names and customer relations associated with the purchase price from the allocation of Yongkang Scrou and Jinhua An Kao. Such assets are being amortized over their estimated useful lives. Intangible assets are amortized as of June 30, 2018. The amortization expenses for intangible assets were \$167,563 and \$20,524 for the three months ended June 30, 2018 and June 30, 2017, respectively. The amortization expenses for

intangible assets were \$335,588 and \$41,048 for the six months ended June 30, 2018 and June 30, 2017, respectively.

(v) Accounting for Sale of Common Stock and Warrants

Gross proceeds are first allocated according to the initial fair value of the freestanding derivative instruments (i.e. the warrants issued to the Company's investors in its previous offerings, or the "Investor Warrants"). The remaining proceeds are allocated to common stock. The related issuance expenses, including the placement agent cash fees, legal fees, the initial fair value of the warrants issued to the placement agent and others were allocated between the common stock and the Investor Warrants based on how the proceeds are allocated to these instruments. Expenses related to the issuance of common stock were charged to paid-in capital. Expenses related to the issuance of derivative instruments were expensed upon issuance.

(w) Consolidation of variable interest entities

In accordance with accounting standards regarding consolidation of variable interest entities, or VIEs, VIEs are generally entities that lack sufficient equity to finance their activities without additional financial support from other parties or whose equity holders lack adequate decision making ability. All VIEs with which the Company is involved must be evaluated to determine the primary beneficiary of the risks and rewards of the VIE. The primary beneficiary is required to consolidate the VIE for financial reporting purposes.

The Company has concluded, based on the contractual arrangements, that Kandi New Energy is a VIE and that the Company's wholly-owned subsidiary, Kandi Vehicles, absorbs a majority of the risk of loss from the activities of this company, thereby enabling the Company, through Kandi Vehicles, to receive a majority of its respective expected residual returns.

Additionally, because Kandi New Energy is under common control with other entities, the consolidated financial statements have been prepared as if the transactions had occurred retroactively as to the beginning of the reporting period of these consolidated financial statements.

Control and common control are defined under the accounting standards as "an individual, enterprise, or immediate family members who hold more than 50 percent of the voting ownership interest of each entity." Because the owners collectively own 100% of Kandi New Energy, and have agreed to vote their interests in concert since the establishment of each of these three companies as memorialized the Voting Rights Proxy Agreement, the Company believes that the owners collectively have control and common control of Kandi New Energy. Accordingly, the Company believes that Kandi New Energy was constructively held under common control by Kandi Vehicles as of the time the contractual agreements were entered into, establishing Kandi Vehicles as their primary beneficiary. Kandi Vehicles, in turn, is owned by Continental, which is owned by the Company.

(x) Reclassification

The Company adopted ASU 2016-18, "Statement of Cash Flows (Topic 230) - Restricted Cash" in the first quarter of 2018. Certain amounts included in the 2017 condensed consolidated statement of cash flows have been reclassified to conform to the 2018 financial statement presentation as follows:



The Company has included restricted cash of \$12,957,377 and \$22,708,654, respectively, with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows for the six months ended June 30, 2017. As a result, the total amount at the beginning of the period on the statement of cash flows for the six months ended June 30, 2017 has changed from \$12,235,921 to \$25,193,298; the total amount at the end of the period on the statement of cash flows for the six months ended June 30, 2017 has changed from \$7,406,843 to \$30,115,686; and effect of exchange rate changes on the statement of cash of cash flows for the six months ended June 30, 2017 has changed from \$199,530 to \$ 648,835.

The Company has eliminated the line item of restricted cash of \$(9,302,161) from the section of financing activities on the statement of cash flows for the six months ended June 30, 2017. As a result, net cash used by financing activities of \$6,643,401 on the statement of cash flows for the six months ended June 30, 2017 has changed to net cash provided by financing activities of \$2,658,760. Net decrease in cash and cash equivalents and restricted cash of \$5,028,608 on the statement of cash flows for the six months ended June 30, 2017 has changed to net increase in cash and cash equivalents and restricted cash of \$4,273,553.

#### NOTE 7 - NEW ACCOUNTING PRONOUNCEMENTS

Recent accounting pronouncements that the Company has adopted or may be required to adopt in the future are summarized below:

In May 2014, the FASB issued a new standard on revenue recognition related to contracts with customers. This standard supersedes nearly all existing revenue recognition guidance and involves a five-step principles-based approach to recognizing revenue. The new model requires revenue recognition to depict the transfer of promised goods or services to customers in an amount that reflects the consideration a company expects to receive. The new standard also require additional qualitative and quantitative about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments made in applying the revenue guidance, and assets recognized from the costs to obtain or fulfill a contract. The Company adopted this standard in the first quarter of 2018 using the modified retrospective approach. The impact of adoption on its Condensed Consolidated Financial Statements for any period presented is not material.

In November 2015, the Financial Accounting Standards Board (“FASB”) issued ASU 2015-17, “Balance Sheet Classification of Deferred Taxes.” This ASU amends existing guidance to require that deferred income tax assets and liabilities be classified as non-current in a classified balance sheet, and eliminates the prior guidance which required an entity to separate deferred tax assets and liabilities into a current amount and a non-current amount in a classified balance sheet. The Company adopted this standard prospectively in the first quarter of 2018. The impact of adoption on its Condensed Consolidated Financial Statements for any period presented is not material.

In October 2016, the FASB issued Accounting Standards Update ASU 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers Other than Inventory, which requires companies to recognize the income-tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs, rather than when the asset has been sold to an outside party. The Company adopted this standard prospectively in the first quarter of 2018. The impact of adoption on its Condensed Consolidated Financial Statements for any period presented is not material.

In November 2016, the FASB issued ASU 2016-18, “Statement of Cash Flows (Topic 230) - Restricted Cash,” (“ASU 2016-18”). This ASU requires a statement of cash flows to explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The Company adopted this standard in the first quarter of 2018. The impact of adoption on its Condensed Consolidated Financial Statements for any period presented is not material.

In January 2017, the FASB issued Accounting Standards Update ASU 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business, which revises the definition of a business and provides new guidance in evaluating when a set of transferred assets and activities is a business. The Company adopted this standard prospectively in the first quarter of 2018. The impact of adoption on its Condensed Consolidated Financial Statements for any period presented is not material.

In February 2018, the FASB released ASU 2018-2, “Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income.” This standard update addresses a specific consequence of the Tax Cuts and Jobs Act (“U.S. tax reform”) and allows a reclassification from accumulated other comprehensive income to retained earnings for the stranded tax effects resulting from U.S. tax reform. Consequently, the update eliminates the stranded tax effects that were created as a result of the historical U.S. federal corporate income tax rate to the newly enacted U.S. federal corporate income tax rate. The Company is required to adopt this standard in the first quarter of fiscal year 2020, with early adoption permitted. The amendments in this update should be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act is recognized. The Company is currently in the process of evaluating the impact of adoption on its Condensed Consolidated Financial Statements.

#### NOTE 8 - CONCENTRATIONS

##### (a) Customers

For the three-month periods ended June 30, 2018 and June 30, 2017, the Company’s major customers, each of whom accounted for more than 10% of the Company’s consolidated revenue, were as follows:

| Major Customers                              | Sales                                                   |                                                          | Trade Receivable             |                      |
|----------------------------------------------|---------------------------------------------------------|----------------------------------------------------------|------------------------------|----------------------|
|                                              | Three<br>Month<br>Ended<br><b>June<br/>30,<br/>2018</b> | Three<br>Months<br>Ended<br><b>June<br/>30,<br/>2017</b> | <b>June<br/>30,<br/>2018</b> | December 31,<br>2017 |
| Jinhua Chaoneng Automobile Sales Co., Ltd.   | 36%                                                     | -                                                        | 23 %                         | -                    |
| Zhejiang Shikong Energy Technology Co., Ltd. | 30%                                                     | -                                                        | 8 %                          | -                    |
| Kandi Electric Vehicles Group Co., Ltd.      | 27%                                                     | 94                                                       | % 59 %                       | 71 %                 |

For the six-month periods ended June 30, 2018 and June 30, 2017, the Company's major customers, each of whom accounted for more than 10% of the Company's consolidated revenue, were as follows:

| Major Customers                              | Sales<br>Six Months<br>Ended |                  | Trade Receivable<br>Six Months<br>Ended |                      |   |
|----------------------------------------------|------------------------------|------------------|-----------------------------------------|----------------------|---|
|                                              | June<br>30,<br>2018          | June 30,<br>2017 | June<br>30,<br>2018                     | December 31,<br>2017 |   |
| Zhejiang Shikong Energy Technology Co., Ltd. | 35 %                         | -                | 8 %                                     | -                    |   |
| Kandi Electric Vehicles Group Co., Ltd.      | 28 %                         | 86               | % 59 %                                  | 71                   | % |
| Jinhua Chaoneng Automobile Sales Co. Ltd.    | 24 %                         | -                | 23 %                                    | -                    |   |
| Zhejiang Kuke Sports Technology Co., Ltd.    | 10 %                         | -                | 2 %                                     | -                    |   |

(b) Suppliers

For the three-month periods ended June 30, 2018 and June 30, 2017, the Company's material suppliers, each of whom accounted for more than 10% of the Company's total purchases, were as follows:

| Major Suppliers                                  | Purchases<br>Three<br>Month<br>Ended |                     | Accounts Payable<br>Three<br>Months<br>Ended |                      |   |
|--------------------------------------------------|--------------------------------------|---------------------|----------------------------------------------|----------------------|---|
|                                                  | June<br>30,<br>2018                  | June<br>30,<br>2017 | June<br>30,<br>2018                          | December 31,<br>2017 |   |
| Shanghai de Lang Power Battery Co., Ltd.         | 50 %                                 | -                   | 7 %                                          | -                    |   |
| Jiangsu Tian Peng power Co., Ltd.                | 13 %                                 | -                   | 1 %                                          | -                    |   |
| Dongguan Chuangming Battery Technology Co., Ltd. | -                                    | 22                  | % -                                          | 19                   | % |
| Zhejiang Tianneng Energy Technology Co., Ltd.    | -                                    | 17                  | % -                                          | 11                   | % |
| Zhuhai Enpower Electrical Co., Ltd.              | -                                    | 13                  | % 6 %                                        | -                    |   |

For the six-month periods ended June 30, 2018 and June 30, 2017, the Company's material suppliers, each of whom accounted for more than 10% of the Company's total purchases, were as follows:

| Major Suppliers                                  | Purchases                      |                                | Accounts Payable |                   |
|--------------------------------------------------|--------------------------------|--------------------------------|------------------|-------------------|
|                                                  | Six Months Ended June 30, 2018 | Six Months Ended June 30, 2017 | June 30, 2018    | December 31, 2017 |
| Shanghai de Lang Power Battery Co., Ltd.         | 50 %                           | -                              | 7 %              | -                 |
| Dongguan Chuangming Battery Technology Co., Ltd. | -                              | 25                             | %                | 19 %              |
| Zhejiang Tianneng Energy Technology Co., Ltd.    | -                              | 17                             | %                | 11 %              |
| Zhuhai Enpower Electrical Co., Ltd.              | -                              | 12                             | %                | 6 %               |

#### NOTE 9 - EARNINGS PER SHARE

The Company calculates earnings per share in accordance with ASC 260, Earnings Per Share, which requires a dual presentation of basic and diluted earnings per share. Basic earnings per share are computed using the weighted average number of shares outstanding during the reporting period. Diluted earnings per share represents basic earnings per share adjusted to include the potentially dilutive effect of outstanding stock options and warrants (using treasury stock method). For the three months ended June 30, 2018 and June 30, 2017, the average number of potentially dilutive common shares was zero. The potential dilutive common shares as at the six months ended June 30, 2018 and June 30, 2017, were 3,900,000 and 4,400,000 shares respectively.

The following is the calculation of earnings per share for the three-month periods ended June 30, 2018 and 2017:

|                                                     | For three months ended |                |
|-----------------------------------------------------|------------------------|----------------|
|                                                     | June 30, 2018          | 2017           |
| Net income (loss)                                   | \$1,374,525            | \$(11,558,017) |
| Weighted average shares used in basic computation   | 51,140,542             | 47,974,974     |
| Dilutive shares                                     | -                      | -              |
| Weighted average shares used in diluted computation | 51,140,542             | 47,974,974     |
| Earnings (loss) per share:                          |                        |                |
| Basic                                               | \$0.03                 | \$(0.24)       |
| Diluted                                             | \$0.03                 | \$(0.24)       |



The following is the calculation of earnings per share for the six-month periods ended June 30, 2018 and 2017:

|                                                     | For six months ended |                |
|-----------------------------------------------------|----------------------|----------------|
|                                                     | June 30,             |                |
|                                                     | 2018                 | 2017           |
| Net income (loss)                                   | \$5,102,520          | \$(35,711,452) |
| Weighted average shares used in basic computation   | 50,893,356           | 47,854,351     |
| Dilutive shares                                     | -                    | -              |
| Weighted average shares used in diluted computation | 50,893,356           | 47,854,351     |
| Earnings (loss) per share:                          |                      |                |
| Basic                                               | \$0.10               | \$(0.75 )      |
| Diluted                                             | \$0.10               | \$(0.75 )      |

#### NOTE 10 - ACCOUNTS RECEIVABLE

Accounts receivable are summarized as follows:

|                                       | June 30,     | December 31, |
|---------------------------------------|--------------|--------------|
|                                       | 2018         | 2017         |
| Accounts receivable                   | \$34,403,293 | \$34,531,788 |
| Less: allowance for doubtful accounts | (331,362 )   | (133,930 )   |
| Accounts receivable, net              | \$34,071,931 | \$34,397,858 |

#### NOTE 11 - INVENTORIES

Inventories are summarized as follows:

|                   | June 30,    | December 31, |
|-------------------|-------------|--------------|
|                   | 2018        | 2017         |
| Raw material      | \$6,226,902 | \$7,256,498  |
| Work-in-progress  | 2,764,044   | 2,831,678    |
| Finished goods    | 3,592,546   | 6,512,537    |
| Total inventories | 12,583,492  | 16,600,713   |



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|                                                |              |              |
|------------------------------------------------|--------------|--------------|
| Less: provision for slowing moving inventories | (938,624 )   | (620,919 )   |
| Inventories, net                               | \$11,644,868 | \$15,979,794 |

**NOTE 12 - NOTES RECEIVABLE**

As of June 30, 2018 and December 31, 2017, there is no notes receivable from an unrelated party.

