

Big Tree Group, Inc.  
Form 10-Q  
August 14, 2013

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Form 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the period ended June 30, 2013

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

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

Commission File No. 0-27845

BIG TREE GROUP, INC.

(Name of registrant as specified in its charter)

Colorado  
(State or other jurisdiction of incorporation or organization)

84-1304106  
(I.R.S. Employer Identification No.)

South Part 1-101, Nanshe Area, Pengnan Industrial Park on North  
Yingbinbei Road  
in Waisha Town of Longhu District in Shantou, Guangdong, China  
(Address of principal executive offices)

515023  
(Zip Code)

(86)-754-8323888  
(Registrant's telephone number, including area code)

not applicable  
(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if

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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 | <input type="checkbox"/> | Accelerated filer         | <input type="checkbox"/>            |
| Non-accelerated filer   | <input type="checkbox"/> | Smaller reporting company | <input checked="" type="checkbox"/> |

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the most practicable date: 10,350,192 shares of common stock are issued and outstanding as of August 14, 2013.

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BIG TREE GROUP INC AND SUBSIDIARIES  
FORM 10-Q  
June 30, 2013

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We used in this report, the terms "Big Tree," "we," "our," and "us" or the "Company" refers to Big Tree Group, Inc., a Colorado corporation and its wholly-owned subsidiaries Big Tree International Co., Ltd., a Brunei company, ("BT Brunei") and Shantou Big Tree Toys Co., Ltd., a Chinese company ("BT Shantou").

## CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

This report includes forward-looking statements that relate to future events or our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to differ materially from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Words such as, but not limited to, “believe,” “expect,” “anticipate,” “estimate,” “intend,” “plan,” “targets,” “likely,” “aim,” “will,” “would,” “could,” and similar expressions identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and future events and financial trends that we believe may affect our financial condition, results of operation, business strategy and financial needs. Forward-looking statements include, but are not limited to, statements about:

- The circumstances resulting in the restatement of our financial statements and the material weaknesses in our internal control over financial reporting and in our disclosure controls and procedures;
- Transactions with our related parties which may have resulted in violations of the Sarbanes-Oxley Act of 2002;
- Fluctuations in our revenues based upon our revenue recognition policy;
- Factors affecting consumer preferences and customer acceptance of new products;
- Competition in the toy industry;
- Loss of one or more key customers;
- Dependence on third-party contract manufacturers;
- Dependence on certain key personnel;
- Inability to manage our business expansion;
- Infringement by third parties on our intellectual property rights;
- Our inadvertent infringement of third-party intellectual property rights;
- Availability of skilled and unskilled labor and increasing labor costs;
- Lack of insurance coverage and the impact of any loss resulting from product liability or third party liability claims or casualty losses;
- Violation of Foreign Corrupt Practices Act or China anti-corruption laws;
- Economic, legal restrictions and business conditions in China;
- Limited public market for our common stock; and
- Potential conflicts of interest between our controlling shareholders and our shareholders.

You should read thoroughly this report and the documents that we refer to herein with the understanding that our actual future results may be materially different from and/or worse than what we expect. We qualify all of our forward-looking statements by these cautionary statements including those made in Item 1A. Risk Factors of our Annual Report on Form 10-K for the year ended December 31, 2012 as filed with the Securities and Exchange Commission. Other sections of this report include additional factors which could adversely impact our business and financial performance. Moreover, we operate in an evolving environment. New risk factors emerge from time to time and it is not possible for our management to predict all risk factors, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. Except for our ongoing obligations to disclose material information under the Federal securities laws, we undertake no obligation to release publicly any revisions to any

forward-looking statements, to report events or to report the occurrence of unanticipated events. These forward-looking statements speak only as of the date of this report, and you should not rely on these statements without also considering the risks and uncertainties associated with these statements and our business.

## Item 1. Financial Statements

BIG TREE GROUP INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS

|   | June 30,<br>2013<br>(Unaudited) | December<br>31,<br>2012 |
|---|---------------------------------|-------------------------|
| <b>ASSETS</b>   |                                 |                         |
| <b>CURRENT ASSETS:</b>  |                                 |                         |
| Cash  | \$ 30,974                       | \$ 22,167               |
| Accounts receivable, net of allowance of \$58,619 and \$54,135, respectively            | 9,589,606                       | 4,554,077               |
| Inventories   | 1,919,869                       | 1,327,342               |
| Other receivables   | 834,835                         | 1,202,750               |
| Prepaid expenses  | 254,418                         | 171,629                 |
| Advance to suppliers - related parties  | 476,745                         | 529,148                 |
| Advance to suppliers  | 7,207                           | 574,219                 |
| Total Current Assets  | 13,113,654                      | 8,381,332               |
| Security deposit - related party  | 58,317                          | 57,133                  |
| Property and equipment, net   | 170,180                         | 201,757                 |
| Intangible assets, net  | 9,241                           | 10,592                  |
| Total Assets  | \$ 13,351,392                   | \$ 8,650,814            |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>   |                                 |                         |
| <b>CURRENT LIABILITIES:</b>   |                                 |                         |
| Accounts payable and accrued expenses   | \$ 6,651,811                    | \$ 2,003,390            |
| Loan payable  | 3,725,782                       | 3,650,156               |
| Loans payable- related party  | 80,000                          | -                       |
| Advance from customers  | 171,825                         | 142,125                 |
| Salaries payable  | 68,134                          | 60,578                  |
| Other payables  | 13,292                          | 50,926                  |
| Taxes payable   | -                               | 65,586                  |
| Due to related parties  | 1,084,226                       | 10,578                  |
| Total Current Liabilities   | 11,795,070                      | 5,983,339               |
| Loans payable- related party - long term  | -                               | 61,711                  |
| Total Liabilities   | 11,795,070                      | 6,045,050               |
| <b>SHAREHOLDERS' EQUITY:</b>  |                                 |                         |
| Preferred stock No par value; 20,000,000 shares authorized; none issued and outstanding | -                               | -                       |
|   | 104                             | 102                     |

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|   |               |              |
|---|---------------|--------------|
| Common stock \$0.00001 par value; 100,000,000 shares authorized; 10,350,192 and 10,200,179 shares issued and outstanding at June 30, 2013 and December 31, 2012, respectively |               |              |
| Additional paid-in capital  | 302,399       | 207,900      |
| Retained earnings   | 3,061,883     | 2,663,029    |
| Accumulated other comprehensive income (loss)   | 67,633        | (3,297 )     |
| Due from related party  | (1,875,697 )  | (261,970 )   |
| Total Shareholders' Equity  | 1,556,322     | 2,605,764    |
| Total Liabilities and Shareholders' Equity  | \$ 13,351,392 | \$ 8,650,814 |

See accompanying notes to unaudited consolidated financial statements.

**BIG TREE GROUP INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME**  
(Unaudited)

|  | For the Three Months<br>Ended<br>June 30, |                          | For the Six Months Ended<br>June 30, |                          |
|--|---|--------------------------|--------------------------------------|--------------------------|
|  | 2013                                      | 2012<br>(As<br>Restated) | 2013                                 | 2012<br>(As<br>Restated) |
| Revenues   | \$ 11,863,274                             | \$ 5,960,742             | \$ 19,310,975                        | \$ 10,712,827            |
| Cost of revenues                                       | 10,974,138                                | 5,154,695                | 17,727,189                           | 9,385,758                |
| Gross profit   | 889,136                                   | 806,047                  | 1,583,786                            | 1,327,069                |
| <b>OPERATING EXPENSES:</b>                             |   |                          |                                      |                          |
| Selling expenses                                       | 168,083                                   | 130,774                  | 271,998                              | 258,263                  |
| General and administrative                             | 285,251                                   | 173,937                  | 727,930                              | 353,405                  |
| Total operating expenses                               | 453,334                                   | 304,711                  | 999,928                              | 611,668                  |
| Operating income                                       | 435,802                                   | 501,336                  | 583,858                              | 715,401                  |
| <b>OTHER INCOME (EXPENSES):</b>                        |   |                          |                                      |                          |
| Other income (expenses)                                | (36,586 )                                 | 17,499                   | (55,528 )                            | 31,688                   |
| Interest (expense) income, net                         | (65,743 )                                 | (345 )                   | (129,476 )                           | (211 )                   |
| Total other income (expenses)                          | (102,329 )                                | 17,154                   | (185,004 )                           | 31,477                   |
| Income before income taxes                             | 333,473                                   | 518,490                  | 398,854                              | 746,878                  |
| Income taxes   | -   | -                        | -                                    | -                        |
| Net income   | \$ 333,473                                | \$ 518,490               | \$ 398,854                           | \$ 746,878               |
| <b>COMPREHENSIVE INCOME:</b>                           |   |                          |                                      |                          |
| Net income   | \$ 333,473                                | \$ 518,490               | \$ 398,854                           | \$ 746,878               |
| Foreign currency translation income                    | 53,392                                    | 395                      | 70,930                               | 29,113                   |
| COMPREHENSIVE INCOME                                   | \$ 386,865                                | \$ 518,885               | \$ 469,784                           | \$ 775,991               |
| <b>NET INCOME PER COMMON SHARE</b>                     |   |                          |                                      |                          |
| Basic  | \$0.03                                    | \$0.05                   | \$0.04                               | \$0.07                   |
| Diluted  | \$0.03                                    | \$0.05                   | \$0.04                               | \$0.07                   |
| <b>WEIGHTED AVERAGE COMMON SHARES<br/>OUTSTANDING:</b> |   |                          |                                      |                          |
| Basic  | 10,350,192                                | 10,000,179               | 10,347,699                           | 10,000,179               |
| Diluted  | 10,350,192                                | 10,000,179               | 10,347,699                           | 10,000,179               |

See accompanying notes to unaudited consolidated financial statements.





