

China West Coal Energy Inc  
Form 10QSB  
May 21, 2007

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

**FORM 10-QSB**

(Mark One)

Quarterly Report Pursuant To Section 13 Or 15(d) Of The Securities Exchange Act Of 1934

For the quarterly period ended: **March 31, 2007**

Or

Transition Report Pursuant To Section 13 Or 15(d) Of The Securities Exchange Act Of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: **000-51753**

**CHINA WEST COAL ENERGY INC.**

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction of incorporation of  
origination)

75-2882833

(I.R.S. Employer Identification Number)

**Room 2205, Suite A, Zhengxin Building, No. 5, Gaoxin  
1st Road, Gao Xin District, Xi'an, Shaanxi Province,  
People's Republic of China**

(Address of principal executive offices)

N/A

(Zip code)

(029) 8209-1099

(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

The registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes  No

**APPLICABLE ONLY TO CORPORATE ISSUERS:**

Indicate the number of shares outstanding of each issuer's classes of common stock, as of the latest practicable date:  
28,227,250 issued and outstanding as of May 18, 2007.

Transitional Small Business Disclosure Form (Check one): Yes  No



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**FOR QUARTER ENDED MARCH 31, 2007**

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CAUTION REGARDING FORWARD-LOOKING INFORMATION

All statements contained in this Quarterly Report on Form 10-QSB (“Form 10-QSB”) for China West Coal Energy Inc., other than statements of historical facts, that address future activities, events or developments are forward-looking statements, including, but not limited to, statements containing the words “believe,” “anticipate,” “expect” and words of similar import. These statements are based on certain assumptions and analyses made by us in light of our experience and our assessment of historical trends, current conditions and expected future developments as well as other factors we believe are appropriate under the circumstances. However, whether actual results will conform to the expectations and predictions of management is subject to a number of risks and uncertainties that may cause actual results to differ materially.

Such risks include, among others, the following: international, national and local general economic and market conditions; our ability to sustain, manage or forecast our growth; raw material costs and availability; new product development and introduction; existing government regulations and changes in, or the failure to comply with, government regulations; adverse publicity; competition; the loss of significant customers or suppliers; fluctuations and difficulty in forecasting operating results; changes in business strategy or development plans; business disruptions; the ability to attract and retain qualified personnel; the ability to protect technology; and other factors referenced in this and previous filings.

Consequently, all of the forward-looking statements made in this Form 10-QSB are qualified by these cautionary statements and there can be no assurance that the actual results anticipated by management will be realized or, even if substantially realized, that they will have the expected consequences to or effects on our business operations. As used in this Form 10-QSB, unless the context requires otherwise, “we” or “us” or “Registrant” or the “Company” means China West Coal Energy Inc. and its subsidiaries.

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**PART I – FINANCIAL INFORMATION**

**Item 1. Financial Statements**

CHINA WEST COAL ENERGY, INC. AND SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006

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CHINA WEST COAL ENERGY, INC. AND SUBSIDIARIES

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**CHINA WEST COAL ENERGY, INC AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
**AS OF MARCH 31, 2007 AND DECEMBER 31, 2006**

	March 31, 2007 (Unaudited)	December 31, 2006 (Audited)
<b>ASSETS</b>		
<b>Current assets</b>		
Cash on hand and at bank	\$ 2,579,468	\$ 4,450,557
Amounts due from directors (Note 16)	189,076	206,186
Deposits and prepayments (Note 6)	4,259,531	1,830,769
Other receivables	3,679	-
Short term loan to related party (Notes 7,16)	415,186	411,970
Discontinued operations (Note 12)	2,802,879	3,485,462
<b>Total current assets</b>	<b>10,249,819</b>	<b>10,384,944</b>
Property, plant and equipment, net (Note 8)	817,842	623,934
Intangible assets , net (Note 9)	1,545,240	1,533,349
<b>Total assets</b>	<b>\$ 12,612,901</b>	<b>\$ 12,542,227</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Accrued expenses and other payables (Note 10)	\$ 315,029	\$ 372,125
Amount due to a director (Note 16)	102,714	20,702
Advance from customers	586,356	-
Discontinued operations (Note 12)	1,714,010	2,366,631
<b>Total current liabilities</b>	<b>2,718,109</b>	<b>2,759,458</b>
<b>Minority Interest</b>	<b>91,042</b>	<b>94,748</b>
Commitments and Contingencies (Note 17)		
<b>Shareholders' Equity</b>		
Preferred stock, \$0.001 par value, 50,000,000 shares authorized, nil issued and outstanding	-	-
Common stock, \$0.001 par value, 200,000,000 shares authorized, 28,227,250 issued and outstanding	28,227	28,227
Additional paid-in capital	9,209,629	9,209,629
Accumulated deficits	(292,214)	(330,456)
Statutory reserves (Note 11)	348,309	348,309
Accumulated other comprehensive income	509,799	432,312
<b>Total shareholders' equity</b>	<b>9,803,750</b>	<b>9,688,021</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 12,612,901</b>	<b>\$ 12,542,227</b>

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

**CHINA WEST COAL ENERGY, INC AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME AND OTHER COMPREHENSIVE INCOME**  
**FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**

	For the three months ended March 31,	
	2007 (Unaudited)	2006 (Unaudited)
Revenue	\$ -	\$ -
Costs of good sold	-	-
<b>Gross profit</b>	-	-
Selling expenses	1,286	-
General and administrative expenses	51,662	-
Income from discontinued operations (Note 12)	121,843	496,117
	68,895	496,117
Other income (expenses)		
Interest income	6,310	2,364
Sundry expenses	(41,319)	(17,225)
Total other income (expenses)	(35,009)	(14,861)
Income before provision for income taxes and minority interest	33,886	481,256
Provision for income taxes	-	-
Net income before minority interest	33,886	481,256
Less minority interest	(4,356)	-
<b>Net income</b>	38,242	481,256
<b>Other comprehensive income</b>		
Foreign currency translation adjustment	77,487	13,118
<b>Comprehensive income</b>	\$ 115,729	\$ 494,374
<b>Weight average number of shares</b>		
- Basic and diluted	28,227,250	28,227,250
<b>Earnings per share</b>		
- Basic and diluted	\$ 0.004	\$ 0.018

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





**CHINA WEST COAL ENERGY, INC AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**  
**FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**

	Number of shares	Common stock	Additional Paid-in capital	Statutory capital reserves	Statutory welfare reserves	Retained earnings	Accumulated other comprehensive income	Totals
<b>BALANCE,</b> January 1, 2006 (audited)	39,000,000	\$ 4,712,137	\$ 84,759	\$ 106,247	\$ 53,124	\$ 447,982	\$ 125,594	\$ 5,529,843
Net income	-	-	-	-	-	481,256	-	481,256
Capital injection (at par \$0.1208)	31,000,000	3,868,223	-	-	-	-	-	3,868,223
Foreign currency translation gain	-	-	-	-	-	-	13,118	13,118
<b>BALANCE,</b> March 31, 2006 (unaudited)	70,000,000	\$ 8,580,360	\$ 84,759	\$ 106,247	\$ 53,124	\$ 929,238	\$ 138,712	\$ 9,892,440
Capital injection of subsidiaries	-	-	572,737	-	-	-	-	572,737
Exchange to share prior recapitalization	(70,000,000)	(8,580,360)	8,580,360	-	-	-	-	-
Capital acquired on capitalization (at par \$0.001)	2,712,000	2,712	(2,712)	-	-	-	-	-
Cancellation of share (at par \$0.001)	(1,154,350)	(1,154)	1,154	-	-	-	-	-
Recapitalization (at par \$0.001)	26,669,600	26,669	(26,669)	-	-	-	-	-
Net loss	-	-	-	-	-	(1,070,756)	-	(1,070,756)
Transfer to reserve	-	-	-	125,959	62,979	(188,938)	-	-
Foreign currency translation gain	-	-	-	-	-	-	293,600	293,600
<b>BALANCE,</b> December 31, 2006 (audited)	28,227,250	\$ 28,227	\$ 9,209,629	\$ 232,206	\$ 116,103	\$ (330,456)	\$ 432,312	\$ 9,688,021
Net income	-	-	-	-	-	38,242	-	38,242
Foreign currency translation gain	-	-	-	-	-	-	77,487	77,487

BALANCE, March 31, 2007 (unaudited)	28,227,250	\$	28,227	\$	9,209,629	\$	232,206	\$	116,103	\$	(292,214)	\$	509,799	\$	9,803,750
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The accompanying notes are an integral part of these consolidated financial statements.

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**CHINA WEST COAL ENERGY, INC AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**

	For the three months ended March 31,	
	2007 (Unaudited)	2006 (Unaudited)
<b>Cash flows from operating activities:</b>		
Net income	\$ 38,242	\$ 481,256
Adjustments to reconcile net income to cash provided by (used in) operating activities:		
Minority Interest	(4,356)	-
Net income from discontinued operations	(121,843)	(496,117)
Depreciation and amortization	35,338	72,353
(Increase) decrease in assets:		
Other receivables	(2,049)	-
Deposit and prepayment	(2,528,393)	-
Increase (decrease) in liabilities:		
Advance from customers	574,581	-
Accrued expenses and other payable	(57,741)	(72,327)
Net cash provided by discontinued operations	130,005	511,154
Net cash provided by (used in) operating activities	(1,936,216)	496,319
<b>Cash flows from investing activities:</b>		
Amount due from a director	18,341	3,079
Purchase of property, plant and equipment	(29,623)	-
Net cash provided by (used in) investing activities	(11,282)	3,079
<b>Cash flows from financing activities:</b>		
Amount due to a director	80,195	-
Proceeds from injection additional paid in capital from subsidiary	-	3,861,360
Net cash provided by financing activities	80,195	3,861,360
Effect of foreign currency translation	(3,786)	(5,417)
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>(1,871,089)</b>	<b>4,355,341</b>
Cash and cash equivalents, beginning of year	4,450,557	691,268
Cash and cash equivalents, end of year	\$ 2,579,468	\$ 5,046,609

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

**CHINA WEST COAL ENERGY INC. (FORMERLY ENDO NETWORKS, INC.)  
AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**

1. CORPORATION REORGANIZATION AND BUSINESS ACTIVITIES

China West Coal Energy Inc. (formerly Endo Networks, Inc.) (the "Company") was originally incorporated in Texas as "Discount Mortgage Services, Inc." on July 11, 2000 and in September 2001, the Company purchased Endo Networks, Inc., a corporation incorporated in Ontario, Canada on January 11, 2001 ("Endo Canada"). In November 2001, the Company changed its name to Endo Networks, Inc. and was redomiciled to the State of Nevada in December 2002. Prior to the Share Exchange transaction described below, the Company conducted through, and all of the Company's assets were contained within, Endo Canada, in which conceptual and software development was ongoing for approximately two years by the Company founders, through ongoing contract relationships with software development companies.

The Company has incurred losses and has had substantial difficulty in maintaining necessary cash flows for proper operation for years. The Company also required additional investment in infrastructure to sustain and develop its business. The need could not be met by its current cash flows. In view of the foregoing lack of growth and the limited platform for its future growth, the Company's Board determined that it would be in the stockholders' best interests to sell its investment in Endo Canada to Mr. Peter B. Day, the Company's President, CEO and director. The Company's Board believed that Mr. Day's knowledge of their operations would lead to an efficient and expeditious sale process. An Asset and Share Purchase Agreement (the "Purchase Agreement") by and between the Company and Mr. Day was approved by the Board and executed on June 26, 2006. The Company thus discontinued its operations as a result of this sale with effect from September 30, 2006.

On October 18, 2006, the Company entered into a definitive Share Exchange Agreement with Hangson Limited ("Hangson"), whereby the Company acquired all of the outstanding common stock of Hangson in exchange for newly issued shares of the Company's common stock to the Hangson shareholders (the "Share Exchange"). On October 20, 2006 (the "Closing Date"), Hangson became a wholly owned subsidiary and Hangson's shareholders became owners of the majority of the voting stock. The acquisition of Hangson by the Company was accounted for as a reverse merger and a recapitalization because on a post-merger basis, the former shareholders of Hangson held a majority of the Company's outstanding common stock on a voting and diluted basis. As a result, Hangson is deemed to be the acquirer for accounting purposes. From and after the Closing Date of the Share Exchange, the Registrant's primary operations will now consist of the operations of Hangson.

Additionally, on August 18, 2006, Hangson entered into various agreements with Shaanxi Suo'ang Biological Science Technology Co., Ltd. ("Shaanxi Suoang"). Through these contractual arrangements, Hangson has the ability to substantially influence Shaanxi Suoang's daily operations and financial affairs, appoint its senior executives and approve all matters requiring shareholder approval. As a result of these contractual arrangements, which obligates Hangson to absorb a majority of the risk of loss from Shaanxi Suoang activities, enables Hangson to control Shaanxi Suoang, and enables Hangson to receive a majority of Shaanxi Suoang's expected residual returns. Hangson is considered the primary beneficiary of Shaanxi Suoang and as a variable interest entity ("VIE") under FASB Interpretation No. 46R ("FIN 46R"), "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51". Accordingly, the Company consolidates Shaanxi Suoang's results, assets and liabilities in its financial statements. The Company's consolidated assets do not include any collateral for Shaanxi Suoang's obligations. The creditors of Shannxi Suoang do not have recourse to the general credit of the Company.

1. CORPORATION REORGANIZATION AND BUSINESS ACTIVITIES (CONT'D)

Hangson was incorporated under the laws of the British Virgin Islands on June 2, 2006. Hangson does not conduct any substantive operations of its own and conducts its primary business operations through its variable interest entity ("VIE"), Shaanxi Suoang. Shaanxi Suoang is engaged in the research, development, production, marketing and sales of coal-polymer ("COPO") resin products including but not limited to, degradable mulch used for the conservation of moisture and warmth of soil and protection of the roots of plants, and materials used for plastic injection molding, electric wire covering, and garbage bags. Shaanxi Suoang is also engaged in the research, development, production and sale of coal-water mixture ("CMW"), which is a potential fuel substitute for coal, oil or gas. Since December 2006, Shaanxi Suoang ceased its operations in COPO products manufacturing and was planning to fully enter the business of manufacturing and selling CWM through its subsidiary Shaanxi Suo'ang New Energy Enterprise Company Ltd. ("New Energy") in which Shaanxi Suoang owns an 80% equity interest. From January 2007, Shaanxi Suoang ceased its original operation in COPO products business and now acts as a holding company providing administrative and marketing support to New Energy.

