

Kandi Technologies Corp  
Form 10-Q  
August 14, 2012

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**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, 2012**

or

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

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

Commission file number **001-33997**

**KANDI TECHNOLOGIES, CORP.**

(Exact name of registrant as specified in charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**90-0363723**

(I.R.S. Employer Identification No.)

**Jinhua City Industrial Zone**  
**Jinhua, Zhejiang Province**  
**People's Republic of China**  
**Post Code 321016**

(Address of principal executive offices)

\_\_\_\_\_  
**(86 - 579) 82239856**

(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 such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes

No

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

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any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files)

Yes  No

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  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 August 8, 2012 the registrant had issued and outstanding 29,845,122 shares of common stock, par value \$.001 per share.

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**PART I-- FINANCIAL INFORMATION****Item 1. Financial Statements. (Unaudited)**

**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS**

**ASSETS**

|   | <b>June 30,<br/>2012<br/>(Unaudited)</b> | <b>December<br/>31,<br/>2011</b> |
|---|--|----------------------------------|
| <b>CURRENT ASSETS</b>   |  |                                  |
| Cash and cash equivalents   | \$ 3,979,148                             | \$ 2,294,352                     |
| Restricted cash   | 26,803,826                               | 6,634,989                        |
| Accounts receivable   | 24,879,948                               | 12,932,776                       |
| Inventories (net of reserve for slow moving inventory of \$0 and \$72,487 as of June 30, 2012 and December 31, 2011 respectively) | 13,554,630                               | 6,674,467                        |
| Notes receivable  | 15,004,641                               | 37,879,243                       |
| Other receivables   | 752,870                                  | 2,438,917                        |
| Prepayments and prepaid expenses  | 154,484                                  | 185,037                          |
| Due from employees  | 53,676                                   | 79,857                           |
| Advances to suppliers   | 860,348                                  | 852,638                          |
| Deferred taxes  | 19,307                                   | -                                |
| <b>Total Current Assets</b>   | <b>86,062,878</b>                        | <b>69,972,276</b>                |
| <b>LONG-TERM ASSETS</b>   |  |                                  |
| Plant and equipment, net  | 19,284,349                               | 20,981,893                       |
| Land use rights, net  | 14,502,908                               | 10,992,769                       |
| Intangible assets   | 724,639                                  | -                                |
| Construction in progress  | 12,171,948                               | 10,007,601                       |
| Deferred taxes  | 42,640                                   | 89,998                           |
| Investment in associated companies  | 203,408                                  | 229,213                          |
| Goodwill  | 437,525                                  | -                                |
| <b>Total Long-Term Assets</b>   | <b>47,367,417</b>                        | <b>42,301,474</b>                |
| <b>TOTAL ASSETS</b>   | <b>\$ 133,430,295</b>                    | <b>\$ 112,273,750</b>            |

See accompanying notes to condensed consolidated financial statements

**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS**

**LIABILITIES AND STOCKHOLDERS EQUITY**

|  | <b>June 30,<br/>2012<br/>(Unaudited)</b> | <b>December<br/>31,<br/>2011</b> |
|--|--|----------------------------------|
| <b>CURRENT LIABILITIES</b>   |  |                                  |
| Accounts payable   | \$ 8,584,600                             | \$ 5,061,069                     |
| Other payables and accrued expenses  | 1,150,306                                | 3,137,983                        |
| Short-term bank loans  | 36,599,839                               | 36,372,492                       |
| Customer deposits  | 43,407                                   | 1,025,357                        |
| Notes payable, net of discount of \$0 and \$71 as of June 30, 2012 and<br>December 31, 2011 respectively   | 15,174,771                               | 5,847,552                        |
| Income tax payable   | 128,390                                  | 153,730                          |
| Due to employees   | 168,567                                  | 9,455                            |
| Due to related party   | 841,251                                  | 841,251                          |
| Deferred taxes   |  | 56,362                           |
| Financial derivate - liability   | -  | 213                              |
| <b>Total Current Liabilities</b>   | <b>62,691,131</b>                        | <b>52,505,464</b>                |
| <b>LONG-TERM LIABILITIES</b>   |  |                                  |
| Financial derivatives - liability  | 1,957,885                                | 3,919,411                        |
| <b>Total Long-Term Liabilities</b>   | <b>1,957,885</b>                         | <b>3,919,411</b>                 |
| <b>TOTAL LIABILITIES</b>   | <b>64,649,016</b>                        | <b>56,424,875</b>                |
| <b>STOCKHOLDERS EQUITY</b>   |  |                                  |
| Common stock, \$0.001 par value; 100,000,000 shares authorized; 29,845,122 and<br>27,445,600 shares issued and outstanding at June 30, 2012 and December 31,<br>2011, respectively | 29,845                                   | 27,446                           |
| Additional paid-in capital   | 38,345,747                               | 31,533,378                       |
| Retained earnings (the restricted portion is \$1,940,832 at June 30, 2012 and<br>December 31, 2011)  | 22,498,511                               | 19,210,330                       |
| Accumulated other comprehensive income   | 7,907,176                                | 5,077,721                        |
| <b>TOTAL STOCKHOLDERS EQUITY</b>   | <b>68,781,279</b>                        | <b>55,848,875</b>                |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>   | <b>\$ 133,430,295</b>                    | <b>\$ 112,273,750</b>            |

