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PENGE CORP  
Form 10QSB  
February 13, 2007

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

FORM 10-QSB

/X/ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED DECEMBER 31, 2006

/ / TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

PENGE CORP.

-----  
(Exact name of registrant as specified in its charter)

DELAWARE

000-52180

71-0895709

-----  
(State or other jurisdiction  
of incorporation)

-----  
(Commission File No.)

-----  
(IRS Employer  
Identification No.)

1501 NORTH FAIRGROUNDS  
MIDLAND, TEXAS 79705

-----  
(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: (423) 683-8800

Check mark whether the issuer (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

Check mark whether the issuer is a shell company (as defined in Rule 12b-2 of the Act): YES  NO

As of December 31, 2006 the issuer had 24,832,745 shares of common stock outstanding.

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

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PENGE CORP AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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DECEMBER 31, 2006

## PENGE CORP. AND SUBSIDIARIES UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

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## PENGE CORP. AND SUBSIDIARIES UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

### ASSETS

|   | December 31,<br>2006 | June 30,<br>2006 |
|---|----------------------|------------------|
|   | -----                | -----            |
| CURRENT ASSETS:   |                      |                  |
| Cash  | \$ 76,848            | \$ 111,911       |
| Accounts receivable, net of \$23,685 and \$6,193 of<br>allowance for doubtful accounts for December 2006<br>and June 2006 | 88,487               | 89,061           |
| Inventories   | 2,806,137            | 2,442,461        |
| Prepaid expenses  | 430                  | 4,761            |
|   | -----                | -----            |
| Total Current Assets  | 2,971,902            | 2,648,211        |
| PROPERTY, PLANT AND EQUIPMENT, net  | 4,430,686            | 4,710,651        |
| LAND HELD FOR SALE  | 1,636,675            | 1,636,675        |
| OTHER ASSETS:   |                      |                  |
| Deferred loan costs   | 19,859               | 22,000           |
| Goodwill  | 150,000              | 150,000          |

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|                                      |              |             |
|--------------------------------------|--------------|-------------|
| Definite-life intangible assets, net | 8,555        | 13,49       |
|                                      | -----        | -----       |
| Total Other Assets                   | 178,414      | 163,71      |
|                                      | -----        | -----       |
|                                      | \$ 9,217,677 | \$ 9,159,25 |
|                                      | =====        | =====       |

[CONTINUED]

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PENGE CORP. AND SUBSIDIARIES  
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

LIABILITIES & SHAREHOLDERS' EQUITY (DEFICIT)

(CONTINUED)

|   | December 31,<br>2006 | June 30,<br>2006 |
|---|----------------------|------------------|
|   | -----                | -----            |
| <b>CURRENT LIABILITIES:</b>   |                      |                  |
| Current portion of notes payable  | 1,565,979            | 940,2            |
| Current portion of related party notes payable  | 443,976              | 266,8            |
| Current portion of convertible notes payable  | 1,835,653            | 918,1            |
| Current portion of related party convertible notes payable  | 250,000              | 150,0            |
| Current Portion of Lease Liability  | 69,313               | 63,7             |
| Accounts payable  | 878,705              | 1,320,2          |
| Related party accounts payable  | 240,628              | 217,5            |
| Customer deposits   | 80,000               |                  |
| Current derivative liabilities  | 62,246               | 56,2             |
| Other accrued liabilities   | 397,924              | 284,0            |
|   | -----                | -----            |
| Total Current Liabilities   | 5,824,424            | 4,217,0          |
| <b>LONG-TERM DEBT:</b>  |                      |                  |
| Notes payable, less current portion   | 1,500,135            | 1,500,1          |
| Related party notes payable, less current portion   | 721,692              | 771,7            |
| Convertible notes payable, less current portion   | 840,731              | 1,578,1          |
| Related party convertible notes payable,<br>less current portion  | 450,000              | 550,0            |
| Long-term capital lease obligations, less current portion   | 221,216              | 255,5            |
| Deferred income   | 18,339               | 23,3             |
|   | -----                | -----            |
| Total Long-term Debt  | 3,752,113            | 4,678,9          |
|   | -----                | -----            |
|   | 9,576,537            | 8,895,9          |
|   | -----                | -----            |
| <b>STOCKHOLDERS' EQUITY (DEFICIT):</b>  |                      |                  |
| Preferred stock, \$.001 par value, 10,000,000<br>shares authorized, no shares issued and outstanding                                      | -                    | -                |
| Common stock, \$.001 par value, 50,000,000 shares<br>authorized, 24,832,745 and 24,515,730 shares<br>issued and outstanding, respectively | 24,779               | 24,5             |

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|                                     |              |            |
|-------------------------------------|--------------|------------|
| Additional paid-in capital          | 3,788,545    | 3,637,5    |
| Accumulated (Deficit)               | (4,172,184)  | (3,398,8   |
|                                     | -----        | -----      |
| Total Stockholders Equity (Deficit) | (358,860)    | 263,2      |
|                                     | -----        | -----      |
|                                     | \$ 9,217,677 | \$ 9,159,2 |
|                                     | =====        | =====      |

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PENGE CORP. AND SUBSIDIARIES  
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

|                                      | For the Three Months<br>Ended December 31, |              | For the<br>Ended De |
|--------------------------------------|--|--------------|---------------------|
|                                      | 2006                                       | 2005         | 2006                |
|                                      | -----                                      | -----        | -----               |
| NET REVENUES:                        |  |              |                     |
| Sales, net                           | \$ 720,045                                 | \$ 1,229,954 | \$ 1,021,821        |
| COST OF GOODS SOLD                   | 302,691                                    | 904,769      | 536,318             |
|                                      | -----                                      | -----        | -----               |
| GROSS PROFIT                         | 417,354                                    | 325,185      | 485,503             |
|                                      | -----                                      | -----        | -----               |
| OPERATING EXPENSES:                  |  |              |                     |
| Salaries, Wages and Related Expenses | 133,867                                    | 135,609      | 369,979             |
| Consulting                           | -  | 16,125       | -                   |
| Advertising                          | 5,044                                      | 371          | 15,057              |
| Other General and Administrative     | 142,288                                    | 78,455       | 265,873             |
|                                      | -----                                      | -----        | -----               |
| Total Operating Expenses             | 281,199                                    | 230,560      | 650,909             |
|                                      | -----                                      | -----        | -----               |
| INCOME (LOSS) FROM OPERATIONS        | 136,155                                    | 94,625       | (165,406)           |
|                                      | -----                                      | -----        | -----               |
| OTHER INCOME (EXPENSE):              |  |              |                     |
| Interest income                      | -  | 8            | 56                  |
| Interest expense related party       | (73,974)                                   | (44,163)     | (123,541)           |
| Interest expense                     | (218,509)                                  | (150,997)    | (382,760)           |
| Note Conversion/Stock Expense        | (32,215)                                   | (85,657)     | (32,215)            |
| Other income (expense)               | (38,410)                                   | (7,934)      | (69,484)            |
|                                      | -----                                      | -----        | -----               |
| Total Other (Expense)                | (363,108)                                  | (288,743)    | (607,944)           |
|                                      | -----                                      | -----        | -----               |
| LOSS BEFORE INCOME TAXES             | (226,953)                                  | (194,118)    | (773,350)           |
|                                      | -----                                      | -----        | -----               |
| CURRENT TAX EXPENSE                  | -  | -            | -                   |
| CURRENT TAX (BENEFIT)                | -  | -            | -                   |
|                                      | -----                                      | -----        | -----               |
| NET LOSS                             | \$ (226,953)                               | \$ (194,118) | \$ (773,350)        |
|                                      | =====                                      | =====        | =====               |

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|  |            |            |            |
|--|------------|------------|------------|
| BASIC AND DILUTED LOSS<br>PER COMMON SHARE | \$ (0.01)  | \$ (0.01)  | \$ (0.03)  |
| WEIGHTED AVERAGE SHARES<br>OUTSTANDING     | 24,655,942 | 23,395,644 | 24,604,002 |

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PENGE CORP. AND SUBSIDIARIES  
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

|  | For the Six Months<br>Ended December 31, |              |
|--|--|--------------|
|  | 2006                                     | 2005         |
| CASH FLOWS FROM OPERATING ACTIVITIES:  |  |              |
| Net loss   | \$ (773,350)                             | \$ (561,000) |
| Adjustments to reconcile net loss to net cash used by<br>operating activities: |  |              |
| Amortization of deferred loan costs  | 31,442                                   | 20,000       |
| Change in deferred loan costs  | (23,554)                                 | 17,000       |
| Change in allowance for bad debts  | 2,974                                    |              |
| Depreciation and amortization  | 77,401                                   | 170,000      |
| Contingent derivative liabilities  | 6,043                                    |              |
| Accounts receivable  | (2,399)                                  | (94,000)     |
| Inventories  | (221,725)                                | (532,000)    |
| Prepaid expenses   | 3,271                                    | (12,000)     |
| Refundable deposits  |  |              |
| Accounts payable   | (168,981)                                | (71,000)     |
| Accrued liabilities  | 145,206                                  | 433,000      |
| Customer deposits  | 80,000                                   |              |
| Net Cash Used by Operating Activities  | (843,672)                                | (628,000)    |
| CASH FLOWS FROM INVESTING ACTIVITIES:  |  |              |
| Payments for property and equipment  | (23,648)                                 | (483,000)    |
| Proceeds for property and equipment  | 141,193                                  |              |
| Net Cash Provided (Used) by Investing Activities                               | 117,545                                  | (483,000)    |

[Continued]

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PENGE CORP. AND SUBSIDIARIES  
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(CONTINUED)

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|  | For the Six Months<br>Ended December 31, |               |
|--|--|---------------|
|  | 2006                                     | 2005          |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>               |  |               |
| Changes in related party advances                          | 23,038                                   | 13            |
| Proceeds from notes payable                                | 422,500                                  | 322           |
| Payments on notes payable                                  | (6,395)                                  |               |
| Proceeds from related party notes payable                  | 100,000                                  | 102           |
| Payments on related party notes payable                    | (23,893)                                 | (19)          |
| Proceeds from convertible notes payable                    | 150,000                                  | 412           |
| Payments on convertible notes payable                      | (9,422)                                  |               |
| Proceeds from capital lease obligations                    |  | 38            |
| Payments on capital lease obligations                      | (28,768)                                 |               |
| Proceeds from stock subscription receivables               | -  | 143           |
| Proceeds from issuance of common stock                     | 64,000                                   | 26            |
| <b>Net Cash Provided by Financing Activities</b>           | <b>691,060</b>                           | <b>1,039</b>  |
| <b>INCREASE IN CASH AND EQUIVALENTS</b>                    | <b>(35,067)</b>                          | <b>(72)</b>   |
| <b>CASH AND EQUIVALENTS AT THE BEGINNING OF THE PERIOD</b> | <b>111,915</b>                           | <b>338</b>    |
| <b>CASH AND EQUIVALENTS AT THE END OF THE PERIOD</b>       | <b>\$ 76,848</b>                         | <b>\$ 265</b> |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>  |  |               |
| Cash paid during the period for:                           |  |               |
| Interest   | \$ 368,793                               | \$ 284        |
| Income Taxes   | \$ -                                     | \$            |

[Continued]

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PENGE CORP. AND SUBSIDIARIES  
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(CONTINUED)

SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING  
ACTIVITIES:

FOR THE SIX MONTHS ENDED DECEMBER 31, 2006

In August 2006, the Company paid \$6,000 towards and a related party assumed \$50,000 of a \$56,000 note payable.

In October 2006, the Company issued 8,572 shares of common stock valued at \$15,585 to satisfy the decrease in the private placement share price of \$0.70 to \$0.55.

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In October 2006, the Company executed two Promissory Notes for outstanding accounts payable for a total of \$272,528 with BWI and Eason Horticulture Resources.

In November 2006, the Company issued 50,000 shares of common stock valued at \$27,500 as part of a secured Promissory note.

In November 2006, the Company issued 100,000 shares of common stock valued at \$55,000 as part of a Commercial Lease agreement.

FOR THE SIX MONTHS ENDED DECEMBER 31, 2005

During the year, a related party paid \$72,169 from the sale of personal property against a note payable of the Company.

In November 2005, the Company entered into a Capital Equipment lease agreement which netted the Company \$38,888 over the carrying value of the leased assets.

In December 2005, the Company received 408,296 shares of treasury stock to satisfy a subscription receivable.

In December 2005, the Company entered into a secured, convertible Promissory Note for \$242,000 for 119.47 acres in Midland, Texas.

In December 2005, notes payable of \$300,000 plus accrued interest were converted into 1,091,995 shares of stock.

In December 2005, the Company assumed a note of a related party and reduced the related party's note by \$133,000.

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### PENGE CORP. AND SUBSIDIARIES NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION - Penge Corp., ("Parent") was organized under the laws of the State of Nevada and was reincorporated in Delaware by a Merger on May 17, 1987.

Penge Corp. ("Penge") was organized under the laws of the State of Nevada on August 6, 2002.

Major Trees, Inc. ("MT Subsidiary") was organized under the laws of the State of Arizona on December 29, 1993.

S&S Plant Farms, Inc. ("S&S Subsidiary") was organized under the laws of the State of Texas on February 23, 1995.

Texas Landscape Center, Inc. ("TLC Subsidiary") was organized under the laws of the State of Texas on September 1, 2005. The subsidiary was organized by the Parent and as such, became a wholly owned subsidiary of the Parent. The financial statements include operations of Texas Landscape Center, Inc from September 1, 2005 through December 31, 2006.