Notes receivable from the JV Company and related parties as of June 30, 2018, and December 31, 2017, are summarized as follows:

|                            | June<br>30,<br>2018 | December 31,<br>2017 |
|----------------------------|---------------------|----------------------|
| Notes receivable as below: |                     |                      |
| Bank acceptance notes      | -                   | 1,137,289            |
| Notes receivable           | \$ -                | \$ 1,137,289         |

Details of notes receivable from the JV Company and related parties as of December 31, 2017, are as set forth below:

| Index | Amount<br>(\$) | Counter party                              | Relationship                    | Nature                | Manner of<br>settlement |
|-------|----------------|--------------------------------------------|---------------------------------|-----------------------|-------------------------|
| 1     | 922,126        | Kandi Electric Vehicles Group<br>Co., Ltd. | Joint Venture of the<br>Company | Payments for<br>sales | Not due                 |
| 2     | 153,688        | Kandi Jiangsu                              | Subsidiary of the JV<br>Company | Payments for<br>sales | Not due                 |
| 3     | 61,475         | Kandi Changxing                            | Subsidiary of the JV<br>Company | Payments for<br>sales | Not due                 |

**NOTE 13 - PROPERTY, PLANT AND EQUIPMENT**

Property, plants and equipment as of June 30, 2018 and December 31, 2017, consisted of the following:

|           | June 30,<br>2018 | December 31,<br>2017 |
|-----------|------------------|----------------------|
| At cost:  |                  |                      |
| Buildings | \$ 13,619,001    | \$ 13,853,340        |

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|                                                 |                |                |
|-------------------------------------------------|----------------|----------------|
| Machinery and equipment                         | 9,803,904      | 7,916,562      |
| Office equipment                                | 638,881        | 532,774        |
| Motor vehicles and other transport equipment    | 413,387        | 382,866        |
| Moulds and others                               | 28,138,190     | 28,659,714     |
|                                                 | 52,613,363     | 51,345,256     |
| Less : Accumulated depreciation                 |                |                |
| Buildings                                       | \$(4,833,360 ) | \$(4,683,040 ) |
| Machinery and equipment                         | (7,233,293 )   | (7,216,464 )   |
| Office equipment                                | (356,956 )     | (305,367 )     |
| Motor vehicles and other transport equipment    | (321,599 )     | (310,631 )     |
| Moulds and others                               | (26,601,162)   | (26,306,306 )  |
|                                                 | (39,346,370)   | (38,821,808 )  |
| Less: provision for impairment for fixed assets | (460,899 )     | (522,477 )     |
| Plant and equipment, net                        | \$12,806,094   | \$12,000,971   |

As of June 30, 2018 and December 31, 2017, the net book value of plants and equipment pledged as collateral for bank loans was \$8,643,725 and \$9,019,993, respectively.

Depreciation expenses for the three months ended June 30, 2018 and June 30, 2017 were \$653,044 and \$1,071,612, respectively. Depreciation expenses for the six months ended June 30, 2018 and June 30, 2017 were \$1,271,584 and \$2,134,346, respectively

#### NOTE 14 - LAND USE RIGHTS

The Company's land use rights consist of the following:

|                                | June 30,<br>2018 | December 31,<br>2017 |
|--------------------------------|------------------|----------------------|
| Cost of land use rights        | \$ 15,505,825    | \$ 15,676,450        |
| Less: Accumulated amortization | (3,128,518 )     | (3,010,403 )         |
| Land use rights, net           | \$ 12,377,307    | \$ 12,666,047        |

As of June 30, 2018, and December 31, 2017, the net book value of land use rights pledged as collateral for the Company's bank loans was \$8,174,223 and \$8,993,913, respectively. Also see Note 16.

The amortization expenses for the three months ended June 30, 2018 and June 30, 2017, were \$95,692 and \$79,845, respectively. The amortization expenses for the six months ended June 30, 2018 and June 30, 2017, were \$184,591 and \$159,383, respectively. Amortization expenses for the next five years and thereafter is as follows:

|                   |               |
|-------------------|---------------|
| 2018 (Six Months) | \$ 184,591    |
| 2019              | 369,182       |
| 2020              | 369,182       |
| 2021              | 369,182       |
| 2022              | 369,182       |
| Thereafter        | 10,715,988    |
| Total             | \$ 12,377,307 |

**NOTE 15 - CONSTRUCTION-IN-PROGRESS**

## Hainan Facility

In April 2013, the Company signed an agreement with the Wanning city government in Hainan Province to invest a total of RMB 1 billion to establish a factory in Wanning to manufacture 100,000 sets of EV products annually. In January 2016, the Hainan Province government implemented a development plan to centralize manufacturing in certain designated industry parks. As a result, the Wanning facility was relocated from Wanning city to the Haikou city high-tech zone. Based on the agreement with the government, all the expenses and lost assets resulting from the relocation were compensated for by the local government. As a result of the relocation, the contracts to build the manufacturing facility had to be revised in terms of total contract amount, technical requirements, completion milestones and others for the new construction site in Haikou. Currently, the Hainan facility's main project (manufacturing plant and office, main manufacturing equipment and facilities, and new product R&D) has been almost completed and is in the stage of implementation testing and full-line linkage test run. In the second quarter, Geely K23 model has passed the inspections of mandatory projects and product function conducted by the national vehicle product inspection authorities. Based on the inspection results, the Company tested and optimized the production line. Both of the EV products with 200-km and 300-km driving ranges have already been included in the government's public announcements as of the date of this report. Next, it is expected to be included in the model directory of sales tax exemption jointly issued by the State Administration of Taxation and other departments. The factory plans to start arranging process inspection, trial production and project completion and acceptance. After the completion of the matters above, the construction of the Hainan factory will be officially completed. The Company endeavors to complete the construction and transfer the associated construction-in-progress to fixed assets in August 2018, and endeavors to complete the installation of equipment and transfer the associated construction-in-progress to fixed assets in September 2018.

No depreciation is provided for CIP until such time as the facility is completed and placed into operation.

The contractual obligations under CIP of the Company as of June 30, 2018 are as follows:

| <b>Project</b>        | <b>Total in CIP<br/>as of<br/>June 30,<br/>2018</b> | <b>Estimate to<br/>complete</b> | <b>Total<br/>contract<br/>amount</b> |
|-----------------------|-----------------------------------------------------|---------------------------------|--------------------------------------|
| Kandi Hainan facility | \$69,541,416                                        | \$14,582,261                    | \$84,123,677                         |
| Total                 | \$69,541,416                                        | \$14,582,261                    | \$84,123,677                         |

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As of June 30, 2018, and December 31, 2017, the Company had CIP amounting to \$69,541,416 and \$53,083,925, respectively.

All interest expenses previously capitalized for CIP were reimbursed by the government. There was no interest expense capitalized for CIP for the three and six months ended June 30, 2018.

#### NOTE 16 - SHORT -TERM AND LONG-TERM BANK LOANS

Short-term loans are summarized as follows:

|                                                                                                                                                                                                                         | June 30,<br>2018 | December 31,<br>2017 |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------|----------------------|
| Loans from China Ever-bright Bank                                                                                                                                                                                       |                  |                      |
| Interest rate 5.22% per annum, paid off on April 25, 2018, secured by the assets of Kandi Vehicle, guaranteed by Mr. Hu Xiaoming and his wife, also guaranteed by Company's subsidiaries. Also see Note 13 and Note 14. | -                | 10,758,141           |
| Interest rate 5.655% per annum, due on April 25, 2019, secured by the assets of Kandi Vehicle, guaranteed by Mr. Hu Xiaoming and his wife, also guaranteed by Company's subsidiaries. Also see Note 13 and Note 14.     | 10,575,536       |                      |
| Loans from Hangzhou Bank                                                                                                                                                                                                |                  |                      |
| Interest rate 4.79% per annum, due on October 16, 2018, secured by the assets of Kandi Vehicle. Also see Note 13 and Note 14.                                                                                           | 7,372,659        | 7,499,962            |
| Interest rate 4.79% per annum, paid off on July 4, 2018, secured by the assets of Kandi Vehicle. Also see Note 13 and Note 14.                                                                                          | 10,907,910       | 11,096,255           |
| Interest rate 4.35% per annum, paid off on March 26, 2018, secured by the assets of Kandi Vehicle. Also see Note 13 and Note 14.                                                                                        | -                | 3,688,506            |
| Interest rate 5.66% per annum, due March 25, 2019, secured by the assets of Kandi Vehicle. Also see Note 13 and Note 14.                                                                                                | 3,625,898        | -                    |
|                                                                                                                                                                                                                         | \$32,482,003     | \$ 33,042,864        |

Long-term loans are summarized as follows:

|                                                                                                          | June 30,<br>2018 | December 31,<br>2017 |
|----------------------------------------------------------------------------------------------------------|------------------|----------------------|
| Loans from Haikou Rural Credit Cooperative                                                               |                  |                      |
| Interest rate 7% per annum, due on December 12, 2021, guaranteed by Kandi Vehicles and Kandi New Energy. | 30,064,737       | 30,737,547           |
|                                                                                                          | \$30,064,737     | 30,737,547           |

The interest expense of short-term and long-term bank loans for the three months ended June 30, 2018, and 2017 was \$433,914 and \$548,810, respectively. The interest expense of short-term and long-term bank loans for the six months ended June 30, 2018, and 2017 was \$848,232 and \$1,163,263, respectively.



As of June 30, 2018, the aggregate amount of short-term and long-term loans guaranteed by various third parties was \$0.

**NOTE 17 - NOTES PAYABLE**

By issuing bank notes payable rather than paying cash to suppliers, the Company can defer payments until the bank notes payable are due. Depending on bank requirements, the Company may need to deposit restricted cash in banks to back up the bank notes payable, while the restricted cash deposited in the banks will generate interest income.

A bank acceptance note is a promised future payment, or time draft, which is accepted and guaranteed by a bank and drawn on a deposit at the bank. The banker's acceptance specifies the amount of the funds, the date, and the person to which the payment is due.

After acceptance, the draft becomes an unconditional liability of the bank, but the holder of the draft can sell (exchange) it for cash at a discount to a buyer who is willing to wait until the maturity date for the funds in the deposit. \$7,878,200 and \$11,218,688 were held as collateral for the notes payable as of June 30, 2018, and December 31, 2017, respectively.

As is common business practice in the PRC, the Company issues notes payable to its suppliers as settlement for accounts payable.

The Company's notes payable also include the borrowing from the third party.

Notes payable for June 30, 2018 and December 31, 2017 were summarized as follows:

|                               | June 30,<br>2018 | December 31,<br>2017 |
|-------------------------------|------------------|----------------------|
| <u>Bank acceptance notes:</u> |                  |                      |
| Due January 4, 2018           | \$-              | \$ 4,987,167         |
| Due April 19, 2018            | -                | 230,532              |
| Due May 6, 2018               | -                | 1,168,027            |

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|                              |              |              |
|------------------------------|--------------|--------------|
| Due June 18, 2018            | -            | 2,305,316    |
| Due June 21, 2018            | -            | 376,019      |
| Due June 25, 2018            | -            | 153,688      |
| Due June 27, 2018            | -            | 76,844       |
| Due June 29, 2018            | -            | 2,382,160    |
| Due August 13, 2018          | 755,395      | -            |
| Due December 13, 2018        | 6,798,559    | -            |
| Commercial acceptance notes: |              |              |
| Due March 26, 2018           | -            | 10,758,140   |
| Due December 30, 2018        | 11,183,891   | -            |
| Other Notes Payable:         |              |              |
| Due May 6, 2019              | 110,675      | 5,638,052    |
| Total                        | \$18,848,520 | \$28,075,945 |

## NOTE 18 - TAXES

### (a) Corporation Income Tax

Pursuant to the tax laws and regulations of the PRC, the Company's applicable corporate income tax ("CIT") rate is 25%. However, Kandi Vehicles qualifies as a High and New Technology Enterprise ("HNTE") company in the PRC, and is entitled to pay a reduced income tax rate of 15% for the years presented. HNTE need to be authenticated every three years. In November 2017 the Company renewed its HNTE eligibility which will now expire in 2020. The applicable CIT rate of each of the Company's four other subsidiaries, Kandi New Energy, Yongkang Scrou, Kandi Hainan and Jinhua An Kao, the JV Company and its subsidiaries, and the Service Company is 25%.

Our tax provision or benefit from income taxes for interim periods is determined using an estimate of our annual effective tax rate, adjusted for discrete items, if any, that are taken into account in the relevant period. Each quarter we update our estimate of the annual effective tax rate, and if our estimated tax rate changes, we make a cumulative adjustment. For 2018, we estimate that our effective tax rate will be favorably affected by non-taxable income such as the share of income of the JV Company and the gain from the change of fair value of contingent liabilities and certain research and development super-deduction and adversely affected by non-deductible expenses such as part of entertainment expenses. We record valuation allowances against the deferred tax assets associated with losses for which we may not realize a related tax benefit. After combining research and development tax credits of 25% on certain qualified research and development expenses, the Company's effective tax rates for the six months ended June 30, 2018, and 2017 were a tax expenses of 2.59% on a reported income before taxes of approximately \$5.2 million, and an effective income tax rate with a tax benefit of 12.08% for the same period of last year on a reported loss before taxes of approximately \$40.6 million, respectively.

Our quarterly tax provision, and our quarterly estimate of our annual effective tax rate, is subject to significant variation due to several factors, including variability in accurately predicting our pre-tax and taxable income and loss, acquisitions (including integrations) and investments, changes in our stock price, changes in our deferred tax assets and liabilities and their valuation, foreign currency gains (losses), changes in regulations and interpretations related to tax, accounting, and other areas. Additionally, our effective tax rate can be more or less volatile based on the amount of pre-tax income or loss. Our income tax provision for the six months ended June 30, 2018 and 2017 was tax expenses of \$135,645 and tax benefits of \$4,907,936, respectively.

Effective January 1, 2007, the Company adopted the guidance in ASC 740 related to uncertain tax positions. The guidance addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under ASC 740, the Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements

from such a position should be measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. ASC 740 also provides guidance on de-recognition, classification, interest and penalties on income taxes, accounting in interim periods and requires increased disclosures. As of June 30, 2018, the Company did not have any liability for unrecognized tax benefits. The Company files income tax returns with the U.S. Internal Revenue Services (“IRS”) and those states where the Company has operations. The Company is subject to U.S. federal or state income tax examinations by the IRS and relevant state tax authorities for years after 2006. During the periods open to examination, the Company has net operating loss carry forwards (“NOLs”) for U.S. federal and state tax purposes that have attributes from closed periods. Since these NOLs may be utilized in future periods, they remain subject to examination. The Company also files certain tax returns in the PRC. As of June 30, 2018, the Company was not aware of any pending income tax examinations by U.S. or PRC tax authorities. The Company records interest and penalties on uncertain tax provisions as income tax expense. As of June 30, 2018 the Company has no accrued interest or penalties related to uncertain tax positions. The Company has not recorded a provision for U.S. federal income tax for six months ended June 30, 2018 due to a net operating loss in 2017 and an accumulated net operating loss carry forward from prior years in the United States.

As of June 30, 2018, the aggregate NOLs in 2016 through 2017 of \$25.25 million deriving from entities in the PRC will expire in varying amount between 2021 and 2022. The cumulative net operating loss in the PRC can be carried forward for five years, to offset future net profits for income tax purposes. The cumulative net operating loss in the U.S. can be carried forward for twenty years. The cumulative net operating loss in Hong Kong can be carried forward without an expiration date.

(b) Tax Holiday Effect

For the six months ended June 30, 2018 and 2017, the PRC CIT rate was 25%. Certain subsidiaries of the Company are entitled to tax exemptions (tax holidays) for the six months ended June 30, 2018 and 2017.

The combined effects of income tax expense exemptions and reductions available to the Company for the six months ended June 30, 2018 and 2017 are as follows:

|                                   | Six Months Ended |          |
|-----------------------------------|------------------|----------|
|                                   | June 30,         |          |
|                                   | 2018             | 2017     |
| Tax benefit (holiday) credit      | \$38,861         | \$19,195 |
| Basic net income per share effect | \$0.000          | \$0.000  |

(C) The Tax Cuts and Job Act

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (“Tax Act”). The Tax Act makes broad and complex changes to the U.S. tax code that will affect our fiscal period ended June 30, 2018 and going-forward, including, but not limited to, (1) reducing the U.S. federal corporate tax rate effective January 1, 2018, (2) requiring a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries that is payable over eight years.

