

CHINA AUTOMOTIVE SYSTEMS INC  
Form 10-Q  
November 08, 2011

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

FORM 10-Q

(Mark one)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended September 30, 2011

Or

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

Commission file number: 000-33123

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

Delaware  
(State or other jurisdiction of incorporation or  
organization)

33-0885775  
(I.R.S. employer identification number)

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

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

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

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

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

Large accelerated filer   
Non-accelerated filer (Do not check if a smaller reporting company)

Accelerated filer   
Smaller reporting company

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

As of November 8, 2011, the Company had 28,083,534 shares of common stock issued and outstanding.

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Cautionary Statement

This quarterly report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. These statements relate to future events or the Company's future financial performance. The Company has attempted to identify forward-looking statements by terminology including "anticipates," "believes," "expects," "can," "continues," "could," "estimates," "expects," "may," "plans," "potential," "predicts," "should" or "will" or the negative of these terms or other comparable terminology. Such statements are subject to certain risks and uncertainties, including the matters set forth in this report or other reports or documents the Company files with the Securities and Exchange Commission from time to time, which could cause actual results or outcomes to differ materially from those projected. Although the Company believes that the expectations reflected in the forward-looking statements are reasonable, the Company cannot guarantee future results, levels of activity, performance or achievements. Undue reliance should not be placed on these forward-looking statements which speak only as of the date hereof. The Company undertakes no obligation to update these forward-looking statements. The Company's expectations are as of the date this Form 10-Q is filed, and the Company does not intend to update any of the forward-looking statements after the date this quarterly report on Form 10-Q is filed to confirm these statements to actual results, unless required by law. All of the forward-looking statements are qualified in their entirety by reference to the factors discussed under Item 1A. "Risk Factors" in the Company's Annual Report on Form 10-K for the year ended December 31, 2010 filed with the Securities and Exchange Commission.

## PART 1 — FINANCIAL INFORMATION

## Item 1. FINANCIAL STATEMENTS.

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

	Three Months Ended September 30,	
	2011	2010
Net product sales, including \$7,817,723 and \$1,717,483 to related parties for the three months ended September 30, 2011 and 2010	\$ 75,002,717	\$ 76,102,844
Cost of product sold, including \$2,842,267 and \$4,885,768 purchased from related parties for the three months ended September 30, 2011 and 2010	61,215,974	57,929,284
Gross profit	13,786,743	18,173,560
Add: Gain (loss) on other sales	465,950	(152,481)
Less: Operating expenses		
Selling expenses	2,170,775	2,095,321
General and administrative expenses	3,413,930	2,506,504
Research and development expenses	2,708,777	1,247,881
Total operating expenses	8,293,482	5,849,706
Income from operations	5,959,211	12,171,373
Add: Other income, net	48,891	-
Financial expenses, net	(1,279,008)	(707,527)
Gain on change in fair value of derivative	7,788,137	8,687,977
Income before income tax expenses and equity in earnings of affiliated companies	12,517,231	20,151,823
Less: Income taxes	1,068,548	1,866,157
Add: Equity in earnings of affiliated companies	42,817	-
Net income	11,491,500	18,285,666
Net income attributable to noncontrolling interest	(1,382,653)	(2,350,280)
Net income attributable to parent company	10,108,847	15,935,386
Allocation to convertible notes holders	(1,071,091)	(2,153,261)
Net income attributable to parent company's common shareholders	\$ 9,037,756	\$ 13,782,125
Net income attributable to parent company's common shareholders per share		
Basic	\$ 0.32	\$ 0.51
Diluted	\$ 0.10	\$ 0.26
Weighted average number of common shares outstanding		
Basic	28,083,534	27,112,689
Diluted	31,503,995	31,562,661

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

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

	Nine Months Ended September 30,	
	2011	2010
Net product sales, including \$30,474,574 and \$6,319,594 to related parties for the nine months ended September 30, 2011 and 2010	\$ 248,522,773	\$ 245,416,671
Cost of product sold, including \$12,972,362 and \$14,481,952 purchased from related parties for the nine months ended September 30, 2011 and 2010	199,950,452	184,897,834
Gross profit	48,572,321	60,518,837
Add: Gain on other sales	1,359,871	981,128
Less: Operating expenses		
Selling expenses	7,123,063	6,866,249
General and administrative expenses	10,868,767	8,567,854
Research and development expenses	6,609,136	4,291,044
Total operating expenses	24,600,966	19,725,147
Income from operations	25,331,226	41,774,818
Add: Other income, net	154,465	266,379
Financial expenses, net	(2,902,150)	(2,056,431)
Gain on change in fair value of derivative	19,373,520	14,122,730
Gain on convertible notes conversion	1,564,418	-
Income before income tax expenses and equity in earnings of affiliated companies	43,521,479	54,107,496
Less: Income taxes	4,314,912	6,442,971
Add: Equity in earnings of affiliated companies	129,363	-
Net income	39,335,930	47,664,525
Net income attributable to noncontrolling interest	(5,241,143)	(8,227,985)
Net income attributable to parent company	34,094,787	39,436,540
Allocation to convertible notes holders	(3,831,484)	(5,334,715)
Net income attributable to parent company's common shareholders	\$ 30,263,303	\$ 34,101,825
Net income attributable to parent company's common shareholders per share		
Basic	\$ 1.09	\$ 1.26
Diluted	\$ 0.50	\$ 0.87
Weighted average number of common shares outstanding		
Basic	27,881,821	27,078,180
Diluted	31,531,253	31,560,119

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

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

	Three Months Ended September 30,	
	2011	2010
Net income	\$ 11,491,500	\$ 18,285,666
Other comprehensive income:		
Foreign currency translation gain, net of tax	4,212,418	2,179,442
Comprehensive income	15,703,918	20,465,108
Comprehensive income attributable to noncontrolling interest	(2,112,396)	(2,750,677)
Comprehensive income attributable to parent company	\$ 13,591,522	\$ 17,714,431

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

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

	Nine Months Ended September 30,	
	2011	2010
Net income	\$ 39,335,930	\$ 47,664,525
Other comprehensive income:		
Foreign currency translation gain, net of tax	9,228,737	3,105,593
Comprehensive income	48,564,667	50,770,118
Comprehensive income attributable to noncontrolling interest	(6,842,591)	(8,779,852)
Comprehensive income attributable to parent company	\$ 41,722,076	\$ 41,990,266

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

China Automotive Systems, Inc.  
Condensed Unaudited Consolidated Balance Sheets

	September 30, 2011	December 31, 2010
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 76,067,212	\$ 49,424,979
Pledged cash deposits	20,368,026	20,983,891
Accounts and notes receivable, net, including \$9,716,604 and \$5,466,842 from related parties at September 30, 2011 and December 31, 2010	197,860,106	195,858,988
Advance payments and other, including \$1,061,303 and \$1,334,069 to related parties at September 30, 2011 and December 31, 2010	3,916,286	4,226,137
Inventories	51,304,394	36,870,272
Current deferred tax assets	3,525,332	3,511,421
<b>Total current assets</b>	<b>353,041,356</b>	<b>310,875,688</b>
Long-term assets:		
Other receivables, net, including \$432,287 and \$350,464 from related parties at September 30, 2011 and December 31, 2010	2,249,222	2,801,434
Long-term investments	3,426,863	3,162,136
Property, plant and equipment, net	81,641,156	75,380,747
Intangible assets, net	683,972	662,089
Advance payments for property, plant and equipment, including \$5,507,634 and \$7,534,440 to related parties at September 30, 2011 and December 31, 2010	7,303,422	9,373,977
Non-current deferred tax assets	3,915,647	3,271,594
<b>Total assets</b>	<b>\$ 452,261,638</b>	<b>\$ 405,527,665</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Bank loans	\$ 11,801,917	\$ 6,794,812
Accounts and notes payable, including \$1,584,274 and \$1,867,926 to related parties at September 30, 2011 and December 31, 2010	163,597,833	148,517,423
Convertible notes payable	-	30,000,000
Compound derivative liabilities	-	25,271,808
Customer deposits	1,019,821	720,883
Accrued payroll and related costs	4,866,414	4,927,200
Accrued expenses and other payables	23,361,401	29,072,710
Accrued pension costs	3,927,004	3,851,988
Taxes payable	4,302,174	6,860,946
Amounts due to shareholders/directors	355,512	353,817
Deferred tax liabilities	446,966	312,304
<b>Total current liabilities</b>	<b>213,679,042</b>	<b>256,683,891</b>
Long-term liabilities:		
Convertible notes payable	23,571,429	-
Compound derivative liabilities	2,156,715	-
Accrued make-whole redemption interest expense of convertible notes	6,967,774	-
Advances payable	975,625	603,983
<b>Total liabilities</b>	<b>247,350,585</b>	<b>257,287,874</b>
Commitments and contingencies		



Stockholders' equity:		
Preferred stock, \$0.0001 par value - Authorized - 20,000,000 shares; issued and outstanding – None	-	-
Common stock, \$0.0001 par value - Authorized - 80,000,000 shares; issued and outstanding – 28,083,534 shares and 27,175,826 shares at September 30, 2011 and December 31, 2010	2,808	2,717
Additional paid-in capital	38,676,931	28,565,153
Retained earnings-		
Appropriated	9,026,960	8,767,797
Unappropriated	92,815,475	58,979,851
Accumulated other comprehensive income	23,584,789	15,957,500
<b>Total parent company stockholders' equity</b>	<b>164,106,963</b>	<b>112,273,018</b>
Noncontrolling interests	40,804,090	35,966,773
<b>Total stockholders' equity</b>	<b>204,911,053</b>	<b>148,239,791</b>
Total liabilities and stockholders' equity	\$ 452,261,638	\$ 405,527,665

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

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

	Nine Months Ended September 30,	
	2011	2010
<b>Cash flows from operating activities:</b>		
Net income	\$ 39,335,930	\$ 47,664,525
<b>Adjustments to reconcile net income from continuing operations to net cash provided by operating activities:</b>		
Stock-based compensation	-	422,714
Depreciation and amortization	10,144,624	6,955,969
Allowance for doubtful accounts recovered	(78,263)	(1,127,767)
Deferred income taxes assets and liabilities	(250,819)	(540,385)
Equity in earnings of affiliated companies	(129,363)	-
Gain on convertible notes conversion	(1,564,418)	-
Gain on change in fair value of derivative	(19,373,520)	(14,122,730)
Other operating adjustments	116,271	324,963
<b>Changes in operating assets and liabilities:</b>		
<b>(Increase) decrease in:</b>		
Pledged deposits	1,459,912	(8,012,615)
Accounts and notes receivable	6,713,715	(22,430,886)
Advance payments and other	505,920	(678,156)
Inventories	(12,614,377)	(12,728,686)
<b>Increase (decrease) in:</b>		
Accounts and notes payable	8,504,008	33,298,924
Customer deposits	252,157	(34,138)
Accrued payroll and related costs	(249,117)	67,681
Accrued expenses and other payables	1,835,213	1,298,885
Accrued pension costs	(81,174)	137,283
Taxes payable	(2,798,154)	(891,031)
<b>Net cash provided by operating activities</b>	<b>31,728,545</b>	<b>29,604,550</b>
<b>Cash flows from investing activities:</b>		
Decrease (increase) in other receivables	624,969	(2,221,935)
Cash received from disposal of equipment	134,039	396,489
Cash paid to acquire property, plant and equipment	(10,805,460)	(24,005,602)
Cash paid to acquire intangible assets	(121,132)	(60,586)
<b>Net cash used in investing activities</b>	<b>(10,167,584)</b>	<b>(25,891,634)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from bank loans	4,791,706	3,685,215
Dividends paid to the noncontrolling interest holders of joint-venture companies	(1,691,608)	(2,871,603)
Shares issued for stock options exercised	-	278,900
Increase (decrease) in amounts due to shareholders/directors	(19,938)	97,406
<b>Net cash provided by financing activities</b>	<b>3,080,160</b>	<b>1,189,918</b>
Effects of exchange rate on cash and cash equivalents	2,001,112	818,849
<b>Net increase in cash and cash equivalents</b>	<b>26,642,233</b>	<b>5,721,683</b>
Cash and cash equivalents at beginning of period	49,424,979	43,480,176
<b>Cash and cash equivalents at end of period</b>	<b>\$ 76,067,212</b>	<b>\$ 49,201,859</b>

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

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

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

	Nine Months Ended September 30,	
	2011	2010
Cash paid for interest	\$ 1,689,318	\$ 1,146,971
Cash paid for income taxes	\$ 7,189,788	\$ 5,362,363

SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:

	Nine Months Ended September 30,	
	2011	2010
Issuance of common shares for the conversion of convertible notes	\$ 10,111,869	\$ -

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

China Automotive Systems, Inc. and Subsidiaries  
Notes to Condensed Unaudited Consolidated Financial Statements  
Three Months and Nine Months Ended September 30, 2011 and 2010

1. Organization and Business

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

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

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

The Company owns the following aggregate net interests in seven Sino-foreign joint ventures, a wholly-owned subsidiary and two joint ventures organized in the PRC as of September 30, 2011 and 2010.

Name of Entity	Percentage Interest	
	September 30, 2011	December 31, 2010
Shashi Jiulong Power Steering Gears Co., Ltd., “Jiulong” 1	81.00%	81.00%
Jingzhou Henglong Automotive Parts Co., Ltd., “Henglong” 2	80.00%	80.00%
Shenyang Jinbei Henglong Automotive Steering System Co., Ltd., “Shenyang” 3	70.00%	70.00%
Zhejiang Henglong & Vie Pump-Manu Co., Ltd., “Zhejiang” 4	51.00%	51.00%
Universal Sensor Application Inc., “USAI” 5	83.34%	83.34%
Wuhan Jielong Electric Power Steering Co., Ltd., “Jielong” 6	85.00%	85.00%
Wuhu HengLong Automotive Steering System Co., Ltd., “Wuhu” 7	77.33%	77.33%
Jingzhou Hengsheng Automotive System Co., Ltd, “Hengsheng” 8	100.00%	100.00%
Jingzhou Henglong Automotive Technology (Testing) Center, “Testing Center” 9	80.00%	80.00%
Beijing Henglong Automotive System Co., Ltd., “Beijing Henglong” 10	50.00%	50.00%

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

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

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

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

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

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

7. Wuhu was established in 2006 and mainly engages in production and sales of automobile steering systems.
8. Hengsheng was established in 2007 and mainly engages in production and sales of automobile steering systems.
9. In December 2009, Henglong, a subsidiary of Genesis, formed Jingzhou Henglong Automotive Technology (Testing) Center, "Testing Center".
10. Beijing Henglong was established in 2010 and is mainly engaged in the design, development and manufacture of both hydraulic and electric power steering systems and parts. According to the joint venture agreement, the Company does not have voting control of Beijing Henglong. Therefore, the Company's consolidated financial statements do not include Beijing Henglong, and such investment is accounted for by the equity method.

2. Basis of Presentation and Significant Accounting Policies

(a) Basis of Presentation

Basis of Presentation – For the three months and nine months ended September 30, 2011 and 2010, the accompanying unaudited consolidated financial statements include the accounts of the Company and its subsidiaries. The subsidiaries include the seven Sino-foreign joint ventures, a wholly-owned subsidiary and two joint ventures organized in the PRC mentioned in Note 1. Significant inter-company balances and transactions have been eliminated upon consolidation. The unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America.

The accompanying interim condensed consolidated financial statements are unaudited, but in the opinion of the Company's management, contain all adjustments, which include normal recurring adjustments, necessary to present fairly the financial position, the results of operations and cash flows for the three months and nine months ended September 30, 2011 and 2010, respectively.

The consolidated balance sheet as of December 31, 2010 is derived from the Company's audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

Certain information and footnote disclosures normally included in financial statements that have been prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission, although the Company's management believes that the disclosures contained in these financial statements are adequate to make the information presented herein not misleading. For further information, refer to the financial statements and the notes thereto included in the Company's 2010 Annual Report on Form 10-K, as filed with the Securities and Exchange Commission.

The results of operations for the nine months ended September 30, 2011 are not necessarily indicative of the results of operations to be expected for the full fiscal year ending December 31, 2011.

