

CHINA RUITAI INTERNATIONAL HOLDINGS CO., LTD.  
Form 10-Q  
August 14, 2009

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

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

For the quarterly period ended June 30, 2009

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

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

Commission File Number: 000-04494

**CHINA RUITAI INTERNATIONAL HOLDINGS CO., LTD.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation)

**13-5661446**

(IRS Employer Identification  
Number)

**Wenyang Town**

**Feicheng City**

**ShanDong, China 271603**

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(Address of principal executive offices)

**86 538 3850 703**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Not Applicable.

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

Accelerated filer

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

Smaller reporting company

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

As of July 31, 2009 the Issuer had 26,000,000 shares of common stock issued and outstanding.

**PART I-FINANCIAL INFORMATION**

**ITEM 1.**

**FINANCIAL STATEMENTS.**

The consolidated financial statements of China RuiTai International Holdings Co., Ltd., a Delaware corporation, included herein were prepared, without audit, pursuant to rules and regulations of the Securities and Exchange Commission. Because certain information and notes normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America were condensed or omitted pursuant to such rules and regulations, these financial statements should be read in conjunction with the financial statements and notes thereto included in the audited financial statements of China RuiTai International Holdings, Co., Ltd. in its Form 10-K, and all amendments thereto, for the fiscal year ended December 31, 2008.

**CHINA RUITAI INTERNATIONAL HOLDINGS CO., LTD.**

**FINANCIAL STATEMENTS**

**PERIOD ENDED JUNE 30, 2009**

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**CHINA RUITAI INTERNATIONAL HOLDINGS CO., LTD. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

|  | June 30,<br><u>2009</u><br><u>(unaudited)</u> | December 31,<br><u>2008</u> |
|--|---|-----------------------------|
| <b>ASSETS</b>                                      |   |                             |
| Current Assets:                                    |   |                             |
| Cash and cash equivalents                          | \$ 1,865,139                                  | \$ 5,319,456                |
| Bank checks and commercial paper                   | 9,033,677                                     | 8,244,207                   |
| Accounts receivable, net (Note 5)                  | 5,092,911                                     | 3,295,341                   |
| Due from unaffiliated suppliers (Note 6)           | 518,174                                       | 346,976                     |
| Prepaid expenses (Note 7)                          | 2,676,279                                     | 2,330,898                   |
| Inventory (Note 8)                                 | 7,083,856                                     | 8,157,592                   |
| Advance to employees (Note 15)                     | 204,101                                       | 150,294                     |
| Restricted cash (Note 11)                          | 29,219,261                                    | 19,112,900                  |
| Due from a related party-current portion (Note 15) | 15,940,153                                    | 10,321,711                  |
| Total current assets                               | 71,633,551                                    | 57,279,375                  |
| Property and Equipment, net (Note 9)               | 13,467,279                                    | 12,936,668                  |
| Land use right, net (Note 10)                      | 5,037,319                                     | 5,084,515                   |
| Long-term investment                               | 887,973                                       | 886,780                     |
| Due from a related party (Note 15)                 | 5,931,837                                     | 5,931,837                   |
| Total Assets                                       | \$ 96,957,959                                 | \$ 82,119,175               |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>        |   |                             |
| Current Liabilities:                               |   |                             |
| Bank loan (Note 13)                                | \$ 22,782,257                                 | \$ 22,022,146               |
| Bank checks payable (Note 12)                      | 39,446,002                                    | 29,180,000                  |
| Accounts payable and accrued expenses              | 6,693,279                                     | 6,247,060                   |
| Taxes payable                                      | 5,777,083                                     | 5,411,445                   |
| Deferred revenue                                   | 607,954                                       | 418,776                     |
| Due to employees (Note 15)                         | 1,671,123                                     | 1,707,383                   |
| Employee security deposit                          | 1,017,893                                     | 972,181                     |
| Total Current Liabilities                          | 77,995,591                                    | 65,958,991                  |



|  |               |               |
|--|---------------|---------------|
| Commitments and Contingencies (Note 22)  | -             | -             |
| Shareholders' Equity:  |               |               |
| China Ruitai International Holdings Co., Ltd.                                      |               |               |
| Shareholders' Equity   |               |               |
| Preferred stock, par value \$0.001, 10,000,000 shares authorized,                  |               |               |
| authorized, no shares outstanding as of June 30, 2009 and December 31, 2008        | -             | -             |
| Common stock, par value \$0.001, 50,000,000 shares authorized,                     |               |               |
| 26,000,000 shares issued and outstanding as of June 30, 2009 and December 31, 2008 | 26,000        | 26,000        |
| Additional paid-in capital   | 2,908,171     | 2,908,171     |
| Unamortized contractual services costs   | -             | (165,978)     |
| Statutory Reserves   | 1,369,652     | 1,369,652     |
| Retained earnings  | 13,148,634    | 10,560,128    |
| Accumulated other comprehensive income   | 1,325,694     | 1,304,357     |
| Total China Ruitai International Holdings Co., Ltd. Shareholders' equity           | 18,778,151    | 16,002,330    |
| Noncontrolling Interest  | 184,217       | 157,854       |
| Total Shareholders' Equity   | 18,962,368    | 16,160,184    |
| Total Liabilities and Shareholders' Equity   | \$ 96,957,959 | \$ 82,119,175 |

**See Notes to Consolidated Financial Statements**

**CHINA RUITAI INTERNATIONAL HOLDINGS CO., LTD. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS**

|  | For the Three Months Ended |                    | For the Six Months Ended |                    |
|--|----------------------------|--------------------|--------------------------|--------------------|
|  | June 30,                   |                    | June 30,                 |                    |
|  | <u>2009</u>                | <u>2008</u>        | <u>2009</u>              | <u>2008</u>        |
|  | <u>(unaudited)</u>         | <u>(unaudited)</u> | <u>(unaudited)</u>       | <u>(unaudited)</u> |
| Revenues                               |                            |                    |                          |                    |
| Sales                                  | \$ 8,463,783               | \$ 9,823,948       | \$ 16,694,963            | \$ 19,245,939      |
| Costs of Sales                         | 5,506,063                  | 7,084,546          | 10,482,604               | 13,496,330         |
| Gross Profit                           | 2,957,720                  | 2,739,402          | 6,212,359                | 5,749,609          |
| Operating Expenses                     |                            |                    |                          |                    |
| Selling expenses                       |                            |                    |                          |                    |
| Sales commission                       | 190,349                    | 113,189            | 286,447                  | 324,914            |
| Freight-out                            | 162,771                    | 194,466            | 323,781                  | 380,923            |
| Advertising                            | 26,019                     | 16,748             | 26,019                   | 17,433             |
| Travel and entertainment               | 44,824                     | 31,511             | 68,990                   | 63,086             |
| Office expenses                        | 9,548                      | 14,896             | 16,608                   | 51,763             |
| Other selling expenses                 | 11,483                     | 18,112             | 12,126                   | 25,693             |
| Total selling expenses                 | 444,994                    | 388,922            | 733,971                  | 863,812            |
| General and administrative expenses    |                            |                    |                          |                    |
| Payroll and employees benefits         | 67,185                     | 146,010            | 215,180                  | 272,774            |
| Insurance                              | 85,241                     | 72,182             | 187,810                  | 163,828            |
| Consultant fees                        | 64,770                     | 126,910            | 203,188                  | 287,724            |
| Professional fees                      | 29,638                     | 10,987             | 40,019                   | 16,860             |
| Research and development expenses      | 126,777                    | -                  | 287,375                  | -                  |
| Depreciation and amortization expenses | 35,751                     | 26,996             | 70,690                   | 53,304             |
| Taxes                                  | 52,733                     | 103,759            | 87,260                   | 103,759            |
| Office expenses                        | 130,437                    | 63,074             | 236,374                  | 261,015            |
| Travel and entertainment               | 80,013                     | 118,697            | 122,561                  | 152,682            |
|  | 11,192                     | 8,735              | 48,513                   | 54,738             |



Other general and  
administrative

|  |           |           |           |           |
|--|-----------|-----------|-----------|-----------|
| Total general and<br>administrative expenses | 683,737   | 677,350   | 1,498,970 | 1,366,684 |
| Total Operating Expenses                     | 1,128,731 | 1,066,272 | 2,232,941 | 2,230,496 |

|  |              |              |              |             |
|--|--------------|--------------|--------------|-------------|
| Income from Operations   | 1,828,989    | 1,673,130    | 3,979,418    | 3,519,113   |
| Other Income (Expense)   |              |              |              |             |
| Interest income  | 382,513      | 319,020      | 924,916      | 720,997     |
| Interest expense   | (483,531)    | (597,794)    | (1,249,082)  | (1,225,020) |
| Gain(Loss) on foreign currency transaction                               | 40,662       | 7,816        | (10,937)     | 7,816       |
| Loss on physical inventory count (Note 21)                               | (146,200)    | -            | (146,200)    | -           |
| Other income (expense)   | (21,527)     | 10,394       | (11,911)     | 8,225       |
| Total other income (expense)   | (228,083)    | (260,564)    | (493,214)    | (487,982)   |
| Income before Provision for Income Tax                                   | 1,600,906    | 1,412,566    | 3,486,204    | 3,031,131   |
| Provision for Income Tax   | 400,225      | 353,141      | 871,551      | 757,782     |
| Net Income   | 1,200,681    | 1,059,425    | 2,614,653    | 2,273,349   |
| Less: Net income attributable to noncontrolling interest                 | (12,007)     | (10,594)     | (26,147)     | (22,733)    |
| Net Income attributable to China Ruitai International Holdings Co., Ltd. | \$ 1,188,674 | \$ 1,048,831 | \$ 2,588,506 | 2,250,616   |

**See Notes to Consolidated Financial Statements**

**CHINA RUITAI INTERNATIONAL HOLDINGS CO., LTD. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

|  | For the Six Months Ended<br>June 30, |                                   |
|--|--------------------------------------|-----------------------------------|
|  | <u>2009</u><br><u>(unaudited)</u>    | <u>2008</u><br><u>(unaudited)</u> |
| <u>Operating Activities</u>  |                                      |                                   |
| Net income (loss)  | \$ 2,588,506                         | \$ 2,250,616                      |
| Adjustments to reconcile net income (loss)<br>to<br>net cash provided (used) by operating<br>activities: |                                      |                                   |
| Minority interest  | 26,147                               | 22,733                            |
| Depreciation   | 633,970                              | 503,881                           |
| Amortization of land use rights  | 53,500                               | 51,444                            |
| Amortization of contractual service<br>costs   | 165,978                              | 100,933                           |
| Changes in operating assets and liabilities:   |                                      |                                   |
| (Increase)/Decrease in bank checks and<br>commercial paper   | (778,556)                            | (97,771)                          |
| (Increase)/Decrease in accounts<br>receivable  | (1,793,548)                          | (1,323,644)                       |
| (Increase)/Decrease in prepaid expenses  | (342,323)                            | 562,884                           |
| (Increase)/Decrease in inventory   | 1,084,961                            | (3,289,699)                       |
| (Increase)/Decrease in advance to<br>employees   | (53,617)                             | (109,265)                         |
| Increase/(Decrease) in accounts payable<br>and accrued expenses  | 437,914                              | (1,144,563)                       |
| Increase/(Decrease) in bank checks<br>payable  | 10,229,087                           | 1,929,976                         |
| Increase/(Decrease) in taxes payable   | 358,439                              | 568,480                           |
| Increase/(Decrease) in deferred revenue  | 188,658                              | (512,898)                         |
| Increase/(Decrease) in employee<br>security deposit  | 44,414                               | 66,324                            |
| Net cash provided (used) by operating<br>activities  | 12,843,530                           | (420,569)                         |

Investing Activities

|   |             |             |
|---|-------------|-------------|
| Purchase of fixed assets                | (1,146,764) | (1,081,706) |
| Purchase of land use rights             | -           | (7,069)     |
| Loans to unaffiliated suppliers         | (170,770)   | (165,171)   |
| Loans to a related party                | (5,597,857) | -           |
| Payback of loans to a related party     |             | 1,475,634   |
| Net cash (used) by investing activities | (6,915,391) | 221,688     |

Financing Activities

|  |              |    |           |
|--|--------------|----|-----------|
| Bank loans   | 730,648      |    | 1,413,904 |
| Payback of bank loans  | -            |    | -         |
| Decrease (Increase) in restricted cash to secure bank checks payable | (10,082,958) |    | (459,510) |
| Loans from employees   | -            |    | 384,698   |
| Payback of loans from employees                                      | (38,566)     |    | -         |
| Net cash provided (used) by financing activities                     | (9,390,876)  |    | 1,339,092 |
| <br>   |              |    |           |
| Increase (decrease) in cash  | (3,462,737)  |    | 1,140,211 |
| Effects of exchange rates on cash                                    | 8,420        |    | 256,388   |
| Cash at beginning of period  | 5,319,456    |    | 4,166,713 |
| Cash at end of period  | \$ 1,865,139 | \$ | 5,563,312 |

Supplemental Disclosures of Cash Flow Information:

Cash paid (received) during year for:

|              |              |    |           |
|--------------|--------------|----|-----------|
| Interest     | \$ 1,249,083 | \$ | 1,140,679 |
| Income taxes | \$ 515,713   | \$ | 374,129   |

**See Notes to Consolidated Financial Statements.**

**CHINA RUITAI INTERNATIONAL HOLDINGS CO., LTD. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1-BASIS OF PRESENTATION**

The accompanying unaudited financial statements as of June 30, 2009 and for the three and six months ended June 30, 2009 and 2008 have been prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ) for interim financial information. They do not include all of the information and footnotes for complete financial statements as required by GAAP. In Management's opinion, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. The results of operations for the three and six months ended June 30, 2009 and 2008 presented are not necessarily indicative of the results to be expected for the full year. These financial statements should be read in conjunction with the Company's audited financial statements and notes thereto for the fiscal year ended December 31, 2008.