The SEC staff issued Staff Accounting Bulletin (“SAB”) No. 118, which provides guidance on accounting for the tax effects of the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Tax Act enactment date for companies to complete the accounting under ASC 740. In accordance with SAB 118, a company must reflect the income tax effects of those aspects of the Tax Act for which the accounting under ASC 740 is complete. To the extent that a company’s accounting for certain income tax effects of the Tax Act is incomplete but it is able to determine a reasonable estimate, it must record a provisional estimate in the financial statements. If a company cannot determine a provisional estimate to be included in the financial statements, it should continue to apply ASC 740 on the basis of the provisions of the tax laws that were in effect immediately before the enactment of the Tax Act.

For various reasons that are discussed more fully below, we have not fully completed our accounting for the income tax effects of certain elements of the Tax Act. If we were able to make reasonable estimates of the effects of elements for which our analysis is not yet complete, we recorded provisional adjustments. If we were not yet able to make reasonable estimates of the impact of certain elements, we have not recorded any adjustments related to those elements and have continued accounting for them in accordance with ASC 740 on the basis of the tax laws in effect before the Tax Act.

Our accounting for the following elements of the Tax Act is incomplete. However, we were able to make reasonable estimates of certain effects and, therefore, recorded provisional adjustments as follows:

Reduction of U.S. Federal Corporate Tax Rate: The Tax Act reduces the corporate tax rate to 21.0%, effective January 1, 2018. For certain deferred tax assets and deferred tax liabilities, we have recorded a provisional decrease of \$0.3 million, respectively, with a corresponding net adjustment to valuation allowance of \$0.3 million for the year ended December 31, 2017. While we are able to make a reasonable estimate of the impact of the reduction in corporate rate, it may be affected by other analyses related to the Tax Act, including, but not limited to, our calculation of deemed repatriation of deferred foreign income and the state tax effect of adjustments made to federal temporary differences.

**Deemed Repatriation Transition Tax:** The Deemed Repatriation Transition Tax (“Transition Tax”) is a tax on previously untaxed accumulated and current earnings and profits (“E&P”) of certain foreign subsidiaries. To determine the amount of the Transition Tax, we must determine, in addition to other factors, the amount of post-1986 E&P of the relevant subsidiaries, as well as the amount of non-U.S. income taxes paid on such earnings. Due to the timing of the enactment and the complexity involved in applying the provisions of the Act, we could not make reasonable estimates of the effects and did not record provisional amounts in our financial statements as of June 30, 2018. However, we are continuing to gather information to precisely compute the amount of the Transition Tax.

## NOTE 19 - STOCK OPTIONS

On May 29, 2015, the Compensation Committee of the Board of Directors of the Company approved the grant of stock options to purchase 4,900,000 shares of the Company’s common stock, at an exercise price of \$9.72 per share, to the Company’s directors, officers and senior employees. The stock options will vest ratably over three years and expire on the tenth anniversary of the grant date. The Company valued the stock options at \$39,990,540 and will amortize the stock compensation expense using the straight-line method over the service period from May 29, 2015, through May 29, 2018. The value of the stock options was estimated using the Black Scholes Model with an expected volatility of 90%, an expected life of 10 years, a risk-free interest rate of 2.23% and an expected dividend yield of 0.00%. There were \$1,586,926 in stock compensation expenses associated with stock options booked for the six months ended June 30, 2018. After netting of an expense reversal of \$2,644,877 for forfeited stock options for the six months ended June 30, 2018, the net stock compensation expenses associated with stock options were negative \$1,057,951 for the six months ended June 30, 2018.

The following is a summary of the stock option activities of the Company:

|                                   | Number of<br>Shares | Weighted<br>Average<br>Exercise<br>Price |
|-----------------------------------|---------------------|------------------------------------------|
| Outstanding as of January 1, 2017 | 4,566,667           | \$ 9.72                                  |
| Granted                           | —                   | —                                        |
| Exercised                         | —                   | —                                        |
| Cancelled                         | —                   | —                                        |
| Forfeited                         | (333,333 )          | 9.72                                     |
| Outstanding as of January 1, 2018 | 4,233,334           | 9.72                                     |
| Granted                           | —                   | —                                        |
| Exercised                         | —                   | —                                        |
| Cancelled                         | —                   | —                                        |
| Forfeited                         | (333,334 )          | 9.72                                     |
| Outstanding as of June 30, 2018   | 3,900,000           | \$ 9.72                                  |

The fair value of each of the 4,900,000 options issued to the employees and directors on May 29, 2015 is \$8.1613 per share.



## NOTE 20 - STOCK AWARD

In connection with the appointment of Mr. Henry Yu as a member of the Board of Directors (the "Board"), and as compensation, the Board authorized the Company to provide Mr. Henry Yu with 5,000 shares of Company's restricted common stock every six months, beginning in July 2011.

As compensation having Mr. Jerry Lewin's services as a member of the Board, the Board authorized the Company to provide Mr. Jerry Lewin with 5,000 shares of Company's restricted common stock every six months, beginning in August 2011.

As compensation having Ms. Kewa Luo's services as the Company's investor relation officer, the Board authorized the Company to provide Ms. Kewa Luo with 5,000 shares of the Company's common stock every six months, beginning in September 2013.

In November 2016, the Company entered into a three-year employment agreement with Mr. Mei Bing, who is now the Company's Chief Financial Officer. Under the agreement, Mr. Mei Bing is entitled to receive an aggregate 10,000 shares of common stock each year, vested in four equal quarterly installments of 2,500 shares.

The fair value of stock awards based on service is determined based on the closing price of the common stock on the date the shares are approved by the Board for grant. The compensation costs for awards of common stock are recognized over the requisite service period of three or six months.

On December 30, 2013, the Board approved a proposal (as submitted by the Compensation Committee) of an award (the "Board's Pre-Approved Award Grant Sub-Plan under the 2008 Plan") for certain executives and other key employees, comprising a total of 335,000 shares of common stock for each fiscal year, beginning with the 2013 fiscal year, under the Company's 2008 Omnibus Long-Term Incentive Plan (the "2008 Plan"), if the Company's "Non-GAAP Net Income" for the current fiscal year increased by 10% comparing to that of the 2013. The specific number of shares of common stock to be issued in respect of such award could proportionally increase or decrease if the actual Non-GAAP Net Income increase is more or less than 10%. "Non-GAAP Net Income" means the Company's net income for a particular year calculated in accordance with GAAP, excluding option-related expenses, stock award expenses, and the effects caused by the change of fair value of financial derivatives. For example, if Non-GAAP Net Income for the 2014 fiscal year increased by 10% compared to the Non-GAAP Net Income for the 2013 fiscal year, the selected executives and other key employees each would be granted his or her target amount of common stock of the Company. If Non-GAAP Net Income in 2014 is less than Non-GAAP Net Income in 2013, then no common stock would be granted. If Non-GAAP Net Income in 2014 increased compared to Non-GAAP Net Income in 2013 but the

increase is less than 10%, then the target amount of the common stock grant would be proportionately decreased. If Non-GAAP Net Income in 2014 increased compared to Non-GAAP Net Income in 2013 but the increase is more than 10%, then the target amount of the common stock grant would be proportionately increased up to 200% of the target amount based on the modification to 2013's proposal in 2014. Any such increase in the grant would be subject to the total number of shares available under the 2008 Plan, and the Company's Board and shareholders will need to approve any increase in the number of shares reserved under the 2008 Plan if all the shares originally reserved are granted. On May 20, 2015, the shareholders of the Company approved an increase of 9,000,000 shares under the 2008 Plan at its annual meeting. On September 26, 2016, the Board approved to terminate the previous Board's Pre-Approved Award Grant Sub-Plan under the 2008 Plan and adopted a new plan to reduce the total number of shares of common stock of the stock award for selected executives and key employees from 335,000 shares of common stock to 250,000 shares of common stock for each fiscal year, with the other terms remaining the same. On February 13, 2017, the Board authorized the Company to grant 246,900 shares of common shares to certain management members and employees as compensation for their past services under the 2008 Plan. On April 18, 2018, the Board authorized the Company to grant 238,600 shares of common shares to certain management members and employees as compensation for their past services under the 2008 Plan.

The fair value of each award granted under the 2008 Plan is determined based on the closing price of the Company's stock on the date of grant of such award. Stock-based compensation expenses are calculated based on grant date fair value and number of awards expected to be earned at the end of each quarter and recognized in the quarter. In subsequent periods, stock-based compensation expenses are adjusted based on grant date fair value and the change of number of awards expected to be earned. Final stock-based compensation expenses for the year are calculated based on grant date fair value and number of awards earned for the year and recognized at the end of year.

For three months ended June 30, 2018 and 2017, the Company recognized \$1,248,535 and \$21,050 of employee stock award expenses for stock compensation and annual incentive award under the 2008 Plan paid to Board members, management and consultants under General and Administrative Expenses, respectively. For six months ended June 30, 2018 and 2017, the Company recognized \$1,280,210 and \$1,364,675 of employee stock award expenses for stock compensation and annual incentive award under the 2008 Plan paid to Board members, management and consultants under General and Administrative Expenses, respectively.

#### NOTE 21 - INTANGIBLE ASSETS

Intangible assets include acquired other intangibles of trade name, customer relations and patent recorded at estimated fair values in accordance with purchase accounting guidelines for acquisitions. The Company acquired patents as a result of its acquisition of Jinhua An Kao which were valued in conjunction with the Company's purchase accounting at approximately \$5 million (see Note 26). The patents acquired have estimated economic useful lives of approximately 7.5 to 9.17 years.

The following table provides the gross carrying value and accumulated amortization for each major class of our intangible assets, other than goodwill:

|                                 | <b>Remaining<br/>useful life</b> | <b>June 30,<br/>2018</b> | <b>December 31,<br/>2017</b> |
|---------------------------------|----------------------------------|--------------------------|------------------------------|
| Gross carrying amount:          |                                  |                          |                              |
| Trade name                      | 3.5 years                        | \$492,235                | \$ 492,235                   |
| Customer relations              | 3.5 years                        | 304,086                  | 304,086                      |
| Patent                          | 7-8.67 years                     | 4,804,315                | -                            |
|                                 |                                  | 5,600,636                | 796,321                      |
| Less : Accumulated amortization |                                  |                          |                              |
| Trade name                      |                                  | \$(312,934 )             | \$ (287,561 )                |
| Customer relations              |                                  | (193,319 )               | (177,644 )                   |
| Patent                          |                                  | (283,306 )               | -                            |
|                                 |                                  | (789,559 )               | (465,205 )                   |

|                        |             |            |
|------------------------|-------------|------------|
| Intangible assets, net | \$4,811,077 | \$ 331,116 |
|------------------------|-------------|------------|

The aggregate amortization expenses for those intangible assets that continue to be amortized is reflected in amortization of intangible assets in the Consolidated Statements of Income and Comprehensive Income and were \$167,563 and \$20,524 for the three months ended June 30, 2018 and 2017, respectively. And \$335,588 and \$41,048 for the six months ended June 30, 2018 and 2017, respectively.

Amortization expenses for the next five years and thereafter are as follows:

|                   |             |
|-------------------|-------------|
| 2018 (Six Months) | \$335,587   |
| 2019              | 671,175     |
| 2020              | 671,175     |
| 2021              | 671,175     |
| 2022              | 591,816     |
| Thereafter        | 1,870,149   |
| Total             | \$4,811,077 |

## **NOTE 22 - SUMMARIZED INFORMATION OF EQUITY METHOD INVESTMENT IN THE JV COMPANY**

The Company's consolidated net income includes the Company's proportionate share of the net income or loss of the Company's equity method investees. When the Company records its proportionate share of net income in such investees, it increases equity income (loss) – net in the Company's consolidated statements of income and the Company's carrying value in that investment. Conversely, when the Company records its proportionate share of a net loss in such investees, it decreases equity income (loss) – net in the Company's consolidated statements of income and the Company's carrying value in that investment. All intra-entity profits and losses with the Company's equity method investees have been eliminated.

As of June 30, 2018, the JV Company consolidated its interests in the following entities on its financial statements: (1) its 100% interest in Kandi Changxing; (2) its 100% interest in Zhejiang Chang Dian and each of its two direct wholly-owned subsidiaries, i.e., Chang Dian Tonglu and Chang Dian Changxing; (3) its 100% interest in Kandi Shanghai; (4) its 100% interest in Kandi Jiangsu and each of its four direct wholly-owned subsidiaries, i.e., JiHeKang, JiHeKang Service Company, Liuchuang and Kandi Jinhua; and (5) 100% interest in each of the directly wholly-owned subsidiaries of JiHeKang, i.e., Tianjin BoHaiWan, Jiangsu JiDian, JiHeKang Tianjin and Guangdong JiHeKang. The Company accounted for its investments in the JV Company under the equity method of accounting because the Company has a 50% ownership interest in the JV Company. As a result, the Company's consolidated net income for the six months ended June 30, 2018, and 2017, included equity income from the JV Company during such periods.



The combined results of operations and financial position of the JV Company are summarized below:

|                                                                   | Three months ended |                |
|-------------------------------------------------------------------|--------------------|----------------|
|                                                                   | June 30,           | 2017           |
|                                                                   | 2018               |                |
| Condensed income statement information:                           |                    |                |
| Net sales                                                         | \$ 19,640,026      | \$ 18,650,533  |
| Gross loss                                                        | (4,685,789 )       | (1,487,979 )   |
| % of net sales                                                    | -23.9 %            | -8.0 %         |
| Net income (loss)                                                 | 4,751,137          | (14,577,384)   |
| % of net sales                                                    | 24.2 %             | -78.2 %        |
| Company's share in net income (loss) of JV based on 50% ownership | \$2,375,569        | \$(7,288,692 ) |

|                                                                   | Six Months ended |                |
|-------------------------------------------------------------------|------------------|----------------|
|                                                                   | June 30,         | 2017           |
|                                                                   | 2018             |                |
| Condensed income statement information:                           |                  |                |
| Net sales                                                         | \$53,412,231     | \$ 19,928,152  |
| Gross profit(loss)                                                | 874,613          | (1,824,736 )   |
| % of net sales                                                    | 1.6 %            | -9.2 %         |
| Net income (loss)                                                 | 5,772,776        | (25,185,112)   |
| % of net sales                                                    | 10.8 %           | -126.4 %       |
| Company's share in net income (loss) of JV based on 50% ownership | \$2,886,388      | \$(12,592,556) |

|                                      | June 30,       | December 31,   |
|--------------------------------------|----------------|----------------|
|                                      | 2018           | 2017           |
| Condensed balance sheet information: |                |                |
| Current assets                       | \$ 725,174,240 | \$ 696,683,086 |
| Noncurrent assets                    | 169,100,215    | 179,943,752    |
| Total assets                         | \$ 894,274,455 | \$ 876,626,838 |
| Current liabilities                  | 583,411,292    | 703,629,444    |
| Noncurrent liabilities               | 789,192        | 30,737,547     |
| Equity                               | 310,073,971    | 142,259,847    |
| Total liabilities and equity         | \$ 894,274,455 | \$ 876,626,838 |

For the six months ended June 30, 2018, and 2017, the JV Company's revenues were derived primarily from the sales of EV products and EV parts in China. During the first half of 2018, the JV Company sold a total of 5,097 units of EV products in the PRC. Because the Company has a 50% ownership interest in the JV Company and accounted for its investments in the JV Company under the equity method of accounting, the Company did not consolidate the JV Company's financial results, but rather included equity income from the JV Company during such periods.

