Sino Clean Energy Inc
Form 10-Q
November 18, 2011

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

FORM 10-Q

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

For the quarterly period ended September 30, 2011

or

¨ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from to .

Commission File Number 001-34773

SINO CLEAN ENERGY INC.
(Exact name of registrant as specified in its charter)

Nevada	75-2882833
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

Room 1502, Building D, Wangzuo International City Building
No. 1 Tangyuan Road, Gaoxin District
Xi'an, Shaanxi Province, People's Republic of China
(Address of Principal Executive Offices Including Zip Code)

+86 29 8844-7960
(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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 xNo ¨

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 x No ¨

Indicate by check mark if the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company

Large Accelerated Filer ¨ Accelerated Filer ¨ Non-Accelerated Filer ¨ Smaller reporting company x

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act).

Yes ¨ No x

As of November 10, 2011, 23,863,701 shares of the issuer's common stock, par value $0.001, were outstanding.

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PART I

FINANCIAL INFORMATION

ITEM 1 FINANCIAL STATEMENTS

Sino Clean Energy Inc. and Subsidiaries
Condensed Consolidated Balance Sheets

	September 30, 2011 (Unaudited)	December 31, 2010
ASSETS		
Cash and cash equivalents	$ 59,410,230	$ 52,055,857
Accounts receivable, net of allowance for doubtful accounts of $1,083,006 and $0 at September 30, 2011 and December 31, 2010, respectively	12,152,648	3,856,941
Inventories	2,158,712	1,261,334
Prepaid inventories	14,547,285	10,242,878
Prepaid and other current assets	41,370	51,048
Due from related party-Suo'ang BST	-	10,307,912
Land use right – current portion	75,200	40,079
Total current assets	88,385,445	77,816,049
Land use right – non-current portion	5,499,758	1,799,889
Property, plant and equipment, net	18,823,510	13,609,932
Deposit on land use rights, plant and equipment	6,263,308	9,409,091
Goodwill	762,018	762,018
Total assets	$ 119,734,039	$ 103,396,979
LIABILITIES AND SHAREHOLDERS' EQUITY		
Accounts payable and accrued expenses	2,844,059	1,560,183
Taxes payable	1,829,071	3,329,844
Mortgage payable – current portion	5,762	5,450
Amount due to director	48,454	48,457
Derivative liabilities	659,949	14,555,027
Total current liabilities	5,387,295	19,498,961
Mortgage payable –non-current portion	161,208	160,095
Total liabilities	5,548,503	19,659,056
Commitments and contingencies		
Shareholders' Equity		
Preferred stock, $0.001 par value, 50,000,000 shares authorized, none issued and outstanding		
Common stock, $0.001 par value, 30,000,000 shares authorized, 23,863,701 and 23,452,270 issued and outstanding as of September 30, 2011 and December 31, 2010 respectively	23,841	23,452
Additional paid-in capital	67,291,387	66,567,560
Treasury stock, at cost, 321,100 and 0 shares, respectively	(799,423)	-

Retained earnings	37,288,125	9,221,924
Statutory reserves	4,739,048	4,739,048
Accumulated other comprehensive income	5,642,558	3,185,939
Total shareholders’ equity	114,185,536	83,737,923
Total liabilities and shareholders’ equity	$ 119,734,039	$ 103,396,979

See accompanying notes to the condensed consolidated financial statements

Sino Clean Energy Inc. and Subsidiaries

Condensed Consolidated Statements of Income and Other Comprehensive Income (Unaudited)

	Three months ended September 30, 2011	Three months ended September 30, 2010	Nine months ended September 30, 2011	Nine months ended September 30, 2010
Revenue	$17,150,169	$24,913,134	$73,948,258	$73,571,899
Cost of goods sold	(11,415,576)	(15,269,720)	(47,575,971)	(44,448,913)
Gross profit	5,734,593	9,643,414	26,372,287	29,122,986
Selling expenses	852,075	1,156,147	3,673,993	3,203,245
General and administrative expenses	1,229,089	579,837	4,773,222	1,925,072
Income from operations	3,653,429	7,907,430	17,925,072	23,994,669
Other income (expense)				
Interest and finance cost	(5,437)	(5,735)	(5,437)	(10,459,201)
Interest income	77,695	29,889	193,594	62,113
Gain on extinguishment of derivative liability	3,107,884	-	3,590,721	28,404,181
Change in fair value of derivative liabilities	(2,686,654)	(970,813)	10,304,357	(2,348,479)
Total other income (expense)	493,488	(946,659)	14,083,235	15,658,614
Income before provision for income taxes	4,146,917	6,960,771	32,008,307	39,653,283
Provision for income taxes	878,248	1,349,424	3,942,106	4,640,556
Net income	3,268,669	5,611,347	28,066,201	35,012,727
Other comprehensive income				
Foreign currency translation adjustment	294,399	67,493	2,456,619	348,965
Comprehensive income	$3,563,068	$5,678,840	$30,522,820	$35,361,692
Weighted average number of shares				
-Basic	23,499,604	16,703,844	23,482,939	15,385,062
-Diluted	23,499,604	18,780,537	23,482,939	18,668,856
Income (loss) per common share				
- Basic	$0.14	$0.34	$1.20	$2.28
- Diluted	$0.14	$0.30	$1.20	$1.88