**Note 2-ORGANIZATION AND BUSINESS BACKGROUND**

China Ruitai International Holdings Co., Ltd. ("China Ruitai" or the "Company") was initially organized under the laws of the State of Delaware on November 15, 1955 as Inland Mineral Resources Corp. The Company subsequently changes its name to Parker-Levitt Corporation, and in 1997 changed its name to Commercial Property Corporation, and in 2006 changed its name to Shangdong Ruitai Chemical Co., Ltd. on March 12, 2007, the Company changed its name to China Ruitai International Holdings Co., Ltd. On February 26, 2007, the Company changed its fiscal year end from October 31 to December 31.

The Company was engaged in various real estate and development projects. The Company was not successful and discontinued the majority of its operations by 1981. On November 19, 1997, the Company issued common stock that resulted in a change in control and entered into a new development stage as defined in Statement of Financial Accounting Standards No. 7, "Accounting and Reporting by Development Stage Enterprises".

On August 29, 2007, the Company entered into a Share Exchange Agreement with Pacific Capital Group Co., Ltd., ( Pacific Capital Group ) a corporation incorporated under the laws of the Republic of Vanuatu, and the stockholders of Pacific Capital Group (the Stockholders ). Pursuant to the terms of the Share Exchange Agreement, the Stockholders agreed to transfer all of the issued and outstanding shares of common stock in Pacific Capital Group to the Company in exchange for the issuance of an aggregate of 22,645,348 shares of the Company's common stock to the Stockholders, thereby causing Pacific Capital Group and Pacific Capital Group's majority-owned operating subsidiary,

TaiAn RuiTai Cellulose Co., Ltd. ( TaiAn ), a Chinese limited liability company, to become wholly-owned and majority owned-subsiidiaries, respectively of the Company. The parties closed the share exchange contemplated by the Share Exchange Agreement on November 8, 2007.

The Share Exchange is being accounted for as a reverse merger, since the stockholders of Pacific Capital Group own a majority of the outstanding shares of the Company s common stock immediately following the Share Exchange. Pacific Capital Group is deemed to be the acquirer in the reverse merger. Consequently, the assets and liabilities and the historical operations that will be reflected in the financial statements for periods prior to the Share Exchange will be those of Pacific Capital Group and its subsidiary and will be recorded at the historical cost basis. After completion of the Share Exchange, the Company s consolidated financial statements will include the assets and liabilities of both China Ruitai and Pacific Capital Group, the historical operations of Pacific Capital Group and the operations of the Company and its subsidiaries from

the closing date of the Share Exchange.

Pacific Capital Group was incorporated on November 23, 2006 under the laws of the Republic of Vanuatu as a holding company, for the purposes of seeking and consummating a merger or acquisition with a business entity. On April 26, 2007, following the approval by the relevant governmental authorities in the PRC, Pacific Capital Group acquired a 99% ownership interest in TaiAn, which was formed in the PRC on November 10, 1999. As a result of the transaction, TaiAn became a majority-owned subsidiary of Pacific Capital Group.

TaiAn is the only one of these affiliated companies that is engaged in business operations. China RuiTai and Pacific Capital Group are holding companies, whose business is to hold an equity ownership interest in TaiAn. TaiAn is engaged in the production, sales, and exportation of deeply processed chemicals, with a primary focus on non-ionic cellulose ether products. TaiAn's assets exist solely in the PRC, and its revenues are derived from its operations therein.

China Ruitai, Pacific Capital Group, and TaiAn are hereafter referred to as the Company.

### **Note 3-CONTROL BY PRINCIPAL OWNERS**

The directors, executive officers, their affiliates, and related parties own, directly or indirectly, beneficially and in the aggregate, the majority of the voting power of the outstanding capital of the Company. Accordingly, directors, executive officers and their affiliates, if they voted their shares uniformly, would have the ability to control the approval of most corporate actions, including approving significant expenses, increasing the authorized capital and the dissolution, merger or sale of the Company's assets.

### **Note 4-SIGNIFICANT ACCOUNTING POLICIES**

#### **Basis of consolidation**

The consolidated financial statements include the accounts of the Company and all its majority-owned subsidiaries which require consolidation. Inter-company transactions have been eliminated in consolidation.

The consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States of America ("US GAAP"). This basis of accounting differs from that used in the statutory accounts of



the Company, which are prepared in accordance with the "Accounting Principles of China " ("PRC GAAP"). Certain accounting principles, which are stipulated by US GAAP, are not applicable in the PRC GAAP. The difference between PRC GAAP accounts of the Company and its US GAAP financial statements is immaterial.

### **Foreign Currencies Translation**

The Company maintains its books and accounting records in PRC currency "Renminbi" ("RMB"), which is determined as the functional currency. Transactions denominated in currencies other than RMB are translated into RMB at the exchange rates quoted by the People's Bank of China ( PBOC ) prevailing at the date of the transactions. Monetary assets and liabilities denominated in currencies other than RMB are translated into RMB using the applicable exchange rates quoted by the PBOC at the balance sheet dates. Exchange differences are included in the statements of changes in owners' equity. Gain and losses resulting from foreign currency transactions are included in operations.

The Company's financial statements are translated into the reporting currency, the United States Dollar ( US\$ ). Assets and liabilities of the Company are translated at the prevailing exchange rate at each

reporting period end. Contributed capital accounts are translated using the historical rate of exchange when capital is injected. Income and expense accounts are translated at the average rate of exchange during the reporting period. Translation adjustments resulting from translation of these financial statements are reflected as accumulated other comprehensive income (loss) in the owners' equity.

### **Foreign Currencies Translation (continued)**

Translation adjustments resulting from this process are included in accumulated other comprehensive income (loss) in the consolidated statement of changes in shareholders' equity and amounted to \$1,325,694 as of June 30, 2009, and \$1,304,357 as of December 31, 2008. The balance sheet amounts with the exception of equity at June 30, 2009 were translated at 6.84 RMB to \$1.00 USD as compared to 6.85 RMB at December 31, 2008. The equity accounts were stated at their historical rate. The average translation rates applied to income statement accounts for the six months ended June 30, 2009 and 2008 were 6.84 RMB and 7.07 RMB, respectively.

### **Statement of Cash Flows**

In accordance with SFAS No. 95, Statement of Cash Flows, cash flows from the Company's operations is calculated based upon the functional currency. As a result, amounts related to assets and liabilities reported on the statement of cash flows may not necessarily agree with changes in the corresponding balances on the balance sheet.

### **Revenue Recognition**

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to unaffiliated customer or picked up by unaffiliated customers in the Company's warehouse, title and risk of loss have been transferred, collectability is reasonably assured and pricing is fixed or determinable. The corresponding freight-out and handling costs are included in the selling expenses.

### **Deferred Revenue**

Deferred revenue consists of prepayments to the Company for products that have not yet been delivered to the customers. Payments received prior to satisfying the Company's revenue recognition criteria are recorded as deferred revenue.

### **Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results when ultimately realized could differ from those estimates.

### **Fair Value of Measurements**

The Company adopted Statement of Financial Accounting Standards No. 157, Fair Value Measurements ( SFAS 157 ), effective January 1, 2008. The provisions of SFAS 157 are to be applied prospectively.

SFAS 157 clarifies that fair value is an estimate of the exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants

(i.e., the exit price at the measurement date). Under SFAS 157, fair value measurements are not adjusted for transaction cost. SFAS 157 provides for use of a fair value hierarchy that prioritizes inputs to valuation techniques used to measure fair value into three levels:

**Level 1:**

Unadjusted quoted prices in active markets for identical assets or liabilities

**Level 2:**

Input other than quoted market prices that are observable, either directly or indirectly, and reasonably available. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability and are developed based on market data obtained from sources independent of the Company.

**Level 3:**

Unobservable inputs. Unobservable inputs reflect the assumptions that the Company develops based on available information about what market participants would use in valuing the asset or liability.

An asset or liability's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Availability of observable inputs can vary and is affected by a variety of factors. The Company uses judgment in determining fair value of assets and liabilities and Level 3 assets and liabilities involve greater judgment than Level 1 and Level 2 assets or liabilities.

**Subsequent Events**

The Company evaluated subsequent events through the time of filing this Quarterly Report on Form 10-Q on August 14, 2009. We are not aware of any significant events that occurred subsequent to the balance sheet date but prior to the filing of this report that would have a material impact on our financial statements.

**Cash and Cash Equivalents**

Cash and cash equivalents include cash on hand, deposits in banks with maturities of three months or less, and all highly liquid investments which are unrestricted as to withdrawal or use, and which have original maturities of three months or less at the time of purchase.

### **Bank checks and commercial paper**

Bank checks and commercial paper include bank checks and commercial paper with original maturities of approximately 180 days or less at the time of issuance. Book value approximates fair value because of the short maturity of those instruments. The Company receives these financial instruments as payments from its customers in the ordinary course of business.

### **Accounts Receivable**

Accounts receivable are recorded at the invoiced amount and do not bear interest. We generally grant new customers a one-month period in which to pay for goods that we have delivered to them, and we grant existing customers a two to three month period in which to pay for goods that we have delivered to them. We used an indirect method of accounting to write off any accounts receivable which exceeded the allotted three month time period which we provide to our customers. In circumstances in which we receive payment for accounts receivable which have previously been written off, we reverse the allowance and bad debt expenses.

### **Concentrations of Credit Risk**

Financial instruments that subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents. The Company maintains its cash and cash equivalents with high-quality institutions. Deposits held with banks may exceed the amount of insurance provided on such deposits. Generally these deposits may be redeemed upon demand and therefore bear minimal risk.

### **Fair Value of Financial Instruments**

The carrying value of financial instruments including cash and cash equivalents, bank checks and commercial paper, receivables, accounts payable and accrued expenses, approximates their fair value due to the relatively short-term nature of these instruments.

### **Inventory**

Inventories are stated at the lower of cost or market value. Actual cost is used to value raw materials and supplies. Finished goods and work-in-progress are valued on the weighted-average-cost method. Elements of costs in finished good and work-in-progress include raw materials, direct labor, and manufacturing overhead.

### **Due from unaffiliated suppliers**

The Company has been extending temporally short-term loans to some unaffiliated suppliers. These loans are unsecured, non-interest bearing and have no fixed terms of repayment, therefore, deemed payable on demand. Cash flows from due from unaffiliated suppliers are classified as cash flows from investing activities.

The Management believes the loans can help theses suppliers run their business, and in turn these suppliers can provide raw materials and services to the Company in a stable price. The Managements evaluates the financial resources of the borrowers on a regular basis, to make sure the suppliers have the capability to pay back these loans. Also, the Company has never had any bad debt with these suppliers. Therefore, the Management believes that these loans are collectable.

### **Long-term investment**

The long-term investment represents monetary investments in the Wenyang Xinyong Bank, a local state owned bank in Wenyang County, Shandong Province, PRC. The investments are transferable in accordance with the laws of the PRC. The investments are carried at cost which approximates fair value. The Company did not purchase any such long-term investment in the six months ended June 30, 2009 and 2008, respectively. Dividend income on these investments is recorded when received. There were no dividend received in the six months ended June 30, 2009 and 2008, respectively. The Company may sell these investments back to the bank at the book value.

### **Valuation of Long-Lived assets**

The Company accounts for impairment of plant and equipment and amortizable intangible assets in accordance with SFAS No. 144, Accounting for Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed Of . Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be

recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

### **Restricted cash, and Bank checks payable**

The Company pays its suppliers with bank checks in its ordinary business transactions. Generally, the Company deposits 40% to 100% of the bank check amount into a restricted bank account, the bank then issues a bank check payable to a supplier in 180 days or less. The Company delivers the bank check as payment to the supplier, who can discount the bank check before its maturity. When the bank check reaches maturity, the bank pays the check using funds from the restricted bank accounts and the balance, if any, from other bank account(s) that the Company has with the bank. While the bank does not charge interest expenses on the balance, the bank pays interest on the deposit in the restricted bank account to the Company. The bank generally charges 0.0005% of the bank check amount as service fee for issuance of the bank check. The Company also takes out bank checks to make loans to Shandong Ruitai as disclosed more fully in Note 15.

### **Property, Plant and Equipment**

Property, plant and equipment are carried at cost. Maintenance, repairs and minor renewals are expensed as incurred; major renewals and improvements that extend the lives or increase the capacity of plant assets are capitalized.

When assets are retired or disposed of, the cost and accumulated depreciation are removed from the accounts, and any resulting gains or losses are included in income in the reporting period of disposition.

Depreciation is calculated on a straight-line basis over the estimated useful life of the assets without residual value. The percentages or depreciable life applied are:

|                                |               |
|--------------------------------|---------------|
| Building and warehouses        | 20 years      |
| Machinery and equipment        | 7 to 10 years |
| Office equipment and furniture | 5 years       |
| Motor vehicles                 | 5 years       |

### **Land Use Right**



All land belongs to the State in PRC. Enterprises and individuals can pay the State a fee to obtain a right to use a piece of land for commercial purpose or residential purpose for an initial period of 50 years or 70 years, respectively. The land use right can be sold, purchased, and exchanged in the market. The successor owner of the land use right will reduce the amount of time which has been consumed by the predecessor owner.

The Company owns the right to use a piece of land, approximately 23 acre, located in the Wenyang County, Shandong Province for a fifty-year period ended December 2, 2055; and a piece of land, approximately 36 acre, also located in the Wenyang County, Shanxi Province for a forty-eight-year period ended June 5, 2054. The costs of these land use rights are amortized over their prospective beneficial period, using the straight-line method with no residual value. The Company's production facilities and headquarters building are located in these two pieces of land.

### **Government Subsidies**

The Company records government grants as current liabilities upon reception. A government subsidy

revenue is recognized only when there is reasonable assurance that the Company has complied with all conditions attached to the grant. The Company did not recognize government subsidy revenue for the six months ended June 30, 2009 and 2008, respectively.

### **Research and Development Costs**

Research and development costs relating to the development of new products and processes, including significant improvements and refinements to existing products, are expensed when incurred. The major components of these research and development costs include experimental materials and labor costs. The research and development cost was immaterial in the six months ended June 30, 2008, and was included into other general and administration expenses. The research and development cost was \$287,375 for the six months ended June 30, 2009, which principally included materials used in developing new products.