**BIG TREE GROUP INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)

|   | For the Six Months Ended<br>June 30, |                          |
|---|--------------------------------------|--------------------------|
|   | 2013                                 | 2012<br>(As<br>Restated) |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |                                      |                          |
| Net income  | \$ 398,854                           | \$ 746,878               |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: |                                      |                          |
| Depreciation and amortization   | 39,606                               | 23,022                   |
| Stock-based compensation  | 94,501                               | -                        |
| Bad debt expense  | 3,327                                | -                        |
| Changes in operating assets and liabilities:  |                                      |                          |
| Accounts receivable   | (4,891,997)                          | (1,825,705)              |
| Advance to suppliers  | 572,757                              | 44,791                   |
| Advance to suppliers-related parties  | 62,693                               | 67,121                   |
| Prepaid expenses and other current assets   | 310,242                              | (375,678 )               |
| Inventories   | (559,022 )                           | (1,414,875)              |
| Accounts payable and accrued expenses   | 4,566,069                            | 1,280,769                |
| Due to related party  | -                                    | 1,617,578                |
| Other payables  | (36,664 )                            | 139,568                  |
| Taxes payable   | (66,234 )                            | 1,931                    |
| Advance from customers  | 26,472                               | (329,571 )               |
| Net cash provided by (used in) operating activities   | 520,605                              | (24,171 )                |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |                                      |                          |
| Purchase of property and equipment  | (2,675 )                             | (111,041 )               |
| Net cash used in investing activities   | (2,675 )                             | (111,041 )               |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>  |                                      |                          |
| Proceeds from related party advances  | 1,390,844                            | 518,497                  |
| Repayment of related parties advances   | (327,593 )                           | -                        |
| Due from related party  | (1,591,210)                          | -                        |
| Proceeds from loans payable   | 18,290                               | -                        |
| Net cash (used in) provided by financing activities   | (509,669 )                           | 518,497                  |
| Effect of exchange rate on cash   | 546                                  | 23,983                   |
| Net increase in cash  | 8,807                                | 407,268                  |

|  |           |           |
|--|-----------|-----------|
| Cash - beginning of period                               | 22,167    | 246,720   |
| Cash - end of period                                     | \$30,974  | \$653,988 |
| <b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b> |           |           |
| Cash paid for income taxes                               | \$71,533  | \$11,334  |
| Cash paid for interest                                   | \$129,968 | \$-       |

See accompanying notes to unaudited consolidated financial statements.

BIG TREE GROUP, INC. AND SUBSIDIARIES  
Notes to Unaudited Consolidated Financial Statements  
June 30, 2013

NOTE 1 – ORGANIZATION AND OPERATIONS

The Company

Big Tree Group, Inc. (formerly Transax International Limited) (“we”, “us”, “our,” or the “Company”) was incorporated in the State of Colorado in 1987. Prior to December 2011, the Company, through its subsidiary, Medlink Conectividade em Saude Ltda (“MedlinkConectividade”) was an international provider of information network solutions specifically designed for healthcare providers and health insurance companies. On April 4, 2011, pursuant to a Quota Purchase and Sale Agreement amongst Transax Limited, QC Holding I Participacoes S.A., a corporation organized under the laws of Brazil (“QC Holding”), and MedlinkConectividade, the Company sold 100% of its interest in MedlinkConectividade to QC Holding. From April 4, 2011 until December 30, 2011, we had nominal assets, no revenues and limited operations consisting of financial reporting, general administration, and seeking new business opportunities with a merger candidate.

On December 30, 2011, the Company entered into a Share Exchange Agreement (the “Share Exchange Agreement”) with Big Tree International Co., Ltd., a Brunei company (“BT Brunei”) and its shareholder, Lins (HK) International Trading Limited (“BT Hong Kong”). Under the Share Exchange Agreement, we exchanged 6,500,000 shares of our Series C Convertible Preferred Stock (the “Series C Preferred Stock”) to acquire 100% of the issued and outstanding shares of BT Brunei from its sole shareholder BT Hong Kong. Each share of the Series C Preferred Stock was convertible into one share of our common stock after giving effect to a pending 1 for 700 reverse stock split (the “Reverse Stock Split”) and represented approximately 65% of the issued and outstanding shares of our common stock, and is hereinafter referred to as the “Exchange”. On December 30, 2011, BT Hong Kong became a shareholder of the Company. The Share Exchange Agreement was approved by our Board of Directors on December 30, 2011 and no approval of our shareholders was necessary under Colorado law. The transaction was accounted for as a reverse merger and recapitalization of BT Brunei whereby BT Brunei is considered the acquirer for accounting purposes and the 6,500,000 shares of our Series C Preferred Stock were accounted for as paid in capital of our company. As a result of the consummation of the Share Exchange, BT Brunei and its subsidiary, Shantou Big Tree Toys Co., Ltd., a Chinese company (“BT Shantou”), are now our wholly-owned subsidiaries. Accordingly, the historical financial statements are those of BT Brunei and BT Shantou upon the consummation of the Share Exchange transaction on December 30, 2011. Management of BT Brunei and BT Shantou has assumed operational, management and governance control immediately following the reverse merger transaction.

After the acquisition of BT Brunei, we are in the business of toys sourcing, distribution and contractual manufacturing targeting international and domestic distributors and customers in the toys industry. Our main business focus is to function as a “one stop shop” for the sourcing, distribution and specialty manufacturing of toys and related products. The Company conducts these operations through both BT Brunei and our BT Shantou subsidiary. We are located in Shantou City of Guangdong province, the geographical region well-known for toys manufacturing and exporting in China. We are not a manufacturer. We provide procurement services for international toy distributors and wholesalers, including identifying, evaluating, and engaging one or more local manufacturers, trading companies or distributors for the requested supply of toys, as well as original equipment manufacturing (“OEM”) services. The OEM services include engaging toy manufacturers directly or through other toy trading companies or distributors to either manufacture toys to specific specifications requested by our customers, or customize an existing toy product to meet our customer’s request such as through changes in mechanical functionality, appearance, physical dimension, and materials. We sources a wide variety of toys made of plastic, wood, metal, wool, and electronic materials, primarily targeting children from infants to teenagers. We enable our customers to view these toys either through our website or

at our extensive toy showrooms located in Shantou, China. Customers can easily contact our online representatives for inquiry and place orders, or visit the toy showrooms and choose from the displayed toy samples provided by our manufacturing partners.

In 2009, BT Shantou developed a proprietary construction toy consisting of plastic pieces that can plug-in together to make a wide variety of objects. We registered the patents for its utility model and design in Hong Kong and mainland China during 2010 and 2011. On June 1, 2010, BT Shantou entered into a 10-year contract manufacturing agreement with Shantou Xinzhongyang Toy Industrial Co., Ltd. (“Xinzhongyang”), a related party, to produce this proprietary toy under the name of Big Tree Educational Magic Puzzle (the “Big Tree Magic Puzzle”).

#### Basis of presentation

The accompanying unaudited consolidated financial statements for the three and six month periods ended June 30, 2013 and 2012 have been prepared in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim financial reporting and pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). The consolidated unaudited financial statements for the interim periods presented are unaudited and reflect all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the periods presented. Financial results for interim periods are not necessarily indicative of results that should be expected for the full year. The accompanying unaudited consolidated financial statements reflect the consolidated financial position and result of operations of the Company and our subsidiaries, BT Brunei and BT Shantou. All significant intercompany accounts and transactions have been eliminated in consolidation.

BIG TREE GROUP, INC. AND SUBSIDIARIES  
 Notes to Unaudited Consolidated Financial Statements  
 June 30, 2013

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Foreign Currency Translation

The reporting currency of the Company is the U.S. dollar. Our functional currency is the Chinese Renminbi (“RMB”). In accordance with Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) Section 830-20-35, the unaudited consolidated financial statements were translated into United States dollars using balance sheet date rates of exchange for assets and liabilities, and average rates of exchange for the period for the income statements. Net gains and losses resulting from foreign exchange transactions were included in the unaudited consolidated statements of operations and comprehensive income. Translation adjustments resulting from the process of translating the local currency financial statements into U.S. dollars are included in other comprehensive income or loss within the shareholders’ equity.

RMB is not a fully convertible currency. All foreign exchange transactions involving RMB must take place either through the People’s Bank of China (the “PBOC”) or other institutions authorized to buy and sell foreign exchange. The exchange rate adopted for the foreign exchange transactions are the rates of exchange quoted by the PBOC, which are determined largely by supply and demand. Translation of amounts from RMB into United States dollars (“\$”) was made at the following exchange rates for the respective periods:

|  |                      |
|--|----------------------|
| Balance sheet:   |                      |
| As of June 30, 2013  | RMB 6.1732 to \$1.00 |
| As of December 31, 2012  | RMB 6.3011 to \$1.00 |
| Statement of operations and comprehensive income and cash flows: |                      |
| Six months ended June 30, 2013                                   | RMB 6.2395 to \$1.00 |
| Six months ended June 30, 2012                                   | RMB 6.3027 to \$1.00 |

Cash flows from the Company's operations are calculated based upon the local currencies using the average translation rate. As a result, amounts related to assets and liabilities reported on the statement of cash flows will not necessarily agree with changes in the corresponding balances on the balance sheets.

Use of estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates for the three and six month periods ended June 30, 2013 and 2012 include the allowance for doubtful accounts on accounts receivable, allowance for obsolete inventory, the useful life of property and equipment and intangible assets, and the valuation of stock-based compensation.

Fair value of financial instruments

We adopted the guidance of ASC 820 for fair value measurements which clarifies the definition of fair value, prescribes methods for measuring fair value, and establishes a fair value hierarchy to classify the inputs used in measuring fair value as follows:

Level 1-Inputs are unadjusted quoted prices in active markets for identical assets or liabilities available at the measurement date.

Level 2-Inputs are quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, inputs other than quoted prices that are observable, and inputs derived from or corroborated by observable market data.

Level 3-Inputs are unobservable inputs which reflect the reporting entity's own assumptions on what assumptions the market participants would use in pricing the asset or liability based on the best available information.

The carrying amounts reported in the balance sheets for cash, accounts receivable, accounts payable and accrued expenses, and loans payable approximate their fair market value based on the short-term maturity of these instruments. We did not identify any assets or liabilities that are required to be presented on the balance sheets at fair value in accordance with the accounting guidance.

BIG TREE GROUP, INC. AND SUBSIDIARIES  
Notes to Unaudited Consolidated Financial Statements  
June 30, 2013

ASC 825-10 “Financial Instruments”, allows entities to voluntarily choose to measure certain financial assets and liabilities at fair value (fair value option). The fair value option may be elected on an instrument-by-instrument basis and is irrevocable, unless a new election date occurs. If the fair value option is elected for an instrument, unrealized gains and losses for that instrument should be reported in earnings at each subsequent reporting date. We did not elect to apply the fair value option to any outstanding instruments.

#### Cash and equivalents

For purposes of the consolidated statements of cash flows, we consider all highly liquid instruments purchased with a maturity of three months or less and money market accounts to be cash equivalents. We maintain cash and cash equivalents with various financial institutions mainly in the PRC and Hong Kong. Balances in banks in the PRC and Hong Kong are uninsured.

#### Accounts receivable

Accounts receivable are recorded at the invoiced amount, net of an allowance for doubtful accounts. The allowance for doubtful accounts reflects our best estimate of the amount of probable credit losses in our existing accounts receivable. We determined the allowance based on historical write-off experience, customer specific facts and economic conditions. Bad debt expense is included in general and administrative expense, if any.