Note: The following table illustrates the captions used in the Company's Income Statements for its equity based investment in the JV Company.

The Company's equity method investments in the JV Company for the six months ended June 30, 2018 and 2017 are as follows:

|                                                                   | June 30,<br>2018 | June 30,<br>2017 |
|-------------------------------------------------------------------|------------------|------------------|
| Investment in JV Company, beginning of the period,                | \$70,681,013     | \$77,453,014     |
| Investment in JV Company in 2018                                  | 82,338,100       | -                |
| Share of loss                                                     |                  |                  |
| Company's share in net income (loss) of JV based on 50% ownership | 2,886,388        | (12,592,556)     |
| Intercompany transaction elimination                              | (177,427 )       | (1,530,488 )     |
| Year 2017 unrealized profit realized                              | 458,790          | 223,077          |
| Subtotal                                                          | 3,167,751        | (13,899,967)     |
| Exchange difference                                               | (1,320,538 )     | 1,705,929        |
| Investment in JV Company, end of the period                       | \$154,866,326    | \$65,258,976     |

Sales to the Company's customers, the JV Company and its subsidiaries, for the three months ended June 30, 2018, were \$4,740,751 or 29% of the Company's total revenue, a decrease of 81.9% from \$26,171,724 of the same quarter last year. Sales to the Company's customers, the JV Company and its subsidiaries, for the six months ended June 30, 2018, were \$7,344,195 or 30% of the Company's total revenue, a decrease of 73.3% from \$27,483,366 of the same quarter last year. Sales to the JV Company and its subsidiaries were primarily of battery packs, body parts, EV drive motors, EV controllers, air conditioning units and other auto parts.



As of June 30, 2018 and December 31, 2017, the current and noncurrent amount due from the JV Company and its subsidiaries, was \$64,814,123 and \$162,329,623, respectively. The breakdown is as below:

|                     | June 30,<br>2018 | December 31,<br>2017 |
|---------------------|------------------|----------------------|
| Kandi Shanghai      | \$1,546,278      | \$2,354,195          |
| Kandi Changxing     | 246,592          | 912,760              |
| Kandi Jinhua        | -                | 15,718               |
| Kandi Jiangsu       | 1,482,535        | 1,506,199            |
| Liuchuang           | 727,430          | -                    |
| Zhejiang Chang Dian | 284,382          | -                    |
| JV Company          | 60,526,906       | 157,540,751          |
| Consolidated JV     | \$64,814,123     | \$162,329,623        |

On May 23, 2018, in order to obtain the manufacturing license, the JV Company increased its registered capital by RMB 1.09 billion (approximately \$165 million), of which Kandi Vehicle contributed its portion by converting the loans lent to the JV company in the amount of RMB 545 million (approximately \$83 million) that were previously included in the current and noncurrent amount due from the JV Company and its subsidiaries to the JV Company's registered capital. Geely Group became a new shareholder of the JV Company by investing RMB 545 million (approximately \$83 million) in the JV Company.

As of June 30, 2018 and December 31, 2017, the current and noncurrent amount due to the JV Company and its subsidiaries, was \$38,694 and \$0, respectively. The breakdown is as below:

|                 | June 30,<br>2018 | December 31,<br>2017 |
|-----------------|------------------|----------------------|
| Kandi Jinhua    | \$38,694         | \$ -                 |
| Consolidated JV | \$38,694         | \$ -                 |

**NOTE 23 - COMMITMENTS AND CONTINGENCIES****Guarantees and pledged collateral for bank loans to other parties**

## (1) Guarantees for bank loans

|                                         | June 30,<br><b>2018</b> | December 31,<br><b>2017</b> |
|-----------------------------------------|-------------------------|-----------------------------|
| Guarantee provided to                   |                         |                             |
| Kandi Electric Vehicles Group Co., Ltd. | 7,553,954               | -                           |
| Total                                   | \$7,553,954             | \$ -                        |

On March 15, 2013, the Company entered into a guarantee contract to serve as the guarantor of Nanlong Group Co., Ltd. (“NGCL”) for NGCL’s loan in the amount of \$3,021,582 from Shanghai Pudong Development Bank Jinhua Branch, with a related loan period of March 15, 2013, to March 15, 2016. NGCL is not related to the Company. Under this guarantee contract, the Company agreed to assume joint liability as the loan guarantor. In April 2017, Shanghai Pudong Development Bank filed a suit against NGCL, the Company and ten other parties in Zhejiang Province People’s Court in Yongkang City, alleging NGCL defaulted on a bank loan borrowed from Shanghai Pudong Development Bank for a principal amount of approximately \$2.9 million and demanding the guarantor to bear the liability for compensation. On May 27, 2017, a judicial mediation took place in Yongkang City and a mediation settlement reached in court, which the plaintiff agreed NGCL would repay the loan principal and interest plus legal expenses in installments. As of June 30, 2018, according to the enterprise credit report issued by the Credit Center of People’s Bank of China (PBOC) or the central bank of the People’s Republic of China, the Company’s guarantee for NGCL’s loan has been removed. The Company expects the likelihood of incurring losses in connection with this matter to be remote.

On September 29, 2015, the Company entered into a guarantee contract to serve as the guarantor of Zhejiang Shuguang Industrial Co., Ltd. (“ZSICL”) for a bank loan in the amount of \$4,381,293 from Ping An Bank, with a related loan period of September 29, 2015, to September 28, 2016. ZSICL is not related to the Company. Under this guarantee contract, the Company agreed to perform all the obligations of ZSICL under the loan contract if ZSICL fails to perform its obligations as set forth therein. In August 2016, Ping An Bank Yiwu Branch (“Ping An Bank”) filed a suit against ZSICL, the Company, and three other parties in Zhejiang Province People’s Court in Yiwu City, alleging ZSICL defaulted on a bank loan borrowed from Ping An Bank for a principal amount of RMB 29 million or approximately \$4.2 million (the “Principal”), for which the Company is a guarantor along with other three parties. On December 25, 2016, the court ruled that ZSICL should repay Ping An Bank the Principal and associated interest remaining on the bank loan within 10 days once the adjudication is effective; and the Company and other three parties, acted as guarantors, have joint liability for this bank loan. On July 31, 2017, the Company and Ping An Bank reached an agreement to settle. According to the agreement, the Company will pay Ping An Bank RMB 20 million or

approximately \$3.0 million in four installments before October 31, 2017 to release the Company from the guarantor liability for this default. As of June 30, 2018 and December 31, 2017, the Company has made all four installments in the total of RMB 20 million or approximately \$3.0 million to Ping An Bank and thus the Company has been released from the guarantor liability for this default. According to the Company's agreement with ZSICL, ZSICL agreed to reimburse all the Company's losses due to ZSICL's default on the loan principal and interests, of which RMB 9.9 million has been reimbursed to the Company as of the date of this report and the remaining RMB 10.1 million will be reimbursed in installments within next three years. The Company expects the likelihood of incurring losses in connection with this matter to be low.

On February 12, 2018, the Company entered into a guarantee contract to serve as the guarantor for the JV Company for bank loans in the aggregate amount of \$7,553,954 from Bank of China, with a related loan period of February 12, 2018 to August 11, 2018. Under this guarantee contract, the Company agreed to perform all the obligations of the JV Company under the loan contract if the JV Company fails to perform its obligations as set forth therein.

(2) Pledged collateral for bank loans to other parties.

As of June 30, 2018 and December 31, 2017, none of the Company's land use rights or plants and equipment were pledged as collateral securing bank loans to other parties.

## **Litigation**

Beginning in March 2017, putative shareholder class actions were filed against Kandi Technologies Group, Inc. and certain of its current and former directors and officers in the United States District Court for the Central District of California and the United States District Court for the Southern District of New York. The complaints generally allege violations of the federal securities laws based Kandi's disclosure in March 2017 that its financial statements for the years 2014, 2015 and the first three quarters of 2016 would need to be restated, and seek damages on behalf of putative classes of shareholders who purchased or acquired Kandi's securities prior to March 13, 2017. All the remaining cases are in the New York federal court, and lead plaintiff and lead counsel have been appointed.

Beginning in May 2017, purported shareholder derivative actions based on the same underlying events described above were filed against certain current and former directors of Kandi in the United States District Court for the Southern District of New York. Lead plaintiff and lead counsel have been appointed.

In October 2017, a shareholder filed a books and records action against the Company in the Delaware Court of Chancery seeking the production of certain documents generally relating to the same underlying items described above as well as attorney's fees. The Company was served with Plaintiff's verified Complaint Pursuant to 8 Del. C. Section 220 to Compel Inspection of Books and Records ("Verified Complaint") on October 4, 2017. On November 10, 2017, the Company filed its Answer to Plaintiff's Verified Complaint. The Court of Chancery originally set the matter for trial on March 14, 2018. At the joint request of the parties, the Court of Chancery adjourned the March 14th trial date to allow the parties and their counsel to attempt to negotiate a possible resolution of the matter, which negotiations were and remain ongoing without acknowledgement of any liability or prejudice to the parties' respective positions. Currently, no definitive resolution has been reached and the matter has not been rescheduled for trial.

The Company believes that although its financial statements for the years 2014, 2015 and the first three quarters of 2016 were restated, the restatements had no effect on its net income. The Company further believes that the claims referenced above are without merit, and it intends to defend against the lawsuits vigorously. The Company is unable to estimate the possible loss, if any, associated with this lawsuit. The ultimate outcome of any litigation is uncertain and the outcome of these matters, whether favorable or unfavorable, could have a negative impact on its financial condition or results of operations due to defense costs, diversion of management resources and other factors.

Litigation can be costly, and adverse results in the cases could result in substantial monetary judgments. No assurance can be made that litigation will not have a material adverse effect on its future financial position.

**NOTE 24 - SEGMENT REPORTING**

The Company has one operating segment. The Company's revenue and long-lived assets are primarily derived from and located in China. The Company does not have manufacturing operations outside of China.

The following table sets forth disaggregation of revenue:

|                                         | Three Months Ended June 30 |               |
|-----------------------------------------|----------------------------|---------------|
|                                         | 2018                       | 2017          |
|                                         | Sales Revenue              | Sales Revenue |
| Primary geographical markets            |                            |               |
| Overseas                                | \$ 663,178                 | \$ 886,374    |
| China                                   | 15,696,428                 | 26,438,905    |
| Total                                   | \$ 16,359,606              | \$ 27,325,279 |
| Major products                          |                            |               |
| EV parts                                | \$ 15,509,780              | \$ 26,202,818 |
| Off-road vehicles                       | 849,826                    | 1,122,461     |
| Total                                   | \$ 16,359,606              | \$ 27,325,279 |
| Timing of revenue recognition           |                            |               |
| Products transferred at a point in time | \$ 16,359,606              | \$ 27,325,279 |
| Total                                   | \$ 16,359,606              | \$ 27,325,279 |
|                                         |                            |               |
|                                         | Six Months Ended June 30,  |               |
|                                         | 2018                       | 2017          |
|                                         | Sales Revenue              | Sales Revenue |
| Primary geographical markets            |                            |               |
| Overseas                                | \$ 2,488,440               | \$ 2,402,538  |
| China                                   | 22,207,073                 | 29,197,314    |
| Total                                   | \$ 24,695,513              | \$ 31,599,852 |
| Major products                          |                            |               |
| EV parts                                | \$ 21,882,377              | \$ 28,867,714 |
| Off-road vehicles                       | 2,813,136                  | 2,732,138     |
| Total                                   | \$ 24,695,513              | \$ 31,599,852 |
| Timing of revenue recognition           |                            |               |
| Products transferred at a point in time | \$ 24,695,513              | \$ 31,599,852 |
| Total                                   | \$ 24,695,513              | \$ 31,599,852 |



**NOTE 25 - Related Party Transactions**

The Board must approve all related party transactions. All material related party transactions will be made or entered into on terms that are no less favorable to the Company than can be obtained from unaffiliated third parties.

There were no sales to related parties (other than the JV Company and its subsidiaries) for the three months ended June 30, 2018 and 2017. There were no sales to related parties (other than the JV Company and its subsidiaries) for the six months ended June 30, 2018 and 2017.

The details for amounts due from related parties (other than the JV Company) as of June 30, 2018 and December 31, 2017 were as below:

|                              | June<br>30,<br>2018 | December 31,<br>2017 |
|------------------------------|---------------------|----------------------|
| Service Company              | -                   | 162,048              |
| Total due from related party | \$-                 | \$ 162,048           |

The Company had a 9.5% ownership interest in the Service Company and Mr. Hu, Chairman and CEO of the Company, has a 13% ownership interest in the Service Company. In June 2018, Kandi Vehicles transferred its 9.5% ownership interest in the Service Company to Geely Group. As a result of this transaction, the amounts due from related party in connection with the Service Company were transferred to accounts receivable. The main transactions between the Company and the Service Company are purchases by the Service Company of batteries and EV parts.

For transactions with the JV Company, please refer to Note 22.

**NOTE 26 - Acquisition**

On January 3, 2018, Kandi Vehicles completed the acquisition of 100% of the equity of Jinhua An Kao Power Technology Co., Ltd located in Jinhua City, Zhejiang Province, China. Jinhua An Kao manufactures and markets a unique system of pure electric car battery replacement technologies including an intelligent constant-temperature charging station, a 50-100 channel intelligent battery charging system, a car battery replacement tool, and a car



washing machine. Jinhua An Kao also owns plug-in and soft-connection PACK technology. The acquisition is intended to strengthen Kandi's EV battery exchange offerings in order to be the best available in the market. The Company paid approximately RMB 25.93 million (approximately \$4 million) at the closing of the transaction using the cash on hand and issued a total of 2,959,837 shares of restrictive stock or 6.2% of the Company's total outstanding shares of the common stock valued at approximately \$20.7 million to the former shareholder of Jinhua An Kao and his designees (the "An Kao Shareholders"), and may be required to pay future consideration up to an additional 2,959,837 shares of common stock, which are being held in escrow, to be released contingent upon the achievement of certain net income-based milestones in next three years. Any escrowed shares that are not released from escrow to the An Kao Shareholders for failure to achieve the milestones will be forfeited and returned to the Company for cancellation. While the escrowed shares are held in escrow, the Company will retain all voting rights with respect to the shares.

As of the acquisition date, the Company recorded a contingent liability of approximately \$8.71 million, representing the estimated fair value of the contingent consideration the Company currently expects to pay to the An Kao Shareholders upon the achievement of certain net income-based milestones. The Supplementary Agreement sets forth the terms and conditions of the issuance of these shares. The fair value of the contingent consideration liability associated with additional 2,959,837 shares of restrictive common stock was estimated by using Monte Carlo simulation method, which took into account all possible scenarios. This fair value measurement is classified as Level 3 within the fair value hierarchy prescribed by ASC Topic 820, Fair Value Measurement and Disclosures. In accordance with ASC Topic 805, Business Combinations, the Company will re-measure this liability each reporting period and record changes in the fair value through a separate line item within the Company's consolidated statements of Income. During the first half of 2018, the Company recorded a gain of approximately \$3.37 million in the accompanying statements of income representing the decrease in fair value of this obligation between the acquisition date and June 30, 2018, which was largely due to the decline of the Company's stock price during the period.