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Parent, Penge, MT Subsidiary, S&S Subsidiary, and TLC Subsidiary ("the Company") grow landscaping and garden plants, flowers, shrubs, trees and other agricultural products for sale to retail nurseries, landscape professionals, and the general public in Southwestern United States. The Company has, at the present time, not paid any dividends and any dividends that may be paid in the future will depend upon the financial requirements of the Company and other relevant factors.

CONSOLIDATION -The financial statements presented reflect the accounts of Parent, Penge, MT Subsidiary, S&S Subsidiary, and TLC Subsidiary; all significant inter-company transactions have been eliminated in consolidation.

AGRICULTURAL PRODUCTION - The Company accounts for their agricultural activities in accordance with Statement of Position 85-3, "Accounting by Agricultural Producers and Agricultural Cooperatives". All direct and indirect costs of growing crops are either accumulated as inventory or expensed as cost of goods sold. Permanent land development costs are capitalized and not depreciated. Limited-life land development costs and the development costs to bring long-life and intermediate-life plants into production are capitalized and depreciated using the straight-line method over the estimated useful lives of the assets.

CASH AND CASH EQUIVALENTS - The Company considers all highly-liquid debt investments purchased with an original maturity of three months or less to be cash equivalents. The Company had \$0 and \$0 in excess of federally insured limits at December 31, 2006 and June 30, 2006, respectively.

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### PENGE CORP. AND SUBSIDIARIES NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ACCOUNTS RECEIVABLE - Accounts receivable consist of trade receivables arising in the normal course of business. At December 31, 2006 and June 30, 2006, the Company has an allowance for doubtful accounts of \$23,685 and \$6,193, respectively, which reflects the Company's best estimate of probable losses inherent in the accounts receivable balance. The Company estimates allowances for doubtful accounts based on the aged receivable balances and historical losses. The Company records interest income on delinquent accounts receivable only when payment is received. The Company first applies payments received on delinquent accounts receivable to eliminate the outstanding principal. The Company charges off uncollectible accounts receivable when management estimates no possibility of collecting the related receivable. The Company considers accounts receivable to be past due or delinquent based on contractual terms.

INVENTORIES - Finished goods inventory is stated at the lower of cost or market using the retail method as the Company has a large quantity of inventory items that have similar costs and markups; the Company does not have any individually significant items. Because the Company's inventory has these characteristics, it is not beneficial to track inventory costs to each individual unit of inventory. Under the retail method, the Company counts and extends their inventory at estimated sales prices, based upon historical sales, which it then multiplies by its cost ratio to determine inventory at cost. The Company's cost ratio is determined by adding the total cost of the



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beginning inventory and all direct and indirect costs of growing crops divided by the total estimated sales price of ending inventory, based on historical sales, plus sales revenues. Raw material inventory is stated at the lower of market or cost using the first-in first-out (FIFO) method.

PROPERTY AND EQUIPMENT - Property and equipment are stated at cost or carryover basis. Expenditures for major renewals and betterments that extend the useful lives of property and equipment are capitalized upon being placed in service. Expenditures for maintenance and repairs are charged to expense as incurred. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. In accordance with Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", the Company periodically reviews their property and equipment for impairment.

LAND HELD FOR SALE - Land held for sale is recorded at the lower of cost or net realizable value.

INTANGIBLE ASSETS - The Company accounts for their intangible assets in accordance with Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets". SFAS No. 142 establishes three classifications for intangible assets including definite-life intangible assets, indefinite-life intangible assets and goodwill and requires different accounting treatment and disclosures for each classification. In accordance with SFAS No. 142, the Company periodically reviews their intangible assets for impairment.

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### PENGE CORP. AND SUBSIDIARIES NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

PRODUCT WARRANTY - The Company does not warranty their agricultural products against damage that may occur prior to delivery to the customer. The Company does warrant trees and shrubs sold through the one retail site. At December 31, 2006 and June 30, 2006, the Company has established a reserve for future warranty expense of \$4,540 and \$0, respectively.

REVENUE RECOGNITION - The Company's revenue comes primarily from the sale of agricultural products. The Company recognizes revenue from retail sales at the time of retail purchase. The Company recognizes revenue from landscaping and wholesale customers when rights and risk of ownership have passed to the customer, there is persuasive evidence of a sales arrangement, product has been shipped, (delivered to or picked up by the customer), the price and terms are finalized and collection of the resulting receivable is reasonably assured.

ADVERTISING COSTS - Cost incurred in connection with advertising of the Company's products are expensed as incurred. Such costs amounted to \$5,044 and \$371 for the three months ended December 31, 2006 and December 31, 2005 respectively and \$15,057 and \$1,926 for the six months ended December 31, 2006 and December 31, 2005, respectively.

LEASE COMMITMENTS - The Company accounts for lease commitments in accordance with SFAS 98, wherein the underlying assets are capitalized and the capital lease obligation recorded if the lease commitments meet the

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requirement for capitalization. All other lease obligations accounted are accounted for as operating leases wherein payments are expensed as the obligation arises [See Note 11].

STOCK-BASED COMPENSATION - The Company has stock option plans that provide for stock-based employee compensation, including the granting of stock options, to certain key employees [See Note 12]. Prior to July 1, 2005, the Company applied APB Opinion No. 25, "Accounting for Stock Issued to Employees", and related Interpretations in accounting for awards made under the Company's stock-based compensation plans. Under this method, compensation expense was recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price.

During the periods presented in the accompanying financial statements, the Company has granted options under its 2002 Stock Incentive Plan. The Company has adopted the provisions of SFAS No. 123R using the modified-prospective transition method and the disclosures that follow are based on applying SFAS No. 123R. Under this transition method, compensation expense recognized

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### PENGE CORP. AND SUBSIDIARIES NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

during the year ended June 30, 2006 included: (a) compensation expense for all share-based awards granted prior to, but not yet vested as of July 1, 2005, and (b) compensation expense for all share-based awards granted on or after July 1, 2005. Accordingly, no compensation cost has been recognized for grants of options to employees and directors in the accompanying statements of operations with an associated recognized tax benefit of \$0 of which \$0 was capitalized as an asset for the period ended December 2006 and 2005 respectively. In accordance with the modified-prospective transition method, the Company's financial statements for the prior year have not been restated to reflect, and do not include, the impact of SFAS 123R. Had compensation cost for the Company's stock option plans and agreements been determined based on the fair value at the grant date for awards in 2005 consistent with the provisions of SFAS No. 123R, the Company's net loss and basic net loss per common share would have been increased to the pro forma amounts indicated below:

|  | December 31,<br>2005 |
|--|----------------------|
|  |                      |
| Net loss, as reported  | \$ (561,775)         |
| Add: Stock-based employee<br>compensation expense included in<br>reported net loss                     | -                    |
| Deduct: Total stock-based employee<br>compensation expense determined<br>under fair value based method | -                    |
|  |                      |
| Net loss   | (561,775)            |
|  |                      |
| Loss per common share, as reported   | \$ (0.02)            |
| Loss per common share, pro forma   | \$ (0.02)            |

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INCOME TAXES - The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" [SEE NOTE 13].

LOSS PER SHARE - The Company calculates loss per share in accordance with the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 128 "Earnings Per Share." Basic loss per common share is based on the weighted average number of common shares outstanding during each period. Diluted earnings per common share when presented are based on shares outstanding as computed under basic EPS and potentially dilutive common shares. Potential common shares included in the diluted earnings per share calculation include in-the-money stock options that have been granted but have not been exercised and convertible notes payable. [SEE NOTE 14]

Continued

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### PENGE CORP. AND SUBSIDIARIES NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ACCOUNTING ESTIMATES - The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosures of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reported period. Actual results could differ from those estimated.

FAIR VALUE OF FINANCIAL INSTRUMENTS -The fair value of the Company's accounts receivable, accounts payable, accrued liabilities, and notes payable approximate their carrying values based on their effective interest rates compared to current market prices for similar assets and liabilities.

RECLASSIFICATION - The financial statements for the period ended prior to December 31, 2006 have been reclassified to conform to the headings and classifications used in the December 31, 2006 financial statements.

RECENTLY ENACTED ACCOUNTING STANDARDS - In May 2005, the FASB issued Statement of Financial Accounting Standards No. 154 ("SFAS 154"), "Accounting Changes and Error Corrections" which replaces APB Opinion No. 20 "Accounting Changes" and SFAS No. 3, "Reporting Accounting Changes in Interim Financial Statements--An Amendment of APB Opinion No. 28". SFAS 154 requires retrospective application to prior periods' financial statements of a voluntary change in accounting principal unless it is not practicable. SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005 and is required to be adopted by the Company in the first quarter of fiscal 2006. The impact that the adoption of SFAS 154 will have on Penge Corp results of operations and financial position will depend on the nature of future accounting changes adopted by Penge Corp and the nature of transitional guidance provided in future accounting pronouncements.

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Continued

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PENGE CORP. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 GOING CONCERN

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles of the United States of America, which contemplate continuation of the Company as a going concern. However, the Company has current liabilities in excess of current assets, incurred significant, recurring losses and has not generated positive cash flow from operating activities. These factors raise substantial doubt about the ability of the Company to continue as a going concern. In this regard, management is proposing to raise any necessary additional funds not provided by operations through loans or through additional sales of their common stock or through possible business combinations. There is no assurance that the Company will be successful in raising this additional capital or in achieving profitable operations. The financial statements do not include any adjustments that might result from the outcome of these uncertainties.

NOTE 3 INVENTORIES

Inventories consist of the following at:

|   | December 31,<br>2006 | June 30,<br>2006 |
|---|----------------------|------------------|
|   | -----                | -----            |
| Raw Materials                                     | \$ 19,471            | \$ 97,904        |
| Finished Goods                                    | 2,816,206            | 2,369,565        |
| Allowance for obsolete / slow<br>moving inventory | (25,000)             | (25,000)         |
| Warranty Reserve                                  | (4,540)              | -                |
|   | -----                | -----            |
|   | \$ 2,806,137         | \$ 2,442,269     |
|   | =====                | =====            |

Most of the Company's inventories are collateral on various notes payable [See Notes 7, 8, 9 and 10].

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PENGE CORP. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4 PROPERTY, PLANT AND EQUIPMENT

Property and equipment consist of the following at:

Estimated

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|                                    | Useful Lives of<br>Assets (Years) | December 31,<br>2006 | June 30,<br>2006 |
|------------------------------------|-----------------------------------|----------------------|------------------|
|                                    | -----                             | -----                | -----            |
| Office furniture and equipment     | 1 - 10                            | \$ 80,886            | \$ 78,944        |
| Retail furniture and equipment     | 1 - 10                            | 620,645              | 613,113          |
| Farm equipment                     | 2 - 15                            | 2,369,968            | 2,540,857        |
| Buildings                          | 20 - 30                           | 1,397,138            | 1,394,278        |
| Land                               | not applicable                    | 592,753              | 592,753          |
| Construction in Progress           | not applicable                    | 113,510              | 15,539           |
|                                    |                                   | -----                | -----            |
| Total                              |                                   | 5,174,900            | 5,235,484        |
| Less accumulated depreciation      |                                   | (744,214)            | (524,834)        |
|                                    |                                   | -----                | -----            |
| Property, Plant and Equipment, net |                                   | \$ 4,430,686         | \$ 4,710,650     |
|                                    |                                   | =====                | =====            |

Depreciation expense for the six months ended December 31, 2006 and 2005 was \$50,614 and \$3,805, respectively. All of the Company's property and equipment are collateral for certain notes payable [See Notes 7, 8, 9 and 10].

NOTE 5 LAND HELD FOR RESALE

FARM LAND - On December 21, 2005, the Company purchased a 119 acre parcel in Midland, Texas for \$242,000. At December 31, 2006, the land is held as collateral on a note payable [See Note 9].

COMMERCIAL PROPERTY - In 2005, the Company also purchased 7 acres of commercial property in San Angelo, Texas for \$1,394,675. At December 31, 2006, the land is held as collateral on a note payable [See Note 9].

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 GOODWILL / DEFINITE-LIFE INTANGIBLE ASSETS

The following is a summary of goodwill and definite-life intangible assets:

|   | December 31,<br>2006 | June 30,<br>2006 |
|---|----------------------|------------------|
|   | -----                | -----            |
| GOODWILL  |                      |                  |
| Goodwill  | \$ 150,000           | \$ 150,000       |
|   | -----                | -----            |
| DEFINITE-LIFE INTANGIBLE ASSETS                 |                      |                  |
| 5-year non-compete contract with<br>note holder | 28,907               | 28,907           |
| 5-year non-compete contract with<br>shareholder | 28,907               | 28,907           |
| Less accumulated amortization                   | (49,259)             | (44,324)         |
|   | -----                | -----            |

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Net Definite-Life Intangible Assets \$ 8,555 \$ 13,490  
===== =====

The Company estimates that its amortization expense will be approximately as follows for the twelve month periods ended:

| December 31, | Amortization<br>Expense |
|--------------|-------------------------|
| -----        | -----                   |
| 2007         | 8,555                   |
| Thereafter   | -                       |
|              | -----                   |
|              | 8,555                   |

Definite Life Intangible Assets - The Company is amortizing their definite-life intangible assets on a straight-line basis over five years. Amortization expense of \$4,935 and \$5,781 was recorded for the six months ended December 31, 2006 and 2005, respectively, and has been included in general and administrative expense.

Goodwill - The Company recorded goodwill of \$150,000 in connection with the acquisition of Profile Diagnostic Sciences, Inc. as the purchase price of \$150,000 exceeds the \$0 net book value of the assets acquired.