See accompanying notes to condensed consolidated financial statements

**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS) AND  
COMPREHENSIVE INCOME (LOSS)**  
**(UNAUDITED)**

|  | Three Months Ended |                  | Six Months Ended |                  |
|--|--------------------|------------------|------------------|------------------|
|  | June 30,<br>2012   | June 30,<br>2011 | June 30,<br>2012 | June 30,<br>2011 |
| <b>REVENUES, NET</b>                                   | \$ 11,060,976      | \$ 10,137,702    | \$ 25,416,517    | \$ 18,479,208    |
| <b>COST OF GOODS SOLD</b>                              | (9,272,719)        | (7,795,987)      | (20,287,410)     | (14,076,060)     |
| <b>GROSS PROFIT</b>                                    | 1,788,257          | 2,341,715        | 5,129,107        | 4,403,148        |
| Research and development                               | (620,090)          | (574,588)        | (1,376,186)      | (1,086,540)      |
| Selling and marketing                                  | (79,201)           | (92,679)         | (173,036)        | (149,615)        |
| General and administrative                             | (896,050)          | (827,529)        | (1,579,670)      | (1,501,396)      |
| <b>INCOME FROM CONTINUING<br/>OPERATIONS</b>           | 192,916            | 846,919          | 2,000,215        | 1,665,597        |
| Interest income (expense), net                         | (188,542)          | 275,466          | (56,940)         | (21,804)         |
| Change in fair value of financial<br>instruments       | 1,018,576          | 2,367,594        | 1,961,526        | 7,752,772        |
| Government grants                                      | 25,308             | 273,139          | 25,308           | 280,727          |
| Investment (loss) income                               | (14,010)           | (8,490)          | (27,411)         | (7,276)          |
| Other income, net                                      | 12,134             | 53,526           | 46,602           | 167,232          |
| <b>INCOME (LOSS) BEFORE INCOME<br/>TAXES</b>           | 1,046,382          | 3,808,154        | 3,949,300        | 9,837,248        |
| <b>INCOME TAX EXPENSE</b>                              | (141,154)          | (186,811)        | (661,120)        | (277,505)        |
| <b>NET INCOME</b>                                      | 905,228            | 3,621,343        | 3,288,180        | 9,559,743        |
| <b>OTHER COMPREHENSIVE INCOME</b>                      |                    |                  |                  |                  |
| Foreign currency translation                           | 2,434,039          | 827,820          | 2,829,455        | 1,146,420        |
| <b>COMPREHENSIVE INCOME (LOSS)</b>                     | \$ 3,339,267       | \$ 4,449,163     | \$ 6,117,635     | \$ 10,706,163    |
| <b>WEIGHTED AVERAGE SHARES<br/>OUTSTANDING BASIC</b>   | 29,845,122         | 27,440,878       | 28,647,746       | 27,431,851       |
| <b>WEIGHTED AVERAGE SHARES<br/>OUTSTANDING DILUTED</b> | 31,166,260         | 28,578,592       | 29,990,967       | 28,786,145       |
| <b>NET INCOME PER SHARE, BASIC</b>                     | \$ 0.03            | \$ 0.13          | \$ 0.11          | \$ 0.35          |
| <b>NET INCOME PER SHARE, DILUTED</b>                   | \$ 0.03            | \$ 0.13          | \$ 0.11          | \$ 0.33          |