See accompanying notes to the condensed consolidated financial statements

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Sino-Clean Energy, Inc. and Subsidiaries

Condensed Consolidated Statements of Changes in Shareholders' Equity

For the nine months ended September 30, 2011
(Unaudited)

	Common Stock		Additional paid-in	Treasury	Statutory	Retained	Accumulated other comprehensive	
	Share	Amount	capital	Stock	Reserve	earnings	income	Total
Balance, January 1, 2011	23,452,270	$23,452	$66,567,560	-	$4,739,048	$9,221,924	$3,185,939	$83,737,923
Share issued for exercise of warrants and options	411,431	389	593,827	-	-	-	-	594,216
Purchase of treasury stock	-	-	-	(799,423)	-	-	-	(799,423)
Fair value of vested stock options	-	-	130,000	-	-	-	-	130,000
Net income	-	-	-	-	-	28,066,201	-	28,066,201
Foreign currency translation gain	-	-	-	-	-	-	2,456,619	2,456,619
Balance, September 30, 2011	23,863,701	$23,841	$67,291,387	(799,423)	$4,739,048	$37,288,125	$5,642,558	$114,185,536

See accompanying notes to the condensed consolidated financial statements

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Sino Clean Energy Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Nine months ended September 30, 2011	2010
Cash flows from operating activities:		
Net income	$ 28,066,201	$ 35,012,727
Adjustments to reconcile net income to cash provided by operating activities :		
Depreciation and amortization	2,221,025	1,593,325
Amortization of discount on convertible notes	-	8,601,975
Fair value of vested stock options	130,000	34,152
Fair value of common stock issued for repayment of interest expense	-	1,864,701
Change in fair value of derivative liabilities	(10,304,357)	2,348,479
Gain on extinguishment of derivative liability	(3,590,721)	(28,404,181)
Bad debt expense	1,072,124	-
Change in operating assets and liabilities :		
Accounts receivable	(9,478,656)	171,480
Inventories	(930,043)	(418,740)
Prepaid inventories	(4,569,666)	(86,835)
Prepaid and other current assets	8,356	269,146
Tax recoverable	-	138,984
Accounts payable and accrued expenses	1,324,280	(491,938)
Taxes payable	(1,414,540)	644,310
Net cash provided by operating activities	2,534,003	21,277,585
Cash flows from investing activities:		
Deposits on land use rights, plant and equipment	(6,262,212)	(2,239,737)
Repayment from related party- Suo'ang BST	10,172,674	-
Purchase of property, plant and equipment	(1,280,304)	(2,621,605)
Issuance of note receivable	(300,000)	-
Collection of note receivable	300,000	-
Net cash provided by (used in) investing activities	2,630,158	(4,861,342)
Cash flows from financing activities:		
Prepayment and deposits related to deferred offering costs	-	(652,053)
Cash received from exercise of warrants	594,216	263,256
Proceed of mortgage payable	-	163,135
Repayment of mortgage payable	(2,636)	(2,039)
Purchase of treasury stock	(799,423)	-
Net cash used in financing activities	(207,843)	(227,701)
Effect of foreign currency translation	2,398,055	(143,004)
Net increase in cash and cash equivalents	7,354,373	16,045,538
Cash and cash equivalents, beginning of period	52,055,857	18,302,558
Cash and cash equivalents, end of period	$ 59,410,230	$ 34,348,096

Supplemental Disclosure Information:		
Cash paid for taxes	$ 4,948,779	$ 4,296,422
Supplemental non-cash investing and financing activities:		
Deposits applied to purchase of land use rights, property, plant and equipment	$ 9,285,645	$ -
Increase in property, plant and equipment and accounts payable and accrued expenses	$ -	$ 1,175,144
Issuance of shares upon conversion of convertible notes	$ -	$ 10,217,000