The components of the preliminary purchase price as of the acquisition date for Jinhua An Kao are as follows:

|                                        |              |
|----------------------------------------|--------------|
| Cash                                   | \$3,988,765  |
| Stock awards                           | 20,718,859   |
| Fair value of contingent consideration | 8,712,996    |
| Total                                  | \$33,420,620 |

The Company accounted for the acquisition as business combinations and, in accordance with ASC Topic 805. The Company has recorded the assets acquired and liabilities assumed at their respective fair values as of the acquisition date. The following summarizes the preliminary purchase price allocations:

|                               |                  |
|-------------------------------|------------------|
|                               | Jinhua An<br>Kao |
| Goodwill                      | \$24,216,559     |
| Amortizable intangible assets | 4,892,165        |
| Other net assets              | 5,552,986        |
| Deferred income taxes         | (1,241,090 )     |
| Total                         | \$33,420,620     |

Transaction costs of \$33,295 associated with the acquisition were expensed as incurred through general and administrative expenses in the statement of income in 2018.

The Company allocated the preliminary purchase price to specific intangible asset categories as of the acquisition date for Jinhua An Kao as follows:

|                                | Amount<br>Assigned | Estimated<br>useful<br>life<br>(in years) |
|--------------------------------|--------------------|-------------------------------------------|
| Amortizable intangible assets: |                    |                                           |
| Patents                        | \$4,892,165        | 7.5 – 9.17                                |

The Company allocated the preliminary purchase price to specific intangible assets for patents that the Company acquired. The Company believes that the estimated intangible asset value so determined represent the fair value at the date of acquisition and do not exceed the amount a third party would pay for the assets. The Company used the asset based approach to derive the fair value of the amortizable intangible assets. These fair value measurements are based on significant unobservable inputs, including estimates and assumptions and, accordingly, are classified as Level 3 within the fair value hierarchy prescribed by the ASC Topic 820.

The Company recorded the excess of the purchase price over the estimated fair values of the identified assets as goodwill, which is non-deductible for tax purposes. Goodwill was established due to primarily to revenue and earnings projections associated with Jinhua An Kao’s future operations, as well as synergies expected to be gained from the integration of the business into the Company’s existed operations.

The Company’s condensed consolidated financial statements included approximately \$9.5 million of revenue and approximately \$1.3 million of operating income related to the operating results for Jinhua An Kao from its date of acquisition.

The following unaudited pro forma financial information presents the combined results of operations of Kandi and the Acquired Business as if the acquisition had occurred as of January 1, 2017. The pro forma information is not necessarily indicative of what the financial position or results of operations actually would have been had the acquisition been completed as of January 1, 2017. In addition, the unaudited pro forma financial information is not indicative of, nor does it purport to project, the future financial position or operation results of Kandi. The unaudited pro forma financial information excludes acquisition and integration costs and does not give effect to any estimated and potential cost savings or other operating efficiencies that could result from acquisition.

#### **Unaudited Pro Forma Condensed Combined Statements of Operations Information**

|                                             | Six Months Ended June 30 |                |
|---------------------------------------------|--------------------------|----------------|
|                                             | 2018                     | 2017           |
| Revenue                                     | \$24,695,513             | \$38,251,087   |
| (LOSS) FROM OPERATIONS                      | \$(2,435,714 )           | \$(30,820,314) |
| NET INCOME (LOSS)                           | \$5,102,520              | \$(34,491,168) |
| WEIGHTED AVERAGE SHARES OUTSTANDING BASIC   | \$0.10                   | \$(0.68 )      |
| WEIGHTED AVERAGE SHARES OUTSTANDING DILUTED | \$0.10                   | \$(0.68 )      |

## **Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.**

This report contains forward-looking statements within the meaning of the federal securities laws that relate to future events or our future financial performance. In some cases, you can identify forward-looking statements by terminology, such as “may,” “will,” “should,” “could,” “expect,” “plan,” “anticipate,” “believe,” “estimate,” “project,” “predict,” “potential” or “continue” or the negative of such terms or other comparable terminology, although not all forward-looking statements contain such terms.

In addition, these forward-looking statements include, but are not limited to, statements regarding implementing our business strategy; development and marketing of our products; our estimates of future revenue and profitability; our expectations regarding future expenses, including research and development, sales and marketing, manufacturing and general and administrative expenses; difficulty or inability to raise additional financing, if needed, on terms acceptable to us; our estimates regarding our capital requirements and our needs for additional financing; attracting and retaining customers and employees; sources of revenue and anticipated revenue; and competition in our market.

Forward-looking statements are only predictions. Although we believe that the expectations reflected in these forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. All of our forward-looking information is subject to risks and uncertainties that could cause actual results to differ materially from the results expected. Although it is not possible to identify all factors, these risks and uncertainties include the risk factors and the timing of any of those risk factors described in our Annual Report on Form 10-K for the year ended December 31, 2016 and those set forth from time to time in our other filings with the Securities and Exchange Commission (“SEC”). These documents are available on the SEC’s Electronic Data Gathering and Analysis Retrieval System at <http://www.sec.gov>.

### **Critical Accounting Policies and Estimates**

This section should be read together with the Summary of Significant Accounting Policies in the attached consolidated financial statements included in this report.

#### ***Estimates affecting accounts receivable and inventories***

The preparation of our consolidated financial statements requires management to make estimates and assumptions that affect our reporting of assets and liabilities (and contingent assets and liabilities). These estimates are particularly

significant where they affect the reported net realizable value of our accounts receivable and inventories.

Accounts receivable are recognized and carried at net realizable value. An allowance for doubtful accounts is recorded in the period when a loss is probable based on an assessment of specific factors, such as troubled collection, historical experience, accounts aging, ongoing business relations and other factors. Accounts are written off after exhaustive efforts at collection. If accounts receivable are to be provided for, or written off, they would be recognized in the consolidated statement of operations within operating expenses. We had an allowance for doubtful accounts of \$331,362 and \$133,930 as of June 30, 2018 and December 31, 2017, in accordance with our management's judgment based on their best knowledge.

Inventory is stated at the lower of cost, determined on a weighted average basis, or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business less the estimated cost of completion and the estimated costs necessary to make the sale. Adjustments to reduce the cost of inventory to its net realizable value are made, if required, for estimated excess, obsolescence, or impaired balances. When inventories are sold, their carrying amount is charged to expense in the year in which the revenue is recognized. Write-downs for declines in net realizable value or for losses of inventories are recognized as an expense in the year the impairment or loss occurs. There was a \$938,624 and \$620,919 of decline in net realizable value of inventory as of June 30, 2018 and December 31, 2017, respectively, due to our provision for slow moving inventory.

Although we believe that there is little likelihood that actual results will differ materially from our current estimates, if customer demand for our products decreases significantly in the near future, or if the financial condition of our customers deteriorates in the near future, we could realize significant write downs for slow-moving inventories or uncollectible accounts receivable.

#### ***Policy affecting recognition of revenue***

Our revenue recognition policy plays a key role in our consolidated financial statements.

We recognize revenue when goods or services are transferred to customers in an amount that reflects the consideration which it expects to receive in exchange for those goods or services. In determining when and how revenue is recognized from contracts with customers, we perform the following five-step analysis: (i) identification of contract with customer (ii) determination of performance obligations (iii) measurement of the transaction price (iv) allocation of the transaction price to the performance obligations and (v) recognition of revenue when (or as) we satisfy each performance obligation.

We generate revenue through the sale of EV products, EV parts and off-road vehicles and our revenue recognition policies for our EV products, EV parts and off-road vehicles are the same. The revenue is recognized at a point in time once we have determined that the customer has obtained control over the product. Control is typically deemed to have been transferred to the customer when the performance obligation is fulfilled, usually at the time of delivery, at the net sales price (transaction price). Estimates of variable consideration, such as volume discounts and rebates, are determined, reviewed and revised periodically by management. Revenue is recognized net of any taxes collected from customers, which are subsequently remitted to governmental authorities. Shipping and handling costs for product shipments occur prior to the customer obtaining control of the goods are accounted for as fulfillment costs rather than separate performance obligations and recorded as sales and marketing expenses.





*Policy affecting options, warrants and convertible notes*

Our stock option cost is recorded in accordance with ASC 718 and ASC 505. The fair value of stock options is estimated using the Black-Scholes -Merton model. Our expected volatility assumption is based on the historical volatility of our stock. The expected life assumption is primarily based on the expiration date of the option. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Stock option expense recognition is based on awards expected to vest. There were no estimated forfeitures. ASC standards require forfeitures to be estimated at the time of grant and revised in subsequent periods, if necessary, if actual forfeitures differ from those estimates.

Our warrant costs are recorded in liabilities and equities, respectively, in accordance with ASC 480, ASC 505 and ASC 815. The fair value of a warrant, which is classified as a liability, is estimated using the Binomial Tree model and the lattice valuation model. Our expected volatility assumption is based on the historical volatility of our common stock. The expected life assumption is primarily based on the expiration date of the warrant. The risk-free interest rate for the expected term of the warrant is based on the U.S. Treasury yield curve in effect at the time of measurement. Our warrants, which are freestanding derivatives classified as liabilities on the balance sheet, are measured at fair value on each reporting date, with decreases in fair value recognized in earnings and increases in fair values recognized in expenses.

The fair value of equity-based warrants, which are not considered derivatives under ASC 815, is estimated using the Black-Scholes -Merton model. Our expected volatility assumption is based on the historical volatility of our common stock. The expected life assumption is primarily based on the expiration date of the warrant. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

In accordance with ASC 815, the conversion feature of the convertible notes is separated from the debt instrument and accounted for separately as a derivative instrument. On the date the convertible notes are issued, the conversion feature is recorded as a liability at its fair value, and future decreases in fair value are recognized in earnings while increases in fair values are recognized in expenses. We used the Black-Scholes -Merton option-pricing model to obtain the fair value of the conversion feature. The expected volatility assumption is based on the historical volatility of our common stock. The expected life assumption is primarily based on the expiration date of the conversion features. The risk-free interest rate for the expected term of the conversion features is based on the U.S. Treasury yield curve in effect at the time of measurement.

*Warranty Liability*

Most of our non-EV products (“Legacy Products”) are exported out of China to foreign countries that have legal and regulatory requirements with which we are not familiar. The development of warranty policies for our Legacy Products in each of these countries would be virtually impossible and prohibitively expensive. Therefore, we provide price incentives and free parts to our customers and in exchange, our customers establish appropriate warranty policies and assume warranty responsibilities.

Consequently, warranty issues are taken into consideration during price negotiations for our products. Free parts are delivered along with the products, and when products are sold, the related parts are recorded as cost of goods sold. Due to the reliability of our products, we have been able to maintain this warranty policy and we have not had any product liability attributed to our products.

For the EV products that we sell in China, we provide a three year or 50,000 kilometer manufacturer warranty. This warranty affects the Company through our participation and investment in the JV Company, which manufactures the EV products.

## Results of Operations

### Overview

We are one of the leading manufacturers of EV products (through the JV Company), EV parts and off road vehicles in China. For the six months ended June 30, 2018, we recognized total revenue of \$24,695,513 as compared to \$31,599,852 for the six months ended June 30, 2017, a decrease of \$6,904,339, or 21.8%, primarily because, according to the changes of national subsidy policies in 2018, the JV Company discontinued the manufacturing and selling of its EV products with a driving range of less than 200km and shifted its focus to the development of new EV models with a driving range exceeding 300km. Currently, our new 300km EV models K23, K27, and K28 (EX3) received the approval from the Ministry of Industry and Information Technology of the People's Republic of China. In August, the JV Company has started normal production. For the six months ended June 30, 2018, we recorded \$3,403,963 of gross profits, a decrease of \$1,020,305 or 23.1% from the same period of 2017. Gross margin for the six months ended June 30, 2018, was 13.8%, a decrease from 14.0% from the six months ended June 30, 2017. We recorded a net income of \$5,102,520 for the six months ended June 30, 2018, compared to net loss of \$35,711,452 in the same period of 2017, largely due to profits from the JV Company and decreased R&D expenses this period as compared to the same period of last year.

### Comparison of the Three Months Ended June 30, 2018 and 2017

The following table sets forth the amounts and percentage relationship to revenue of certain items in our condensed consolidated statements of income (loss) and comprehensive income (loss) for the three months ended June 30, 2018 and 2017.

|                                                 | Three Months Ended |                 |            | Three Months Ended |                 |              | Change in<br>Amount | Change<br>in<br>% |
|-------------------------------------------------|--------------------|-----------------|------------|--------------------|-----------------|--------------|---------------------|-------------------|
|                                                 | June 30,<br>2018   | % of<br>Revenue |            | June 30,<br>2017   | % of<br>Revenue |              |                     |                   |
| REVENUES FROM UNRELATED PARTY, NET              | 11,618,855         | 71.0 %          | 1,153,555  | 4.2 %              |                 | 10,465,300   | 907.2 %             |                   |
| REVENUES FROM JV COMPANY AND RELATED PARTY, NET | 4,740,751          | 29.0 %          | 26,171,724 | 95.8 %             |                 | (21,430,973) | (81.9 %)            |                   |
| REVENUES, NET                                   | 16,359,606         |                 | 27,325,279 |                    |                 | (10,965,673) | (40.1 %)            |                   |

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|                                                  |              |          |              |          |              |           |
|--------------------------------------------------|--------------|----------|--------------|----------|--------------|-----------|
| COST OF GOODS SOLD                               | (14,301,594) | (87.4 %) | (23,568,343) | (86.3 %) | 9,266,749    | (39.3 %)  |
| GROSS PROFIT                                     | 2,058,012    | 12.6 %   | 3,756,936    | 13.7 %   | (1,698,924 ) | (45.2 %)  |
| OPERATING EXPENSES:                              |              |          |              |          |              |           |
| Research and development                         | (642,889 )   | (3.9 %)  | (5,142,041 ) | (18.8 %) | 4,499,152    | (87.5 %)  |
| Selling and marketing                            | (228,173 )   | (1.4 %)  | (402,253 )   | (1.5 %)  | 174,080      | (43.3 %)  |
| General and administrative                       | (3,861,263 ) | (23.6 %) | (1,558,652 ) | (5.7 %)  | (2,302,611 ) | 147.7 %   |
| Total Operating Expenses                         | (4,732,325 ) | (28.9 %) | (7,102,946 ) | (26.0 %) | 2,370,621    | (33.4 %)  |
| INCOME (LOSS) FROM OPERATIONS                    | (2,674,313 ) | (16.3 %) | (3,346,010 ) | (12.2 %) | 671,697      | (20.1 %)  |
| OTHER INCOME(EXPENSE):                           |              |          |              |          |              |           |
| Interest income                                  | 456,784      | 2.8 %    | 559,425      | 2.0 %    | (102,641 )   | (18.3 %)  |
| Interest expense                                 | (471,616 )   | (2.9 %)  | (548,810 )   | (2.0 %)  | 77,194       | (14.1 %)  |
| Change in fair value of contingent consideration | 686,833      | 4.2 %    | -            | 0.0 %    | 686,833      | -         |
| Government grants                                | 15,558       | 0.1 %    | 262,137      | 1.0 %    | (246,579 )   | (94.1 %)  |
| Share of income (loss) after tax of JV           | 2,372,696    | 14.5 %   | (8,738,254 ) | (32.0 %) | 11,110,950   | (127.2 %) |
| Other income , net                               | 627,582      | 3.8 %    | 121,556      | 0.4 %    | 506,026      | 416.3 %   |
| Total other income (expense), net                | 3,687,837    | 22.5 %   | (8,343,946 ) | (30.5 %) | 12,031,783   | (144.2 %) |
| INCOME (LOSS) BEFORE INCOME TAXES                | 1,013,524    | 6.2 %    | (11,689,956) | (42.8 %) | 12,703,480   | (108.7 %) |
| INCOME TAX (EXPENSE) BENEFIT                     | 361,001      | 2.2 %    | 131,939      | 0.5 %    | 229,062      | 173.6 %   |
| NET INCOME (LOSS)                                | 1,374,525    | 8.4 %    | (11,558,017) | (42.3 %) | 12,932,542   | (111.9 %) |

**(a) Revenue**

For the three months ended June 30, 2018, our revenue was \$16,359,606 compared to \$27,325,279 for the same period of 2017, a decrease of \$10,965,673 or 40.1%. The decrease in revenue was mainly due to the decrease in EV parts sales during this quarter. The selling prices of our products for the three months ended June 30, 2018 didn't change materially on average from the same period last year. The decrease in revenue was primarily due to the decrease of sales volume.