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 CONVERTIBLE NOTES PAYABLE

The Company had the following convertible notes payable summarized in groups with similar attributes at:

|  | December 31,<br>2006 | June<br>2006 |
|--|----------------------|--------------|
|  | -----                | -----        |
| 12% Note payable, maturing in May to June 2007, convertible at \$.65 per share for the first twelve months and \$.75 per share for the second twelve months, secured by UCC-1 lien against inventory     | 270,000              | 2            |
| 12% Note Payable, maturing in February 2007, convertible at \$.30 per share through February 2007, secured by UCC-1 lien against inventory   | 228,000              | 2            |
| 12% Note Payable, maturing in June to October 2007, convertible at \$.65 per share for the first twelve months and \$.75 per share for the second twelve months, secured by UCC-1 lien against inventory | 750,000              | 7            |
| 12% Note payable, maturing in October 2007 to May 2008, convertible at \$.95 per share for the first twelve months and \$1.05 for the second twelve  |                      |              |

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|   |         |   |
|---|---------|---|
| months, secured by UCC-1 lien against inventory   | 452,500 | 4 |
| 15% Note Payable, maturing in 2007, convertible at \$.30 per share (At the time of conversion, the creditor can require the Company to redeem any amount of the shares in the conversion at \$.345 per share), secured by a lien using a Trust Deed and Trust Deed Note, against Major Trees, a lien using a Trust Deed and Trust Deed Note, against Major Trees, TX, and a term life insurance policy on two officers of the Company | 409,649 | 3 |
| 12% Note payable, maturing in January 2008, convertible at \$.95 per share for the first twelve months and \$1.10 for the second twelve months, secured by A UCC-1 lien against inventory   | 200,000 | 2 |

Continued

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 CONVERTIBLE NOTES PAYABLE (CONTINUED)

|   |             |        |
|---|-------------|--------|
| 12% Note payable, maturing in March 2008, convertible at \$.95 per share for the first twelve months and \$1.10 for the second twelve months, secured by 119.47 acres in Midland, TX      | 216,235     | 2      |
| 12% Note payable, maturing in January 2008, convertible at \$.95 per share for the first twelve months and \$1.10 for the second twelve months, secured by A UCC-1 lien against inventory | 150,000     |        |
| Total   | 2,676,384   | 2,4    |
| Less Current Portion  | (1,835,653) | (9)    |
|   | \$ 840,731  | \$ 1,5 |
|   | =====       | =====  |

The convertible notes payable mature as follows for the twelve-month periods ended:

| December 31, | Principle<br>Due |
|--------------|------------------|
| -----        | -----            |
| 2007         | \$ 1,835,653     |
| 2008         | 840,731          |

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Thereafter -  
 -----  
 \$ 2,676,384  
 =====

The discounts due to the beneficial conversion feature of the notes are being amortized over the term of the respective notes. For the six months ended December 31, 2006 and 2005, the Company amortized \$0 and \$18,691, respectively, the discounts on notes payable as interest expense.

At December 31, 2006, the Company had a total of \$19,860 in loan fees and costs from establishing these convertible notes payable. These costs have been deferred and are being amortized over the term of the respective notes. For the six months ended December 31, 2006, the Company amortized \$19,860 of the deferred loan costs as interest expense.

For the six months ended December 31, 2006 and 2005, interest expense on the convertible notes payable amounted to \$159,572 and \$117,677, respectively.

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PENGE CORP. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8 RELATED PARTY CONVERTIBLE NOTES PAYABLE

The Company had the following related party convertible notes payable summarized in groups with similar attributes due to shareholders of the Company at:

|   | December 31,<br>2006 | June<br>2005 |
|---|----------------------|--------------|
|   | -----                | -----        |
| 12% Notes payable, maturing in 2007, convertible at \$ .30 per share through February 2007, secured by UCC-1 lien against inventory   | 100,000              | 1            |
| 12% Notes payable, maturing in 2008, convertible at \$ .65 per share for the first twelve months and \$ .75 per share for the second twelve months, secured by UCC-1 lien against inventory | 50,000               |              |
| 12% Notes payable, maturing in 2007, convertible at \$ .30 per share through February 2007, secured by inventory  | 100,000              | 1            |
| 12% Notes Payable, maturing in 2008, convertible at \$ .70 per share through January 31, 2008, secured by TLC's building and land in Midland, TX  | 450,000              | 4            |
| Total   | 700,000              | 7            |
| Less Current Portion  | (250,000)            | (1)          |
|   | -----                | -----        |
|   | \$ 450,000           | \$ 5         |
|   | =====                | =====        |



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The related party convertible notes payable mature as follows for the twelve-month periods ended:

| December 31,<br>----- | Principle<br>Due<br>----- |
|-----------------------|---------------------------|
| 2007                  | \$ 250,000                |
| 2008                  | 450,000                   |
| Thereafter            | -                         |
|                       | -----                     |
|                       | \$ 700,000                |
|                       | =====                     |

Continued

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8 RELATED PARTY CONVERTIBLE NOTES PAYABLE (CONTINUED)

The discounts due to the beneficial conversion feature of the notes are being amortized over the term of the respective notes. For the six months ended

December 31, 2006 and 2005, the Company amortized \$938 and \$3,616, respectively, of the discounts on notes payable as interest expense.

At December 31, 2006, the Company had a total of \$0 in loan fees and costs from establishing these convertible notes payable. These costs have been deferred and are being amortized over the term of the respective notes. For the six months ended December 31, 2006 and 2005, the Company amortized \$229 and \$1,375 respectively, of the deferred loan costs as interest expense.

For the six months ended December 31, 2006 and 2005, interest expense on the related party convertible notes payable amounted to \$33,262 and \$15,122, respectively.

NOTE 9 NOTES PAYABLE

The Company had the following notes payable summarized in groups with similar attributes at:

|   | December 31,<br>2006<br>----- | June<br>200<br>----- |
|---|-------------------------------|----------------------|
| 7% Notes payable, yearly payments of \$50,000, mature in 2007, secured by Major Tree's outstanding shares of capital stock, financial books and records, equipment, and furniture | \$ 77,150                     | \$                   |
| Unsecured 6% Notes payable, maturing  |                               |                      |

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|   |         |   |
|---|---------|---|
| 2007  | 18,055  |   |
| 24% Notes payable, maturity extended to August 15, 2006, beginning balance of \$200,000 secured by land. Security was released upon principle payment of \$144,000 in June 2006 | -       |   |
| 24% Notes payable, maturing December 15, 2006 secured by land; extended month to month on December 1, 2006.   | 200,000 | 1 |
| 14% Notes payable maturing in 2006, secured by MT Subsidiary's land in Cochise County, AZ. Verbally extended to monthly; good standing on 12/31/06                              | 311,337 | 2 |

Continued

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 9      NOTES PAYABLE (CONTINUED)

|  |         |   |
|--|---------|---|
| 14% Notes payable, maturing in 2007, secured by the property of an officer in Clark County, Nevada. In September 2005 an officer of the Company paid \$72,169 in behalf of the Company and the lien on the property was released by the holder of the note | 105,399 |   |
| 12% Notes payable, balloon payment due upon maturity, matures in 2007, secured by inventory  | 85,577  |   |
| 6.75% Note payable, monthly payments of \$3,355, matures in 2021, secured by TLC's building and land   | 367,833 | 3 |
| 7% Note payable, monthly payments of \$1,370, mature in 2008, secured by S&S' land and office building   | 125,974 | 1 |
| 24% Notes payable, maturing November 2006, unsecured.  | 150,000 |   |
| 24% Notes payable, maturing December 2006, unsecured.  | 60,000  |   |
| 24% Notes payable, maturing January 2007, unsecured.   | 80,000  |   |
| 24% Notes payable, maturing December 2006, unsecured.  | 30,000  |   |

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|   |         |
|---|---------|
| 24% Notes payable, maturing January 2007,<br>unsecured.   | 50,000  |
| 9% Notes payable, maturing September 2007,<br>unsecured.  | 161,498 |
| 12% Notes payable, maturing September 2008,<br>unsecured. | 76,972  |

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 9 NOTES PAYABLE (CONTINUED)

Interest rate will be 6% note payable until July 1, 2006.

Beginning July 1, 2006, interest will accrue at the rate per year that will be the lesser of .5% in excess of the Prime Interest Rate as published by the Wall Street Journal; or the maximum nonusurious rate of interest permitted by applicable law. Beginning January 2007, monthly payments necessary to amortize the balance over a period ending July 2015 will be required. The note matures on July 1, 2010 when the balance will be due. Note is secured by land in San Angelo, TX which is held for resale. Extension of interest only through January 2007.

|                      |              |        |
|----------------------|--------------|--------|
|                      | 1,166,319    | 1,1    |
| Total                | 3,066,114    | 2,4    |
| Less Current Portion | (1,565,979)  | (9)    |
|                      | \$ 1,500,135 | \$ 1,5 |

The notes payable mature as follows for the twelve-month periods ended:

| December 31, | Principle Due |
|--------------|---------------|
| 2007         | \$ 1,565,979  |
| 2008         | 249,278       |
| 2009         | 99,407        |
| 2010         | 106,938       |
| 2011         | 115,040       |
| Thereafter   | 929,472       |
|              | \$ 3,066,114  |

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At December 31, 2006, the Company had a total of \$19,860 in loan fees and costs from establishing these notes payable. These costs have been deferred and are being amortized over the term of the respective notes. For the six months ended December 31, 2006, the Company amortized \$30,270 of the deferred loan costs as interest expense.

For the six months ended December 31, 2006 and 2005, interest expense on the notes payable amounted to \$164,643 and \$89,383, respectively.

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10 RELATED PARTY NOTES PAYABLE

The Company had the following related party notes payable summarized in groups with similar attributes due to shareholders of the Company at:

|   | December 31,<br>2006 | June<br>2005 |
|---|----------------------|--------------|
|   | -----                | -----        |
| 7% Note payable, yearly payments of \$75,000, maturing in 2009, secured by Major Tree's farmland, buildings, and equipment  | \$ 194,292           | \$ 2         |
| 8% Note payable, monthly payments of \$2,500, maturing in 2009, secured by land and inventory   | 267,007              | 2            |
| 7% Note payable, quarterly payments of \$11,660 through March 2007, quarterly payments of \$13,527 from March 2007 through March 2009, quarterly payments of \$15,483 from March 2009 through March 2010, mature in 2010, secured by all of the issued and outstanding shares of S&S Plant Farm, Inc.'s capital stock | 365,393              | 3            |
| 12% Note payable, quarterly interest payments beginning April 2006, maturing January 10, 2007, unsecured.   | 88,976               | 1            |
| 10% Note payable, maturing in 2007, secured by UCC-1 lien against inventory, net discount for options issued of \$0 and \$938   | 50,000               |              |
| 12% Notes payable, balloon payment due upon maturity, mature in 2007, secured by inventory  | 50,000               |              |
| 24% Notes payable, balloon payments due upon maturity, mature in 2008, unsecured.   | 150,000              |              |
|   | -----                | -----        |
| Total   | 1,165,668            | 1,0          |
| Less Current Portion  | (443,976)            | (2           |
|   | -----                | -----        |

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10 RELATED PARTY NOTES PAYABLE

At December 31, 2006, the Company had a total of \$0 in loan fees and costs from establishing these notes payable. For the three months ended December 31, 2006 and 2005, the Company amortized \$229 and \$1,375, respectively, of the deferred loan costs as interest expense. For the six months ended December 31, 2006 and 2005, interest expense on the related party notes payable amounted to \$56,716 and \$41,307, respectively.

The notes payable mature as follows for the six-month periods ended:

| December 31,<br>----- | Principle<br>Due<br>----- |
|-----------------------|---------------------------|
| 2007                  | \$ 443,976                |
| 2008                  | 142,220                   |
| 2009                  | 529,836                   |
| 2010                  | 49,636                    |
| 2011                  | -                         |
| Thereafter            | -                         |
|                       | -----                     |
|                       | \$ 1,165,668              |
|                       | =====                     |

The discounts due to the options issued with the notes are being amortized over the term of the respective notes. For the six months ended December 31, 2006 and 2005, the Company amortized \$938 and \$3,616, respectively, of the discounts on notes payable as interest expense.

NOTE 11 CAPITAL LEASES OBLIGATION

The Company leases equipment under capital leases and that expire on October 2009 and July through November 2010. The gross amount of assets recorded under capital leases and the associated accumulated depreciation are included under property and equipment and are as follows:

|                               |                               |
|-------------------------------|-------------------------------|
|                               | December 31,<br>2006<br>----- |
| Farm equipment                | \$ 360,181                    |
|                               | -----                         |
| Total                         | 360,181                       |
| Less accumulated depreciation | (91,848)                      |
|                               | -----                         |
| Net Leased Equipment          | \$ 268,333                    |
|                               | =====                         |

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PENGE CORP. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11 CAPITAL LEASES OBLIGATION (CONTINUED)

The Company amortizes its lease obligations over the term of each lease. Amortization expense was \$22,753 for the six months ended December 31, 2006.

The future minimum lease payments are as follows for the twelve-month periods ended:

| Amortization<br>December 31,<br>----- | Amount Due<br>----- |
|---------------------------------------|---------------------|
| 2007                                  | \$ 97,630           |
| 2008                                  | 96,021              |
| 2009                                  | 93,822              |
| 2010                                  | 62,698              |
| Thereafter                            | -                   |
|                                       | -----               |
| Total minimum obligations             | 350,171             |
| Executory costs and interest          | (59,642)            |
|                                       | -----               |
| PV of minimum obligations             | 290,529             |
| Current portion                       | (69,313)            |
|                                       | -----               |
| Long-term obligations                 | \$ 221,216<br>===== |

NOTE 12 CAPITAL STOCK AND OPTIONS

PREFERRED STOCK - In October 2004, Parent amended its articles of incorporation to authorize 10,000,000 shares of preferred stock, \$.001 par value, with such rights, preferences and designations and to be issued in such series as determined by the Board of Directors. At December 31, 2006 and June 30, 2006, no preferred shares were issued and outstanding.