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

(b) Recent Accounting Pronouncements

In July 2010, the FASB issued new disclosure guidance related to the credit quality of financing receivables and the allowance for credit losses. The guidance will require companies to provide more information about the credit quality of their financing receivables in the disclosures to financial statements including, but not limited to, significant purchases and sales of financing receivables, aging information and credit quality indicators. The Company adopted this accounting standard upon its effective date for years ending on or after December 15, 2010. The Company has evaluated the new disclosure requirement in accordance with the accounting guidance and the adoption did not have a significant impact on the Company's financial position, results of operations or cash flows.

In December 2010, FASB issued revised guidance on the "Disclosure of Supplementary Pro Forma Information for Business Combinations." The revised guidance specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual

reporting period only. The revised guidance also expands the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The revised guidance is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The Company adopted the new guidance as of January 1, 2011 and the adoption did not have a significant impact on the Company's financial position, results of operations or cash flows.

In 2011, the Financial Accounting Standards Board ("FASB") issued new accounting guidance that amends certain fair value measurement principles and disclosure requirements. The new guidance states that the concepts of highest and best use and valuation premise are only relevant when measuring the fair value of nonfinancial assets and prohibits the grouping of financial instruments for purposes of determining their fair values when the unit of account is specified in other guidance. The Company will adopt this accounting standard upon its effective date for periods ending on or after December 15, 2011, and does not anticipate that this adoption will have a significant impact on the Company's financial position or results of operations.

In 2011, the FASB issued new disclosure guidance related to the presentation of the Statement of Comprehensive Income. This guidance eliminates the current option to report other comprehensive income and its components in the statement of changes in equity. The standard requires an entity to present the total of comprehensive income, net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The Company will adopt this accounting standard upon its effective date for periods ending on or after December 15, 2011, and does not anticipate that this adoption will have any impact on the Company's financial position or results of operations.

(c) Significant Accounting Policies

Foreign Currencies – The Parent Company (CAAS) and Henglong USA Corporation (HLUSA) maintain their books and records in United States Dollars, "USD," their functional currency. The Company's subsidiaries based in the PRC and Genesis maintain their books and records in Renminbi, their functional currency. In accordance with ASC Topic 830, foreign currency transactions denominated in currencies other than the functional currency are remeasured into the functional currency at the rate of exchange prevailing at the balance sheet date for monetary items. Nonmonetary items are remeasured at historical rates. Income and expenses are remeasured at the rate in effect on the transaction dates. Transaction gains and losses, if any, are included in the determination of net income for the period.



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

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

In July 2004, the Company adopted a stock incentive plan. The maximum number of common shares for issuance under this plan is 2,200,000 with a period of 10 years. The stock incentive plan provides for the issuance, to the Company's officers, directors, management and employees, of options to purchase shares of the Company's common stock. Since the adoption of the stock incentive plan, the Company has issued 456,350 stock options under this plan, and there remain 1,743,650 stock options issuable in the future. As of September 30, 2011, the Company had 236,768 stock options outstanding.

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

**Comprehensive Income** – The Company has adopted ASC Topic 220, "Reporting Comprehensive Income." ASC Topic 220 establishes standards for the reporting and display of comprehensive income, its components and accumulated balances in a full set of general purpose financial statements. ASC Topic 220 defines comprehensive income to include all changes in equity except those resulting from investments by owners and distributions to owners, including adjustments to minimum pension liabilities, accumulated foreign currency translation, and unrealized gains or losses on marketable securities.

**Financial Instruments** – The Company adopted the provisions of ASC 815, "Derivatives and Hedging Activities," that address the determination of whether an instrument meets the definition of a derivative being indexed to a company's own stock for purposes of applying the scope exception as provided for in accordance with ASC 815-15. Upon adoption of the standard on the effective date, the Company bifurcated the conversion feature embedded in the Convertible Notes (see Note 13), classifying it in liabilities and measuring it at fair value at each reporting period, with changes reflected in earnings, until the Convertible Notes are settled.

**Fair Value Measurements** – For purposes of fair value measurements, the Company applies the applicable provisions of ASC 820, "Fair Value Measurements". Accordingly, fair value for the Company's financial accounting and reporting purposes represents the estimated price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the designated measurement date. With an objective to increase consistency and comparability in fair value measurements and related disclosures, the Financial Accounting Standard Board established the fair value hierarchy which prioritizes the inputs to valuation techniques used to measure fair value into three broad levels.

Level 1 Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. An active market for the asset or liability is a market in which

transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available. As at September 30, 2011 and December 31, 2010, the Company does not have any fair value assets and liabilities classified as Level 1.

Level 2 Inputs are other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability. As at September 30, 2011 and December 31, 2010, the Company does not have any fair value assets and liabilities classified as Level 2.

Level 3 Inputs are unobservable inputs for the asset or liability. Unobservable inputs are used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. However, the fair value measurement objective remains the same, that is, an exit price from the perspective of a market participant that holds the asset or owes the liability. Therefore, unobservable inputs shall reflect the reporting entity's own assumptions about the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk. The compound derivative liabilities are classified as Level 3 as the inputs reflect management's best estimate of what market participants would use in pricing the liability at the measurement date.

For a summary of changes in Level 3 derivative liabilities for the year ended December 31, 2010 and for the nine months ended September 30, 2011, please see note 14.

3. Pledged cash deposits

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

4. Accounts and notes receivable

The Company's accounts receivable at September 30, 2011 and December 31, 2010 are summarized as follows:

	September 30, 2011	December 31, 2010
Accounts receivable	\$ 112,822,032	\$ 122,379,968
Notes receivable 1	88,000,471	76,407,523
	200,822,503	198,787,491
Less: allowance for doubtful accounts	(2,962,397)	(2,928,503)
Balance at the end of the period	\$ 197,860,106	\$ 195,858,988

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

5. Inventories

The Company's inventories at September 30, 2011 and December 31, 2010 consisted of the following:

	September 30, 2011	December 31, 2010
Raw materials	\$ 15,692,397	\$ 11,394,670
Work in process	8,341,702	7,537,766
Finished goods	27,270,295	17,937,836
Balance at the end of the period	\$ 51,304,394	\$ 36,870,272

6. Other receivables

The Company's other receivables at September 30, 2011 and December 31, 2010 are summarized as follows:

	September 30, 2011	December 31, 2010
Other receivables 1	\$ 2,987,734	\$ 3,501,967
Less: allowance for doubtful accounts	(738,512)	(700,533)
Balance at the end of the period	\$ 2,249,222	\$ 2,801,434

- Other receivables consist of amounts advanced to both related and unrelated parties, primarily as unsecured demand loans, with no stated interest rate or due date. These receivables originate as part of the Company's normal operating activities.



## 7. Long term Investments

On September 30, 2011 and December 31, 2010, the Company's balance of long-term investment was \$3,426,863 and \$3,162,136, respectively. For the long-term investments in which the Company has no voting control, such investments were accounted for using the equity method or cost method.

On January 24, 2010, the Company invested \$3,095,414 to establish a fifty-fifty joint venture company, Beijing Henglong Automotive System Co., Ltd., "Beijing Henglong," with an unrelated party. The Company accounts for its operating results with the equity method of accounting. On September 30, 2011 and December 31, 2010, the Company has \$3,341,889 and \$3,080,598 of net equity in Beijing Henglong, respectively.

The Company's share of net assets and net income is reported in the consolidated financial statements as "long-term investment" on the consolidated balance sheets and "equity in earnings of affiliated companies" on the consolidated statements of operations. The Company's consolidated financial statements reflect the equity earnings of non-consolidated affiliates of \$42,817 and \$129,363 in the three months and nine months ended September 30, 2011, respectively, and nil in the same periods of 2010.

## 8. Property, plant and equipment

The Company's property, plant and equipment at September 30, 2011 and December 31, 2010 are summarized as follows:

	September 30, 2011	December 31, 2010
Land use rights and buildings	\$ 39,204,983	\$ 36,983,940
Machinery and equipment	94,200,741	81,905,845
Electronic equipment	6,217,672	5,840,308
Motor vehicles	3,154,196	2,902,738
Construction in progress	6,636,312	4,686,699
	149,413,904	132,319,530
Less: Accumulated depreciation	(67,772,748)	(56,938,783)
Balance at the end of the period	\$ 81,641,156	\$ 75,380,747

Depreciation expenses for the three months ended September 30, 2011 and 2010 were \$3,527,206 and \$2,097,734, respectively. Depreciation expenses for the nine months ended September 30, 2011 and 2010 were \$10,019,376 and \$6,910,835, respectively.

## 9. Intangible assets

The Company's intangible assets at September 30, 2011 and December 31, 2010 are summarized as follows:

	September 30, 2011	December 31, 2010
Costs:		
Patent technology	\$ 1,700,533	\$ 1,536,268
Management software license	552,592	509,221
	2,253,125	2,045,489
Less: Amortization	(1,569,153)	(1,383,400)

Balance at the end of the period	\$	683,972	\$	662,089
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For the three months ended September 30, 2011 and 2010, amortization expenses were \$43,856 and \$38,092, respectively. For the nine months ended September 30, 2011 and 2010, amortization expenses were \$125,248 and \$45,134, respectively.

10. Deferred Income Tax Assets

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

The components of estimated deferred income tax assets at September 30, 2011 and December 31, 2010 were as follows:

	September 30, 2011	December 31, 2010
<b>Deferred Tax Assets</b>		
Losses carryforward (U.S.)	\$ 2,802,742	\$ 2,422,312
Losses carryforward (PRC)	966,815	804,147
Product warranties and other reserves	3,075,577	2,871,844
Property, plant and equipment, net	3,863,175	3,271,594
Accrued make-whole interest expense for convertible notes	2,438,721	2,320,938
Share-based compensation	366,464	366,464
Bonus accrual	109,777	182,970
Other accruals	842,789	943,373
Others	152,946	314,795
Total deferred tax assets	14,619,006	13,498,437
Less: taxable temporary difference related to revenue recognition	(655,757)	(801,562)
Total deferred tax assets, net	13,963,249	12,696,875
Less: Valuation allowance	(6,522,270)	(5,913,860)
Total deferred tax assets, net of valuation allowance	\$ 7,440,979	\$ 6,783,015

As of September 30, 2011, the valuation allowance was \$6,522,270, including \$5,607,927 allowance for the Company's deferred tax assets in the U.S. and \$914,343 allowance for the Company's non-U.S. deferred tax assets. Based on the Company's current operations in the U.S., management believes that the deferred tax assets in the U.S. are not likely to be realized in the future. For the non-U.S. deferred tax assets, pursuant to certain tax laws and regulations in China, management believes such amount will not be used to offset future taxable income. No valuation allowance is made on the remaining deferred tax assets as management believes that these deferred tax assets will be realized in the future based on existing and expected operations.

#### 11. Bank loans

At September 30, 2011, the Company, through its Sino-foreign joint ventures, had outstanding fixed-rate short-term bank loans of \$11,801,917 with weighted average interest rate at 6.64% per annum. These loans are secured with some of the property and equipment of the Company, and are repayable within one year.

At December 31, 2010, the Company, through its Sino-foreign joint ventures, had outstanding fixed-rate short-term bank loans of \$6,794,812, with weighted average interest rate at 5.25% per annum. These loans are secured with some of the property and equipment of the Company and are repayable within one year.

#### 12. Accounts and notes payable

The Company's accounts and notes payable at September 30, 2011 and December 31, 2010 are summarized as follows:

	September 30, 2011	December 31, 2010
Accounts payable	\$ 106,160,958	\$ 95,726,549
Notes payable 1	57,436,875	52,790,874
Balance at the end of the period	\$ 163,597,833	\$ 148,517,423

1. Notes payable represent accounts payable in the form of bills of exchange whose acceptances are guaranteed and settlements are handled by banks. The Company has pledged cash deposits, notes receivable and certain property plant and machinery to secure notes payable granted by banks.



## 13. Convertible Notes payable

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

The Convertible Notes bear annual interest rates of 3%, 3.5%, 4%, 4.5%, 5% and 5% for each year of 2008, 2009, 2010, 2011, 2012 and 2013, respectively. The interest on the Convertible Notes shall be computed commencing from the issuance date and will be payable in cash in arrears semi-annually on January 15, and July 15 of each year with the first interest payable date on July 15, 2008. From and after the occurrence and during the continuance of an Event of Default defined in the relevant Convertible Notes agreements, the interest rate then in effect shall be increased by two percent (2%) until the event of default is remedied.

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

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

0-6 months:	125	%
6-12 months:	125	%
12-18 months:	135	%
18-24 months:	135	%
24-30 months:	145	%
30-36 months:	145	%
36-42 months:	155	%
42-48 months:	155	%

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

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

On each six month anniversary of the issuance date beginning August 15, 2008, the conversion price will be adjusted downward to the Reset Reference Price, as defined below, if the weighted average price for the twenty (20) consecutive trading days immediately prior to the applicable six month anniversary, the "Reset Reference Price", is less than 95% of the conversion price in effect as of such applicable six month anniversary date. The foregoing

notwithstanding, the conversion price will not be reduced via such reset provision to less than \$7.0822. The conversion price is also subject to weighted-average antidilution adjustments, but in no event will the conversion price be reduced to less than \$6.7417. If and whenever on or after the issuance date, the Company issues or sells its shares of Common Stock or other convertible securities, except for certain defined exempt issuances, for a consideration per share less than a price equal to the conversion price in effect on the issuance date immediately prior to such issue or sale, the original conversion price then in effect shall be adjusted by a weighted-average antidilution formula.

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

As of August 15, 2008, based on the inception conversion price and reset conversion price, the Convertible Note could be converted into 3,953,596 and 4,941,967 of common shares, respectively. At the commitment date, the stock price was \$6.09, and the "effective" conversion price was \$6.93. Accordingly, since the effective conversion price was higher than the market value of the stock, the debt instruments are not considered "in the money" and no beneficial conversion feature is present.

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

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

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

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

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

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

debt extinguishment and recorded in interest expense.

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

In connection with the Convertible Notes, the Company issued 1,317,864 detachable warrants, the “Warrants,” to purchase from the Company shares of common stock of the Company at the exercise price of \$8.8527 per share. On February 15, 2009, the warrants expired unexercised and the warrants were forfeited.

On the issuance date, February 15, 2008, the Company has evaluated the Convertible Notes for terms and conditions that would be considered to be features of embedded derivatives. Generally, such features would be required to be separated from the host contract and accounted for as derivative financial instruments when certain conditions are met. Certain features, such as the conversion option, were found to be exempt, as they satisfied the conditions as set forth in ASC Topic 815 (formerly paragraph 11(a) of SFAS 133) for instruments that are being (1) indexed to the Company's own stock, and (2) classified as equity in the financial position statement. Other features, such as puts, were not required to be bifurcated from the debt host as they are clearly and closely associated with the risk of the debt-type host instrument.

Upon the adoption of ASC 815-40 on January 1, 2009, the Company bifurcated the embedded conversion feature from the Convertible Debt and classified that financial instrument in liabilities at fair value. The Company has accounted for this change in accounting principle by reflecting the cumulative effect as an adjustment to its beginning retained earnings for the year ended December 31, 2009. The cumulative effect adjustment that the Company made is the difference between the amounts that it has recognized on the Convertible Notes payable (prior to the adoption of ASC 815-40) and the amounts that would have been recognized if the amended guidance had been effective on the issuance date of the Convertible Notes payable, which was February 15, 2008. The following table reflects the cumulative effect of the differences:

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

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

As indicated above, due to the Company's WAP Default on March 17, 2009, the Convertible Notes holders had the option to elect to exercise their rights to require the Company to redeem the Convertible Notes. The remaining amount of \$3,891,148 unamortized discount on the Convertible Notes was recorded to its full face value and the redemption make-whole amount of \$520,000 was accrued. On April 8, 2009, the Company and YA Global reached a settlement agreement, whereby under the terms of the settlement agreement, the Company paid a redemption amount of \$5,000,000 of principal and \$41,667 of interest to YA Global, and accrual of \$571,181 for make-whole redemption interest to YA Global was waived and accounted for as a gain on debt extinguishment. On September 22, 2009, LBCCA Liquidator revoked the redemption notices that were sent on April 24, 2009, and continued to hold the Company's Convertible Notes, of which the face value was \$30,000,000. The Company accepted such revocation on September 23, 2009.