### **Advertising Costs**

Advertising costs are expensed as incurred and included as part of selling and marketing expenses in accordance with the American Institute of Certified Public Accountants ("AICPA") Statement of Position 93-7, "Reporting for Advertising Costs". Advertising costs was \$26,019 and \$17,433 for the six months ended June 30, 2009 and 2008, respectively.

### **Value-added Tax (VAT)**

Sales revenue represents the invoiced value of goods, net of a value-added tax (VAT). All of the Company's products that are sold in PRC are subject to a Chinese value-added tax at a rate of 17% of the gross sales price or at a rate approved by the Chinese local government. This VAT may be offset by VAT paid on purchase of raw materials included in the cost of producing the finished goods.

### **Comprehensive Income**

Statement of Financial Accounting Standards (SFAS) No. 130, Reporting Comprehensive Income, establishes standards for reporting and display of comprehensive income, its components and accumulated balances. Comprehensive income as defined includes all changes in equity during a period from non-owner sources. Accumulated comprehensive income, as presented in the accompanying statements of changes in owners' equity consists of changes in unrealized gains and losses on foreign currency translation. This comprehensive income is not included in the computation of income tax expense or benefit.

### **Segment Reporting**

SFAS No. 131 Disclosures about Segments of an Enterprise and Related Information establishes standards for reporting information about operating segments on a basis consistent with the Company's internal organization structure as well as information about geographical areas, business segments and major customers in financial statements. The Company currently operates in one principal business segment.

### **Related parties**

For the purposes of these financial statements, parties are considered to be related if one party has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Company and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

## **Pension and Employee Benefits**

Full time employees of the PRC entities participate in a government mandated multi-employer defined contribution plan pursuant to which certain pension benefits, medical care, unemployment insurance, employee housing fund and other welfare benefits are provided to employees. Chinese labor regulations require the Company to accrue for these benefits based on certain percentages of the employees' salaries. The Management believes full time employees who have passed the probation period are entitled to such benefits. The total provisions for such employee benefits was \$34,085, and \$55,643 for the six months ended June 30, 2009 and 2008, respectively.

## **Statutory Reserves**

Pursuant to the applicable laws in PRC, PRC entities are required to make appropriations to three non-distributable reserve funds, the statutory surplus reserve, statutory public welfare fund, and discretionary surplus reserve, based on after-tax net earnings as determined in accordance with the PRC GAAP, after offsetting any prior years' losses. Appropriation to the statutory surplus reserve should be at least 10% of the after-tax net earnings until the reserve is equal to 50% of the Company's registered capital. Appropriation to the statutory public welfare fund is 5% to 10% of the after-tax net earnings. The statutory public welfare fund is established for the purpose of providing employee facilities and other collective benefits to the employees and is non-distributable other than in liquidation. No appropriations to the discretionary surplus reserve are made at the discretion of the Board of Directors.

The Company's operating subsidiary, TaiAn has made appropriations to its statutory reserves up to 50% of its registered capital as of December 31, 2008. Therefore, TaiAn is not required to make appropriations to its statutory reserves any more.

## **Income Taxes**

The Company accounts for income tax using SFAS No. 109 "Accounting for Income Taxes", which requires the asset and liability approach for financial accounting and reporting for income taxes. Under this approach, deferred income taxes are provided for the estimated future tax effects attributable to temporary differences between financial statement carrying amounts of assets and liabilities and their respective tax bases, and for the expected future tax benefits from loss carry-forwards and provisions, if any. Deferred tax assets and liabilities are measured using the enacted tax rates expected in the years of recovery or reversal and the effect from a change in tax rates is recognized in the statement of operations in the period of enactment. A valuation allowance is provided to reduce the amount of deferred tax assets if it is considered more likely than not that some portion of, or all of the deferred tax assets will not be realized.

The Company accounts for income taxes in interim periods as required by Accounting Principles Board Opinion No. 28 "Interim Financial Reporting" and as interpreted by FASB Interpretation No. 18, "Accounting for Income Taxes in Interim Periods". The Company has determined an estimated annual effective tax rate. The rate will be revised, if

necessary, as of the end of each successive interim period during the Company's fiscal year to its best current estimate.

The estimated annual effective tax rate is applied to the year-to-date ordinary income (or loss) at the end of the interim period.

### **Earnings (Loss) Per Share**

The Company reports earnings per share in accordance with the provisions of SFAS No. 128, Earnings Per Share. SFAS No. 128 requires presentation of basic and diluted earnings per share in conjunction with the

disclosure of the methodology used in computing such earnings per share. Basic earnings (loss) per share is computed by dividing income (loss) available to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted earnings per share is computed similar to basic earnings per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. There are 350,000 shares and 275,000 shares of warrants issued and outstanding as of June 30, 2009 and 2008, respectively, as more fully disclosed in Note 19.

#### **Adoption of FIN 48**

Effective January 1, 2007, the Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on de-recognition of tax benefits, classification on the balance sheet, interest and penalties, accounting in interim periods, disclosure, and transition. In accordance with FIN 48, the Company performed a self-assessment and concluded that there were no significant uncertain tax positions requiring recognition in its financial statements.

#### **Adoption of SFAS No. 157**

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, "Fair Value Measurements". SFAS No. 157 defines fair value, establishes a framework and gives guidance regarding the methods used for measuring fair value, and expands disclosures about fair value measurements. In February 2008, the FASB issued FASB Staff Position 157-1, "Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13" ("FSP 157-1") and FASB Staff Position 157-2, "Effective Date of FASB Statement No. 157" ("FSP 157-2"). FSP 157-1 amends SFAS No. 157 to remove certain leasing transactions from its scope. FSP 157-2 delays the effective date of SFAS No. 157 for all non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), until fiscal years beginning after November 15, 2008. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company adopted SFAS No. 157 effective January 1, 2008 for all financial assets and liabilities as required, and effective January 1, 2009 for all non-financial assets and non-financial liabilities as allowed by FSP FAS 157-2. The adoption of SFAS No. 157 did not have a material impact on the Company's financial position and results of operations.

On October 10, 2008, the FASB issued FSP FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active. The FSP clarifies the application of FASB Statement No. 157, Fair Value Measurements, in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. The FSP is effective

immediately, and includes prior period financial statements that have not yet been issued.

**Adoption of SFAS No. 159**

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115, which is effective for fiscal years beginning after November 15, 2007. SFAS No. 159 is an elective standard which permits an entity to

choose to measure many financial instruments and certain other items at fair value at specified election dates. Subsequent unrealized gains and losses on items for which the fair value option has been elected will be reported in earnings. The Company did not elect the fair value option for any assets or liabilities that were not previously carried at fair value. Accordingly, the adoption of SFAS 159 did not have a material impact on the Company's financial position and results of operations.

#### **Adoption of SFAS No. 160 and SFAS 141R**

In December 2007, the FASB issued Statements of Financial Accounting Standards No. 141 (revised 2007), Business Combinations ( SFAS 141R ) and No. 160, Noncontrolling Interests in Consolidated Financial Statements (an amendment to ARB No. 51 ( SFAS 160 )). Both SFAS 141R and SFAS 160 are to be adopted effective January 1, 2009. SFAS 141R requires the application of several new or modified accounting concepts that, due to their complexity, could introduce a degree of volatility in periods subsequent to a material business combination. SFAS 141R requires that all business combinations result in assets and liabilities acquired being recorded at their fair value, with limited exceptions. Other areas related to business combinations that will require changes from current GAAP include: contingent consideration, acquisition costs, contingencies, restructuring costs, in process research and development and income taxes, among others. SFAS 160 will primarily impact the presentation of minority or noncontrolling interests within the Balance Sheet and Statement of Operations as well as the accounting for transactions with noncontrolling interest holders. The Company adopted SFAS No. 141 (revised 2007) and SFAS No. 160 on January 1, 2009. The adoption of these statements principally affects the presentation of the accompanying consolidated financial statements upon adoption, and the effects on future periods will depend on the nature and significance of business combinations subject to these statements.

#### **Adoption of SFAS No. 161**

In March 2008, the FASB issued Statement of Financial Accounting Standards No. 161, Disclosures about Derivative Hedging Instruments and Hedging Activities (an amendment of FASB Statement No. 133 ( SFAS 161 )). SFAS 161, which is effective January 1, 2009, requires enhanced qualitative and quantitative disclosures with respect to derivatives and hedging activities. The adoption of SFAS No. 161 did not have a material effect on the Company's financial position and results of operations.

#### **Adoption of FSP FAS 142-3**

In April 2008, the FASB issued Staff Position FAS 142-3, Determination of the Useful Life of Intangible Assets ( FSP FAS 142-3 ) which amends the factors an entity should consider in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FAS No. 142, Goodwill and Other Intangible Assets ( FAS No. 142 ). FSP FAS 142-3 applies to intangible assets that are acquired individually or with a group of assets and intangible assets acquired in both business combinations and asset acquisitions. It removes a provision under FAS No. 142, requiring an entity to consider whether a contractual renewal or extension clause can be accomplished without



substantial cost or material modifications of the existing terms and conditions associated with the asset. Instead, FSP FAS 142-3 requires that an entity consider its own experience in renewing similar arrangements. An entity would consider market participant assumptions regarding renewal if no such relevant experience exists. FSP FAS 142-3 is effective for year ends beginning after December 15, 2008 with early adoption prohibited. The adoption of FSP FAS 142-3 did not have a material effect on the Company's financial position and results of operations.

**Adoption of FSP No. EITF 03-6-1**

In June 2008, the Financial Accounting Standards Board ( FASB ) issued FSP No. EITF 03-6-1,

Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities ( FSP EITF 03-6-1 ). FSP EITF 03-6-1 concludes that unvested share-based payment awards that contain rights to receive non-forfeitable dividends or dividend equivalents are participating securities, and thus, should be included in the two-class method of computing earnings per share ( EPS ). FSP EITF 03-6-1 is effective for fiscal years beginning after December 15, 2008, and interim periods within those years. Early application of EITF 03-6-1 is prohibited. It also requires that all prior-period EPS data be adjusted retrospectively. The adoption of FSP No. EITF 03-6-1 did not have a material effect on the Company's financial position and results of operations.

### **Recent Accounting Pronouncements**

In June 2009, the FASB issued SFAS No. 168, "The FASB Accounting Standards Codification (the "Codification"). The Codification will become the source of authoritative U.S. generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission (SEC) under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of this Statement, the Codification will supersede all then-existing non-SEC accounting and reporting standards. All other non-grandfathered non-SEC accounting literature not included in the Codification will become nonauthoritative. This Statement is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Management does not expect that the adoption of SFAS No. 168 would have a material effect on the Company's financial position and results of operations.

In June 2009, the FASB issued SFAS No. 167, "Amendments to FASB Interpretation No. 46(R)." SFAS No. 167, among other things, requires a qualitative rather than a quantitative analysis to determine the primary beneficiary of a variable interest entity ("VIE"); requires continuous assessments of whether an enterprise is the primary beneficiary of a VIE; enhances disclosures about an enterprise's involvement with a VIE; and amends certain guidance for determining whether an entity is a VIE. Under SFAS No. 167, a VIE must be consolidated if the enterprise has both (a) the power to direct the activities of the VIE that most significantly impact the entity's economic performance, and (b) the obligation to absorb losses or the right to receive benefits from the VIE that could potentially be significant to the VIE. SFAS No. 167 will be effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, and for interim periods within that first annual reporting period. Earlier application is prohibited. The Management does not expect that the adoption of SFAS No. 167 would have a material effect on the Company's financial position and results of operations.

In June, 2009, the FASB issued SFAS No. 166, "Accounting for Transfers of Financial Assets". SFAS No. 166 is a revision to FASB SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities", and requires more information about transfers of financial assets, including securitization transactions, and where companies have continuing exposure to the risks related to transferred financial assets. SFAS No. 166 also eliminates the concept of a "qualifying special-purpose entity", changes the requirements for derecognizing financial assets and requires additional disclosures. FASB No. 166 must be applied as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, and for interim periods within that first annual reporting period. Earlier application is prohibited. The Management does not expect that the adoption of SFAS No. 166 would have a material effect on the Company's financial position and results of operations.

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events." SFAS No. 165 establishes authoritative accounting and disclosure guidance for recognized and non-recognized subsequent events that occur after the balance sheet date but before financial statements are issued. SFAS No. 165 also requires disclosure of the date through which an entity has evaluated subsequent events and the basis for that date. In accordance with this Statement, an entity should apply the requirements to interim or annual financial

periods ending after June 15, 2009. The adoption of SFAS No. 165 had no material impact on the Company's financial position and results of operations.

In April 2009, the FASB issued FSP FAS 141(R)-1, Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies. This FSP requires that assets acquired and liabilities assumed in a business combination that arise from contingencies be recognized at fair value if fair value can be reasonably estimated. If fair value cannot be reasonably estimated, the asset or liability would generally be recognized in accordance with SFAS No. 5, Accounting for Contingencies and FASB Interpretation No. 14, Reasonable Estimation of the Amount of a Loss. Further, the FASB removed the subsequent accounting guidance for assets and liabilities arising from contingencies from SFAS No. 141(R). The requirements of this FSP carry forward without significant revision the guidance on contingencies of SFAS No. 141, Business Combinations, which was superseded by SFAS No. 141(R). The FSP also eliminates the requirement to disclose an estimate of the range of possible outcomes of recognized contingencies at the acquisition date. For unrecognized contingencies, the FASB requires that entities include only the disclosures required by SFAS No. 5. This FSP was adopted effective January 1, 2009. There was no impact upon adoption, and its effects on future periods will depend on the nature and significance of business combinations subject to this statement.