See accompanying notes to condensed consolidated financial statements



**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**

|  | <b>Six Months Ended June 30</b> |                |
|--|---------------------------------|----------------|
|  | <b>2012</b>                     | <b>2011</b>    |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>   |                                 |                |
| Net income (loss)  | \$ 3,288,180                    | \$ 9,559,743   |
| Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities: |                                 |                |
| Depreciation and amortization  | 2,470,911                       | 2,317,662      |
| Deferred taxes   | (24,219)                        | 58,459         |
| Option and warrant expense   | 19,053                          | 138,315        |
| Change of derivative instruments fair value  | (1,961,526)                     | (7,752,771)    |
| Loss in investment in associated company   | 27,411                          | 16,819         |
| <b>Changes in operating assets and liabilities:</b>  |                                 |                |
| <b>(Increase) Decrease In:</b>   |                                 |                |
| Accounts receivable  | (11,844,213)                    | 7,991,676      |
| Inventories  | (6,826,372)                     | (5,214,768)    |
| Other receivables and prepaid expenses   | 1,701,831                       | (773,085)      |
| Due from employees   | 185,624                         | 20,490         |
| Prepayments and prepaid expenses   | 30,204                          | (9,321,749)    |
| Marketable equity securities (trading)   | -                               | 303,596        |
| <b>Increase (Decrease) In:</b>   |                                 |                |
| Accounts payable   | 3,484,295                       | (1,413,790)    |
| Other payables and accrued liabilities   | (1,990,887)                     | (134,299)      |
| Customer deposits  | (988,344)                       | (10,616)       |
| Income tax payable   | (26,411)                        | 57,387         |
| Net cash (used in) provided by operating activities  | \$ (12,454,463)                 | \$ (4,156,931) |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>   |                                 |                |
| Cash Acquired in Acquisition   | 112,551                         | -              |
| Purchases of plant and equipment   | (452,393)                       | (201,490)      |
| Purchase of construction in progress   | (2,091,168)                     | (93,652)       |
| Issuance of notes receivable   | -                               | (2,733,584)    |
| Repayments of notes receivable   | 23,123,103                      | 7,260,308      |
| Net cash provided by (used in) investing activities  | \$ 20,692,093                   | \$ 4,231,582   |

See accompanying notes to condensed consolidated financial statements



**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**

|   | <b>Six Months Ended June 30</b> |                     |
|---|---------------------------------|---------------------|
|   | <b>2012</b>                     | <b>2011</b>         |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                |                                 |                     |
| Restricted cash   | \$ (20,103,142)                 | \$ (8,857,647)      |
| Proceeds from short-term bank loans                         | 14,749,822                      | 14,507,848          |
| Repayments of short-term bank loans                         | (14,781,440)                    | (14,507,848)        |
| Proceeds from notes payable                                 | 15,160,857                      | 29,473,839          |
| Repayments of notes payable                                 | (5,883,855)                     | (19,224,884)        |
| Option exercise & other financing                           | 67,403                          | 60,069              |
| Common Stock Issued, net of Cost of Capital                 | 3,740,423                       | -                   |
| Net cash provided by financing activities                   | (7,049,932)                     | 1,451,377           |
| <b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b> | <b>1,187,698</b>                | <b>1,526,028</b>    |
| Effect of exchange rate changes on cash                     | 497,098                         | 92,029              |
| Cash and cash equivalents at beginning of period            | 2,294,352                       | 7,754,166           |
| <b><u>CASH AND CASH EQUIVALENTS AT END OF PERIOD</u></b>    | <b>\$ 3,979,148</b>             | <b>\$ 9,372,223</b> |

**SUPPLEMENTARY CASH FLOW INFORMATION**

|  |              |              |
|--|--------------|--------------|
| Income taxes paid                        | \$ 687,530   | \$ 220,119   |
| Interest paid                            | \$ 1,316,591 | \$ 1,232,993 |
| Issuance of Common Stock for Acquisition | \$ 8,616,416 | -            |

See accompanying notes to condensed consolidated financial statements

**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 (UNAUDITED)**

**NOTE 1 ORGANIZATION AND PRINCIPAL ACTIVITIES**

The Company was incorporated under the laws of the State of Delaware on March 31, 2004. On August 13, 2007, the Company changed its name from Stone Mountain Resources, Inc. to Kandi Technologies, Corp.

On June 29, 2007, the Company executed an exchange agreement to acquire 100% of Continental Development Limited, a Hong Kong corporation and its wholly owned subsidiary Zhejiang Kandi Vehicles Co., Ltd. ( Kandi Vehicles ).

In the first fiscal quarter of 2011, Jinhua Kandi New Energy Vehicles Co., Ltd. ( Kandi New Energy ) was incorporated by Kandi Vehicles and Mr. Xiaoming Hu, the Chairman and CEO of the Company.

On April 25, The Company completed the acquisition of KO NGA Investment Limited and its subsidiaries of K S Asia Limited Group Limited, Yongkang K S Electric Limited and Yongkang Scrou Electric Co. with consideration of 2,354,212 shares of the Company s common stock. Yongkang Scrou Electric Co. is an operation vehicle of manufacturing various auto generators.