Outstanding account balances are reviewed individually for collectability. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

#### Inventories

We value inventories, consisting of finished goods only, at the lower of cost or market value. Cost is determined on the first in-first out method. We regularly review our inventories on hand and, when necessary, record a provision for excess or obsolete inventories based primarily on the current selling price. As of June 30, 2013 and December 31, 2012, there were no charges for inventory reserve provision.

#### Prepaid expenses

Prepaid expenses primarily consist of prepaid advertising expenses and prepaid taxes.

#### Advance to suppliers (related and non-related parties)

Advance to suppliers consist of advance to suppliers for merchandise that had not yet been shipped.

#### Property and equipment

Property and equipment are recorded at cost. Expenditures for major additions and betterments are capitalized. Maintenance and repairs are expensed as incurred. Depreciation of property and equipment is computed by the straight-line method (after taking into account their respective estimated residual values) over the assets estimated useful lives. Upon sale or retirement of property and equipment, the related cost and accumulated



depreciation are removed from the accounts and any gain or loss is reflected in operations. Leasehold improvements, if any, are amortized on a straight-line basis over the lease period or the estimated useful life, whichever is shorter. Upon becoming fully amortized, the related cost and accumulated amortization are removed from the accounts.

#### Impairment of long-lived assets

In accordance with ASC 360, our long-lived assets, which include property and equipment, and automobiles are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. We assess the recoverability of our long-lived assets by comparing the projected undiscounted net cash flows associated with the related long-lived asset or group of long-lived assets over their remaining estimated useful lives against their respective carrying amounts. Impairment, if any, is based on the excess of the carrying amount over the fair value of those assets. Fair value is generally determined using the asset's expected future discounted cash flows or market value, if readily determinable. If long-lived assets are determined to be recoverable, but the newly determined remaining estimated useful lives are shorter than originally estimated, the net book values of the long-lived assets are depreciated over the newly determined remaining estimated useful lives. We determined there were no impairments of long-lived assets as of June 30, 2013 and December 31, 2012.

BIG TREE GROUP, INC. AND SUBSIDIARIES  
Notes to Unaudited Consolidated Financial Statements  
June 30, 2013

## Advance from customers

Advance from customers represent prepayments to us for merchandise that had not yet been shipped to customers.

## Revenue recognition

We follow the guidance of ASC 605, "Revenue Recognition," and the Securities and Exchange Commission's Staff Accounting Bulletin ("SAB") No. 104 and SAB Topic 13 for revenue recognition. Revenues for our product sales are recognized when all four of the following criteria are met: (i) persuasive evidence of an arrangement exists through a formal purchase order or contract; (ii) delivery of the products has occurred and risks and rewards of ownership have passed to the customer; (iii) the selling price is both fixed and determinable based on agreement between us and our customer; and (iv) collectability is reasonably assured. For any advance payments from customers, revenues are deferred until such a time when all the four criteria mentioned above are fully met.

Revenue is accounted for in accordance with the ASC 605-45, reporting revenue either gross as a principal or net as an agent depending upon the nature of the sales transaction. Revenue is recognized on a gross basis when the Company determines the sale meets the conditions of ASC 605-45, "Reporting Revenue Gross as a Principal versus Net as an Agent." When the Company does not meet the criteria for gross revenue recognition under ASC 605-45, the Company reports the revenue on a net basis.

In accordance with ASC 605-45-45, "Principal Considerations - Other Presentation Matters", we report our revenues from sales of toys as follows:

| Allocation of Revenues                          | Revenue Recognition (1)<br>For the three months ended June 30, 2013 |            |               | Revenue Recognition (1)<br>For the three months ended June 30, 2012<br>(as restated) |            |              |
|---|---|------------|---------------|--|------------|--------------|
|   | Gross Method  | Net Method | Total         | Gross Method   | Net Method | Total        |
| Revenues, excluding sales reported on net basis | \$ 11,844,100   | \$ -       | \$ 11,844,100 | \$ 5,584,344   | \$ -       | \$ 5,584,344 |
| Net revenues from sales reported on net basis   | -   | 19,174     | 19,174        | -  | 376,398    | 376,398      |
| Total revenues                                  | \$ 11,844,100   | \$ 19,174  | \$ 11,863,274 | \$ 5,584,344   | \$ 376,398 | \$ 5,960,742 |

| Allocation of Revenues                          | Revenue Recognition (1)<br>For the Six Months Ended June 30, 2013 |            |               | Revenue Recognition (1)<br>For the Six Months Ended June 30, 2012<br>(as restated) |            |               |
|---|---|------------|---------------|--|------------|---------------|
|   | Gross Method  | Net Method | Total         | Gross Method   | Net Method | Total         |
| Revenues, excluding sales reported on net basis | \$ 19,247,073   | \$ -       | \$ 19,247,073 | \$ 10,198,830  | \$ -       | \$ 10,198,830 |
|   | -   | 63,902     | 63,902        | -  | 513,997    | 513,997       |

Net revenues from sales  
reported on net basis

|                |               |           |               |               |            |               |
|----------------|---------------|-----------|---------------|---------------|------------|---------------|
| Total revenues | \$ 19,247,073 | \$ 63,902 | \$ 19,310,975 | \$ 10,198,830 | \$ 513,997 | \$ 10,712,827 |
|----------------|---------------|-----------|---------------|---------------|------------|---------------|

(1) Certain revenues from our sales are based on a net reporting because they do not meet the criteria for gross reporting method pursuant to ASC 605-45-45. This means that all cost of purchases from those sales will be netted with the revenues generated by the sale of those toys. Additionally, handling fees related to sales reported on a net basis are also netted with these revenues. All other revenues from sales are based on gross reporting pursuant to criteria outlined in ASC 605-45-45, as follows:

- we are the primary obligor to provide the product or services desired by our customers;
  - we have discretion in supplier selection.
  - we have latitude in establishing price;
- we have credit risk – see Note 10 for customer concentrations and credit risk; and
- we have inventory risk before customer order and upon customer return;

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BIG TREE GROUP, INC. AND SUBSIDIARIES  
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#### Income taxes

We account for income taxes under ASC 740, “Expenses – Income Taxes”. ASC 740 requires the recognition of deferred tax assets and liabilities for both the expected impact of differences between the financial statements and the tax basis of assets and liabilities, and for the expected future tax benefit to be derived from tax losses and tax credit carry forwards. ASC 740 additionally requires the establishment of a valuation allowance to reflect the likelihood of realization of deferred tax assets.

All of BT Shantou operations are in the PRC and are governed by the Income Tax Law of the People’s Republic of China and local income tax laws (the PRC Income Tax Law”). Pursuant to the PRC Income Tax Law, we are subject to tax at a maximum statutory rate of 25% (inclusive of state and local income taxes).

Big Tree International Co., Ltd. (“BT Brunei”) was incorporated in the State of Brunei Darussalam, and is not subject to any corporate income taxes in accordance to the laws and regulations of that country.

We applied the provisions of ASC 740-10-50, “Accounting for Uncertainty in Income Taxes”, which provides clarification related to the process associated with accounting for uncertain tax positions recognized in our financial statements. Audit periods remain open for review until the statute of limitations has passed. The completion of review or the expiration of the statute of limitations for a given audit period could result in an adjustment to the Company’s liability for income taxes. Any such adjustment could be material to the Company’s results of operations for any given quarterly or annual period based, in part, upon the results of operations for the given period. As of June 30, 2013, we had no uncertain tax positions, and will continue to evaluate for uncertain positions in the future.

#### Value added taxes

Pursuant to the Provisional Regulation of China on Value Added Tax (“VAT”) and their rules, all entities and individuals that are engaged in the sale of goods in China are generally required to pay VAT at a rate of 17.0% of the gross sales proceeds received, less any deductible VAT already paid or borne by the taxpayer. Further, when exporting goods, the exporter is entitled to a portion of or a full refund of the VAT that it has already paid or borne.

#### Shipping costs

For the three months ended June 30, 2013 and 2012, shipping costs are included in selling expenses and totaled \$42,896 and \$19,719, respectively. Shipping costs amounted to \$56,068 and \$36,690 for the six months ended June 30, 2013 and 2012, respectively.

#### Advertising

Advertising is expensed as incurred and is included in selling expenses on the accompanying consolidated statements of operations and comprehensive income. For the three months ended June 30, 2013 and 2012, advertising expense amounted to \$27,326 and \$44,854, respectively. For the six months ended June 30, 2013 and 2012, advertising expense amounted to \$45,800 and \$83,805, respectively.

#### Comprehensive income (loss)

Comprehensive income (loss) consists of net income and foreign currency translation adjustments, and is presented in our Consolidated Statements of Operations and Comprehensive Income (Loss).

Reverse stock split and conversion of preferred shares

We effected a one-for-700 reverse stock split on December 11, 2012. All share and per share information has been retroactively adjusted to reflect this reverse stock split. Additionally, upon the effectiveness of the reverse stock split, all outstanding convertible series B and C shares were automatically converted into common shares.

BIG TREE GROUP, INC. AND SUBSIDIARIES  
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Net income per share of common stock

Basic net income per common share is computed by dividing net income available to common stockholders by the weighted average number of shares of common stock outstanding during the period. Diluted net income per common share is computed by dividing net income by the weighted average number of shares of common stock, common stock equivalents and potentially dilutive securities outstanding during each period. For the three and six months ended June 30, 2012, both basic and diluted weighted-average number of common shares included the 3,362,749 shares of Series B convertible preferred shares issued in connection with the pre-merger transactions and the 6,500,000 shares of Series C convertible preferred shares issued in connection with the Shares Exchange Transaction as if the common shares are issued at the issuance date in connection with the pre-merger transactions and are issued at the earliest period presented or retroactively restated as a result of recapitalization since these convertible preferred shares have automatic conversion feature. These Series B and Series C are deemed converted. As of June 30, 2013 and December 31, 2012, we did not have any common stock equivalents and potentially dilutive common shares.

Recently issued accounting pronouncements

In July 2013, the FASB issued Accounting Standards Update “(ASU)” 2013-11, "Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists" ("ASU 2013-11"). The provisions of the rule require an unrecognized tax benefit to be presented as a reduction to a deferred tax asset in the financial statements for an NOL carryforward, a similar tax loss, or a tax credit carryforward except in circumstances when the carryforward or tax loss is not available at the reporting date under the tax laws of the applicable jurisdiction to settle any additional income taxes or the tax law does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purposes. When those circumstances exist, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. The new financial statement presentation provisions relating to this update are prospective and effective for interim and annual periods beginning after December 15, 2013, with early adoption permitted. The Company does not anticipate a material impact to the consolidated financial statements related to this guidance.