COMMON STOCK - In November 2006, the Company issued 100,000 shares of their previously authorized but unissued common stock for the signing of a lease with a two-year buyout to purchase the Odessa, TX location, stock valued at \$55,000, or \$0.55 per share.

In November 2006, the Company issued 50,000 shares of their previously authorized but unissued common stock for interest expense of \$27,500, or \$0.55 per share.

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### PENGE CORP. AND SUBSIDIARIES NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 12 CAPITAL STOCK AND OPTIONS (CONTINUED)

In October 2006, the Company issued 58,182 shares of their previously authorized but unissued common stock for cash of \$32,000, or \$0.55 per share.

In October 2006, the Company issued 8,572 shares of their previously authorized but unissued common stock for a reduction in private placement value of stock valued at \$15,585 or \$0.55 per share.

In September 2006, the Company issued 45,714 shares of their previously authorized but unissued common stock for cash of \$32,000, or \$.70 per share

In March and June 2006, the Company issued 59,286 shares of their previously authorized but unissued common stock for services and supplies valued at \$41,500 or \$.70 per share.

In April 2006, the Company issued 35,715 shares of their previously authorized but unissued common stock for cash of \$25,000, or \$.70 per share.

In March 2006, the Company issued 15,000 shares of their previously authorized but unissued common stock for services and supplies valued at \$10,500 or \$.70 per share.

In February and March 2006, the Company issued 142,860 shares of their previously authorized but unissued common stock for cash of \$100,000, or \$.70 per share.

In January 2006, the Company issued 50,000 shares of their previously authorized but unissued common stock for employee services rendered valued at \$35,000 or \$.70 per share.

In December 2005, the Company issued 666,667 shares of their previously authorized but unissued common stock for the conversion of \$200,000 note payable, or \$.30 per share.

In December 2005, the Company issued 308,921 shares of their previously authorized but unissued common stock for the conversion of \$75,000 note payable and \$2,230 interest, or \$.25 per share. The Company recorded an additional \$55,117 in interest for the adjusting the conversion price to \$0.25 per share.

In December 2005, the Company issued 116,407 shares of their previously authorized but unissued common stock for the conversion of \$25,000 note payable and \$110 interest, or \$.22 per share. The Company recorded an additional \$45,632 in interest for the adjusting the conversion price to \$0.22 per share.

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### NOTE 12 CAPITAL STOCK AND OPTIONS (CONTINUED)

In November 2005, the Company issued 35,714 shares of their previously authorized but unissued common stock for cash of \$25,000, or \$.70 per share

In August 2005, the Company issued 5,000 shares of their previously authorized but unissued common stock for the exercise of options at \$.30 per share.

SUBSCRIPTION RECEIVABLE - During Fiscal 2006, the Company received cash of \$233,977 in payment of subscriptions receivable due from officers of the Company. Also during 2006, the Company received 408,296 common shares valued at \$0.88 per share in payment of \$359,300 in subscriptions receivable from officers of the Company. The 408,296 common shares were held in treasury until canceled during June 2006.

STOCK OPTION PLAN - In October 2002, the Company's Board of Directors approved and adopted the "2002 Stock Incentive Plan" ("the Plan") with a maximum of 8,000,000 shares of common stock reserved for issuance under the Plan. The Plan provides for both the direct award of shares and for the grant of options to purchase shares to employees, officers, directors, agents, consultants, advisors and independent contractors. Awards under the Plan will be granted as determined by the Board of Directors and the Board of Directors shall determine which eligible persons are to receive Incentive Stock Options, Non-Statutory Stock Options or stock issuances. The Board of Directors also sets the number of shares, the exercise price and the exercise terms for grants. Options granted to non-exempt employees are required to have an exercise price of at least 85% of the fair market value of the common stock at the time of grant. Incentive Stock Options must be granted with an exercise price of at least 100% (110% for shareholders who own at

least 10% of the Company's outstanding stock) of the fair market value of the common stock at the time of grant. Incentive Stock Options are required to expire within 10 years. At December 31, 2006 and 2005, total awards available to be granted from the plan amounted to 3,150,000 and 3,150,000, respectively.

The fair value of each of the Company's stock option awards is estimated on the date of grant using a Black-Scholes option-pricing model that uses the assumptions noted in the table below. The fair value of the Company's stock Option awards is expensed on a graded vesting straight-line basis over the vesting period of the options, which is generally immediate. Expected volatility is based on an average of historical volatility of the Company's stock. The risk-free interest rate for periods within the contractual life of the stock option award is based on the yield curve of a zero-coupon U.S. Treasury bond on the date the award is granted with a maturity

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 12 CAPITAL STOCK AND OPTIONS (CONTINUED)



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equal to the expected term of the award. The expected term of awards granted is derived from historical experience under the Company's stock-based compensation plans and represents the period of time that awards granted are expected to be outstanding.

The fair value of each option granted is estimated on the date granted using the Black-Scholes option pricing model with the following weighted-average assumptions used for grants during the six months ended December 31, 2006: expected dividend yields of zero, expected life of 4.43 years, expected volatility of 302.4%, and risk-free interest rates of 3.9%.

A summary of the status of options granted at December 31, 2006, and changes during the period then ended are as follows:

|  | For the Six Months Ended<br>December 31, 2006 |  |  |
|--|---|--|--|
|  | Shares  | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual Term |
| Outstanding at beginning of period             | 845,000                                       | \$ 0.25                                  | 4.68 years   |
| Granted  | -   | -  | -  |
| Exercised                                      | -   | -  | -  |
| Forfeited                                      | -   | -  | -  |
| Expired  | -   | -  | -  |
| Outstanding at end of period                   | 845,000                                       | \$ 0.25                                  | 4.43 years   |
| Vested and expected to vest in the future      | 845,000                                       | \$ 0.25                                  | 4.43 years   |
| Exercisable at end of period                   | 845,000                                       | \$ 0.25                                  | 4.43 years   |
| Weighted average fair value of options granted | -   | \$ -                                     | -  |

The Company had no non vested options at the beginning of the period. At December 31, 2006 the Company had no non vested options resulting in no unrecognized compensation expense.

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PENGE CORP. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 12 CAPITAL STOCK AND OPTIONS (CONTINUED)

The total intrinsic value of options exercised during the six months ended December 31, 2006 and 2005 was \$0 and \$2,000 respectively. Intrinsic value is measured using the fair market value at the date of exercise (for shares

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exercised) or at December 31, 2006 and 2005 (for outstanding options), less the applicable exercise price.

During the six months ended December 31, 2006 and 2005, the Company received cash of \$0 and \$1,500 and recorded a subscription receivable of \$0 and \$0 upon the exercise of awards. The Company realized no tax benefit due to the exercise of options as the Company had a loss for the period and historical net operating loss carry forwards.

Common shares issued upon exercise of options are issued from available authorized but unissued common shares. As of December 31, 2006, the Company has no plans to repurchase common shares issued upon exercise of options.

A summary of the status of stock options outstanding at December 31, 2006 is presented below:

| Range of Exercise Prices | Options Outstanding |   |                                 | Options Exercisable |                                 |
|--------------------------|---------------------|---|---------------------------------|---------------------|---------------------------------|
|                          | Number Outstanding  | Weighted Average Remaining Contractual Life | Weighted Average Exercise Price | Number Exercisable  | Weighted Average Exercise Price |
| \$ 0.10                  | 200,000             | 5.84 years                                  | \$ 0.10                         | 200,000             | \$                              |
| 0.30                     | 645,000             | 3.04 years                                  | 0.30                            | 645,000             |                                 |
| \$0.10-0.30              | 845,000             | 4.43 years                                  | \$ 0.25                         | 845,000             | \$                              |

NOTE 13 INCOME TAXES

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes". Which requires the Company to provide a net deferred tax asset or liability equal to the expected future tax benefit or expense of temporary reporting differences between book and tax accounting methods and any available operating loss or tax credit carryforwards.

At December 31, 2006 and June 30, 2006, the total of all deferred tax assets is approximately \$913,000 and \$804,000 and the total of all deferred tax liabilities is \$191,000 and \$191,000. The amount of and ultimate realization of the benefits from the deferred tax assets is dependent, in part, upon the tax laws in effect, the future earnings of the Company, and other future events, the effects of which cannot be determined. Because of these uncertainties surrounding the realization of the NOL carryforwards, the Company has established a valuation allowance of approximately \$722,000 and \$613,000 at December 31, 2006 and June 30, 2006. The change in the valuation allowance for the six months ended December 31, 2006 was approximately \$27,000.

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### NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

At December 31, 2006 and June 30, 2006, the Company has available unused net operating loss carryforwards of approximately \$5,430,000 and \$4,650,000 respectively, which may be applied against future taxable income and which expire in various years through 2026. Also, the Company has unused capital loss carryovers at December 31, 2006 and June 30, 2006 of approximately \$81,000 and \$81,000, respectively, which expire in various years through 2009.

#### NOTE 14 LOSS PER SHARE

The following data shows the amounts used in computing loss per share:

|  | For the Three Months<br>Ended December 31, |              | For the Six Months<br>Ended December 31, |              |
|--|--|--------------|--|--------------|
|  | 2006                                       | 2005         | 2006                                     | 2005         |
| Loss from operations available to<br>common shareholders (numerator)   | \$ (226,953)                               | \$ (194,118) | \$ (773,350)                             | \$ (773,350) |
| Weighted average number of common<br>shares outstanding used in loss per<br>share for the period (denominator) | 24,655,942                                 | 23,395,644   | 24,604,002                               | 23,395,644   |

At December 31, 2006, the Company had outstanding options to purchase 845,000 shares and notes payable convertible into 6,268,361 shares which were not used in the computation of loss per share because their effect would be anti-dilutive. At December 31, 2005, the Company had outstanding options 850,000 shares and notes payable convertible into 5,714,692 shares which were not used in the computation of loss per share because their effect would be anti-dilutive.

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### PENGE CORP. AND SUBSIDIARIES NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 15 RELATED PARTY TRANSACTIONS

RELATED PARTY ADVANCES - During the six months ended December 31, 2006 and 2005, officers/shareholders of the Company and their relatives have made advances to the Company and the Company has repaid the advances as funds have been available. During the six months ended December 31, 2006 officers/shareholders of the Company and their relatives made advances totaling \$56,248 and the company repaid advances totaling \$0. Since the Company owed \$184,380 from prior-year advances, the remaining balance owed to the officers/shareholders of the Company and their relatives at December 31, 2006 is \$240,628.

During the year ended June 30, 2006, officers/shareholders of the Company and their relatives have made advances to the Company and the Company has

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repaid the advances as funds have been available. During the year ended June 30, 2006, officers/shareholders of the Company and their relatives made advances totaling \$244,853 and the company repaid advances totaling \$65,618. Since the Company owed \$5,144 from prior-year advances, the remaining balance owed to the officers/shareholders of the Company and their relatives at June 30, 2006 is \$184,380.

### NOTE 16 CONCENTRATIONS

ACCOUNTS RECEIVABLE - At December 31, 2006, 14% of the Company's accounts receivable was owed by only one customer. At June 30, 2006, 41% of the Company's accounts receivable was owed by three customers. The following table lists the percent of the receivables owed by those customers that accounted for 10% or more of the total accounts receivable at December 31, 2006 and June 30, 2006 respectively:

|            | December 31, 2006<br>----- | June 30, 2006<br>----- |
|------------|----------------------------|------------------------|
| Customer A | 14%                        | *                      |
| Customer B | *                          | 17%                    |
| Customer C | *                          | 14%                    |
| Customer D | *                          | 10%                    |

\* Customer did not account for 10% or more of total accounts receivable

REVENUES - During the six months ended December 31, 2006 and 2005, respectively, the Company had a significant customer which accounted for 26% and 50% of the Company's total sales. The loss of this significant customer could adversely affect the Company's business and financial condition.

Our revenue decreased due to cessation of unprofitable wholesale business through S&S Plant Farm and the cessation of business with the Texas region of Home Depot due to a high probability of sales returns from the Texas region's new vendor consignment model. Cost of goods sold decreased due to lower sales, and Cost of goods sold as a percentage of sales decreased from 76% for the six months ended December 2005 to 52.5% for the six months ended December 2006 as a result of eliminating low margin sales at S&S Plant Farm and having higher margins sales at Texas Landscape Center.

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## PENGE CORP. AND SUBSIDIARIES NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 17 COMMITMENTS AND CONTINGENCIES

DERIVATIVE LIABILITY FOR THE REDEMPTION OF COMMON STOCK - The Company has a convertible note payable which is convertible into common stock at \$.30 per share. At the time of conversion, the creditor can require the Company to redeem any amount of the shares issued in the conversion at \$.345 per share. At December 31, 2006, the Company owed \$409,650 in principal and \$5,325 in accrued interest on the note. If the note had been converted into stock on December 31, 2006, then the Company would have issued 1,383,250 shares of common stock which would have been redeemable at the creditor's option for \$477,221. The Company has recorded a remaining contingent derivative liability of \$62,246 associated with the option.