On March 1, 2011, LBCCA Liquidator converted \$6,428,571 principal amount of the Convertible Notes at a conversion price of \$7.0822 per share, and the Company issued 907,708 shares of its common stock to the investor. On the conversion date, the market price of the common shares issued was \$10,111,869 (\$11.14 per share) and the value of the conversion consideration was \$11,676,287, including \$6,428,571 of principal, \$1,506,143 of coupon interest and make-whole amount payable and \$3,741,573 of derivative liabilities under such principal. The amount of coupon interest, make-whole and derivative liabilities included in the value of the conversion consideration were determined by pro-rating the accrued coupon interest, accrued make-whole amount and the fair value of the derivative liabilities based on the principal amount of the Convertible Notes converted as a percentage of the outstanding balance prior to their conversion. The Company recorded a gain on Convertible Notes conversion of \$1,564,418, which is the difference between the market price of the common stock and the conversion consideration.

On September 30, 2011 and December 31, 2010, the carrying value of the Company's Convertible Notes payable was \$23,571,429 and \$30,000,000, respectively.

14. Compound derivative liabilities

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

The Company's derivative financial instruments (liabilities) consisted of a compound embedded derivative that originated in connection with the Company's Convertible Note Payable and Warrant Financing Arrangement. Derivative liabilities are carried at fair value. The following table summarizes the compound derivative liabilities as of September 30, 2011 and December 31, 2010:

Financial Instrument	September 30, 2011	December 31, 2010
Compound derivative liability	\$ 2,156,715	\$ 25,271,808
Common shares to which the derivative liability is linked	3,328,264	4,235,972

Changes in the fair value of compound derivative liabilities are recorded in gain (loss) on change in fair value of derivative in the income statement. The following tables summarize the components of gain (loss) on change in fair value of derivative arising from fair value adjustments and other changes to compound derivative liabilities during the nine months ended September 30, 2011 and 2010:

	Nine Months Ended September 30,	
	2011	2010
Balances at January 1	\$ 25,271,808	\$ 45,443,506
Decrease due to convertible notes conversion on March 1, 2011(see note 13)	(3,741,573)	-
Decrease in fair value adjustments 1	(19,373,520)	(14,122,730)
Balances at September 30	\$ 2,156,715	\$ 31,320,776

- Recorded in the gain on change in fair value of derivative line in the statements of income.

The following tables summarize the components of gain (loss) on change in fair value of derivative arising from fair value adjustments and other changes to compound derivative liabilities during the three months ended September 30, 2011 and 2010:

	Three Months Ended September 30,	
	2011	2010
Balances at July 1	\$ 9,944,852	\$ 40,008,753
Decrease in fair value adjustments 1	(7,788,137)	(8,687,977)
Balances at September 30	\$ 2,156,715	\$ 31,320,776

- Recorded in the gain on change in fair value of derivative line in the statements of income.

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

The Company's embedded conversion option derivative represents the conversion option, term-extending option, certain redemption and put features in the Company's Convertible Notes payable. See Note 13 for additional information about the Company's Convertible Notes payable. The features embedded in the Convertible Notes were combined into one compound embedded derivative that the Company measured at fair value using the Monte Carlo valuation technique. Monte Carlo was believed by the Company's management to be the best available technique for this compound derivative because, in addition to providing for inputs such as trading market values, volatilities and

risk free rates, Monte Carlo also embodies assumptions that provide for credit risk, interest risk and redemption behaviors, i.e., assumptions market participants exchanging debt-type instruments would also consider. Monte Carlo simulates multiple outcomes over the period to maturity using multiple assumption inputs also over the period to maturity. The following table sets forth (i) the range of inputs for each significant assumption and (ii) the equivalent, or averages, of each significant assumption as of September 30, 2011, December 31, 2010, September 30, 2010 and December 31, 2009 (effective date of accounting principle change):

September 30, 2011 Assumptions:	Range		Equivalent
	Low	High	
Volatility	49.84%	76.78%	63.59%
Market adjusted interest rates	9.46%	18.13%	15.06%
Credit risk adjusted rates	17.43%	17.43%	17.43%
Implied expected life (years)	-	-	1.36



December 31, 2010 Assumptions:	Range		Equivalent
	Low	High	
Volatility	43.14%	76.00%	63.00%
Market adjusted interest rates	5.14%	20.15%	9.64%
Credit risk adjusted rates	14.75%	15.82%	15.11%
Implied expected life (years)	—	—	1.73

September 30, 2010 Assumptions:	Range		Equivalent
	Low	High	
Volatility	58.71%	78.45%	71.75%
Market adjusted interest rates	2.71%	21.55%	9.02%
Credit risk adjusted rates	15.88%	17.23%	15.94%
Implied expected life (years)	-	-	1.79

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

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

#### 15. Accrued expenses and other payables

The Company's accrued expenses and other payables at September 30, 2011 and December 31, 2010 are summarized as follows:

	September 30,	
	2011	December 31, 2010
Accrued expenses	\$ 2,714,520	\$ 3,627,768
Accrued interest 1	354,375	7,143,751
Other payables	1,920,511	2,826,354
Warranty reserves 2	16,445,783	13,944,392
Dividend payable to noncontrolling interest shareholders of Joint-ventures	1,926,212	1,530,445
Balance at the end of the period	\$ 23,361,401	\$ 29,072,710

1. On September 30, 2011 and December 31, 2010, the Company's balance of accrued interest was \$354,375 and \$7,143,751, respectively, which includes nil and \$6,631,251 of accrued provision on make-whole redemption interest for the annual redemption on the convertible notes, respectively. As of December 31, 2010, the Company's balance of accrued interest includes make-whole redemption interest which was payable upon the Annual

Redemption on February 15, 2011, if the Convertible Notes were redeemed. However, as of September 30, 2011, make-whole redemption interest was classified to long-term liabilities as there was no other mandatory annual redemption subsequent to February 15, 2011. (see note 16)

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

For the nine months ended September 30, 2011 and 2010, the warranties activities were as follows:

	Nine Months Ended September 30,	
	2011	2010
Balance at the beginning of period	\$ 13,944,392	\$ 9,092,462
Additions during the period	8,012,821	7,254,858
Settlement within period, by cash or actual material	(6,099,057)	(5,459,215)
Foreign currency translation gain	587,627	212,085
Balance at end of period	\$ 16,445,783	\$ 11,100,190

## 16. Accrued make-whole redemption interest expense for Convertible Notes

In February 2008, the Company sold to two accredited institutional investors \$35 million of convertible notes, the "Convertible Notes," with a scheduled maturity date of February 15, 2013. Pursuant to the terms of the Convertible Notes, on each of February 15, 2010 and February 15, 2011, the Convertible Note holders had the right, in their sole discretion, to require that the Company redeem the Convertible Notes in whole but not in part, by delivering written notice thereof to the Company. The portion of the Convertible Note subject to redemption pursuant to this annual redemption right will be redeemed by the Company in cash at a price equal to the sum of the conversion amount being redeemed and the Annual Redemption Make Whole Amount. The "Annual Redemption Make Whole Amount" means a premium to the conversion amount such that the total amount received by the Convertible Notes holder upon any annual redemption represents a gross yield on the original principal amount of eleven percent (11%), with interest computed on the basis of actual number of days elapsed over a 360-day year. On February 15, 2011, the Convertible Notes holder did not exercise its annual redemption right. Therefore, the next scheduled redemption date is the maturity date of February 15, 2013 and the make-whole provision accrued after February 15, 2011 was based on the "Maturity Make Whole Amount." "Maturity Make Whole Amount" means a premium to the Conversion Amount such that the total amount received by the Holder at Maturity represents a gross yield to the Holder on the Original Principal Amount as of the Maturity Date equal to thirteen percent (13%), with interest computed on the basis of actual number of days elapsed over a 360-day year. The make-whole redemption interest is recorded under accrued interest before February 15, 2011 due to its current liabilities feature and thereafter reclassified to and recorded as non-current liability.

During the nine months ended September 30, 2011 and 2010, the accrued provision on make-whole redemption interest pursuant to the term of Convertible Notes was as follows:

	Nine Months Ended September 30,	
	2011	2010
Balance at beginning of the period	\$ 6,631,251	\$ 4,763,771
Amounts provided for during the period	1,838,648	1,324,146
Decrease due to convertible notes conversion	(1,502,125)	-
Balance at end of period	\$ 6,967,774	\$ 6,087,917

## 17. Taxes payable

The Company's taxes payable at September 30, 2011 and December 31, 2010 are summarized as follows:

	September 30, 2011	December 31, 2010
Value-added tax payable	\$ 3,776,613	\$ 3,203,808
Income tax payable	230,172	3,273,776
Other tax payable	295,389	383,362
Balance at end of the period	\$ 4,302,174	\$ 6,860,946

## 18. Advances payable

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

These subsidies have different rules and regulations governing the criteria necessary for the Company to enjoy the benefits and these subsidies are recognized as income upon the government's inspection and approval.

The balances are unsecured, interest-free and will be repayable to the Chinese government if the usage of such advance does not continue to qualify for the subsidy when the Company fails to meet those criteria.

## 19. Share capital and additional paid-in capital

The activities in the Company's share capital and additional paid-in capital account during the nine months ended September 30, 2011 and 2010 are summarized as follows:

	Share Capital		
	Shares	Par Value	Additional paid-in capital
Balance at January 1, 2011	27,175,826	\$ 2,717	\$ 28,565,153
Issuance of common shares for the conversion of convertible notes 1	907,708	91	10,111,778
Balance at September 30, 2011	28,083,534	\$ 2,808	\$ 38,676,931

	Share Capital		
	Shares	Par Value	Additional paid-in capital
Balance at January 1, 2010	27,046,244	\$ 2,704	\$ 27,515,064
Shares issued for stock options exercised	69,582	7	278,893
Share-based compensation	-	-	422,714
Balance at September 30, 2010	27,115,826	\$ 2,711	\$ 28,216,671

1. On March 1, 2011, an investor converted \$6,428,571 principal amount of the Convertible Notes at a conversion price of \$7.0822 per share, and the Company issued 907,708 shares of its common stock to the investor. No additional consideration was paid for the conversion of the Convertible Notes into common stock. The market price of the Company's common stock was \$11.14 on such date.

## 20. Noncontrolling interests

The Company's activities in respect of the amounts of the noncontrolling interests' equity at September 30, 2011 and 2010 are summarized as follows:

	Nine Months Ended September 30,	
	2011	2010
Balance at beginning of the period	\$ 35,966,773	\$ 27,138,357
Add: Additions during the period—		
Income attributable to noncontrolling interests	5,241,143	8,227,985
Less: Decreases during the period		
Dividends declared to the noncontrolling interest holders of joint-venture companies	(2,005,274)	(3,288,909)
Foreign currency translation gain	1,601,448	551,867
Balance at end of period	\$ 40,804,090	\$ 32,629,300

## 21. Retained earnings—Appropriated

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

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

During the nine months ended September 30, 2011 and 2010, the Company recorded appropriate statutory surplus reserve of \$259,163 and \$443,264, respectively.

## 22. Financial expenses

During the three months ended September 30, 2011 and 2010, the Company recorded financial expenses which are summarized as follows:

	Three Months Ended September 30,	
	2011	2010
Coupon interest and make-whole redemption interest	\$ 905,545	\$ 843,333
Interest (income) expense, net	(183,765)	31,911
Foreign exchange (gain) loss, net	488,645	(157,538)
(Gain) loss of note discount, net	39,821	(52,185)
Handling charge	28,762	42,006
Total	\$ 1,279,008	\$ 707,527

During the nine months ended September 30, 2011 and 2010, the Company recorded financial expenses which are summarized as follows:

	Nine Months Ended September 30,	
	2011	2010
Interest expenses, net 1	\$ 2,261,130	\$ 2,109,210
Foreign exchange (gain) loss, net	431,333	(90,146)
(Gain) loss of note discount, net	90,244	(65,261)
Handling charge	119,443	102,628
<b>Total</b>	<b>\$ 2,902,150</b>	<b>\$ 2,056,431</b>

1. Including coupon interest expenses and accrued make-whole redemption interest expenses associated with the Convertible Notes of \$2,691,238 and \$2,205,397 for the nine months ended September 30, 2011 and 2010, respectively.

23. Gain on change in fair value of derivative

During the three months ended September 30, 2011 and 2010, the Company recorded gain on change in fair value of derivative is summarized as follows:

	Three Months Ended September 30,	
	2011	2010
Gain from adjustment of fair value of compound derivative Liabilities	\$ 7,788,137	\$ 8,687,977

During the three months ended September 30, 2011, the Company's common stock market price dropped to \$4.72 from \$8.63 at the closing of prior quarter. Thus, the intrinsic value of the embedded conversion feature in financial instruments decreased, the fair value of compound derivative liabilities decreased, and the gain on change in fair value of derivatives increased. (see note 14)

During the three months ended September 30, 2010, the Company's common stock market price dropped to \$15.28 from \$17.60 at the beginning of the period. Thus, the intrinsic value of the embedded conversion feature in financial instruments decreased, the fair value of compound derivative liabilities decreased, and the gain on change in fair value of derivatives increased. (see note 14)

During the nine months ended September 30, 2011 and 2010, the Company recorded gain on change in fair value of derivative is summarized as follows:

	Nine Months Ended September 30,	
	2011	2010
Gain from adjustment of fair value of compound derivative Liabilities	\$ 19,373,520	\$ 14,122,730

During the nine months ended September 30, 2011, the Company's common stock market price dropped to \$4.72 from \$13.62 at the beginning of the period. Thus, the intrinsic value of the embedded conversion feature in financial instruments decreased, the fair value of compound derivative liabilities decreased, and the gain on change in fair value of derivatives increased. (see note 14)

During the nine months ended September 30, 2010, the Company's common stock market price dropped to \$15.28 from \$18.71 at the beginning of the period. Thus, the intrinsic value of the embedded conversion feature in financial instruments decreased, the fair value of compound derivative liabilities decreased, and the gain on change in fair value of derivatives increased. (see note 14)

24. Gain on Convertible Notes conversion

During the three months ended September 30, 2011 and 2010, no Convertible Notes were converted.

During the nine months ended September 30, 2011, gain on Convertible Notes conversion was \$1,564,418. During the nine months ended September 30, 2010, no Convertible Notes were converted. (see note 13)

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25. Income tax rate

The Company's subsidiaries registered in the PRC are subject to state and local income taxes within the PRC at the applicable tax rate of 25% on the taxable income as reported in their PRC statutory financial statements in accordance with the relevant income tax laws applicable to foreign invested enterprise.

Pursuant to the New China Income Tax Law and the Implementing Rules (New CIT) which were effective as of January 1, 2008, dividends generated after January 1, 2008 and payable by a foreign-invested enterprise to its foreign investors will be subject to a 10% withholding tax if the foreign investors are considered as non-resident enterprises without any establishment or place within China or if the dividends payable have no connection with the establishment or place of the foreign investors within China, unless any such foreign investor's jurisdiction of incorporation has a tax treaty with China that provides for a different withholding arrangement.

Genesis, the Company's wholly owned subsidiary and the direct holder of the equity interests in the Company's Joint Venture subsidiaries in China, is incorporated in Hong Kong. According to the Mainland and Hong Kong Taxation Arrangement, dividends paid by a foreign-invested enterprise in China to its direct holding company in Hong Kong will be subject to withholding tax at a rate of no more than 5%, if the foreign investor owns directly at least 25% of the shares of the foreign-invested enterprise. Under the New CIT Law and the Implementing Rules, if Genesis is regarded as a non-resident enterprise and therefore is required to pay a 5% withholding tax for any dividends payable to it from Joint Venture subsidiaries.

The Company provides for deferred income taxes on the unremitted earnings of foreign subsidiaries unless such earnings are deemed to be permanently reinvested outside the United States.