In March 2013, the FASB issued ASU 2013-05 Topic 830 - Foreign Currency Matters (“ASU 2013-05”). ASU 2013-05 resolves the diversity in practice about whether Subtopic 810-10, Consolidation-Overall, or Subtopic 830-30, ASU 2013-05 applies to the release of the cumulative translation adjustment into net income when a parent either sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business within a foreign entity. In addition, the amendments in ASU-2013-05 resolve the diversity in practice for the treatment of business combinations achieved in stages (sometimes referred to as step acquisitions) involving a foreign entity. The amendments in ASU-2013-05 are effective prospectively for fiscal years (and interim reporting periods within those years) beginning after December 15, 2013. The Company does not expect the adoption of ASU-2013-05 to have a material effect on the Company's consolidated financial statements.

In February 2013, the FASB issued ASU No. 2013-02 “Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income” (ASU 2013-02), which is included in ASC Topic 220 (Comprehensive Income). The objective of ASU 2013-02 is to improve the reporting of reclassifications out of accumulated other comprehensive income. The amendments are effective prospectively for reporting periods beginning after December 15, 2012. The adoption of ASU 2013-02 did not have a material impact on the Company’s consolidated financial position, results of

operations or cash flows.

In December 2011, the FASB issued ASU 2011-11, "Balance Sheet (Topic 210)". The objective of this Update is to provide enhanced disclosures that will enable users of its financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position. This includes the effect or potential effect of rights of setoff associated with an entity's recognized assets and recognized liabilities within the scope of this Update. The amendments require enhanced disclosures by requiring improved information about financial instruments and derivative instruments that are either (1) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either Section 210-20-45 or Section 815-10-45. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. The adoption of ASU 2011-11 did not have a material effect on the Company's consolidated financial position, results of operations or cash flows.

BIG TREE GROUP, INC. AND SUBSIDIARIES  
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In July 2012, FASB issued ASU No. 2012-02, Intangibles-Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment. ASU No. 2012-02 simplifies the guidance for testing the decline in the realizable value (impairment) of indefinite-lived intangible assets other than goodwill. ASU No. 2012-02 allows an entity the option of first performing a qualitative assessment to determine whether it is more likely than not that an indefinite-lived intangible asset is impaired. The amendments in this ASU are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted. The adoption of ASU No. 2012-02 did not have a material impact on our consolidated financial position, results of operations or cash flows.

In August 2012, the FASB issued ASU 2012-03, “Technical Amendments and Corrections to SEC Sections: Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin (SAB) No. 114, Technical Amendments Pursuant to SEC Release No. 33-9250, and Corrections Related to FASB Accounting Standards Update 2010-22 (SEC Update)” in Accounting Standards Update No. 2012-03. This update amends various SEC paragraphs pursuant to the issuance of SAB No. 114. The adoption of ASU 2012-03 did not have a material impact on the Company’s consolidated financial position, results of operations or cash flows.

In October 2012, the FASB issued ASU 2012-04, “Technical Corrections and Improvements” in Accounting Standards Update No. 2012-04 (“ASU 2012-04”). The amendments in this update cover a wide range of topics in the Accounting Standards Codification. These amendments include technical corrections and improvements to the Accounting Standards Codification and conforming amendments related to fair value measurements. The amendments in this update will be effective for fiscal periods beginning after December 15, 2012. The adoption of ASU 2012-04 did not have a material impact on the Company’s consolidated financial position, results of operations or cash flows.

A variety of proposed or otherwise potential accounting standards are currently under study by standard setting organizations and various regulatory agencies. Due to the tentative and preliminary nature of those proposed standards, we have not determined whether implementation of such proposed standards would be material to our consolidated financial statements.

NOTE 3 – OTHER RECEIVABLES

Other receivables mainly consists of export tax refund from China's State Administration of Taxation. As a measure to encourage export, the Chinese tax code provides for a tax refund based on the amount and products exported by Chinese corporate taxpayers. The statutory tax refund rate is 15% of cost of goods sold for export sales. Other receivables consist of the following:

|                       | June 30,<br>2013 | December 31,<br>2012 |
|-----------------------|------------------|----------------------|
| Tax refund receivable | \$ 816,338       | \$ 1,189,971         |
| Other                 | 18,497           | 12,779               |
| Total                 | \$ 834,835       | \$ 1,202,750         |

NOTE 4 – PROPERTY AND EQUIPMENT

At June 30, 2013 and December 31, 2012, property and equipment consisted of the following:



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|                                | Estimated<br>Life | June 30,<br>2013 | December 31,<br>2012 |
|--------------------------------|-------------------|------------------|----------------------|
| Office equipment               | 5 Years           | \$ 31,515        | \$ 34,639            |
| Vehicles                       | 5 Years           | 81,575           | 79,920               |
| Machinery and equipment        | 3 Years           | 174,282          | 170,743              |
|                                |                   | 287,372          | 285,302              |
| Less: accumulated depreciation |                   | (117,192)        | (83,545)             |
|                                |                   | \$ 170,180       | \$ 201,757           |

For the three months ended June 30, 2013 and 2012, depreciation expenses amounted to \$19,065 and \$12,746, respectively. Depreciation expenses amounted to \$38,053 and \$21,486 for the six months ended June 30, 2013 and 2012, respectively.

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BIG TREE GROUP, INC. AND SUBSIDIARIES  
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NOTE 5 – INTANGIBLE ASSETS

Intangible assets represent accounting software purchased in July 2011, which is amortized on a straight line basis during its useful life of 5 years. For the three months ended June 30, 2013 and 2012, amortization expenses amounted to \$781 and \$796, respectively. For the six months ended June 30, 2013 and 2012, amortization expenses amounted to \$1,553 and \$1,536, respectively.

NOTE 6 – ADVANCE FROM CUSTOMERS

Advance from customers represent prepayment to us for merchandise that had not been shipped to customers. Advance from customers amounted to \$171,825 and \$142,125 as of June 30, 2013 and December 31, 2012, respectively.

NOTE 7 – LOAN PAYABLE

On November 2, 2012, we borrowed RMB 23,000,000 (\$3,725,782 and \$3,650,156 at June 30, 2013 and December 31, 2012, respectively) from Guangfa Bank Co., Ltd. Shantou Zhongshan Branch. Under the terms of loan agreement, interest is payable monthly at an annual rate of 6.9% and is due on November 2, 2013. If the loan is not paid by the due date, the default annual interest rate shall be 8.97% per annum. The loan is secured by a property owned by Shantou Youbang International Express Supervision Center Co., Ltd., a company owned by Ms. Guihong Zheng, Mr. Wei Lin's wife, and by a personal guarantee of Xinna Cai, a third party. For the three months ended June 30, 2013 and 2012, interest expense related to this loan amounted to \$65,346 and \$0, respectively. For the six months ended June 30, 2013 and 2012, interest expense related to this loan amounted to \$128,540 and \$0, respectively. We intend to renew this loan on the due date and extend the due date.

NOTE 8 – RELATED PARTY TRANSACTIONS

Prepaid expenses - related party

From time to time we advance funds to related parties for business travel and expenses. On June 30, 2013 and December 31, 2012, we advanced Guihong Zheng \$1,515 and \$1,484 for business expenses, respectively, which has been included in prepaid expenses on the accompanying consolidated balance sheets.

Loans payable – related party

On March 21, 2012 and May 9, 2012, we entered into promissory note agreements aggregating \$80,000 with China Direct Investments, Inc.. The proceeds of the loans were used for working capital purposes. The loan amounts of \$20,000 and \$60,000 and all accrued and unpaid interest are due no later than the earlier of on March 20, 2014 and May 9, 2014, respectively, or upon the completion of an offering of the Company's securities to raise capital. As of December 31, 2012, the Company received proceeds under these promissory notes of \$61,711 and the remaining proceeds were received in 2013. The loans bear interest at 2% per annum. For the three months ended June 30, 2013 and 2012, interest expense related to these loans amounted to \$399 and \$0, respectively. For the six months ended June 30, 2013 and 2012, interest expense related to these loans amounted to \$938 and \$0, respectively.

Advances to suppliers – related parties

We purchase products from Universal Toys Trading (Hong Kong) Limited (“Universal Toys”) that we sell to our customers. The sole shareholder of Universal Toys is Mr. Xiaodong Ou, the brother-in-law of our Chairman and Chief Executive Officer, Mr. Wei Lin. During the three months ended June 30, 2013 and 2012, we purchased \$0.2 million and \$0.3 million from Universal Toys. During the six months ended June 30, 2013 and 2012, we purchased \$0.2 million and \$0.8 million from Universal Toys. At June 30, 2013 and December 31, 2012, we owed Universal Toys \$0 and \$0, respectively. The Company agreed to purchase various products from Universal Toys, Universal Toys fills the purchase order in accordance with the Company’s specifications, and the Company is then obligated to pay Universal Toys upon delivery in accordance with its customary terms offered other suppliers /vendors.

On June 1, 2010, BT Shantou entered into a 10-year contract manufacturing agreement with Xinzhongyang Toys Industrial Co. Ltd., (“Xinzhongyang”) to produce the Big Tree Magic Puzzle (3D). Mr. Lin, our Chief Executive Officer and Ms. Guihong Zheng, his wife own Xinzhongyang. During the three months ended June 30, 2013 and 2012, we purchased approximately \$197,000 and \$80,000 from Xinzhongyang, respectively. During the six months ended June 30, 2013 and 2012, we purchased approximately \$200,000 and \$113,000 from Xinzhongyang, respectively.