See accompanying notes to the condensed consolidated financial statements

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Sino Clean Energy Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

For the nine months ended September 30, 2011 and 2010

1. ORGANIZATION AND BUSINESS ACTIVITIES

Sino Clean Energy Inc. (sometimes referred to in this quarterly report as the "Company", "we" or "our") is a holding company that, through its subsidiaries, is a leading third party commercial producer and distributor of coal-water slurry fuel ("CWSF") in China. CWSF is a clean fuel that consists of fine coal particles suspended in water. Our CWSF products are mainly used to fuel boilers and furnaces to generate steam and heat for residential and industrial applications. We sell our products in China and our customers include industrial, commercial, residential and government organizations. Our strong reputation in the CWSF industry in China, together with our established track record for consistently delivering products in large quantities, has enabled us to expand our customer base. We primarily use washed coal to produce CWSF. We acquire the raw materials for each of our production facilities primarily from nearby coal mines. We have established strong relationships with our suppliers and our ability to purchase large quantities of raw materials has allowed us to achieve favorable pricing and delivery terms.

Corporate Organization and History

We were originally incorporated in Texas as "Discount Mortgage Services, Inc." on July 11, 2000. In September 2001, we purchased Endo Networks, Inc., a Canadian software developer, and changed our name to "Endo Networks, Inc." on November 5, 2001. We re-domiciled to the State of Nevada on December 13, 2001.

On October 20, 2006 we consummated a share exchange transaction with Hangson, a British Virgin Islands company, the stockholders of Hangson and a majority of our stockholders. We issued a total of 2,600,000 shares of our common stock to the Hangson shareholders and a consultant in the transaction, in exchange for 100% of the common stock of Hangson. As a result of the transaction we became engaged in the CWSF business, through the operations of Suo'ang BST and Suo'ang New Energy. On January 4, 2007, we changed our name from "Endo Networks, Inc." to "China West Coal Energy Inc.", and then on August 15, 2007, we changed our name again to our present name, Sino Clean Energy Inc.

Hangson was a holding company that controlled Suo'ang BST and Suo'ang BST's 80%-owned subsidiary Suo'ang New Energy, through a series of contractual arrangements. The remaining 20% of Suo'ang New Energy was owned by Mr. Peng Zhou, a member of our board of directors and, at that time, the chief operating officer of Suo'ang BST. Suo'ang BST, through Suo'ang New Energy, commenced CWSF production in July 2007. Although Hangson was entitled to acquire the remaining 20% of Suo'ang New Energy from Mr. Zhou, the transfer was not completed and Mr. Zhou remained as the record shareholder of Suo'ang New Energy.

In 2009, we effected a reorganization of our corporate structure in order to make Suo'ang New Energy a wholly-owned subsidiary which included entering into a series of agreements transferring the contractual arrangements, through which Hangson controlled Suo'ang BST, to Suoke Clean Energy.

On September 15, 2009, Suo'ang BST and Hangson entered into a share transfer agreement with Suoke Clean Energy pursuant to which Suo'ang BST and Hangson agreed to transfer 100% of the equity interests in Suo'ang New Energy to Suoke Clean Energy. However, since Mr. Zhou still owned 20% of Suo'ang New Energy, on November 10, 2009, Suo'ang BST and Hangson entered into a subsequent share transfer agreement with Suoke Clean Energy to transfer 80% of Suo'ang New Energy's equity interests to Suoke Clean Energy and, Mr. Zhou, with Hangson's consent, entered into a share transfer agreement with Suoke Clean Energy to transfer the remaining 20% equity interest of Suo'ang New Energy. On November 12, 2009, Suo'ang New Energy received a new business license from the Tongchuan Administration for Industry and Commerce, which reflected that the acquisition of 100% of the equity of Suo'ang New Energy by Suoke Clean Energy had been completed. As a result we were able, through Suoke Clean Energy, to own 100% of the equity interests of Suo'ang New Energy.

On October 12, 2009, Suo'ang New Energy established a wholly-owned subsidiary to conduct the CWSF business in Shenyang, Liaoning Province. On December 31, 2009, we entered into a series of termination agreements to terminate the contractual arrangements by and among Suoke Clean Energy, Suo'ang BST and certain stockholders of Suo'ang BST. We no longer needed to keep such contractual arrangements in place due to the fact that Suo'ang BST was no longer engaged in any substantial business operations. In connection with the termination agreements, certain assets held by Suo'ang BST, such as office equipment, vehicles, bank deposits, and accounts receivable, were transferred to Suoke Clean Energy. Employees of Suo'ang BST signed new employment contracts with Suoke Clean Energy. All rights and obligations under certain business operation agreements and research and development contracts between Suo'ang BST and third parties were assigned to Suo'ang New Energy. Hangson has had no substantive operations of its own after the transfer and termination of the contractual arrangements.