On October 18, 2006, the Company executed a Share Exchange Agreement (the "Exchange Agreement") by and between Hangson, and the stockholders of 100% of Hangson's common stock (the "Hangson Stockholders"), on the one hand, and the Company and a majority of the Company's stockholders, on the other hand. The closing of this transaction (the "Closing") occurred on October 20, 2006 (the "Closing Date").

The Company effected a 1 for 5 reverse split of its common stock, which is effective as of October 17, 2006. The Company's Board of Directors approved the Reverse Split in June 2006 and a majority of its stockholders approved it at the annual shareholder meeting on September 5, 2006. The Company had a total of 2,712,000 shares of common stock outstanding after the reverse split.

Under the Exchange Agreement, on the Closing Date, the Company issued a total of 26,000,000 shares of the Company's Common Stock (the "Shares") to Hangson Stockholders and to Viking Partners, Inc. ("Viking"), a consultant in this transaction, in exchange for 100% of the common stock of Hangson. Additionally, immediately prior to the Closing, Peter B. Day, the Company's former President, CEO and sole director voluntarily cancelled 715,500 (post 1-for-5 reverse split) shares of the 915,500 (post 1-for-5 reverse split) shares of the Company's common stock that he owns; and three of the Company's other shareholders also voluntarily cancelled a total of 438,850 (post 1-for-5 reverse split) shares of the Company's common stock that they own. Also pursuant to the Exchange Agreement, and as approved by a majority of the Company's shareholders, the Company split its common stock on a 1-for-5 reverse basis (the "Reverse Split") prior to the Closing Date. Further, prior to the Closing, the Company issued an additional 669,600 shares after the Reverse Split pursuant to certain anti-dilution provisions contained in agreements the Company had with two of the Company's consultants. After the share cancellations, the Reverse Split and the consultant anti-dilution share issuances, the Company had a total of approximately 2,227,250 shares of common stock outstanding. After the Closing, the Company had 28,227,250 shares of common stock outstanding, with the Hangson's Stockholders owning approximately 85% of the Company's common stock, and with the balance of the Company's common stock held by those who held the Company's shares prior to the Share Exchange. In addition, at the Closing, Hangson paid the Company's creditors a total of US\$500,000 for consulting services rendered, in order to satisfy certain obligations as set forth in the Exchange Agreement.

1. CORPORATION REORGANIZATION AND BUSINESS ACTIVITIES (CONT'D)

On June 19, 2005, Shaanxi Suo'ang entered into an agreement to establish a subsidiary named Shaanxi SuoKe New Energy Enterprise Company Limited ("SuoKe") together with a third party company named PengYuan Enterprise Company Ltd. ("PengYuan") and Mr. Peng Zhou in which the Company invested \$343,750 holding a 55% interest in SuoKe. The purpose for establishment of SuoKe was to carry out the operation of CWM. However, since the cooperation with PengYuan did not proceed as expected, the Company disposed of its investment in SuoKe and transferred its 55% interest in it to Mr. Peng Zhou. Based on an agreement signed between Peng Zhou and Shaanxi Suo'ang, the 55% investment in SuoKe was transferred to Mr. Peng Zhou at the cost in the amount of \$343,750.

On May 8, 2006, Shaanxi Suo'ang entered into an agreement to establish a subsidiary named Shaanxi Suo'ang New Energy Enterprise Company Limited ("Suo'ang New Energy") together with Mr. Peng Zhou, in which Shaanxi Suo'ang has injected a capital of \$496,000 representing an 80% equity interest in Suo'ang New Energy and Mr. Peng Zhou has injected \$124,100 and representing an 20% equity interest in Suo'ang New energy. Suo'ang New Energy was formed for the purpose of engaging in the research, development, production and sale of "coal water mixture", a fuel to substitute for coal, oil or gas. As of December 31, 2006, the plant was under construction and the Company expects to commence operation around July 2007.

2. GOING CONCERN AND MANAGEMENT'S PLANS

The accompanying financial statements have been prepared based on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. In January 2007, the Company ceased its COPO resin operation and is now principally engaged in research, development, production, marketing and sales of "coal-water mixture" business. The new business has not commenced operations and the Company may need additional financing to meet cash requirements for start up and to ensure continuity as a going concern.

The accompanying financial statements do not include any adjustments relating to the recoverability and classification of recorded amounts of assets or the amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. Management believes the Company's ability to continue as a going concern is dependent upon its ability to achieve and maintain profitable operations for the new business in 2007. The Company has already entered into sales contracts in respect of the "coal-water mixture" business which the management believes will generate sufficient cash flow to meet its obligations on a timely basis in the foreseeable future.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of presentation and consolidation

The accompanying consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America.

The consolidated financial statements include the financial statements of the Company, Hangson and its variable interest entities, Shaanxi Suo'ang and its controlled subsidiary, Suo'ang New Energy. All significant inter-company transactions and balances among the Company, Hangson and its variable interest entities are eliminated upon consolidation.

By the end of the year, Shaanxi Suo'ang's main operation was discontinued and the assets were classified as assets held for sale and discontinued operation.





3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

(a) Basis of presentation and consolidation (Cont'd)

On September 15, 2005, the Company established a subsidiary named Shaanxi Suoke New Energy Industry Company Limited ("Shaanxi Suoke") in which the Company injected a capital of \$335,500 representing 55% equity interest in Shaanxi Suoke. Shaanxi Suoke was formed for the purpose of engaging in the research, development, production and sale of "coal water mixture", a fuel to substitute for coal, oil or gas.

However, since its establishment, Shaanxi Suoke has never commenced any operations. Nor has the Company gained any control of the board of Shaanxi Suoke. In addition, by a resolution on May 15, 2006, the Company sold the 55% equity interest of Shaanxi Suoke to one of the shareholders of Shaanxi Suoke, Mr. Peng Zhou, who established another subsidiary named Suo'ang New Energy together with Shaanxi Suo'ang, at cost with a cash consideration of \$335,500.

Statement of Financial Accounting Standards ("SFAS") No. 94 "Consolidation of All Majority-Owned Subsidiary" requires that all majority-owned subsidiaries shall be consolidated except those where control is likely to be temporary or it does not rest with the majority owner. Accordingly, these financial statements do not consolidate Shaanxi Suoke for the three months ended March 31, 2007 and 2006, because of the lack of ability to control Shaanxi Suoke. Results of Shaanxi Suoke since its establishment to March 31, 2007 and 2006 were immaterial.

(b) Use of estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Because of the use of estimates inherent in the financial reporting process, actual results could differ from those estimates. Significant estimates include estimates of accruals and determination of fair values for assets disposed.

(c) Accounts and other receivables

Accounts and other receivables are recognized and carried at original invoiced amount less an allowance for any uncollectible accounts.

The Company uses the aging method to estimate the valuation allowance for anticipated uncollectible receivable balances. Under the aging method, bad debts determined by management are based on historical experience as well as the current economic climate and are applied to customers' balances categorized by the number of months the underlying invoices have remained outstanding. The valuation allowance balance is adjusted to the amount computed as a result of the aging method. When facts subsequently become available to indicate that an adjustment to the allowance should be made, this is recorded as a change in estimate in the current year. As of March 31, 2007, accounts and other receivables were net of allowances of \$3,801 and Nil, respectively. As of December 31, 2006, accounts and other receivables were net of allowances of \$3,772 and Nil, respectively.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

(d) Inventories

Inventories from the discontinued operations are stated at the lower of cost, as determined on a weighted average basis, or net realizable value. Costs of inventories include purchase and related costs incurred in bringing the products to their present location and condition.

(e) Property, plant and equipment

Property, plant and equipment are recorded at cost less accumulated depreciation and amortization. Gains or losses on disposals are reflected as gain or loss in the year of disposal. The cost of improvements that extend the life of plant, property and equipment are capitalized. These capitalized costs may include structural improvements, equipment and fixtures. All ordinary repair and maintenance costs are expensed as incurred.

Depreciation or amortization for financial reporting purposes is provided using the straight-line method over the estimated useful lives of the assets as follows:

Leasehold properties	the shorter of the useful life or the lease term
Leasehold improvements	the shorter of the useful life or the lease term
Plant and machinery	10 years
Office equipment	5 years
Motor vehicles	3 years

(f) Construction in progress

Construction in progress includes direct costs of factory buildings. Construction in progress is not depreciated until such time as the assets are completed and put into operational use.

(g) Lease prepayment

Lease prepayment represents the prepaid land use right. Lease prepayment is amortized over the term of 50 years.

(h) Impairment

The Company accounts for impairment of long-lived assets including property, plant and equipment, and amortizable intangible assets in accordance with SFAS No.144, *Accounting for Impairment of Long-Lived Assets to be Disposed Of*, which requires an impairment loss to be recognized when the carrying amount of a long-lived asset or asset group exceeds its fair value and is not recoverable (when carrying amount exceeds the gross, undiscounted cash flows from use and disposition). The impairment loss is measured as the excess of the carrying amount over the asset's (or asset group's) fair value.

(i) Comprehensive income

SFAS No. 130, *Reporting Comprehensive Income*, requires disclosure of all components of comprehensive income and loss on an annual and interim basis. Comprehensive income and loss is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. The Company had accumulated other comprehensive income of \$509,799 and \$138,712 for the periods ended March 31, 2007 and 2006 respectively. The other comprehensive income arose from the changes in foreign currency exchange rate.



3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

(j) Fair value of financial instruments

The Company believes that the carrying values of its cash and cash equivalents, other receivables and other payables as of March 31, 2007 approximate to their respective fair values due to the short-term nature of those instruments.

(k) Revenue recognition

Revenues of the Company include COPO resin product sales which have been classified as discontinued operations. Sales are recognized when the following four revenue criteria are met: persuasive evidence of an arrangement exists, delivery has occurred, the selling price is fixed or determinable, and collectibility is reasonably assured. Revenues are presented net of value added tax (VAT). No return allowance is made as products are normally not returnable upon acceptance by the customers.

(l) Advertising expenses

Advertising expenses are expensed to operations in the period incurred.

(m) Research and development costs

Research and development costs are expensed to operations as incurred.

(n) Stock based compensation

The Company has adopted Statement of Financial Accounting Standards No. 123R "Accounting for Stock-Based Compensation" ("SFAS 123R"), which defines a fair-value-based method of accounting for stock based employee compensation and transactions in which an entity issues its equity instruments to acquire goods and services from non-employees. Stock compensation for stock granted to non-employees has been determined in accordance with SFAS 123R and the Emerging Issues Task Force consensus in Issue No. 96-18, "Accounting for Equity Instruments that are issued to Other than Employees for Acquiring, or in Conjunction with Selling Goods or Services" ("EITF 96-18"), as the fair value of the consideration received or the fair value of equity instruments issued, whichever is more reliably measured.

(o) Earnings per share

Basic earnings per share ("EPS") is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period.

(p) Income taxes

The Company accounts for income taxes in accordance with SFAS No. 109, *Accounting for Income Taxes*. SFAS No. 109 requires an asset and liability approach for financial accounting and reporting for income taxes and allows recognition and measurement of deferred tax assets based upon the likelihood of realization of 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. 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 deductibility is uncertain.



3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

(q) Foreign currency translation

The reporting currency of the Company is the United States Dollars. All assets and liabilities accounts have been translated into United States Dollars using the current exchange rate at the balance sheet date. Capital stock is recorded at historical rates. Revenue and expenses are translated using the average exchange rate in the year. The resulting gain and loss has been reported as other comprehensive income (loss) within the shareholder's equity.

(r) Related parties

Parties are considered to be related to the Company if the parties, directly or indirectly, through one or more intermediaries, control, are controlled by, or are under common control with the Company. Related parties also include principal owners of the Company, its management, members of the immediate families of principal owners of the Company and its management and other parties with which the Company may deal if one party controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests. A party which can significantly influence the management or operating policies of the transacting parties or if it has an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests is also a related party.

(s) Recently issued accounting pronouncements

In February 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments" ("SFAS 155"). This Statement amends FASB Statements No. 133, Accounting for Derivative Instruments and Hedging Activities, and No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. This Statement resolves issues addressed in Statement 133 Implementation Issue No. D1, "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets." SFAS No. 155 permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, clarifies which interest-only strips and principal-only strips are not subject to the requirements of Statement 133, and establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation. It also clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives and amends Statement 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. This Statement is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The Company has not yet determined the impact of the adoption of SFAS No. 155 on its financial statements, if any.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

(s) Recently issued accounting pronouncements (Cont'd)

In March 2006, the FASB issued SFAS No. 156, "Accounting for Servicing of Financial Assets" ("SFAS 156"). This Statement amends FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, with respect to the accounting for separately recognized servicing assets and servicing liabilities. This Statement requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in indicated situations; requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable; permits an entity to choose relevant subsequent measurement methods for each class of separately recognized servicing assets and servicing liabilities; at its initial adoption, permits a one-time reclassification of available-for-sale securities to trading securities by entities with recognized servicing rights, without calling into question the treatment of other available-for-sale securities under Statement 115, provided that the available-for-sale securities are identified in some manner as offsetting the entity's exposure to changes in fair value of servicing assets or servicing liabilities that a servicer elects to subsequently measure at fair value; and requires separate presentation of servicing assets and servicing liabilities subsequently measured at fair value in the statement of financial position and additional disclosures for all separately recognized servicing assets and servicing liabilities. The Company has determined that the adoption of SFAS No. 156 did not have a material impact on its Consolidated Financial Statements.

The FASB issued FASB Interpretation No. ("FIN") 48, "Accounting for Uncertainty in Income Taxes," in June 2006. This interpretation establishes new standards for the financial statement recognition, measurement and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. The new rules will be effective for the Company in the first quarter of 2008. The Company does not anticipate that the adoption of this standard will have a material effect on its financial statements.

In September 2006, the SEC issued Staff Accounting Bulletin ("SAB") 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements," which eliminated the diversity in practice surrounding the quantification and evaluation of financial statement errors. The guidance outlined in SAB 108 is effective for the Company and is consistent with its historical practices for assessing such matters when circumstances have required such an evaluation. Accordingly, the Company does not believe that the adoption of SAB 108 will have any impact on its financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements, ("SFAS 157"), to define fair value, establish a framework for measuring fair value in accordance with generally accepted accounting principles and expand disclosures about fair value measurements. SFAS 157 requires quantitative disclosures using a tabular format in all periods (interim and annual) and qualitative disclosures about the valuation techniques used to measure fair value in all annual periods. The provisions of this Statement shall be effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company will be required to adopt the provisions of this statement as of January 1, 2008. The Company is currently evaluating the impact of adopting SFAS 157.