In connection with an internal reorganization, for the purposes of reducing expenses, Kandi Vehicles and Yongkang KS Electric Co., Ltd ( Yongkang KS Electric ), each a wholly-owned subsidiary of the Company, entered into a Share Transfer Agreement, dated June 27, 2012. Pursuant to the terms and conditions of this agreement, Yongkang KS Electric sold, transferred and assigned its entire ownership interest in Yongkang Scrou Electric Co. ( Yongkang Scrou ) to Kandi Vehicles for a transfer price of RMB40,000,000. As a result of this transaction, Yongkang Scrou became a wholly-owned subsidiary of Kandi Vehicles.

In connection with, and in furtherance of, the internal reorganization noted above, the Company and three of its subsidiaries, Kandi Vehicles, Yongkang KS Electric and Yongkang Scrou entered into an Offset Agreement of credits and debts, dated June 29, 2012. Pursuant to the terms and conditions of this agreement, the parties agreed to offset the payables and receivables of RMB40,000,000 involving share/ownership transfer described above. For clarification, Kandi Vehicles is not required to remit payment of the RMB40,000,000 transfer price to Yongkang KS Electric.

On June 29, 2012, the Company entered into a Share Transfer Agreement with a non-affiliated third-party, Mr. Chen Huabin. Pursuant to the terms and conditions of this agreement, the Company sold, transferred and assigned all of its interest in and to certain shell subsidiaries, KO NGA Investment Limited and its subsidiaries, to Mr. Chen Huabin for \$1.00. This transaction did not have a material impact on the Company s operating results or financial position.

The Company s organization chart as of this reporting date is as follows:



**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 (UNAUDITED)**

**NOTE 1 ORGANIZATION AND PRINCIPAL ACTIVITIES (CONTINUED)**

Kandi Vehicles has a 50% ownership interest and controls the Board of Directors in Kandi New Energy. Under Share Escrow and Trust Agreement, Loan Agreement, Contractor Agreement, between Kandi Vehicles and the other equity owner, Kandi Vehicles is entitled to 100% of the economic benefits, voting rights and residual interests (100% profits and loss absorption rate) in Kandi New Energy.

The primary operations of the Company are designing, developing, manufacturing, and commercializing of all-terrain vehicles, go-karts, and specialized automobile related products for the PRC and global markets.

**NOTE 2 LIQUIDITY**

As of June 30, 2012, the Company's working capital surplus was \$23,371,747.

As of June 30, 2012, the Company had credit lines from commercial banks of \$41,457,664, of which \$31,330,601 was used as of June 30, 2012.

The Company believes that its cash flows generated internally may not be sufficient to support growth of future operations and repay short term bank loans for the next twelve months if needed. However, the Company believes its access to existing financing sources and established relationships with PRC banks will enable it to meet its obligations and fund its ongoing operations.

The Company has historically financed itself through short-term commercial bank loans from PRC banks. The terms of these loans are typically for one year, and upon the payment of all outstanding principal and interest on such loans, the banks have typically rolled over these loans for additional one-year terms, with adjustments made to the interest rate to reflect prevailing market rates. The Company believes this situation has not changed and short-term bank loans will be available on normal trade terms if needed.

**NOTE 3 BASIS OF PRESENTATION**

The Company maintains its general ledger and journals with the accrual method accounting for financial reporting purposes. The financial statements and notes are representations of management. Accounting policies adopted by the Company conform to generally accepted accounting principles in the United States of America and have been consistently applied in the presentation of financial statements.

The financial information included herein for the six month periods ended June 30, 2012 and 2011 is unaudited; however, such information reflects all adjustments, consisting of normal recurring adjustments, that are, in the opinion of management, necessary for a fair presentation of the Company's condensed consolidated financial statements for these interim periods.

The results of operations for the six month period ended June 30, 2012 are not necessarily indicative of the results expected for the entire fiscal year ending December 31, 2012.

**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 (UNAUDITED)**

**NOTE 4 PRINCIPLES OF CONSOLIDATION**

The consolidated financial statements reflect the accounts of the Company and its ownership interest in following subsidiaries:

- (i) Continental Development, Ltd. ( Continental ) (a wholly-owned subsidiary of the Company)
- (ii) Zhejiang Kandi Vehicles Co., Ltd. ( Kandi Vehicles ) (a wholly-owned subsidiary of Continental)
- (iii) Jinhua Three Parties New Energy Vehicles Service Co., Ltd. ( Jinhua Service ) (a 30% owned subsidiary of Kandi Vehicles)
- (iv) Jinhua Kandi New Energy Vehicles Co., Ltd. ( Kandi New Energy ) (a 50% owned subsidiary of Kandi Vehicles with 100% profits and loss absorption due to contractual agreement)
- (v) Yongkang Scrou Electric. Co., Ltd (a wholly-owned subsidiary of Kandi Vehicles)

Inter-company accounts and transactions have been eliminated in a consolidation.