BIG TREE GROUP, INC. AND SUBSIDIARIES  
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Advances to suppliers – related parties reflect prepayments to the above related party suppliers for purchases of toy products not yet received. As of June 30, 2013 and December 31, 2012, advances to suppliers – related parties consisted of the following:

|                                       | June 30,<br>2013  | December 31,<br>2012 |
|---------------------------------------|-------------------|----------------------|
| Advances to supplier - Universal Toys | \$ 138,743        | \$ 64,943            |
| Advances to supplier - Xinzhongyang   | 338,002           | 464,205              |
| <b>Total</b>                          | <b>\$ 476,745</b> | <b>\$ 529,148</b>    |

#### Due from related party

From time to time, BT Shantou receives advances from and makes advances to Xinzhongyang, for working capital purposes. At times the total payment the Company repaid to Xinzhongyang exceeds the total balance due to Xinzhongyang. Xinzhongyang is under the common control of Mr. Lin and his wife. At June 30, 2013 and December 31, 2012, amounts due from related party amounted to \$1,875,697 and \$261,970, respectively. The Company accounted for and presented the advances due from related party as a reduction of stockholders' equity in accordance with the guidance of ASC 505-10-45. It is possible that these working capital advances by us to Xinzhongyang could be deemed to be in violation of Section 402 of the Sarbanes-Oxley Act of 2002, however, we have not made a determination as of the date hereof if the advances resulted in a violation of that provision. We expect that the working capital advance made by us to Xinzhongyang will be repaid. If, however, the amount is not repaid and/or it was determined that these advances violated the prohibitions of Section 402 from making loans to executive officers or directors, the Company could be subject to investigation and/or litigation that could involve significant time and costs and may not be resolved favorably. The Company is unable to predict the extent of its ultimate liability with respect to these transactions. The costs and other effects of any future litigation, government investigations, legal and administrative cases and proceedings, settlements, judgments and investigations, claims and changes in this matter could have a material adverse effect on the Company's financial condition and operating results. For the six months ended June 30, 2013, due from related party activity consisted of the following:

|  |                     |
|--|---------------------|
| Balance, December 31, 2012               | \$ 261,970          |
| Working capital advances to Xinzhongyang | 2,791,474           |
| Repayments made by Xinzhongyang          | (1,200,264)         |
| Effect of foreign currency exchange      | 22,517              |
| <b>Balance, June 30, 2013</b>            | <b>\$ 1,875,697</b> |

#### Due to related parties

From time to time we received advances from related parties for working capital purposes. The advances bear no interest and are payable on demand. For the six months ended June 30, 2013, due to related party activities consisted of the following:

| Wei Lin<br>(1) | China Direct<br>Investments, Inc. | Total |
|----------------|-----------------------------------|-------|
|----------------|-----------------------------------|-------|

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|                                     |    |           |     |           |
|-------------------------------------|----|-----------|-----|-----------|
|                                     |    |           | (2) |           |
| Balance, December 31, 2012          | \$ | -         | \$  | 10,578    |
| Working capital advances            |    | 1,259,715 |     | 95,129    |
| Repayments                          |    | (327,593) |     | -         |
| Effect of foreign currency exchange |    | 46,397    |     | -         |
| Balance, June 30, 2013              | \$ | 978,519   | \$  | 105,707   |
|                                     |    |           |     | \$        |
|                                     |    |           |     | 1,084,226 |

- (1) Mr. Wei Lin is our chief executive officer and Chairman of the Board. At June 30, 2013, balances due to Mr. Lin primarily consisted of advances for working capital.
- (2) China Direct Investments, Inc. is a principal shareholder of the Company. The balance on June 30, 2013 consisted of amounts due to China Direct Investments, Inc. for advances to the Company to pay certain legal and accounting fees. These advances bear no interest and are payable on demand.

BIG TREE GROUP, INC. AND SUBSIDIARIES  
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#### Operating lease– related party

BT Shantou leases its principal executive offices and our first toy showroom for RMB 72,000 per annum from Yunjia, a company owned by Mr. Lin and his wife, Guihong Zheng. During the three months ended June 30, 2013 and 2012, we paid Yunjia RMB18,000 and RMB 18,000 (approximately \$2,868 and \$2,858), respectively, in rent expense. During the six months ended June 30, 2013 and 2012, we paid Yunjia RMB 36,000 and RMB 36,000 (approximately \$5,770 and \$5,712), respectively, in rent expense. The lease expires on December 31, 2021.

Effective October 1, 2012 we leased a second showroom in Shantou from Shantou Youbang International Supervise Center, Co., Ltd. (“Shantou Youbang”), a company owned by Ms. Guihong Zheng, Mr. Wei Lin’s wife, for an annual rent of RMB 1,440,000 (approximately \$228,571). The lease of the showroom expires on December 31, 2017. In connection with this lease, we paid a security deposit to Shantou Youbang of RMB 360,000 (\$58,317 and \$57,133 at June 30, 2013 and December 31, 2012, respectively) which is reflected as a security deposit – related party on the accompanying consolidated balance sheets. During the three months ended June 30, 2013 and 2012, rent expense amounted to \$58,041 and \$0, respectively. During the six months ended June 30, 2013 and 2012, rent expense for the Shantou Youbang showroom amounted to \$115,394 and \$0, respectively.

#### NOTE 9 - OTHER PAYABLE

On June 30, 2013, other payable of \$13,292 consisted of accrued consulting fee. On December 31, 2012, other payable of \$50,926 consisted of accrued shipping and inspection fees.

#### NOTE 10– CONCENTRATIONS AND CREDIT RISK

##### (i) Customer Concentrations

Customer concentrations for the six months ended June 30, 2013 and 2012 and as of June 30, 2013 and December 31, 2012, were as follows:

|                                      | Net Sales                             |              | Accounts Receivable |                      |
|--------------------------------------|---------------------------------------|--------------|---------------------|----------------------|
|                                      | For six months ended June 30,<br>2013 | 2012         | June 30,<br>2013    | December 31,<br>2012 |
| Always Trading International Limited | 21.9%                                 | 13.4%        | 14.7%               | 56.4%                |
| Poundland Far East Ltd               | 10.8%                                 | 11.0%        | 6.1%                | -                    |
| <b>Total</b>                         | <b>32.7%</b>                          | <b>24.4%</b> | <b>20.8%</b>        | <b>56.4%</b>         |

A reduction in sales from or loss of such customers would have a material adverse effect on our results of operations and financial condition

##### (ii) Vendor Concentrations

Vendor purchase concentrations for the six months ended June 30, 2013 and 2012 and as of June 30, 2013 and December 31, 2012, were as follows:

Net Purchases

Accounts Payable

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|  | For six months ended June 30, |       | June 30, | December 31, |
|--|-------------------------------|-------|----------|--------------|
|  | 2013                          | 2012  | 2013     | 2012         |
| Universal Toys (HK) Ltd (1)                | 1.2%                          | 4.6%  | -        | -            |
| Jiada Toys                                 | 10.1%                         | 7.6%  | 15.0%    | 35.1%        |
| Changtai Toys (Prosperous Toys)            | 45.8%                         | 45.5% | 34.5%    | -            |
| Yintai International (Win Tide)            | 29.4%                         | 29.8% | 32.3%    | -            |
| Guangdong Chenghai Xiongcheng Plastic Toys | 2.5%                          | -     | 6.2%     | 19.8%        |
| Total                                      | 89.0%                         | 87.5% | 88.0%    | 54.9%        |

- (1) Universal Toys is a related party, whose sole shareholder is Mr. Xiaodong Ou, the brother-in-law of Mr. Wei Lin, our Chairman and CEO. See Note 8 – Related Party Transactions.

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## (iii) Credit Risk

The Company's operations are carried out in the PRC. Accordingly, the Company's business, financial condition and results of operations may be influenced by the political, economic and legal environment in the PRC, and by the general state of the PRC's economy. The Company's operations in the PRC are subject to specific considerations and significant risks not typically associated with companies in North America. The Company's results may be adversely affected by changes in governmental policies with respect to laws and regulations, anti-inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation, among other things.

Financial instruments which potentially subject the Company to concentrations of credit risk consist principally of cash and trade accounts receivable. Substantially all of the Company's cash is maintained with state-owned banks within the PRC, the currency of which is not free trading, and no deposits are covered by insurance. Foreign exchange transactions are required to be conducted through institutions authorized by the Chinese government and there is no guarantee that Chinese currency can be converted to U.S. or other currencies. We have not experienced any losses in such accounts and believe we are not exposed to any risks on its cash in bank accounts.

At June 30, 2013 and December 31, 2012, the Company's cash balances by geographic area were as follows:

| Country:                        | June 30, 2013 |        |        | December 31, 2012 |        |        |
|---------------------------------|---------------|--------|--------|-------------------|--------|--------|
| PRC                             | \$            | 4,373  | 14.1%  | \$                | 11,001 | 49.6%  |
| United States                   |               | -      | -      |                   | 379    | 1.7%   |
| Hong Kong                       |               | 26,601 | 85.9%  |                   | 10,787 | 48.7%  |
| Total cash and cash equivalents | \$            | 30,974 | 100.0% | \$                | 22,167 | 100.0% |

## (iv) Foreign currency risk

We cannot guarantee that the current exchange rate will not fluctuate. There is always the possibility that we could post the same amount of profit for two comparable periods, and because of a fluctuating exchange rate actually post higher or lower profit depending on exchange rate of RMB converted to U.S. dollars on that date. The exchange rate could fluctuate depending on changes in the political and economic environments without notice.

## NOTE 11 - STOCKHOLDERS' EQUITY

## Preferred Stock

The Company is authorized to issue 20,000,000 shares of Preferred Stock, no par value, with such designations, rights and preferences as may be determined from time to time by the Board of Directors. As of June 30, 2013 and December 31, 2012, there were no shares issued and outstanding.

## Common Stock

The Company is authorized to issue 100,000,000 shares of Common Stock; \$0.00001 par value. As of June 30, 2013 and December 31, 2012, there were 10,350,192 and 10,200,179 shares of common stock issued and outstanding, respectively.



Common stock issued for services

On January 3, 2013, we entered into a consulting agreement with Dore Perler to engage Mr. Perler to provide us with sales consulting and managerial services related to our operations in North America for a period terminating on January 31, 2014. The consulting agreement provides that we shall issue Pearl Group 150,000 shares of our post-reverse-split common stock. Such shares were issued on March 28, 2013. The Company valued these common shares at the fair value of \$0.63 per common share based on the quoted trading price of the common stock on the grant date which is the measurement date. In connection with issuance of these common shares, the Company recorded stock-based compensation of \$94,500.

BIG TREE GROUP, INC. AND SUBSIDIARIES  
Notes to Unaudited Consolidated Financial Statements  
June 30, 2013

## NOTE 12 – COMMITMENTS AND CONTINGENCIES

Effective on December 18, 2011 we have operated two mini showrooms with 570 and 600 square feet respectively located in the terminals for domestic flights and international flights in Jieyang Chaoshan International Airport. The vendor permits and leases associated with the showrooms obtained from Shantou Airport Company of Guangdong Airport Management Corporation (“GAMC”) will expire on February 17, 2015. During the term, we are obliged to pay for two mini showrooms with a combined monthly fee of RMB15,929 (approximately \$2,470) to Shantou Airport Company, including vendor permit fee of RMB8,299 (approximately \$1,290), rent of RMB6,540 (approximately \$1,010), and administration fee of RMB1,090 (approximately \$170).

See Note 8 – Related Party Transactions for the detail terms on the related party operating leases of our principal executive offices and the two showroom facilities.

Future minimum rental payments required under third party and related parties operating leases are as follows:

| 12 months period ending June<br>30: | Third Party | Related Parties<br>(See Note 8) | Total        |
|-------------------------------------|-------------|---------------------------------|--------------|
| 2014                                | \$ 12,713   | \$ 244,930                      | \$ 257,643   |
| 2015                                | 8,475       | 244,930                         | 253,405      |
| 2016                                | -           | 244,930                         | 244,930      |
| 2017                                | -           | 244,930                         | 244,930      |
| 2018                                | -           | 128,297                         | 128,297      |
| Thereafter                          | -           | 40,822                          | 40,822       |
| Total                               | \$ 21,188   | \$ 1,148,839                    | \$ 1,170,027 |

## Litigation

From time to time we may be a defendant and plaintiff in various other legal proceedings arising in the normal course of our business. As of the date of this Annual Report, our management is not aware of any proceedings to which any of our directors, officers, or affiliates, or any associate of any such director, officer, affiliate, or security holder is a party adverse to our company or has a material interest adverse to us.