In September 2006, the FASB issued Statement No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - An amendment of FASB Statements No. 87, 88, 106, and 132(R)" ("SFAS 158"). This Statement enhances disclosure regarding the funded status of an employer's defined benefit postretirement plan by (a) requiring companies to include the funding status in comprehensive income, (b) recognize transactions and events that affect the funded status in the financial statements in the year in which they occur, and (c) at a measurement date of the employer's fiscal year-end. Statement No. 158 effective for fiscal years ending after December 15, 2008, and is not expected to apply to the Company.

In February 2007, FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115 (“SFAS 159”). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair values. SFAS 159 is effective for fiscal years after November 15, 2007. The Company is currently evaluating the impact of adopting SFAS 159 on its financial statements.

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4.

CONCENTRATION OF CREDIT RISK

- (a) Financial instruments which potentially expose the Company to concentrations of credit risk, consist of cash and cash equivalents and accounts receivable arising from discontinued business. The Company performs ongoing evaluations of their cash position and credit evaluations to ensure collections and minimize losses.
- (b) As of March 31, 2007 and December 31, 2006, the Company's bank deposits were all placed with banks in the PRC where there is currently no rule or regulation in place for obligatory insurance of bank accounts.
- (c) For the periods ended March 31, 2007 and 2006, all of the Company's sales arose in the PRC and were generated by the discontinued operation. All accounts receivable as of March 31, 2007 and December 31, 2006 also arose in the PRC generated from the discontinued operation
- (d) Details of the customers accounting for 10% or more of total sales for the period ended March 31, 2007 and 2006 are as follows:

	Periods ended March 31,	
	2007	2006
Company A	\$ 4,850	\$ 411,810
Company B	-	360,476
Company C	-	360,286
Company D	-	325,053
Company E	-	243,943
Company F	-	216,589

The accounts receivable from the three customers with the largest receivable balance represents 71% and 54% of the balance of the account at March 31, 2007 and December 31, 2006, respectively. Since these accounts receivable originated from the COPO resin business, which was discontinued in 2007, part of these amounts have been reclassified to discontinued operations.

5. CURRENT VULNERABILITY DUE TO CERTAIN CONCENTRATIONS

The Company's operations are all carried out in the PRC. Accordingly, the Company's business, financial condition and results of operations may be influenced by the political, economic and legal environments in the PRC, and by the general state of the PRC's economy.

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

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6. DEPOSITS AND PREPAYMENT

Deposits and prepayment consist of the following,

	March 31, 2007	March 31, 2006
Advance to suppliers	\$ 2,582,000	\$ -
Prepayment for construction in progress	1,675,718	1,827,932
Rental deposit	479	1,902
Others	1,334	935
	\$ 4,259,531	\$ 1,830,769

7. INTEREST BEARING LOAN TO A RELATED PARTY

An interest bearing loan has been lent to a related company, Shaanxi Hanzhong New Century Real Estate Company Limited which was controlled by a shareholder, Mr. Yang Feng. The loan was lent with a term of five years from November 5, 2002 to November 5, 2007 and bears interest at 7.2% per annum. A majority shareholder of the Shaanxi Suo'ang, Shaanxi Hanzhong Blue Tide Costumes Group Corporation Limited, guaranteed the repayment of this loan with all of its assets and issued a commitment letter to Shaanxi Suo'ang. According to a supplement agreement signed between both parties and witnessed by a PRC lawyer, the loan is repayable in one lump sum in May 2007.

8. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consists of the following,

	March 31, 2007	December 31, 2006
Construction in progress	\$ 781,322	\$ 579,610
Office equipment	58,762	57,771
Motor vehicles	120,558	119,624
	960,642	757,005
Less: Accumulated depreciation	(142,800)	(133,071)
	\$ 817,842	\$ 623,934

Construction in progress included above was the construction of buildings, production lines and machinery for the "coal-water mixture" business. The construction work commenced in June 2006 and the first phase is expected to be completed and become operational in 2007.

The depreciation expenses on property, plant and equipment for the periods ended March 31, 2007 and 2006 were \$9,729 and \$13,798 respectively.

9.

INTANGIBLE ASSETS

Intangible assets consist of the following as of,

	March 31, 2007	December 31, 2006
Lease prepayment	\$ 1,559,270	\$ 1,547,192
Accounting software	1,846	1,832
	1,561,116	1,549,024
Less: Accumulated amortization	(15,876)	(15,675)
	\$ 1,545,240	\$ 1,533,349

Lease prepayment represents the prepaid land use right. In 2006, the Company paid \$1,547,192 for obtaining a land use rights located at Yao Zhou Ou, PRC. The Company is in the process of obtaining the land use right certificate. Management expects that the application will be completed in July 2007 and expects that there should be no legal barriers for the Company to obtain an ownership certificate.

The amortization expense on intangible assets for the periods ended March 31, 2007 and 2006 were \$201 and \$24,253, respectively. For each of the next five years, annual amortization expense on the land use rights and accounting software will be \$30,944 and \$366, respectively.

10.

ACCRUED EXPENSES AND OTHER PAYABLES

Accrued expenses and other payables consist of the following as of,

	March 31, 2007	December 31, 2006
Accrued operating expenses	\$ 195,688	\$ 235,769
Accrued staff welfare	54,791	52,993
Other payable	64,550	68,363
	\$ 315,029	\$ 357,125

11.

STATUTORY RESERVES

As stipulated by the PRC's Company Law, net income after taxation can only be distributed as dividends after appropriation has been made for the following:

- (a) Making up cumulative prior years' losses, if any;
- (b) Allocations to the "Statutory capital reserve" of at least 10% of income after tax, as determined under PRC accounting rules and regulations, until the fund amounts to 50% of the Company's registered capital, which is restricted for set off against losses, expansion of production and operation or increase in registered capital
- (c) Allocations of 5-10% of income after tax, as determined under PRC accounting rules and regulations, to the Company's "Statutory common welfare fund", which is restricted for capital expenditure for the collective benefits of the Company's employees; and
- (d) Allocations to the discretionary surplus reserve, if approved in the shareholders' general meeting.



11. STATUTORY RESERVES (CONT'D)

Statutory reserves consist of the following as of,

	March 31, 2007	December 31, 2006
Statutory capital reserve	\$ 232,206	\$ 232,206
Statutory common welfare fund	116,103	116,103
	\$ 348,309	\$ 348,309

12. DISCONTINUED OPERATIONS

(a) Assets of discontinued operation consist of the followings as of,

	March 31, 2007	December 31, 2006
<b><u>ASSETS</u></b>		
<b><u>Current Assets</u></b>		
Accounts receivable, amounted to \$309,478 and \$754,407 net of allowances for doubtful accounts of \$3,801 and \$3,772, as of March 31, 2007 and December 31, 2006, respectively	\$ 305,677	\$ 750,635
Patent and machineries transfer receivable	133,619	256,200
Other receivable	38,730	39,071
Assets held for sale (Note 13)	2,324,853	2,439,556
	\$ 2,802,879	\$ 3,485,462

Patent and machineries transfer receivable represents the amount receivable for the disposal of patent and machineries.

	March 31, 2007	December 31, 2006
<b><u>LIABILITIES</u></b>		
<b><u>Current Liabilities</u></b>		
Accounts payable	\$ 267,995	\$ 864,787
Deposits on property held for resale	1,409,100	1,409,100
Taxes payable	25,834	92,744
Others	11,081	-
	\$ 1,714,010	2,366,631

12. DISCONTINUED OPERATIONS (CONT'D)

(b) Results of discontinued operations consist of the following for the three months ended,

	March 31, 2007	March 31, 2006
<b>Revenue</b>	\$ 4,850	\$ 2,092,428
Cost of goods sold	4,604	1,540,951
<b>Gross profit</b>	246	551,477
<b>Operating expenses</b>		
Selling expenses	-	83,775
General and administrative expenses	-	85,240
<b>Income from discontinued operations</b>	246	382,462
<b>Other income (expenses)</b>		
Rental income, net of outgoings	121,597	113,655
<b>Income from discontinued operations before income taxes</b>	121,843	496,117
Provision for income taxes	-	-
<b>Net income from discontinued operations</b>	\$ 121,843	\$ 496,117

(c) Cash flows from of discontinued operations consist of the following for the three months ended:

	March 31, 2007	March 31, 2006
<b>Cash flows from discontinued operations</b>		
Net income	\$ 121,843	\$ 496,117
Adjustments to reconcile net income to net cash provided by (used in) discontinued operations:		
Change in operating assets and liabilities:		
(Increase) decrease in:		
Accounts receivable, trade	441,705	(400,610)
Other receivables, deposits and prepayments	210,606	60,125
Inventories	13,458	3,252
Increase (decrease) in:		
Accounts payable	(591,341)	350,509
Taxes payable	(66,266)	1,761
<b>Net cash provided by discontinued operations</b>	\$ 130,005	\$ 511,154

13. ASSETS HELD FOR SALE

Assets held for sale consist of the following as of,

	March 31, 2007	December 31, 2006
Properties and leasehold improvements (Note a)	\$ 2,324,853	\$ 2,334,934
Machinery (Note b)	-	89,670
Inventory (Note c)	-	14,952
	\$ 2,324,853	\$ 2,439,556

13. ASSETS HELD FOR SALE (CONT'D)(a) Property and leasehold improvements

Property and leasehold improvements consist of the following as of,

	March 31, 2007	December 31, 2006
Cost	\$ 2,563,945	\$ 2,544,085
Accumulated depreciation	(239,092)	(209,151)
	\$ 2,324,853	\$ 2,334,934

During the year 2004, the Company exchanged leasehold properties consisting of three floors in a commercial building and having a net book value of \$1,691,555 for other leasehold properties also consisting of three floors in the same building and having a fair value of \$1,773,697. The terms of the exchange also required the Company to pay cash of \$501,205. The Company accounts for the cash component as an acquisition of real estate, and the nonmonetary component based on the recorded amount of \$1,691,555 of the leasehold properties given up.

On June 13, 2006, the Company signed a property transfer agreement with a related company, Han Zhong Si Xiong Ke Chuang Commercial Company Ltd., which is controlled by the shareholder of the Company, Mr. Yanjun Zhao, to dispose the leasehold properties together with the leasehold improvement at a cash consideration of approximately \$2,450,000 which is \$120,000 lower than the evaluated value according to an appraisal report issued by Xi'An Zheng Heng Assets Valuation Company Ltd. As such, there was gain on disposal of the property and leasehold improvements of \$ 115,066. According to the agreement, the cash consideration would be settled by installment with the last installment on or before March 31, 2007 and the title of the property will be passed to the buyer upon receipt of the 95% of the total consideration paid to the Company. As at December 31, 2006, an amount of \$1,409,100 has been received by the Company and recorded as deposits on property held for resale.

On March 25, 2007, the Company and the buyer entered into a supplementary agreement whereby the Company agrees to transfer the title of the properties to the buyer when the buyer pays the remaining balance of approximately \$1,040,900 before the date of May 31, 2007.

The depreciation expense on property and leasehold improvement for the periods ended March 31, 2007 and 2006 were \$29,941 and \$26,070 respectively.

(b) Machinery

Machinery consist of the following as of,

	March 31, 2007	December 31, 2006
Cost	\$ -	\$ 324,086
Impairment	-	(170,166)
Accumulated depreciation	-	(64,250)
	\$ -	\$ 89,670

In 2007, the Company and the buyer entered into an agreement whereby the Company agreed to sell the machinery to a related company, HanZhongWeiDa Commercial Company Limited which controlled by LePing Yao, a shareholder of Shaanxi Suoang at a consideration of \$89,670. The Company accounts for impairment of the machinery in accordance with SFAS No.144, Accounting for Impairment of Long-Lived Assets to be Disposed Of, of \$170,166 in

2006.

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13. ASSETS HELD FOR SALE (CONT'D)(b) Machinery (Cont'd)

The depreciation expense on machinery for the periods ended March 31, 2007 and 2006 were \$Nil and \$13,798 respectively.

(c) Inventories

Inventories consist of the following as of,

	March 31, 2007	December 31, 2006
Raw materials	\$ -	\$ 7,608
Finished goods	-	5,244
Packing materials		229
Consumables	-	1,871
	\$ -	\$ 14,952

In 2007, the Company sold the inventories to unrelated third parties.

14. INCOME TAXES

Companies in the PRC are generally subject to PRC Enterprise Income Taxes at a statutory rate of 33% (30% of national income tax plus 3% local income tax) on the net income. However, Shaanxi Suoang has been approved as a "high and new technology enterprise" and under PRC Income Tax Laws, it is entitled to a preferential tax rate of 15% upon expiry of a two year's tax holiday for 2004 and 2005, within which no income taxes were being charged. Shaanxi Suoang is subject to the income tax from 2006. For the year ended December 31, 2006, income tax expenses are \$214,482, which all related to the discontinued operations. Another PRC subsidiary, Suo'ang New Energy has only been newly established and carried no operations in year 2006. During the year, there is no income and no income tax liability.

The Company and Hangson are not subject to any income taxes as the companies have no income for the periods ended March 31, 2007 and 2006.

The following table reconciles the U.S. statutory rates to the Company's effective tax rate:

	2007	2006
U.S. statutory rate	34.00%	34.00%
Foreign income not recognized in the U.S.	(34.00%)	(34.00%)
China preferential income tax rate	15.00%	15.00%
Tax holiday	-	(15.00%)
Effective tax rate	15.00%	-

No significant deferred tax liabilities or assets existed as of either March 31, 2007 or December 31, 2006.

15.

EARNINGS PER SHARE

Basic earnings per share (EPS) for the periods ended March 31, 2007 and 2006 were determined by dividing net income for the years by the weighted average number of common shares outstanding. The weighted average number of common shares outstanding was adjusted to account for the effects of the share exchange transaction as a reverse acquisition as more fully described in Note 1.

The Company has retroactively adjusted the weighted average number of common shares outstanding by deeming that the one-for-five (1:5) reverse stock split during the year had occurred as of the beginning of the earliest period presented.

The reconciliations of the denominators of the basic and diluted EPS computations are as follows:

	March 31, 2007	March 31, 2006
Denominator for Basic EPS	28,227,250	28,227,250
Weighted average effect on denominator for Basic EPS	28,227,250	28,227,250

16.