**NOTE 5 USE OF ESTIMATES**

The preparation of financial statements in conformity with generally accepted accounting principles in the United States 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 consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. Management makes these estimates using the best information available at the time the estimates are made; however actual results when ultimately realized could differ from those estimates.

**NOTE 6 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**(a) Economic and Political Risks**

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

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

**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 (UNAUDITED)**

**NOTE 6 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)****(b) Fair Value of Financial Instruments**

ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market.

These tiers include:

- Level 1 defined as observable inputs such as quoted prices in active markets;
- Level 2 defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and
- Level 3 defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

The assets measured at fair value on a recurring basis subject to the disclosure requirements of ASC 820 as of June 30, 2012 are as follows:

|                           | Fair Value Measurements at Reporting Date Using Quoted Prices in |              |              |   |
|---------------------------|--|--------------|--------------|---|
|                           | Active Markets   | Significant  | Significant  |   |
|                           | for  | Other        | Unobservable |   |
| Carrying value            | Identical Assets   | Observable   | Inputs       |   |
| as                        | (Level 1)  | Inputs       | (Level 3)    |   |
| of June 30,               |  | (Level 2)    |              |   |
| 2012                      |  |              |              |   |
| Cash and cash equivalents | \$ 3,979,148   | \$ 3,979,148 | -            | - |
| Restricted cash           | 26,803,826   | 26,803,826   | -            | - |
| Warrants                  | 1,957,885  | -            | 1,957,885    | - |

Cash and cash equivalents consist primarily of highly rated money market funds at a variety of well-known institutions with original maturities of three months or less. Restricted cash represents time deposits on account, some of which is used to secure short-term bank loans and notes payable. The original cost of these assets approximates fair value due to their short term maturity.

Warrants which are accounted as liabilities, are treated as derivative instruments, which will be measured at each reporting date for their fair value using Level 2 inputs. Also see Note 6 section (s).

The Company's non-financial assets are measured on a recurring basis. These non-financial assets are measured for impairment annually on the Company's measurement date at the reporting unit level using Level 3 inputs. For most assets, ASC 820 requires that the impact of changes resulting from its application be applied prospectively in the year in which the statement is initially applied.

The Company's non-financial assets measured on a non-recurring basis include the Company's property, plant and equipment and finite-use intangible assets which are measured for recoverability when indicators for impairment are present. ASC 820 requires companies to disclose assets and liabilities measured on a non-recurring basis in the period

in which the remeasurement at fair value is performed. The Company has reviewed its long-lived assets as of June 30, 2012 and determined that there are no significant assets to be tested for recoverability under ASC 360 and as such, no fair value measurements related to non-financial assets have been made during the six months ended June 30, 2012.

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**NOTE 6 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)****(c) Cash and Cash Equivalents**

The Company considers highly liquid investments purchased with original maturities of three months or less to be cash equivalents.

Restricted cash on June 30, 2012 and December 31, 2011 represent time deposits on account, some of which are used to secure short-term bank loans and notes payable. As of June 30, 2012, our restricted cash was as set forth on the table below:

| Purpose   | Amount       |
|---|--------------|
| Used to secure short-term bank loans (also see Note 14) | \$ 2,373,531 |
| Used to secure note payable (also see Note 15)          | 13,608,241   |
| Pure time deposits                                      | 10,822,054   |
| Total   | 26,803,826   |

**(d) Inventories**

Inventories are stated at the lower of cost or net realizable value (market value). The cost of raw materials is determined on the basis of weighted average. The cost of finished goods is determined on the weighted average basis and comprises direct materials, direct labor and an appropriate proportion of overhead.

Net realizable value is based on estimated selling prices less any further costs expected to be incurred for completion and selling expense.

**(e) Accounts Receivable**

Accounts receivable are recognized and carried at net realizable value. An allowance for doubtful accounts will be recorded in the period when a loss is probable based on an assessment of specific evidence indicating troubled collection, historical experience, accounts aging, ongoing business relation and other factors. Accounts are written off after exhaustive efforts at collection. If accounts receivable are to be provided for, or written off, they would be recognized in the consolidated statement of operations within operating expenses. At June 30, 2012 and December 31, 2011, the Company has no allowance for doubtful accounts, as per the management's judgment based on their best knowledge.

As of June 30, 2012 and December 31, 2011, the longest credit term used, in connection with certain selected customers was 120 days.