In April 2009, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) Financial Accounting Standard (FAS) 157-4 Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly. Based on the guidance, if an entity determines that the level of activity for an asset or liability has significantly decreased and that a transaction is not orderly, further analysis of transactions or quoted prices is needed, and a significant adjustment to the transaction or quoted prices may be necessary to estimate fair value in accordance with Statement of Financial Accounting Standards (SFAS) No. 157 Fair Value Measurements. This FSP is to be applied prospectively and is effective for interim and annual periods ending after June 15, 2009 with early adoption permitted for periods ending after March 15, 2009. The adoption of this FSP did not have a material effect on the Company's financial position and results of operations.

In April 2009, the FASB issued FSP FAS 115-2 and FAS 124-2 Recognition and Presentation of Other-Than-Temporary Impairments. The guidance applies to investments in debt securities for which other-than-temporary impairments may be recorded. If an entity's management asserts that it does not have the intent to sell a debt security and it is more likely than not that it will not have to sell the security before recovery of its cost basis, then an entity may separate other-than-temporary impairments into two components: 1) the amount related to credit losses (recorded in earnings), and 2) all other amounts (recorded in other comprehensive income). This FSP is to be applied prospectively and is effective for interim and annual periods ending after June 15, 2009 with early adoption permitted for periods ending after March 15, 2009. The adoption of this FSP did not have a material effect on the Company's financial position and results of operations.

In April 2009, the FASB issued FSP FAS 107-1 and Accounting Principles Board (APB) 28-1 Interim Disclosures about Fair Value of Financial Instruments. The FSP amends SFAS No. 107 Disclosures about Fair Value of Financial Instruments to require an entity to provide disclosures about fair value of financial instruments in interim financial information. This FSP is to be applied prospectively and is effective for interim and annual periods ending after June 15, 2009 with early adoption permitted for periods ending after March 15, 2009. The Company will adopt this FSP for

its quarter ending June 30, 2009. The adoption of this FSP did not have a material effect on the Company's financial position and results of operations.

**Note 5-ACCOUNTS RECEIVABLE**

Accounts receivable consists of the following:

|                                       | June 30,<br><u>2009</u><br><u>(unaudited)</u> | December 31,<br><u>2008</u> |
|---------------------------------------|---|-----------------------------|
| Accounts receivable                   | \$ 6,697,697                                  | \$ 4,867,649                |
| Less: Allowance for doubtful accounts | (1,604,786)                                   | (1,572,308)                 |
| Accounts receivable, net              | \$ 5,092,911                                  | \$ 3,295,341                |

Bad debt expense charged to operations was \$30,369 and \$0 for the six months ended June 30, 2009 and 2008, respectively.

**Note 6-DUE FROM UNAFFILIATED SUPPLIERS**

Due from unaffiliated suppliers consist of following:

|                                      | June 30,<br><u>2009</u><br><u>(unaudited)</u> | December 31,<br><u>2008</u> |
|--------------------------------------|---|-----------------------------|
| Fengcheng Yingbo Food Co., Ltd.      | \$ 292,193                                    | \$ 291,800                  |
| Shangdong Ashide Chemicals Co., Ltd. | 73,048  | -                           |
| Other companies                      | 152,933                                       | 55,176                      |
|                                      | \$ 518,174                                    | \$ 346,976                  |

**Note 7-PREPAID EXPENSES**

Prepaid expenses consist of following:

| June 30,<br><u>2009</u> | December 31,<br><u>2008</u> |
|-------------------------|-----------------------------|
|-------------------------|-----------------------------|

(unaudited)

|                              |    |           |    |           |
|------------------------------|----|-----------|----|-----------|
| Machinery and parts          | \$ | 205,752   | \$ | 308,325   |
| Raw materials and supplies   |    | 2,268,707 |    | 1,811,725 |
| Packing and supply materials |    | 1,325     |    | 1,610     |
| Freight-out                  |    | 13,872    |    | 1,268     |
| Consultancy fees             |    | 159,430   |    | 207,123   |
| Office expenses              |    | 27,193    |    | 847       |
|                              | \$ | 2,676,279 | \$ | 2,330,898 |

**Note 8-INVENTORIES**

Inventories consist of following:

|                                | June 30,<br><u>2009</u><br><u>(unaudited)</u> | December 31,<br><u>2008</u> |
|--------------------------------|---|-----------------------------|
| Finished goods                 | \$ 4,320,495                                  | \$ 5,492,366                |
| Work-in-progress               | 1,079,998                                     | 1,044,048                   |
| Raw materials                  | 1,562,022                                     | 1,576,534                   |
| Supplies and packing materials | 121,341                                       | 44,644                      |
|                                | \$ 7,083,856                                  | \$ 8,157,592                |

**Note 9-PROPERTY, PLANT AND EQUIPMENT**

The following is a summary of property, plant and equipment:

|                                | June 30,<br><u>2009</u><br><u>(unaudited)</u> | December 31,<br><u>2008</u> |
|--------------------------------|---|-----------------------------|
| Building and warehouses        | \$ 7,910,798                                  | \$ 7,835,356                |
| Machinery and equipment        | 9,541,570                                     | 8,743,251                   |
| Office equipment and furniture | 71,730  | 63,597                      |
| Motor vehicles                 | 464,554                                       | 463,928                     |
|                                | 17,988,652                                    | 17,106,132                  |
| Less: Accumulated depreciation | (4,954,466)                                   | (4,315,364)                 |
| Add: Construction in progress  | 433,093                                       | 145,900                     |
| Total                          | \$ 13,467,279                                 | \$ 12,936,668               |



Depreciation expense charged to operations was \$633,970 and \$503,881 for the six months ended June 30, 2009 and 2008, respectively.

**Note 10-LAND USE RIGHT**

The following is a summary of land use right, less amortization:

| June 30,<br><u>2009</u><br><u>(unaudited)</u> | December 31,<br><u>2008</u> |
|---|-----------------------------|
|---|-----------------------------|

|                     |    |           |    |           |
|---------------------|----|-----------|----|-----------|
| Land use right      | \$ | 5,403,946 | \$ | 5,396,684 |
| Less: Amortization  |    | (366,627) |    | (312,169) |
| Land use right, net | \$ | 5,037,319 | \$ | 5,084,515 |

Amortization expense charged to operations was \$53,500 and \$51,444 for the six months ended June 30, 2009 and 2008, respectively.

#### Note 11-RESTRICTED CASH

Restricted cash consists of following:

| <u>Financial Institutions</u>                     | June 30,<br><u>2009</u><br><u>(unaudited)</u> | December 31,<br><u>2008</u> |
|---|---|-----------------------------|
| Jinan Branch of Shanghai Pudong Development Bank  | \$ 4,382,889                                  | \$ 4,377,000                |
| Feicheng Branch of Bank of China                  | 5,989,949                                     | 1,459,000                   |
| Wenyang Branch of Agriculture Bank                |   | 1,750,800                   |
| Feichang Branch of Agriculture Bank               | 1,460,963                                     | -                           |
| Wenyang Credit Bank                               | 3,506,311                                     | 3,501,600                   |
| Feicheng Branch of Construction Bank              | 4,382,889                                     | -                           |
| Feicheng Branch of Transportation Bank            | 3,652,408                                     | 2,188,500                   |
| Jinan Wendong Branch of Shenzhen Development Bank | 5,843,852                                     | 5,836,000                   |
|   | \$ 29,219,261                                 | \$ 19,112,900               |

#### Note 12-BANK CHECKS PAYABLE

Bank checks payable consists of following:

|          |              |
|----------|--------------|
| June 30, | December 31, |
|----------|--------------|

| <u>Financial Institutions</u>                     | <u>2009</u><br><u>(unaudited)</u> | <u>2008</u>   |
|---|-----------------------------------|---------------|
| Feicheng Branch of Bank of China                  | \$ 9,496,260                      | \$ 2,918,000  |
| Feicheng Branch of Transportation Bank            | 5,113,371                         | 4,377,000     |
| Wenyang Credit Bank                               | 5,843,852                         | 5,836,000     |
| Jinan Branch of Shanghai Pudong Development Bank  | 4,382,889                         | 4,377,000     |
| Feicheng Branch of Construction Bank              | 4,382,889                         | -             |
| Wenyang Branch of Agriculture Bank                | 1,460,963                         | 2,918,000     |
| Jinan Wendong Branch of Shenzhen Development Bank | 8,765,778                         | 8,754,000     |
|   | \$ 39,446,002                     | \$ 29,180,000 |

**Note 13-INTEREST INCOME**

Interest income consists of following:

|  | For the Six Months Ended                      |   |
|--|---|---|
|  | June 30,<br><u>2009</u><br><u>(unaudited)</u> | June 30,<br><u>2008</u><br><u>(unaudited)</u> |
| Imputed interest income from loans to Shangdong Ruitai | \$ 747,526                                    | \$ 502,282                                    |
| Interest income from deposits in banks                 | 176,456                                       | 218,715                                       |
| Other interest income                                  | 934   | -   |
|  | \$ 924,916                                    | \$ 720,997                                    |

**Note 14-INTEREST EXPENSES**

Interest expenses consist of following:

|   | For the Six Months Ended                      |   |
|---|---|---|
|   | June 30,<br><u>2009</u><br><u>(unaudited)</u> | June 30,<br><u>2008</u><br><u>(unaudited)</u> |
| Interest expenses for bank loans              | \$ 768,932                                    | \$ 851,726                                    |
| Interest expenses for discount on bank checks | 410,932                                       | 289,379                                       |
| Interest expenses for due to employees        | 69,218  | 83,915  |
|   | \$ 1,249,082                                  | \$ 1,225,020                                  |

**Note 15-RELATED PARTY TRANSACTIONS****Purchase from a related party**

TaiAn purchases hot steam from Shandong Ruitai' power plant. Hot steam is one of the major raw materials for TaiAn's production and TaiAn records the costs of hot steam into its manufacturing costs. The Management believes the transaction is on terms no less favorable to the Company than those reasonably obtainable from third parties. TaiAn purchased hot steam of \$1,380,488 and \$978,653 from Shandong Ruitai in the six months ended June 30, 2009 and 2008, respectively.

### **Due to employees**

Due to Employees represents loans from employees to finance the Company's operations due to a lack of cash resources. There are no formal loan agreements for these loans, therefore, these loans were unsecured, and have no fixed terms of repayment. The employees can inject or withdraw funds as they wish. The Company pays 6% interest on these loans monthly for the period July 1, 2007 through March 31, 2009. Beginning from April 1, 2009, the Company pays 5% interest on these loans monthly. Cash flows from these activities are classified as cash flows from financing activities. The Company paid interest of \$69,218

and \$83,915 for the six months ended June 30, 2009 and 2008, respectively.

### **Advance to employees**

Advance to employee are advances to employees who are working on projects on behalf of the Company. After the work is finished, they will submit expense reports with supporting documents to the accounting department. Then, the expenses are debited into the relevant accounts and the advances are credited out. Cash flows from these activities are classified as cash flows from operating activities.

### **Due from a related party**

Due from a related party" represents loans to Shandong Ruitai Chemicals Co., Ltd. ("Shandong Ruitai"), then a majority owner of TaiAn. Shandong Ruitai had owned 75% equity ownership interest of TaiAn January 2000 through February 2007. On March 20, 2007, Shandong Ruitai sold 74% equity ownership interest of TaiAn to Pacific Capital Group Co., Ltd. Mr. Xingfu Lv, our President, and Mr. Dianming Ma, our CEO, collectively own 100% of equity ownership interest in Shandong Ruitai.

TaiAn has been extending loans to Shangdong Ruitai and the balance amounted to \$21,871,990 as of June 30, 2009. These loans were unsecured, non-interest bearing and have no fixed terms of repayment, therefore, deemed payable on demand. Cash flows from due from a shareholder are classified as cash flows from investing activities. The Managements evaluates the financial resources of the borrower on a regular basis, to make sure Shandong Ruitai has the capability to pay back these loans.

As TaiAn became the only operating subsidiary of a public company, TaiAn signed loan agreement with Shangdong Ruitai in December 2007. Pursuant to the loan agreement, Shangdong Ruitai will pay 7 interest on the outstanding balance monthly. The Management believes that the interest rate approximates the fair market interest rate as compared to the Company's bank loans. Shandong Ruitai pledges its power plant as collateral for the loans and Mr. Lv and Mr. Ma guarantee the loans. Also, Shandong Ruitai will gradually pay off these loans in a three-year period ended December 31, 2010, with 30% in 2008, 30% in 2009, and the rest of 40% in 2010. However, Shandong Ruitai did not meet its payment obligations under the loan agreement and as a result, Shandong Ruitai is in default under the terms of the loan agreement. The Management of the Company is negotiating with Shandong Ruitai regarding the potential restructuring of the debt and is also considering the take over of the power plant which was pledged as security under the loan agreement.

The following is a summary of due from Shandong Ruitai:

June 30,                      December 31,

|   | <u>2009</u>        | <u>2008</u>   |
|---|--------------------|---------------|
|   | <u>(unaudited)</u> |               |
| Due from Shangdong Ruitai-current portion   | \$ 15,940,153      | \$ 10,321,711 |
| Due from Shangdong Ruitai-long-term portion | 5,931,837          | 5,931,837     |
| Total due from Shandong Ruitai              | \$ 21,871,990      | \$ 16,253,548 |

Imputed interest income recognized from due from Shangdong Ruitai amounted to \$747,526 and \$502,282 for the six months ended June 30, 2009 and 2008.