RELATED PARTY TRANSACTIONS

(a)

Related party receivables and payables

Amounts receivable from a related party and directors are summary as follows as of:

	March 31, 2007	December 31, 2006
<u>Loan to a related party</u>		
Shaanxi Hanzhong New Century Real Estate Company Limited (see Note 7)		
Principal	\$ 387,300	\$ 384,300
Interest receivable	27,886	27,670
	\$ 415,186	\$ 411,970
<u>Amounts due from directors</u>		
Mr. Baowen Ren, also a shareholder of the Company	\$ 127,108	\$ 144,698
Mr. Peng Zhou, also a shareholder of the Company and Suoang New Energy	61,968	61,488
	\$ 189,076	\$ 206,186
<u>Amount due to a director</u>		
Mr. Peng Zhou, also a shareholder of the Company and Suoang New Energy	\$ 102,714	\$ 20,702

Balance with Shaanxi Hanzhong New Century Real Estate Company Limited represented an interest bearing loan which was fully described in Note 7.

Balances with Mr. Baowen Ren and Mr. Peng Zhou represent cash advances by the Company. These balances are interest free and unsecured and have no fixed repayment dates. It is expected that the balances will be received or repaid within one year.



16. RELATED PARTY TRANSACTIONS (CONT'D)(b) Guarantee given by a shareholder

A majority shareholder of Shaanxi Suoang, Shaanxi Hanzhong Blue Tide Costumes Group Corporation Limited, has guaranteed the repayment of the long-term interest bearing loan advanced to a related company, Shaanxi Hanzhong New Century Real Estate Company Limited, controlled by Mr. Yang Feng as more fully described in Note 7 and above.

(c) Transfer of property

On June 13, 2006, the Company signed a property transfer agreement with a related company, HanZhong SiXiong KeChuang Commercial Company Ltd., which is controlled by the shareholder of the Company, Mr. Yanjun Zhao to dispose the leasehold properties together with the leasehold improvement at the cash consideration of approximately \$2,450,000. The title of the property will only be transferred until payment of 95% consideration as more fully described in Note 13.

17. COMMITMENTS AND CONTINGENCIES(a) Capital expenditure commitments

During the fiscal year 2006, the Company entered into various contracts for the construction of a new plant for its coal water mixture business. Furthermore, the Company also entered into several contracts to purchase machinery.

The Company's commitments for capital expenditure as of March 31, 2007 are as follows:

Contracted but not accrued for:

Construction of factory buildings	\$	186,613
Purchase of machinery		625,709
Total	\$	812,322

(b) Operating lease commitments

As of March 31, 2007, the Company's total future minimum lease payments under non-cancelable operating leases to be paid in each of the five succeeding years are as follows:

Years ending December 31,		
2007	\$	4,889
2008		4,889
2009		2,637
2010 and thereafter		-
Total Operating Lease Commitments	\$	12,415

(c) Ownership Certificate of the leased property

According to relevant PRC laws and regulations, a land use right certificate, along with government approvals for land planning, project planning, and construction need to be obtained before construction of building is commenced. An ownership certificate shall be granted by the government upon application under the condition that the aforementioned certificate and government approvals are obtained.



17. COMMITMENTS AND CONTINGENCIES (CONT'D)

(c) Ownership Certificate of the leased property (Cont'd)

The Company has not yet obtained the ownership certificate. However, the developer of the leasehold property held for re-sale has applied to obtain the ownership certificate for approval. Moreover, the developer of the leasehold property held for re-sale had already obtained approvals for land planning, project planning, and construction.

Management believes, under the condition that the developer is granted a land use right certificate and related approvals, there should be no legal barriers for the Company to obtain an ownership certificate for the leasehold property held for re-sale. However, in the event that the Company fails to obtain the ownership certificate for the leasehold property held for re-sale, there is the risk that the buildings may need to be vacated as illegitimate ownership. However, management believes that this possibility, while present, is very remote. As a result, no provision has been made in the financial statements for this potential occurrence.

(d) Social insurance of Employees

According to the prevailing laws and regulations of the PRC, the Company is required to cover its employees with medical, retirement and unemployment insurance programs. Management believes that due to the transient nature of its employees, the Company does not need to provide all employees with such social insurance.

In the event that any current or former employee files a complaint with the PRC government, the Company may be subject to making up the social insurance as well as administrative fines. As the Company believes that these fines would not be material, no provision has been made in this regard.

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## **Item 2. Management’s Discussion and Analysis or Plan of Operation.**

*The following management’s discussion and analysis should be read in conjunction with our consolidated financial statements and the notes thereto and the other financial information appearing elsewhere in this item. In addition to historical information, the following discussion contains certain forward-looking statements within the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. These statements relate to our future plans, objectives, expectations and intentions. These statements may be identified by the use of words such as “may”, “will”, “could”, “expect”, “anticipate”, “intend”, “believe”, “estimate”, “plan”, “predict”, and similar terms or terminology, or the negative of such terms or other comparable terminology. Although we believe the expectations expressed in these forward-looking statements are based on reasonable assumptions within the bound of our knowledge of our business, our actual results could differ materially from those discussed in these statements. Factors that could contribute to such differences include, but are not limited to, those discussed in the “Risk Factors” section of this Quarterly Report on Form 10-QSB. We undertake no obligation to update publicly any forward-looking statements for any reason even if new information becomes available or other events occur in the future.*

*Our financial statements are prepared in US Dollars and in accordance with accounting principles generally accepted in the United States. See “Exchange Rates” below for information concerning the exchanges rates at which Renminbi were translated into US Dollars at various pertinent dates and for pertinent periods.*

*In this Form 10-QSB, references to “we”, “our”, “us”, “Company”, “CWCE” or the “Registrant” refer to China West Coal Energy Inc., a Nevada corporation and its subsidiaries.*

### **Overview**

China West Coal Energy Inc. (“CWCE” or the “Company”) is engaged in the research, development, production and sale of its “coal water mixture” product, a fuel substitute for oil, gas or coal. The Company was originally incorporated in Texas as “Discount Mortgage Services, Inc.” on July 11, 2000 and in September 2001, the Company purchased Endo Networks, Inc., a corporation incorporated in Ontario, Canada on January 11, 2001 (“Endo Canada”). In November 2001, the Company changed its name to Endo Networks, Inc. and was redomiciled to the State of Nevada in December 2002. Prior to the Share Exchange transaction described below, the Company conducted through, and all of the Company’s assets were contained within, Endo Canada, in which conceptual and software development was ongoing for approximately two years by the Company founders, through ongoing contract relationships with software development companies.

On October 18, 2006, we entered into a definitive Share Exchange Agreement with Hangson Limited (“Hangson”), whereby we would acquire all of the outstanding common stock of Hangson in exchange for newly-issued shares of our common stock to the Hangson shareholders (the “Share Exchange”). On October 20, 2006 (the “Closing Date”), Hangson became our wholly-owned subsidiary and Hangson’s shareholders became owners of the majority of our voting stock. The acquisition of Hangson by us was accounted for as a reverse merger because on a post-merger basis, the former shareholders of Hangson held a majority of our outstanding common stock on a voting and fully-diluted basis. As a result, Hangson is deemed to be the acquirer for accounting purposes. From and after the Closing Date of the Share Exchange, the Registrant’s primary operations consisted of the operations of Hangson.

Additionally, on August 18, 2006, Hangson entered various agreements Shaanxi Suo’ang Biological Science & Technology Co., Ltd. (“Shaanxi Suoang”). Through these contractual arrangements, we have the ability to substantially influence Shaanxi Suoang’s daily operations and financial affairs, appoint its senior executives and approve all matters requiring shareholder approval. As a result of these contractual arrangements, which obligates Hangson to absorb a majority of the risk of loss from Shaanxi Suoang activities, it enables Hangson to control Shaanxi Suoang, and enables Hangson to receive a majority of Shaanxi Suoang’s expected residual returns, Hangson is considered to be the primary beneficiary of Shaanxi Suoang. Accordingly, we consolidate Shaanxi Suoang’s results, assets and liabilities in our

financial statements. For a description of these contractual arrangements, see the section titled “Contractual Arrangements with Shaanxi Suoang and its Shareholders” in the Company’s Annual Report on Form 10-KSB filed with the SEC on May 3, 2007. The Company’s consolidated assets do not include any collateral for Shaanxi Suoang’s obligations. The creditors of Shaanxi Suoang do not have recourse to the general credit of the Company.

Effective January 4, 2007, we changed our name from “Endo Networks, Inc.” to “China West Coal Energy Inc.” (the “Name Change”) and we increased the number of our authorized shares of capital stock to 250,000,000 shares, which include 200,000,000 shares of common stock and 50,000,000 shares of preferred stock (“Authorized Shares Amendment”), by filing a Certificate of Amendment to amend our Articles of Incorporation. On November 27, 2006, holders of a majority of our outstanding common stock approved the Name Change and the Authorized Shares Amendment to our Articles of Incorporation. On December 8, 2006, we filed a definitive information statement on Schedule 14C with the SEC, which was delivered to our stockholders of record to notify them that the stockholders had approved the Name Change and the Authorized Shares Amendment to our Articles of Incorporation. Further, and as discussed more fully in the Form 8-K Current Report filed by the Company with the SEC on January 16, 2007, the Company’s Board of Directors, by unanimous written consent, approved a change of the Company’s fiscal year. The Company’s new fiscal year begins on January 1st and ends on December 31st of each year.



Our primary business operations are conducted through our wholly-owned subsidiary Hangson Limited (“Hangson”). Hangson was incorporated under the laws of the British Virgin Islands on June 2, 2006. Hangson does not have any substantive operations of its own and conducts its primary business operations through Shaanxi Suoang, which through the contractual arrangements described above is deemed Hangson’s variable interest entity (“VIE”). For the majority of fiscal 2006, Shaanxi Suoang was engaged in two lines of businesses: the research, development, production, marketing and sales of coal-polymer (“COPO”) resin products, and also in the research, development, production and sale of “coal-water mixture,” fuel substitute product (“CWM Fuel”). However, the Company subsequently decided to focus on its CWM Fuel product business. Thus, as of January 2007, Shaanxi Suoang ceased operations of the COPO resin products business and is now focused on its CWM Fuel product business. Shaanxi Suoang conducts its CWM Fuel operations through its subsidiary, Shaanxi Suoang New Energy Enterprise Company Ltd. (“Suoang New Energy”). Shaanxi Suoang owns a controlling 80% equity interest in Suoang New Energy. The Company entered into sales contracts for the sale of its CWM fuel in early 2007. Construction of the Company’s CWM Fuel production plant is nearing completion. The Company expects the CWM Fuel production plant will become operational and production of its CWM Fuel will commence in July 2007.

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

#### *Lease prepayment*

Lease prepayment represents the prepaid land use right. Lease prepayment is amortized over the term of 50 years.

#### *Property, plant and equipment*

Property, plant and equipment are recorded at cost less accumulated depreciation and amortization. Gains or losses on disposals are reflected as gain or loss in the year of disposal. The cost of improvements that extend the life of plant, property and equipment are capitalized. These capitalized costs may include structural improvements, equipment and fixtures. All ordinary repair and maintenance costs are expensed as incurred.

Depreciation or amortization for financial reporting purposes is provided using the straight-line method over the estimated useful lives.

#### *Impairment*

The Company accounts for impairment of long-lived assets including property, plant and equipment, and amortizable intangible assets in accordance with SFAS No.144, *Accounting for Impairment of Long-Lived Assets to be Disposed Of*, which requires an impairment loss to be recognized when the carrying amount of a long-lived asset or asset group exceeds its fair value and is not recoverable (when carrying amount exceeds the gross, undiscounted cash flows from use and disposition). The impairment loss is measured as the excess of the carrying amount over the asset’s (or asset group’s) fair value.

#### *Income taxes*

The Company accounts for income taxes in accordance with SFAS No. 109, *Accounting for Income Taxes*. SFAS No. 109 requires an asset and liability approach for financial accounting and reporting for income taxes and allows recognition and measurement of deferred tax assets based upon the likelihood of realization of 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. 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 deductibility is uncertain.

*Revenue recognition*

Revenues of the Company include COPO resin product sales which have been classified as discontinued operations. Sales are recognized when the following four revenue criteria are met: persuasive evidence of an arrangement exists, delivery has occurred, the selling price is fixed or determinable, and collectibility is reasonably assured. Revenues are presented net of value added tax (VAT). No return allowance is made as products are normally not returnable upon acceptance by the customers

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*Foreign currency transactions*

The Company determines its functional currency based on the criteria of SFAS 52, *Foreign Currency Translation* and has determined RMB to be their functional currency. Transactions denominated in foreign currencies are translated into the functional currency at the exchange rates prevailing on the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the exchange rates prevailing on the balance sheet date. Exchange gains or losses are included in the statement of operations.

*Foreign currency translation*

The reporting currency of the Company is the United States Dollars. All assets and liabilities accounts have been translated into United States Dollars using the current exchange rate at the balance sheet date. Capital stock is recorded at historical rates. Revenue and expenses are translated using the average exchange rate in the year. The resulting gain and loss has been reported as other comprehensive income (loss) within the shareholder's equity.

*Use of estimates*

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Because of the use of estimates inherent in the financial reporting process, actual results could differ from those estimates. Significant estimates include estimates of accruals and determination of fair values for assets disposal.

**Going Concern**

In January 2007, the Company ceased its COPO resin products operations and is principally engaged in research, development, production, marketing and sales of "coal-water mixture" business. The new CWM Fuel business has not commenced production as of the date of this report. Furthermore, the Company signed an agreement to dispose of leasehold property it owned in the previous years which generated rental income in order to accumulate funds to support the new CWM Fuel operation. These circumstances indicate that the Company may need additional financing to meet cash requirements for its operations in order to continue as a going concern.

The accompanying financial statements do not include any adjustments relating to the recoverability and classification of recorded amounts of assets or the amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. Management believes the Company's ability to continue as a going concern is dependent upon its ability to maintain profitable operations for the new business. In 2007, the Company entered into sales contracts for the sale of its CWM Fuel product. Management believes the Company will be able to commence production of its CWM Fuel product and be able to generate sufficient cash flow from these sales contracts to meet its obligations on a timely basis in the foreseeable future.

**RESULTS OF OPERATIONS**

**Three month period ended March 31, 2007 as compared to three month period ended March 31, 2006**

During the quarter ended March 31, 2007, we had revenues from discontinued operations of \$4,850 as compared to revenues of \$2,092,428 during the quarter ended March 31, 2006, a decrease of approximately 99%. Net revenue from discontinued operations was \$121,843 for the quarter ended March 31, 2007 as compared to \$496,117 for the quarter ended March 31, 2006, a decrease of approximately 75.44%. In general, this decrease is mainly attributable to the cessation of the Company's COPO resin products operation.



