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ADVANCED BATTERY TECHNOLOGIES, INC.
Form 10QSB
August 21, 2006

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

FORM 10-QSB

Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 30, 2006

Transition Report pursuant to 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period to

Commission File No. 0-13337

ADVANCED BATTERY TECHNOLOGIES, INC.

(Name of Small Business Issuer in Its Charter)

DELAWARE

22-2497491

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

21 West 39th Street, Suite 2A, New York, NY 10018

(Address of principal executive offices)

212-391-2752

(Issuer's telephone number, including area code)

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

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

The number of shares outstanding of each of the issuer's class of equity as of the latest practicable date is stated below:

| Title of each class of Common Stock | Outstanding as of August 18, 2006 |
|-------------------------------------|-----------------------------------|
| ----- | ----- |
| Common Stock, \$0.001 par value | 49,127,710 |

Transitional Small Business Disclosure Format (check one): Yes No

PART I - FINANCIAL INFORMATION

ADVANCED BATTERY TECHNOLOGIES, INC.

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CONSOLIDATED BALANCE SHEET

| | June 30, 2006 (Unaudited) USD ----- |
|---|--|
| ASSETS | |
| Current assets | |
| Cash and cash equivalents | 1,514 |
| Accounts receivable | 2,841,743 |
| Inventories | 314,054 |
| Prepayments, deposits and other receivable | 824,773 |
| | ----- |
| Total current assets | 3,982,084 |
| Property, plant and equipment, net | 7,708,438 |
| Construction in process | 3,966,824 |
| Deposits for acquisition of property, plant and equipment | 1,833 |
| Rights to use land and power, net | 420,030 |
| Patents, net | 103,315 |
| Prepaid expenses | 1,299,841 |
| | ----- |
| Total assets | 17,482,365 ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | |
| Current liabilities | |
| Accounts payable | 240,677 |
| Accrued expenses and other payable | 1,025,151 |
| Short-term bank and other borrowings (Note 7) | 3,848,157 |
| Customer deposits | 107,637 |
| Welfare payable | 145,719 |
| | ----- |
| Total current liabilities | 5,367,341 |
| Stockholders' equity | |
| Common stock (Note 8) | 49,128 |
| Additional paid-in capital (Note 9) | 13,937,014 |
| Accumulated deficit | (2,053,706) |
| Accumulated other comprehensive income | 182,588 |
| | ----- |
| Total stockholders' equity | 12,115,024 |
| | ----- |
| Total liabilities and stockholders' equity | 17,482,365 ===== |

See the accompanying notes to the unaudited consolidated financial statements

-2-

ADVANCED BATTERY TECHNOLOGIES, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

| | Three months ended June 30, | | Six months ended June 30, | |
|---------------|-----------------------------|-------------|---------------------------|-------------|
| | 2006 | 2005 | 2006 | 2005 |
| | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) |
| | USD | USD | USD | USD |
| | ----- | | ----- | |
| Revenue | 3,175,452 | 236,360 | 5,084,449 | 267,767 |
| Cost of sales | (2,133,663) | (156,205) | (3,340,483) | (180,370) |

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| | | | | |
|---|-----------|-----------|-----------|-----------|
| Gross profit | 1,041,789 | 80,155 | 1,743,966 | 87,397 |
| Other income | - | 578 | - | 1,379 |
| Selling expenses | (3,961) | (5,255) | (12,578) | (8,251) |
| General and administrative expenses | (367,930) | (502,237) | (704,482) | (944,076) |
| Interest expense | (70,496) | (61,690) | (131,384) | (110,406) |
| Income/(loss) before minority interests | 599,402 | (488,449) | 895,522 | (973,957) |
| Minority interests | - | 31,529 | - | 80,746 |
| Net income/(loss) | 599,402 | (456,920) | 895,522 | (893,211) |
| Net income/(loss) per share | | | | |
| Basic and diluted (Note 10) | 0.013 | (0.019) | 0.020 | (0.039) |