As of September 30, 2011, the Company still has undistributed earnings of approximately \$93 million from investment in foreign subsidiaries that are considered permanently reinvested. Since these amounts are permanently reinvested, no deferred income tax has been provided on such earnings.

During 2009, Jiulong was awarded the title of Advanced Technology Enterprises, and based on the PRC income tax law, it was subject to enterprise income tax at a rate of 15% for 2008, 2009 and 2010. In 2011, the Company expects Jiulong to qualify for Advanced Technology Enterprises and continue to be taxed at the 15% tax rate based on the Company's assessment of its qualification to obtain the preferential tax rate. However, this is subject to re-assessment by the government, and if approved, its term will be extended for another three years. If Jiulong fails to pass the re-assessment by the government, it would be subject to a tax rate of 25%.

During 2008, Henglong was awarded the title of Advanced Technology Enterprises, and based on the PRC income tax law, it was subject to enterprise income tax at a rate of 15% for 2008, 2009 and 2010. In 2011, the Company expects Henglong to qualify for Advanced Technology Enterprises and continue to be taxed at the 15% tax rate based on the Company's assessment of its qualification to obtain the preferential tax rate. However, this is subject to re-assessment by the government, and if approved, its term will be extended for another three years. If Henglong fails to pass the re-assessment by the government, it would be subject to a tax rate of 25%.

During 2009, Shenyang was awarded the title of Advanced Technology Enterprises, and based on the PRC income tax law, it was subject to enterprise income tax at a rate of 15% for 2009, 2010 and 2011.

During 2009, Zhejiang was awarded the title of Advanced Technology Enterprises, and based on the PRC income tax law, it was subject to enterprise income tax at a rate of 15% for 2009, 2010 and 2011.

Wuhu is subject to income tax at a rate of 11%, 12% and 12.5% for the three years from 2010 to 2012, and Jielong and Hengsheng are subject to income tax at a rate of 12.5% for the three years from 2010 to 2012.

There is no assessable profit for USAI and Testing Center in 2010, 2009 and 2008. Based on PRC income tax laws, they are subject to income tax at a rate of 12.5% for 2011 and 2012 if they have taxable income.

No provision for Hong Kong tax is made as Genesis is an investment holding company, and has no operating income in Hong Kong for the three months and the nine months ended September 30, 2010 and 2011. The Hong Kong enterprise income tax rate is 16.5%.

No provision for US tax is made as the Company has no operating income in the US for the three months and the nine months ended September 30, 2010 and 2011. The US enterprise income tax rate is 35%.

26. Income per share

In periods when the Company generates income, the Company calculates basic earnings per share ("EPS") using the two-class method, pursuant to ASC 260, "Earnings Per Share". The two-class method is required as the Company's Convertible Notes qualify as participating securities, having the right to receive dividends should dividends be declared on common stock. Under this method, earnings for the period are allocated on a pro-rata basis to the common stockholders and to the holders of Convertible Notes based on the weighted average number of common shares outstanding and number of shares that could be converted. The Company does not use the two-class method in periods when it generates a loss as the holders of the Convertible Notes do not participate in losses.

For diluted earnings per share, the Company uses the more dilutive of the if-converted method or two-class method for Convertible Notes and treasury stock method for options, assuming the issuance of common shares, if dilutive, resulting from the exercise of options and warrants.

The calculations of diluted income per share attributable to the parent company were:

	Three Months Ended September 30,	
	2011	2010
<b>Numerator:</b>		
Net income attributable to the parent company	\$ 10,108,847	\$ 15,935,386
Allocation to Convertible Notes holders	(1,071,091)	(2,153,261)
Net income attributable to the parent company's common shareholders – Basic	9,037,756	13,782,125
<b>Dilutive effect of:</b>		
Add: Allocation to convertible Notes holders	1,071,091	2,153,261
Add: Interest expenses of convertible Notes payable	905,545	843,333
Less: Gain on change in fair value of derivative	(7,788,137)	(8,687,977)
Net income attributable to the parent company's common shareholders – Diluted	\$ 3,226,255	\$ 8,090,742
<b>Denominator:</b>		
Weighted average shares outstanding	28,083,534	27,112,689
Dilutive effects of stock options	92,197	214,000
Dilutive effect of convertible notes	3,328,264	4,235,972
Denominator for dilutive income per share – Diluted	31,503,995	31,562,661
Net income per common share attributable to parent company – Basic	\$ 0.32	\$ 0.51
Net income per common share attributable to parent company – Diluted	\$ 0.10	\$ 0.26

The following table summarizes potential common shares outstanding excluded from the calculation of diluted income per share for three months ended September 30, 2011 and 2010 because such an inclusion would have an anti-dilutive effect.

	Three Months Ended September 30,	
	2011	2010
Shares issuable under stock options	52,500	-

	Nine Months Ended September 30,	
	2011	2010
<b>Numerator:</b>		
Net income attributable to the parent company	\$ 34,094,787	\$ 39,436,540
Allocation to convertible notes holders	(3,831,484)	(5,334,715)
Net income attributable to the parent company's common shareholders – Basic	30,263,303	34,101,825
<b>Dilutive effect of:</b>		
Add: Allocation to convertible notes holders	3,831,484	5,334,715
Add: Interest expenses of convertible notes payable	2,691,238	2,205,397
Less: Gain on change in fair value of derivative	(19,373,520)	(14,122,730)
Less: Gain on convertible notes conversion	(1,564,418)	-
Net income attributable to the parent company's common shareholders – Diluted	\$ 15,848,087	\$ 27,519,207

Denominator:

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Weighted average shares outstanding	27,881,821	27,078,180
Dilutive effects of stock options	119,455	245,967
Dilutive effect of convertible notes	3,529,977	4,235,972
Denominator for dilutive income per share – Diluted	31,531,253	31,560,119
Net income per common share attributable to parent company – Basic	\$ 1.09	\$ 1.26
Net income per common share attributable to parent company – Diluted	\$ 0.50	\$ 0.87

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The following table summarizes potential common shares outstanding excluded from the calculation of diluted income per share for the nine months ended September 30, 2011 and 2010 because such an inclusion would have an anti-dilutive effect.

	Nine Months Ended September 30,	
	2011	2010
Shares issuable under stock options	37,500	-

## 27. Significant concentrations

A significant portion of the Company's business is conducted in China where the currency is the RMB. Regulations in China permit foreign owned entities to freely convert the RMB into foreign currency for transactions that fall under the "current account," which includes trade related receipts and payments, interest and dividends. Accordingly, the Company's Chinese subsidiaries may use RMB to purchase foreign exchange for settlement of such "current account" transactions without pre-approval. However, pursuant to applicable regulations, foreign-invested enterprises in China may pay dividends only out of their accumulated profits, if any, determined in accordance with Chinese accounting standards and regulations. In calculating accumulated profits, foreign investment enterprises in China are required to allocate at least 10% of their accumulated profits each year, if any, to fund certain reserve funds, including mandated employee benefits funds, unless these reserves have reached 50% of the registered capital of the enterprises.

Transactions other than those that fall under the "current account" and that involve conversion of RMB into a foreign currency are classified as "capital account" transactions; examples of "capital account" transactions include repatriations of investment by or loans to foreign owners, or direct equity investments in a foreign entity by a China domiciled entity. "Capital account" transactions require prior approval from China's State Administration of Foreign Exchange, or SAFE, or its provincial branch to convert a remittance into a foreign currency, such as U.S. Dollars, and transmit the foreign currency outside of China.

This system could be changed at any time and any such change may affect the ability of the Company or its subsidiaries in China to repatriate capital or profits, if any, outside China. Furthermore, SAFE has a significant degree of administrative discretion in implementing the laws and has used this discretion to limit convertibility of current account payments out of China. Whether as a result of a deterioration in the Chinese balance of payments, a shift in the Chinese macroeconomic prospects or any number of other reasons, China could impose additional restrictions on capital remittances abroad. As a result of these and other restrictions under the laws and regulations of the People's Republic of China, or the PRC, the Company's China subsidiaries are restricted in their ability to transfer a portion of their net assets to the parent. The Company has no assurance that the relevant Chinese governmental authorities in the future will not limit further or eliminate the ability of the Company's Chinese subsidiaries to purchase foreign currencies and transfer such funds to the Company to meet its liquidity or other business needs.

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

During the nine months ended September 30, 2011, the Company's ten largest customers accounted for 73.1% of its consolidated net sales, with each of two customers individually accounting for more than 10% of consolidated net sales, i.e., 12.0%, and 10.0% individually, or an aggregate of 22.0%. At September 30, 2011, approximately 16.5% of accounts receivable were from trade transactions with the aforementioned two customers.

During the nine months ended September 30, 2010, the Company's ten largest customers accounted for 76.3% of its consolidated net sales, with each of two customers individually accounting for more than 10% of consolidated net

sales, i.e., 15.3%, and 11.7% individually, or an aggregate of 27.0%. At September 30, 2010, approximately 16.2% of accounts receivable were from trade transactions with the aforementioned two customers.

## 28. Related party transactions and balances

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

## Related sales

	Three Months Ended September 30,	
	2011	2010
Merchandise sold to related parties	\$ 7,817,723	\$ 1,717,483

	Nine Months Ended September 30,	
	2011	2010
Merchandise sold to related parties	\$ 30,474,574	\$ 6,319,594

## Related purchases

	Three Months Ended September 30,	
	2011	2010
Materials purchased from related parties	\$ 2,842,267	\$ 4,885,768
Technology purchased from related parties	262,967	119,383
Equipment purchased from related parties	807,259	406,894
Total	\$ 3,912,493	\$ 5,412,045

	Nine Months Ended September 30,	
	2011	2010
Materials purchased from related parties	12,972,362	\$ 14,481,952
Technology purchased from related parties	324,776	295,861
Equipment purchased from related parties	3,078,861	1,741,842
Total	\$ 16,375,999	\$ 16,519,655

## Related receivables

	September 30, 2011	December 31, 2010
Accounts receivable	\$ 9,716,604	\$ 5,466,842
Other receivables	432,287	350,464
Total	\$ 10,148,891	\$ 5,817,306

## Related advances

	September 30, 2011	December 31, 2010
Advanced equipment payment to related parties	\$ 5,507,634	\$ 7,534,440
Advanced components and parts processing charges and others	1,061,303	1,334,069
Total	\$ 6,568,937	\$ 8,868,509

## Related payables

	September 30, 2011	December 31, 2010
Accounts payable	\$ 1,584,274	\$ 1,867,926

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

Related parties pledged certain land use rights and buildings as security for the Company's credit facilities provided by banks.

As of November 8, 2011, the date the Company issued these financial statements, Hanlin Chen, Chairman, owns 63.6% of the common stock of the Company and has the effective power to control the vote on substantially all significant matters without the approval of other stockholders.



## 29. Commitments and contingencies

Legal Proceedings – On October 25, 2011, a purported securities class action was filed in the United States District Court for the Southern District of New York on behalf of all purchasers of the Company's securities between March 25, 2010 and March 17, 2011. The complaint alleges that the Company and certain of its present and former officers and directors violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, and the rules promulgated thereunder, and seeks unspecified damages. The Company has not yet responded to the complaint, but believes the allegations in the complaint are without merit. The Company intends to defend itself vigorously against the claims.

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

In addition to the convertible notes, bank loans, notes payables and the related interest, the following table summarizes the Company's major commitments and contingencies as of September 30, 2011:

	Payment Obligations by Period						Total
	2011	1	2012	2013	2014	Thereafter	
Obligations for service agreements	\$-		\$204,567	\$-	\$-	\$-	\$204,567
Interest on Convertible Notes, redemption at maturity and short-term bank loan	178,098		1,353,204	4,442,107	-	-	5,973,409
Obligations for purchasing agreements	11,338,115		1,964,622	-	-	-	13,302,737
Total	\$11,515,213		\$3,522,393	\$4,442,107	\$-	\$-	\$19,480,713

1. Remaining 3 months in 2011.

## 30. Off-balance sheet arrangements

At September 30, 2011 and 2010, the Company did not have any transactions, obligations or relationships that could be considered off-balance sheet arrangements.

## 31. Segment reporting

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

During the nine months ended September 30, 2011 and 2010, the Company had nine product sectors, five of them were principal profit makers, which were reported as separate sectors which engaged in the production and sales of power steering (Henglong, Jiulong, Shenyang and Wuhu), and power pumps (Zhejiang). The other four sectors which were established in 2005, 2006 and 2007, respectively, engaged in the production and sale of sensor modules (USAI), electronic power steering (Jielong), power steering (Hengsheng), and provision of after sales and R&D services

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(HLUSA). Since the revenues, net income and net assets of these four sectors are less than 10% of its segment in the consolidated financial statements, the Company incorporated these four sectors into “other sector.”

The Company’s product sector information is as follows:

	Henglong	Jiulong	Shenyang	Zhejiang	Wuhu	Other sector	Other 1	Total
For the Three Months Ended September 30, 2011 (unaudited):								
Revenue								
Net product sales – external	\$33,554,847	\$14,378,275	\$7,693,079	\$4,084,863	\$8,555,802	\$6,735,851	\$-	\$75,002,7
Net product sales – internal	5,741,672	991,308	87,488	1,236,784	-	7,548,445	(15,605,697)	-
Total revenue	\$39,296,519	\$15,369,583	\$7,780,567	\$5,321,647	\$8,555,802	\$14,284,296	\$(15,605,697)	\$75,002,7
Net income (loss)	\$4,879,030	\$426,125	\$541,445	\$431,852	\$(101,577 )	\$(567,998 )	\$5,882,623	\$11,491,5
Net income (loss) attributable to noncontrolling interests	981,315	81,558	162,810	212,295	(23,094 )	(65,062 )	32,831	1,382,65
Net income (loss) attributable to Parent company	\$3,897,715	\$344,567	\$378,635	\$219,557	\$(78,483 )	\$(502,936 )	\$5,849,792	\$10,108,8

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	Henglong	Jiulong	Shenyang	Zhejiang	Wuhu	Other sector	Other 1	Total
For the Three Months Ended September 30, 2010 (unaudited):								
Revenue								
Net product sales – external	\$32,438,683	\$19,627,536	\$8,243,405	\$5,209,763	\$8,709,931	\$1,873,526	\$-	\$76,102,844
Net product sales – internal	3,867,397	644,897	874,497	298,653	-	10,535,962	(16,221,406)	-
Total revenue	\$36,306,080	\$20,272,433	\$9,117,902	\$5,508,416	\$8,709,931	\$12,409,488	\$(16,221,406)	\$76,102,844
Net income	\$5,551,699	\$1,322,547	\$1,383,920	\$1,044,941	679,989	424,793	7,877,777	18,285,606
Net income attributable to noncontrolling interests	1,110,602	251,337	415,226	512,082	154,167	123,291	(216,425)	2,350,280
Net income attributable to Parent company	\$4,441,097	\$1,071,210	\$968,694	\$532,859	\$525,822	\$301,502	\$8,094,202	\$15,935,326
For the Nine Months Ended September 30, 2011 (unaudited):								
Revenue								
Net product sales – external	\$121,194,561	\$49,448,053	\$20,638,036	\$13,020,246	\$25,689,081	\$18,532,796	\$-	\$248,872,673
Net product sales – internal	19,811,708	2,967,932	1,859,961	1,607,384	-	26,373,038	(52,620,023)	-
Total revenue	\$141,006,269	\$52,415,985	\$22,497,997	\$14,627,630	\$25,689,081	\$44,905,834	\$(52,620,023)	\$248,872,673
Net income (loss)	\$19,048,473	\$2,105,937	\$1,064,894	\$1,533,516	\$(222,844)	\$(1,258,913)	\$17,064,867	\$39,270,820
Net income (loss) attributable to noncontrolling interests	3,814,105	400,597	319,792	751,977	(50,575)	(178,171)	183,418	5,630,134
Net income (loss) attributable to Parent company	\$15,234,368	\$1,705,340	\$745,102	\$781,539	\$(172,269)	\$(1,080,742)	\$16,881,449	\$33,640,686
For the Nine Months Ended September 30, 2010 (unaudited):								
Revenue								
Net product sales – external	\$121,194,561	\$49,448,053	\$20,638,036	\$13,020,246	\$25,689,081	\$18,532,796	\$-	\$248,872,673
Net product sales – internal	19,811,708	2,967,932	1,859,961	1,607,384	-	26,373,038	(52,620,023)	-
Total revenue	\$141,006,269	\$52,415,985	\$22,497,997	\$14,627,630	\$25,689,081	\$44,905,834	\$(52,620,023)	\$248,872,673
Net income (loss)	\$19,048,473	\$2,105,937	\$1,064,894	\$1,533,516	\$(222,844)	\$(1,258,913)	\$17,064,867	\$39,270,820
Net income (loss) attributable to noncontrolling interests	3,814,105	400,597	319,792	751,977	(50,575)	(178,171)	183,418	5,630,134
Net income (loss) attributable to Parent company	\$15,234,368	\$1,705,340	\$745,102	\$781,539	\$(172,269)	\$(1,080,742)	\$16,881,449	\$33,640,686

For the Nine  
Months Ended  
September 30,  
2010

(unaudited):

Revenue

Net product

sales – external	\$ 112,860,428	\$ 64,452,631	\$ 23,733,187	\$ 16,368,355	\$ 22,628,769	\$ 5,373,301	\$
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Net product

sales – internal	25,834,595	1,951,660	4,643,477	1,870,369	-	23,418,794	(57,718,895)
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Total revenue	\$ 138,695,023	\$ 66,404,291	\$ 28,376,664	\$ 18,238,724	\$ 22,628,769	\$ 28,792,095	\$ (57,718,895)
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Net income	\$ 21,766,839	\$ 4,628,930	\$ 3,169,070	\$ 3,261,626	1,014,753	1,803,417	12,019,890
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Net income

attributable to

noncontrolling

interests	4,353,628	879,552	950,771	1,598,258	230,058	146,951	68,767
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Net income

attributable to

Parent

company	\$ 17,413,211	\$ 3,749,378	\$ 2,218,299	\$ 1,663,368	\$ 784,695	\$ 1,656,466	\$ 11,951,123
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1. Other includes activity not allocated to the product sectors and elimination of inter-sector transactions.