**GENERAL AND ADMINISTRATIVE EXPENSES.** General and administrative expenses totaled \$51,662 for the quarter ended March 31, 2007 as compared to \$0 for the quarter ended March 31, 2006. This increase is primarily attributable to the expenses for the development of the Company's new CWM Fuel product.

**NET INCOME.** We had a net income of \$33,886 for the quarter ended March 31, 2007 as compared to a net income \$481,256 for the quarter ended March 31, 2006. The decrease in net income is primarily attributable to cessation of the Company's COPO resin product operation.

## **PLAN OF OPERATIONS**

As discussed more fully above, we ceased operations of our COPO Resin product business, and the Company is now currently engaged in research, development, marketing and sales of its coal water mixture fuel (hereinafter "CWM Fuel"). CWM Fuel is a fuel substitute that can be used instead of oil, coal and gas, in industrial boilers, power plant boilers and industrial kilns that are used for central heating of government buildings, schools, armed forces' barracks, and residential communities, and also in industrial production facilities. We have already entered into sales contracts for the sale of our CWM Fuel in early 2007. Further, the Company is currently constructing its coal water mixture production plant in the city of Tongchuan, and is currently planning for an annual production capacity of 300,000 tons of its CWM Fuel, which would be one of the largest in Western China.. We believe that construction of the first phase of this plant, which will allow us to commence operations of our CWM Fuel business, will be completed by June 2007. We expect the plant operations and the production and delivery of our CWM Fuel product will commence in July 2007.

## **LIQUIDITY AND CAPITAL RESOURCES**

Net cash flow used in operating activities was \$1,936,216 for the three months ended March 31, 2007 and net cash flow provided by operating activities \$496,319 for the three months ended March 31, 2006. The decrease in our net cash flow provided by operating activities for the three months ended March 31, 2006 was mainly due to the payment of purchase deposit

Net cash flow used in investing activities was \$11,282 and net cash flow provided by investing activities \$3,079 for the three months ended March 31, 2007 and 2006, respectively. Uses of cash flow for investing activities were mainly related to the purchase of plant and equipment.

Net cash flow provided by financing activities was \$80,195 in relation to advances from a director for the three months ended March 31, 2007. The net cash flow provided by financing activities of \$3,861,360 for the three months ended March 31, 2006 was mainly due to the proceeds from an injection of additional paid in capital from a subsidiary in 2006.

We believe that we have adequate capital resources to continue our operations and will not need to raise capital in the near future. We believe that our current cash balance and the revenues that will be generated will cover anticipated operating expenses for a period of at least one year without supplementing our cash reserves. We may, however, raise additional capital to further develop our products.

## **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to our investors.

## **Exchange Rates**

Shaanxi Suoang maintains its books and records in Renminbi (“RMB”), the lawful currency of the PRC. In general, for consolidation purposes, the Company translates Shaanxi Suoang’s assets and liabilities into US Dollars using the applicable exchange rates prevailing at the balance sheet date, and the statement of income is translated at average exchange rates during the reporting period. Adjustments resulting from the translation of Shaanxi Suoang’s financial statements are recorded as accumulated other comprehensive income.

Until July 21, 2005, RMB had been pegged to US\$ at the rate of RMB8.30: US\$1.00. On July 21, 2005, the PRC government reformed the exchange rate system into a managed floating exchange rate system based on market supply and demand with reference to a basket of currencies. In addition, the exchange rate of RMB to US\$ was adjusted to RMB8.11: US\$1.00 as of July 21, 2005. The People’s Bank of China announces the closing price of a foreign currency such as US\$ traded against RMB in the inter-bank foreign exchange market after the closing of the market on each working day, which will become the unified exchange rate for the trading against RMB on the following working day. The daily trading price of US\$ against RMB in the inter-bank foreign exchange market is allowed to float within a band of  $\pm 0.3\%$  around the unified exchange rate published by the People’s Bank of China. This quotation of exchange rates does not imply free convertibility of RMB to other foreign currencies. All foreign exchange transactions continue to take place either through the Bank of China or other banks authorized to buy and sell foreign currencies at the exchange rates quoted by the People’s Bank of China. Approval of foreign currency payments by the Bank of China or other institutions required submitting a payment application form together with invoices, shipping documents and signed contracts.

The exchange rates used to translate amounts in RMB into US Dollars for the purposes of preparing the consolidated financial statements or otherwise stated in this MD&A were as follows:

	March 31, 2007	December 31, 2006	March 31, 2006
Balance sheet items, except for the registered and paid-up capital, as of end of period/year	USD0.1291:RMB1	USD0.1281:RMB1	USD0.1245:RMB1
Amounts included in the statement of operations, statement of changes in stockholders' equity and statement of cash flows for the period/ year ended	USD0.1265:RMB1	USD0.1260:RMB1	USD0.1263:RMB1

No representation is made that RMB amounts have been, or would be, converted into US\$ at the above rates.

### **Inflation**

We believe that inflation has not had a material effect on our operations to date.

## **RISK FACTORS**

### **Factors Affecting Business, Operating Results and Financial Condition**

*An investment in our securities is very speculative and involves a high degree of risk. You should carefully consider the following risk factors, along with the other matters referred to in this Quarterly Report, before you decide to buy our securities. If you decide to buy our securities, you should be able to afford a complete loss of your investment.*

### **Risks Associated With Our Business**

#### ***FACTORS THAT MAY AFFECT FUTURE PERFORMANCE***

Before investing in our common stock you should carefully consider the following risk factors, the other information included herein and the information included in our other reports and filings. Our business, financial condition, and the trading price of our common stock could be adversely affected by these and other risks.

*Our limited operating history makes it difficult to evaluate our future prospects and results of operations.*

We have a limited operating history. Shaanxi Suoang commenced operations in 2002 and first achieved profitability in the year ended 2004. Accordingly, you should consider our future prospects in light of the risks and uncertainties experienced by early stage companies in evolving industries such as the coal products and alternative energy industry in China. An investor in our securities must consider the risks, uncertainties and difficulties frequently encountered by companies in new and rapidly evolving markets. The risks and difficulties we face include challenges in accurate financial planning as a result of limited historical data and the uncertainties resulting from having had a relatively limited time period in which to implement and evaluate our business strategies as compared to older companies with longer operating histories.

*We recently ceased operations of our COPO resin product business and the production of our CWM Fuel product has yet to commence.*

In December 2006, we decided to solely focus on the research, development, production, marketing and sale of our CWM Fuel product and thus, in January 2007, we ceased operations and have phased out our COPO resin product business. In early 2007, we entered into contracts for the sale of our CWM Fuel product. We believe the first phase of the construction of our CWM Fuel manufacturing plant will be completed in June 2007, and that production and delivery of our CWM Fuel product will commence in July 2007. However, there can be no assurance that we will be able to successfully complete the construction of our CWM manufacturing plant in a timely manner. Assuming we complete the construction of our CWM Fuel plant and commence production of our CWM Fuel product, we cannot assure you that our operations will be able to generate sufficient revenue to continue our operations or that our new CWM Fuel business operations will be profitable.



***Our independent auditor has expressed doubt about our ability to continue as a going concern because we ceased our COPO resin operation, which was our main resource of working capital, we disposed of leasehold property which generated rental income and production of our new Coal Water Mixture (“CWM”) fuel product has not commenced.***

Our independent auditor has noted in its report concerning our financial statements as of December 31, 2006 that the Company ceased its COPO resin operation, which was the main resource of the Company’s working capital, disposed of leasehold property, which generated rental income, and started a new Coal Water Mixture (“CWM”) fuel business subsequent to the balance sheet date. The independent auditor further noted that production facilities of the Company’s CWM Fuel are under construction and operations have not yet commenced. The independent auditor stated that these conditions raise substantial doubt about our ability to continue as a going concern. We cannot assure you that we will achieve operating profits in the future.

***We Must Obtain Additional Financing to Execute Our Business Plan***

The projected revenues from the sale of our CWM Fuel product may not be adequate to support our expansion and product development programs. We will need additional funds to build and maintain our new production facilities, pursue further research and development, obtain regulatory approvals; file, prosecute, defend and enforce our intellectual property rights and market our products. We will seek additional funds through public or private equity or debt financing, strategic transactions and/or from other sources. We could enter into collaborative arrangements for the development of particular products that would lead to our relinquishing some or all rights to the related technology or products.

There are no assurances that future funding will be available on favorable terms or at all. If additional funding is not obtained, we will need to reduce, defer or cancel development programs, planned initiatives or overhead expenditures, to the extent necessary. The failure to fund our capital requirements would have a material adverse effect on our business, financial condition and results of operations.

***Our business and results of operations are dependent on coal markets, which may be cyclical.***

As the majority of our revenue will be derived from sales of coal-based products, our business and operating results are substantially dependent on the domestic supply for coal. The domestic and international coal markets are cyclical and exhibit fluctuation in supply and demand from year to year and are subject to numerous factors beyond our control, including, but not limited to, the economic conditions in the PRC, the global economic conditions and fluctuations in industries with high demand for coal, such as the power and steel industries. Fluctuations in supply and demand for coal have effects on coal prices, which in turn affect our operating and financial performance. We have experienced substantial price fluctuations in the past and believe that such fluctuations will continue. The demand for coal is primarily affected by the overall economic development and the demand for coal from the electricity generation, steel and construction industries. The supply of coal on the other hand, is primarily affected by the geographical location of the coal supplies, the volume of coal produced by the domestic and international coal suppliers, and the quality and price of competing sources of coal. Alternative fuels such as natural gas, oil and nuclear power, alternative energy sources such as hydroelectric power, and international shipping costs also have effects on the market demand for coal. Excess demand for coal may have an adverse effect on coal prices which would in turn cause a decline in our profitability. A significant increase in domestic coal prices could also materially and adversely affect our business and result of operations.

***Our business relies on our major customers.***

Our revenues from the sale of the CWM Fuel will be initially derived from sales to 3 major customers, Shaanxi Hau Yuen Paper Industry Company Limited, Shaanxi Tongchuan Yi Tong Gao Ya Dian Chi Factory, and Shaanxi Yao

Zhou Jian Qin Cement Company Limited. Given the large percentage of our revenues to be derived from our sales to these 3 major customers, any adverse developments to Shaanxi Yao Zhou Jian Qin Cement Company Limited, Shaanxi Tongchuan Yi Tong Gao Ya Dian Chi Factory and Shaanxi Hau Yuen Paper Industry Company Limited business operations could have an adverse impact on our results of operations.

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***Competition in the PRC and the international coal industry is increasing and our business and prospects will be adversely affected if we are not able to compete effectively.***

We face competition in all areas of our business. Competition in the coal energy industry is based on many factors, including price, production capacity, quality and characteristics, transportation capability and costs, blending capability and brand name. Our coal-based products business competes in the domestic market in China and in international markets with other large domestic coal-based products companies and we will also have to compete with other competitors in the coal water mixture product industry. Some of our competitors may have greater financial, marketing, distribution and other resources than we do, and more well-known brand names in the markets. We currently compete favorably on the quality of our coal-based products. However, there can be no assurance that we will continue to compete favorably due to quality improvements by our competitors and this may have a material adverse impact on our results of operations.

***We may suffer losses resulting from industry-related accidents and lack of insurance.***

We operate manufacturing facilities that may be affected by water, gas, fire or structural problems. As a result, we, like other coal-based products companies, may experience accidents that will cause property damage and personal injuries. Although we have implemented safety measures for our production facilities and provided on-the-job training for our employees, there can be no assurance that industry-related accidents will not occur in the future.

We do not currently maintain fire, casualty or other property insurance covering our properties, equipment or inventories, other than with respect to vehicles. In addition, we do not maintain any business interruption insurance or any third party liability insurance to cover claims in respect of personal injury, property or environmental damage arising from accidents on our properties, other than third party liability insurance with respect to vehicles. Any uninsured losses and liabilities incurred by us could have a material adverse effect on our financial condition and results of operations.

***Our business operations may be adversely affected by present or future environmental regulations.***

As a producer of coal products, we are subject to significant, extensive, and increasingly stringent environmental protection laws and regulations in China. These laws and regulations:

impose fees for the discharge of waste substances;

require the establishment of reserves for reclamation and rehabilitation;

require the payment of fines for serious environmental offenses; and

allow the PRC Government, at its discretion, to close any facility that fails to comply with orders requiring it to correct or stop operations causing environmental damage.

Our operations may produce significant amounts of waste water, gas and solid waste materials. Currently, the PRC Government is moving toward more rigorous enforcement of applicable laws and regulations as well as the adoption and enforcement of more stringent environmental standards. Our capital expenditure for environmental regulatory compliance may not be sufficient and we may need to allocate additional funds for such purpose. If we fail to comply with current or future environmental laws and regulations, we may be required to pay penalties or fines or take corrective actions, any of which may have a material adverse effect on our business operations and financial condition.

In addition, China is a signatory to the 1992 United Nations Framework Convention on Climate Change and the 1997 Kyoto Protocol, which are intended to limit emissions of greenhouse gases. Efforts to control greenhouse gas emission in China could result in reduced use of coal if power generators switch to sources of fuel with lower carbon dioxide emissions, which in turn could reduce the revenues of our business and have a material adverse effect on our results of operations.

***Our operations, which are conducted in the PRC, are subject to a number of risks relating to the PRC.***

Our business operations are located in the PRC and thus we are subject to a number of risks relating to the PRC. The central and local PRC governments continue to support the development and operation of coal industry in the PRC. If the PRC Government changes its current policies that are currently beneficial to us, we may face significant constraints on our flexibility and ability to expand our business operations or to maximize our profitability.

Under current PRC regulatory requirements, our projects for the development of our coal water mixture fuel substitute require PRC Government approval. If any of our important projects required for our growth or cost reduction are not approved, or are not approved on a timely basis, our financial condition and operating performances could be adversely affected.

The PRC Government has been reforming, and is expected to continue to reform its economic system. Many of the reforms are unprecedented or experimental, and are expected to be refined and improved. Other political, economic and social factors can also lead to further readjustment of the reform measures. This refining and readjustment process may not always have a positive effect on our operations. Our operating results may be adversely affected by changes in the PRC's economic and social conditions and by changes in policies of the PRC Government such as changes in laws and regulations (or the interpretation thereof), imposition of additional restrictions on currency conversion and reduction in tariff protection and other import restrictions.