See the accompanying notes to the unaudited consolidated financial statements

-3-

ADVANCED BATTERY TECHNOLOGIES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Six months ended June 30, | |
|---|---------------------------|-------------|
| | 2006 | 2005 |
| | (Unaudited) | (Unaudited) |
| | USD | USD |
| | ----- | ----- |
| Cash flows from operating activities: | | |
| Net income/(loss) | 895,522 | (893,211) |
| Adjustments to reconcile net income/(loss) to net cash provided by/(used in) operating activities : | | |
| Depreciation and amortization | 335,806 | 119,377 |
| Amortization of prepaid expenses | 177,218 | 677,052 |
| Stock compensation expenses | 164,178 | - |
| Minority interests | - | (80,746) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (862,427) | 258 |
| Inventories | 69,310 | (132,944) |
| Prepayments, deposits and other receivable | 105,738 | (833,624) |
| Accounts payable, accrued expenses and other payable | (606,069) | 78,287 |
| Customer deposits | (15,598) | 579,317 |
| Welfare payable | 27,283 | 22,223 |
| | ----- | ----- |
| Net cash provided by/(used in) operating activities | 290,961 | (464,011) |
| | ----- | ----- |
| Cash flows from investing activities: | | |
| Purchase of property, plant and equipment | (8,801) | (1,375,616) |
| Additions to construction in process | - | (1,148,454) |
| | ----- | ----- |
| Net cash used in investing activities | (8,801) | (2,524,070) |

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| | | |
|---|-----------|-----------|
| | ----- | ----- |
| Cash flows from financing activities: | | |
| Net proceeds from issuance of common stocks | - | 1,691,542 |
| Decrease in loan payable | (296,041) | (27,788) |
| Decrease in car loan | (2,324) | - |
| Increase in long-term debts | - | 594,116 |
| | ----- | ----- |
| Net cash (used in)/provided by financing activities | (298,365) | 2,257,870 |
| | ----- | ----- |
| Net decrease in cash and cash equivalents | (16,205) | (730,211) |
| Effect of foreign exchange rate changes | 11 | 2,181 |
| Cash and cash equivalents, beginning of period | 17,708 | 758,015 |
| | ----- | ----- |
| Cash and cash equivalents, end of period | 1,514 | 29,985 |
| | ===== | ===== |

See the accompanying notes to the unaudited consolidated financial statements

-4-

ADVANCED BATTERY TECHNOLOGIES, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF THE COMPANY

Advanced Battery Technologies, Inc. ("ABAT" or the "Company") was incorporated in the State of Delaware on January 16, 1984.

The Company is engaged in the business of designing, manufacturing and marketing of rechargeable polymer lithium-ion batteries through its subsidiaries, Cashtech Investment Limited ("Cashtech") and Heilongjiang Zhong Qiang Power-Tech Co., Ltd. ("ZQ Power-Tech"). Cashtech is a British Virgin Islands corporation and ZQ Power-Tech is a limited liability company established in the People's Republic of China (the "PRC") in which Cashtech originally owned 70% interest as of December 31, 2005. On January 6, 2006, Mr. Zhiguo Fu ("Mr. Fu"), the chairman of ABAT, transferred to Cashtech shares of ZQ Power-Tech representing 30% of the outstanding shares of ZQ Power-Tech. As a result of the transfer, Cashtech now owns 100% of the capital stock of ZQ Power-Tech. Details of the transaction are set out in note 5.

2. BASIS OF PRESENTATION

- (i) The accompanying consolidated financial statements of the Company and its subsidiaries (the "Group") have been prepared in accordance with generally accepted accounting principles in the United States of America for interim consolidated financial information. Accordingly, they do not include all the information and notes necessary for comprehensive consolidated financial statements.

In the opinion of the management of ABAT, all adjustments necessary for a fair presentation of the financial position and the results of operations and cash flows for the interim periods have been included. Interim results are not necessarily indicative of results for a full year.

- (ii) The Group has accumulated deficit as of June 30, 2006. However, based on the substantial backlog of orders of approximately USD6.4 million that the Group has accumulated and the Group had attained

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net income for the current interim period which indicated an improvement to the current operations, the management of the Group believes that the backlog of orders and improved operation results will generate sufficient revenue and cash flows to enable the Group to continue as a going concern.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies followed by the Company are set forth in the section "Summary of significant accounting policies" of the consolidated financial statements of the Company included in the Company's Form 10-KSB submitted to the United States Securities and Exchange Commission on April 14, 2006.