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

### General Overview

China Automotive Systems, Inc., including, when the context so requires, its subsidiaries and the subsidiaries' interests in the Sino-foreign joint ventures described below, is referred to herein as the "Company." The Company, through its Sino-foreign joint ventures, engages in the manufacture and sales of automotive systems and components in the People's Republic of China, the "PRC" or "China," as described below.

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

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

The Company owns the following aggregate net interests in seven Sino-foreign joint ventures, a wholly-owned subsidiary and two joint ventures organized in the PRC as of September 30, 2011 and 2010.

Name of Entity	Percentage Interest			
	September 30, 2011		September 30, 2010	
Shashi Jiulong Power Steering Gears Co., Ltd., "Jiulong" 1	81.00	%	81.00	%
Jingzhou Henglong Automotive Parts Co., Ltd., "Henglong" 2	80.00	%	80.00	%
Shenyang Jinbei Henglong Automotive Steering System Co., Ltd., "Shenyang" 3	70.00	%	70.00	%
Zhejiang Henglong & Vie Pump-Manu Co., Ltd., "Zhejiang" 4	51.00	%	51.00	%
Universal Sensor Application Inc., "USAI" 5	83.34	%	83.34	%
Wuhan Jielong Electric Power Steering Co., Ltd., "Jielong" 6	85.00	%	85.00	%
Wuhu HengLong Automotive Steering System Co., Ltd., "Wuhu" 7	77.33	%	77.33	%
Jingzhou Hengsheng Automotive System Co., Ltd, "Hengsheng" 8	100.00	%	100.00	%
Jingzhou Henglong Automotive Technology (Testing) Center, "Testing Center" 9	80.00	%	80.00	%
Beijing Henglong Automotive System Co., Ltd., "Beijing Henglong" 10	50.00	%	50.00	%

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

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

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

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

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

6. Jielong was established in 2006 and mainly engages in production and sales of electric power steering.

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

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

9. In December 2009, Henglong, a subsidiary of Genesis, formed Jingzhou Henglong Automotive Technology (Testing) Center, "Testing Center," which is mainly engaged in research and development of new products.

10. Beijing Henglong was established in 2010 and is mainly engaged in design, development and manufacture of both hydraulic and electric power steering systems and parts. According to the joint venture agreement, the Company does not have voting control of Beijing Henglong. Therefore, the Company's consolidated financial statements do not include Beijing Henglong, and such investment is accounted for by the equity method.

On October 12, 2011, the board of directors of the Company approved a reorganization of the group companies operating as subsidiaries in China. The reorganization is intended to improve the Company's marketing of its products in China by presenting a more unified structure under one PRC-based holding company and to improve the administration and control of the various China-based subsidiaries. Following the reorganization, all of the China-based operating companies will be subsidiaries of the China-based holding company, Henglong Group Automotive Systems, Inc., which itself will be as subsidiary of Great Genesis Holdings Limited. The reorganization will not have a material impact on the Company's consolidated financial position or results of operations, and should not impact the tax treatment of the Company or its subsidiaries in any material respect. The reorganization is currently underway, and is expected to be completed by the second quarter of 2012.

#### Critical Accounting Policies

The Company prepares its unaudited condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amount of revenues and expenses during the reporting periods. Management periodically evaluates the estimates and judgments made. Management bases its estimates and judgments on historical experience and on various factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates as a result of different assumptions or conditions. The following critical accounting policies affect the more significant judgments and estimates used in the preparation of the Company's condensed consolidated financial statements.

The Company considers an accounting estimate to be critical if:

It requires the Company to make assumptions about matters that were uncertain at the time the Company was making the estimate; and

Changes in the estimate or different estimates that the Company could have selected would have had a material impact on its financial condition or results of operations.

Critical accounting estimates affecting the income statement component relate primarily to revenue from Product Sales Recognition. The Company recognizes revenue when the significant risks and rewards of ownership have been transferred to the customer pursuant to PRC law, including factors such as when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, sales and value added tax laws have been complied with, and collectability is probable. The Company recognizes product sales generally at the time the product is installed on original equipment manufacturing, "OEM," production line, and a small number of product sales is recognized at the time the product is shipped. Concurrent with the recognition of revenue, the Company reduces revenue for estimated product returns.

Additionally, the table below presents information about the nature and rationale for the Company's other critical accounting estimates in the Balance Sheet:

Balance Sheet Caption	Critical Estimate Item	Nature of Estimates Required	Assumptions/Approaches Used	Key Factors
Accrued liabilities and other long-term	Warranty obligations	Estimating warranty requires the Company to forecast the	The Company bases its estimate on historical trends of	• VM

Liabilities	<p>resolution of existing claims and expected future claims on products sold. Vehicle Manufacturers (VM) are increasingly seeking to hold suppliers responsible for product warranties, which may impact the Company's exposure to these costs.</p>	<p>units sold and payment amounts, combined with its current understanding of the status of existing claims and discussions with its customers.</p>	<ul style="list-style-type: none"> <li>• VM policy decisions regarding warranty claims</li> </ul>	
<p>Property, plant and equipment, intangible assets and other long-term assets</p>	<p>Valuation of long-lived assets and investments</p>	<p>The Company is required from time-to-time to review the recoverability of certain of its assets based on projections of anticipated future cash flows, including future profitability assessments of various product lines.</p>	<p>The Company estimates cash flows using internal budgets based on recent sales data, independent automotive production volume estimates and customer commitments.</p>	<ul style="list-style-type: none"> <li>• Future production estimates</li> <li>• Customer preferences and decisions</li> <li>• Economic growth</li> <li>• Margins</li> </ul>
<p>Accounts and notes receivable</p>	<p>Provision for doubtful accounts and notes receivable</p>	<p>Estimating the provision for doubtful accounts and notes receivables requires the Company to analyze and monitor each customer's credit standing and financial condition regularly. The Company grants credit to its customers, generally on an open account basis. It may have a material adverse effect on the Company's operating expense disclosure if such assessments were improper.</p>	<p>The Company grants credit to its customers for three to four months based on each customer's current credit standing and financial data. The Company assesses an allowance on an individual customer basis, under normal circumstances; the Company does not record any provision for doubtful accounts for those accounts receivable amounts which were in credit terms. For those receivables out of credit terms, the Company records any provision for doubtful accounts according to customers financial position assessment.</p>	<ul style="list-style-type: none"> <li>• Customers' credit standing and financial condition</li> </ul>



Deferred income taxes	Recoverability of deferred tax assets	The Company is required to estimate whether recoverability of the Company's deferred tax assets is more likely than not based on forecasts of taxable earnings in the related tax jurisdiction.	The Company uses historical and projected future operating results, based upon approved business plans, including a review of the eligible carry forward period, tax planning opportunities and other relevant considerations.	<ul style="list-style-type: none"> <li>• Tax law changes</li> <li>• Variances in future projected profitability, including by taxing entity</li> </ul>
Convertible Notes payable, discount of convertible note payable, compound derivative liabilities	Compound derivative liabilities	The Company is required to estimate the fair value of compound derivative liabilities at inception and completion of each reporting period	The Company uses Monte Carlo Valuation Model ("MCS") to determine fair value of compound derivative liabilities	<ul style="list-style-type: none"> <li>• Volatility</li> <li>• Risk-free rate</li> <li>• Interest market risk</li> <li>• Credit risk</li> <li>• Redemption behavior before maturity</li> </ul>

In addition, there are other items within the Company's financial statements that require estimation, but are not as critical as those discussed above. These include the allowance for reserves for excess and obsolete inventory. Although not significant in recent years, changes in estimates used in these and other items could have a significant effect on the Company's consolidated financial statements.

## RECENT ACCOUNTING PRONOUNCEMENTS

In July 2010, the FASB issued new disclosure guidance related to the credit quality of financing receivables and the allowance for credit losses. The guidance will require companies to provide more information about the credit quality of their financing receivables in the disclosures to financial statements including, but not limited to, significant purchases and sales of financing receivables, aging information and credit quality indicators. The Company adopted this accounting standard upon its effective date for years ending on or after December 15, 2010. The Company has evaluated the new disclosure requirement in accordance with the accounting guidance and the adoption did not have a significant impact on the Company's financial position, results of operations or cash flows.

In December 2010, FASB issued revised guidance on the "Disclosure of Supplementary Pro Forma Information for Business Combinations." The revised guidance specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The revised guidance also expands the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The revised guidance is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The Company adopted the new guidance as of January 1, 2011 and the adoption did not have a significant impact on the Company's financial position, results of operations or cash flows.

In 2011, the Financial Accounting Standards Board ("FASB") issued new accounting guidance that amends certain fair value measurement principles and disclosure requirements. The new guidance states that the concepts of highest

and best use and valuation premise are only relevant when measuring the fair value of nonfinancial assets and prohibits the grouping of financial instruments for purposes of determining their fair values when the unit of account is specified in other guidance. The Company will adopt this accounting standard upon its effective date for periods ending on or after December 15, 2011, and does not anticipate that this adoption will have a significant impact on the Company's financial position or results of operations.

In 2011, the FASB issued new disclosure guidance related to the presentation of the Statement of Comprehensive Income. This guidance eliminates the current option to report other comprehensive income and its components in the statement of changes in equity. The standard requires an entity to present the total of comprehensive income, net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The Company will adopt this accounting standard upon its effective date for periods ending on or after December 15, 2011, and does not anticipate that this adoption will have any impact on the Company's financial position or results of operations.

#### Executive Summary

China Automotive Systems, Inc. is a leading power steering systems supplier for China automobile industry. The Company has business relations with more than sixty vehicle manufacturers, including FAW Group, Dongfeng Auto Group and Changan Automobile Group, three of the five largest automobile manufacturers in China; Shenyang Brilliance Jinbei Co., Ltd., the largest light vehicle manufacturer in China; Chery Automobile Co., Ltd, the largest state owned car manufacturer in China, BYD Auto Co., Ltd and Zhejiang Geely Automobile Co., Ltd., the largest privately owned car manufacturers in China. From 2008, the Company has supplied power steering pumps and power steering gear to the Sino-Foreign joint ventures established by General Motors (GM), Citroen and Volkswagen in China. In 2009, the Company began to supply power steering gear to Chrysler North America. Most of the Company's production and research and development institutes are located in China. The Company has 3,000 employees dedicated to design, development, manufacture and sales of its products.

By leveraging its extensive experience, innovative technology and geographic strengths, the Company aims to grow leading positions in automotive power steering systems and to further improve overall margins, long-term operating profitability and cash flows. To achieve these goals and to respond to industry factors and trends, the Company is continuing work to improve its operations and business structure and achieve profitable growth.

Financial results for the three months and the nine months ended September 30, 2011 are summarized as follows.

Sales of \$75,002,717 and \$248,522,773 for the three months and the nine months ended September 30, 2011, compared to \$76,102,844 and \$245,416,671 for the same periods of 2010.

Gross profit of \$13,786,743, or 18.4% of sales, for the three-month period ended September 30, 2011, down from \$18,173,560, or 23.9% of sales, for the same period of 2010. For the nine-month periods ended September 30, 2011 and 2010, a gross profit of \$48,572,321, or 19.5% of sales, down from \$60,518,837, or 24.7% of sales.

Selling expenses of \$2,170,775 for the three-month period ended September 30, 2011, \$75,454 higher than the same period of 2010. For the nine-month period ended September 30, 2011, selling expense of \$7,123,063, \$256,814 higher than the same period of 2010.

General and administrative expenses of \$3,413,930 for the three-month period ended September 30, 2011, \$907,426 higher than the same period of 2010. For the nine-month period ended September 30, 2011, general and administrative expenses were \$10,868,767, \$2,300,913 higher than the same period in 2010.

Net income attributable to parent company of \$10,108,847 for the three-month period ended September 30, 2011, decreased by \$5,826,539 from the same period of 2010. For the nine-month period ended September 30, 2011, net income attributable to parent company of \$34,094,787, decreased by \$5,341,753 as compared to the same period in 2010.

Earnings per share to common shareholders of \$0.32 on a basic, and \$0.10 on a diluted, basis for the three months ended September 30, 2011, compared to earnings per share of \$0.51 on a basic, and \$0.26 on a diluted, basis for the same period in 2010. For the nine months ended September 30, 2011, earnings per share to common shareholders of \$1.09 on a basic, and \$0.50 on a diluted basis, compared to earnings per share of \$1.26 on a basic, and \$0.87 on a diluted, basis for the same period in 2010.

- Cash of \$76,067,212 as of September 30, 2011, \$26,642,233 more than as of December 31, 2010.

Cash provided by operating activities of \$31,728,545 for the nine months ended September 30, 2011, compared to cash provided by operating activities of \$29,604,550 for the same periods in 2010.

Capital expenditures of \$10,926,592 for the nine months ended September 30, 2011, lower than the same period in 2010 by \$13,139,596.

#### Results of Operations—Three Months Ended September 30, 2011 And 2010

	Net Sales				Cost of sales			
	2011	2010	Change		2011	2010	Change	
Henglong	\$39,296,519	\$36,306,680	\$2,989,839	8.2 %	\$30,885,142	\$27,981,448	\$2,903,694	10.4 %
Jiulong	15,369,583	20,272,433	(4,902,850)	-24.2	13,455,206	17,339,396	(3,884,190)	-22.4
Shenyang	7,780,567	9,117,902	(1,337,335)	-14.7	6,670,103	7,091,850	(421,747)	-5.9
Zhejiang	5,321,647	5,508,416	(186,769)	-3.4	4,127,589	3,823,739	303,850	7.9
Wuhu	8,555,802	8,709,931	(154,129)	-1.8	8,385,248	7,706,526	678,722	8.8
Other Sectors	14,284,296	12,408,888	1,875,408	15.1	13,421,396	10,784,539	2,636,857	24.5
Elimination	(15,605,697)	(16,221,406)	615,709	-3.8	(15,728,710)	(16,798,214)	1,069,504	-6.4
Total	\$75,002,717	\$76,102,844	\$(1,100,127)	-1.4 %	\$61,215,974	\$57,929,284	\$3,286,690	5.7 %

Net Sales

Net sales were \$75,002,717 for the three months ended September 30, 2011, compared with \$76,102,844 for the three months ended September 30, 2010, a decrease of \$1,100,127, or 1.4%, mainly due to a slow down in China's auto industry. Affected by the expiration of incentive policies and monetary tightening, the growth of China's auto output and sales started to slow down after two years of rapid growth, which negatively impacted the demand, hence, the decrease in Company's net sales, as more than 90% of the Company's business is derived from China. For the three months ended September 30, 2011, the decreased sales volume led to a net sales decrease of \$6,510,731 and increase in the average selling price because of the sales of newly developed steering gear models, which have a higher price point, and the stable increase of exported products, which led to a net sales increase of \$417,554, and the appreciation of the RMB against the U.S. dollar led to a net sales increase of \$4,993,050 compared with the same period of 2010.