### NOTE 18 SUBSEQUENT EVENTS

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COMMON STOCK ISSUANCE - In January 2007, the Company issued 45,455 shares of their previously authorized but unissued common stock for cash of \$25,000, or \$0.55 per share.

CONVERSION OF NOTES PAYABLE TO STOCK - In January 2007, the Company converted a \$150,000 Promissory Note between Penge Corp and Gary Rowbotham dated July 12, 2006 to common stock at \$0.30 per share for a total of 500,000 shares.

In January 2007, the Company converted a \$50,000 Promissory Note between Penge Corp and Campbell Family Properties, Ltd. dated June 15, 2005 to common stock at \$0.55 per share for a total of 90,909 shares.

In January 2007, the Company signed \$25,000 in notes payable. The note accrues interest at 12% per annum and is due August 2007.

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### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-QSB (this "Report") contains various forward-looking statements. Such statements can be identified by the use of the forward-looking words "anticipate," "estimate," "project," "likely," "believe," "intend," "expect" or similar words. These statements discuss future expectations, contain projections regarding future developments, operations, or financial conditions, or state other forward-looking information. When considering such forward-looking statements, you should keep in mind the risk factors noted in "the subsection titled "Risk Factors" below and other cautionary statements throughout this Report and our other filings with the SEC. You should also keep in mind that all forward-looking statements are based on management's existing beliefs about present and future events outside of management's control and on assumptions that may prove to be incorrect. If one or more risks identified in this Report or any other applicable filings materializes, or any other underlying assumptions prove incorrect, our actual results may vary materially from those anticipated, estimated, projected, or intended.

#### OVERVIEW

Penge Corp is a Delaware corporation incorporated in 1987 with its principal offices at 1501 North Fairgrounds, Midland, Texas 79705. Our telephone number is (432) 683-8800. We are in the wholesale and retail nursery business. Our stock is traded on the OTC Pink Sheets under the symbol "PNGC."

Our operations are directly or indirectly run through a subsidiary, Penge Corp, a Nevada corporation ("Penge Nevada"), which was organized in 2002 to engage in the nursery business. On June 30, 2005, Penge Nevada merged with a subsidiary of Profile Diagnostic Sciences, Inc., a Delaware corporation with no current operations. Following the merger, the officers and directors of Penge Nevada became the officers and directors of Profile Diagnostic Sciences, Inc. and the business Penge Nevada and its affiliates became the business of Profile Diagnostic Sciences, Inc. Following the merger, we changed the name of Profile

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Diagnostic Sciences, Inc. to "Penge Corp" Unless otherwise specified, references to "Penge," "we," "us" or the "company" for periods prior to June 30, 2005 relate to Penge Nevada and its affiliates. For periods from and after June 30, 2005, those descriptions relate to Penge Corp (f/k/a Profile Diagnostic Sciences, Inc.) and its affiliates, including Penge Nevada.

Since commencing business in August 2002, we have acquired the land and certain other assets from three tree, shrub and plant farms, one of which is in Arizona and two of which are in Texas. As we have acquired the properties, we have taken steps to improve operations and to expand the number of trees, shrubs and plants growing on, and harvested from, each such property.

In October 2005, we purchased a vacant 13,000 square foot building on 3.8 acres in Midland, Texas for the site of our first retail nursery. We completed a \$951,000 dollar conversion of the property including a complete remodel of the building and the addition of 32,000 square feet of greenhouse and 40,000 feet of tree display area. Going forward both the wholesale and retail business will be done at the retail center.

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In 2005, we also purchased 7 acres of commercial property in San Angelo, Texas that shares an intersection with Wal-Mart, Lowe's and Sam's Club. Based upon the sales price of recently sold land at the same intersection, we believe that our property is currently worth more than we paid for it. We plan to either sell or develop the property. We have not entered into any agreements with respect to the sale or development of this site.

In December 2006, we entered into a Commercial Lease Agreement with Marrs & Smith, Ltd., with respect to commercial property located in at 2600 Andres Highway, Odessa, Texas. The primary term of the lease is approximately two (2) years, and our base rent under the lease is \$4,000 per month. The property is expected to be used primarily for a landscape center and nursery.

In connection with the lease, we also entered into a Contract of Sale with Marrs & Smith, Ltd. for the purchase of the property underlying the lease. The purchase price for the property is \$861,704.33, subject to discount if we close the transaction prior to December 1, 2008. The closing date of the transaction must be on or after December 1, 2007, but before December 1, 2008. We also issued 100,000 shares of common stock to Marrs & Smith, Ltd. in connection with this agreement.

Going forward, our focus will be to create and to expand a vertically integrated wholesale and retail nursery business. We expect that our tree, shrub and plant farms will be able to provide a substantial portion of the inventories for our recently opened and planned retail nurseries in the coming years. By owning the tree, shrub and plant farms that provide much of the inventory for the retail nurseries, we believe that we will be able to compete with, and even undercut, the "big box stores" that have become the dominant force in the retail nursery business. These big box stores have been driving many retail nurseries out of business by buying nursery materials in large quantities at big discounts from wholesale nursery growers in the United States. This allows them to sell at a discount using smaller margins and to undercut the small nurseries by 30% to 50%. We believe that our vertically integrated wholesale/retail nursery business model will allow us to compete with the big box stores on price, while providing better selection and service.

For our wholesale business, our goal is to expand the number of trees and

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shrubs planted on our farms in the next few years while holding down increases in our administrative and other general operating expenses. As we spread our production costs over a larger inventory, we also hope to experience a decline in our per-unit production and sales costs. We do not plan to expand our wholesale sales. Instead, we plan to provide most of what we grow to our retail centers.

### GENERAL OUTLOOK

#### OUR INDUSTRY AND WHOLESALE/RETAIL BUSINESS MODEL

The retail nursery business has been under attack for many years from Home Depot, Lowe's and Wal-Mart. These big box stores buy nursery materials in large quantities at big discounts from wholesale nursery growers. This allows them to sell at a discount, using smaller margins, and to undercut the small nurseries by 30%-50%. Small nurseries generally cannot compete on price and so they try to compete by offering better service, better selection, and convenience. Although this approach has worked for some small nurseries, it has not worked for most of them, and a large number of small nurseries have gone out of business in the last 10 years primarily because they are unable to compete on price with the big box stores.

In the last 5 years, a new model has emerged in the nursery industry that we believe is able to compete effectively with the big box stores. This model requires a retail nursery to grow a substantial percentage its own plant material (trees, shrubs, and flowers) instead of buying them from a wholesale grower. It is capital intensive for a retail nursery to grow its own products and it takes from 3-5 years to grow its initial inventory. But, once the model is in place, it can allow the retail nursery to offer products at prices that are lower than or equal to those of the big box stores, while continuing to offer a level of selection and service that the big box stores can not offer.

Over the last 4 years, we have purchased wholesale operations growing trees, shrubs, and flowers and plan to continue to open retail operations in addition to our Midland, Texas retail nursery. We believe that this new hybrid retail/wholesale nursery business model will enable us to increase sales and create and sustain a profitable operation. We also believe that the competition in Texas and surrounding areas has not switched over to the new model, which should give us at least a 3 - 5 year head start on rolling out the model in this region.

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#### OUR WHOLESALE BUSINESS

We currently own three wholesale nursery operations in Texas and Arizona. At the end of 2002, we purchased a 272-acre tree farm near Tucson, Arizona known as "Major Trees" and now referred to as our Major Trees Tucson Farm. In May of 2004, we acquired a 17-acre of farming property near Houston Texas on which we have established a wholesale operation and which we refer to as our Major Trees Houston Farm. In 2005, we purchased the S&S Plant Farm in Midland, Texas which specializes in plants and flowers. This last farm is a 50-acre property with 8 acres under greenhouse and shade house, and a full complement of equipment and machinery for propagating trees, shrubs, plants and flowers from seeds and plugs.

We now have hundreds of thousands of trees and shrubs planted on the three wholesale farms, and enough infrastructure and equipment to grow trees, shrubs,

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and flowers for multiple locations in west Texas.

Our wholesale operations are able to provide products to our retail nurseries, which we believe will allow us to offer competitive pricing, service and selection. Although we plan to divert our landscape trees, shrubs, plants and flowers to our retail stores as demand at such stores grows, we plan to continue our wholesale business for the foreseeable future. We currently grow a variety of landscape trees, shrubs, bedding plants and flowers on three farms in Texas and Arizona. Our major wholesale customers include retail nurseries, major retail outlets and landscape companies located in the southwest United States. We have experienced strong demand from retailers and landscape companies for our landscape products in the southwest United States over the last three years, even as our production capacity has continued to grow, and expect to be able to maintain relationships with a sufficient number of our customers in order to be able to sell inventory that is not shipped to our retail stores.

### OUR RETAIL BUSINESS

Our current retail operations consist of an approximately 4-acre retail nursery in Midland, Texas. Midland is a town of just over 100,000 people in West Texas. In December 2006, we entered into a two-year lease agreement with a buy-out provision with Marrs & Smith, Ltd. for an approximately 4-acre retail site in Odessa, Texas. Our rent under the lease is \$4,000 per month, and we have the option to purchase the property for \$861,704.33 on or after December 1, 2007, but before December 1, 2008. Odessa is a town of approximately 120,000 people in West Texas and is located approximately 20 miles from Midland.

In October 2005, we purchased a vacant 13,000 square foot building on 3.8 acres in Midland, Texas for the site of our first retail nursery. We completed a \$951,000 dollar conversion of the property, including a complete remodel of the building and the addition of 32,000 square feet of greenhouse and 40,000 feet of tree display area.

In 2005, we also purchased 7 acres of commercial property in San Angelo, Texas that shares an intersection with Wal-Mart, Lowe's and Sam's Club. We plan to either sell or develop the property. We have not entered into any agreements with respect to the sale or development of this site; however, the property is currently listed for sale.

As the availability of capital and other business factors permit, we plan to aggressively open retail centers and ramp up our wholesale operations in the coming years in Texas and surrounding areas. There are over 30 million people in this region, which we believe could allow us to build a large number of nurseries to compete in these markets.

### LIQUIDITY AND CAPITAL RESOURCES

CAPITAL COMMITMENTS AND EXPENDITURES. The following table discloses aggregate information about our contractual obligations including long-term debt, operating and capital lease payments, office lease payments, contractual service agreements and the periods in which payments are due as of December 31, 2006.

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LESS THAN  
1 YEAR

2-3 YEARS

4-5 YEARS



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| CONTRACTUAL OBLIGATIONS                   | TOTAL            | (1/1/07 TO<br>12/31/07) | (1/1/08 TO<br>12/31/09) | (1/1/10 TO<br>12/31/11) |
|---|------------------|-------------------------|-------------------------|-------------------------|
| Operating leases                          | --               | --                      | --                      | --                      |
| Capital leases                            | 290,529          | 69,313                  | 159,839                 | 61,377                  |
| Office lease                              | --               | --                      | --                      | --                      |
| Contractual service agreements            | --               | --                      | --                      | --                      |
| Notes payable                             | 7,608,166        | 4,095,607               | 2,311,472               | 271,614                 |
| <b>Total contractual cash obligations</b> | <b>7,898,695</b> | <b>4,164,920</b>        | <b>2,471,311</b>        | <b>332,991</b>          |

During the six month ended December 31, 2006, we entered into convertible and nonconvertible notes in an aggregate principal amount of \$960,970.42 with interest rates ranging from 9% per annum to 24% per annum. As of December 31, 2006, the total amount owed under outstanding notes payable was \$7,608,166 in the aggregate, \$4,095,607 of which is due and payable within a period of one year. Of such notes, as of December 31, 2006, as a result of extensions, none are in default.

As of December 31, 2006, we had \$76,848 in cash and cash equivalents. This represents a decrease of \$35,067 compared to June 30, 2006. Cash used during the six months ended December 31, 2006 includes approximately \$844,000 used in operations as well as approximately \$118,000 provided by investing activities. Sources of cash during the six months ended December 31, 2006 included a net amount of approximately \$691,000 from financing activities. Of the approximately \$691,000 of net cash provided by financing activities, approximately \$632,000 was from net cash received less payments made on notes, and \$64,000 represented the proceeds from issuance of common stock less offering costs. The difference between the approximately \$691,000 of net cash provided by financing activities and the cash itemized above represented new notes payable, advances from related parties, payments on related party advances and loan costs and payments on capital lease obligations.

There were no material capital expenditures for the quarter ended December 31, 2006.

We anticipate making capital expenditures during Fiscal 2007. Specifically, resources permitting, we plan to spend approximately \$500,000 for inventory sold during Fiscal 2006, inventory and a new watering system, structural repairs, and other remodeling for the Odessa location, and \$1,000,000 for a third retail nursery.

LIQUIDITY. The following table reflects selected balance sheet data as of December 31, 2006:

|                                | DECEMBER 31, 2006 |
|--------------------------------|-------------------|
| BALANCE SHEET DATA:            |                   |
| Cash and cash equivalents..... | 76,848            |
| Working capital (deficit)..... | (2,852,522)       |
| Total assets.....              | 9,217,677         |
| Retained deficit.....          | (4,172,184)       |
| Stockholders' equity.....      | (358,860)         |

As of December 31, 2006, we had \$76,848 in cash and cash equivalents, total current assets of \$2,971,902 and current liabilities of \$5,824,424, representing a current working capital deficit of (\$2,852,522). Our current liabilities as of December 31, 2006 include a \$2,085,653 balance on secured

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convertible notes due within one year, and a \$2,009,955 principal balance on secured and unsecured non-convertible notes payable due within one year.