-5-

ADVANCED BATTERY TECHNOLOGIES, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

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

Recent accounting pronouncements

In February 2006, the Financial Accounting Standards Board issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments, which amends SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities ("SFAS No. 155"), and SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. SFAS No. 155 simplifies the accounting for certain derivatives embedded in other financial instruments by allowing them to be accounted for as a whole if the holder elects to account for the whole instrument on a fair value basis. SFAS No. 155 also clarifies and amends certain other provisions of SFAS No. 133 and SFAS No. 140. SFAS No. 155 is effective for all financial instruments acquired, issued or subject to a remeasurement event occurring in fiscal years beginning after September 15, 2006. Earlier adoption is permitted, provided the Company has not yet issued financial statements, including for interim periods, for that fiscal year. We do not expect the adoption of SFAS No. 155 to have a material impact on our consolidated financial position, results of operations or cash flows as the Company currently has no financial instruments within the scope of SFAS No. 155. The Company does not anticipate the adoption of SFAS No. 155 to have a material impact as it currently has no financial instruments within the scope of SFAS No. 155.

In March 2006, the Financial Accounting Standards Board issued SFAS No. 156, Accounting for Servicing of Financial Assets, which amends SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. SFAS No. 156 requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value. The company can elect subsequent fair value measurement of its servicing assets and servicing liabilities by class, thus simplifying its accounting and providing for income statement recognition of the potential offsetting changes in fair value of the servicing assets, servicing liabilities, and related derivative instruments. SFAS No. 156 is effective for all financial instruments acquired, issued or subject to a remeasurement event occurring in fiscal years beginning after September 15, 2006. Earlier adoption is permitted as of the beginning of an entity's fiscal year, provided the company has not yet issued financial statements, including interim financial statements, for any period of that fiscal year. The Company does not early adopt SFAS No. 156.

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4. INCOME TAXES

No provision for income tax is made as the Company's operating subsidiary in the PRC is entitled to an income tax holiday. The subsidiary is eligible to the income tax holiday of 5 years commencing from its first profit-making year.

5. ACQUISITION OF MINORITY INTERESTS IN ZQ POWER-TECH

As mentioned in note 1, Mr. Fu transferred his 30% interest in ZQ Power-Tech to Cashtech in exchange for 11,780,594 shares of the Company's common stock.

The amount of USD1,865,456, which represents the share of net assets by Mr. Fu in ZQ Power-Tech in excess of par value of the shares issued, was included in additional paid-in capital.

-6-

ADVANCED BATTERY TECHNOLOGIES, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

6. ACQUISITION OF A PATENT

On January 10, 2006, ABAT issued 4,400,000 shares of common stock to Mr. Fu in return for a patent transferred to ZQ Power-Tech by him.

The patent was recognized at the par value of the shares issued due to the nature of transaction being between related parties.

7. SHORT-TERM BANK AND OTHER BORROWINGS

Short-term bank and other borrowings consist of the following:

| | USD |
|----------------------------------|-----------|
| Bank borrowings (Note 7(i)) | 3,372,300 |
| Loan payable (Note 7(ii)) | 374,700 |
| Other loan payable (Note 7(iii)) | 101,157 |
| | ----- |
| | 3,848,157 |
| | ===== |

(i) The bank loans have maturity of less than one year from June 30, 2006 and are secured by the Group's buildings and right to use land. Loan amounts of USD2,498,000, USD624,500 and USD249,800 bear interest at 8.064%, 6.045% and 5.655% per annum respectively.

(ii) The loan payable represents an interest-free and unsecured demand loan from Shuangcheng National Owned Assets Operation Ltd. with on fixed term of repayment.

(iii) The other loans are due to non-related third parties and are interest-free, unsecured and repayable on demand.

8. COMMON STOCK

| | No. of shares | Amount |
|---------------|---------------|--------|
| | | USD |
| Authorized :- | ----- | |

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| | | |
|---|------------|--------|
| Common stock at USD0.001 par value | 60,000,000 | 60,000 |
| | ===== | ===== |
| Issued and outstanding :- | | |
| At January 1, 2006 | 25,337,116 | 25,337 |
| Shares issued for acquisition of minority interests in ZQ Power-Tech (Note 5) | 11,780,594 | 11,781 |
| Shares issued for acquisition of a patent (Note6) | 4,400,000 | 4,400 |
| Shares issued to consultants (Note 8(i)) | 60,000 | 60 |
| Shares issued to employees (Note 8(ii)) | 7,550,000 | 7,550 |
| | ----- | ----- |
| At June 30, 2006 | 49,127,710 | 49,128 |
| | ===== | ===== |