Net sales for Henglong was \$39,296,519 for the three months ended September 30, 2011, compared with \$36,306,680 for the three months ended September 30, 2010, representing an increase of \$2,989,839, or 8.2%, including decreased sales volume with a sales decrease of \$109,258, increased sales price with a sales increase of \$982,567 and the effect of foreign currency translation with a sales increase of \$2,116,530.

Net sales for Jiulong was \$15,369,583 for the three months ended September 30, 2011, compared with \$20,272,433 for the three months ended September 30, 2010, representing a decrease of \$4,902,850, or 24.2%. Excluding the net sales of \$1,765,018 to Chrysler during the three months ended September 30, 2010 which is now included in Other Sector, net sales decrease was \$3,137,832, or 17.0%, including decreased sales volume with a sales decrease of \$4,066,341, increased sales price with a sales increase of \$227,743 and the effect of foreign currency translation with a sales increase of \$700,766.

Net sales for Shenyang was \$7,780,567 for the three months ended September 30, 2011, compared with \$9,117,902 for the three months ended September 30, 2010, representing a decrease of \$1,337,335, or 14.7%, including decreased sales volume with a sales decrease of \$2,236,009, increased sales price with a sales increase of \$417,841 and the effect of foreign currency translation with a sales increase of \$480,833.

Net sales for Zhejiang was \$5,321,647 for the three months ended September 30, 2011, compared with \$5,508,416 for the three months ended September 30, 2010, representing a decrease of \$186,769, or 3.4%, including decreased sales volume with a sales decrease of \$245,677, decreased sales price with a sales decrease of \$240,164 and the effect of foreign currency translation with a sales increase of \$299,072.

Net sales for Wuhu was \$8,555,802 for the three months ended September 30, 2011, compared with \$8,709,931 for the three months ended September 30, 2010, representing a decrease of \$154,129, or 1.8%, including decreased sales volume with a sales decrease of \$783,591, increased sales price with a sales increase of \$205,333 and the effect of foreign currency translation with a sales increase of \$424,129.

Net sales for Other Sectors was \$14,284,296 for the three months ended September 30, 2011, compared with \$12,408,888 for the three months ended September 30, 2010, representing an increase of \$1,875,408, or 15.1%. Including net sales of \$1,765,018 related to sales to Chrysler recorded by Jiulong during the three months ended September 30, 2010, net sales for Other Sector increased \$110,390, or 0.8%, including increased sales volume with a sales increase of \$153,143 because of the export auto output increase, decreased sales price with a sales decrease of \$76,748 and the effect of foreign currency translation with a sales increase of \$33,995.

#### Cost of Sales

For the three months ended September 30, 2011, the cost of sales was \$61,215,974, compared with \$57,929,284 for the same period of 2010, an increase of \$3,286,690, or 5.7%, mainly due to the effect of foreign currency translation. For the three months ended September 30, 2011, the RMB appreciated approximately 7% against the U.S. dollar, which led to a cost of sales increase of \$4,058,605, while the decreased sales volume led to a cost of sales decrease of \$5,656,142 and the increase of average unit cost with a cost of sales increase of \$4,884,227, compared with the same period of 2010.

Cost of sales for Henglong was \$30,885,142 for the three months ended September 30, 2011, compared with \$27,981,448 for the three months ended September 30, 2010, representing an increase of \$2,903,694, or 10.4%, including decreased sale volumes with a cost of sales decrease of \$207,622, increased unit cost with a cost of sales increase of \$1,483,057 and the effect of foreign currency translation with a cost increase of \$1,628,259.

Cost of sales for Jiulong was \$13,455,206 for the three months ended September 30, 2011, compared with \$17,339,396 for the three months ended September 30, 2010, representing a decrease of \$3,884,190, or 22.4%. Excluding cost of sales of \$1,436,327 related to sales to Chrysler during the three months ended September 30, 2010, cost of sales decrease was \$2,447,863, or 15.4%, including decreased sales volumes with a cost of sales decrease of \$3,523,085, increased unit cost with a cost of sales increase of \$479,870 and the effect of foreign currency translation with a cost increase of \$595,352.

Cost of sales for Shenyang was \$6,670,103 for the three months ended September 30, 2011, compared with \$7,091,850 for the three months ended September 30, 2010, representing a decrease of \$421,747, or 5.9%, including decreased sales volumes with a cost of sales decrease of \$1,749,189, increased unit cost with a cost of sales increase of \$936,955 and the effect of foreign currency translation with a cost increase of \$390,487.

Cost of sales for Zhejiang was \$4,127,589 for the three months ended September 30, 2011, compared with \$3,823,739 for the three months ended September 30, 2010, representing an increase of \$303,850, or 7.9%, including decreased sales volumes with a cost of sales decrease of \$154,500, increased unit cost with a cost of sales increase of \$246,343 and the effect of foreign currency translation with a cost increase of \$212,007.

Cost of sales for Wuhu was \$8,385,248 for the three months ended September 30, 2011, compared with \$7,706,526 for the three months ended September 30, 2010, representing an increase of \$678,722, or 8.8%, including decreased sales volumes with a cost of sales decrease of \$812,058, increased unit cost with a cost of sales increase of \$1,106,163 and the effect of foreign currency translation with an increase of \$384,617.

Cost of sales for Other Sectors was \$13,421,396 for the three months ended September 30, 2011, compared with \$10,784,539 for the three months ended September 30, 2010, representing an increase of \$2,636,857, or 24.5%. Including cost of sales of \$1,436,327 to Chrysler sales during the three months ended September 30, 2010, cost of sales increase was \$1,200,530, or 9.8%, including increased sale volume with a cost of sales increase of \$814,074, increased unit cost with a cost of sales increase of \$159,472 and the effect of foreign currency translation with an increase of \$226,984.

Gross margin was 18.4% for the three months ended September 30, 2011, a decrease of 5.5 percentage points from 23.9% for the same period of 2010, primarily due to an increase in average unit cost as a result of increased raw materials prices in China.

#### Gain on Other Sales

Gain on other sales consists of net amount retained from sales of materials and other assets. For the three months ended September 30, 2011, gain on other sales was \$465,950, compared with loss on other sales of \$152,481 for the same period of 2010, an increase of \$618,431, mainly due to increased sales of materials.

#### Selling Expenses

Selling expenses were \$2,170,775 for the three months ended September 30, 2011, compared with \$2,095,321 for the same period of 2010, an increase of \$75,454, or 3.6%, mainly due to the increase in travelling expense and warehouse rent charges.

#### General and Administrative Expenses

General and administrative expenses were \$3,413,930 for the three months ended September 30, 2011, compared with \$2,506,504 for the same period of 2010, an increase of \$907,426, or 36.2%, mainly due to increases in salaries and wages expenses and labor insurance expenses, which were caused by inflation in the labor cost, and a decrease in recovery of doubtful accounts.

#### Research and Development Expenses

Research and development expenses were \$2,708,777 for the three months ended September 30, 2011, compared with \$1,247,881 for the three months ended September 30, 2010, an increase of \$1,460,896, or 117.1 %.

The global automotive parts industry is highly competitive; winning and maintaining new business requires suppliers to rapidly produce new and innovative products on a cost-competitive basis. From 2010, foreign OEMs significantly increased their demand for electronic steering gear, "EPS," but the related technology in China is still in the research and development and testing stage. In order to bring to market "EPS" quickly, the Company continues to invest heavily in

the R&D of “EPS” in 2011, including increasing the Company’s senior technicians and advanced manufacture equipment on “EPS,” establishing the “EPS” trial-production department, introducing technology expectations and purchasing advanced technology and test equipment.

#### Income from Operations

Income from operations was \$5,959,211 for the three months ended September 30, 2011, compared with \$12,171,373 for the three months ended September 30, 2010, a decrease of \$6,212,162, or 51.0%, including a decrease of \$4,386,817, or 24.1%, in gross profit, an increase of \$618,431 in gain on other sales, and an increase of \$2,443,776, or 41.8%, in operating expenses.



#### Financial Expenses, net

Financial expenses were \$1,279,008 for the three months ended September 30, 2011, compared to financial expenses of \$707,527 for the same period of 2010, an increase of \$571,481, or 80.8%, mainly due to the increase in loss on foreign currency exchange, as the Company's subsidiaries based in the PRC and Genesis maintain their books and records in Renminbi, their functional currency, and Hengsheng, a subsidiary of the Company based in the PRC, settles its external sales in U.S. dollars. For the three months ended September 30, 2011, the RMB appreciated approximately 7% against the U.S. dollar, compared with the same period in 2010.

#### Gain on Change in Fair Value of Derivative

Gain on change in fair value of derivative was \$7,788,137 for the three months ended September 30, 2011, compared with a gain of \$8,687,977 for the same period of 2010, a decrease of \$899,840.

During the three months ended September 30, 2011, the Company's common stock market price dropped to \$4.72 from \$8.63 at the closing of prior quarter. Thus, the intrinsic value of the embedded conversion feature in financial instruments decreased, the fair value of compound derivative liabilities decreased and the gain on change in fair value of derivatives increased. (see note 14)

During the three months ended September 30, 2010, the Company's common stock market price dropped to \$15.28 from \$17.60 at the beginning of the period. Thus, the intrinsic value of the embedded conversion feature in financial instruments decreased, the fair value of compound derivative liabilities decreased and the gain on change in fair value of derivatives increased. (see note 14)

#### Income Before Income Tax Expenses and Equity In Earnings Of Affiliated Companies

Income before income tax expenses and equity in earnings of affiliated companies was \$12,517,231 for the three months ended September 30, 2011, compared with \$20,151,823 for the three months ended September 30, 2010, a decrease of \$7,634,592, or 37.9%, mainly due to a decrease in income from operations of \$6,212,162 and a decrease in gain on change in fair value of derivative of \$899,840.

#### Income Taxes

Income tax expense was \$1,068,548 for the three months ended September 30, 2011, compared with \$1,866,157 of income tax expense for the three months ended September 30, 2010, a decrease of \$797,609 due to the decrease of income before income tax and the decrease in the effective tax rate. For the three months ended September 30, 2011, among these income before income tax, the proportion of permanent difference, namely non-taxable gain on fair value adjustment, was higher than in the same period of 2010, so the effective tax rate for the three months ended September 30, 2011 was lower than that in the three months ended September 30, 2010.

#### Net Income

Net income was \$11,491,500 for the three months ended September 30, 2011, compared with a net income of \$18,285,666 for the three months ended September 30, 2010, a decrease of \$6,794,166, mainly including a decrease in income before income tax expenses and equity in earnings of affiliated companies of \$7,634,592 and a decrease in income taxes expenses of \$797,609.

#### Net Income Attributable to Noncontrolling Interest

Noncontrolling interest in the earnings of the Sino-foreign joint ventures amounted to \$1,382,653 for the three months ended September 30, 2011, compared with \$2,350,280 for the three months ended September 30, 2010, a decrease of \$967,627, or 41.2%, primarily due to the decrease in Sino-foreign joint ventures' net income.

The Company owns different equity interests in seven Sino-foreign joint ventures, through which it conducts its operations. All the operating results of these seven Sino-foreign joint ventures were consolidated in the Company's financial statements as of September 30, 2011 and 2010. The Company records the noncontrolling interest's share in the earnings of the respective Sino-foreign joint ventures for each period.

#### Net Income Attributable to Parent Company

Net income attributable to parent company was \$10,108,847 for the three months ended September 30, 2011, compared with a net income of \$15,935,386 for the three months ended September 30, 2010, a decrease of \$5,826,539, including a decrease of \$6,794,166 in net income and a decrease of \$967,627 in net income attributable to noncontrolling interest.

## Results of Operations—Nine Months Ended September 30, 2011 and 2010

	Net Sales				Cost of sales			
	2011	2010	Change		2011	2010	Change	
Henglong	\$ 141,006,269	\$ 138,695,023	\$ 2,311,246	1.7 %	\$ 110,980,677	\$ 105,072,685	\$ 5,907,992	5.6 %
Jiulong	52,415,985	66,404,291	(13,988,306)	-21.1	45,434,798	57,012,846	(11,578,048)	-20.3
Shenyang	22,497,997	28,376,664	(5,878,667 )	-20.7	19,600,009	23,829,846	(4,229,837 )	-17.8
Zhejiang	14,627,630	18,238,724	(3,611,094 )	-19.8	11,126,154	13,033,040	(1,906,886 )	-14.6
Wuhu	25,689,081	22,628,769	3,060,312	13.5	24,814,112	20,876,023	3,938,089	18.9
Other Sectors	44,905,834	28,792,095	16,113,739	56.0	41,430,508	24,150,705	17,279,803	71.5
Elimination								
1	(52,620,023 )	(57,718,895 )	5,098,872	-8.8	(53,435,806 )	(59,077,311 )	5,641,505	-9.5
Total	\$ 248,522,773	\$ 245,416,671	\$ 3,106,102	1.3 %	\$ 199,950,452	\$ 184,897,834	\$ 15,052,618	8.1 %

1. Elimination of inter-sector transactions.

## Net Sales

Net sales were \$248,522,773 for the nine months ended September 30, 2011, compared with \$245,416,671 for the nine months ended September 30, 2010, an increase of \$3,106,102, or 1.3%, mainly due to the appreciation of the RMB against the U.S. dollar. For the nine months ended September 30, 2011, the decreased sales volume led to a net sales decrease of \$76,654 and a decline in the average selling price with a net sales decrease of \$11,267,535 and the appreciation of the RMB against the U.S. dollar led to a net sales increase of \$14,450,291 compared with the same period of 2010.

Net sales for Henglong was \$141,006,269 for the nine months ended September 30, 2011, compared with \$138,695,023 for the nine months ended September 30, 2010, representing an increase of \$2,311,246, or 1.7%. The net sales increase was mainly due to increased sales volumes with a sales increase of \$5,387,284, decreased sales price with a sales decrease of \$9,806,634 and the effect of foreign currency translation with a sales increase of \$6,730,596.

Net sales for Jiulong was \$52,415,985 for the nine months ended September 30, 2011, compared with \$66,404,291 for the nine months ended September 30, 2010, representing a decrease of \$13,988,306, or 21.1%. Excluding the net sales of \$9,497,104 to Chrysler during the nine months ended September 30, 2010, net sales decrease was \$4,491,202, or 7.9%. The net sales decrease was mainly due to decreased sales volumes with a sales decrease of \$5,796,320, increased sales prices resulting from newly developed steering gear models with prices higher than previous models with a sales increase of \$293,739 and the effect of foreign currency translation with a sales increase of \$1,011,379.

Net sales for Shenyang was \$22,497,997 for the nine months ended September 30, 2011, compared with \$28,376,664 for the nine months ended September 30, 2010, representing a decrease of \$5,878,667, or 20.7%. The net sales decrease was mainly due to decreased sales volumes with a sales decrease of \$7,892,921, increased sales price with a sales increase of \$666,765 and the effect of foreign currency translation with a sales increase of \$1,347,489.

Net sales for Zhejiang was \$14,627,630 for the nine months ended September 30, 2011, compared with \$18,238,724 for the nine months ended September 30, 2010, representing a decrease of \$3,611,094, or 19.8%. The net sales decrease was mainly due to decreased sales volumes with a sales decrease of \$3,665,876, decreased sales price with a sales decrease of \$817,231 and the effect of foreign currency translation with a sales increase of \$872,013.