Since 1994, the conversion of Renminbi into foreign currencies, including Hong Kong and U.S. dollars, has been based on rates set by the People's Bank of China, or PBOC, which are set daily based on the previous day's PRC interbank foreign exchange market rate and current exchange rates on the world financial markets. Since 1994, the official exchange rate for the conversion of Renminbi to U.S. dollars has generally been stable. On July 21, 2005, however, PBOC announced a reform of its exchange rate system. Under the reform, Renminbi is no longer effectively linked to US dollars but instead is allowed to trade in a tight 0.3% band against a basket of foreign currencies. Any further appreciation of Renminbi in the future will increase the cost of our export sales, reduce our account receivables denominated in foreign currencies and adversely affect our financial condition and results of operations. On the other hand, any devaluation of the Renminbi may adversely affect the value of, and dividends payable on our shares we receive our revenues and denominate our profits in Renminbi. Our financial condition and operating performance may also be affected by changes in the value of certain currencies other than Renminbi in which our earnings and obligations are denominated. In particular, a devaluation of the Renminbi is likely to increase the portion of our cash flow required to satisfy our foreign currency-denominated obligations.

Since 1997, many new laws and regulations covering general economic matters have been promulgated in the PRC. Despite this activity to develop the legal system, PRC's system of laws is not yet complete. Even where adequate law exists, enforcement of existing laws or contracts based on existing law may be uncertain and sporadic, and it may be difficult to obtain swift and equitable enforcement or to obtain enforcement of a judgment by a court of another jurisdiction. The relative inexperience of PRC's judiciary in many cases creates additional uncertainty as to the outcome of any litigation. In addition, interpretation of statutes and regulations may be subject to government policies reflecting domestic political changes.

***Our coal water mixture production facilities will be subject to extensive regulation by the PRC Government and government regulations may limit our activities and adversely affect our business operations.***

Our coal water mixture operation, like those of other PRC energy companies, is subject to extensive regulation established by the PRC Government. Central governmental authorities, such as the National Development and Reform Commission, the State Environmental Protection Administration, the Ministry of Land and Resources, the State Administration of Coal Mine Safety, the and the State Bureau of Taxation, and provincial and local authorities and agencies exercise extensive control over various aspects of China's coal industry and transportation (including rail and sea transport). These controls affect the following material aspects of our operations:

pricing of our transport services;

industry-specific taxes and fees;

target of our capital investments;

pension funds appropriation; and

environmental and safety standards.

We may face significant constraints on our ability to implement our business strategies or to carry out or expand our business operations. Our business may also be materially and adversely affected by future changes in certain regulations and policies of the PRC Government in respect of the coal industry. New legislation or regulations may be adopted that may materially and adversely affect our coal water mixture operations, our cost structure or the demand for our products. In addition, new legislation or regulations or different or more stringent interpretation of existing laws and regulations may also require us to substantially change our existing operations or incur significant costs.

***The Profitability of Our Products Depend on Our Ability to Operate Without Infringing the Proprietary Rights of Others and to Protect Proprietary Rights***

We must operate without infringing the proprietary rights of third parties and without third parties circumventing our rights. The patent positions of coal and biotechnology enterprises, including ours, are uncertain and involve complex legal and factual questions for which important legal principles are largely unresolved. For example, no consistent policy has emerged regarding the breadth of bio-technology patent claims that are granted by the U.S. Patent and Trademark Office or enforced by the U.S. federal courts. In addition, the scope of the originally claimed subject matter in a patent application can be significantly reduced before a patent is issued. The patent situation outside the U.S. is even more uncertain and is currently undergoing review and revision in many countries. For our products, which have or in the future may have, obtained patent protection, their profitability may depend in part on our ability to obtain and maintain patents and licenses and preserve trade secrets, and the period our intellectual property remains exclusive. Because patent applications are maintained in secrecy in some cases, we cannot be certain that we or our licensors are the first creators of inventions described in pending patent applications or patents or the first to file patent applications for such inventions.

***Other companies may independently develop similar products and design around any patented products we develop.***

We cannot assure you that:

any of our future patent applications will result in the issuance of patents;

we will develop additional patentable products;

any patents that we are issued will provide us with any competitive advantages;

the patents of others will not impede our ability to do business; or

third parties will not be able to circumvent our patents.

A number of coal-based products companies, bio-technology companies, research and academic companies and institutions have developed technologies, filed patent applications or received patents on technologies that may relate to our business. If these technologies, applications or patents conflict with ours, our ability to sell our products may be curtailed. If patents that cover our activities are issued to other companies, we may not be able to obtain licenses at a reasonable cost, or at all. We may also be unable to develop our technology, or introduce, manufacture or sell current or future products we have planned.

Patent litigation is becoming widespread in the bio-technology industry. Such litigation may affect our efforts to form collaborations, to conduct research or development, to conduct clinical testing or to manufacture or market any products under development. There are no assurances that our patents would be held valid or enforceable by a court or that a competitor's technology or product would be found to infringe our patents in the event of patent litigation. Our business could be materially affected by an adverse outcome to such litigation. We could incur substantial costs and devote significant management resources to defend our patent position or to seek a declaration that another company's patents are invalid.

Much of our know-how and technology may not be patentable, though it may constitute trade secrets. There are no assurances that we will be able to meaningfully protect our trade secrets. We cannot assure you that any of our existing confidentiality agreements with employees, consultants, advisors or collaborators will provide meaningful protection for our trade secrets, know-how or other proprietary information in the event of any unauthorized use or

disclosure. Collaborators, advisors or consultants may dispute the ownership of proprietary rights to our technology, for example by asserting that they developed the technology independently.



***We May Encounter Difficulties in Manufacturing our Products***

Before our products can be profitable, they must be produced in commercial quantities in a cost-effective manufacturing process that complies with regulatory requirements, including production and quality control regulations. If we cannot arrange for or maintain commercial-scale manufacturing on acceptable terms, or if there are delays or difficulties in the manufacturing process, we may not be able to conduct product testing, obtain regulatory approval or meet demand for our products. Production of our products could require raw materials which are scarce or which can be obtained only from a limited number of sources. If we are unable to obtain adequate supplies of such raw materials, the development, regulatory approval and marketing of our products could be delayed.

***We May Not Be Able to Obtain the Regulatory Approvals or Clearances That Are Necessary to Commercialize Our Products***

The PRC imposes statutory and regulatory obligations upon the manufacture and sale of our products. Each regulatory authority typically has a lengthy approval process in which it examines product testing data and the facilities in which the product is manufactured. Regulatory submissions must meet complex criteria to demonstrate the safety and efficacy of the ultimate products. Addressing these criteria requires considerable data collection, verification and analysis. We may spend time and money preparing regulatory submissions or applications without assurances as to whether they will be approved on a timely basis or at all.

Our product candidates may require additional development prior to their commercialization. These steps and the process of obtaining required approvals and clearances can be costly and time-consuming. If our potential products are not successfully developed, cannot be proven to be safe and effective through product testing, or do not receive applicable regulatory approvals and clearances, or if there are delays in the process:

the commercialization of our products could be adversely affected;

any competitive advantages of the products could be diminished; and

revenues or collaborative milestones from the products could be reduced or delayed.

Governmental and regulatory authorities may approve a product candidate for fewer indications or narrower circumstances than requested or may condition approval on the performance of post-marketing studies for a product candidate. Even if a product receives regulatory approval and clearance, it may later exhibit adverse side effects that limit or prevent its widespread use or that force us to withdraw the product from the market.

Any marketed product and its manufacturer will continue to be subject to strict regulation after approval. Results of post-marketing programs may limit or expand the further marketing of products. Unforeseen problems with an approved product or any violation of regulations could result in restrictions on the product, including its withdrawal from the market and possible civil actions.

In manufacturing our products, we will be required to comply with applicable good manufacturing practices regulations, which include requirements relating to quality control and quality assurance, as well as the maintenance of records and documentation. If we cannot comply with regulatory requirements, including applicable good manufacturing practice requirements, we may not be allowed to develop or market the product candidates. If we fail to comply with applicable regulatory requirements at any stage during the regulatory process, we may be subject to sanctions, including fines, product recalls or seizures, injunctions, refusal of regulatory agencies to review pending market approval applications or supplements to approve applications, total or partial suspension of production, civil penalties, withdrawals of previously approved marketing applications and criminal prosecution.

***Competitors May Develop and Market Products That Are Less Expensive, More Effective or Safer, Making Our Products Obsolete or Uncompetitive***

Some of our competitors and potential competitors have greater product development capabilities and financial, scientific, marketing and human resources than we do. Technological competition from other alternative energy or other coal-based product companies is intense and is expected to increase. Other companies have developed technologies that could be the basis for competitive products. Some of these products may be produced with an entirely different approach or may be manufactured differently than the products we are developing. Alternative products may be developed that are more effective and are less costly than our products. Competitors may succeed in developing products earlier than us, obtaining approvals and clearances for such products more rapidly than us, or developing products that are more effective than ours. Over time, our technology or products may become obsolete or uncompetitive.

***Our Products May Not Gain Market Acceptance***

Our products may not gain market acceptance in the coal-based products community. The degree of market acceptance of any product depends on a number of factors, including establishment and demonstration of our products' efficacy and safety, cost-effectiveness, advantages over alternative products, and marketing and distribution support for the products. Limited information regarding these factors is available in connection with our products or products that may compete with ours.

To directly market and distribute our products, we or our collaborators require a marketing and sales force with appropriate technical expertise and supporting distribution capabilities. We may not be able to further establish sales, marketing and distribution capabilities or enter into arrangements with third parties on acceptable terms. If we or our partners cannot successfully market and sell our products, our ability to generate revenue will be limited.

***Our Operations and the Use of Our Products Could Subject Us to Damages Relating to Injuries or Accidental Contamination.***

Our research and development processes involve the controlled use of hazardous materials. We are subject to federal, provincial and local PRC laws and regulations governing the use, manufacture, storage, handling and disposal of such materials and waste products. The risk of accidental contamination or injury from handling and disposing of such materials cannot be completely eliminated. In the event of an accident involving hazardous materials, we could be held liable for resulting damages. We are not insured with respect to this liability. Such liability could exceed our resources. In the future we could incur significant costs to comply with PRC environmental laws and regulations.

***If We Were Successfully Sued for Product Liability, We Could Face Substantial liabilities That May Exceed Our Resources.***

We may be held liable if any product we develop, or any product which is made using our technologies, causes injury or is found unsuitable during product testing, manufacturing, marketing, sale or use. We currently do not have product liability insurance. We are not insured with respect to this liability. If we choose to obtain product liability insurance but cannot obtain sufficient insurance coverage at an acceptable cost or otherwise protect against potential product liability claims, the commercialization of products that we develop may be prevented or inhibited. If we are sued for any injury caused by our products, our liability could exceed our total assets.

***We Have Limited Business Insurance Coverage.***

The insurance industry in China is still at an early stage of development. Insurance companies in China offer limited business insurance products. We do not have any business liability or disruption insurance coverage for our operations in China. Any business disruption, litigation or natural disaster may result in our incurring substantial costs and the diversion of our resources.

***Our Success Depends on Attracting and Retaining Qualified Personnel***

We depend on a core management and scientific team. The loss of any of these individuals could prevent us from achieving our business objective of commercializing our product candidates. Our future success will depend in large part on our continued ability to attract and retain other highly qualified scientific, technical and management personnel, as well as personnel with expertise in clinical testing and government regulation. We face competition for personnel from other companies, universities, public and private research institutions, government entities and other organizations. If our recruitment and retention efforts are unsuccessful, our business operations could suffer.



### **Risk Related to the Alternative Energy Industry**

*A drop in the retail price of conventional energy or other alternative energy may have a negative effect on our business.*

A customer's decision to purchase our CWM Fuel product will be primarily driven by the return on investment resulting from the energy savings from our CWM Fuel product. Any fluctuations in economic and market conditions that impact the viability of conventional and other alternative energy sources, such as decreases in the prices of oil and other fossil fuels could cause the demand for our CWM Fuel product to decline. Although we believe that current levels of retail energy prices support a reasonable return on investment for our CWM Fuel product, there can be no assurance that future retail pricing of conventional energy and other alternative energy will remain at such levels.

*Existing regulations and changes to such regulations may present technical, regulatory and economic barriers to the purchase and use of coal water mixture product, which may significantly affect the demand for our products.*

Our CWM Fuel product will be subject to oversight and regulation in accordance with national and local ordinances or regulations relating to safety, environmental protection, and related matters. We are responsible for knowing such ordinances and requirements must design our CWM Fuel product to comply with varying standards. Any new government regulations or utility policies pertaining to our products may result in significant additional expenses to us and, as a result, could cause a significant reduction in demand for our product.

If our CWM Fuel product is not suitable for widespread adoption or sufficient demand for our CWM Fuel product does not develop or takes longer to develop than we anticipate, our sales would not significantly increase and we would be unable to achieve or sustain profitability.

The market for CWM Fuel products is emerging and rapidly evolving, and its future success is uncertain. If CWM Fuel and clean coal technology prove unsuitable for widespread commercial deployment or if demand for our CWM Fuel product fails to develop sufficiently, we may be unable to generate enough revenues to achieve and sustain profitability. In addition, demand for CWM Fuel product in the markets and geographic regions we target may not develop or may develop more slowly than we anticipate. Many factors will influence the widespread adoption of coal water mixture technology and demand for our products, including:

cost-effectiveness of coal water mixture technologies as compared with conventional and other alternative energy technologies;

performance and reliability of our coal water mixture product as compared with conventional and other alternative energy products;

capital expenditures by customers that tend to decrease if the PRC or global economy slows down; and

availability of government subsidies and incentives.

### **Risks Related to Our Corporate Structure**

*PRC laws and regulations governing our businesses and the validity of certain of our contractual arrangements are uncertain. If we are found to be in violation, we could be subject to sanctions. In addition, changes in such PRC laws and regulations may materially and adversely affect our business.*

There are substantial uncertainties regarding the interpretation and application of PRC laws and regulations, including, but not limited to, the laws and regulations governing our business, or the enforcement and performance of our contractual arrangements with our affiliated Chinese entity, Shaanxi Suoang, and its shareholders. We are considered a foreign person or foreign invested enterprise under PRC law. As a result, we are subject to PRC law limitations on foreign ownership of Chinese companies. These laws and regulations are relatively new and may be subject to change, and their official interpretation and enforcement may involve substantial uncertainty. The effectiveness of newly enacted laws, regulations or amendments may be delayed, resulting in detrimental reliance by foreign investors. New laws and regulations that affect existing and proposed future businesses may also be applied retroactively.