## NOTE 13 – RESTATEMENT

The Company’s consolidated financial statements have been restated as of June 30, 2012 and for the three and six months ended June 30, 2012. On April 3, 2013, we determined that we incorrectly understated an obligation due to related parties and overstated additional paid -in capital. On July 5, 2011 BT Brunei acquired 100% of the equity interest in BT Shantou from Mr. Lin and Ms. Zheng at the price of RMB 5,000,000, representing the original capital contributed by Mr. Lin and Ms. Zheng in BT Shantou. Previously, in consolidation, we erroneously reduced amounts due to related parties in order to eliminate BT Brunei’s investment in BT Shantou instead of reducing additional paid-in capital. Accordingly, we restated our consolidated balance sheet at June 30, 2012 to properly reflect an increase in amounts due to related party, Mr. Lin of \$792,531, we reduced additional paid-in capital by \$691,748, we reduced retained earnings by \$5,297, and we reduced accumulated other comprehensive income by \$95,486. The correction of this accounting error resulted in an increase in total liabilities of \$792,531 and a reduction in

shareholders' equity of \$792,531.

Additionally, for the three and six months ended June 30, 2012, we reduced comprehensive income by \$414 and \$95,486 on the consolidated statement of operations and comprehensive income, respectively. The restatement did not affect net income or net income per common share.

Accordingly, the Company's consolidated balance sheet at June 30, 2012 and the consolidated statement of operations and comprehensive income for the three and six months then ended have been restated herein. The effect of correcting this error in the Company's consolidated financial statements at June 30, 2012 and for the three and six months ended June 30, 2012 are shown in the table as follows:

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BIG TREE GROUP, INC. AND SUBSIDIARIES  
Notes to Unaudited Consolidated Financial Statements  
June 30, 2013

| Consolidated Balance Sheet data   | June 30 2012              |                           |              |
|---|---------------------------|---------------------------|--------------|
|   | As previously<br>reported | Adjustments to<br>Restate | Restated     |
| Total Assets  | \$ 7,814,541              | \$ -                      | \$ 7,814,541 |
| Due to related parties  | 2,183,093                 | 792,531 (a)               | 2,975,624    |
| Total Current Liabilities   | 5,190,686                 | 792,531                   | 5,983,217    |
| Total Liabilities   | 5,190,686                 | 792,531                   | 5,983,217    |
| <b>Stockholders' Equity:</b>  |                           |                           |              |
| Common stock (\$0.00001 par value;<br>100,000,000 shares authorized; 96,078,960<br>shares issued and outstanding at June 30,<br>2012) | 961                       | -                         | 961          |
| Additional paid-in capital  | 691,748                   | (691,748) (a)             | -            |
| Retained earnings   | 1,819,205                 | (5,297) (a)               | 1,813,908    |
| Accumulated other comprehensive income  | 111,941                   | (95,486) (a)              | 16,455       |
| Total Stockholders' Equity  | 2,623,855                 | (792,531)                 | 1,831,324    |
| Total Liabilities and Stockholders' Equity  | \$ 7,814,541              | \$ -                      | \$ 7,814,541 |

(a) To properly increase the liability due to Mr. Lin and Ms. Zheng by \$792,531, to reduce additional paid-in capital by \$691,748, to reduce retained earnings by \$5,297, and to reduce accumulated other comprehensive income by \$95,486.

| Consolidated<br>Statement of<br>operations and<br>comprehensive<br>income: | For the Three Months Ended<br>June 30, 2012<br>(Unaudited) |                           |            | For the Six Months Ended<br>June 30, 2012<br>(Unaudited) |                           |            |
|--|--|---------------------------|------------|--|---------------------------|------------|
|  | As<br>previously<br>reported                               | Adjustments<br>to Restate | Restated   | As<br>previously<br>reported                             | Adjustments<br>to Restate | Restated   |
|  | Net income   | \$ 518,490                | \$ -       | \$ 518,490   | \$ 746,878                | \$ -       |
| Foreign currency<br>translation<br>adjustment                              | 809  | (414) (b)                 | 395        | 124,599  | (95,486) (b)              | 29,113     |
| Comprehensive<br>income  | \$ 519,299   | \$ (414)                  | \$ 518,885 | \$ 871,477   | \$ (95,486)               | \$ 775,991 |

(b) To properly reflect change in comprehensive income.

## NOTE 14 - SUBSEQUENT EVENTS

Since June 30, 2013, the Company received repayments of advances made to Xinzhongyang of RMB 4,135,000 (approximately \$669,830) (See Note 8).

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

The following discussion of our financial condition and results of operation should be read in conjunction with our unaudited consolidated financial statements and footnotes for the three and six months ended June 30, 2013 and 2012.

### Overview

Our main business focus is to function as a “one stop shop” for the sourcing, distribution and specialty manufacturing of toys and related products. We conduct these operations through both BT Brunei, which focuses on export sales, and BT Shantou, which concentrates on PRC domestic sales. We are located in Shantou City of Guangdong province, the geographical region well-known for toys manufacturing and exporting in China. We provide procurement services for international toy distributors and wholesalers, including identifying, evaluating, and engaging one or more local manufacturers, trading companies or distributors for the requested supply of toys, as well as original equipment manufacturing (“OEM”) services. The OEM services include engaging toy manufacturers directly or through other toy trading companies or distributors to either manufacture toys to specific specifications requested by our customers, or customize an existing toy product to meet our customer’s request such as through changes in mechanical functionality, appearance, physical dimension, and materials. We do not manufacture any products. We source a wide variety of 300,000 toys made of plastic, wood, metal, wool, and electronic materials, primarily targeting children from infants to teenagers.

We source toys to distributors, trading companies, and wholesalers primarily located in mainland China, Hong Kong, Europe, South America, and Asia. The end customers are typically children, ranging from infants to teenagers, in these countries and regions. In 2013, we opened our toy experience center and a second showroom which is being used to provide our customers and potential customers the opportunity to see all the toys we offer with a one-stop shop experience.

We are dependent upon certain customers and suppliers. During the six months ended June 30, 2013, two customers represented 32.7% of total revenues. During the six months ended June 30, 2013, five of our suppliers accounted for 88.7% of our toy purchases. During the first six months of 2012, one major customer represented approximately 11.0% of our total revenues. During the first six months of 2012, four of our suppliers accounted for 87.5% of our toy purchases.

In 2011, we started selling Big Tree Magic Puzzle directly to Chinese domestic end consumers including children and grown-ups through our own sales counters in Dennis Department Stores and online store at Taobao Mall (www.Tmall.com), the biggest B2C online retailing platform in China. In 2012, we closed our counters at Dennis Department Stores. The sales from this product represented less than 1% of our total revenue during 2012 and 2011. During 2013, we plan on utilizing our existing distribution channels in an effort to increase the sales of this proprietary product. In addition, and subject to the availability of additional capital, of which there are no assurances, should sales of this product increase in 2013 we plan on opening retail locations from which this propriety product can be offered. While we are in the early stages of planning these locations and have not finalized any of these expansion plans, including the target number of locations, we estimate that the cost per new location will be approximately RMB50,000 to RMB100,000 (approximately US \$8,000 to US \$16,000).

In addition to a continued focus on increasing our revenues from our procurement and OEM sourcing services, and sales of our Big Tree Magic Puzzle (3D), our growth strategies include possibly opening satellite sales offices and branches in the U.S. and other cities in China as well as the potential acquisition of distributors. We are in the early stages of development of these plans as well and have not finalized any cost or timing estimates and are not a party to

any agreements. Our ability to undertake any of these expansion plans is also dependent upon our ability to raise additional capital, of which there are no assurances.

Lastly, we continue to evaluate the financial and operating benefits of acquisitions of Yunjia and/or Xinzhongyang, related parties. If we should determine to proceed with the acquisition of Yunjia or Xinzhongyang, or both, of which there is no assurance, it is likely that we would acquire these companies for equity in our company which will be dilutive to our existing shareholders. We are not a party to any agreements at this time for an acquisition of either Yunjia or Xinzhongyang and we may determine that neither acquisition would provide a financial or operating benefit to our company.

## Results of Operations

### Revenues

Our consolidated revenues for the second quarter of 2013 amounted to \$11.9 million, an increase of \$5.9 million over the same period in 2012. Our consolidated revenues for the first six months of 2013 amounted to \$19.3 million, an increase of \$8.6 million over the same period in 2012.

For the three and six months ended June 30, 2013, BT Shantou's revenues increase by approximately \$2.2 million and \$3.5 million respectively. This increase was primarily due to an increase in sales to one customer, Always Trading International Limited ("Always") which we accounted for on a gross basis as a principal. For the six months ended June 30, 2013 and 2012, sales to Always accounted for 21.9% and 13.4% of total sales, respectively. Pursuant to our revenue recognition policy, in the 2013 periods, we recorded less sales on a net basis as an agent as compared to the comparable periods in 2012. Our revenue accounted for on a net basis as an agent decreased during the three and six months ended June 30, 2013 as compared to the three and six months ended June 30, 2012 mainly due to the nature of the sales transactions completed in the comparative periods. The increase in Brunei's revenue for the three and six months ended June 30, 2013 as compared to the comparable periods of 2012 was primarily due to the recent opening of our new toy show room.

Our strategy is to utilize BT Brunei to continue to increase our customer base for export sales of toys, while continuing to expand our domestic distribution sales channels within China through BT Shantou. BT Brunei is organized in the State of Brunei Darussalam which is a non-taxable jurisdiction. Net income from BT Brunei are not subject to income taxes as compared to sales revenues from BT Shantou which are subject to a PRC tax rate of 25%. These operational costs savings have permitted the Company to leverage its export sales contacts to significantly expand the Company's export sales in 2012 and in the first half of 2013 by permitting us to be more price competitive. Our revenues during the six months ended June 30, 2013 were generated from exports of toys, and accordingly, we are susceptible to the fluctuations and uncertainty of international trading conditions, currency exchange rates, and global financial crisis. In addition, due to the inflation and continuous appreciation of RMB in the past few years which has resulted in an increase in the wholesale price of toys, we will continue to face challenges in finding ways to effectively compete in the pricing of toy products in our domestic and export markets while maintaining our margins. We expect our revenues to increase in the rest of 2013 over 2012 as we continue to expand our export sales efforts.