**Note 16- BANK LOANS**

**Bank loans consist of the following as of June 30, 2009:**

| <u>Financial Institutions</u>          | <u>Loan Amount</u> | <u>Duration</u>       | <u>Monthly Interest Rate</u> | <u>Guaranteed By</u>                                |
|--|--------------------|-----------------------|------------------------------|---|
| Feicheng Branch of Bank of China       | \$ 438,289         | 02/04/2009-01/28/2010 | 4.868                        |   |
| Feicheng Branch of Bank of China       | 1,460,963          | 02/27/2009-02/26/2010 | 4.368                        |   |
| Feicheng Branch of Bank of China       | 701,262            | 03/18/2009-03/17/2010 | 4.868                        | Shandong<br>Ashide<br>Chemicals<br>Co., Ltd.        |
| Feicheng Branch of Bank of China       | 613,604            | 03/18/2009-03/17/2010 | 4.868                        |   |
| Feicheng Branch of Bank of China       | 876,578            | 03/25/2009-03/24/2010 | 4.868                        |   |
| Feicheng Branch of Bank of China       | 1,460,963          | 04/23/2009-04/22/2010 | 6.848                        |   |
| Feicheng Branch of Bank of China       | 1,022,674          | 05/26/2009-05/25/2010 | 4.425                        |   |
| Feicheng Branch of Bank of China       | 1,314,867          | 06/02/2009-06/01/2010 | 4.425                        |   |
| Feicheng Branch of Bank of China       | 1,460,963          | 10/24/2008-10/23/2009 | 6.3525                       |   |
| Feicheng Branch of Transportation Bank | 1,460,963          | 01/13/2009-10/11/2009 | 4.8667                       |   |
| Wenyang Branch of Feicheng Credit Bank | 876,578            | 05/28/2009-05/28/2010 | 4.4250                       |   |
| Wenyang Branch of Feicheng Credit Bank | 1,212,599          | 01/24/2009-01/24/2010 | 4.4250                       | Shandong<br>Zhuiyuan<br>Mining<br>Group Co.,<br>Ltd |
| Wenyang Branch of Feicheng Credit Bank | 1,116,176          | 01/24/2009-01/24/2010 | 4.4250                       |   |
| Wenyang Branch of Feicheng Credit Bank | 1,460,963          | 01/17/2009-01/17/2010 | 4.4250                       |   |
| Jinan Branch of Shanghai Pudong Bank   | 2,921,926          | 08/12/2008-08/12/2009 | 6.8475                       | Feicheng<br>Ashide<br>Chemicals<br>Co., Ltd.        |
| Jinan Branch of Shanghai Pudong Bank   | 1,460,963          | 08/01/2008-08/01/2009 | 6.8475                       | Shandong<br>Zhuiyuan<br>Mining<br>Group Co.,<br>Ltd |
| Wenyang Branch of Agriculture Bank     | 1,460,963          | 05/31/2009-05/28/2010 | 5.800%                       |   |
| Wenyang Branch of Agriculture Bank     | 1,460,963          | 05/31/2009-05/28/2010 | 5.800%                       |   |
| Total                                  | \$ 22,782,257      |                       |                              |   |

Interest expense charged to operations for these bank loans was \$768,932.04 for the six months ended June 30, 2009. The weighted-average outstanding bank loan balance is \$22,005,197, and the weighted-average monthly interest rate is 5.78 .



Bank loans consist of the following as of December 31, 2008:

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| <u>Financial Institutions</u>          | <u>Loan Amount</u> | <u>Duration</u>       | <u>Monthly Interest Rate</u> | <u>Guaranteed By</u>                                   |
|--|--------------------|-----------------------|------------------------------|--|
| Feicheng Branch of Bank of China       | \$ 437,700         | 02/28/2008-01/27/2009 | 7.47                         |  |
| Feicheng Branch of Bank of China       | 1,459,000          | 02/28/2008-02/27/2009 | 7.47                         |  |
| Feicheng Branch of Bank of China       | 700,320            | 03/19/2008-03/18/2009 | 7.47                         |  |
| Feicheng Branch of Bank of China       | 612,780            | 03/19/2008-03/18/2009 | 7.47                         | Shandong<br>Ashide                                     |
| Feicheng Branch of Bank of China       | 875,400            | 03/26/2008-03/25/2009 | 6.8475                       | Chemicals<br>Co., Ltd.                                 |
| Feicheng Branch of Bank of China       | 1,459,000          | 04/24/2008-04/23/2009 | 6.8475                       |  |
| Feicheng Branch of Bank of China       | 1,021,300          | 05/26/2008-05/25/2009 | 6.8475                       |  |
| Feicheng Branch of Bank of China       | 1,313,100          | 06/03/2008-06/02/2009 | 6.8475                       |  |
| Feicheng Branch of Bank of China       | 1,459,000          | 10/24/2008-10/23/2009 | 6.3525                       |  |
| Taian Branch of Transportation Bank    | 729,500            | 07/28/2008-01/28/2009 | 6.0225                       |  |
| Wenyang Branch of Feicheng Credit Bank | 875,400            | 05/28/2008-05/28/2009 | 6.225                        | Shandong<br>Ashide<br>Chemicals<br>Co., Ltd.           |
| Wenyang Branch of Feicheng Credit Bank | 1,210,970          | 01/31/2008-01/31/2009 | 6.225                        | Shandong<br>Zhuiyuan<br>Mining<br>Group Co.,<br>Ltd    |
| Wenyang Branch of Feicheng Credit Bank | 1,114,676          | 01/30/2008-01/30/2009 | 6.225                        |  |
| Wenyang Branch of Feicheng Credit Bank | 1,459,000          | 01/29/2008-01/29/2009 | 6.225                        |  |
| Jinan Branch of Shanghai Pudong Bank   | 2,918,000          | 08/12/2008-08/12/2009 | 6.8475                       | Feicheng<br>Ashide<br>Chemicals<br>Co., Ltd.           |
| Jinan Branch of Shanghai Pudong Bank   | 1,459,000          | 08/01/2008-08/01/2009 | 6.8475                       | Shandong<br>Suolide<br>Welding<br>Materials<br>Co.,Ltd |
| Wenyang Branch of Agriculture Bank     | 1,459,000          | 11/28/2008-05/24/2009 | 5.460                        | Shandong<br>Ashide<br>Chemicals<br>Co., Ltd.           |
| Wenyang Branch of Agriculture Bank     | 1,459,000          | 01/24/2008-01/22/2009 | 8.0925                       |  |
| Total                                  | \$ 22,022,146      |                       |                              |  |

Interest expense charged to operations for these bank loans was \$1,804,733 for the year ended December 31, 2008. The weighted-average outstanding bank loan balance is \$22,390,850; and the weighted-average monthly interest rate

is 6.78 .

**Note 17- EARNINGS PER SHARE**

The following is information of net income per share:

|  | For the Six Months Ended<br>June 30, |                                   |
|--|--------------------------------------|-----------------------------------|
|  | <u>2009</u><br><u>(unaudited)</u>    | <u>2008</u><br><u>(unaudited)</u> |
| Net income attributable to                                 |                                      |                                   |
| China Ruitai International Holdings Co., Ltd. Shareholders | \$ 2,588,506                         | \$ 2,250,616                      |
| Weighted average shares used in basic computation          | 26,000,000                           | 26,000,000                        |
| Effect of dilutive securities:                             |                                      |                                   |
| Warrants   | 350,000                              | 50,000                            |
| Weighted average shares used in diluted computation        | 26,350,000                           | 26,050,000                        |
| Earnings per share:  |                                      |                                   |
| Basic  | \$ 0.10                              | \$ 0.09                           |
| Diluted  | \$ 0.10                              | \$ 0.09                           |

**Note 18- STATEMENT OF CONSOLIDATED COMPRESENTATIVE INCOME**

|   | For the Six Months Ended<br>June 30, |                                   |
|---|--------------------------------------|-----------------------------------|
|   | <u>2009</u><br><u>(unaudited)</u>    | <u>2008</u><br><u>(unaudited)</u> |
| Net income  | \$ 2,614,653                         | \$ 2,273,349                      |
| Other comprehensive income, net of tax:   |                                      |                                   |
| Effects of foreign currency conversion  | 21,553                               | 697,513                           |
| Total other comprehensive, not of tax   | 21,553                               | 697,513                           |
| Comprehensive income  | 2,636,206                            | 2,970,862                         |
| Comprehensive income attributable to<br>the noncontrolling interest                   | (26,363)                             | (29,709)                          |
| Comprehensive income attributable to<br>China Ruitai International Holdings Co., Ltd. | \$ 2,609,843                         | \$ 2,941,154                      |

**Note 19- WARRANT**

During March 2008 the Company engaged a consultant to conduct a program of investor relations activities, for a primary period of twelve months ended February 28, 2009, and continue on a month-to-month basis thereafter upon mutual consent. The terms of the agreement are for the consultant to receive a cash payment per month plus a warrant to purchase 150,000 shares of the Company's restricted common stock at a price of \$3.05 per share. The warrant has a term of four (4) years and is vested 50% on March 1, 2008 and 50% on

September 30, 2008. The Management valued the warrant at \$1.16 per share using the Black-Schole pricing model with assumptions summarized below, for a total of \$174,000, which will be amortized over the prospective beneficial period.

| <u>Grant Date</u><br><u>Stock Price</u> | <u>Exercise</u><br><u>Price</u> | <u>Warrant Life</u> | <u>Risk Free</u><br><u>Interest Rate</u> | <u>Expected</u><br><u>Volatility</u> |
|---|---------------------------------|---------------------|--|--------------------------------------|
| \$2.90                                  | \$4.00                          | 4.0 years           | 2.00%                                    | 51%                                  |

Risk free interest rate: Current interest rate of short-dated government bonds such as discount rate on U.S. Government Treasury Bills with 30 days left until maturity.

Volatility: 51% is the volatility of our common stock price October 9, 2007 through March 3, 2008, which is the only available period for our common stocks price quoted in the OTCBB at the time when we valued the cost of the warrant.

Warrant costs charged to operation as consultant fees for the six months ended June 30, 2009 and 2008 were \$29,000 and \$58,000, respectively.

On May 19, 2008, the Company engaged a consultant to as its exclusive investment banker and agent for a one-year period ended May 19, 2009, and subject to cancellation by thirty (30) days written notice by certified mail. One of the compensation to the consultant is to issue the consultant a warrant to purchase 200,000 shares of the Company's common stock at a price of \$4.00 per share. The warrant has a term of five (5) years and was issued on May 19, 2008.

The Management valued the warrant at \$1.84 per share using the Black-Schole pricing model with assumptions summarized below, for a total of \$368,000, which will be amortized over the prospective beneficial period.

| <u>Grant Date</u><br><u>Stock Price</u> | <u>Exercise</u><br><u>Price</u> | <u>Warrant Life</u> | <u>Risk Free</u><br><u>Interest Rate</u> | <u>Expected</u><br><u>Volatility</u> |
|---|---------------------------------|---------------------|--|--------------------------------------|
| \$4.00                                  | \$4.00                          | 5.0 years           | 2.00%                                    | 51%                                  |

Risk free interest rate: Current interest rate of short-dated government bonds such as discount rate on U.S. Government Treasury Bills with 30 days left until maturity.

Volatility: 51% is the volatility of our common stock price October 9, 2007 through May 19, 2008, which is the only available period for our common stocks price quoted in the OTCBB at the time when we valued the cost of the

warrant.

Warrant costs charged to operation as consultant fees for the six months ended June 30, 2009 and 2008 were \$136,978 and \$42,933, respectively.

**Note 20- SEGMENT REPORTING**

The major products consist of following

|   | For the six Months Ended<br>June 30, |                                   |
|---|--------------------------------------|-----------------------------------|
| <b>Revenue</b>                          | <u>2009</u><br><u>(unaudited)</u>    | <u>2008</u><br><u>(unaudited)</u> |
| 1 Methyl Cellulose (MC)                 | 1,135,236                            | 2,174,326                         |
| 2 Hydroxypropyl Methyl Cellulose (HPMC) | 12,593,826                           | 14,356,449                        |
| 3 Hydroxypropyl Cellulose (HPC)         | 391,742                              | 109,977                           |
| 4 Ethyl Cellulose (EC)                  | 1,004,286                            | 981,889                           |
| 5 Hydroxyethyl Cellulose (HEC)          | 462,224                              | 569,311                           |
| 6 HEMC                                  | 137,388                              | 187,548                           |
| 7 Hydroxypropyl Cellulose (HPC)         | 754                                  | 4,342                             |
| 8 HP                                    | 159,578                              | 121,210                           |
| 9 Microcrystalline Cellulose (MCC)      | 83,199                               | 28,916                            |
| 10 CMC                                  | 20,932                               | 69,661                            |
| 11 Film Coating Pre-Mixed Reagent.      | 361,786                              | 365,831                           |
| 12 Raw materials                        | 344,012                              | 276,479                           |
| <br><b>Cost of Sales</b>                |                                      |                                   |
| 1 Methyl Cellulose (MC)                 | 954,475                              | 1,773,444                         |
| 2 Hydroxypropyl Methyl Cellulose (HPMC) | 7,672,599                            | 9,813,530                         |
| 3 Hydroxypropyl Cellulose (HPC)         | 219,569                              | 40,701                            |
| 4 Ethyl Cellulose (EC)                  | 490,483                              | 613,526                           |
| 5 Hydroxyethyl Cellulose (HEC)          | 379,979                              | 533,406                           |
| 6 HEMC                                  | 126,165                              | 154,466                           |
| 7 Hydroxypropyl Cellulose (HPC)         | 464                                  | 4,547                             |
| 8 HP                                    | 44,309                               | 47,010                            |
| 9 Microcrystalline Cellulose (MCC)      | 55,881                               | 23,699                            |
| 10 CMC                                  | 23,325                               | 103,576                           |
| 11 Film Coating Pre-Mixed Reagent.      | 98,974                               | 103,096                           |
| 12 Raw materials                        | 416,381                              | 285,329                           |
| <br><b>Gross Profit</b>                 |                                      |                                   |
| 1 Methyl Cellulose (MC)                 | 180,761                              | 400,882                           |
| 2 Hydroxypropyl Methyl Cellulose (HPMC) | 4,921,227                            | 4,542,919                         |
| 3 Hydroxypropyl Cellulose (HPC)         | 172,173                              | 69,276                            |
| 4 Ethyl Cellulose (EC)                  | 513,803                              | 368,363                           |



5 Hydroxyethyl Cellulose (HEC)

82,245

35,905

|                                    |          |          |
|------------------------------------|----------|----------|
| 6 HEMC                             | 11,223   | 33,082   |
| 7 Hydroxypropyl Cellulose (HPC)    | 290      | (205)    |
| 8 HP                               | 115,269  | 74,200   |
| 9 Microcrystalline Cellulose (MCC) | 27,318   | 5,217    |
| 10 CMC                             | (2,393)  | (33,915) |
| 11 Film Coating Pre-Mixed Reagent. | 262,812  | 262,735  |
| 12 Raw materials                   | (72,369) | (8,850)  |