The PRC government has broad discretion in dealing with violations of laws and regulations, including levying fines, revoking business and other licenses and requiring actions necessary for compliance. In particular, licenses and permits issued or granted to us by relevant governmental bodies may be revoked at a later time by higher regulatory bodies. We cannot predict the effect of the interpretation of existing or new PRC laws or regulations on our businesses. We cannot assure you that our current ownership and operating structure would not be found in violation of any current or future PRC laws or regulations. As a result, we may be subject to sanctions, including fines, and could be required to restructure our operations or cease to provide certain services. Any of these or similar actions could significantly disrupt our business operations or restrict us from conducting a substantial portion of our business operations, which could materially and adversely affect our business, financial condition and results of operations.

***We may be adversely affected by complexity, uncertainties and changes in PRC regulation of our business and companies, including limitations on our ability to own key assets.***

The PRC government regulates the coal and bio-technology industries including foreign ownership of, and the licensing and permit requirements pertaining to, companies in these industry. These laws and regulations are relatively new and evolving, and their interpretation and enforcement involve significant uncertainty. As a result, in certain circumstances it may be difficult to determine what actions or omissions may be deemed to be a violation of applicable laws and regulations. Issues, risks and uncertainties relating to PRC government regulation of our industry include the following:

we only have contractual control over Shaanxi Suoang. We do not own it due to the restriction of foreign investment in Chinese businesses; and

uncertainties relating to the regulation of the coal product and alternative energy business in China, including evolving licensing practices, means that permits, licenses or operations at our company may be subject to challenge. This may disrupt our business, or subject us to sanctions, requirements to increase capital or other conditions or enforcement, or compromise enforceability of related contractual arrangements, or have other harmful effects on us.

The interpretation and application of existing PRC laws, regulations and policies and possible new laws, regulations or policies have created substantial uncertainties regarding the legality of existing and future foreign investments in, and the businesses and activities of, alternative energy and bio-technology businesses in China, including our business.

***In order to comply with PRC laws limiting foreign ownership of Chinese companies, we conduct our business through Shaanxi Suoang by means of contractual arrangements. If the PRC government determines that these contractual arrangements do not comply with applicable regulations, our business could be adversely affected.***

The PRC government restricts foreign investment in businesses in China. Accordingly, we operate our business in China through Shaanxi Suoang. Shaanxi Suoang holds the licenses and approvals necessary to operate our coal-based products business in China. We have contractual arrangements with Shaanxi Suoang and its shareholders that allow us to substantially control Shaanxi Suoang. We cannot assure you, however, that we will be able to enforce these contracts.

Although we believe we comply with current PRC regulations, we cannot assure you that the PRC government would agree that these operating arrangements comply with PRC licensing, registration or other regulatory requirements, with existing policies or with requirements or policies that may be adopted in the future. If the PRC government determines that we do not comply with applicable law, it could revoke our business and operating licenses, require us to discontinue or restrict our operations, restrict our right to collect revenues, require us to restructure our operations, impose additional conditions or requirements with which we may not be able to comply, impose restrictions on our business operations or on our customers, or take other regulatory or enforcement actions against us that could be harmful to our business.

***Our contractual arrangements with Shaanxi Suoang and its shareholders may not be as effective in providing control over these entities as direct ownership.***

Since PRC law limits foreign equity ownership in companies in China, we operate our business through an affiliated Chinese company, referred to herein as Shaanxi Suoang. We have no equity ownership interest in Shaanxi Suoang and rely on contractual arrangements to control and operate such business. These contractual arrangements may not be as

effective in providing control over Shaanxi Suoang as direct ownership. For example, Shaanxi Suoang could fail to take actions required for our business despite its contractual obligation to do so. If Shaanxi Suoang fails to perform under their agreements with us, we may have to rely on legal remedies under PRC law, which may not be effective. In addition, we cannot assure you that Shaanxi Suoang's shareholders would always act in our best interests.



***The Chairman of the Board of Directors of Shaanxi Suoang has potential conflicts of interest with us, which may adversely affect our business.***

Mr. Baowen Ren, our Chief Executive Officer, is also the Chairman of the Board of Directors of Shaanxi Suoang. Conflicts of interests between his duties to our company and Shaanxi Suoang may arise. As Mr. Ren is a director and executive officer of our Company, he has a duty of loyalty and care to us under Nevada law when there are any potential conflicts of interests between our company and Shaanxi Suoang. We cannot assure you, however, that when conflicts of interest arise, Mr. Ren will act completely in our interests or that conflicts of interests will be resolved in our favor. In addition, Mr. Ren could violate his legal duties by diverting business opportunities from us to others. If we cannot resolve any conflicts of interest between us and Mr. Ren, we would have to rely on legal proceedings, which could result in the disruption of our business.

### **Risks Related to Doing Business in China**

***Adverse changes in economic and political policies of the PRC government could have a material adverse effect on the overall economic growth of China, which could adversely affect our business.***

Substantially all of our business operations are conducted in China. Accordingly, our results of operations, financial condition and prospects are subject to a significant degree to economic, political and legal developments in China. China's economy differs from the economies of most developed countries in many respects, including with respect to the amount of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. While the PRC economy has experienced significant growth in the past 20 years, growth has been uneven across different regions and among various economic sectors of China. The PRC government has implemented various measures to encourage economic development and guide the allocation of resources. Some of these measures benefit the overall PRC economy, but may also have a negative effect on us. For example, our financial condition and results of operations may be adversely affected by government control over capital investments or changes in tax regulations that are applicable to us. Since early 2004, the PRC government has implemented certain measures to control the pace of economic growth. Such measures may cause a decrease in the level of economic activity in China, which in turn could adversely affect our results of operations and financial condition.

***If PRC law were to phase out the preferential tax benefits currently being extended to foreign invested enterprises and "new or high-technology enterprises" located in a high-tech zone, we would have to pay more taxes, which could have a material and adverse effect on our financial condition and results of operations.***

Under PRC laws and regulations, an enterprise may enjoy preferential tax benefits if it is registered in a high-tech zone and also qualifies as "new or high-technology enterprise". As an enterprise as well as a certified "new or high-technology enterprise" located in a high-tech zone in Xian, Shaanxi Suoang is entitled to a two-year exemption from enterprise income tax beginning from its first year of operation, followed by a 15% tax rate so long as it continues to qualify as a "new or high-technology enterprise." Shaanxi Suoang is currently subject to a 15% enterprise income tax rate for so long as its status as a "new or high-technology enterprise" remains unchanged. If the PRC law were to phase out preferential tax benefits currently granted to "new or high-technology enterprises" and technology consulting services, we would be subject to the standard statutory tax rate, which currently is 33%, and we would be unable to obtain business tax refunds for our provision of technology consulting services. Loss of these preferential tax treatments could have a material and adverse effect on our financial condition and results of operations.

***Shaanxi Suoang is subject to restrictions on making payments to us.***

Hangson, our wholly owned subsidiary, is a holding company incorporated in the British Virgin Islands and it does not have any assets or conduct any business operations other than our investments in our variable interest entity

(“VIE”) in China, Shaanxi Suoang. As a result of our holding company structure, we rely entirely on payments from Shaanxi Suoang under our contractual arrangements. The PRC government also imposes controls on the conversion of RMB into foreign currencies and the remittance of currencies out of China. We may experience difficulties in completing the administrative procedures necessary to obtain and remit foreign currency. (See the section below titled “Government control of currency conversion may affect the value of your investment.”) Furthermore, if our VIE in China incurs debt on its own in the future, the instruments governing the debt may restrict its ability to make payments. If we are unable to receive all of the revenues from our operations through these contractual or dividend arrangements, we may be unable to pay dividends on our ordinary shares.

***Uncertainties with respect to the PRC legal system could adversely affect us.***

We conduct our business primarily through Hangson and our VIE, Shaanxi Suoang. Our operations in China are governed by PRC laws and regulations. We are generally subject to laws and regulations in China. The PRC legal system is based on written statutes. Prior court decisions may be cited for reference but have limited precedential value.

However, China has not developed a fully integrated legal system and recently enacted laws and regulations may not sufficiently cover all aspects of economic activities in China. In particular, because these laws and regulations are relatively new, and because of the limited volume of published decisions and their nonbinding nature, the interpretation and enforcement of these laws and regulations involve uncertainties. In addition, the PRC legal system is based in part on government policies and internal rules (some of which are not published on a timely basis or at all) that may have a retroactive effect. As a result, we may not be aware of our violation of these policies and rules until some time after the violation. In addition, any litigation in China may be protracted and result in substantial costs and diversion of resources and management attention.

***You may experience difficulties in effecting service of legal process, enforcing foreign judgments or bringing original actions in China based on United States or other foreign laws against us, our management or the experts named in the prospectus.***

We conduct substantially all of our operations in China and the majority of our assets are located in China. In addition, all of our executive officers reside within China. As a result, it may not be possible to effect service of process within the United States or in China against us or upon our executive officers, including with respect to matters arising under U.S. federal securities laws or applicable state securities laws. Moreover, there is uncertainty that the courts of China would enforce judgments of U.S. courts against us or our directors and officers based on the civil liability provisions of the securities laws of the United States or any state, or entertain an original action brought in China based upon the securities laws of the United States or any state.

***Governmental control of currency conversion may affect the value of your investment.***

The PRC government imposes controls on the convertibility of RMB into foreign currencies and, in certain cases, the remittance of currency out of China. We receive substantially all of our revenues in RMB. Under our current structure, our income is primarily derived from payments from Shaanxi Suoang. Shortages in the availability of foreign currency may restrict the ability of our PRC subsidiaries and our affiliated entity to remit sufficient foreign currency to pay dividends or other payments to us, or otherwise satisfy their foreign currency denominated obligations. Under existing PRC foreign exchange regulations, payments of current account items, including profit distributions, interest payments and expenditures from trade-related transactions, can be made in foreign currencies without prior approval from the PRC State Administration of Foreign Exchange by complying with certain procedural requirements. However, approval from appropriate government authorities is required where RMB is to be converted into foreign currency and remitted out of China to pay capital expenses such as the repayment of bank loans denominated in foreign currencies. The PRC government may also at its discretion restrict access in the future to foreign currencies for current account transactions. If the foreign exchange control system prevents us from obtaining sufficient foreign currency to satisfy our currency demands, we may not be able to pay dividends in foreign currencies to our shareholders.

***Fluctuation in the value of RMB may have a material adverse effect on your investment.***

The value of RMB against the U.S. dollar and other currencies may fluctuate and is affected by, among other things, changes in political and economic conditions. Our revenues and costs are mostly denominated in RMB, while a significant portion of our financial assets are denominated in U.S. dollars. We rely entirely on fees paid to us by our

VIE in China. Any significant fluctuation in value of RMB may materially and adversely affect our cash flows, revenues, earnings and financial position, and the value of, and any dividends payable on, our stock in U.S. dollars. For example, an appreciation of RMB against the U.S. dollar would make any new RMB denominated investments or expenditures more costly to us, to the extent that we need to convert U.S. dollars into RMB for such purposes. An appreciation of RMB against the U.S. dollar would also result in foreign currency translation losses for financial reporting purposes when we translate our U.S. dollar denominated financial assets into RMB, as RMB is our reporting currency.

***We face risks related to health epidemics and other outbreaks.***

Our business could be adversely affected by the effects of avian flu, SARS or another epidemic or outbreak. China reported a number of cases of SARS in April 2004. In 2005, there have been reports on the occurrences of avian flu in various parts of China, including a few confirmed human cases. Any prolonged recurrence of avian flu, SARS or other adverse public health developments in China may have a material adverse effect on our business operations. These could include our ability to travel or ship our products, as well as temporary closure of our manufacturing facilities. Such closures or travel or shipment restrictions would severely disrupt our business operations and adversely affect our results of operations. We have not adopted any written preventive measures or contingency plans to combat any future outbreak of avian flu, SARS or any other epidemic.

### **Risks Related to an Investment in Our Securities**

#### ***To Date, We Have Not Paid Any Cash Dividends and No Cash Dividends Will be Paid in the Foreseeable Future.***

We do not anticipate paying cash dividends on our common stock in the foreseeable future and we may not have sufficient funds legally available to pay dividends. Even if the funds are legally available for distribution, we may nevertheless decide not to pay any dividends. We intend to retain all earnings for the company's operations.

#### ***The Application of the "Penny Stock" Rules Could Adversely Affect the Market Price of Our Common Stock and Increase Your Transaction Costs to Sell Those Shares.***

As long as the trading price of our common shares is below \$5 per share, the open-market trading of our common shares will be subject to the "penny stock" rules. The "penny stock" rules impose additional sales practice requirements on broker-dealers who sell securities to persons other than established customers and accredited investors (generally those with assets in excess of \$1,000,000 or annual income exceeding \$200,000 or \$300,000 together with their spouse). For transactions covered by these rules, the broker-dealer must make a special suitability determination for the purchase of securities and have received the purchaser's written consent to the transaction before the purchase. Additionally, for any transaction involving a penny stock, unless exempt, the broker-dealer must deliver, before the transaction, a disclosure schedule prescribed by the Securities and Exchange Commission relating to the penny stock market. The broker-dealer also must disclose the commissions payable to both the broker-dealer and the registered representative and current quotations for the securities. Finally, monthly statements must be sent disclosing recent price information on the limited market in penny stocks. These additional burdens imposed on broker-dealers may restrict the ability or decrease the willingness of broker-dealers to sell our common shares, and may result in decreased liquidity for our common shares and increased transaction costs for sales and purchases of our common shares as compared to other securities.

#### ***Our Common Shares are Thinly Traded and, You May be Unable to Sell at or Near Ask Prices or at All if You Need to Sell Your Shares to Raise Money or Otherwise Desire to Liquidate Your Shares.***

The Company cannot predict the extent to which an active public market for its common stock will develop or be sustained. However, the Company does not rule out the possibility of applying for listing on the Nasdaq National Market or other exchanges.

Our common shares have historically been sporadically or "thinly-traded" on the "Over-the-Counter Bulletin Board", meaning that the number of persons interested in purchasing our common shares at or near bid prices at any given time may be relatively small or non-existent. This situation is attributable to a number of factors, including the fact that we are a small company which is relatively unknown to stock analysts, stock brokers, institutional investors and others in the investment community that generate or influence sales volume, and that even if we came to the attention of such persons, they tend to be risk-averse and would be reluctant to follow an unproven company such as ours or purchase or recommend the purchase of our shares until such time as we became more seasoned and viable. As a consequence, there may be periods of several days or more when trading activity in our shares is minimal or non-existent, as compared to a seasoned issuer which has a large and steady volume of trading activity that will generally support continuous sales without an adverse effect on share price. We cannot give you any assurance that a broader or more active public trading market for our common stock will develop or be sustained, or that current trading levels will be sustained.