In accordance with ASC 605-45-45, "Principal Considerations - Other Presentation Matters", we report our revenues from sales of toys as follows:

| Allocation of Revenues                          | Revenue Recognition (1)<br>For the three months ended June 30, 2013 |                  |                      | For the three months ended June 30,<br>2012<br>(as restated) |                   |                     |
|---|---|------------------|----------------------|--|-------------------|---------------------|
|   | Gross Method  | Net Method       | Total                | Gross Method   | Net Method        | Total               |
| Revenues, excluding sales reported on net basis | \$ 11,844,100   | \$ -             | \$ 11,844,100        | \$ 5,584,344   | \$ -              | \$ 5,584,344        |
| Net Revenues from sales reported on net basis   | -   | 19,174           | 19,174               | -  | 376,398           | 376,398             |
| <b>Total Revenues</b>                           | <b>\$ 11,844,100</b>  | <b>\$ 19,174</b> | <b>\$ 11,863,274</b> | <b>\$ 5,584,344</b>  | <b>\$ 376,398</b> | <b>\$ 5,960,742</b> |

| Allocation of Revenues | Revenue Recognition (1)<br>For the Six Months Ended June 30, 2013 |            |               | For the Six Months Ended June 30, 2012<br>(as restated) |            |               |
|------------------------|---|------------|---------------|---|------------|---------------|
|                        | Gross Method  | Net Method | Total         | Gross Method  | Net Method | Total         |
|                        | \$ 19,247,073   | \$ -       | \$ 19,247,073 | \$ 10,198,830   | \$ -       | \$ 10,198,830 |



Revenues,  
excluding sales reported on  
net basis

Net Revenues from sales  
reported on net basis

|                |               |           |               |               |            |               |
|----------------|---------------|-----------|---------------|---------------|------------|---------------|
|                | -             | 63,902    | 63,902        | -             | 513,997    | 513,997       |
| Total Revenues | \$ 19,247,073 | \$ 63,902 | \$ 19,310,975 | \$ 10,198,830 | \$ 513,997 | \$ 10,712,827 |

(1) Certain revenues from our sales are based on a net reporting because they do not meet the criteria for gross reporting method pursuant to ASC 605-45-45. This means that all cost of purchases from those sales will be netted with the revenues generated by the sale of those toys. Additionally, handling fees related to sales reported on a net basis are also netted with these revenues. All other revenues from sales are based on gross reporting pursuant to criteria outlined in ASC 605-45-45, as follows:

- we are the primary obligor to provide the product or services desired by our customers;
  - we have discretion in supplier selection.
  - we have latitude in establishing price;
- we have credit risk – see Note 10 for customer concentrations and credit risk; and
- we have inventory risk before customer order and upon customer return;

Additionally, handling fees related to sales reported on a net basis are also netted with these revenues.

If we change the relationship with our customers or vendors and do not meet any of the criteria, pursuant to our revenue recognition policy, we record revenues on a net basis (revenues less cost of revenues and handling fees).

### Cost of Revenues

Cost of revenues includes the cost of purchases of product and product handling fees which amounts to approximately three percent of the purchase amount on revenues recorded on a gross basis pursuant to our revenue recognition policy. Cost of revenues was \$11.0 million for the second quarter of 2013, an increase of \$5.8 million over the same period of 2012, while cost of revenues as a percentage of revenues increased to 92.5% in the second quarter of 2013 from 86.5% in the same period of 2012. Cost of revenues was \$17.7 million for the first six months of 2013, an increase of \$8.3 million over the same period of 2012, while cost of revenues as a percentage of revenues increased to 91.8% in the first six months of 2013 from 87.6% in the same period of 2012. The amount of cost of revenues and cost of revenues as a percentage of revenues fluctuates depending on our revenue recognition policy. For example, if we record more revenue on a gross basis, cost of revenues will increase and cost of revenues as a percentage of revenues will increase. Conversely, if we record less revenue on a gross basis, cost of revenues will decrease and cost of revenues as a percentage of revenues will decrease.

### Gross Profit

Our gross profit was \$0.9 million for the second quarter of 2013, an increase of \$0.1 million over the same period of 2012. Our consolidated gross margin was 7.5% for the second quarter of 2013 as compared to 13.5% for the same period in 2012. Our gross profit was \$1.6 million for the six months of 2013, an increase of \$0.3 million over the same period of 2012. Our consolidated gross margin was 8.2% for the six months of 2013 as compared to 12.4% for the same period in 2012. We continue our 2012 strategy to lower the gross margins on our international sales to gain a higher market share. As previously discussed above, revenue is accounted for in accordance with the ASC 605-45, reporting revenue either on a gross basis as a principal or net basis as an agent depending upon the nature of the sales transaction. Accordingly, our gross margin will fluctuate if we change the relationship with our customers or vendors and do not meet any of the criteria, pursuant to our revenue recognition policy. Currently, we are not able to quantify this future fluctuation in gross margins.

### Operating Expenses

Operating expenses, comprised of selling and general and administrative expenses, amounted to \$453,000 for the second quarter of 2013, an increase of \$149,000 as compared to the same period in 2012. Selling expense increased by \$37,309 in the second quarter of 2013 as compared to the same period in 2012 primarily due to an increase in shipping expense of \$23,200 and an increase in salary expense of \$12,000. General and administrative expenses increased by \$111,000 in the second quarter of 2013 as compared to the same period in 2012. This increase was primarily due to \$37,700 increase in salary expense and a \$60,000 increase in rent expense – related party associated with the lease of our new showroom. We expect operating expenses to continue to increase in 2013, including increased costs associated with our public company reporting obligations, but we are unable at this time to quantify the amount of the expected increase.

Operating expenses amounted to \$1.0 million for the six months of 2013, an increase of \$0.4 million over the same period in 2012. Selling expense increased by \$13,735 in the six months of 2013 as compared to the same period in 2012 primarily due to an increase in salary expense. General and administrative expenses increased by approximately \$375,000 in the six months of 2013 as compared to the same period in 2012. This increase was primarily due to an increase in salary of \$69,000, a \$115,000 increase in rent expense – related party associated with the lease of our new showroom, and the recording of stock-based consulting fees of \$94,500 for business development services. We expect operating expenses to continue to increase in 2013, including increased costs associated with our public company reporting obligations, but we are unable at this time to quantify the amount of the expected increase.

Other Income (Expenses)

For the three and six months of 2013, other expenses amounted to \$102,329 and \$185,004 as compared to other income of \$17,154 and \$31,477 for the same period of 2012. During the three and six months ended June 30, 2013, we incurred interest expense of approximately \$65,700 and \$129,500 related primarily to our bank loan. We did not incur such interest expense during the same period of 2012. Additionally, we incurred exchange loss of \$58,000 and \$74,000 during the three and six months ended June 30, 2013. We also incurred other income of \$24,000 during the three and six months ended June 30, 2013.

Net Income

As a results of the discussion above, our net income for the second quarter of 2013 and 2012 amounted to \$333,473, or \$0.03 per common share (basic and diluted) and \$518,490, or \$0.05 per common share (basic and diluted), respectively. Our net income for the six months ended June 30, 2013 and 2012 amounted to \$398,854, or \$0.04 per common share (basic and diluted) and \$746,878, or \$0.07 per common share (basic and diluted), respectively.

## Liquidity and Capital Resources

Liquidity is the ability of a company to generate sufficient cash to meet its operational cash requirements. We had working capital of \$1.3 million as of June 30, 2013, as compared to \$2.4 million as of December 31, 2012. Our primary uses of cash have been for purchases of toy products, for working capital needs and for advances made to related parties. Our primary sources of cash are derived from revenues from the sales of our toy products, from bank loans and from advances from related parties.

At June 30, 2013 and December 31, 2012, the Company's cash balances by geographic area were as follows:

| Country:                        | June 30, 2013 |        | December 31, 2012 |    |        |        |
|---------------------------------|---------------|--------|-------------------|----|--------|--------|
| PRC                             | \$            | 4,373  | 14.1%             | \$ | 11,001 | 49.6%  |
| United States                   |               | -      | -                 |    | 379    | 1.7%   |
| Hong Kong                       |               | 26,601 | 85.9%             |    | 10,787 | 48.7%  |
| Total cash and cash equivalents | \$            | 30,974 | 100.0%            | \$ | 22,167 | 100.0% |

Cash held in banks in the PRC and Hong Kong are not insured. The value of cash on deposit in China has been converted to U.S. dollars based on the exchange rates as of respective balance sheet dates. In 1996, the Chinese government introduced regulations, which relaxed restrictions on the conversion of the RMB; however restrictions still remain, including but not limited to restrictions on foreign invested entities. Foreign invested entities may only buy, sell or remit foreign currencies after providing valid commercial documents at only those banks authorized to conduct foreign exchanges. Furthermore, the conversion of RMB for capital account items, including direct investments and loans, is subject to PRC government approval. Chinese entities are required to establish and maintain separate foreign exchange accounts for capital account items. We cannot be certain Chinese regulatory authorities will not impose more stringent restrictions on the convertibility and outflow of RMB, especially with respect to foreign exchange transactions. Accordingly, cash on deposit in banks in the PRC is not readily deployable by us for purposes outside of China.

Total current assets at June 30, 2013 increased by \$4.7 million from December 31, 2012. The principal contributor to this change was a \$5.0 million increase in accounts receivable and an increase in inventories of \$0.6 million offset by a \$0.6 million decrease in advance to suppliers-non-related parties. Total current liabilities at June 30, 2013 increased by \$5.8 million as compared to December 31, 2012 primarily due to a \$4.7 million increase in accounts payable and accrued expenses, which was a result of increased purchases to fulfill higher sales volume in the first six months of 2013, together with \$1.0 million increase in due to related parties. The increase in due to related parties reflects funds advanced to us by our Chairman and CEO, as well as other related parties, for working capital.

We do not have any commitments for capital expenditures and expect that our cash on hand and cash flow from operations will be sufficient to sustain our operations for at least the next twelve months. However, the following trends are reasonably likely to require us to raise additional capital.

- An increase in working capital requirements to finance near term and long term growth strategy including possible acquisitions;
- Increases in capital expenditures, marketing and administrative expenses to support the sales growth of our company;
- The costs for recruitment and retention of additional management and personnel to support our operations and expansion plans; and
-

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The additional costs, including legal accounting and consulting fees, associated with a public company and related compliance activities.

In 2012, we entered into two-year promissory note agreements with China Direct Investments, Inc., respectively, for an aggregate loan amount of \$80,000. The proceeds of the loans were used for working capital purposes. As of December 31, 2012, we received proceeds under these promissory notes of \$61,711 and the remaining proceeds were received in 2013. The loan amounts of \$20,000 and \$60,000 and all accrued and unpaid interest are due no later than the earlier of on March 20, 2014 and May 9, 2014, respectively, or upon the completion of an offering of our securities to raise capital. The loans bear interest at 2% per annum.