The following table summarizes our revenues by product types for the three months ended June 30, 2018 and 2017:

|                   | Three Months Ended<br>June 30 |               |
|-------------------|-------------------------------|---------------|
|                   | <b>2018</b>                   | <b>2017</b>   |
|                   | <b>Sales</b>                  | <b>Sales</b>  |
| EV parts          | \$ 15,509,780                 | \$ 26,202,818 |
| Off-road vehicles | 849,826                       | 1,122,461     |
| Total             | \$ 16,359,606                 | \$ 27,325,279 |

**EV Parts**

During the three months ended June 30, 2018, our revenues from the sale of EV parts were \$15,509,780, representing a decrease of \$10,693,038 or 40.8% from \$26,202,818 for the same quarter of 2017.

Our revenue for the three months ended June 30, 2018 primarily consisted of the sales of battery packs, body parts, EV controllers, air conditioning units and other auto parts for use in the manufacturing of EV products, which accounted for 94.8% of total sales. Among total sales for the three months ended June 30, 2018, approximately 79.5% were related to the sale of battery packs. In compliance with the regulation of the Chinese auto industry, we hold the necessary production licenses to manufacture the battery packs exclusively used in EV products manufactured by the JV Company. Besides the sale of battery packs, approximately 2.4% of total sales were related to sales of EV controllers, approximately 5.5% of the total sales were related to sales of air conditioning units, approximately 5.0% of total sales were related to sales of EV drive motors and approximately 2.3% of total sales were related to sales of body parts and other auto parts.

During the three months ended June 30, 2018 and 2017, our revenues from the sale of EV parts to the JV Company and its subsidiaries accounted for approximately 29% and 96% of our total net revenue for the quarter, respectively. The EV parts we sold to the JV Company were used in manufacturing pure EV products by the JV Company's subsidiaries.

### Off-Road Vehicles

During the three months ended June 30, 2018, our revenues from the sale of off-road vehicles including go karts, all-terrain vehicles ("ATVs"), and others, were \$849,826, representing a decrease of \$272,635 or 24.3% from \$1,122,461 for the same quarter of 2017.

Our off-road vehicles business line accounted for approximately 5.2% of our total net revenue for the three months ended June 30, 2018. Of our off-road vehicle revenue, our go-kart business accounted for approximately 5.2% of our total net revenue.

The following table shows the breakdown of our net revenues:

|                                         | Three Months Ended<br>June 30,    |                                   |
|-----------------------------------------|-----------------------------------|-----------------------------------|
|                                         | <b>2018<br/>Sales<br/>Revenue</b> | <b>2017<br/>Sales<br/>Revenue</b> |
| Primary geographical markets            |                                   |                                   |
| Overseas                                | \$663,178                         | \$886,374                         |
| China                                   | 15,696,428                        | 26,438,905                        |
| Total                                   | \$16,359,606                      | \$27,325,279                      |
| Major products                          |                                   |                                   |
| EV parts                                | \$15,509,780                      | \$26,202,818                      |
| Off-road vehicles                       | 849,826                           | 1,122,461                         |
| Total                                   | \$16,359,606                      | \$27,325,279                      |
| Timing of revenue recognition           |                                   |                                   |
| Products transferred at a point in time | \$16,359,606                      | \$27,325,279                      |
| Total                                   | \$16,359,606                      | \$27,325,279                      |



**(b) Cost of goods sold**

Cost of goods sold was \$14,301,594 during the three months ended June 30, 2018, representing a decrease of \$9,266,749, or 39.3%, compared to \$23,568,343 for the same period of 2017. The decrease was primarily due to the corresponding decrease in sales. Please refer to the Gross Profit section below for product margin analysis.

**(c) Gross profit**

Our margins by product for the past three years are as set forth below:

|                      | Three Months Ended June 30,<br>2018 |            |                         |             | 2017         |            |                         |             |
|----------------------|-------------------------------------|------------|-------------------------|-------------|--------------|------------|-------------------------|-------------|
|                      | Sales                               | Cost       | <b>Gross<br/>Profit</b> | Margin<br>% | Sales        | Cost       | <b>Gross<br/>Profit</b> | Margin<br>% |
| EV parts             | \$15,509,780                        | 13,583,969 | 1,925,811               | 12.4 %      | \$26,202,818 | 22,606,828 | 3,595,990               | 13.7 %      |
| Off-road<br>vehicles | 849,826                             | 717,625    | 132,201                 | 15.6 %      | 1,122,461    | 961,515    | 160,946                 | 14.3 %      |
| Total                | \$16,359,606                        | 14,301,594 | 2,058,012               | 12.6 %      | \$27,325,279 | 23,568,343 | 3,756,936               | 13.7 %      |

Gross profit for the second quarter of 2018 decreased 45.2% to \$2,058,012, compared to \$3,756,936 for the same period last year. This was primarily attributable to the sales decrease. Our gross margin decreased to 12.6% compared to 13.7% for the same period of 2017. The decrease in our gross margin was mainly due to the vast majority of gross profits came from less profitable EV parts business in the three months ended June 30, 2018.

**(d) Research and development**

Research and development expenses, including materials, labor, equipment depreciation, design, testing, inspection, and other related expenses totaled \$642,889 for the second quarter of 2018, a decrease of \$4,499,152 or 87.5% compared to \$5,142,041 for the same period of last year. This decrease was primarily due to the completion of most R&D works and the significant decrease in research and development expenses related to the development of EV Model K23 at Hainan facility for the three months ended June 30, 2018. For the three months ended June 30, 2018 and 2017, approximately 0% and 94.1% of our research and development expenses were spent on the research and



development of EV Model K23 at Hainan facility, respectively, and the rest was spent on other various EV and off-road vehicles research and development projects.

**(e) Sales and marketing**

Selling and distribution expenses were \$228,173 for the second quarter of 2018, compared to \$402,253 for the same period last year, a decrease of \$174,080 or 43.4%. This decrease was primarily attributable to the decrease in product maintenance expenses and shipping costs during this period because of decreased sales this quarter as compared to the same quarter of last year.

**(f) General and administrative expenses**

General and administrative expenses were \$3,861,263 for the second quarter of 2018, compared to \$1,558,652 for the same period of last year, an increase in expenses of \$2,302,611 or 147.7%. For the three months ended June 30, 2018, general and administrative expenses included \$1,837,965 in expenses for common stock awards and stock options to employees and Board members, compared to \$2,016,043 of common stock awards and stock options expenses for the same period in 2017. Excluding stock compensation expense, our net general and administrative expenses for the three months ended June 30, 2018 were \$2,023,298, an increase of \$2,480,689, from negative \$457,391 for the same period of 2017, which was largely because we included an adjustment of approximately \$1.7 million of expense reduction to a previously accrued contingent loss in connection with a litigation last year.

**(g) Interest income**

Interest income was \$456,784 for the second quarter of 2018, a decrease of \$102,641 or 18.3% compared to \$559,425 for the same period of last year. This decrease was primarily attributable to decreased interests earned on the loans lent to the JV Company as the loans were converted to the JV Company's registered capital during the second quarter.

**(h) Interest expenses**

Interest expenses were \$471,616 in the second quarter of 2018, a decrease of \$77,194 or 14.1% compared to \$548,810 for the same period of last year. This decrease was primarily due to less interest expenses incurred associated with the note payable to a third party. Of the interest expenses, \$0 and \$1,054 were discounts associated with the settlement of bank acceptance notes for the three months ended June 30, 2018 and 2017, respectively.

**(i) Change in fair value of contingent consideration**

For the second quarter of 2018, the gain related to changes in the fair value of contingent consideration was \$686,833, which was mainly the result of the decrease in fair value of contingent liability during the second quarter for the acquisition of Jinhua An Kao.

**(j) Government grants**

Government grants were \$15,558 for the second quarter of 2018, compared to \$262,137 for the same quarter last year, representing a decrease of \$246,579, or 94.1%, which was largely due to less government awards received from local government during the second quarter.

**(k) Share of income (loss) after tax of the JV Company**

For the second quarter of 2018, the JV Company's net sales were \$19,640,026, gross loss was \$4,685,789, and net income was \$4,751,137. We accounted for our investments in the JV Company under the equity method of accounting because we have a 50% ownership interest in the JV Company. As a result, we recorded 50% of the JV Company's income for \$2,375,569 for the second quarter of 2018. After eliminating intra-entity profits and losses, our share of income after tax of the JV Company was \$2,372,696 for the second quarter of 2018, an increase of \$11,110,950 compared to \$8,738,254 of share of (loss) after tax of the JV Company in the same period of last year. The increase of the JV Company's profits was largely due to moderate EV product sales this period as compared to limited EV products sold in the same period of 2017 and realized local government grants for operations.

During the second quarter of 2018, the JV Company sold a total of 1,802 units of EV products in the PRC.

**(l) Other income, net**

Net other income was \$627,582 for the second quarter of 2018, an increase of \$506,026 or 416.3% compared to net other income of \$121,556 for the same period of last year, which was largely due to the fees earned on technology development services during the second quarter.

**(m) Income Taxes**

In accordance with the relevant Chinese tax laws and regulations, our applicable corporate income tax rate is 25%. However, Kandi Vehicles is qualified as a high technology enterprise in China and is therefore entitled to use a reduced income tax rate of 15%.

Each of our wholly-owned subsidiaries, Kandi New Energy, Yongkang Scrou, Kandi Hainan and Jinhua An Kao, has an applicable corporate income tax rate of 25%.

We have a 50% ownership interest in the JV Company, which has an applicable corporate income tax rate of 25%. Each of the JV Company's subsidiaries has an applicable corporate income tax rate of 25% as well.

Our actual effective income tax rate for the second quarter of 2018 was a tax benefit of 35.62% on a reported income before taxes of approximately \$1.0 million, compared to an effective income tax rate with a tax benefit of 1.1% on a reported loss before taxes of approximately \$11.6 million for the same period of last year.

**(n) Net income (loss)**

Net income was \$1,374,525 for the second quarter of 2018, an increase of \$12,932,542 compared to net loss \$11,558,017 for the same period of last year. The increase was primarily attributable to the profits from the JV Company and decreased R&D expenses this period as compared to the same period of last year.

Excluding (i) the effects of stock compensation expenses, which were \$1,837,965 and \$2,016,043 for the second quarter of 2018 and 2017, respectively, and (ii) the change in fair value of contingent consideration which was a gain of \$686,833 and \$0 for the three months ended June 30, 2018 and 2017, respectively, our non-GAAP net income was \$2,525,657 for the three months ended June 30, 2018 as compared to non-GAAP net loss \$9,541,974 for the same period of 2017, an increase of \$12,067,631, or 126.5%. The increase in net income (non-GAAP) was primarily attributable to profits from the JV Company and decreased R&D expenses this period as compared to the same period of last year.

We make reference to certain non-GAAP financial measures, i.e., adjusted net income. Management believes that such adjusted financial results are useful for investors in evaluating our operating performance because they present a meaningful measure of corporate performance. See the non-GAAP reconciliation table below. Any non-GAAP measures should not be considered as a substitute for, and should only be read in conjunction with, measures of financial performance prepared in accordance with the GAAP.

The following table summarizes our non-GAAP net income for the three months ended June 30, 2018 and 2017:

|                                                  | Three Months Ended |                |
|--------------------------------------------------|--------------------|----------------|
|                                                  | June 30,           |                |
|                                                  | 2018               | 2017           |
| GAAP net income (loss)                           | \$1,374,525        | \$(11,558,017) |
| Stock compensation expenses                      | 1,837,965          | 2,016,043      |
| Change in fair value of contingent consideration | (686,833 )         | -              |
| Non-GAAP net income (loss)                       | \$2,525,657        | \$(9,541,974 ) |

### Comparison of the Six Months Ended June 30, 2018 and 2017

The following table sets forth the amounts and percentage relationship to revenue of certain items in our condensed consolidated statements of income (loss) and comprehensive income (loss) for the six months ended June 30, 2018 and 2017.

|                                                       | Six Months Ended |                 |              |           |  | Change in    | Change   |
|-------------------------------------------------------|------------------|-----------------|--------------|-----------|--|--------------|----------|
|                                                       | June 30,<br>2018 | % of<br>Revenue |              |           |  |              |          |
| REVENUES FROM<br>UNRELATED PARTY, NET                 | \$17,351,318     | 70.3 %          | \$4,116,486  | 13.0 %    |  | 13,234,832   | 321.5 %  |
| REVENUES FROM JV<br>COMPANY AND RELATED<br>PARTY, NET | 7,344,195        | 29.7 %          | 27,483,366   | 87.0 %    |  | (20,139,171) | (73.3 %) |
| REVENUES, NET                                         | 24,695,513       | 100.0 %         | 31,599,852   | 100.0 %   |  | (6,904,339 ) | (21.8 %) |
| COST OF GOODS SOLD                                    | (21,291,550)     | (86.2 %)        | (27,175,584) | (86.0 %)  |  | 5,884,034    | (21.7 %) |
| GROSS PROFIT                                          | 3,403,963        | 13.8 %          | 4,424,268    | 14.0 %    |  | (1,020,305 ) | (23.1 %) |
| OPERATING EXPENSES:                                   |                  |                 |              |           |  |              |          |
| Research and development                              | (1,400,187 )     | (5.7 %)         | (25,911,773) | (82.0 %)  |  | 24,511,586   | (94.6 %) |
| Selling and marketing                                 | (976,398 )       | (4.0 %)         | (760,562 )   | (2.4 %)   |  | (215,836 )   | 28.4 %   |
| General and administrative                            | (3,463,092 )     | (14.0 %)        | (9,877,946 ) | (31.3 %)  |  | 6,414,854    | (64.9 %) |
| Total Operating Expenses                              | (5,839,677 )     | (23.6 %)        | (36,550,281) | (115.7 %) |  | 30,710,604   | (84.0 %) |
|                                                       | (2,435,714 )     | (9.9 %)         | (32,126,013) | (101.7 %) |  | 29,690,299   | (92.4 %) |

INCOME (LOSS) FROM  
OPERATIONS

## OTHER INCOME(EXPENSE):

|                                                  |                |          |        |                  |            |        |                  |            |        |
|--------------------------------------------------|----------------|----------|--------|------------------|------------|--------|------------------|------------|--------|
| Interest income                                  | 1,399,777      | 5.7      | %      | 1,090,067        | 3.4        | %      | 309,710          | 28.4       | %      |
| Interest expense                                 | (1,022,033 )   | (4.1     | %)     | (1,163,263 )     | (3.7       | %)     | 141,230          | (12.1      | %)     |
| Change in fair value of contingent consideration | 3,367,012      | 13.6     | %      | -                | 0.0        | %      | 3,367,012        | -          |        |
| Government grants                                | 110,813        | 0.4      | %      | 5,329,611        | 16.9       | %      | (5,218,798 )     | (97.9      | %)     |
| Share of income (loss) after tax of JV           | 3,167,751      | 12.8     | %      | (13,899,967)     | (44.0      | %)     | 17,067,718       | (122.8     | %)     |
| Other income, net                                | 650,559        | 2.6      | %      | 150,177          | 0.5        | %      | 500,382          | 333.2      | %      |
| Total other income (expense), net                | 7,673,879      | 31.1     | %      | (8,493,375 )     | (26.9      | %)     | 16,167,254       | (190.4     | %)     |
| <br>INCOME (LOSS) BEFORE<br>INCOME TAXES         | <br>5,238,165  | <br>21.2 | <br>%  | <br>(40,619,388) | <br>(128.5 | <br>%) | <br>45,857,553   | <br>(112.9 | <br>%) |
| <br>INCOME TAX (EXPENSE)<br>BENEFIT              | <br>(135,645 ) | <br>(0.5 | <br>%) | <br>4,907,936    | <br>15.5   | <br>%  | <br>(5,043,581 ) | <br>(102.8 | <br>%) |
| <br>NET INCOME (LOSS)                            | <br>5,102,520  | <br>20.7 | <br>%  | <br>(35,711,452) | <br>(113.0 | <br>%) | <br>40,813,972   | <br>(114.3 | <br>%) |

**(a) Revenue**

For the six months ended June 30, 2018, our revenue was \$24,695,513 compared to 31,599,852 for the same period of 2017, a decrease of \$6,904,339 or 21.8%. The decrease in revenue was mainly due to the decrease in EV parts sales during this period. The selling prices of our products for the six months ended June 30, 2018 didn't change materially on average from the same period last year. The decrease in revenue was primarily due to the decrease of sales volume.