With respect to the current portion of our notes payable, we believe that most of the holders of the convertible and non-convertible notes coming due in the next year will either convert such debt to equity or replace existing notes with notes with deferred payment dates. To the extent that does not occur, we believe that we can raise capital sufficient to repay the current portion of our long term debt through the issuance of additional notes and the sale of equity securities and warrants.

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In addition, members of our management have informally agreed to provide up to \$400,000 of short-term financing to us. Such financing bears interest at 12% per annum. Management may demand payment on 30 days written notice.

Other than the informal and nonbinding commitments from management, we do not have any specific commitments from third parties to provide financing needed to cover any capital shortfalls with respect to our operations, planned capital expenditures or near-term debt obligations. We caution that, particularly in light of the early stage of our business, such financing may not be available on favorable terms, or at all. We may be compelled to divert substantial portions of our existing cash and future cash flow to the repayment of debt, which would limit our ability to replace or expand inventory and acquire additional farms. This would have an adverse affect on revenues in the coming years. Certain of such debt is secured by our real property, and holders of the unsecured debt have standard remedies available to creditor and secured creditors. If we were to default on such notes and the holders were to exercise their remedies, we would incur substantial legal expenses, penalties and related costs and could be forced to seek bankruptcy protection or to discontinue operations.

Our consolidated financial statements have been prepared on the assumption that our Company will continue as a going concern. Our independent registered public accounting firm has issued its report dated August 12, 2006 that includes an explanatory paragraph stating that recurring losses raise substantial doubt about our ability to continue as a going concern. It has been necessary to rely upon financing from the issuance of promissory notes and the sale of our equity securities to sustain operations in the past. Additional financing will be required if we are to continue as a going concern.

### OFF-BALANCE SHEET ARRANGEMENTS

There were no off-balance sheet arrangements at December 31, 2006.

### SEASONALITY

Our underlying wholesale business is the production and sale of trees, shrubs, bedding plants, and flowers to retailers and landscape companies. As with other agricultural businesses, our business is seasonal in nature with the majority of our revenues coming during the March-June and September-December periods.

On our Major Trees Tucson Farm, we generally harvest trees in the fall and generate over 80% of our revenues from that farm between October and December. Revenues from our Major Trees Tucson Farm during other months of the year are growing but are still small. Costs associated with the Major Trees Tucson Farm also peak during approximately the same period as we harvest the trees,

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transport them to market and conduct most of our planting activities.

On our S&S Plant Farm and the Major Trees Houston Farm, we generally harvest trees, shrubs, bedding plants and flowers between March and June and between September and December of each year. We generate substantially all of our revenues from those farms directly or indirectly through our retail operations at the Texas Landscape Center, during the same period. We also incur increased transportation, sales and planting expenses during that period.

The acquisition of the Texas-based farms and the commencement of our retail business has helped balance the seasonality of our business to some extent. Even so, we will continue to experience dramatic increases and decreases in revenue and expenses throughout the year and, as a result, our quarterly or multi-quarterly results will generally not be indicative of our annual results.

### CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Management is basing this discussion and analysis of our financial condition and results of operations on our consolidated financial statements. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our critical accounting policies and estimates, including those related to agricultural productions, inventories, property and

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equipment, acquisition costs and revenue recognition. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting policies affect the more significant judgments and estimates used in the preparation of our consolidated financial statements. These judgments and estimates affect the reported amounts of assets and liabilities and the reported amounts of revenues and expenses during the reporting periods. Changes to these judgments and estimates could adversely affect our future results of operations and cash flows.

- o Agricultural Production - We account for agricultural activities in accordance with Statement of Position 85-3, "Accounting by Agricultural Producers and Agricultural Cooperatives". All direct and indirect costs of growing crops are either accumulated as inventory or expensed as cost of goods sold. Permanent land development costs are capitalized and not depreciated. Limited-life land development costs and the development costs to bring long-life and intermediate-life plants into production are capitalized and depreciated using the straight-line method over the estimated useful lives of the assets.

- o Inventories - Growing crops inventory is stated at the lower of cost or market using the retail method as we have a large quantity of inventory items that have similar costs and markups; we do not have any individually significant items. Because our inventory has these characteristics, it is not beneficial to track inventory costs to each individual unit of inventory. Under the retail method, we count and extend our inventory at estimated sales prices, based upon historical sales, which we then multiply by our cost ratio to determine inventory at cost. Our cost ratio is determined by adding the total cost of the

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beginning inventory and all direct and indirect costs of growing crops divided by the total estimated sales price of ending inventory, based on historical sales, plus sales revenues. Raw material inventory is stated at the lower of market or cost using the first-in first-out (FIFO) method.

o Property and Equipment - Property and equipment are stated at cost or carryover basis. Expenditures for major renewals and betterments that extend the useful lives of property and equipment are capitalized upon being placed in service. Expenditures for maintenance and repairs are charged to expense as incurred. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. In accordance with Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", we periodically review our property and equipment for impairment.

o Revenue Recognition - Our revenue comes primarily from the sale of agricultural products. We recognize revenue from retail sales at the time of retail purchase. We recognize revenue from landscaping and wholesale customers when rights and risk of ownership have passed to the customer, there is persuasive evidence of a sales arrangement, product has been shipped (delivered or picked up by the customer), the price and terms are finalized and collection of the resulting receivable is reasonably assured.

### RESULTS OF OPERATIONS

THREE AND SIX MONTHS ENDED DECEMBER 31, 2006 COMPARED TO THREE AND SIX MONTHS ENDED DECEMBER 31, 2005

The following table reflects selected operational results for the Three and the Six Months Ended December 31, 2006 compared to the Three and the Six Months Ended December 31, 2005:

|                               | THREE MONTHS ENDED<br>DECEMBER 31<br>----- |              | SIX MONTHS ENDED<br>DECEMBER 31<br>----- |              |
|-------------------------------|--|--------------|--|--------------|
|                               | 2006<br>----                               | 2005<br>---- | 2006<br>----                             | 2005<br>---- |
| Statement of Operations Data: |  |              |  |              |
| REVENUE                       | \$ 720,045                                 | \$1,229,954  | \$1,021,821                              | \$1,432,737  |
| COST OF GOODS SOLD            | (302,691)                                  | (904,769)    | (536,318)                                | (1,087,789)  |
|                               | -----                                      | -----        | -----                                    | -----        |
| GROSS PROFIT                  | 417,354                                    | 325,185      | 485,503                                  | 344,948      |
| OPERATING EXPENSES            | (281,199)                                  | (230,560)    | (650,909)                                | (480,008)    |
|                               | -----                                      | -----        | -----                                    | -----        |
| LOSS FROM OPERATIONS          | 136,155                                    | 94,625       | (165,406)                                | (135,060)    |
| INTEREST AND OTHER EXPENSE    | (363,108)                                  | (288,743)    | (607,944)                                | (426,715)    |
|                               | -----                                      | -----        | -----                                    | -----        |
| NET LOSS                      | \$ (226,953)                               | \$ (194,118) | \$ (773,350)                             | \$ (561,775) |
|                               | -----                                      | -----        | -----                                    | -----        |
| LOSS PER COMMON SHARE         | (0.01)                                     | (0.01)       | (0.03)                                   | (0.02)       |
|                               | -----                                      | -----        | -----                                    | -----        |

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Our results of operations for the six months ended December 31, 2006 included the operations of our Major Trees Houston Farm, Major Trees Tucson Farm, S&S Plant Farm and the Texas Landscape Center. Our results of operations for the six months ended December 31, 2005 included our three farms but not the Texas Landscape Center.

REVENUE AND COSTS OF GOOD SOLD. Our revenues are derived primarily from the sale of plants, trees, shrubs and other retail nursery products. Revenues decreased from \$1,229,954 for the three months ended December 2005 to \$720,045 for the three months ended December 2006. Costs of Good Sold decreased from \$904,769 for the three months ended December 2005 to \$302,691 for the three months ended December 2006. Our revenue decreased due to cessation of unprofitable wholesale business through S&S Plant Farm and the cessation of approximately \$350,000 in wholesale business with the Texas region of Home Depot due to a high probability of sales returns from the Home Depot new vendor consignment model in the Texas region.

The California region of our Home Depot relationship which accounted for approximately \$265,000 in the quarter ended December 31, 2006, has not been affected by the termination of our Texas region; however, if the California region of Home Depot decides to use the pay by scan consignment model, we will likely terminate our relationship with Home Depot. We are currently working to diversify our customer base within the landscape market and we are selling the Major Trees' products through our own retail location which provides us with a higher margin sale.

Cost of goods sold decreased due to lower sales, and Cost of goods sold as a percentage of sales decreased from 73% for the three months ended December 2005 to 42% for the three months ended December 2006 as a result of eliminating low margin sales at S&S Plant Farm and having higher margins sales at Texas Landscape Center.

Revenues decreased from \$1,432,737 for the six months ended December 2005 to \$1,021,821 for the six months ended December 2006. Costs of Good Sold decreased from \$1,087,789 for the six months ended December 2005 to \$536,318 for the six months ended December 2006. Cost of goods sold decreased due to lower sales, and Cost of goods sold as a percentage of sales decreased from 76% for the six months ended December 2005 to 52.5% for the six months ended December 2006.

OPERATING EXPENSES. Operating expenses consist primarily of personnel expense associated with management, consulting fees, travel expenses, professional fees, general overhead and non-allocated depreciation. Operating expenses increased from \$230,560 for the three months ended December 2005 to \$281,199 for the three months ended December 2006. Operating expenses as a percentage of revenue increased from 19 % for the three months ended December 2005 to 39% for the three months ended December 2006. The increase in operating expense was due to increased wages and salaries, advertising, accounting/legal fees, and other general and administrative expenses associated with the addition of the Texas Landscape Center. We expect our operating expenses as a percentage of revenue to decrease through the remainder of the fiscal year ending June 30, 2007 ("fiscal 2007")..

Operating expenses increased from \$480,008 for the six months ended December 2005 to \$650,909 for the six months ended December 2006. Operating expenses as a percentage of revenue increased from 33.5% for the six months ended December 2005 to 63.7% for the six months ended December 2006.

OTHER EXPENSE. Other expense consists of interest paid on outstanding notes payable, amortization of deferred loan costs, noncash notes payable costs, stock conversions and losses on the disposal of fixed assets. Other expense increased from \$288,743 for the three months ended December 2005 to \$363,108 for

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the three months ended December 2006. An increase in other expenses was attributed to the additional financing during the current three months ended December 2006 over the prior year's three months ended December 2005. The majority of the increase in other expenses was a result of an increase in finance charges and interest expense due to an increase in indebtedness and interest on indebtedness. We expect our other expenses to increase as a percentage of revenue short-term and then to decrease as a percentage of revenue long-term as our short and long-term notes are paid off and converted to stock.

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Other expense increased from \$426,715 for the six months ended December 2005 to \$607,944 for the six months ended December 2006. An increase in other expenses was attributed to the additional financing during the current six months ended December 2006 over the prior year's six months ended December 2005.

NET LOSS. Our net loss increased from \$194,118 for the three months ended December 2005 to \$226,953 for the three months ended December 2006. The increase in net loss is due primarily to an increase in salaries and wages, interest expense and other general and administrative expenses. We expect our net loss to increase as a result of conversion expenses related to our convertible debt for the remainder of Fiscal 2007 and to decrease in the fiscal year ending June 30, 2008 as a result of higher sales, increased gross margins, and lower operating expenses as a percentage of sales.

Our net loss increased from \$561,775 for the six months ended December 2005 to \$773,350 for the six months ended December 2006.

### CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

We consider all forward-looking statements contained in this Quarterly Report to be covered by and to qualify for the safe harbor protection provided by Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended. Stockholders and prospective stockholders should understand that several factors govern whether the results described by any such forward-looking statement will be or can be achieved. Any one of those factors could cause actual results to differ materially from those projected in this report.

The forward-looking statements contained in this report include plans and objectives of management for future operations, plans relating to the products and predictions regarding our economic performance. Assumptions applicable to the foregoing involve judgments with respect to, among other things, future economic, competitive, and market conditions, future business decisions, and the time and money required to successfully complete development projects, all of which are difficult or impossible to predict accurately and many of which are beyond our control. Although we believe that the assumptions underlying the forward-looking statements are reasonable, any of those assumptions could prove inaccurate. Therefore, we cannot assure that the results contemplated in any of the forward-looking statements contained herein will be realized. The impact of actual experience and business developments may cause us to alter our marketing, capital expenditure plans, or other budgets, which may in turn affect our results of operations. In light of the inherent uncertainties in forward-looking statements, the inclusion of any such statement does not guarantee that our objectives or plans will be achieved. Among other risk factors to consider are the factors identified in the subsection entitled "Factors That May Affect Future Results" below.

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### FACTORS THAT MAY AFFECT FUTURE RESULTS

Our short and long-term success is subject to certain risks, many of which are substantial in nature. The following risk factors should be carefully considered, in addition to other risks identified in this report, when evaluating an investment in our common stock. Any one of these factors could cause actual results of operations to differ materially from projected results.

### RISK FACTORS

An investment in our common stock involves a high degree of risk. You should consider the following discussion of risks in addition to the other information in this Report before purchasing any shares of our common stock. In addition to historical information, the information in this Report contains forward-looking statements about our future business and performance. Our actual operating results and financial performance may be very different from what we expect as of the date of this Report. The risks described in this Report represent the risks that management has identified and determined to be material to our company. Additional risks and uncertainties not currently known to us, or that we currently deem to be immaterial, may also materially and adversely affect our business operations. Any of these risks could materially and adversely affect our business, results of operations and financial condition.