**(f) Note receivable**

Notes receivable represents short-term loans to third parties with the maximum term of one year. Interest income is recognized according to each agreement between a borrower and the Company on an accrual basis. If notes receivable are to be provided for, or written off, they are recognized in the relevant year if the loan default is probable, reasonably sure and the loss can be reasonably estimated. The Company recognizes income if the written-off loan is recovered at a future date. In case of foreclosure procedures or legal actions being taken, the Company provides accrual for the related foreclosure expense and related litigation expenses.



**(g) Prepayments**

Prepayments represent cash paid in advance to suppliers. As of June 30, 2012, prepayments included cash paid advances to raw material suppliers and prepaid expenses, such as water and electricity fees.

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**NOTE 6 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**(h) Plant and Equipment**

Plant and equipment are carried at cost less accumulated depreciation. Depreciation is provided over their estimated useful lives, using the straight-line method. Leasehold improvements are amortized over the life of the asset or the term of the lease, whichever is shorter. Estimated useful lives are as follows:

|                         |          |
|-------------------------|----------|
| Buildings               | 30 years |
| Machinery and equipment | 10 years |
| Office equipment        | 5 years  |
| Motor vehicles          | 5 years  |
| Moulds                  | 5 years  |

The cost and related accumulated depreciation of assets sold or otherwise retired are eliminated from the accounts and any gain or loss is included in the statement of income. The cost of maintenance and repairs is charged to expense as incurred, whereas significant renewals and betterments are capitalized.

**(i) Construction in Progress**

Construction in progress represents direct costs of construction or the acquisition cost of buildings or machinery and design fees. Capitalization of these costs ceases and the construction in progress is transferred to plant and equipment when substantially all of the activities necessary to prepare the assets for their intended use are completed. No depreciation is provided until the assets are completed and ready for their intended use.

**(j) Land Use Rights**

According to the laws of China, land in the PRC is owned by the government and its ownership cannot be sold to an individual or a company. However, the government grants the user a land use right to use the land. The land use rights granted to the Company are being amortized using the straight-line method over the lease term of fifty years.

**(k) Accounting for the Impairment of Long-Lived Assets**

The Company periodically evaluates the carrying value of long-lived assets to be held and used, including intangible assets subject to amortization, when events and circumstances warrant such a review, pursuant to the guidelines established in ASC No. 350. The carrying value of a long-lived asset is considered impaired when the anticipated undiscounted cash flow from such asset is separately identifiable and is less than its carrying value. In that event, a loss is recognized based on the amount by which the carrying value exceeds the fair market value of the long-lived asset. Fair market value is determined primarily using the anticipated cash flows discounted at a rate commensurate with the risk involved. Losses on long-lived assets to be disposed of are determined in a similar manner, except that fair market values are reduced for the cost to dispose.

During the reporting period, there was no impairment loss.

**(l) Revenue Recognition**

Revenues represent the invoiced value of goods sold, recognized upon the shipment of goods to customers. Revenues are recognized when all of the following criteria are met:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred or services have been rendered;
- The seller's price to the buyer is fixed or determinable; and
- Collectability is reasonably assured.

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**NOTE 6 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)****(m) Research and Development**

Expenditures relating to the development of new products and processes, including significant improvement to existing products are expensed as incurred. Research and development expenses were \$1,376,186 and \$1,086,540 for the six months ended June 30, 2012 and 2011, respectively.

**(n) Government Grant**

Grants received from the PRC Government for assisting in the Company's technical research and development efforts are netted against the relevant research and development costs incurred when the proceeds are received or collectible.

For the six months ended June 30, 2012 and 2011, \$25,308 and \$280,727, respectively, was received from the PRC government for the Company's contribution to the local economy.

**(o) Income Taxes**

The Company accounts for income tax using an asset and liability approach and allows for recognition of deferred tax benefits in future years. Under the asset and liability approach, deferred taxes are provided for the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The accounting for deferred tax calculation represents the management's best estimate on the most likely future tax consequences of events that have been recognized in our financial statements or tax returns and related future anticipation. A valuation allowance is provided for deferred tax assets if it is more likely than not these items will either expire before the Company is able to realize their benefits, or that future realization is uncertain.

**(p) Foreign Currency Translation**

The accompanying consolidated financial statements are presented in United States dollars. The functional currency of the Company is the Renminbi (RMB). Capital accounts of the consolidated financial statements are translated into United States dollars from RMB at their historical exchange rates when the capital transactions occurred.