Net sales for Wuhu was \$25,689,081 for the nine months ended September 30, 2011, compared with \$22,628,769 for the nine months ended September 30, 2010, representing an increase of \$3,060,312, or 13.5%. The net sales increase was mainly due to increased sales volumes with a sales increase of \$3,642,147, decreased sales price with a sales decrease of \$1,638,899 and the effect of foreign currency translation with a sales increase of \$1,057,064.

Net sales for Other Sector was \$44,905,834 for the nine months ended September 30, 2011, compared with \$28,792,095 for the nine months ended September 30, 2010, representing an increase of \$16,113,739 or 56.0%. Including net sales of \$9,497,104 related to sales to Chrysler recorded by Jiulong during the nine months ended September 30, 2010, net sales increase was \$6,616,635, or 17.3%, including increased sales volumes with a sales increase of \$6,326,461, decreased sales price with a sales decrease of \$240,794 and the effect of foreign currency translation with a sales increase of 530,968.

## Cost of Sales

For the nine months ended September 30, 2011, the cost of sales was \$199,950,452, compared with \$184,897,834, for the same period of 2010, an increase of \$15,052,618, or 8.1%, mainly due to the appreciation of the RMB against the U.S. dollar.

Cost of sales for Henglong was \$110,980,677 for the nine months ended September 30, 2011, compared with \$105,072,685 for the nine months ended September 30, 2010, representing an increase of \$5,907,992, or 5.6%. The cost of sales increase was mainly due to increased sale volumes with a cost of sales increase of \$4,579,779, decreased unit cost with a cost of sales decrease of \$3,782,880 and the effect of foreign currency translation with a cost increase of \$5,111,093.

Cost of sales for Jiulong was \$45,434,798 for the nine months ended September 30, 2011, compared with \$57,012,846 for the nine months ended September 30, 2010, representing a decrease of \$11,578,048, or 20.3%. Excluding cost of sales of \$7,430,534 related to sales to Chrysler during the nine months ended September 30, 2010, cost of sales decrease was \$4,147,514, or 8.4%, including decreased sales volumes with a cost of sales decrease of \$5,741,146, increased unit cost with a cost of sales increase of \$619,865 and the effect of foreign currency translation with a cost increase of \$973,767.

Cost of sales for Shenyang was \$19,600,009 for the nine months ended September 30, 2011, compared with \$23,829,846 for the nine months ended September 30, 2010, representing a decrease of \$4,229,837, or 17.8%. The cost of sales decrease was mainly due to decreased sales volumes with a cost of sales decrease of \$6,727,437, increased unit cost with a cost of sales increase of \$1,351,334 and the effect of foreign currency translation with a cost increase of \$1,146,266.

Cost of sales for Zhejiang was \$11,126,154 for the nine months ended September 30, 2011, compared with \$13,033,040 for the nine months ended September 30, 2010, representing a decrease of \$1,906,886, or 14.6%. The cost of sales decrease was mainly due to decreased sales volumes with a cost of sales decrease of \$2,639,063, increased unit cost with a cost of sales increase of \$103,608 and the effect of foreign currency translation with a cost increase of \$628,569.

Cost of sales for Wuhu was \$24,814,112 for the nine months ended September 30, 2011, compared with \$20,876,023 for the nine months ended September 30, 2010, representing an increase of \$3,938,089, or 18.9%. The cost of sales increase was mainly due to increased sales volumes with a cost of sales increase of \$3,374,836, decreased unit cost with a cost of sales decrease of \$423,537 and the effect of foreign currency translation with a cost increase of \$986,790.

Cost of sales for Other Sectors was \$41,430,508 for the nine months ended September 30, 2011, compared with \$24,150,705 for the nine months ended September 30, 2010, representing an increase of \$17,279,803, or 71.5%. Including cost of sales of \$7,430,534 related to sales to Chrysler during the nine months ended September 30, 2010, cost of sales for other sectors increased \$9,849,269, or 31.2%, including increased sales volumes with a cost of sales increase of \$7,745,046, increased unit cost with a cost of sales increase of \$1,486,171 and the effect of foreign currency translation with a cost increase of \$618,052.

Gross margin was 19.5% for the nine months ended September 30, 2011, a 5.2 percentage point decrease from 24.7% for the same period of 2010, primarily due to the decline of average selling price and decreased sales volumes in some operations resulting from a contraction in certain areas of the auto market in China.

## Gain on Other Sales

Gain on other sales consists of net amount retained from sales of materials and other assets. For the nine months ended September 30, 2011, gain on other sales was \$1,359,871, compared with \$981,128 for the same period of 2010, an increase of \$378,743, or 38.6%, mainly due to increased sales of materials.

#### Selling Expenses

Selling expenses were \$7,123,063 for the nine months ended September 30, 2011, compared with \$6,866,249 for the same period of 2010, an increase of \$256,814, or 3.7%. Major increases were warehouse rent charges and transportation expenses.

The increase in rent expense was due to increased inventory level and rent price.

The increase in transportation expense was due to a rise in the price of oil, which led to increases in domestic transportation prices.

### General and Administrative Expenses

General and administrative expenses were \$10,868,767 for the nine months ended September 30, 2011, compared with \$8,567,854 for the same period of 2010, an increase of \$2,300,913, or 26.9%. The increase was primarily due to increases in salaries and wages expenses, labor insurance expenses and listing expenses and a decrease in the recovery of doubtful accounts.

The increases in salaries and wages and labor insurance expenses were mainly due to the inflation of labor expenses.

The increase in listing expense was mainly due to increased cost related to being a publicly-listed entity and the Company's need to evaluate its internal control over financial reporting.

### Research and Development Expenses

Research and development expenses were \$6,609,136 for the nine months ended September 30, 2011, compared with \$4,291,044 for the nine months ended September 30, 2010, an increase of \$2,318,092, or 54.0%.

The global automotive parts industry is highly competitive; winning and maintaining new business requires suppliers to rapidly produce new and innovative products on a cost-competitive basis. From 2010, foreign OEMs significantly increased their demand for Electronic Steering Gear, "EPS," but the related technology in China is still in the research and development and testing stage. In order to bring to market "EPS" quickly, the Company continues to invest heavily in the R&D of "EPS" in 2011, including increasing the Company's senior technicians and advanced manufacture equipment on "EPS," establishing the "EPS" trial-production department, introducing technology expectations and purchasing advanced technology and test equipment. The Company expects such R&D cost to continue to increase going forward as it seeks to offer new and innovative products to the market.

### Income from Operations

Income from operations was \$25,331,226 for the nine months ended September 30, 2011, compared with \$41,774,818 for the nine months ended September 30, 2010, a decrease of \$16,443,592, or 39.4%, as a result of a decrease of \$11,946,516 or 19.7% in gross profit, an increase of \$378,743 or 38.6% in gain on other sales, and an increase of \$4,875,819, or 24.7%, in operating expenses.

### Financial Expenses

Financial expenses were \$2,902,150 for the nine months ended September 30, 2011, compared with \$2,056,431 for the nine months ended September 30, 2010, an increase of \$845,719, primarily as a result of the fact that (a) beginning on February 15, 2011, the Company accrued interest at the rate of 13% according to the terms of the Convertible Notes, and during the nine months ended September 30, 2010, the Company accrued interest at the rate of 11%; (b) the financial expense for the nine months ended September 30, 2010 was lower as the interest and make-whole amount have been accrued for to its redemption value upon the WAP default; and (c) the decrease in loss on foreign currency exchange, as the Company's subsidiaries based in the PRC and Genesis maintain their books and records in Renminbi, their functional currency, and Hengsheng, a subsidiary of the Company based in the PRC, settles its external sales in U.S. dollars. For the nine months ended September 30, 2011, the RMB appreciated approximately 6% against the U.S. dollar, compared with the same period in 2010.

### Gain on Change in Fair Value of Derivative

Gain on change in fair value of derivative was \$19,373,520 for the nine months ended September 30, 2011, compared with a gain of \$14,122,730 for the same period of 2010, an increase of \$5,250,790.

During the nine months ended September 30, 2011, the Company's common stock market price dropped to \$4.72 from \$13.62 at the beginning of the period. Thus, the intrinsic value of the embedded conversion feature in financial instruments decreased, the fair value of compound derivative liabilities decreased and the gain on change in fair value of derivatives increased. (see note 14)

During the nine months ended September 30, 2010, the Company's common stock market price dropped to \$15.28 from \$18.71 at the beginning of the period. Thus, the intrinsic value of the embedded conversion feature in financial instruments decreased, the fair value of compound derivative liabilities decreased and the gain on change in fair value of derivatives increased. (see note 14)

#### Gain on Convertible Notes Conversion

During the nine months ended September 30, 2011, gain on Convertible Notes conversion was \$1,564,418. During the nine months ended September 30, 2010, there was no such gain.



On March 1, 2011, an investor converted \$6,428,571 principal amount of the Convertible Notes at a conversion price of \$7.0822 per share and the Company issued 907,708 shares of its common stock to the investor. On the conversion date, the market price of the common shares issued was \$10,111,869 (\$11.14 per share) and the value of the conversion consideration was \$11,676,287, including \$6,428,571 of principal, \$1,506,143 of coupon interest and make-whole amount payable and \$3,741,573 of derivative liabilities under such principal. The Company recorded a gain on Convertible Notes conversion of \$1,564,418, which is the difference between the market price of the common stock and the conversion consideration.

#### Income Before Income Tax Expenses and Equity In Earnings Of Affiliated Companies

Income before income tax expenses and equity in earnings of affiliated companies was \$43,521,479 for the nine months ended September 30, 2011, compared with \$54,107,496 for the nine months ended September 30, 2010, a decrease of \$10,586,017, or 19.6%, including a decrease in income from operations of \$16,443,592, an increase in gain on other sales of \$378,743, an increase in financial expense of \$845,719, an increase in gain on change in fair value of derivative of \$5,250,790 and an increase in gain on Convertible Notes conversion of \$1,564,418.

#### Income Taxes

Income tax expense was \$4,314,912 for the nine months ended September 30, 2011, compared with \$6,442,971 of income tax expense for the nine months ended September 30, 2010, a decrease of \$2,128,059, or 33.0%, mainly because of the decrease of income before income tax and the decrease in the effective tax rate. For the nine months ended September 30, 2011, among these income before income tax, the proportion of permanent difference, namely non-taxable gain on fair value adjustment, was higher than that in the same period of 2010, so the effective tax rate for the nine months ended September 30, 2011 was lower than that in the nine months ended September 30, 2010.

#### Net Income

Net income was \$39,335,930 for the nine months ended September 30, 2011, compared with \$47,664,525 for the nine months ended September 30, 2010, a decrease of \$8,328,595 or 17.5%, including a decrease in income before income tax expenses and equity in earnings of affiliated companies of \$10,586,017, or 19.6%, a decrease in income tax expenses of \$2,128,059, or 33.0%, and an increase in equity in earnings of affiliated companies of \$129,363.

#### Net Income Attributable to Noncontrolling Interest

Net income attributable to noncontrolling interest was \$5,241,143 for the nine months ended September 30, 2011, compared with \$8,227,985 for the nine months ended September 30, 2010, a decrease of \$2,986,842, or 36.3%, primarily due to the decrease in the share of the Sino-foreign joint ventures' net income.

The Company owns different equity interests in seven Sino-foreign joint ventures, through which it conducts its operations. All the operating results of these seven Sino-foreign joint ventures were consolidated in the Company's financial statements as of September 30, 2011 and 2010. The Company records the noncontrolling interest's share in the earnings of the respective Sino-foreign joint ventures for each period.

#### Net Income Attributable to Parent Company

Net income attributable to parent company was \$34,094,787 for the nine months ended September 30, 2011, compared with a net income of \$39,436,540 for the nine months ended September 30, 2010, a decrease of \$5,341,753, or 13.5%, mainly due to a decrease in operation income.

## Liquidity and Capital Resources

### Capital Resources and Use of Cash

The Company has historically financed its liquidity requirements from a variety of sources, including short-term borrowings under bank credit agreements, bankers' acceptance, issuances of capital stock and notes and internally generated cash. As of September 30, 2011, the Company had cash and cash equivalents of \$76,067,212, compared with \$49,424,979 as of December 31, 2010, an increase of \$26,642,233, or 53.9%.

The Company had working capital of \$139,362,314 as of September 30, 2011, compared with \$54,191,797 as of December 31, 2010, an increase of \$85,170,517, or 157.2%. According to the terms of Convertible Notes, Convertible Notes payable, compound derivative liabilities and accrued make-whole redemption interest expense for Convertible Notes were recorded as current liabilities before February 15, 2011, and thereafter reclassified to and recorded as non-current liabilities (refer to Note 16). As a result, working capital increased after the reclassification.

## Capital Source

The Company's capital source is multifaceted, such as obtaining bank loans and notes payables. In financing activities and operating activities, the Company's banks require the Company to sign a line of credit agreement and repay such facilities within one year. On the condition that the Company can provide adequate mortgage security and has not violated the terms of the line of credit agreement, such one year facilities can be extended for another year (see the table in section (a) Bank loans).

The Company had bank loans maturing in less than one year of \$11,801,917 and notes payables of \$57,436,875 as of September 30, 2011.

The Company currently expects to be able to obtain similar bank loans and notes payables in the future if it can provide adequate mortgage security following the termination of the agreements (see the table in section (a) Bank loan). If the Company is not able to do so, it will have to refinance such debt as it becomes due or repay that debt to the extent it has cash available from operations or from the proceeds of additional issuances of capital stock. Owing to depreciation, the value of the mortgages securing the above-mentioned bank loans and banker's acceptance bills will be devalued by approximately \$6,417,605. If the Company wishes to obtain the same amount of bank loans and banker's acceptance bills, it will have to provide \$11,308,315 additional mortgages as of the maturity date of such agreements (see the table in section (a) Bank loan). The Company still can obtain a reduced line of credit with a reduction of \$6,417,605, which is 56.8% (the mortgage rates) of \$11,308,315, if it cannot provide additional mortgages. The Company expects that the reduction of bank loans will not have a material adverse effect on its liquidity.

On February 15, 2008, the Company issued \$35,000,000 of Convertible Notes to Lehman Brothers Commercial Corporation Asia Limited, "LBCCA", and YA Global Investments, L.P., "YA Global", maturing in 5 years. According to the terms of the Senior Convertible Notes (as described in Note 13), Convertible Notes may be required to be repaid in cash on or prior to their maturity. For example, Convertible Note holders are entitled to require the Company to redeem all or any portion of the Convertible Notes in cash, if the Weighted Average Price (WAP) for twenty (20) consecutive trading days is less than \$3.187 at any time following February 15, 2009, the "WAP Default," by delivering written redemption notice to the Company within five (5) business days after the receipt of the Company's notice of the WAP Default.

As a result of the worldwide financial turmoil in 2008 and the first half of 2009, the Company's stock's WAP for twenty (20) consecutive trading days ended on March 16, 2009 was below \$3.187. On March 17, 2009, the Company delivered two WAP Default notices to the Convertible Note holders. On March 27, 2009, the Company received a letter dated March 26, 2009 from YA Global, one of the Convertible Note holders, electing to require the Company to redeem all the three Convertible Notes it held in the total principal amount of \$5,000,000, together with interest, late charges, if any, and the Other Make Whole Amount as defined in Section 5(d) of the Convertible Notes. After negotiation, on April 15, 2009, the Company paid YA Global \$5,041,667 for the total principal amount (\$5,000,000), together with interest and late charges, if any. YA Global has waived its entitlement to the Other Make Whole Amount.