### RISKS REGARDING OUR COMPANY AND OUR BUSINESS

OUR LIMITED OPERATING HISTORY AND EVOLVING BUSINESS PLAN MAKE IT DIFFICULT FOR YOU TO EVALUATE OUR PERFORMANCE AND FORECAST OUR FUTURE.

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We were formed and began operations in 2002, have made several acquisitions of businesses and assets in the last 4 years and are in the process of expanding the focus of our business to include retail, as well as wholesale, nursery operations. We began operating tree, shrub and plant farms less than four years ago and are just entering into the retail nursery business. None of our key management personnel have any experience in the retail nursery business. Our limited operating history, recent acquisitions, and expanding business focus make it difficult for you to evaluate our ability to generate revenues, manage costs, create profits and generate cash from operations. Before investing in our common stock, you should consider the risks and difficulties we may encounter as a relatively new business, including risks related to our ability to

- o implement our business plan;
- o obtain capital necessary to continue operations and implement our business plan;
- o anticipate and adapt to changes in the market;
- o find, acquire and develop new wholesale and retail properties;
- o administer and manage our operations; and
- o successfully compete in the retail nursery industry.

If we fail to successfully manage these risks, our operations and financial condition will suffer, and we may fail.

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WE HAVE INCURRED SUBSTANTIAL LOSSES SINCE OUR INCEPTION AND MAY CONTINUE TO INCUR LOSSES IN THE FUTURE.

We have experienced net losses in each twelve-month period since inception, with a retained deficit of approximately \$4,172,184 as of December 31, 2006. As we continue to invest in the purchase of new properties or businesses, and to expand our wholesale and retail operations, it is unlikely we will become profitable in the near future. Even if we do become profitable, we may not be able to maintain profitability or to increase profitability in the future.

OUR ACCOUNTANTS HAVE INCLUDED AN EXPLANATORY PARAGRAPH IN OUR FINANCIAL STATEMENTS REGARDING OUR STATUS AS A "GOING CONCERN."

Our consolidated financial statements have been prepared on the assumption that our Company will continue as a going concern. Our independent registered public accounting firm has issued its report dated August 12, 2006 that includes an explanatory paragraph stating that recurring losses raise substantial doubt about our ability to continue as a going concern. Our product line is limited, and it has been necessary to rely upon financing from the issuance of promissory notes and the sale of our equity securities to sustain operations in the past. Additional financing will be required if we are to continue as a going concern.

IF WE CANNOT RAISE SUFFICIENT CAPITAL AT REASONABLE PRICES, WE MAY BE UNABLE TO MEET EXISTING OBLIGATIONS OR ADEQUATELY EXPLOIT EXISTING OR FUTURE OPPORTUNITIES.

As of December 31, 2006, we had \$76,848 in cash and cash equivalents and a working capital account deficit of \$2,852,522. We need to obtain significant additional working capital to implement our business plan of expanding our retail nursery operations and to be able to meet our financial obligations as they become due. We may not be able to raise the additional capital needed, or we may be forced to pay an extremely high price for capital. Factors affecting the availability and price of capital may include the following:

- o the availability and cost of capital generally;
- o our financial results;
- o market interest, or lack of interest, in our industry and business plan;
- o the success of our business;
- o the amount of our capital needs; and

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- o the amount of debt, options, warrants and convertible securities we have outstanding.

If we cannot raise sufficient capital or are forced to pay a high price for capital, we may be unable to meet current or future obligations or adequately exploit existing or future opportunities. If we are unable to obtain capital for an extended period of time, we may be forced to discontinue operations.

WE HAVE PLEDGED A SIGNIFICANT PORTION OF OUR ASSETS TO SECURE FINANCING AGREEMENTS, AND IF WE DEFAULT UNDER SUCH ARRANGEMENTS, OUR CREDITORS MAY FORECLOSE ON OUR PLEDGED ASSETS.



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We have pledged substantially all of our assets to secure notes payable funding each of our farms and commercial properties and to secure other indebtedness. Governing security agreements grant our creditors the rights and remedies that are commonly provided a secured creditor. If we default under such arrangements, such creditors may foreclose on, seize, and dispose of all pledged assets. If this were to occur, we would be forced to discontinue operations.

OUR EXPANSION INTO THE RETAIL NURSERY BUSINESS CREATES NUMEROUS ADDITIONAL RISKS.

We opened our first retail nursery in Midland, Texas and plan to establish additional retail stores throughout Texas and the surrounding area over the next several years. Our business plans anticipate our becoming an integrated wholesale retail operation. Our foray into the retail nursery business may fail for various reasons, including the following:

- o We do not have experience in the retail nursery business and may have failed to properly anticipate marketing needs, operating costs, inventory costs, competition for retail employees, its affect on our wholesale business and other important aspects of the nursery retail business.
- o We may be unable to draw customers from, and compete with, large stores such as Home Depot or Wal-Mart, which dominate the markets we hope to penetrate. Such stores have established reputations, customer bases and significant amounts of capital. Such capital could be used to increase their advertising, offer goods at a price that is below our production or purchase costs (even if at a short-term loss) or aggressively compete in other ways.
- o If initial sales are slower than expected, we may not have, or may be unable to obtain, the capital necessary to continue operation of our initial retail store or subsequent stores until sales expand.
- o We may be unable to supply all variety or quantities of trees, shrubs, flowers and other plants for our retail store. If not, plant inventory may not be available from other sources or may be available only at a high cost.
- o We do not have, or expect to have, in place long-term supply agreements for non-plant items typically sold at retail stores, such as containers, fertilizers and tools. We may be unable to purchase such inventory at a cost that will permit us to be competitive with the big box stores on those items.

We have invested significantly in, and borrowed extensively in order to fund, our new retail nursery business. The failure of our retail business to grow as expected or for individual stores to become profitable within a reasonable time after opening would likely create a significant liquidity problem and otherwise materially adversely affect our business, our operations, and our financial condition.

WE ARE REQUIRED TO MAKE PAYMENTS UNDER OUTSTANDING NOTES IN AMOUNTS EXCEEDING OUR EXISTING CASH AND CASH EQUIVALENTS BEGINNING IN 2007.

We have issued convertible and nonconvertible notes to fund operations having a principal amount of \$7,608,166 as of December 31, 2006. Of these notes, \$6,107,087 are secured by our farming and commercial properties, and by trees contained in inventory. As of December 31, 2006, our monthly interest payment with respect to such notes was approximately \$60,000 per month, and we are required to begin paying down principal on these notes at various times

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beginning in 2007.

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The amounts payable under our outstanding notes in the current fiscal year exceed our current cash and cash equivalents. If we default on payments under these notes, the holders will have the right to accelerate principal and interest payments and pursue remedies available at law and under governing documents. The exercise of such remedies would likely result in our insolvency.

OUR WHOLESALE BUSINESS HAS HISTORICALLY BEEN DEPENDENT UPON A FEW CUSTOMERS, AND UNTIL OUR RETAIL OPERATIONS ARE DEVELOPED TO THE POINT WHERE WE CAN USE SUBSTANTIALLY ALL OF OUR WHOLESALE PRODUCTS, WE WILL CONTINUE TO BE VULNERABLE TO ACTIONS BY A FEW CUSTOMERS.

In 2006, Home Depots located in the Texas region adopted a pay by scan consignment model, which shifted much of the risk of their sales to their suppliers. We terminated our relationship with Home Depot in such region, and this termination caused an approximately \$350,000 reduction in revenue for the three months in ended December 31, 2006, compared to the same period in 2005. Home Depots in the California region accounted for approximately \$265,000 in revenue in the quarter ended December 31, 2006. If our relationship with Home Depot in the California region is terminated, or we lose another significant customer, our revenues will be harmed for the short term, and possibly for the long term.

WE MAY BE UNABLE TO SELL A PORTION OF OUR PROPERTY IN SAN ANGELO, TEXAS OR OTHERWISE OBTAIN CAPITAL IN ORDER TO BUILD A RETAIL STORE ON THAT SITE, WHICH IS AN IMPORTANT COMPONENT OF OUR BUSINESS PLAN.

We own approximately 7 acres of commercial property in San Angelo, Texas, a portion of which we plan to sell to partially fund the construction of a retail store. We have listed such property for sale, but do not have any commitments from any parties to purchase such property. Even if a portion of the San Angelo property were sold, we would likely need additional capital in order to complete the construction of a retail store on that site. We do not have the capital in order to build the retail store and do not have any commitments to provide capital. Because we are unprofitable and already highly leveraged, we may be unable to obtain capital necessary to commence or complete construction of a retail store. Even if we are able to obtain needed capital, we may not obtain it on a timely basis and may be forced to pay a high price for capital. Our business plan anticipates that we will be able to complete construction of, and open, a store in San Angelo Texas by the spring of 2008, which is the primary revenue period for a retail nursery. If we fail, because of the absence of capital or for other reasons, to complete timely construction of that store, our revenues for 2008 will be less than expected, and our results of operations will be harmed, in part because we will continue to have debt obligations associated with the San Angelo site but may not have a commensurate amount of revenue in order to fund the debt.

WE MAY BE UNABLE TO CONTINUE TO IDENTIFY APPROPRIATE ACQUISITION TARGETS OR CONSUMMATE ACQUISITIONS OF THOSE TARGETS, AND IF WE ARE UNABLE TO DO SO OUR BUSINESS WILL NOT CONTINUE TO GROW AS PLANNED.

Our business plan anticipates growth in part through continued acquisition of farming and retail properties or businesses. We may be unable to implement that acquisition strategy for several reasons, including the following:

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- o We may be unable to locate suitable nursery businesses or properties for acquisition for various reasons, including:
  - o the absence of such businesses or properties;
  - o our lack of knowledge of such businesses or properties or the fact that they are for sale;
  - o our lack of sufficient working capital to conduct an adequate search for potential acquisition targets, and to conduct the due diligence necessary to evaluate the appropriateness of a potential target; and
  - o our lack of expertise or experience in evaluating or operating the types of businesses or properties that are for sale.
- o The owners of businesses and properties that we are interested in acquiring may be unwilling to sell to us for various reasons, including:
  - o an unwillingness to accept our restricted equity securities or a promissory note as consideration;
  - o a desire to receive cash and a lack of confidence in our ability to obtain the cash necessary to close;
  - o concerns with our ability to operate the business profitably or appropriately, and
  - o a desire to be acquired by a larger company for strategic or personal reasons (including the desire to be employed by a larger, more stable acquirer).
  - o We may be unable to raise the capital necessary to purchase those businesses or properties that we identify as potential acquisition targets quickly enough or at all in order to be able to consummate desired acquisitions.

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If we cannot continue to identify appropriate acquisition targets and consummate acquisitions, our business will not continue to grow as planned.

WE MAY BE UNABLE TO MANAGE SIGNIFICANT GROWTH.

To successfully implement our business strategy, we must establish and achieve substantial growth in our customer base through expansion of production and sales from existing properties, through business acquisitions, and through expansion into the retail nursery business. If achieved, significant growth would place significant demands on our management and systems of financial and internal controls, particularly because of the number of places of businesses from which we operate or expect to operate. Moreover, significant growth would require an increase in the number of our personnel, particularly within sales, accounting and management. The market for such personnel remains highly competitive, and we may not be able to attract and retain the qualified personnel required by our business strategy. If successful in expanding our business, we may outgrow our present management capacity, placing additional strains on our human resources in trying to locate, manage and staff multiple locations. If we are unable to adequately manage our projected growth, our operations and financial condition may fail to improve, or even deteriorate.

WE ARE DEPENDENT UPON KEY PERSONNEL, AND THE LOSS OF SUCH PERSONNEL COULD SIGNIFICANTLY IMPAIR OUR ABILITY TO IMPLEMENT OUR BUSINESS PLAN.

We are highly dependent upon the efforts of management, particularly Kirk Fischer, our Chairman and Chief Executive Officer, KC Holmes, our President and Chief Financial Officer, and Jim Fischer, our Vice President of Arizona Tree Operations. Competition for management personnel is intense, and the number of

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qualified managers knowledgeable about, and interested in, the tree and shrub nursery industry is limited. As a result, we may be unable to retain our key management employees or attract other highly qualified employees in the future. In addition, the large number of shares of common stock issued to our officers and directors to date are not subject to repurchase rights if such persons terminate employment with us, decreasing our ability to provide equity-based incentive for new management. We may be required to offer significant salaries and equity-based compensation in order to retain or attract qualified management personnel and key employees. If we are unsuccessful in retaining or attracting such employees, the reduction in the quantity or quality of personnel may lead to a decline in our production, sales or service capacity.

OUR RETAIL CENTER IS OUR PRIMARY SOURCE OF REVENUE THE COMPETITIVENESS OF OUR PRICES IS DEPENDENT UPON OUR FARMS' ABILITIES TO PROVIDE A SUBSTANTIAL AMOUNT OF OUR INVENTORY.

Our retail center is our primary source of revenue and our ability to offer competitive prices will be dependent upon our ability to produce a substantial portion of our inventory on our farms. The various plant varieties that we grow on the farms are subject to risks associated with disease, insects, weather, drought, fire and other natural hazards. We cannot prevent or predict the impact of disease, insects, weather, drought, fire or other natural hazards on our trees, shrubs and plants. If our trees, shrubs and plants we grow are damaged or destroyed by any of those elements, we could suffer a significant loss of revenue and assets. The loss would be particularly significant if the affected plants were the Eldarica Pine, which accounted for approximately 46% of our revenue in Fiscal 2005 and 28% of our sales in Fiscal 2006.