Effective May 7, 2010, the Company announced a reverse stock split pursuant to which each ten shares of Company's common stock then issued and outstanding was automatically converted into one share of the Company's common stock. All share and per share amounts in the accompanying condensed consolidated financial statements have been adjusted to reflect the reverse stock split as if it had occurred at the beginning of the earliest period presented.

In August 2010, the Company acquired all the outstanding capital stock of Dongguan Clean Energy Water Coal Mixture Company ("Dongguan Clean Energy"). At the time, the assets and liabilities of Dongguan Clean Energy consisted primarily of a business license to manufacture and distribute CWSF in Guangdong, which the Company began to use in January 2011.

2.SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation and consolidation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the rules and regulations of the United States Securities and Exchange Commission ("SEC"). Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. The financial statements contained herein should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's 2010 Annual Report on Form 10-K for the fiscal year ended December 31, 2010, filed with the SEC. The results of operations for interim periods are not necessarily indicative of the results expected for a full year or for any future period.

The consolidated financial statements include the financial statements of the Company, its wholly owned subsidiaries Wiscon, Tongchuan Suoke Clean Energy, Shaanxi Suo'ang New Energy, Shenyang Suo'ang New Energy and Dongguan Clean Energy Water Coal Mixture Company. Intercompany accounts and transactions have been eliminated in consolidation.

Use of estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Because of the use of estimates inherent in the financial reporting process, actual results could differ from those estimates. Those estimates and assumptions include estimates for allowance for doubtful accounts, inventory valuation, impairment consideration, and assumptions used in the valuation of derivative liabilities.

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Revenue recognition

Revenues of the Company are from sales of CWSF.

Sales are recognized when the following four revenue criteria are met: persuasive evidence of an arrangement exists, delivery has occurred, the selling price is fixed or determinable, and collectability is reasonably assured. Revenues are presented net of value added tax (“VAT”). In our revenue arrangements, physical delivery is the point in time when customer acceptance occurs since title and risk of loss are transferred to the customer. No return allowance is made as products are not returnable upon acceptance by the customers.

Cost of goods sold

Expenses which comprise cost of goods sold are the direct cost of raw materials (coal, ferrous sulfate, and coal water mixture chemicals), the costs incurred to get the raw materials to our production plants, salaries of production workers, electricity use for production equipment, water used for production, and manufacturing overhead. Manufacturing overhead includes materials, depreciation and amortization related to property, plant, and equipment used directly in production of inventory, rent related to plants used directly in the production of inventory, and other such costs associated with preparing our CWSF for sale. For the three month period ended September 30, 2011 and 2010, cost of goods sold was $11,415,576 and $15,269,720 respectively. For the nine month period ended September 30, 2011 and 2010, cost of goods sold was $47,575,971, and $44,448,913 respectively.

The transportation costs of shipping CWSF to our customers of $803,836 and $1,262,115 for the three month period ended September 30, 2011and 2010 respectively and $3,575,422 and $3,511,414 for the nine month period ended September 30, 2011 and 2010 respectively, are included in selling expenses on the condensed consolidated statements of income and other comprehensive income.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and bank deposits. For financial reporting purposes, the Company considers all highly liquid investments purchased with original maturity of three months or less to be cash equivalents.

Accounts receivable

Accounts receivable are recognized and carried at the original invoiced amount less an allowance for any uncollectible accounts. The Company uses the aging method to estimate the valuation allowance for anticipated uncollectible receivable balances. Under the aging method, bad debts determined by management are based on historical experience as well as the current economic climate and are applied to customers’ balances categorized by the number of months the underlying invoices have remained outstanding. The valuation allowance balance is adjusted to the amount computed as a result of the aging method. When facts subsequently become available to indicate that an adjustment to the bad debt allowance should be made, this is recorded as a change in estimate in the current year. As of September 30, 2011, the allowance for doubtful accounts was $1,083,006. As of December 31, 2010 there was no allowance for doubtful accounts.