On November 2, 2012, we borrowed RMB 23,000,000 (\$3,725,782 at June 30, 2013) from Guangfa Bank Co., Ltd. Shantou Zhongshan Branch. We used the proceeds of this loan for working capital purposes, including the purchase of toy products. Under the terms of loan agreement, interest is payable monthly at an annual rate of 6.9% and is due on November 2, 2013. If the loan is not paid by the due date, the default interest rate shall be 8.97% per annum. The loan is secured by a property owned by Shantou Youbang, a company owned by Ms. Guihong Zheng, Mr. Wei Lin's wife, and personally guaranteed by Xinna Cai, a third party. We intend to renew this loan on the due date and extend the due date.

From time to time we received advances from related parties for working capital purposes. The advances bear no interest and are payable on demand. For the six months ended June 30, 2013, due to related party activities consisted of the following:

|                                     |    | Wei Lin   | China Direct<br>Investments, Inc. | Total        |
|-------------------------------------|----|-----------|-----------------------------------|--------------|
| Balance, December 31, 2012          | \$ | -         | \$ 10,578                         | \$ 10,578    |
| Working capital advances            |    | 1,259,715 | 95,129                            | 1,354,844    |
| Repayments                          |    | (327,593) | -                                 | (327,593)    |
| Effect of foreign currency exchange |    | 46,397    | -                                 | 46,397       |
| Balance, June 30, 2013              | \$ | 978,519   | \$ 105,707                        | \$ 1,084,226 |

Other than the loans discussed above and working capital advanced from related parties, we do not have any external sources of working capital. We may seek to raise capital through the sale of equity in our company, however, we are not a party to any agreement or understandings at this time and there are no assurances we will be able to raise capital on terms satisfactory to us, or at all. If we are unable to raise additional capital as may be needed, our ability to grow our company and increase our revenues in future periods will be adversely impacted.

#### Cash Flows Analysis

##### NET CASH FLOW PROVIDED BY (USED IN) OPERATING ACTIVITIES:

Net cash provided by operating activities was approximately \$0.5 million for the first six months of 2013, as compared to net cash used in operating activities of \$24,171 for the same period of 2012. For the first six months of 2013, cash flows provided by operating activities was primarily attributable to our net income of \$398,854 adjusted for the add back of non-cash items such as depreciation and amortization of \$39,606, stock-based compensation of \$94,501 and bad debt expense of \$3,327 and changes in operating assets and liabilities such as a decrease in advances to suppliers of approximately \$0.6 million and an increase in accounts payable and accrued expenses of approximately \$4.6 million, which offset by an increase in accounts receivable and an increase in prepaid expenses and other current assets of approximately \$4.9 million and \$0.3 million, respectively. For the first six months of 2012, net cash used in operating activities was primarily attributable to an increase of approximately \$1.8 million in accounts receivable from higher sales and approximately \$1.4 million used for inventory to fulfill higher customer demand, partially offset by an increase of approximately \$1.6 million in due to related party from trading activities and an increase of approximately \$1.3 million in account payable and accrued expenses for higher toy purchases.

##### NET CASH FLOW USED IN INVESTING ACTIVITIES:

Net cash used in investing activities amounted to \$2,675 for the first six months of 2013 as a result of the purchase of property and equipment compared with \$0.1 million for the first six months of 2012.

##### NET CASH FLOW (USED IN) PROVIDED BY FINANCING ACTIVITIES:

Net cash used in financing activities was approximately \$0.5 million for the first six months of 2013, due to an increase in the amount of advances made to a related party of approximately \$1.6 million offset by net proceeds we received from a related party advances of approximately \$1.4 million and the repayment of related party advances of approximately \$0.3 million. For the first six months of 2012, we received proceeds from advances from a related party of \$0.5 million.

We have certain fixed contractual obligations and commitments that include future estimated payments. Changes in our business needs, cancellation provisions, changing interest rates, and other factors may result in actual payments differing from the estimates. We cannot provide certainty regarding the timing and amounts of payments. We have presented below a summary of the most significant assumptions used in our determination of amounts presented in the tables, in order to assist in the review of this information within the context of our consolidated financial position, results of operations, and cash flows. The following tables summarize our contractual obligations as of June 30, 2013 (dollars in thousands), and the effect these obligations are expected to have on our liquidity and cash flows in future periods.

Payments Due by Period

| Contractual obligations (dollars in thousands) : | Payments Due by Period |                  |           |           |          |
|--|------------------------|------------------|-----------|-----------|----------|
|  | Total                  | Less than 1 year | 1-3 years | 3-5 years | 5+ years |
| Loans payable                                    | \$ 3,800               | \$ 3,800         | \$ -      | \$ -      | \$ -     |
| Total  | \$ 3,800               | \$ 3,800         | \$ -      | \$ -      | \$ -     |

### Off Balance Sheet Arrangements

Under SEC regulations, we are required to disclose our off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, such as changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors. An off-balance sheet arrangement means a transaction, agreement or contractual arrangement to which any entity that is not consolidated with us as a party, under which we have:

- Any obligation under certain guarantee contracts,
- Any retained or contingent interest in assets transferred to an unconsolidated entity or similar arrangement that serves as credit, liquidity or market risk support to that entity for such assets,
- Any obligation under a contract that would be accounted for as a derivative instrument, except that it is both indexed to our stock and classified in stockholder's equity in our statement of financial position, and
- Any obligation arising out of a material variable interest held by us in an unconsolidated entity that provides financing, liquidity, market risk or credit risk support to us, or engages in leasing, hedging or research and development services with us.

We do not have any off-balance sheet arrangements that we are required to disclose pursuant to these regulations. In the ordinary course of business, we enter into operating lease commitments, purchase commitments and other contractual obligations. These transactions are recognized in our financial statements in accordance with U.S. GAAP.

### Critical Accounting Policies

The preparation of financial statements in conformity with U.S. GAAP requires estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities in the consolidated financial statements and accompanying notes. The SEC has defined a company's critical accounting policies as the ones that are most important to the portrayal of the company's financial condition and results of operations, and which require the company to make its most difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Based on this definition, we have identified the critical accounting policies and judgments addressed below. We also have other significant accounting policies, which involve the use of estimates, judgments and assumptions that are significant to understanding our results, which are described in Note 2 to our financial statements. Although we believe that our estimates, assumptions and judgments are reasonable, they are based upon information presently available. Actual results may differ significantly from these estimates under different assumptions, judgments or conditions.

#### Revenue recognition

We follow the guidance of ASC 605, "Revenue Recognition," and the SEC Staff Accounting Bulletin (SAB) No. 104 and SAB Topic 13 for revenue recognition. In general, we record revenue when persuasive evidence of an arrangement exists, services have been rendered or product delivery has occurred, the sales price to the customer is fixed or determinable and collectability is reasonably assured.

Revenues for our product sales are recognized when all four of the following criteria are met: (i) persuasive evidence of an arrangement exists through a formal purchase order; (ii) delivery of the products has occurred and risks and rewards of ownership have passed to the customer; (iii) the selling price is both fixed and determinable based upon an



agreement between our company and our customer; and (iv) collectability is reasonably assured. For any advance payments from customers, revenues are deferred until such a time when all the four criteria mentioned above are fully met.

Revenue is accounted for in accordance with the ASC 605-45, reporting revenue either gross as a principal or net as an agent depending upon the nature of the sales transaction. Revenue is recognized on a gross basis when the Company determines the sale meets the conditions of ASC 605-45, "Reporting Revenue Gross as a Principal versus Net as an Agent." When the Company does not meet the criteria for gross revenue recognition under ASC 605-45, the Company reports the revenue on a net basis -See Note 2 for details on computation of net and gross reporting methods.

#### Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates for the three and six month periods ended June 30, 2013 and 2012 include the allowance for doubtful accounts on accounts receivable, allowance for obsolete inventory, the useful life of property and equipment and intangible assets, and the valuation of stock-based compensation.

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

Not applicable for smaller reporting companies.

### ITEM 4. CONTROLS AND PROCEDURES

#### Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")) that are designed to ensure that information required to be disclosed by us in reports that we file under the Exchange Act is recorded, processed, summarized and reported as specified in the SEC's rules and forms and that such information required to be disclosed by us in reports that we file under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer (CEO), and our Chief Financial Officer (CFO), to allow timely decisions regarding required disclosure. Management, with the participation of our CEO and CFO, performed an evaluation of the effectiveness of our disclosure controls and procedures as of June 30, 2013.

Based on this evaluation we concluded that as of June 30, 2013 our disclosure controls and procedures were not effective such that the information relating to our company, including our consolidated subsidiaries, required to be disclosed in our SEC reports (i) is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and (ii) is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure as a result of continuing material weaknesses in our internal control over financial reporting previously identified in our Annual Report on Form 10-K for the year ended December 31, 2012.

#### Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting during our fiscal quarter ended June 30, 2013 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II - OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

We are not a party to any pending litigation.

#### ITEM 1A. RISK FACTORS.

Risk factors describing the major risks to our business can be found under Item 1A, "Risk Factors", in our fiscal 2012 Annual Report on Form 10-K. There has been no material change in our risk factors from those previously discussed in the 2012 Annual Report on Form 10-K for the year ended December 31, 2012.

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

None

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable to our company's operation

ITEM 5. OTHER INFORMATION

None

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ITEM 6. EXHIBITS

Description of Exhibit

31.1 Section 302 Certificate of Chief Executive Officer.\*

31.2 Section 302 Certificate of Chief Financial Officer.\*

32.1 Section 906 Certificate of Chief Executive Officer and Chief Financial Officer.\*

101.INS XBRL INSTANCE DOCUMENT \*\*

101.SCH XBRL TAXONOMY EXTENSION SCHEMA \*\*

101.CAL XBRL TAXONOMY EXTENSION CALCULATION LINKBASE \*\*

101.DEF XBRL TAXONOMY EXTENSION DEFINITION LINKBASE \*\*

101.LAB XBRL TAXONOMY EXTENSION LABEL LINKBASE \*\*

101.PRE XBRL TAXONOMY EXTENSION PRESENTATION LINKBASE \*\*

\* Filed herewith.

In accordance with Regulation S-T, the XBRL-formatted interactive data files that comprise Exhibit 101

\*\* in this Quarterly Report on Form 10-Q shall be deemed “furnished” and not “filed”.

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.

Date: August 14, 2013

BIG TREE GROUP, INC.

By: /s/ Wei Lin

Wei Lin

Chairman and Chief Executive Officer, principal executive officer

Date: August 14, 2013

By: /s/ Jiale Cai

Jiale Cai, Chief Financial Officer, principal financial and accounting officer