Assets and liabilities are translated at the exchange rates as of balance sheet date. Income and expenditures are translated at the average exchange rate of the year, which was obtained from website: <http://www.oanda.com>

|                                    | <b>June 30,<br/>2012</b> | <b>December 31,<br/>2011</b> | <b>June 30,<br/>2011</b> |
|------------------------------------|--------------------------|------------------------------|--------------------------|
| Period end RMB : USD exchange rate | 6.3197                   | 6.3647                       | 6.4640                   |
| Average RMB : USD exchange rate    | 6.3255                   | 6.4735                       | 6.5482                   |

**(q) Comprehensive Income**

Comprehensive income is defined to include all changes in equity except those resulting from investments by owners and distributions to owners. Among other disclosures, all items that are required to be recognized under current accounting standards as components of comprehensive income are required to be reported in a financial statement that is presented with the same prominence as other financial statements. Comprehensive income includes net income and

the foreign currency translation changes.

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**NOTE 6 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**(r) Stock Option Cost**

The Company's stock option cost is recorded in accordance with ASC 718 and ASC 505.

The fair value of stock options is estimated using the Black-Scholes-Merton model. The Company's expected volatility assumption is based on the historical volatility of the Company's stock. The expected life assumption is primarily based on the expiration date of the option. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

Stock option expense recognized is based on awards expected to vest, and there were no estimated forfeitures. ASC standards requires forfeitures to be estimated at the time of grant and revised in subsequent periods, if necessary, if actual forfeitures differ from those estimates.

The stock based compensation expense for the period ended June 30, 2012 was \$19,053. Also see Note 17.

**(s) Warrant Cost**

The Company's warrant costs are recorded in liabilities and equities respectively in accordance with ASC 480, ASC 505 and ASC 815.

The fair value of warrants, which is classified as a liability, is estimated using the Black-Scholes-Merton model. The Company's expected volatility assumption is based on the historical volatility of the Company's stock. The expected life assumption is primarily based on the expiration date of the warrant. The risk-free interest rate for the expected term of the warrant is based on the U.S. Treasury yield curve in effect at the time of measurement. The warrants, which are freestanding derivatives and are classified as liabilities on the balance sheet, will be measured at fair value on each reporting date, with decreases in fair value recognized in earnings and increases in fair values were recognized in expenses.

The Company determined that the fair value of equity based warrants, which are not considered derivatives under ASC 815, is estimated using the Black-Scholes-Merton model. The Company's expected volatility assumption is based on the historical volatility of the Company's stock. The expected life assumption is primarily based on the expiration date of the warrant. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

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**NOTE 7 NEW ACCOUNTING PRONOUNCEMENTS**

**Recent Accounting Pronouncements**

In April 2011, the Financial Accounting Standard Board ( FASB ) issued Accounting Standard Update ( ASU ) ASU 2011-03, Consideration of Effective Control on Repurchase Agreements, which deals with the accounting for repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. ASU 2011-03 changes the rules for determining when these transactions should be accounted for as financings, as opposed to sales. The guidance in ASU 2011-03 is effective for the first interim or annual period beginning on or after December 15, 2011. The guidance should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. We adopted this ASU beginning January 1, 2012. The adoption of ASU 2011-03 did not have a material impact on the Company's financial condition or results of operation.

In May 2011, the FASB issued ASU 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards ( IFRS ). ASU 2011-04 clarifies some existing concepts, eliminates wording differences between U.S. GAAP and IFRS, and in some limited cases, changes some principles to achieve convergence between U.S. GAAP and IFRS. ASU 2011-04 results in a consistent definition of fair value and common requirements for measurement of and disclosure about fair value between U.S. GAAP and IFRS. ASU 2011-04 also expands the disclosures for fair value measurements that are estimated using significant unobservable (Level 3) inputs. ASU 2011-04 will be effective for the Company beginning after December 15, 2011. We adopted this ASU beginning January 1, 2012. The adoption of ASU 2011-04 did not have a material impact on the Company's operating results or financial position.

In June 2011, FASB issued ASU 2011-05, Presentation of Comprehensive Income, which requires an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income, or in two separate but consecutive statements. ASU 2011-05 eliminates the option to present components of other comprehensive income as part of the statement of equity. ASU 2011-05 will be effective for the Company beginning after December 15, 2011. We adopted this ASU beginning January 1, 2012. The adoption of ASU 2011-05 did not have a material impact on the Company's operating results or financial position.

In September 2011, the FASB has issued Accounting Standards Update (ASU) No. 2011-08, Intangibles Goodwill and Other (Topic 350): Testing Goodwill for Impairment. ASU 2011-08 is intended to simplify how entities, both public and nonpublic, test goodwill for impairment. ASU 2011-08 permits an entity to first assess qualitative factors to determine whether it is "more likely than not" that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350, *Intangibles-Goodwill and Other*. The more-likely-than-not threshold is defined as having a likelihood of more than 50%. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued or, for nonpublic entities, have not yet been made available for issuance. We adopted this ASU beginning January 1, 2012. The adoption of ASU 2011-08 did not have a material impact on the Company's operating results or financial position.