Inventories

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

Property, plant and equipment

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

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

Buildings	20 years
Plant and machinery	10 years to 13 years
Office equipment	5 years
Vehicles	3 years

Land use rights

According to the law of China, the government owns all the land in China. Companies or individuals are authorized to possess and use the land only through land use rights granted by the Chinese government. Land use rights are amortized using the straight-line method over the related lease terms of 50 years.

Goodwill

The Company accounts for acquisition of business in accordance with guidance issued by the Financial Accounting Standards Board ("FASB"). Goodwill is not amortized; rather, goodwill is assessed for impairment at least annually. The Company tests goodwill by using a two-step process. In the first step, the fair value of the reporting unit is compared with the carrying amount of the reporting unit, including goodwill. If the carrying amount of the reporting unit exceeds its fair value, goodwill is considered impaired and a second step is performed to measure the amount of impairment loss, if any. Based on management's assessment, there were no indicators of impairment of recorded goodwill at September 30, 2011.

Long-lived Assets

The Company reviews and evaluates its long-lived assets for impairment when events or changes in circumstances indicate that the related carrying amounts may not be recoverable. Impairment is considered to exist if the total estimated future cash flows on an undiscounted basis are less than the carrying amount of the assets, including goodwill, if any. An impairment loss is measured and recorded based on discounted estimated future cash flows. In estimating future cash flows, assets are grouped at the lowest levels for which there are identifiable cash flows that are largely independent of future cash flows from other asset groups.

Based upon management's assessment, there were no indicators of impairment of the Company's long lived assets as of September 30, 2011 or 2010.

Comprehensive income

Under authoritative guidance of the FASB on reporting comprehensive income, disclosure of all components of comprehensive income and loss on an annual and interim basis is required. Comprehensive income is defined to include all changes in equity except those resulting from investments by owners and distributions to owners. For the nine months ended September 30, 2011 and 2010, the Company had other comprehensive income of $2,456,619 and

$348,965, respectively, from foreign currency translation adjustments. For the three months ended September 30, 2011 and 2010, the Company had other comprehensive income of $294,399 and $67,493, respectively, from foreign currency translation adjustments.

Fair value of financial instruments

Fair value measurements are determined using authoritative guidance issued by the FASB, with the exception of the application of the guidance to non-recurring, non-financial assets and liabilities as permitted. Fair value is defined in the authoritative guidance as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. A fair value hierarchy was established, which prioritizes the inputs used in measuring fair value into three broad levels as follows:

Level 1—Quoted prices in active markets for identical assets or liabilities.

Level 2—Inputs, other than the quoted prices in active markets, are observable either directly or indirectly.

Level 3—Unobservable inputs based on the Company's assumptions.

The Company is required to use observable market data if available without undue cost and effort.

The following table presents certain investments and liabilities of the Company's financial assets measured and recorded at fair value on the Company's consolidated balance sheets on a recurring basis and their level within the fair value hierarchy as of September 30, 2011 and December 31, 2010:

	September 30, 2011 (unaudited)			
	Level 1	Level 2	Level 3	Total
Fair value of warrants	$-	$-	$659,949	$659,949

	December 31, 2010			
	Level 1	Level 2	Level 3	Total
Fair value of warrants	$-	$-	$14,555,027	$14,555,027

The changes in level 3 liabilities measured at fair value on a recurring basis are summarized as follows:

	Fair Value of Warrants
Balance at January 1, 2011	$ 14,555,027
Gain on extinguishment of derivatives for the nine month period ended September 30, 2011 on conversion and expiration of 672,935 warrants	(3,590,721)
Fair value adjustment for the nine month period ended September 30, 2011	(10,304,357)
Balance at September 30, 2011	$ 659,949

Derivative financial instruments

The Company evaluates all of its financial instruments to determine if such instruments are derivatives or contain features that qualify as embedded derivatives. For derivative financial instruments that are accounted for as liabilities, the derivative instrument is initially recorded at its fair value and is then re-valued at each reporting date, with changes in the fair value reported in the consolidated statements of operations. For stock-based derivative financial instruments, the Company uses a Monte-Carlo Simulation of Black-Scholers-Merton option pricing model to value the derivative instruments at inception and on subsequent valuation dates. The classification of derivative instruments, including whether such instruments should be recorded as liabilities or as equity, is evaluated at the end of each reporting period. Derivative instrument liabilities are classified in the balance sheet as current or non-current based on whether net-cash settlement of the derivative instrument could be required within 12 months of the balance sheet date.