The market price for our common stock is particularly volatile given our status as a relatively small company with a small and thinly traded "float" and lack of current revenues that could lead to wide fluctuations in our share price. The price at which you purchase our common stock may not be indicative of the price that will prevail in the trading market. You may be unable to sell your common stock at or above your purchase price if at all, which may result in

substantial losses to you.

The market for our common shares is characterized by significant price volatility when compared to seasoned issuers, and we expect that our share price will continue to be more volatile than a seasoned issuer for the indefinite future. The volatility in our share price is attributable to a number of factors. First, as noted above, our common shares are sporadically and/or thinly traded. As a consequence of this lack of liquidity, the trading of relatively small quantities of shares by our shareholders may disproportionately influence the price of those shares in either direction. The price for our shares could, for example, decline precipitously in the event that a large number of our common shares are sold on the market without commensurate demand, as compared to a seasoned issuer which could better absorb those sales without adverse impact on its share price. Secondly, we are a speculative or "risky" investment due to our lack of revenues or profits to date and uncertainty of future market acceptance for our current and potential products. As a consequence of this enhanced risk, more risk-adverse investors may, under the fear of losing all or most of their investment in the event of negative news or lack of progress, be more inclined to sell their shares on the market more quickly and at greater discounts than would be the case with the stock of a seasoned issuer. The following factors may add to the volatility in the price of our common shares: actual or anticipated variations in our quarterly or annual operating results; adverse outcomes; the termination of our contractual agreements with Shaanxi Suoang; and additions or departures of our key personnel, as well as other items discussed under this "Risk Factors" section, as well as elsewhere in this Quarterly Report. Many of these factors are beyond our control and may decrease the market price of our common shares, regardless of our operating performance. We cannot make any predictions or projections as to what the prevailing market price for our common shares will be at any time, including as to whether our common shares will sustain their current market prices, or as to what effect that the sale of shares or the availability of common shares for sale at any time will have on the prevailing market price.

Shareholders should be aware that, according to SEC Release No. 34-29093, the market for penny stocks has suffered in recent years from patterns of fraud and abuse. Such patterns include (1) control of the market for the security by one or a few broker-dealers that are often related to the promoter or issuer; (2) manipulation of prices through prearranged matching of purchases and sales and false and misleading press releases; (3) boiler room practices involving high-pressure sales tactics and unrealistic price projections by inexperienced sales persons; (4) excessive and undisclosed bid-ask differential and markups by selling broker-dealers; and (5) the wholesale dumping of the same securities by promoters and broker-dealers after prices have been manipulated to a desired level, along with the resulting inevitable collapse of those prices and with consequent investor losses. Our management is aware of the abuses that have occurred historically in the penny stock market. Although we do not expect to be in a position to dictate the behavior of the market or of broker-dealers who participate in the market, management will strive within the confines of practical limitations to prevent the described patterns from being established with respect to our securities. The occurrence of these patterns or practices could increase the volatility of our share price.

***Volatility in Our Common Share Price May Subject Us to Securities Litigation.***

The market for our common stock is characterized by significant price volatility when compared to seasoned issuers, and we expect that our share price will continue to be more volatile than a seasoned issuer for the indefinite future. In the past, plaintiffs have often initiated securities class action litigation against a company following periods of volatility in the market price of its securities. We may, in the future, be the target of similar litigation. Securities litigation could result in substantial costs and liabilities and could divert management's attention and resources.

***Our corporate actions are substantially controlled by our principal shareholders and affiliated entities.***

Our principal shareholders and their affiliated entities will own approximately 85% of our outstanding ordinary shares, representing approximately 85% of our voting power. These shareholders, acting individually or as a group, could exert substantial influence over matters such as electing directors and approving mergers or other business combination transactions. In addition, because of the percentage of ownership and voting concentration in these principal shareholders and their affiliated entities, elections of our board of directors will generally be within the control of these shareholders and their affiliated entities. While all of our shareholders are entitled to vote on matters submitted to our shareholders for approval, the concentration of shares and voting control presently lies with these principal shareholders and their affiliated entities. As such, it would be difficult for shareholders to propose and have approved proposals not supported by management. There can be no assurances that matters voted upon by our officers and directors in their capacity as shareholders will be viewed favorably by all shareholders of the company.

***The Elimination of Monetary Liability Against our Directors, Officers and Employees under Nevada law and the Existence of Indemnification Rights to our Directors, Officers and Employees may Result in Substantial Expenditures by our Company and may Discourage Lawsuits Against our Directors, Officers and Employees.***

Our articles of incorporation contains a provision that eliminates the liability of our directors for monetary damages to our company and shareholders to the extent allowed under Nevada law and we are prepared to give such indemnification to our directors and officers to the extent provided by Nevada law. We may also have contractual indemnification obligations under our employment agreements that we enter into with our officers. The foregoing indemnification obligations could result in our company incurring substantial expenditures to cover the cost of settlement or damage awards against directors and officers, which we may be unable to recoup. These provisions and resultant costs may also discourage our company from bringing a lawsuit against directors and officers for breaches of their fiduciary duties, and may similarly discourage the filing of derivative litigation by our shareholders against our directors and officers even though such actions, if successful, might otherwise benefit our company and shareholders.

***Legislative Actions, Higher Insurance Costs and Potential New Accounting Pronouncements may Impact our Future Financial Position and Results of Operations.***

There have been regulatory changes, including the Sarbanes-Oxley Act of 2002, and there may potentially be new accounting pronouncements or additional regulatory rulings that will have an impact on our future financial position and results of operations. The Sarbanes-Oxley Act of 2002 and other rule changes as well as proposed legislative initiatives following the Enron bankruptcy are likely to increase general and administrative costs and expenses. In addition, insurers are likely to increase premiums as a result of high claims rates over the past several years, which we expect will increase our premiums for insurance policies. Further, there could be changes in certain accounting rules. These and other potential changes could materially increase the expenses we report under generally accepted accounting principles, and adversely affect our operating results.

***Past Activities Of The Company And Its Affiliates May Lead To Future Liability For The Company.***

Prior to our entry into the Exchange Agreement with Hangson on October 20, 2006, the Company engaged in businesses unrelated to its current operations. Although the Endo Shareholders are providing certain indemnifications against any loss, liability, claim, damage or expense arising out of or based on any breach of or inaccuracy in any of their representations and warranties made regarding such acquisition, any liabilities relating to such prior business against which Hangson is not completely indemnified may have a material adverse effect on the Company.

***The market price for our stock may be volatile.***

The market price for our stock may be volatile and subject to wide fluctuations in response to factors including the following:

- actual or anticipated fluctuations in our quarterly operating results;
- changes in financial estimates by securities research analysts;
- conditions in bio-technology and coal-based product markets;
- changes in the economic performance or market valuations of other alternative energy and coal-based products companies;
- announcements by us or our competitors of new products, acquisitions, strategic partnerships, joint ventures or capital commitments;
- addition or departure of key personnel;
- fluctuations of exchange rates between RMB and the U.S. dollar;
- intellectual property litigation; and
- general economic or political conditions in China.

In addition, the securities market has from time to time experienced significant price and volume fluctuations that are not related to the operating performance of particular companies. These market fluctuations may also materially and adversely affect the market price of our stock.





***We may need additional capital, and the sale of additional shares or other equity securities could result in additional dilution to our shareholders.***

We believe that our current cash and cash equivalents, anticipated cash flow from operations and the net proceeds from this offering will be sufficient to meet our anticipated cash needs for the near future. We may, however, require additional cash resources due to changed business conditions or other future developments, including any investments or acquisitions we may decide to pursue. If our resources are insufficient to satisfy our cash requirements, we may seek to sell additional equity or debt securities or obtain a credit facility. The sale of additional equity securities could result in additional dilution to our shareholders. The incurrence of indebtedness would result in increased debt service obligations and could result in operating and financing covenants that would restrict our operations. We cannot assure you that financing will be available in amounts or on terms acceptable to us, if at all.

***If we fail to maintain an effective system of internal controls, we may not be able to accurately report our financial results or prevent fraud.***

We are subject to reporting obligations under the U.S. securities laws. The Securities and Exchange Commission, or the SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring every public company to include a management report on such company's internal controls over financial reporting in its annual report, which contains management's assessment of the effectiveness of the company's internal controls over financial reporting. In addition, an independent registered public accounting firm must attest to and report on management's assessment of the effectiveness of the company's internal controls over financial reporting. Our management may conclude that our internal controls over our financial reporting are not effective. Moreover, even if our management concludes that our internal controls over financial reporting are effective, our independent registered public accounting firm may still decline to attest to our management's assessment or may issue a report that is qualified if it is not satisfied with our controls or the level at which our controls are documented, designed, operated or reviewed, or if it interprets the relevant requirements differently from us. Our reporting obligations as a public company will place a significant strain on our management, operational and financial resources and systems for the foreseeable future. Effective internal controls, particularly those related to revenue recognition, are necessary for us to produce reliable financial reports and are important to help prevent fraud. As a result, our failure to achieve and maintain effective internal controls over financial reporting could result in the loss of investor confidence in the reliability of our financial statements, which in turn could harm our business and negatively impact the trading price of our stock. Furthermore, we anticipate that we will incur considerable costs and use significant management time and other resources in an effort to comply with Section 404 and other requirements of the Sarbanes-Oxley Act.

***We will incur increased costs as a result of being a public company.***

As a public company, we will incur significant legal, accounting and other expenses that we did not incur as a private company. In addition, the Sarbanes-Oxley Act, as well as new rules subsequently implemented by SEC have required changes in corporate governance practices of public companies. We expect these new rules and regulations to increase our legal, accounting and financial compliance costs and to make certain corporate activities more time-consuming and costly. In addition, we will incur additional costs associated with our public company reporting requirements. We are currently evaluating and monitoring developments with respect to these new rules, and we cannot predict or estimate the amount of additional costs we may incur or the timing of such costs.

### **Item 3. Controls And Procedures**

(a) *Evaluation of disclosure controls and procedures.* As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as

amended. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the applicable period to ensure that the information required to be disclosed by the Company in reports that it files or submits under the Exchange Act (i) is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and (ii) is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

(b) *Changes in internal controls over financial reporting.* There was no change in our internal control over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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## PART II - OTHER INFORMATION

### Item 1. Legal Proceedings.

None.

### Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

### Item 3. Defaults upon Senior Securities.

None.

### Item 4. Submission of Matters to a Vote of Securities Holders.

None.

### Item 5. Other Information.

None.

### Item 6. Exhibits

<b>Exhibit Number</b>	<b>Description</b>
2.1	Share Exchange Agreement between Endo Networks, Inc., Endo Majority Shareholders, Hangson Ltd. and the Hangson Shareholders dated October 18, 2006 (1)
3.1	Articles of Incorporation of Endo Networks, Inc., a Nevada corporation, as amended. (3)
3.2	Bylaws of Endo Networks, Inc. (3)
3.3	Text of Amendment to our Bylaws (4)
10.1	Asset and Share Purchase Agreement between Registrant and Peter B. Day (for Endo Canada) (2)
10.2	Contract for Technology Transfer between Shaanxi Suo'ang Biological Science & Technology Co., Ltd. and HanZhongWeiDa Commercial Company Limited dated December 25, 2006 (5)
10.3	Contract for Technology Transfer between Shaanxi Suo'ang Biological Science & Technology Co., Ltd. and HanZhongWeiDa Commercial Company Limited dated January 10, 2007 (5)
31.1	Section 302 Certification by the Corporation's Chief Executive Officer *
31.2	Section 302 Certification by the Corporation's Chief Financial Officer *
32.1	Section 906 Certification by the Corporation's Chief Executive Officer *

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- 32.2 Section 906 Certification by the Corporation's Chief Financial Officer \*
- 99.1 Consulting Services Agreement by and between Hangson Limited and Shaanxi Suo'ang Biological Science & Technology Co., Ltd. dated August 18, 2006 (3)
- 99.2 Equity Pledge Agreement by and between Hangson Limited and Shaanxi Suo'ang Biological Science & Technology Co., Ltd. ("Shaanxi Suoang") and Shaanxi Suoang's Majority Shareholders dated August 18, 2006 (3)
- 99.3 Operating Agreement by and between Hangson Limited and Shaanxi Suo'ang Biological Science & Technology Co., Ltd. ("Shaanxi Suoang") and Shaanxi Suoang's Majority Shareholders dated August 18, 2006 (3)

- 99.4 Proxy Agreement by and between Hangson Limited and Shaanxi Suo'ang Biological Science & Technology Co., Ltd. ("Shaanxi Suoang") and Shaanxi Suoang's Majority Shareholders dated August 18, 2006 (3)
- 99.5 Option Agreement between Hangson Limited and Shaanxi Suo'ang Biological Science & Technology Co., Ltd. ("Shaanxi Suoang") and Shaanxi Suoang's Majority Shareholders dated August 18, 2006 (3)
- 99.6 Agreement by and between Shaanxi Suo'ang Biological Science and Technology Co. Ltd. and Hanzhong Si Xiong Ke Chuang Business Co. Ltd. (3)
- 99.7 Supplementary Agreement by and between Shaanxi Suo'ang Biological Science and Technology Co. Ltd. and Hanzhong Si Xiong Ke Chuang Business Co. Ltd. dated March 25, 2007 (5)

\* Filed herewith.

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- (1) Filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on October 18, 2006 and incorporated herein by reference.
- (2) Filed as Exhibit A of Registrant's Schedule 14A filed with the SEC on August 8, 2006 and incorporated herein by reference.
- (3) Filed as Exhibits to the Registrant's Current Report on Form 8-K filed with the SEC on October 26, 2006 and incorporated herein by reference.
- (4) Filed as an Exhibit to the Registrant's Current Report on Form 8-K filed with the SEC on November 17, 2006 and incorporated herein by reference.
- (5) Filed as Exhibits to the Registrant's Annual Report on Form 10-KSB filed with the SEC on May 3, 2007 and incorporated herein by reference.

**[SIGNATURES PAGE FOLLOWS]**

**SIGNATURES**

In accordance with the requirements of the Exchange Act, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**CHINA WEST COAL ENERGY INC.**  
(Registrant)

Date: May 21, 2007

By: /s/ Baowen Ren

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Baowen Ren  
Chief Executive Officer