-7-

ADVANCED BATTERY TECHNOLOGIES, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. COMMON STOCK (CONT'D)

Note :-

- (i) 60,000 shares of common stock were issued as full compensation to three consultants for the provision of research and development services to the Company. An amount of USD34,740, which represents the aggregate fair value of the shares issued in excess of par value, was included in additional paid-in capital.
- (ii) 7,550,000 shares of common stock were issued to twenty-five employees for the provision of future services to the Company. 1,530,000 shares of common stock was granted to five employees under the 2004 Equity Incentive Plan and the remaining 6,020,000 shares were granted to twenty employees under the 2006 Equity Incentive Plan.

9. ADDITIONAL PAID-IN CAPITAL

Included in additional paid-in capital is :-

- (i) An amount of USD1,865,456 which relates to the acquisition of minority interests in ZQ Power-Tech (Note 5);
- (ii) An amount of USD34,740 which relates to the issuance of shares to consultants (Note 8(i));
- (iii) A debit balance of USD1,804,733 which represents the balance of unearned stock compensation. Following the adoption of FAS123R, any unearned stock compensation should be netted against additional paid-in capital and be recognized over the remaining period with a debit to statement of operations as compensation expenses and a credit to additional paid-in capital; and
- (iv) An amount of USD55,428 which relates to the issuance of stocks to employees (Note 8(ii)).

-8-

ADVANCED BATTERY TECHNOLOGIES, INC.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

10. NET INCOME/(LOSS) PER SHARE - BASIC AND DILUTED

The basic and diluted net income/(loss) per share is calculated using the net income/(loss) and the weighted average number of common stock outstanding during both interim periods. The Company has no dilutive instruments and accordingly, the basic and diluted net income/(loss) per share are the same.

| | Three months ended June 30, | | Six months ended June 30, | |
|---|-----------------------------|--------------|---------------------------|--------------|
| | 2006 | 2005 | 2006 | 2005 |
| Net income/(loss) | USD599,402 | USD(456,920) | USD895,522 | USD(893,211) |
| | ===== | ===== | ===== | ===== |
| Weighted average number of shares outstanding | 44,664,450 | 24,599,753 | 44,015,591 | 23,050,807 |
| | ===== | ===== | ===== | ===== |
| Net income/(loss) per share | USD0.013 | USD(0.019) | USD0.020 | USD(0.039) |
| | ===== | ===== | ===== | ===== |

11. SUPPLEMENTAL CASH FLOW INFORMATION

| | Six months ended June 30, | |
|---------------|---------------------------|---------|
| | 2006 | 2005 |
| | USD | USD |
| Interest paid | 131,384 | 110,406 |
| | ===== | ===== |

Other than the above-mentioned information, during the six months ended June 30, 2006, there were non-cash transactions regarding the issuance of the Company's common stock for the acquisitions of minority interests in ZQ Power-Tech (Note 5) and a patent (Note 6), and for the provision of services by certain consultants (Note 8(i)) and employees (Note 8(ii)) respectively.

12. EQUITY INCENTIVE PLAN

- (i) The Company adopted the 2004 Equity Incentive Plan (the "2004 Plan") on August 24, 2004. The purpose of the 2004 Plan is to promote the success and enhance the value of the Company by linking the personal interests of the participants of the 2004 Plan to those of the Company's shareholders, and by providing the participants with an incentive for outstanding performance. The 2004 Plan is further intended to attract and retain the services of the participants upon whose judgment, interest, and special efforts the successful operation of the Group is dependent. The Company has reserved 5,000,000 shares of common stock for the options and awards under the 2004 Plan.

Subject to the terms and provisions of the 2004 Plan, the Board of Directors, at any time and from time to time, may grant shares of stock to eligible persons in such amounts and upon such terms and conditions as the Board of Directors shall determine.

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ADVANCED BATTERY TECHNOLOGIES, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

12. EQUITY INCENTIVE PLAN (CONT'D)

The Committee appointed by the Board of Directors to administer the 2004 Plan shall have the authority to determine all matters relating to the options to be granted under the plan including selection of the individuals to be granted awards or stock options, the number of stocks, the date, the termination of the stock options or awards, the stock option term, vesting schedules and all other terms and conditions thereof.