Stock based compensation

The Company periodically issues stock options and warrants to employees and non-employees in non-capital raising transactions for services and for financing costs. The Company accounts for stock option and warrant grants issued and vesting to employees based on the authoritative guidance provided by the Financial Accounting Standards Board, whereas the value of the award is measured on the date of grant and recognized over the vesting period. The Company accounts for stock option and warrant grants issued and vesting to non-employees in accordance with the authoritative guidance of the Financial Accounting Standards Board, whereas the value of the stock compensation is based upon the measurement date as determined at either a) the date at which a performance commitment is reached, or b) at the date at which the necessary performance to earn the equity instruments is complete. Non-employee stock-based compensation charges generally are amortized over the vesting period on a straight-line basis. In certain circumstances where there are no future performance requirements by the non-employee, option grants are immediately vested and the total stock-based compensation charge is recorded in the period of the measurement date.

The fair value of the Company’s common stock option grant is estimated using the Black-Scholes-Merton option pricing model, which uses certain assumptions related to risk-free interest rates, expected volatility, expected life of the common stock options, and future dividends. Compensation expense is recorded based upon the value derived from the Black-Scholes-Merton option pricing model, and based on actual experience. The assumptions used in the Black-Scholes-Merton option pricing model could materially affect compensation expense recorded in future periods.

Income (loss) per common share

Basic earnings (loss) per share is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding during the period. The diluted earnings (loss) per share calculation give effect to all potentially dilutive common shares outstanding during the period using the treasury stock method for warrants and options. As of September 30, 2011, common stock equivalents were composed of warrants convertible into 2,476,647 shares of the Company’s common stock and options convertible into 165,000 shares of the Company’s common stock. For the three and nine month periods ended September 30, 2011, common stock equivalents have been excluded from the calculation of earnings per share as their effect is anti-dilutive.

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Net income	$3,268,669	$5,611,437	$28,066,201	$35,012,727
Denominator				
Weighted average shares outstanding-basic	23,499,604	16,703,844	23,482,939	15,385,062
Effect of dilutive instruments:				
Warrants and options	-	2,076,693	-	3,283,794
Weighted average shares outstanding-diluted	23,499,604	18,780,537	23,482,939	18,668,856

Foreign currency translation

The accompanying consolidated financial statements are presented in United States dollars. The functional currency of the Company is the Renminbi (“RMB”). Capital accounts of the consolidated financial statements are translated into United States dollars from RMB at their historical exchange rates when the capital transactions occurred. Assets and liabilities are translated at the exchange rate as of the balance sheet date. Income and expenditures are translated at the average exchange rate for the period presented.

	September 30, 2011	December 31, 2010	September 30, 2010
Period end RMB : US$ exchange rate	6.3830	6.6000	6.7011
Average period end RMB : US$ exchange rate	6.4859	6.7690	6.8042

The Renminbi ("RMB") is the functional currency of Tongchuan Suoke Clean Energy, Shaanxi Suo'ang New Energy and Shenyang Suo'ang New Energy (the "Operating Subsidiaries") as it is the currency of the Peoples Republic of China, which is the primary economic environment the Operating Subsidiaries operate in and the environment in which the Company primarily generates and expends cash. The strike price of the Company's options and warrants is denominated in US dollars, a currency other than the Company's functional currency, the RMB.

RMB is not freely convertible into foreign currency and all foreign exchange transactions must take place through authorized institutions. No representation is made that the RMB amounts could have been, or could be, converted into US dollars at the rates used in translation.

Income taxes

The Company uses an asset and liability approach for financial accounting and reporting for income taxes that allows recognition and measurement of deferred tax assets based upon the likelihood of realization of tax benefits in future years. Under the asset and liability approach, deferred taxes are provided for the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. A valuation allowance is provided for deferred tax assets if it is more likely than not these items will either expire before the Company is able to realize their benefits, or that future deductibility is uncertain. The Company's policy is to recognize interest and/or penalties related to income tax matters in income tax expense.

Research and development

Research and development costs are expensed as incurred. For the nine months ended September 30, 2011 and 2010, there were $0 and $146,968 research and development expenses recorded and are included in the general and administrative expenses in the accompanying condensed consolidated statements of income and other comprehensive income.

Concentrations

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of cash and unsecured trade accounts receivable.

Cash denominated in RMB with a US dollar equivalent of $58,925,232 and $23,096,032 at September 30, 2011 and December 31, 2010, respectively, was held in accounts at financial institutions located in the PRC. In addition, the Company maintains funds in bank accounts in the US which at times may exceed the federally insured balance of $250,000. The Company and its subsidiaries have not experienced any losses in such accounts and do not believe the cash is exposed to any significant risk.