The following table summarizes our revenues by product types for the six months ended June 30, 2018 and 2017:

|                   | <b>Six Months Ended</b> |              |
|-------------------|-------------------------|--------------|
|                   | <b>June 30</b>          |              |
|                   | <b>2018</b>             | <b>2017</b>  |
|                   | <b>Sales</b>            | <b>Sales</b> |
| EV parts          | \$21,882,377            | \$28,867,714 |
| Off-road vehicles | 2,813,136               | 2,732,138    |
| Total             | \$24,695,513            | \$31,599,852 |

**EV Parts**

During the six months ended June 30, 2018, our revenues from the sale of EV parts were \$21,882,377, representing a decrease of \$6,985,337 or 24.2% from \$28,867,714 for the same quarter of 2017.

Our revenue for the six months ended June 30, 2018 primarily consisted of the sales of battery packs, body parts, EV controllers, air conditioning units and other auto parts for use in the manufacturing of EV products, which accounted for 88.6% of total sales. Among total sales for the six months ended June 30, 2018, approximately 77.0% were related to the sale of battery packs. Besides the sale of battery packs, approximately 2.2% of total sales were related to sales of EV controllers, approximately 3.8% of the total sales were related to sales of air conditioning units, approximately 3.3% of total sales were related to sales of EV drive motors and approximately 2.4% of total sales were related to sales of body parts and other auto parts.

During the six months ended June 30, 2018 and 2017, our revenues from the sale of EV parts to the JV Company and its subsidiaries accounted for approximately 30% and 87% of our total net revenue for the period, respectively. The EV parts we sold to the JV Company were used in manufacturing pure EV products by the JV Company's subsidiaries.



Off-Road Vehicles

During the six months ended June 30, 2018, our revenues from the sale of off-road vehicles including go karts, all-terrain vehicles (“ATVs”), and others, were \$2,813,136, representing an increase of \$80,998 or 3.0% from \$2,732,138 for the same quarter of 2017, which was largely due to its organic growth.

Our off-road vehicles business line accounted for approximately 11.4% of our total net revenue for the six months ended June 30, 2018. Of our off-road vehicle revenue, our go-kart business accounted for approximately 7.9% of our total net revenue, and our ATV business accounted for approximately 3.5% of our total net revenue.

The following table shows the breakdown of our net revenues:

|                                         | Six Months Ended |              |
|-----------------------------------------|------------------|--------------|
|                                         | June 30          |              |
|                                         | 2018             | 2017         |
|                                         | Sales            | Sales        |
|                                         | Revenue          | Revenue      |
| Primary geographical markets            |                  |              |
| Overseas                                | \$2,488,440      | \$2,402,538  |
| China                                   | 22,207,073       | 29,197,314   |
| Total                                   | \$24,695,513     | \$31,599,852 |
| Major products                          |                  |              |
| EV parts                                | \$21,882,377     | \$28,867,714 |
| Off-road vehicles                       | 2,813,136        | 2,732,138    |
| Total                                   | \$24,695,513     | \$31,599,852 |
| Timing of revenue recognition           |                  |              |
| Products transferred at a point in time | \$24,695,513     | \$31,599,852 |
| Total                                   | \$24,695,513     | \$31,599,852 |

**(b) Cost of goods sold**

Cost of goods sold was \$21,291,550 during the six months ended June 30, 2018, representing a decrease of \$5,884,034, or 21.7%, compared to \$27,175,584 for the same period of 2017. The decrease was primarily due to the corresponding decrease in sales. Please refer to the below Gross Profit section for product margin analysis.

**(c) Gross profit**

Our margins by product for the past three years are as set forth below:

|                   | Six Months Ended June 30<br>2018 |            |              |          | 2017         |            |              |          |
|-------------------|----------------------------------|------------|--------------|----------|--------------|------------|--------------|----------|
|                   | Sales                            | Cost       | Gross Profit | Margin % | Sales        | Cost       | Gross Profit | Margin % |
| EV parts          | \$21,882,377                     | 18,824,760 | 3,057,617    | 14.0 %   | \$28,867,714 | 24,797,448 | 4,070,266    | 14.1 %   |
| Off-road vehicles | 2,813,136                        | 2,466,790  | 346,346      | 12.3 %   | 2,732,138    | 2,378,137  | 354,002      | 13.0 %   |
| Total             | \$24,695,513                     | 21,291,550 | 3,403,963    | 13.8 %   | \$31,599,852 | 27,175,584 | 4,424,268    | 14.0 %   |

Gross profit for the first half of 2018 decreased 23.1% to \$3,403,963, compared to \$4,424,268 for the same period last year. This was primarily attributable to the sales decrease. Our gross margin decreased to 13.8% compared to 14.0% for the same period of 2017. The decrease in our gross margin was mainly because the vast majority of gross profits came from less profitable EV parts business in the six months ended June 30, 2018.

**(d) Research and development**

Research and development expenses, including materials, labor, equipment depreciation, design, testing, inspection, and other related expenses totaled \$1,400,187 for the first half of 2018, a decrease of \$24,511,586 or 94.6% compared to \$25,911,773 for the same period of last year. This decrease was primarily due to the completion of most R&D works and the significant decrease in research and development expenses related to the development of EV Model K23 at Hainan facility for the six months ended June 30, 2018. For the six months ended June 30, 2018 and 2017, approximately 0% and 98.0% of our research and development expenses were spent on the research and development of EV Model K23 at Hainan facility, respectively, and the rest was spent on other various EV and off-road vehicles research and development projects.

**(e) Sales and marketing**

Selling and distribution expenses were \$976,398 for the first half of 2018, compared to \$760,562 for the same period last year, an increase of \$215,836 or 28.4%. This increase was primarily attributable to the increase in sales labor as compared to last year.

**(f) General and administrative expenses**

General and administrative expenses were \$3,463,092 for the first half of 2018, compared to \$9,877,946 for the same period of last year, a decrease in expenses of \$6,414,854 or 64.9%. For the six months ended June 30, 2018, general and administrative expenses included \$2,867,136 in expenses for common stock awards and stock options to employees and Board members net of \$2,644,877 of reversal of previously accrued stock option expenses for forfeited stock option, compared to \$4,493,187 of common stock awards and stock options expenses for the same period in 2017. Excluding stock compensation expense, our net general and administrative expenses for the six months ended June 30, 2018 were \$3,240,833, a decrease of \$2,143,926, or 39.8%, from \$5,384,759 for the same period of 2017, which was largely because we accrued contingent loss of approximately \$2.9 million in connection with litigation last year.

**(g) Interest income**

Interest income was \$1,399,777 for the first half of 2018, an increase of \$309,710 or 28.4% compared to \$1,090,067 for the same period of last year. This increase was primarily attributable to increased interests earned on loans to the JV Company.

**(h) Interest expenses**

Interest expenses were \$1,022,033 in the first half of 2018, a decrease of \$141,230 or 12.1% compared to \$1,163,263 for the same period of last year. This decrease was primarily due to less interest expenses incurred associated with the note payable to a third party. Of the interest expenses, \$53,342, and \$61,583 were discounts associated with the settlement of bank acceptance notes for the six months ended June 30, 2018 and 2017, respectively.

**(i) Change in fair value of contingent consideration**

For the first half of 2018, the gain related to changes in the fair value of contingent consideration was \$3,367,012, which was mainly the result of the decrease in fair value of contingent liability between the acquisition date and June 30, 2018 for the acquisition of Jinhua An Kao.

**(j) Government grants**

Government grants were \$110,813 for the first half of 2018, compared to \$5,329,611 for the same quarter last year, representing a decrease of \$5,218,798, or 97.9%. This decrease in government grants was primarily because there were significant amount of government subsidies we received from Hainan provincial government to assist our development of new EV model last year.

**(k) Share of income (loss) after tax of the JV Company**

For the first half of 2018, the JV Company's net sales were \$53,412,231, gross profit was \$874,613, and net income was \$5,772,776. We accounted for our investments in the JV Company under the equity method of accounting because we have a 50% ownership interest in the JV Company. As a result, we recorded 50% of the JV Company's income for \$2,886,388 for the first half of 2018. After eliminating intra-entity profits and losses, our share of income after tax of the JV Company was \$3,167,751 for the first half of 2018, an increase of \$17,067,718 compared to \$13,899,967 of share of (loss) after tax of the JV Company in the same period of last year. The increase of the JV Company's profits was largely due to moderate EV product sales this period as compared to limited EV products sold in the same period of 2017 and realized local government grants for operations.

During the first half of 2018, the JV Company sold a total of 5,097 units of EV products in the PRC.

**(l) Other income, net**

Net other income was \$650,559 for the first half of 2018, an increase of \$500,382 or 333.2% compared to net other income of \$150,177 for the same period of last year, which was largely due to the fees earned on technology development services during the second quarter.

**(m) Income Taxes**

In accordance with the relevant Chinese tax laws and regulations, our applicable corporate income tax rate is 25%. However, Kandi Vehicles is qualified as a high technology enterprise in China and is therefore entitled to use a reduced income tax rate of 15%.

Each of our wholly-owned subsidiaries, Kandi New Energy, Yongkang Scrou, Kandi Hainan and Jinhua An Kao, has an applicable corporate income tax rate of 25%.

We have a 50% ownership interest in the JV Company, which has an applicable corporate income tax rate of 25%. Each of the JV Company's subsidiaries has an applicable corporate income tax rate of 25% as well.

Our actual effective income tax rate for the first half of 2018 was a tax expense of 2.59% on a reported income before taxes of approximately \$5.2 million, compared to an effective income tax rate with a tax benefit of 12.08% for the same period of last year on a reported loss before taxes of approximately \$40.6 million.

**(n) Net income (loss)**

Net income was \$5,102,520 for the first half of 2018, an increase of \$40,813,972 compared to net loss \$35,711,452 for the same period of last year. The increase was primarily attributable to the profits from the JV Company and significantly decreased R&D expenses this period.

Excluding (i) the effects of stock compensation expenses, which were \$2,867,136 net of a reversal for forfeited stock option of \$2,644,877 and \$4,493,187 for the first half of 2018 and 2017, respectively, and (ii) the change in fair value of contingent consideration which was a gain of \$3,367,012 and \$0 for the six months ended June 30, 2018 and 2017, respectively, our non-GAAP net income was \$1,957,767 for the six months ended June 30, 2018 as compared to non-GAAP net loss \$31,218,265 for the same period of 2017, an increase of \$33,176,032, or 106.3%. The increase in net income (non-GAAP) was primarily attributable to the profits from the JV Company and significantly decreased R&D expenses this period.

We make reference to certain non-GAAP financial measures, i.e., adjusted net income. Management believes that such adjusted financial results are useful for investors in evaluating our operating performance because they present a meaningful measure of corporate performance. See the non-GAAP reconciliation table below. Any non-GAAP measures should not be considered as a substitute for, and should only be read in conjunction with, measures of financial performance prepared in accordance with the GAAP.

The following table summarizes our non-GAAP net income for the six months ended June 30, 2018 and 2017:

|                                                  | Six Months Ended |                |
|--------------------------------------------------|------------------|----------------|
|                                                  | June 30,         |                |
|                                                  | 2018             | 2017           |
| GAAP net income (loss)                           | \$5,102,520      | \$(35,711,452) |
| Stock compensation expenses                      | 222,259          | 4,493,187      |
| Change in fair value of contingent consideration | (3,367,012)      | -              |
| Non-GAAP net income (loss)                       | \$1,957,767      | \$(31,218,265) |

## LIQUIDITY AND CAPITAL RESOURCES

### Cash Flow

For the first half of 2018, cash used in operating activities was \$165,499, as compared to cash used in operating activities of \$1,736,365 for the same period of last year. Our operating cash inflows include cash received primarily from sales of our EV parts and off-road vehicles. These cash inflows are offset largely by cash paid primarily to our suppliers for production materials and parts used in our manufacturing process, operation expenses, employee compensation, and interest expenses on our financings. The major operating activities that provided cash for first half of 2018 were an increase of accounts payable of \$41,319,755 net of assignment of notes receivable from unrelated parties to supplier to settle accounts payable of \$12,570,974, assignment of notes receivable from JV Company and related parties to supplier to settle accounts payable of \$35,176,703, settlement of accounts payable with notes payables of \$19,480,843, adjustment of construction in progress to reduce accounts payable of \$8,299,226, adjustment of advance to supplier to increase accounts payable of \$3,703,808 and cancellation of notes payables to increase accounts payable of \$10,994,880 and an increase of other payables and accrued liabilities of \$25,636,794. The major operating activity that used cash for first half of 2018 was an increase in receivables from the JV Company of \$39,263,079 net of settlement of due from JV Company and related parties with notes receivable of \$36,310,747 and due from JV Company converted to investment in JV Company of \$85,602,991, and an increase of accounts receivable of \$36,123,904 net of settlement of accounts receivables with notes receivable from unrelated parties of \$39,932,517.



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For the first half of 2018, cash used in investing activities was \$620,192, as compared to cash provided by investing activities of \$3,351,158 for the same period of last year. The major investing activities that used cash for first half of 2018 were \$3,694,275 used for the acquisition of Jinhua An Kao net of cash received.