TRADING IN OUR COMMON STOCK IS THIN, AND THERE IS A LIMIT TO THE LIQUIDITY OF OUR COMMON STOCK.

Our common stock is quoted on the OTC Pink Sheets but experiences extremely low volume and is traded on a sporadic basis. Trading in our common stock is likely to be dominated by a few individuals. Because of the thinness of the market for our stock, the price of our common stock may be subject to manipulation by one or more stockholders and may increase or decrease significantly because of buying or selling by a single stockholder. In addition, the low volume of trading limits significantly the number of shares that one can purchase or sell in a short period of time. Consequently, an investor may find it more difficult to dispose of large numbers of shares of our common stock or to obtain a fair price for our common stock in the market.

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EVEN IF A BROADER MARKET FOR OUR COMMON STOCK DEVELOPS, THE MARKET PRICE FOR OUR COMMON STOCK WILL LIKELY CONTINUE TO BE VOLATILE AND MAY CHANGE DRAMATICALLY AT ANY TIME.

Our common stock is quoted on the OTC Pink Sheets, but experiences extremely low volume and is traded on a sporadic basis. Even if a broader market for our common stock develops, the market price of our common stock, like that of the securities of other early-stage companies, can be expected to be highly volatile. Our stock price may change dramatically as the result of announcements of our quarterly results, the execution or termination of significant contracts, significant litigation or other factors or events that would be expected to affect our business or financial condition, results of operations and other factors specific to our business and future prospects. In addition, the market price for our common stock may be affected by various factors not directly

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related to our business, including the following:

- o intentional manipulation of our stock price by existing or future shareholders;
- o short selling of our common stock or related derivative securities;
- o a single acquisition or disposition, or several related acquisitions or dispositions, of a large number of our shares;
- o the interest, or lack of interest, of the market in our business sector, without regard to our financial condition or results of operations;
- o the adoption of governmental regulations and similar developments in the United States or abroad that may affect our ability to offer our products and services or affect our cost structure; and
- o economic and other external market factors, such as a general decline in market prices due to poor economic indicators or investor distrust.

OBTAINING ADDITIONAL CAPITAL THROUGH THE FUTURE SALE OF COMMON STOCK AND DERIVATIVE SECURITIES WILL RESULT IN DILUTION OF SHAREHOLDER INTERESTS.

We plan to raise additional funds in the future by issuing additional shares of common stock, or securities such as convertible notes, options, warrants or preferred stock that are convertible into common stock. Any such sale of common stock or other derivative securities will lead to further dilution of the equity ownership of existing holders of our common stock.

OUR COMMON STOCK IS A "LOW-PRICED STOCK" AND SUBJECT TO REGULATION THAT LIMITS OR RESTRICTS THE POTENTIAL MARKET FOR OUR STOCK.

Shares of our common stock may be deemed to be "low-priced" or "penny stock," resulting in increased risks to our investors and certain requirements being imposed on some brokers who execute transactions in our common stock. In general, a low-priced stock is an equity security that:

- o Is priced under five dollars;
- o Is not traded on a national stock exchange, the Nasdaq National Market or the Nasdaq SmallCap Market;
- o May be listed in the OTC Pink Sheets or the OTC Bulletin Board;
- o Is issued by a company that has less than \$5 million in net tangible assets (if it has been in business less than three years) or has less than \$2 million in net tangible assets (if it has been in business for at least three years); and
- o Is issued by a company that has average revenues of less than \$6 million for the past three years.

We believe that our common stock is presently a "penny stock." At any time the common stock qualifies as a penny stock, the following requirements, among others, will generally apply:

- o Certain broker-dealers who recommend penny stock to persons other than established customers and accredited investors must make a special written suitability determination for the purchaser and receive the purchaser's written agreement to a transaction prior to sale.
- o Prior to executing any transaction involving a penny stock, certain broker-dealers must deliver to certain purchasers a disclosure schedule explaining the risks involved in owning penny stock, the broker-dealer's duties to the customer, a toll-free telephone number for inquiries about the broker-dealer's disciplinary history and the customer's rights and remedies in case of fraud or abuse in the sale.

- o In connection with the execution of any transaction involving a penny stock, certain broker-dealers must deliver to certain purchasers the following:
- o bid and offer price quotes and volume information;
- o the broker-dealer's compensation for the trade;
- o the compensation received by certain salespersons for the trade;
- o monthly accounts statements; and a written statement of the customer's financial situation and investment goals.

ITEM 3. CONTROLS AND PROCEDURES

(a) Based on the evaluation of our "disclosure controls and procedures" (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) or 15d-15(e)) required by paragraph (b) of Rules 13a-15 or 15d-15, our chief executive officer and our chief financial officer have concluded that, as of December 31, 2006, our disclosure controls and procedures were effective in ensuring that information required to be disclosed by the Company in reports that it files under the Exchange Act is recorded, processed, summarized and reported within the time periods required by governing rules and forms.

(b) There have been no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Exchange Act Rules 13a-15 or 15d-15 that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are not aware of any pending or threatened legal proceedings that, singly or in the aggregate, would reasonably be expected to have a material adverse effect on our business, financial condition, or results of operations.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Set forth below is information regarding all equity securities sold Subsequent to September 30, 2006 (unless previously reported).

Between October and December 2006, the Company issued 58,182 shares of common stock for \$32,000 in cash to individual investors. The offer and sale of such shares of our common stock were effected in reliance upon the exemptions for sales of securities not involving a public offering, as set forth in Section 4(2) of the Securities Act and rules promulgated thereunder, based upon the following: (a) the investors confirmed to us that they were "accredited investors," as defined in Rule 501 of Regulation D promulgated under the Securities Act and had such background, education and experience in financial and business matters as to be able to evaluate the merits and risks of an investment in the securities; (b) there was no public offering or general solicitation with respect to each offering; (c) the investors were provided with certain disclosure materials and all other information requested with respect to our company; (d) the investors acknowledged that all securities being purchased were "restricted securities" for purposes of the Securities Act, and agreed to transfer such securities only in a transaction registered under the Securities Act or exempt from registration under the Securities Act; and (e) a legend was placed on the certificates representing each such security stating that it was

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restricted and could only be transferred if subsequently registered under the Securities Act or transferred in a transaction exempt from registration under the Securities Act.

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In November 2006, we issued 100,000 shares of our common stock valued at \$82,500, or \$0.55 per share to Marrs & Smith, Ltd. in connection with our two-year with buyout option lease agreement for a 4-acre retail location in Odessa, Texas. The offer and sale of such shares of our common stock were effected in reliance upon the exemptions for sales of securities not involving a public offering, as set forth in Rule 506 promulgated under the Securities Act and in Section 4(2) of the Securities Act, based upon the following: (a) the investors confirmed to us that they were "accredited investors," as defined in Rule 501 of Regulation D promulgated under the Securities Act and had such background, education and experience in financial and business matters as to be able to evaluate the merits and risks of an investment in the securities; (b) there was no public offering or general solicitation with respect to each offering; (c) the investors were provided with certain disclosure materials and all other information requested with respect to our company; (d) the investors acknowledged that all securities being purchased were "restricted securities" for purposes of the Securities Act, and agreed to transfer such securities only in a transaction registered under the Securities Act or exempt from registration under the Securities Act; and (e) a legend was placed on the certificates representing each such security stating that it was restricted and could only be transferred if subsequently registered under the Securities Act or transferred in a transaction exempt from registration under the Securities Act.

In October 2006, we issued 8,572 shares of our common stock valued at \$15,585, or \$0.55 per share. The shares are related to a private placement that closed in the prior quarter and were issued voluntarily in order to preserve shareholder confidence and relations. The offer and sale of such shares of our common stock were effected in reliance upon the exemptions for sales of securities not involving a public offering, as set forth in Rule 506 promulgated under the Securities Act and in Section 4(2) of the Securities Act, based upon the following: (a) the investors confirmed to us that they were "accredited investors," as defined in Rule 501 of Regulation D promulgated under the Securities Act and had such background, education and experience in financial and business matters as to be able to evaluate the merits and risks of an investment in the securities; (b) there was no public offering or general solicitation with respect to each offering; (c) the investors were provided with certain disclosure materials and all other information requested with respect to our company; (d) the investors acknowledged that all securities being purchased were "restricted securities" for purposes of the Securities Act, and agreed to transfer such securities only in a transaction registered under the Securities Act or exempt from registration under the Securities Act; and (e) a legend was placed on the certificates representing each such security stating that it was restricted and could only be transferred if subsequently registered under the Securities Act or transferred in a transaction exempt from registration under the Securities Act.

On January 3, 2007, we entered into a conversion request with the holder of a \$150,000 Promissory Note pursuant to which it was converted, at the rate of \$0.30 per share, for a total of 500,000 shares. The offer and sale of such shares of our common stock were effected in reliance upon the exemptions for sales of securities not involving a public offering, as set forth in Section 4(2) of the Securities Act and rules promulgated thereunder, based upon the following: (a) the investors confirmed to us that it was an "accredited

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investors," as defined in Rule 501 of Regulation D promulgated under the Securities Act and had such background, education and experience in financial and business matters as to be able to evaluate the merits and risks of an investment in the securities; (b) there was no public offering or general solicitation with respect to each offering; (c) the investor was provided with certain disclosure materials and all other information requested with respect to our company; (d) the investor acknowledged that all securities being purchased were "restricted securities" for purposes of the Securities Act, and agreed to transfer such securities only in a transaction registered under the Securities Act or exempt from registration under the Securities Act; and (e) a legend was placed on the certificates representing each such security stating that it was restricted and could only be transferred if subsequently registered under the Securities Act or transferred in a transaction exempt from registration under the Securities Act.

On January 3, 2007, we entered into a conversion request with the holder of a \$50,000 Promissory Note pursuant to which it was converted, at the rate of \$0.55 per share, for a total of 90,909 shares. The offer and sale of such shares of our common stock were effected in reliance upon the exemptions for sales of securities not involving a public offering, as set forth in Section 4(2) of the Securities Act and rules promulgated thereunder, based upon the following: (a) the investor confirmed to us that it was an "accredited investor," as defined in Rule 501 of Regulation D promulgated under the Securities Act and had such background, education and experience in financial and business matters as to be able to evaluate the merits and risks of an investment in the securities; (b) there was no public offering or general solicitation with respect to each offering; (c) the investor was provided with certain disclosure materials and all other information requested with respect to our company; (d) the investor acknowledged that all securities being purchased were "restricted securities" for purposes of the Securities Act, and agreed to transfer such securities only in a transaction registered under the Securities Act or exempt from registration under the Securities Act; and (e) a legend was placed on the certificates representing each such security stating that it was restricted and could only be transferred if subsequently registered under the Securities Act or transferred in a transaction exempt from registration under the Securities Act.

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### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITIES HOLDERS

None

### ITEM 5. OTHER INFORMATION

On November 1, 2006 we executed a Promissory Note Extension of Trust for four unsecured Promissory Notes, one originally entered into and then extended on August 15, 2006 and three originally entered into between July 28, 2006 and August 11, 2006 between Penge Corp and Rocky Fischer. Under the Modification, the holder agreed to extend the terms on a month to month basis with the ability to call the notes due with 30 days notice.

On December 1, 2006 we executed a Promissory Note Extension of Trust for a Promissory Note dated October 2006 between Penge Corp and Swan & Gardiner, Ltd. Under the Modification, the holder agreed to extend the terms on a month to



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month basis with the ability to call the note due with 30 days notice.

On December 1, 2006 we executed a Promissory Note Extension of Trust for a Promissory Note dated June 2006 between Penge Corp and Philip Oleson. Under the Modification, the holder agreed to extend the terms on a month to month basis with the ability to call the note due with 30 days notice and holder also requested that the 2nd trust deed on San Angelo be recorded and a copy be provided.

On January 30, 2007 we executed a \$25,000 secured Promissory Note between Penge Corp and Corky and Linda Bosworth. The note is secured by trees at S&S Plant Farm valued at a wholesale value of \$100,000.

ITEM 6. EXHIBITS

See the Exhibit Index attached hereto following the signature page.

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SIGNATURES

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

Penge Corp

February 13, 2007  
-----  
Date

By: /s/ Kirk Fischer  
-----  
Kirk Fischer, Chief Executive Officer

February 13, 2007  
-----  
Date

By: /s/ KC Holmes  
-----  
KC Holmes, Chief Financial Officer

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EXHIBIT INDEX

| EXHIBIT NO. | EXHIBIT   | INCORPORATED BY REFERENCE/<br>FILED HEREWITH |
|-------------|---|--|
| 10.1        | Extension of four unsecured Promissory Notes between Penge Corp and Rocky Fischer, dated November 2006. | Filed herewith                               |

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|      |   |                |
|------|---|----------------|
| 10.2 | Extension of unsecured Promissory Note between Penge Corp and Phillip Oleson, dated December 2006.  | Filed herewith |
| 10.3 | Extension of unsecured Promissory Note between Penge Corp and Phillip Oleson, dated December 2006.  | Filed herewith |
| 10.4 | Extension of unsecured Promissory Note between Penge Corp and Swan & Gardiner, dated December 2006. | Filed herewith |
| 10.5 | Promissory Note between Penge Corp and Corky and Linda Bosworth, dated January 2007.                | Filed herewith |
| 31.1 | Section 302 Certification of Chief Executive Officer  | Filed herewith |
| 31.2 | Section 302 Certification of Chief Financial Officer  | Filed herewith |
| 32.1 | Section 906 Certification of Chief Executive Officer  | Filed herewith |
| 32.2 | Section 906 Certification of Chief Financial Officer  | Filed herewith |