For the nine months ended September 30, 2011, one customer, Shenyang Haizhong Heat Resource, Ltd., ("Haizhong Heating") accounted for 19% of sales and 10% of accounts receivable. At September 30, 2011 another customer, Xin Xing Industry Group, accounted for 15% of sales and 34% of accounts receivable. For the nine months ended September 30, 2010, Haizhong Heating accounted for 37% of sales and 25% of accounts receivable. For the nine months ended September 30, 2011 and 2010, there were no other customers who accounted for 10% or more of sales or accounts receivable.

For the nine months ended September 30, 2011,four vendors accounted for 90% of the Company's total purchases (35%, 26%, 15% and 15% respectively), and accounted for 97% of prepaid coal (40%, 26%, 19% and 12% respectively). At September 30, 2011, one vendor accounted for 39% of account payable and accrued expenses.. At December 31, 2010, three vendors accounted for 90% of prepaid coal (36%, 32% and 22% respectively). For the nine months ended September 30, 2010, three vendors accounted for 84% of total purchases (32%, 27% and 25% respectively). At September 30, 2010, one vendor accounted for 13% of accounts payable and accrued expenses and three vendors accounted for 97% of prepaid coal (38%, 32% and 27% respectively).

Economic and Political Risks

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

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

Recently issued accounting pronouncements

In May 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update (ASU) No. 2011-04, "Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs". ASU No. 2011-4 does not require additional fair value measurements and is not intended to establish valuation standards or affect valuation practices outside of financial reporting. The ASU is effective for interim and annual periods beginning after December 15, 2011. The Company will adopt the ASU as required. The ASU will affect the Company's fair value disclosures, but will not affect the Company's results of operations, financial condition or liquidity.

In June 2011, the FASB issued ASU No. 2011-05, "Presentation of Comprehensive Income". The ASU eliminates the option to present the components of other comprehensive income as part of the statement of changes in shareholders' equity, and instead requires consecutive presentation of the statement of net income and other comprehensive income either in a continuous statement of comprehensive income or in two separate but consecutive statements. ASU No. 2011-5 is effective for interim and annual periods beginning after December 15, 2011. The Company will adopt the ASU as required. It will have no affect on the Company's results of operations, financial condition or liquidity.

In September 2011, the FASB issued ASU 2011-08, "Testing Goodwill for Impairment", an update to existing guidance on the assessment of goodwill impairment. This update simplifies the assessment of goodwill for impairment by allowing companies to consider qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount before performing the two step impairment review process. It also amends the examples of events or circumstances that would be considered in a goodwill impairment evaluation. The amendments are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted. The Company is currently evaluating the affects adoption of ASU 2011-08 may have on its goodwill impairment testing.

Other recent accounting pronouncements issued by the FASB (including its Emerging Issues Task Force), the AICPA, and the Securities Exchange Commission (the "SEC") did not or are not believed by management to have a material impact on the Company's present or future consolidated financial statements.

3. INVENTORIES

		September 30, 2011 (unaudited)		December 31, 2010
Inventories consist of the following :				
Raw materials	$	1,351,364	$	858,887
Finished goods		807,348		402,447
	$	2,158,712	$	1,261,334

Prepaid Inventories

The Company has contracts with coal mines to deliver coal for use in the production of CWSF. At times, the Company makes payments in advance of delivery and accounts for these prepayments as prepaid inventory. At September 30, 2011, December 31, 2010 and September 30, 2010, prepaid inventories totaled $14,547,285, $10,242,878 and $5,644,695, respectively.

4. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consist of the following at September 30, 2011 and December 31, 2010:

	September 30, 2011 (unaudited)	December 31, 2010
Buildings	$5,186,624	$3,016,094
Plant and machinery	19,804,698	14,493,705
Office equipment	86,139	80,880
Vehicles	206,597	153,138
	25,284,058	17,743,817
Less: Accumulated depreciation and amortization	(6,460,548)	(4,133,885)
	$18,823,510	$13,609,932

At September 30, 2011, the Company had made a deposit of $3,266,489 (RMB 20,850,000) on a 750,000 ton production line that will be installed in Guangdong during the fourth quarter of 2011 at a total cost of approximately $10.6 million plus approximately $3.0 million for construction costs related to the production line. Also at September 30, 2011, the Company had made a deposit of $2,995,723 (RMB 19,121,700) for construction of office building, road formation and warehouse facility at the production plant of Tongchuan that is expected to be completed in the early 2012 at total cost of $3,791,000(RMB24,000,000).