Following the WAP Default notices, the Company received a letter from the provisional liquidator acting on behalf of LBCCA, the "LBCCA Liquidator," requesting that it be granted an extension until April 24, 2009 to consider its rights under the Convertible Notes. The Company granted an extension to April 15, 2009. The LBCCA Liquidator further requested another extension to April 24, 2009. On April 24, 2009, LBCCA's lawyers sent three Holder Redemption Notices electing to redeem the entire outstanding principal of \$30,000,000, together with interest, late charges, if any, and the Other Make Whole Amount, to be paid on July 23, 2009. The Company discussed settlement with the LBCCA Liquidator, and on or about July 22, 2009, the Company and the LBCCA Liquidator agreed to extend the applicable

holder mandatory redemption date for two months to September 23, 2009 to give more time to the Company and the LBCCA Liquidator to pursue settlement discussion. The Company received a letter dated September 22, 2009 from the LBCCA Liquidator stating that upon the Company's acceptance of the revocation, all holder redemption notices dated April 24, 2009 shall be immediately revoked as if they were never issued, and the letter and the revocation did not purport to amend, restate or supplement any other terms and conditions under the three Notes and Securities Purchase Agreements dated 1 February 2008 between the Company and the LBCCA Liquidator. The Company accepted such revocation on September 23, 2009. On March 1, 2011, LBCCA Liquidator converted \$6,428,571 principal amount of the Convertible Notes at a conversion price of \$7.0822 per share and the Company issued 907,708 shares of its common stock to the investor. No additional consideration was paid for the conversion of the Convertible Notes into common stock.

The Company's ability to redeem the Convertible Notes and meet its payment obligations depends on its cash position and its ability to refinance or generate significant cash flow, which is subject to general economic, financial and competition factors and other factors beyond the Company's control. The Company cannot assure you that it has sufficient funds available or will be able to obtain sufficient funds to meet its payment obligations under the Convertible Notes, and the Company's redemption of the Convertible Notes would result in an adverse effect on its liquidity and capital resources, business, results of operations or financial condition.

(a) Bank loans

As of September 30, 2011, the principal outstanding under the Company's credit facilities and lines of credit was as follows:

	Bank	Due Date	Amount Available	Amount Used	Mortgage Value
Comprehensive credit facilities 1	Bank of China	Jan-12	\$ 22,187,602	\$ 4,720,767	\$ 6,820,752
Comprehensive credit facilities	Jingzhou Commercial Bank	Apr-12	31,471,778	15,222,867	69,924,688
Comprehensive credit facilities	China Construction Bank	Oct-12	12,588,711	3,147,178	13,065,760
Comprehensive credit facilities	Shanghai Pudong Development Bank	Nov-11	15,735,889	7,021,826	15,079,671
Comprehensive credit facilities	China CITIC Bank	Aug-12	16,365,324	10,398,410	16,654,582
Comprehensive credit facilities	Industrial and Commercial Bank of China	May-12	16,050,607	2,486,270	5,657,052
Comprehensive credit facilities 1	China Hua Xia Bank	Jan-12	25,177,422	15,549,629	15,549,629
Comprehensive credit facilities	China Everbright Bank	Aug-12	4,720,767	6,495,083	8,057,463
Total			\$ 144,298,100	\$ 65,042,030	\$ 150,809,597

1. Henglong's comprehensive credit facility with Bank of China, Henglong and Jielong's comprehensive credit facility with Shanghai Pudong Development Bank, and Henglong's comprehensive credit facility with Hua Xia Bank, also need to be guaranteed by Jiulong, another subsidiary of the Company, in addition to the above pledges.

The Company may request banks to issue notes payable or bank loans within its credit line using a 364-day revolving line.

The Company refinanced its short-term debt during 2011 at annual interest rates of 6.31% to 7.57%, and maturity terms of six to twelve months. Pursuant to the comprehensive credit line arrangement, the Company pledged land use rights with an assessed value of \$6.8 million as security for its comprehensive credit facility with the Bank of China; pledged land use rights and equipment with an assessed value of approximately \$69.9 million as security for its revolving comprehensive credit facility with Jingzhou Commercial Bank; pledged land use rights and buildings with an assessed value of approximately \$11.5 million, and accounts receivables with an assessed value of approximately \$1.6 million as security for its comprehensive credit facility with China Construction Bank; pledged land use rights and buildings with an assessed value of approximately \$15.1 million as security for its comprehensive credit facility with Shanghai Pudong Development Bank; pledged land use rights and buildings with an assessed value of approximately \$16.7 million as security for its comprehensive credit facility with China CITIC Bank; pledged land use rights and buildings with an assessed value of approximately \$4.1 million, and accounts receivables with an assessed value of approximately \$1.6 million as security for its comprehensive credit facility with Industrial and Commercial Bank of China; pledged accounts receivables with an assessed value of approximately \$15.5 million as security for its comprehensive credit facility with Hua Xia Bank; and pledged land use rights and buildings with an assessed value of approximately \$8.1 million as security for its comprehensive credit facility with China Everbright Bank.

As of September 30, 2011, the Company has \$79,256,070 available for additional borrowing and the amounts borrowed were used for working capital as detailed below. Additionally, the Company also undertook a note payable facility outside the credit facilities of \$4,196,762 which is also included below.

The following table summarizes the contract information of the short-term borrowings drawn-down from the credit facilities between the banks and the Company as of September 30, 2011:

Bank	Purpose	Borrowing Date	Borrowing Term (Year)	Annual Percentage Rate	Date of Interest Payment	Date of Payment	Amount Payable on Due Date
China Construction Bank	Working Capital	29-Jun-11	1	6.31	% Pay monthly	28-Jun-12	\$ 3,147,178
Industrial and Commercial Bank of China	Working Capital	12-May-11	0.5	6.44	% Pay monthly	9-Oct-11	1,573,589
Bank of China	Working Capital	30-Sep-11	1	6.56	% Pay monthly	29-Sep-12	4,720,767
China CITIC Bank	Working Capital	6-Jul-11	1	7.57	% Pay monthly	5-Jul-12	2,360,383
<b>Total</b>							<b>\$ 11,801,917</b>

The Company must use the loans for the purposes described in the table. If the Company fails, it will be charged a penalty interest at 100% of the specified loan rate. The Company has to pay interest at the interest rate described in the table on the 20th of each month. If the Company fails, it will be charged a compound interest at the specified rate. The Company has to repay the principal outstanding on the specified date in the table. If it fails, it will be charged a penalty interest at 50% of the specified loan rate. Management believes that the Company had complied with such financial covenants as of September 30, 2011, and is expected to continue to comply with them.

The following table summarizes the contract information of issuing notes payable between the banks and the Company as of September 30, 2011:

Purpose	Term (Month)	Due Date	Amount Payable on Due Date
Working Capital	3-6	Oct - 11	\$ 9,409,794
Working Capital	3-6	Nov - 11	10,366,273
Working Capital	3-6	Dec - 11	10,024,932
Working Capital	3-6	Jan - 12	7,259,752
Working Capital	3-6	Feb - 12	7,777,054
Working Capital	3-6	Mar - 12	12,599,070
<b>Total</b>			<b>\$ 57,436,875</b>

The Company must use the loans for the purposes described in the table. If it fails, the banks will no longer issue the notes payable, and it may have an adverse effect on the Company's liquidity and capital source. The Company has to deposit sufficient cash in the designated account of the bank on the due date of notes payable for payment to the suppliers. If the bank has advanced payment to the Company, it will be charged a penalty interest at 150% of the specified loan rate. Management believes that the Company had complied with such financial covenants as of September 30, 2011, and is expected to continue to comply with them.

(b) Financing from investors:

On March 1, 2011, an investor converted \$6,428,571 of the principal amount of the Convertible Notes into common shares.

Cash Requirements

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The following table summarizes the Company's expected cash outflows resulting from financial contracts and commitments. The Company has not included information on its recurring purchases of materials for use in its manufacturing operations. These amounts are generally consistent from year to year, closely reflecting the Company's levels of production, and are not long-term in nature being less than three months.

	Total	Payment Due Dates			
		Less than 1 year	1-3 years	3-5 years	More than 5 Years
Short-term bank loan	\$ 11,801,917	\$ 11,801,917	\$-	\$-	\$-
Notes payable	57,436,875	57,436,875	-	-	-
Convertible Notes payable	23,571,429	-	23,571,429	-	-
Interest on Convertible Notes, make-whole amount at maturity and short-term bank loan	12,552,768	1,142,887	11,409,881	-	-
Other contractual purchase commitments, including information technology	13,507,303	11,338,115	2,169,188	-	-
Total	\$ 118,870,292	\$ 81,719,794	\$ 37,150,498	\$-	\$-



The Company had \$13,302,737 of capital commitments as of September 30, 2011, arising from equipment purchases for expanding production capacity. The Company intends to invest \$11,338,115 in the remaining three months of 2011 using its working capital. Management believes that this will not have a material adverse effect on the Company's liquidity.

#### Cash flows

##### (a) Operating activities

Net cash provided by operations during the nine months ended September 30, 2011 was \$31,728,545, compared with net cash provided of \$29,604,550 for the same period of 2010, an increase of \$2,123,995.

- The primary factors for the increase of cash generated from operations were that certain customers' installment payment schedules under the Company's credit policy increased the Company's cash flows as sales decreased. This factor was offset by an increase of inventory, as the Company's sale growth was not reached.

Cash generated from operations increased as a result of collections from sales exceeding payments for purchases in the nine months ended September 30, 2011 compared with the same period of 2010.

##### (b) Investing activities

The Company expended net cash of \$10,167,584 in investment activities during the nine months ended September 30, 2011, compared with \$25,891,634 during the same period of 2010, a decrease of \$15,724,050, mainly due to a significant slowdown in China's auto market, and the Company reducing the speed of its capital expenditure, accordingly.

##### (c) Financing activities

During the nine months ended September 30, 2011, the Company obtained net cash of \$3,080,160 from financing activities, as compared to \$1,189,918 in for the same period of 2010, an increase of \$1,890,242, mainly due to the increase in loans acquired from banks and the decrease in dividend paid to minority interest holders of the joint ventures.

- During the nine months ended September 30, 2011, the Company acquired net cash of \$4,791,706 from the bank. For the nine months ended September 30, 2010, the Company acquired net cash of \$3,685,215.

During the nine months ended September 30, 2011, the Company paid dividends of \$1,691,608 to the minority interest holders of the joint ventures. During the nine months ended September 30, 2010, the Company paid dividends of \$2,871,603 to the minority interest holders of the joint ventures.

#### Off-Balance Sheet Arrangements

At September 30, 2011 and 2010, the Company did not have any transactions, obligations or relationships that could be considered off-balance sheet arrangements.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

There were no material changes to the disclosure made in the Company's Annual Report on Form 10-K for the year ended December 31, 2010 regarding this matter.



ITEM 4.

CONTROLS AND PROCEDURES.

A. Disclosure Controls and Procedures

The Company's management, under the supervision and with the participation of its chief executive officer and chief financial officer, Messrs. Wu Qizhou and Li Jie, respectively, evaluated the effectiveness of the Company's disclosure controls and procedures as of September 30, 2011, the end of the period covered by this Report. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports, such as this Form 10-Q, that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management evaluated the effectiveness of the Company's disclosure controls and procedures as of September 30, 2011. Based on that evaluation, Messrs. Wu and Li concluded that the Company's disclosure controls and procedures were not effective as of September 30, 2011.

The Company's disclosure controls and procedures are designed to provide reasonable, not absolute, assurance that the objectives of its disclosure control system are met. Because of inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, if any, within a company have been detected.

B. Changes in Internal Control Over Financial Reporting

There have been no changes in the Company's internal control over financial reporting during the three-month period ended September 30, 2011 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II.— OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

On October 25, 2011, a purported securities class action was filed in the United States District Court for the Southern District of New York on behalf of all purchasers of the Company's securities between March 25, 2010 and March 17, 2011. The complaint alleges that the Company and certain of its present and former officers and directors violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, and the rules promulgated thereunder, and seeks unspecified damages. The Company has not yet responded to the complaint, but believes the allegations in the complaint are without merit. The Company intends to defend itself vigorously against the claims.

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

ITEM 1A.RISK FACTORS.

There have been no material changes from the risk factors previously disclosed in Item 1A of the Company's 2010 Annual Report on Form 10-K.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. (REMOVED AND RESERVED.)

None.

ITEM 5. OTHER INFORMATION.

None.

## ITEM 6.

## EXHIBITS.

## INDEX TO EXHIBITS

Exhibit Number	Description
3.1(i)	Certificate of Incorporation (incorporated by reference from the filing on Form 10KSB File No. 000-33123.)
3.1(ii)	Bylaws (incorporated by reference from the Form 10KSB for the year ended December 31, 2002.)
10.1	Joint-venture Agreement, dated March 31, 2006, as amended on May 2, 2006, between Great Genesis Holdings Limited and Wuhu Chery Technology Co., Ltd. (incorporated by reference to the exhibit 10.8 to the Company's Form 10Q Quarterly Report on May 10, 2006 )
10.2	Securities Purchase Agreement dated February 1, 2008 among us, Lehman Brothers Commercial Corporation Asia Limited, and YA Global Investments, L.P. (incorporated by reference to the Company's Form 10-K for the year ended December 31, 2007.)
10.3	Securities Purchase Agreement dated February 15, 2008 between us and the investors. (incorporated by reference to the Company's Form 10-K for the year ended December 31, 2007.)
10.4	Escrow Agreement dated February 15, 2008 among us, U.S. Bank National Association, Lehman Brothers Commercial Corporation Asia Limited, and YA Global Investments, L.P. (incorporated by reference to the Company's Form 10-K for the year ended December 31, 2007.)
10.5	Registration Rights Agreement dated February 15, 2008 among us, Lehman Brothers Commercial Corporation Asia Limited, and YA Global Investments, L.P. (incorporated by reference to the Company's Form 10-K for the year ended December 31, 2007.)
10.6	Senior Convertible Note dated February 15, 2008 in the original principal amount of \$8,571,429 issued by us in favor of TFINN & CO. as nominee for Lehman Brothers Commercial Corporation Asia Limited. (incorporated by reference to the Company's Form 10-K for the year ended December 31, 2007.)
10.7	Senior Convertible Note dated February 15, 2008 in the original principal amount of \$6,428,571 issued by us in favor of TFINN & CO. as nominee for Lehman Brothers Commercial Corporation Asia Limited. (incorporated by reference to the Company's Form 10-K for the year ended December 31, 2007.)
10.8	Senior Convertible Note dated February 15, 2008 in the original principal amount of \$15,000,000 issued by us in favor of TFINN & CO. as nominee for Lehman Brothers Commercial Corporation Asia Limited. (incorporated by reference to the Company's Form 10-K for the year ended December 31, 2007.)
10.9	Closing Warrant to purchase 564,799 shares of common stock at \$8.8527 per share, dated February 15, 2008, issued by us in favor of TFINN & CO. as nominee for Lehman Brothers Commercial Corporation Asia Limited. (incorporated by reference to the Company's Form 10-K for the year ended December 31, 2007.)
10.10	Escrow Warrant to purchase 564,799 shares of common stock at \$8.8527 per share, dated February 15, 2008, issued by us in favor of TFINN & CO. as nominee for Lehman Brothers Commercial Corporation Asia Limited. (incorporated by reference to the Company's Form 10-K for the year ended December 31, 2007.)
31.1	Rule 13a-14(a) Certification*
31.2	Rule 13a-14(a) Certification*
32.1	Section 1350 Certification*
32.2	Section 1350 Certification*
101+	The following materials from the China Automotive Systems, Inc. Quarterly Report on Form 10-Q for the quarter ended September 30, 2011, filed on November 8, 2011 formatted in Extensible Business Reporting Language (XBRL):
	(i) Condensed Unaudited Consolidated Balance Sheets,
	(ii) Condensed Unaudited Consolidated Statements of Operations,
	(iii) Condensed Unaudited Consolidated Statements of Comprehensive Income,

- (iv) Condensed Unaudited Consolidated Statements of Cash Flows, and
- (v) Condensed Unaudited related notes

\*

filed herewith

+XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

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.

CHINA AUTOMOTIVE SYSTEMS, INC.  
(Registrant)

Date: November 8, 2011

By: /s/ Qizhou Wu  
Qizhou Wu  
President and Chief Executive Officer

Date: November 8, 2011

By: /s/ Jie Li  
Jie Li  
Chief Financial Officer