### Geographic Areas Information

While all of the Company's assets and production are located in the PRC, the Company sales products to customers located in the United States, Finland, and other countries, as summarized in the following:

| Geographic<br>Areas | For the Six Months Ended June 30, |   |                               |   |
|---------------------|-----------------------------------|---|-------------------------------|---|
|                     | <u>2009</u>                       |   | <u>2008</u>                   |   |
|                     | <u>Revenue</u><br>(unaudited)     | <u>Percentage of</u><br><u>Total Revenue</u><br>(unaudited) | <u>Revenue</u><br>(unaudited) | <u>Percentage of</u><br><u>Total Revenue</u><br>(unaudited) |
| PRC                 | \$ 10,307,170                     | 61.74%  | \$ 13,804,952                 | 71.73%  |
| South Korea         | 1,982,589                         | 11.88%  | -                             | -   |
| Finland             | 1,350,240                         | 8.09%   | 1,580,100                     | 8.21%   |
| UAE                 | 1,002,322                         | 6.00%   | 670,726                       | 3.49%   |
| U.S.A.              | 532,003                           | 3.19%   | 1,200,692                     | 6.24%   |
| Germany             | 241,728                           | 1.45%   | 418,977                       | 2.18%   |
| Spain               | -                                 | -   | 357,458                       | 1.86%   |
| Other Countries     | 1,278,911                         | 7.66%   | 1,213,034                     | 6.30%   |
| Total               | \$ 16,694,963                     | 100.00%   | \$ 19,245,939                 | 100.00%   |

### Major Customers

The Company has a diversified customer base. There were four major customers who made sales approximately 5% or more of the Company's total sales as summarized in the following:



| <u>Major Customer</u>   | For the Six Months Ended June 30, |   |                               |   |
|---|-----------------------------------|---|-------------------------------|---|
|   | <u>2009</u>                       |   | <u>2008</u>                   |   |
|   | <u>Revenue</u><br>(unaudited)     | <u>Percentage of Total Revenue</u><br>(unaudited) | <u>Revenue</u><br>(unaudited) | <u>Percentage of Total Revenue</u><br>(unaudited) |
| Shiangtaichem   | \$ 1,982,589                      | 11.61%  | \$ -                          | -   |
| Bang And Bonsomer   | 1,350,240                         | 7.91%   | 1,580,100                     | 8.21%   |
| Viscochem Research & Development Co., Ltd.                    | 1,002,322                         | 5.87%   | -                             | -   |
| ChangSha XiangTai Science and Technology Developing Co., Ltd. |                                   |   | 2,005,525                     | 10.42%  |
| <b>Total</b>  | <b>\$ 4,335,151</b>               | <b>25.97%</b>                                     | <b>\$ 3,585,625</b>           | <b>18.63%</b>                                     |

### Major Suppliers

The Company has a diversified Supplier base. There were eight major customers who made sales approximately 5% or more of the Company's total sales as summarized in the following:

| <u>Major Suppliers</u>                            | For the Six Months Ended June 30, |  |                                |  |
|---|-----------------------------------|--|--------------------------------|--|
|   | <u>2009</u>                       |  | <u>2008</u>                    |  |
|   | <u>Purchase</u><br>(unaudited)    | <u>Percentage of Total Purchase</u><br>(unaudited) | <u>Purchase</u><br>(unaudited) | <u>Percentage of Total Purchase</u><br>(unaudited) |
| Tianjun Changda Technology Co., Ltd.              | \$ 1,793,412                      | 19.74%   | \$ 1,870,962                   | 10.10%   |
| Nantong Jiangshan Pesticide Chemical Co., Ltd.    | 1,108,259                         | 12.20%   | 1,059,879                      | 5.72%  |
| Nantong (Xinyu) Chemical Transportation Co., Ltd. | 852,025                           | 9.38%  | 1,369,114                      | 7.39%  |
| Dongaxian Tianyuan Cellulose Co., Ltd.            | 850,102                           | 9.36%  | -                              | -  |
| Zhongyang Jinhanjiang Cellulose Co., Ltd.         | 803,698                           | 8.84%  | -                              | -  |
| JiNing XingChi Chemical Company                   | 570,102                           | 6.27%  | -                              | -  |
| ZiBo HuiLi Cellulose Co., Ltd.                    | -                                 | -  | 5,433,853                      | 29.34%   |

|  |              |        |    |            |        |
|--|--------------|--------|----|------------|--------|
|  |              |        | -  |            |        |
| ChangSha XiangTai Science and<br>Technology Developing Co., Ltd. | -            |        | -  | 1,930,862  | 10.43% |
| Total  | \$ 5,977,598 | 65.78% | \$ | 11,664,670 | 62.99% |

**Note 21- LOSS ON PHYSICALY INVENTORY COUNT**

During the period June 1, 2009 though June 8, 2009, Ruitai temporary stopped its manufacturing process to make repair and maintenance to its production equipments. At the meantime, Ruitai also physically counted its entire inventories, including finished goods, work-in-progress, and raw materials. While the variance of the total quantity was immaterial, there were quantity variances among major products. Ruitai made adjustments to these variances and recorded a loss of \$146,200, which was primarily attributable to the difference of the costs of major products.

## **Note 22- ASSET RETIREMENT OBLIGATIONS**

The Company operates within the requirements of numerous regulations at the local, province, and national levels regarding issues such as the handling and disposal of hazardous chemicals, waste-water treatment and effluent and emissions limitations among others. From a practical standpoint, certain environmental contamination cannot be reasonably determined until a facility or asset is retired or an event occurs that otherwise requires the facility to be tested and monitored. In the absence of such requirements to test for environmental contamination prior to an asset or facility retirement, the Company has concluded that it cannot reasonably estimate the cost associated with such environmental-related asset retirement obligations ( ARO ).

In addition, the Company anticipates operating its manufacturing facilities indefinitely into the future thereby rendering the potential range of settlement dates as indeterminate. Therefore, the Company has not recorded any AROs to recognize legal obligations associated with the retirement of tangible long-lived assets, as contemplated by the Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations ( SFAS 143 ) and FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations - an interpretation of FASB Statement No. 143 ( FIN 47 ).

## **Note 23- COMMITMENTS AND CONTINGENCIES**

### **PRC's political and economic system**

The Company faces a number of risks and challenges not typically associated with companies in North America and Western Europe, since its assets exist solely in the PRC, and its revenues are derived from its operations therein. The PRC is a developing country with an early stage market economic system, overshadowed by the state. Its political and economic systems are very different from the more developed countries and are in a state of change. The PRC also faces many social, economic and political challenges that may produce major shocks and instabilities and even crises, in both its domestic arena and in its relationships with other countries, including the United States. Such shocks, instabilities and crises may in turn significantly and negatively affect the Company's performance.

### **Environmental**

In the ordinary course of its business, the Company is subject to numerous environmental laws and regulations covering compliance matters or imposing liability for the costs of, and damages resulting from, cleaning up sites, past spills, disposals and other releases of hazardous substances. Currently, our environmental compliance costs principally include the costs to run our waste water treatment facility and inspection fees paid to the local environmental department. The amount is immaterial to our operating costs. However, changes in these laws and regulations may significantly increase our environmental compliance costs and therefore have a material adverse

effect on the Company's financial position and results of operations. Also, any failure by the Company to adequately comply with such laws and regulations could subject the Company to significant future liabilities.

### **Governmental control of currency conversion**

The PRC government imposes controls on the convertibility of Renminbi into foreign currencies and, in certain cases, the remittance of currency out of the PRC. The Company receives most of its revenues in Renminbi, which is currently not a freely convertible currency. Shortages in the availability of foreign currency may restrict the Company's ability to remit sufficient foreign currency to satisfy foreign currency dominated obligations. Under existing PRC foreign exchange regulations, payments of current account items, including profit distributions, interest payments and expenditures from the transaction, can be made in

foreign currencies without prior approval from the PRC State Administration of Foreign Exchange by complying with certain procedural requirements. However, approval from appropriate governmental authorities is required where Renminbi is to be converted into foreign currency and remitted out of China to pay capital expenses such as the repayment of bank loans denominated in foreign currencies.

The PRC government may also at its discretion restrict access in the future to foreign currencies for current account transactions. If the foreign exchange control system prevents the Company from obtaining sufficient foreign currency to satisfy its currency demands, the Company may not be able to pay certain of its expenses as they come due.

### **Contingent liabilities**

Prior to the merger with Pacific Capital Group on November 8, 2007, the Company has not been active since discontinuing its real estate operations in 1981. Management believes that there are no valid outstanding liabilities from prior operations. If a creditor were to come forward and claim a liability, the Company has committed to contest such claim to the fullest extent of the law. No amount has been accrued in the financial statements for this contingent liability.

### **Bank loans**

As of June 30, 2009, the Company has an outstanding bank loans of \$22,782,257, which is approximately 50% of its gross revenue in 2008. In addition, these bank loans had a duration of one year and concentrated on certain financial institutions. If these financial institutions stop extending loans to the Company when these loans are mature, the Company may have difficult to meet its payment obligations under the loan agreements. This may significantly and negatively affect the Company's performance.

### **Guaranteed Bank Loans**

The Company has guaranteed certain loans for third-party enterprises, which, in turn, have guaranteed loans for the Company. These guarantees require payment from the Company in the event of default on payment by the respective debtor and, if the debtor defaults, the Company may be required to pay amounts outstanding under the related agreements in addition to the principal amount guaranteed, including accrued interest and related fees.

The Company and these third-party enterprises have been guaranteeing loans for each other in the day-to-day operation, and none of the enterprises, for which the Company have guaranteed loans, have defaulted on any loan repayments, and accordingly, the Company has not recorded any liabilities or losses on such guarantees.



Bank loans that the Company has guaranteed for third-party enterprises consist of the following as of June 30, 2009:

| <u>Borrower</u>                        | <u>Financial<br/>Institutions</u>   | <u>Loan<br/>Amount</u> | <u>Duration</u>                          | <u>Monthly<br/>Interest<br/>Rate</u> | <u>Guaranteed<br/>By</u>               |
|--|-------------------------------------|------------------------|--|--------------------------------------|--|
| Shangdong Ashide<br>Chemical Co., Ltd. | Feicheng Branch of<br>Bank of China | \$ 1,169,039           | 09/18/2008-<br>09/17/2009<br>10/20/2008- | 7.2                                  | TaiAn RuiTai<br>Cellulose Co.,<br>Ltd. |
| Shangdong Ashide<br>Chemical Co., Ltd. | Feicheng Branch of<br>Bank of China | 1,169,039              | 09/30/2009                               | 6.93                                 |  |

|                                     |  |               |                                      |         |
|-------------------------------------|--|---------------|--------------------------------------|---------|
| Shandong Ashide Chemical Co., Ltd.  | Feicheng Branch of Bank of China       | 350,712       | 05/14/2009-05/13/2010<br>01/12/2007- | 7.47    |
| Fei Cheng Ashide Chemical Co., Ltd. | Feicheng Branch of Bank of China       | 1,500,000     | 01/08/2012<br>02/02/2007-            | 8.34    |
| Fei Cheng Ashide Chemical Co., Ltd. | Feicheng Branch of Bank of China       | 800,000       | 01/08/2011<br>12/30/2006-            | 8.41    |
| Fei Cheng Ashide Chemical Co., Ltd. | Feicheng Branch of Bank of China       | 890,000       | 01/08/2010<br>12/30/2006-            | 8.32938 |
| Fei Cheng Ashide Chemical Co., Ltd. | Feicheng Branch of Bank of China       | 700,000       | 01/08/2011<br>04/10/2009-            | 8.32938 |
| Shandong Taipeng Co.,Ltd.           | Feicheng Branch of Agriculture Bank    | 2,338,077     | 04/10/2010<br>08/10/2009-            | 4.425   |
| Shandong Lulong Co.,Ltd.            | Jinan Branch Shenzhen Development Bank | 1,461,298     | 08/09/2010                           | 5.531   |
|                                     | Total                                  | \$ 10,378,164 |                                      |         |

Bank loans that the Company has guaranteed for third-party enterprises consist of the following as of December 31, 2008:

| <u>Borrower</u>                    | <u>Financial Institutions</u>    | <u>Loan Amount</u> | <u>Duration</u>                          | <u>Monthly Interest Rate</u> | <u>Guaranteed By</u>             |
|------------------------------------|----------------------------------|--------------------|--|------------------------------|----------------------------------|
| Shandong Ashide Chemical Co., Ltd. | Feicheng Branch of Bank of China | \$ 1,093,760       | 09/18/2008-<br>09/17/2009<br>10/20/2008- | 7.2                          |                                  |
| Shandong Ashide Chemical Co., Ltd. | Feicheng Branch of Bank of China | 1,093,760          | 09/30/2009<br>05/14/2008-                | 6.93                         |                                  |
| Shandong Ashide Chemical Co., Ltd. | Feicheng Branch of Bank of China | 328,128            | 05/13/2009                               | 7.47                         |                                  |
|                                    |                                  | 1,500,000          | 01/12/2007-                              | 8.34                         | TaiAn RuiTai Cellulose Co., Ltd. |

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|  |                                     |              |             |         |
|--|-------------------------------------|--------------|-------------|---------|
| Fei Cheng Ashide<br>Chemical Co., Ltd. | Feicheng Branch of<br>Bank of China |              | 01/08/2012  |         |
|  |                                     |              | 02/02/2007- |         |
| Fei Cheng Ashide<br>Chemical Co., Ltd. | Feicheng Branch of<br>Bank of China | 800,000      | 01/08/2011  | 8.41    |
|  |                                     |              | 12/30/2006- |         |
| Fei Cheng Ashide<br>Chemical Co., Ltd. | Feicheng Branch of<br>Bank of China | 890,000      | 01/08/2010  | 8.32938 |
|  |                                     |              | 12/30/2006- |         |
| Fei Cheng Ashide<br>Chemical Co., Ltd. | Feicheng Branch of<br>Bank of China | 700,000      | 01/08/2011  | 8.32938 |
|  | Jinan Branch                        |              | 08/10/2008- |         |
| Shandong Lulong<br>Co.,Ltd.            | Shenzhen<br>Development Bank        | 1,459,000    | 08/09/2009  | 5.531   |
|  | Total                               | \$ 7,864,648 |             |         |

**Guaranteed Bank Checks**

The Company has guaranteed bank checks for third-party enterprises. Generally, these companies deposit 40% to 100% of the bank check amount into a restricted bank account, the bank then issues a bank check to these companies or their assignees. The Company guaranteed on the balance of the bank check amounts. These guarantees require payment from the Company in the event of default on payment by the respective debtor and, if the debtor defaults, the Company may be required to pay amounts outstanding under the related agreements in addition to the amount guaranteed, including accrued interest and related fees.