At December 31, 2010, the Company had made deposits for land use rights, plant and equipment totaling $9,409,091 (RMB 62,100,000) for its new facility in Dongguan, Guangdong province. The deposits were reclassified to land use rights, plant and equipment when the Guangdong facility was completed in January 2011.

For the nine months ended September 30, 2011 and 2010, depreciation expense was $2,221,025 and $1,564,103, respectively.

5. MORTGAGE PAYABLE

In January 2010, the Company agreed to purchase office space for approximately $255,000. The Company paid a deposit of approximately $90,000 and the balance was financed by a mortgage in the amount of approximately $165,000. The mortgage term commenced on July 1, 2010, is secured by the office space, and is being amortized over a 20 year term, with a fixed interest rate of 4.46%, with interest payments due of approximately $1,000 per month. Principal payments are due as follows: $5,457 due in 2011, $5,706 due in 2012, $5,965 due in 2013, $6,237 due in 2014, $6,521 due in 2015, and $135,114 thereafter up to 2030 at an average of $9,007 per annum.

6. DERIVATIVE LIABILITY

In June 2008, the FASB issued authoritative guidance on determining whether an instrument (or embedded feature) is indexed to an entity's own stock. Under the authoritative guidance, effective January 1, 2009, instruments which do not have fixed settlement provisions are deemed to be derivative instruments. The strike price of the warrants issued by the Company in connection with certain convertible note offerings made during 2008 and 2009 are exercisable at $1.50 to $2.85 per share, and contain exercise prices that may fluctuate based on the occurrence of future offerings or events. Additionally, the strike price of the warrants is denominated in US dollars, a currency other than the Company's functional currency, the RMB. As a result, theses warrants are not considered indexed to the Company's own stock. The FASB's guidance requires the fair value of these liabilities be re-measured at the end of every reporting period with the change in value reported in the statement of income.

At September 30, 2011 and December 31, 2010, derivative liabilities were made up of the following values as determined by a Monte-Carlo Simulation of Black-Scholers-Merton option pricing model with the following assumptions:

	September 30, 2011 (unaudited)	December 31, 2010
Warrants:		
Risk-free interest rate	0.08% to 0.11%	0.53 %
Expected volatility	107.3% to 135.0%	111.14 %
Expected life (in years)	0.18 years to 1.08 years	1.83 years
Expected dividend yield		
Fair Value:	$ 659,949	$ 14,555,027
Warrants	$ 659,949	$ 14,555,027

The risk-free interest rate was based on rates established by the Federal Reserve Bank, volatility is based on the Company's historical volatility, and the expected life of the warrants was determined by the expiration date of the warrants. The expected dividend yield was based on the fact that the Company has not paid dividends to common shareholders in the past and does not expect to pay dividends to common shareholders in the future.

At December 31, 2010, the Company had recorded a derivative liability of $3,590,721 related to the conversion feature of 672,935 warrants. When the warrants were exercised or expired, the derivative liability was extinguished and a gain on extinguishment of the derivative was recorded. For the nine months ended September 30, 2011 and 2010, change in derivative liability was a gain of $10,304,357 and a loss of $(2,348,479), respectively.

7. COMMON STOCK

During the nine months ended September 30, 2011, the Company issued 388,334 shares of common stock upon exercise of options and warrants for total proceeds of $594,216.

On May 9, 2011, the Board of Directors authorized the repurchase of up to $20 million of the Company's common stock. As of September 30, 2011, the Company had purchased 321,100 shares of common stock for $799,423.

During the nine months ended September 30, 2011, warrants to purchase 54,631 shares of the Company's common stock were exercised on a cashless basis, and pursuant to the warrant agreement, the Company issued 23,097 shares of the Company's common stock.

8. WARRANTS AND OPTIONS

On August 8, 2011, the Company granted to a director an option to purchase 100,000 shares of common stock. The options have an exercise price of $1.52 per share, an expiration date of 6 years from the date of grant, and vested immediately. The Company determined the fair value of the options on the date vested was $130,000 using the Black-Scholes option pricing model with the following assumptions: expected volatility, 124%; risk-free interest rate, 1.4%; expected life of 6 years; and expected dividend yield of 0%. The Company has recorded $130,000 as fair value of the options granted during the nine months ended September 30, 2011.

At September 30, 2011, outstanding warrants and options were as follows:

	Number of Shares under Warrants and Options	Weighted Average Exercise Price
Warrants and options outstanding at January 1, 2011		