For the first half of 2018, cash used in financing activities was \$5,804,126, as compared to cash provided by financing activities of \$2,658,760 for the same period of last year. The major financing activities that provided cash for the first half of 2018 were proceeds from notes payable of \$34,702,510. The major financing activities that used cash for first half of 2018 were \$40,349,566 of repayment of notes payable.

### **Working Capital**

We had a working capital deficit of \$8,644,088 at June 30, 2018 as Kandi Vehicle increased its capital contribution to the JV Company by converting its RMB 545 million (approximately \$83 million) of loans lent to the JV Company to the JV Company's registered capital, which reflected a decrease of \$62,351,990 from a working capital surplus of \$53,707,902 as of December 31, 2017.

We have historically financed our operations through short-term commercial bank loans from Chinese banks. The term of these loans is typically for one year, and upon the payment of all outstanding principal and interest in a particular loan, the banks have typically rolled over the loan for an additional one-year term, with adjustments made to the interest rate to reflect prevailing market rates. We believe this practice has been ongoing year after year and that short-term bank loans will be available with normal trade terms if needed.

### **Capital Requirements and Capital Provided**

Capital requirements and capital provided for the six months ended June 30, 2018 were as follows:

|                                                          | Six Months<br>Ended<br>June 30,<br>2018<br>(In Thousands) |
|----------------------------------------------------------|-----------------------------------------------------------|
| Capital requirements                                     |                                                           |
| Purchase of plant and equipment                          | \$ 122                                                    |
| Purchases of land use rights and other intangible assets | 108                                                       |
| Acquisition of Jinhua An Kao                             | 3,694                                                     |
| Purchase of construction in progress                     | 48                                                        |
| Repayments of short-term bank loans                      | 14,765                                                    |
| Repayments of long-term bank loans                       | 157                                                       |
| Repayments of notes payable                              | 40,350                                                    |

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|                                                                    |           |
|--------------------------------------------------------------------|-----------|
| Internal cash used in operations                                   | 165       |
| Total capital Requirements                                         | \$ 59,409 |
| Capital provided                                                   |           |
| Proceeds from short-term bank loan                                 | 14,765    |
| Proceeds from notes payable                                        | 34,703    |
| Decrease in cash                                                   | 6,620     |
| Long term investment                                               | 1,492     |
| Reimbursement of capitalize interests for construction in progress | 1,860     |
| Total capital provided                                             | \$ 59,440 |

The difference between capital provided and capital required is caused by the effect of exchange rate changes over the past three months.

**Contractual Obligations and Off-balance Sheet Arrangements***Contractual Obligations*

The following table summarizes our contractual obligations:

| Contractual obligations                    | Payments due by period |                         |                  |                   |                          |
|--------------------------------------------|------------------------|-------------------------|------------------|-------------------|--------------------------|
|                                            | <b>Total</b>           | <b>Less than 1 year</b> | <b>1-3 years</b> | <b>3-5 years</b>  | <b>More than 5 years</b> |
| R&D Obligations                            | \$9,064,745            | 9,064,745               | -                | -                 | -                        |
| Hainan Obligations                         | 16,316,541             | 16,316,541              | -                | -                 | -                        |
| Loans from Haikou Rural Credit Cooperative | \$30,064,737           | -                       | -                | 30,064,737        | -                        |
| <b>Total</b>                               | <b>\$55,446,023</b>    | <b>25,381,286</b>       | <b>-</b>         | <b>30,064,737</b> | <b>-</b>                 |

To build the Hainan facility, the Company signed contracts with Nanjing Shangtong Auto Technologies Co., Ltd. (“Nanjing Shangtong”) to purchase a production line and develop a new EV model. As of June 30, 2018, the total contractual amount with Nanjing Shangtong was RMB 912,000,000 or approximately \$137 million, of which RMB 744,000,000 or approximately \$112 million has been paid and RMB 168,000,000 or approximately \$25 million of remaining payments are outstanding as contractual obligations.

*Short-term and long-term Loans:*

For the discussion of short-term and long-term loans, please refer to Note 16 - Short-term and Long-term Loans under Notes to Condensed Consolidated Financial Statements.

*Notes payable:*

For the discussion of notes payable, please refer to Note 17 - Notes Payable under Notes to Condensed Consolidated Financial Statements.



*Guarantees and pledged collateral for third party bank loans*

For the discussion of guarantees and pledged collateral for third party bank loans, please refer to Note 23 –Commitments and Contingencies under Notes to Condensed Consolidated Financial Statements.

**Recent Development Activities:**

On April 8, 2018, the officials of the Department of Industry of the National Development and Reform Commission together with relevant personnel and experts formed a research group and made a special trip to the JV Company Rugao facility to conduct an inspection on the qualifications of Kandi Jiangsu for awarding production license. The group fully affirmed and highly praised the management and products at the facility, also made request for items need to be improved. For these items, National Development and Reform Commission issued the notification of “The National Development and Reform Commission (“NDRC”) General Office’s Notice of rectification about problems related to Jiangsu Guoxin and Kandi Jiangsu’s newly-built pure electric passenger vehicle project” (FGBCY[2018] No.547) on May 12. In accordance with the request of the notice, Kandi Jiangsu made a serious rectification, and submitted a rectification report to the Provincial and Municipal Development and Reform Commission on May 23 after the rectification is completed. On May 28, the Provincial Development and Reform Commission organized relevant departments and experts to Kandi Jiangsu for checking. On June 22, the Jiangsu Provincial Development and Reform Commission reported to the NDRC about the items above passed the rectification checking and request approval or authorization from the Jiangsu Development and Reform Commission according to Rule No.27 as soon as possible. Currently, the Company is waiting for the approval from the NDRC.

On May 23, 2018, we announced the Geely Global Hawk EV model SMA7000BEV20 (Model K22) and SMA7001BEV40 (Model K27) developed by the JV Company have been included in the Ministry of Industry and Information Technology of the People’s Republic of China’s (the “MIIT”) Directory of Recommended Models for Energy Saving and New Energy Vehicle Demonstration and Promotion (the “Fifth Annual Directory of New Energy Vehicles”) under the 2018 No. 24 public announcement. As a result, purchasers of these two approved 200-km EV models will be qualified to receive higher national and local subsidies.

On June 4, 2018, we announced that Kandi entered into a Membership Interests Transfer Agreement (the “Transfer Agreement”) with the two members (the “Transferors”) of Sportsman Country under which Kandi will acquire 100% of the ownership of Sportsman Country. The Transfer Agreement was signed on May 31, 2018. Sportsman Country is a Dallas based sales company primarily engaged in the wholesale of off-road vehicle products, with a small percentage of business in off-road vehicle parts wholesale and retail. Currently, Sportsman Country has a seasoned management team and a distribution force averaging over ten years of sales experience. With countrywide sales channels in the US, its off-road vehicle products are particularly popular to American consumers. According to the terms of the Transfer Agreement, Kandi will transfer \$10.0 million worth of restricted shares to acquire 100% membership interests in

Sportsman Country. Kandi is required to issue \$1.0 million worth of corresponding restricted shares within 30 days from the signing date of the Transfer Agreement, the remaining \$9.0 million worth of corresponding restricted shares will be released from escrow based on its pre-tax profit performance.

On June 7, 2018, we announced that the Geely brand pure electric vehicle (“EV”) models SMA7001BEV41 (Model EX3) and SMA7001BEV45 (Model K23) have been included in the Ministry of Industry and Information Technology of the People’s Republic of China’s (the “MIIT”) Directory of New Product (the “308th Directory”) and Recommended Models for Energy Saving and New Energy Vehicle Demonstration and Promotion (the “6th Annual Directory of New Energy Vehicles”) under the 2018 No. 30 public announcement. As a result, purchasers of these two EV models will be qualified to receive government subsidies.

On June 12, 2018, we announced that the JV Company though JiHeKang signed a Framework Sales Agreement with Sportsman Country on June 10th, 2018 for bringing its pure electric vehicles to the United States. According to the terms, the JV Company will ship pure electric vehicle prototypes to the United States before August 10th, 2018. The shipment will include Model EX3 and Model K22, which are designed for the American market in order to precede opportunity analysis and market assessment. Sportsman Country is responsible for all necessary application procedures for the sale of the JV Company’s pure electric vehicles that are required in the United States. Detailed purchase and procurement plans will be determined based on the progress of preparation work.

On July 2, 2018, we announced that the pure electric vehicle prototypes manufactured by the JV Company completed inspection and were shipped in a freight container on June 29, 2018. The shipment to America includes two Model EX3s and one Model K22, in which the settings of charging ports and software system language of the user interface were upgraded from the original models to satisfy the need of the US market.

On July 27, 2018, Chairman of the Company, Hu Xiaoming, met Mr. Jing Zhu, Chairman of Hainan Provincial Federation of Industry and Commerce and Chairman of the Haima Group in Haikou. The two parties have conducted an in-depth communication on how to seize the opportunity of the comprehensive deepening of reform in Hainan and cooperation to each other in the field of pure electric vehicle development. The two parties are willing to cooperate in this field and start a feasibility study on how to cooperate.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

#### **Exchange Rate Risk**

While our reporting currency is the U.S. dollar, to date the majority of our revenues and costs are denominated in RMB and a significant portion of our assets and liabilities are denominated in RMB. As a result, we are exposed to foreign exchange risk because our revenues and results of operations may be affected by fluctuations in the exchange rate between the U.S. dollar and the RMB. If the RMB depreciates against the U.S. dollar, the value of our RMB revenues and assets as expressed in our U.S. dollar financial statements will decline. Since 2005, China reformed its



exchange rate regime and the RMB is no longer pegged to the U.S. dollar. In 2010, the People's Bank of China decided to move to further reform the RMB exchange rate regime to enhance the flexibility of the RMB exchange rate. Starting August 11, 2015, the RMB changed its trend of appreciation and began to depreciate as compared to the U.S. dollar. As of June 30, 2018, the RMB exchange rate vs. the U.S. dollar was 6.61905, representing about 1.7% depreciation compared to the exchange rate of 6.5067 vs. the U.S. dollar as of December 31, 2017. In the long term, the RMB may appreciate or depreciate more significantly in value against the U.S. dollar or other foreign currencies, depending on the market supply and demand with reference to a basket of currencies.

While the Chinese RMB is freely convertible under the current account, it remains strictly regulated in the capital account. Chinese authorities have expressed their willingness to allow the RMB to be fully convertible in the near future.

To date, we have not entered into any hedging transactions in an effort to reduce our exposure to foreign currency exchange risk. While we may decide to enter into hedging transactions in the future, the effectiveness of these hedges may be limited and we may not be able to successfully hedge our exposure. Accordingly, we may incur economic losses in the future due to foreign exchange rate fluctuations, which could have a negative impact on our financial condition and results of operations.

### **Interest Rate Risk**

We had cash, cash equivalents and restricted cash totaling \$9.5 million as of June 30, 2018. Cash and cash equivalents are held for working capital purposes. We do not enter into investments for trading or speculative purposes. As of June 30, 2018, we had \$32.5 million of short-term bank loans and \$30.1 million of long-term loans outstanding, which are fixed rate instruments. Our exposure to interest rate risk primarily relates to the interest income generated from cash held in bank deposits and notes receivable, and interest expenses generated from short-term bank loans. We believe that we do not have any material exposure to changes in fair value as a result of changes in interest rates due to the short term nature of our cash equivalents. We have not been exposed nor do we anticipate being exposed to material risks due to changes in interest rates.

### **Economic and Political Risks**

Our operations in China are subject to special considerations and significant risks not typically associated with companies in North America and Western Europe. These include risks associated with, among others, the political, economic and legal environment in China and foreign currency exchange. Our performance may be adversely affected by changes in the political and social conditions in China, and by changes in governmental policies with respect to laws and regulations, anti-inflationary measures, currency conversion, remittances abroad, and rates and methods of taxation, among other things.

### **Item 4. Controls and Procedures.**

#### **Evaluation of Disclosure Controls and Procedures**

We have evaluated, under the supervision of our Chief Executive Officer (“CEO”) and our Chief Financial Officer (“CFO”), the effectiveness of disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”) as of June 30, 2018. Based on this evaluation, our CEO and CFO concluded that as of the end of the period covered by this report, our disclosure controls and procedures were effective.

Disclosure controls and procedures are controls and procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act (a) is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and (b) is accumulated and communicated to management, including our CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure. Our management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives as described above.

#### **Changes in Internal Control over Financial Reporting**

There was no change to our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting, except for the following:

We continued our efforts that were initiated in the beginning of 2017 to fully implement the plan for remediation of the material weaknesses in internal control over financial reporting as outlined in the Form 10-K filed with the SEC on March 16, 2017 and improved our internal control over financial reporting.

## **PART II – OTHER INFORMATION**

### **Item 1. Legal Proceedings.**

From time to time, the Company is involved in legal matters arising in the ordinary course of business. Except as set forth in Note 23 - COMMITMENTS AND CONTINGENCIES under Notes to Condensed Consolidated Financial Statements, our management is currently not aware of any legal matters or pending litigation that would have a significant effect on the Company's results of operation of financial statements. Furthermore, the Company is not aware of any other legal matters in which any director, officer, or any owner of record or beneficial owner of more than five percent of any class of voting securities of the Company, or any affiliate of any such director, officer, affiliate of the Company, or security holder, is a party adverse to the Company or has a material adverse interest to the Company. For the detailed discussion of our legal proceedings, please refer to Note 23 - COMMITMENTS AND CONTINGENCIES under Notes to Condensed Consolidated Financial Statements, which is incorporated by reference herein,

### **Item 1A. Risk Factors.**

*Changes and further delays in subsidy payments may have negative impacts on our operations.*

The change in subsidy payment methods in 2017 from paid in advance to paid post-sale and any further delay in releasing subsidy payments for the EVs manufactured and sold in the prior years might cause delays in collection of accounts receivable from our business partners, which will temporarily increase the pressure on our working capital for continuing operations. The unavailability, reduction or elimination of government and economic incentives could have a material adverse effect on our business, financial condition, operating results and prospects.

**Item 6. Exhibits**

| Exhibit Number | Description                                                                                                                                                                      |
|----------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 31.1           | <u>Certification of Principal Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934</u>                                               |
| 31.2           | <u>Certification of Principal Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934</u>                                               |
| 32.1           | <u>Certification of Principal Executive Officer and Principal Financial Officer pursuant to 18 U.S.C. § 1350, as Adopted Pursuant to § 906 of the Sarbanes-Oxley Act of 2002</u> |
| 101.INS        | XBRL Instance Document.                                                                                                                                                          |
| 101.SCH        | XBRL Taxonomy Extension Schema Document.                                                                                                                                         |
| 101.CAL        | XBRL Taxonomy Extension Calculation Linkbase Document.                                                                                                                           |
| 101.LAB        | XBRL Taxonomy Extension Label Linkbase Document.                                                                                                                                 |
| 101.PRE        | XBRL Taxonomy Extension Presentation Linkbase Document.                                                                                                                          |
| 101.DEF        | XBRL Taxonomy Definitions Linkbase Document.                                                                                                                                     |

**SIGNATURES**

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

Date: August 9, 2018 By: /s/ Hu Xiaoming  
Hu Xiaoming  
President and Chief Executive Officer  
(Principal Executive Officer)

Date: August 9, 2018 By: /s/ Mei Bing  
Mei Bing  
Chief Financial Officer  
(Principal Financial Officer and  
Principal Accounting Officer)