The Company measures the compensation cost from share-based payment arrangements with employees with reference to the trading price of the Company's common stock as quoted on the OTC Bulletin Board ("OTCBB") on the date of grant.

A summary of the status of the Company's unearned stock compensation as of June 30, 2006, and changes during the six months ended June 30, 2006, is presented below:

| | USD |
|--|-----------|
| Unearned stock compensation as of January 1, 2006 | 1,905,933 |
| Unearned stock compensation granted | 887,400 |
| Compensation expenses debited to statement of operations with a credit to additional paid-in capital | (115,071) |
| | ----- |
| Unearned stock compensation as of June 30, 2006 | 2,678,262 |
| | ===== |

The unearned stock compensation granted during the current period relates to 1,530,000 shares of common stock granted to five employees (note 8(ii)). The weighted-average grant-date fair value per share is USD0.58. The total unearned stock compensation as of June 30, 2006 is expected to be recognized over a weighted-average period of 9.92 years.

In addition, the compensation cost capitalized as an asset in relation to shares issued under the 2004 Plan in prior years and current period was USD1,299,842. Included were the 60,000 shares of common stock entitled by the consultants as disclosed in note 8(i) and the weighted-average grant-date fair value per share is USD0.58. The compensation cost capitalized was classified as prepaid expenses in the consolidated balance sheet and the amortization for the six months ended June 30, 2006 was USD177,218. The prepaid expenses is expected to be recognized over a weighted-average period of 4.5 years.

- (ii) The Company adopted the 2006 Equity Incentive Plan (the "2006 Plan") on April 24, 2006.

The 2006 Plan became effective on April 18, 2006. Its purpose is to promote the success and enhance the value of the Company by linking the personal interests of the participants to those of the Company's shareholders, and by providing participants with an incentive for outstanding performance. The 2006 Plan is further intended to attract and retain the services of the participants upon whose judgment, interest and special efforts the successful

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operation of the Company and its subsidiaries is dependent.

-10-

ADVANCED BATTERY TECHNOLOGIES, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

12. EQUITY INCENTIVE PLAN (CONT'D)

The number of shares available for grant under the 2006 Plan shall not exceed 8,000,000 shares. Shares of stock and options may be granted to the eligible persons at the discretion of the Company's Board of Directors or the Committee administering the plan. Incentive stock options ("ISO"), nonqualified stock options ("NQSO"), or a combination thereof may be granted but ISOs can only be granted to the Company's employees. The Committee can also grant shares of restricted stock or performance shares (a performance share is equivalent in value to a share of stock) to eligible persons at any time and from time to time.

The exercise price for each ISO awarded under the 2006 Plan shall be equal to 100% of the fair market value of a share on the date the option is granted and be 110% of the fair market value if the eligible person owns stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or of its parent or subsidiary corporations. The exercise price of a NQSO shall be determined by the Committee in its sole discretion.

Each option shall expire at such time as the Committee determines at the time of grant and no option shall be exercisable later than the tenth anniversary date of its grant. The eligible person who owns stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or of its parent or subsidiary corporations shall exercise his/her option before the fifth anniversary date of its grant.

Options shall vest at such times and under such terms and conditions as determined by the Committee; provided, however, unless a different vesting period is provided by the Committee at or before the grant of an option, the options will vest on the first anniversary of the grant. Options granted under the 2006 Plan shall be exercisable at such times and be subject to such restrictions and conditions as the Committee shall in each instance approve, which need not be the same for each grant or for each participant.

No award may be made under the 2006 Plan after December 31, 2015.

The Company measures the compensation cost from share-based payment arrangements with employees with reference to the trading price of the Company's common stock as quoted on the OTCBB on the date of grant.

A summary of the status of the Company's unearned stock compensation as of June 30, 2006, and changes during the six months ended June 30, 2006, is presented below:

| | USD |
|---|------------|
| Unearned stock compensation as of January 1, 2006 | ----- - |
| Unearned stock compensation granted | 3,491,600 |

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| | |
|--|-----------|
| Compensation expenses debited to statement of operations with a credit to additional paid-in capital | (49,107) |
| | ----- |
| Unearned stock compensation as of June 30, 2006 | 3,442,493 |
| | ===== |

-11-

ADVANCED BATTERY TECHNOLOGIES, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

12. EQUITY INCENTIVE PLAN (CONT'D)

The unearned stock compensation granted during the current period relates to 6,020,000 shares of common stock granted to five employees (note 8(ii)). The weighted-average grant-date fair value per share is USD0.58. The total unearned stock compensation as of June 30, 2006 is expected to be recognized over a weighted-average period of 15.3 years.