Both these enterprises and the Company are considered good reputation debtors by local banks. None of the enterprises, for which the Company has guaranteed bank checks, has defaulted on any bank check repayments, and accordingly, the Company has not recorded any liabilities or losses on such guarantees.

Bank checks that the Company has guaranteed for third-party enterprises consist of the following as of June 30, 2009:

| <u>Borrower</u>                            | <u>Financial Institutions</u>                   | <u>Bank Check<br/>Amount</u> | <u>Duration</u>           | <u>Amount in<br/>Restricted<br/>Bank Account</u> | <u>Amount<br/>Guaranteed<br/>By the Company</u> |
|--|---|------------------------------|---------------------------|--|---|
| Shangdong<br>Yinbao<br>Food Co.,<br>Ltd.   | Jinan Branch of<br>Shenzhen<br>Development Bank | 2,922,596                    | 01/10/2009-<br>07/10/2009 | 1,461,298  | 1,461,298                                       |
| Shangdong<br>Taipeng<br>Shiye Co.,<br>Ltd. | Jinan Branch of<br>Shenzhen<br>Development Bank | 2,338,077                    | 01/10/2009<br>-07/10/2010 | 1,169,039  | 1,169,039                                       |
|  | Total   | \$ 5,260,674                 |                           |  |   |

Bank checks that the Company has guaranteed for third-party enterprises consist of the following as of December 31, 2008:

| <u>Borrower</u> | <u>Financial<br/>Institutions</u> | <u>Bank Check<br/>Amount</u> | <u>Duration</u> | <u>Amount in<br/>Restricted<br/>Bank Account</u> | <u>Amount<br/>Guaranteed<br/>By the Company</u> |
|-----------------|-----------------------------------|------------------------------|-----------------|--|---|
|-----------------|-----------------------------------|------------------------------|-----------------|--|---|

|  |   |           |                           |           |           |
|--|---|-----------|---------------------------|-----------|-----------|
| Shangdong<br>Yinbao<br>Food Co.,<br>Ltd.   | Jinan Branch of<br>Shenzhen<br>Development Bank | 2,917,536 | 07/10/2008-<br>01/10/2009 | 1,458,768 | 1,458,768 |
| Shangdong<br>Taipeng<br>Shiye Co.,<br>Ltd. | Jinan Branch of<br>Shenzhen<br>Development Bank | 2,334,029 | 07/10/2008-<br>01/10/2009 | 1,167,014 | 1,167,014 |

## **ITEM 2.**

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

#### **SPECIAL NOTE OF CAUTION REGARDING FORWARD-LOOKING STATEMENTS**

CERTAIN STATEMENTS IN THIS REPORT, INCLUDING STATEMENTS IN THE FOLLOWING DISCUSSION, ARE WHAT ARE KNOWN AS "FORWARD LOOKING STATEMENTS", WHICH ARE BASICALLY STATEMENTS ABOUT THE FUTURE. FOR THAT REASON, THESE STATEMENTS INVOLVE RISK AND UNCERTAINTY SINCE NO ONE CAN ACCURATELY PREDICT THE FUTURE. WORDS SUCH AS "PLANS," "INTENDS," "WILL," "HOPES," "SEEKS," "ANTICIPATES," "EXPECTS "AND THE LIKE OFTEN IDENTIFY SUCH FORWARD LOOKING STATEMENTS, BUT ARE NOT THE ONLY INDICATION THAT A STATEMENT IS A FORWARD LOOKING STATEMENT. SUCH FORWARD LOOKING STATEMENTS INCLUDE STATEMENTS CONCERNING OUR PLANS AND OBJECTIVES WITH RESPECT TO THE PRESENT AND FUTURE OPERATIONS OF THE COMPANY, AND STATEMENTS WHICH EXPRESS OR IMPLY THAT SUCH PRESENT AND FUTURE OPERATIONS WILL OR MAY PRODUCE REVENUES, INCOME OR PROFITS. NUMEROUS FACTORS AND FUTURE EVENTS COULD CAUSE THE COMPANY TO CHANGE SUCH PLANS AND OBJECTIVES OR FAIL TO SUCCESSFULLY IMPLEMENT SUCH PLANS OR ACHIEVE SUCH OBJECTIVES, OR CAUSE SUCH PRESENT AND FUTURE OPERATIONS TO FAIL TO PRODUCE REVENUES, INCOME OR PROFITS. THEREFORE, THE READER IS ADVISED THAT THE FOLLOWING DISCUSSION SHOULD BE CONSIDERED IN LIGHT OF THE DISCUSSION OF RISKS AND OTHER FACTORS CONTAINED IN THIS REPORT ON FORM 10-Q AND IN THE COMPANY'S OTHER FILINGS WITH THE SECURITIES AND EXCHANGE COMMISSION. NO STATEMENTS CONTAINED IN THE FOLLOWING DISCUSSION SHOULD BE CONSTRUED AS A GUARANTEE OR ASSURANCE OF FUTURE PERFORMANCE OR FUTURE RESULTS.

#### **Overview**

China RuiTai International Holdings Co., Ltd. (hereinafter referred to as we, us, our, the Company, or the Registrant) was organized under the laws of the State of Delaware on November 15, 1955, under the name "Inland Mineral Resources Corp." We were formed for the purpose of engaging in all lawful businesses. On March 12, 2007, the Company changed its name to China RuiTai International Holdings Co., Ltd. Currently, the Registrant, through its wholly-owned subsidiary, Pacific Capital Group Co., Ltd., ( Pacific Capital Group ) a corporation incorporated under the laws of the Republic of Vanuatu and its majority-owned subsidiary, TaiAn RuiTai Cellulose Co., Ltd., ( TaiAn ) a Chinese limited liability company, is engaged in the production, sales, and exportation of deeply processed chemicals, with a primary focus on non-ionic cellulose ether products in the Peoples Republic of China ( PRC ).

Cellulose ether is an organic chemical that dissolves in water and other organic solvents. Due to the surface-active properties of cellulose ether, it acts as a thickener and stabilizer in aqueous solutions, making it a beneficial additive in a wide variety of commercial industries and products, including, but not limited to the pharmaceutical industry, the construction industry, PVC products, food and beverage products, petroleum, and cosmetics. Specific examples of applications in which cellulose ether products are used include: as a stabilizer and thickener in latex paint; in mortar dry mix for building materials; to improve the performance of resin in PVC production; as a membrane reagent, stabilizer, and thickener in pharmaceuticals; and to improve jam, ice cream, toothpaste and lipsticks in the food and cosmetic industries.

TaiAn is one of the largest non-ionic cellulose ether producers and exporters in the PRC.

The Chart below depicts the corporate structure of the Registrant. As depicted below, the Registrant owns 100% of the capital stock of Pacific Capital Group and has no other subsidiaries. Pacific Capital Group owns 99% of the capital stock of TaiAn and has no other subsidiaries. TaiAn has no subsidiaries.

### **Results of Operations**

The following discussion and analysis provides information that we believe is relevant to an assessment and understanding of our results of operation and financial condition for the three and six months ended June 30, 2009.

The following discussion should be read in conjunction with the Financial Statements and related Notes appearing elsewhere in this Form 10-Q.

### ***Results of Operations for the Three Month Period Ended June 30, 2009 Compared to the Three Month Period Ended June 30, 2008***

#### **Revenue**



Sales. During the three month period ended June 30, 2009, the Company had sales of \$8,463,783 as compared to sales of \$9,823,948 during the three month period ended June 30, 2008, a decrease of \$1,360,165, or approximately 13.8%. The decrease in sales experienced by the Company was primarily attributable to: (i) the fact that the Company experienced a decrease of 100 tons in total units sold as a result of the general global economic slow-down; and (ii) the fact that the Company reduced the prices of its products to keep its prices in line with those of our competitors. The average selling price decreased \$788 per ton, or approximately 12.8%, in the three month period ended June 30, 2009 as compared to the same period in 2008.

The following chart illustrates the changes in our revenue generated by sales of our products for the three month period ended June 30, 2009, as compared to the three month period ended June 30, 2008:

| Products                              | Three Month Period ended June 30, |                    |             |
|---------------------------------------|-----------------------------------|--------------------|-------------|
|                                       | 2009                              | 2008               | % Change    |
| Methyl Cellulose (MC)                 | \$ 762,926                        | \$ 1,214,084       | -37%        |
| Hydroxypropyl Methyl Cellulose (HPMC) | 6,476,598                         | 7,627,930          | -15%        |
| Hydroxypropyl Cellulose (HPC)         | 49,976                            | 42,235             | +18%        |
| Ethyl Cellulose (EC)                  | 309,431                           | 338,307            | -9%         |
| Hydroxyethyl Cellulose (HEC)          | 273,789                           | 197,935            | +38%        |
| HEMC                                  | 61,289                            | 100,204            | -39%        |
| Hydroxypropyl Cellulose (HPC)         | 393                               | 3,616              | -89%        |
| HP                                    | 98,779                            | 54,588             | +81%        |
| Microcrystalline Cellulose (MCC)      | 54,124                            | 23,156             | +134%       |
| CMC                                   | 11                                | 35,202             | -100%       |
| Film Coating Pre-Mixed Reagent        | 131,595                           | 183,523            | -28%        |
| Raw materials                         | 244,872                           | 3,168              | +7,630%     |
| <b>Total Sales</b>                    | <b>\$8,463,783</b>                | <b>\$9,823,948</b> | <b>-14%</b> |

**Cost of Sales.** During the three month period ended June 30, 2009 the Company's cost of sales was \$5,506,063, as compared to Costs of Sales of \$7,084,546 for the three month period ended June 30, 2008, a decrease of \$1,578,483 of approximately 22%. This decrease in cost of sales experienced by the Company was primarily attributable to: i) a decrease in sales experienced by the Company; and ii) an overall decrease in the costs of raw materials utilized by the Company. The average cost of goods sold decreased \$812 per ton, or approximately 19%, in the three months ended June 30, 2009 as compared to the same period in 2008.

**Gross Profit.** During the three month period ended June 30, 2009 the Company's gross profit was \$2,957,720, as compared to gross profit of \$2,739,402 for the three month period ended June 30, 2008, an increase of \$218,318, or approximately 7.9%. This increase in gross profit experienced by the Company was primarily attributable to the fact that the Company experienced a significant decrease in cost of goods sold from the period ended June 30, 2009 as compared to the same period in 2008.

### Operating Expenses

The operating expenses for the Company are divided into Selling Expenses and General and Administrative Expenses, both of which are discussed below:

**Selling Expenses.** Selling expenses which consist of sales commission, freight charges, travel and other selling expenses totaled \$444,994 for the three months ended June 30, 2009, as compared to \$388,922 for the three month

period ended June 30, 2008, an increase of \$56,072 or approximately 14.4%. This increase is primarily attributable to an increase of \$89,396 in sales commissions paid by the Company, and an increase of \$12,624 in travel expenses paid by the Company. These increases were slightly offset by decreases in other selling expenses due to the decrease in sales experienced by the Company. The Company increased sales commissions and travel expenses to encourage its sales staff to maintain sales in an effort to combat the general slowdown in demand for the Company's products.

General and Administrative Expenses. General and administrative expenses totaled \$683,737 for the three month period ended June 30, 2009, as compared to \$677,350 for the three month period ended June 30, 2008, an increase of \$6,387 or approximately 1%. This small increase is primarily attributable to increases of \$126,698 in Research & Development expenses and \$56,862 in financing fees, both of which were offset by decreases of \$66,176 in payroll, of \$64,536 in consultant fees, and \$54,519 in various taxes during the three month period ended June 30, 2009 as compared to the same period in 2008.

## **Income From Operations**

For the three month period ended June 30, 2009, the Company had income from operations in the amount of \$1,828,989, as compared to income from operations of \$1,673,130 for the three month period ended June 30, 2008, an increase of \$155,859 or approximately 8.5%. The increase in income from operations experienced by the Company was primarily attributable to reduced costs for the acquisition of raw materials and increased selling expenses.

## **Interest Expense**

For the three month period ended June 30, 2009, the Company incurred interest expense in the amount of \$483,531, as compared to interest expense of \$597,794 for the three month period ended June 30, 2008, a decrease of \$114,263, or approximately 19%. The decrease in interest expense incurred by the Company resulted from the fact that the average annual interest rate decreased from 7.9% to 6.93%, a decrease of 0.97%, or approximately 12.2%.

## **Net Income**

The Company had a net income of \$1,200,681 for the three month period ended June 30, 2009 as compared to \$1,059,425 for the three month period ended June 30, 2008, an increase of \$141,256 or approximately 13.3%. The increase in net income is primarily attributable to: i) the fact that the Company experienced an increase in imputed interest income from loans to Shandong Ruitai due to the increased average outstanding balance of the loans; and ii) the fact that the Company experienced a significant decrease in the cost of goods sold as a result of a decrease in the cost of raw materials.