(iii) The total compensation cost for share-based payment arrangements as detailed in notes 12(i) and 12(ii) was as follows:

| | USD |
|----------------------------------|---------|
| Amortization of prepaid expenses | 177,218 |
| Stock compensation expenses | 164,178 |
| | ----- |
| | 341,396 |
| | ===== |

(iv) Other than the transactions as detailed in notes 12(i) and 12(ii), no options or awards have been made, exercised or lapsed during the six months ended June 30, 2006 under the 2004 Plan and the 2006 Plan.

13. COMMITMENTS

At of June 30, 2006, the Group had agreed to pay USD136,356 to Harbin Institute of Technology for the research and development of polymer lithium-ion batteries for motor vehicles.

14. WARRANTIES

The Group warrants that all batteries manufactured by it will be free from defects in material and workmanship under normal use for a period of one year from the date of shipment. The Group's experience for costs and expenses in connection with such warranties has been minimal and during the three months ended June 30, 2006, no amounts have been considered necessary to reserve for warranty costs.

15. RELATED PARTY TRANSACTIONS

Apart from the acquisitions of minority interests in ZQ Power-Tech and a patent from Mr. Fu as referred to in notes 5 and 6 respectively, during the period ended June 30, 2006, the Group had no other material transactions with its related parties.

-12-

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Item 1. Management's Discussion and Analysis or Plan of Operation Forward Looking Statements

The information in this discussion contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements include statements regarding our capital needs, business strategy and expectations. Any statements contained herein that are not statements of historical facts may be deemed to be forward-looking statements. Readers are cautioned that there are risks and uncertainties which may cause actual future results to differ from the results anticipated in these forward-looking statements. A detailed discussion of some of the risks that may cause such a difference has been set forth in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2005 in the section numbered "Item 6" under the heading "Risk Factors That May Affect Future Results." Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's opinions only as of the date hereof. We disclaim any obligation to publicly update these statements, or disclose any difference between its actual results and those reflected in these statements.

Results of Operations

During the year ended December 31, 2003 the activities of our operating subsidiary, "ZQ Power-Tech," were focused on development of its product line and the build-out of its manufacturing facility. ZQ Power-Tech recorded its first significant revenues in the first half of 2004, ending June 30, 2004. For that six month period, it recorded sales totaling \$968,675.

The Company's level of sales fell in the second half of 2004 to \$222,834. The reduction occurred primarily because the Company obtained the financing needed to complete additional factory facilities at ZQ Power-Tech's campus in Heilongjiang. Production was reduced to minimal or none, as management focused on doubling the Company's production capacity and training the necessary personnel. Between 2004 and the end of 2005, the number of employees at our facility increased from 300 to 1260, as we more than doubled our production capacity to its current level of \$40 million per year. We now have two buildings ("A" and "B") in full production, and continue to outfit buildings "C" and "D."

In the fall of 2005 we returned to full production, shipping \$2,618,165 of product in the fourth quarter, to produce total revenues in 2005 of \$4,222,960. Our increased level of activity continued into the first six months of 2006, during which we recorded \$5,084,449 in revenue. By comparison, our revenue during the first six months of 2005 was only \$267,767, as we were focused on building our facility at that time. Since we currently have a backlog of approximately \$6.4 million, we expect to maintain the level of operations that we achieved in the first six months of 2006. We do not include in our current backlog the \$21 million order placed by Aiyingsi in 2004, since the delivery times for that order have been delayed indefinitely.

-13-

ZQ Power-Tech realized a 34% gross margin on its sales in the six months ended June 30, 2006, approximating the 33% ratio that we realized in the first six months of 2005. Our gross margin ratio in the future will depend considerably upon which of ZQ Power-Tech's products are dominating sales. However we do expect our operations in 2006 and beyond to be more efficient than they have been in the past, as we are

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implementing advanced production management systems. We are also gaining experience with our new production lines, which are enabling us to improve the efficiency of the lines and to discover lower-cost sources of raw materials for our products.

Our general and administrative expense fell from \$944,076 in the first six months of 2005 to \$704,482 (14% of revenue) in the first six months of 2006. The reduction reflected, in part, our efforts to increase efficiencies in our operations. The greatest part of the reduction, however, was attributable to the fact that general and administrative expense in 2006 included a non-cash expense of \$677,052 that was primarily attributable to amortization of prepaid consulting fees that were paid by issuing common stock to the consultants. At June 30, 2006 there remained on the Company's balance sheets \$1,299,841 in prepaid expenses that are attributable to prepaid consulting fees to the Company's consultants. We amortized \$177,218 of prepaid expenses and recognized \$164,178 stock compensation expenses during the first six months of 2006. The remaining prepaid expenses and unearned stock compensation will be amortized and recognized over the next few years.

The Company's revenue less expenses produced an income of \$895,522, compared to a loss before minority interest of \$973,957 in the first six months of 2005. In 2005, however, Advanced Battery owned only 70% of ZQ Power-Tech. For that reason, our net loss for the six months ended June 30, 2005 was reduced by \$80,746, representing the 30% of the net loss of ZQ Power-Tech that we did not own. In January 2006 our Chairman, Fu Zhiguo, transferred the remaining 30% of ZQ Power-Tech into the Company's control. In 2006 and hereafter, therefore, we will be able to include 100% of the net income of ZQ Power-Tech in the net income for Advanced Battery Technologies.

Liquidity and Capital Resources

Until December 2004, the development and initial operations of ZQ Power-Tech were financed primarily by contributions to capital made by Fu Zhiguo, the Company's Chairman. On December 1, 2004, ZQ Power-Tech entered into a Loan Agreement with China Financial Bank, and received a loan of 20 million RMB (approximately \$2.4 million). The Loan Agreement requires that the principal be paid in a balloon in November 2006. Interest at 8.064% per annum is payable monthly. \$1.9 million of the obligation is secured by a pledge of ZQ Power-Tech's manufacturing facilities; the remainder of the debt is secured by a pledge of our realty assets.

At June 30, 2006 the Company had a working capital deficit of \$1,385,257, an improvement of \$1,537,514 since December 31, 2005. The primary reason for the decrease in the deficit was the fact that we used the net income in the first six months to reduce our accounts payable by 76%. In addition, we determined that we were entitled to a tax refund of \$206,699 from the government of China, which we received in the second quarter of 2006.

-14-

Although our net income for the first six months of 2006 was \$895,522, our operations provided only \$290,961 in cash for the period, compared to a reduction in cash of \$464,011 in the first six months of 2005. The primary reason for this disparity was the fact that our accounts receivable increased during the recent six month period by nearly the amount of our net income. As we seek new market share, we are tolerating extended payments from a number of our customers, particularly

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our primary distributor, who is allowed 120 days to pay its receivables. For this reason, the growth in our net income will not produce a proportionate increase in cash until we are able to secure better payment terms from our customers.

Despite its negative working capital, ZQ Power-Tech has sufficient liquidity to fund its near-term operations. The principal capital resource available is \$12,097,125 in property, plant and equipment, construction in process, and real property rights, which ZQ Power-Tech owns subject only to the China Financial Bank lien for \$3.4 million. Based on the substantial backlog of orders that ZQ Power-Tech has accumulated, it believes that additional secured financing will be available to it on favorable terms when needed. Until then, if short-term cash shortages occur, Mr. Fu has committed to provide financing as needed.

Based upon the financial resources available to ZQ Power-Tech, management believes that it has sufficient capital and liquidity to sustain operations for the foreseeable future.

Item 3. Controls and Procedures

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 of the end of the period covered by this report. The evaluation was undertaken in consultation with our accounting personnel. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are currently effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. As we develop new business or if we engage in an extraordinary transaction, we will review our disclosure controls and procedures and make sure that they remain adequate.

There were no changes in the internal controls over our financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

-15-

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

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

None.

Item 3. Defaults Upon Senior Securities

Item 4. Submission of Matters To a Vote of Security Holders

Item 5. Other Information

Item 6. Exhibits

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Exhibits

- 31.1 Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

-16-

SIGNATURES

In accordance with Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ADVANCED BATTERY TECHNOLOGIES, INC.

Date: August 18, 2006

By: /s/ Zhiguo Fu

Name: Zhiguo Fu
Title: Chief Executive Officer

Date: August 18, 2006

By: /s/ Guohua Wan

Name: Guohua Wan
Title: Chief Financial Officer

-17-