## ***Results of Operations for the Six Month Period Ended June 30, 2009 Compared to the Six Month Period Ended June 30, 2008***

### **Revenue**

Sales. During the six month period ended June 30, 2009, the Company had sales of \$16,694,963 as compared to sales of \$19,245,939 during the six month period ended June 30, 2008, a decrease of \$2,550,976, or approximately 13.3%. The decrease in sales experienced by the Company was primarily attributable to: (i) the fact that the Company experienced a decrease of 251 tons, or approximately 8.2%, in total units sold as a result of the general global economic slow-down; and (ii) the fact that the Company reduced the prices of its products to keep its prices in line

with those of our competitors. The average selling price decreased \$582 per ton, or approximately 9.1%, in the six months ended June 30, 2009 as compared to the same period in 2008;

The following chart illustrates the changes in our revenue generated by sales of our products for the six month period ended June 30, 2009, as compared to the six month period ended June 30, 2008:

| <b>Products</b>                       | <b>Six Month Period ended June 30,</b> |                    |                    |                 |
|---------------------------------------|--|--------------------|--------------------|-----------------|
|                                       |  | <b><u>2009</u></b> | <b><u>2008</u></b> | <b>% Change</b> |
| Methyl Cellulose (MC)                 | \$                                     | 1,135,236          | \$ 2,174,326       | - 47.8%         |
| Hydroxypropyl Methyl Cellulose (HPMC) |  | 12,593,826         | 14,356,449         | - 12.3%         |
| Hydroxypropyl Cellulose (HPC)         |  | 391,742            | 109,977            | + 256%          |
| Ethyl Cellulose (EC)                  |  | 1,004,286          | 981,889            | +2.3%           |
| Hydroxyethyl Cellulose (HEC)          |  | 462,224            | 569,311            | - 18.8%         |
| HEMC                                  |  | 137,388            | 187,548            | - 26.8%         |

|                                  |                     |                     |                |
|----------------------------------|---------------------|---------------------|----------------|
| Hydroxypropyl Cellulose (HPC)    | 754                 | 4,342               | - 82.6%        |
| HP                               | 159,578             | 121,210             | + 31.7%        |
| Microcrystalline Cellulose (MCC) | 83,199              | 28,916              | + 187.7%       |
| CMC                              | 20,932              | 69,661              | - 70%          |
| Film Coating Pre-Mixed Reagent   | 361,786             | 365,831             | -1.1.%         |
| Raw materials                    | 344,012             | 276,479             | +24.4%         |
| <b>Total Sales</b>               | <b>\$16,694,963</b> | <b>\$19,245,939</b> | <b>- 13.3%</b> |

Cost of Sales. During the six month period ended June 30, 2009 the Company's cost of sales was \$10,482,604, as compared to Costs of Sales of \$13,496,330 for the six month period ended June 30, 2008, a decrease of \$3,013,726, or approximately 22%. This decrease in cost of sales experienced by the Company was primarily attributable to: i) a decrease in sales experienced by the Company; and ii) an overall decrease in the costs of raw materials utilized by the Company. The average cost of goods sold decreased \$729 per ton, or approximately 16.7%, in the six months ended June 30, 2009 as compared to the same period in 2008.

Gross Profit. During the six month period ended June 30, 2009 the Company's gross profit was \$6,212,359, as compared to gross profit of \$5,749,609 for the six month period ended June 30, 2008, an increase of \$462,750 of approximately 8%. This increase in gross profit experienced by the Company was primarily attributable to the fact that the Company experienced a significant decrease in cost of goods sold from the period ended June 30, 2009 as compared to the same period in 2008.

## Operating Expenses

The operating expenses for the Company are divided into Selling Expenses and General and Administrative Expenses, both of which are discussed below:

Selling Expenses. Selling expenses which consist of sales commission, freight charges, travel and other selling expenses totaled \$733,971 for the six months ended June 30, 2009 as compared to \$863,812 for the six month period ended June 30, 2008, a decrease of \$129,841, or approximately 15%. This decrease is primarily attributable to a decrease of \$38,467 in selling commissions, a decrease of \$57,142 in freight out, and a decrease of \$34,232 in other selling expenses due to the decrease in total units sold.

General and Administrative Expenses. General and administrative expenses totaled \$1,498,970 for the six month period ended June 30, 2009, as compared to \$1,366,684 for the six month period ended June 30, 2008, an increase of \$132,286, or approximately 9.7%. This increase is primarily attributable to an increase of \$287,375 in Research &

Development expenses, which was offset by decreases of \$57,594 in payroll and \$84,536 in consultant fees during the six month period ended June 30, 2009 as compared to the same period in 2008.

### **Income From Operations**

For the six month period ended June 30, 2009, the Company had income from operations in the amount of \$3,979,418, as compared to income from operations of \$3,519,113 for the six month period ended June 30, 2008, an increase of \$460,305, or approximately 13%. The increase in income from operations experienced by the Company was primarily attributable to a combination of reduced costs for the acquisition of raw materials and reduced selling expenses.

### **Net Income**

The Company had a net income of \$2,614,653 for the six month period ended June 30, 2009 as compared to \$2,273,349 for the six month period ended June 30, 2008, an increase of \$341,304 or approximately 15%.

The increase in net income is primarily attributable to: i) the fact that the Company experienced an increase in imputed interest income from loans to Shandong Ruitai due to the increased average outstanding balance of the loans; and ii) the fact that the Company experienced a significant decrease in the cost of goods sold as a result of a decrease in the cost of raw materials.

### **Liquidity and Capital Resources**

The Company anticipates that the existing cash and cash equivalents on hand, together with the net cash flows generated from its business activities will be sufficient to meet the working capital requirements for its on-going projects and to sustain the business operations for the next twelve months.

### **Total Current Assets & Total Assets**

As of June 30, 2009, our unaudited balance sheet reflects that we have: i) total current assets of \$71,633,551, as compared to total current assets of \$57,279,375 at December 31, 2008, an increase of \$14,354,176, or approximately 25%; and ii) total assets of \$96,957,959 as of June 30, 2009, compared to \$82,119,175 as of December 31, 2008, an increase of \$14,838,784, or approximately 18%. The Company's total assets increased due to changes that the Company experienced in cash and cash equivalents, bank checks and commercial paper, restricted cash, and amounts due from a related party, all of which are discussed below.

**Cash and Cash Equivalents.** As of June 30, 2009, our unaudited balance sheet reflects that we have cash and cash equivalents of \$1,865,139, as compared to \$5,319,456, at December 31, 2008 a decrease of 3,454,317, or approximately 6.5%. The decrease is primarily attributable to the increase experienced by the Company in its loans to a related party, Shandong Ruitai.

**Bank Checks and Commercial Paper.** As of June 30, 2009, our unaudited balance sheet reflects that we have bank checks and commercial paper of \$9,033,677 as compared to bank checks and commercial paper of \$8,244,207 at December 31, 2008, an increase of \$789,470, or approximately 9.6%. The increase in the Company's bank checks and commercial paper was primarily attributable to cash conversion of outstanding bank checks and commercial paper.

**Restricted Cash.** As of June 30, 2009, our unaudited balance sheet reflects that we have restricted cash of \$29,219,261, as compared to restricted cash of \$19,112,900, at December 31, 2008, an increase of \$10,106,361, or approximately 5.3%. The increase in restricted cash was primarily attributable to the increase in compensation balance needed to secure the bank checks payable due to an overall increase in bank checks payable.



Due From Related Party. Due from a related party represents loans to Shandong Ruitai Chemicals Co., Ltd. ("Shandong Ruitai"), a former majority owner of TaiAn. Shandong Ruitai had owned 75% equity ownership interest of TaiAn from January 2000 through February 2007. On March 20, 2007, Shandong sold a 74% equity ownership interest of TaiAn to Pacific Capital Group Co., Ltd. Mr. Xingfu Lu, our President, and Mr. Dianmin Ma, our CEO, collectively own 100% of equity ownership interest in Shandong Ruitai.

As TaiAn became the only operating subsidiary of a public company, subsequent to the closing of the Share Exchange, on December 31, 2007, Shandong Ruitai entered into a Loan Contract with TaiAn for the repayment of the outstanding balance of the loans. Pursuant to the terms of the Loan Contract, Shandong Ruitai will repay the principal outstanding balance of the loan and interest which is accruing monthly at 7% over a three-year period ending December 31, 2010, with 30% of the principal and interest due as of the fiscal year ending 2008, 30% of the principal and interest due as of the fiscal year ending 2009, and 40% of the principal and interest due as of the fiscal year ending 2010. The repayment obligations of Shandong Ruitai under the Loan Contract are secured by a thermal power plant owned by Shandong Ruitai.

Additionally, Shandong Ruitai's repayment obligations are personally guaranteed by Shandong Ruitai's principals, Mr. Dian Min Ma and Mr. Xingfu Lu. The foregoing description of the loan contract is qualified in its entirety by reference to the Loan Contract which was filed as Exhibit 10.7 to the Company's Form 10-KSB filed with the Securities and Exchange Commission on April 15, 2008, and is hereby incorporated by reference.

As of June 30, 2009, our unaudited balance sheet reflects that we have an amount due from related party of \$ 21,871,990, as compared to an amount due from related party of \$ 16,253,548 at December 31, 2008, an increase of \$ 5,618,442. The increase in the amount due from related party from December 2008 to June 2009 was primarily attributable to: i) the fact that the Company advanced additional funds to Shandong RuiTai; and ii) the fact that Shandong Ruitai did not meet its payment obligations under the Loan Contract and as a result, Shandong Ruitai is in default under the terms of the Loan Contract, a copy of which was filed as Exhibit 10.7 to the Company's Form 10-KSB filed with the Securities and Exchange Commission on April 15, 2008, and is hereby incorporated by reference.

Currently, Shandong Ruitai is in default under the Loan Agreement. The Management of the Company is negotiating with Shandong Ruitai regarding the potential restructuring of the debt and is also considering other options.

### **Total Current Liabilities**

As of June 30, 2009, our unaudited balance sheet reflects that we have total current liabilities of \$77,995,591, as compared to total current liabilities of \$65,958,991 at December 31, 2008, an increase of \$12,036,600, or approximately 18.2%. The increase in the Company's total current liabilities was primarily attributable to an increase experienced by the Company in Bank Check Payable.

Bank Checks Payable. As of June 30, 2009, our unaudited balance sheet reflects that we have Bank Checks Payable of \$39,446,002, as compared to bank checks payable of \$29,180,000 as of December 31, 2008, an increase of \$10,266,002, or approximately 35%. The increase in our Bank Checks Payable was primarily attributable to the Company's utilization of Bank Checks for business operations.

### **Operating Activities**

Our unaudited balance sheet reflects that net cash of \$12,843,530 was provided by operating activities during the six period ended June 30, 2009, compared to net cash used by operating activities of \$420,569 during the six month period ended June 30, 2008, representing a change of \$ 12,422,961. The increase in net cash provided by our operating activities was primarily attributable to increases in bank checks payables, accounts payable and accrued expenses, and a decrease in inventory.

### **Investing Activities**

During the six month period ended June 30, 2009, the net cash used in investing activities was \$(6,915,391), as compared to net cash provided by investing activities of \$221,688 for the six month period ended June 30, 2008, a change of \$6,693,703 in the cash used in investing activities. The change in net cash used in investing activities was primarily attributable to an increase in loans to a related party.

### **Financing Activities**

During the six month period ended June 30, 2009, the net cash used by financing activities was \$(9,390,876), as compared to net cash provided by financing activities of \$1,339,092 for the six month period ended June 30, 2008. The change in net cash used by financing activities was primarily attributable to an increase in restricted cash needed to secure the bank checks payable.

## **Off Balance Sheet Arrangements**

The Company does not have any off-balance sheet arrangements.

### **ITEM 3.**

#### **QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

Not Applicable.

### **ITEM 4T.**

#### **CONTROLS AND PROCEDURES.**

##### **Disclosure Controls and Procedures**

The Securities and Exchange Commission defines the term "disclosure controls and procedures" to mean the company's controls and other procedures of an issuer that are designed to ensure that information required to be disclosed in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Securities Exchange Act of 1934 is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. The Company maintains such a system of controls and procedures in an effort to ensure that all information which it is required to disclose in the reports it files under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified under the SEC's rules and forms and that information required to be disclosed is accumulated and communicated to principal executive and principal financial officers to allow timely decisions regarding disclosure.

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are designed to provide reasonable assurance of achieving the objectives of timely alerting them to material information required to be included in our periodic SEC reports and of ensuring that such information is recorded, processed, summarized and reported with the time periods specified. Our chief executive officer and chief financial officer also concluded that our disclosure controls and

procedures were effective as of the end of the period covered by this report to provide reasonable assurance of the achievement of these objectives.

### **Changes in Internal Control over Financial Reporting**

There was no change in the Company's internal control over financial reporting during the period ended June 30, 2009, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II-OTHER INFORMATION**

### **ITEM 1.**

#### **LEGAL PROCEEDINGS.**

The Company is not a party to any pending legal proceedings, and no such proceedings are known to be contemplated. No director, officer or affiliate of the Company, and no owner of record or beneficial owner

of more than 5.0% of the securities of the Company, or any associate of any such director, officer or security holder is a party adverse to the Company or has a material interest adverse to the Company in reference to pending litigation.

**ITEM 1A.**

**RISK FACTORS.**

Not Applicable.

**ITEM 2.**

**UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.**

None.

**ITEM 3.**

**DEFAULTS UPON SENIOR SECURITIES.**

None.

**ITEM 4.**

**SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.**

None.

**ITEM 5.**

**OTHER INFORMATION.**

None.

**ITEM 6.**

**EXHIBITS.**

(a)

The following exhibits are filed herewith:

31.1

Certifications pursuant to Rule 13a-14(a) or 15d-14(a) under the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2

Certifications pursuant to Rule 13a-14(a) or 15d-14(a) under the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1

Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32,2

Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

**SIGNATURES**

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

**CHINA RUITAI INTERNATIONAL HOLDINGS CO., LTD.**

By: /s/ Dian Min Ma, Chief Executive Officer

Date: August 14, 2009



By: /s/ Gang Ma, Chief Financial Officer

Date: August 14, 2009