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**NOTE 7 NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)**

**Recent Accounting Pronouncements (Continued)**

In December 2011, the FASB has issued ASU No. 2011-11, *Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities*. ASU No. 2011-11 is intended to provide enhanced disclosures that will enable users of its financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position. This includes the effect or potential effect of rights of setoff associated with an entity's recognized assets and recognized liabilities within the scope of this Update. The amendments require enhanced disclosures by requiring improved information about financial instruments and derivative instruments that are either (i) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (ii) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either Section 210-20-45 or Section 815-10-45. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. The Company is evaluating whether the adoption of ASU 2011-11 will have a material effect on its operating results or financial position; however, the Company does not expect the adoption of ASU No. 2011-11 to have a material effect on its operating results or financial position.

In December 2011, the FASB has issued ASU No. 2011-12, *Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05*. ASU No. 2011-12 is intended to supersede certain pending paragraphs in Accounting Standards Update No. 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income*, to effectively defer only those changes in Update 2011-05 that relate to the presentation of reclassification adjustments out of accumulated other comprehensive income. The amendments will be temporary to allow the Board time to redeliberate the presentation requirements for reclassifications out of accumulated other comprehensive income for annual and interim financial statements for public, private, and nonprofit entities. All other requirements in ASU No. 2011-05 are not affected by ASU No. 2011-12, including the requirement to report comprehensive income either in a single continuous financial statement or in two separate but consecutive financial statements. Public entities should apply these requirements for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of ASU 2011-12 did not have a material impact on the Company's operating results or financial position.

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**NOTE 8 CONCENTRATIONS****(a) Customers**

The Company's major customers for the period ended June 30, 2012 accounted for the following percentages of total sales and accounts receivable as follows:

| Major Customers | Sales                          |                                | Accounts Receivable |                   |
|-----------------|--------------------------------|--------------------------------|---------------------|-------------------|
|                 | Six Months Ended June 30, 2012 | Six Months Ended June 30, 2011 | June 30, 2012       | December 31, 2011 |
| Company A       | 55%                            | -                              | 58%                 | 2%                |
| Company B       | 26%                            | 15%                            | 22%                 | 18%               |
| Company C       | 11%                            | 11%                            | 18%                 | 56%               |
| Company D       | -                              | -                              | -                   | -                 |
| Company E       | -                              | 2%                             | -                   | 1%                |

**(b) Suppliers**

The Company's major suppliers for the six months ended June 30, 2012 accounted for the following percentage of total purchases and accounts payable as follows:

| Major Suppliers | Purchases                      |                                | Accounts Payable |                   |
|-----------------|--------------------------------|--------------------------------|------------------|-------------------|
|                 | Six Months Ended June 30, 2012 | Six Months Ended June 30, 2011 | June 30, 2012    | December 31, 2011 |
| Company F       | 48%                            | 77%                            | 4%               | 1%                |
| Company G       | 25%                            | 2%                             | 18%              | -                 |
| Company H       | 2%                             | 1%                             | 1%               | 1%                |
| Company I       | 2%                             | 1%                             | 2%               | -                 |
| Company J       | 1%                             | 1%                             | 1%               | 1%                |

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**NOTE 9 INCOME (LOSS) PER SHARE**

The Company calculates earnings per share in accordance with ASC 260, Earnings Per Share, which requires a dual presentation of basic and diluted earnings per share. Basic earnings per share are computed using the weighted average number of shares outstanding during the reporting period. Diluted earnings per share represents basic earnings per share adjusted to include the potentially dilutive effect of outstanding stock options, warrants and convertible note (using the if-converted method). For the six months ended June 30, 2012, there are 1,343,221 potentially dilutive common shares.

The following table sets forth the computation of basic and diluted net income per common share:

| Six months Ended June 30,                           | 2012         | 2011         |
|---|--------------|--------------|
| Net income (loss)                                   | \$ 3,288,180 | \$ 9,559,743 |
| Weighted average shares of common stock outstanding |              |              |
| Basic   | 28,647,746   | 27,431,851   |
| Dilutive shares                                     | 1,343,221    | 1,354,294    |
| Diluted   | 29,990,967   | 28,786,145   |
| Basic income per share                              | \$ 0.11      | \$ 0.35      |
| Diluted income per share                            | \$ 0.11      | \$ 0.33      |

Also see Note 17.

**NOTE 10 - INVENTORIES**

Inventories are summarized as follows:

|   | <b>June 30, 2012</b> |            | <b>December 31, 2011</b> |           |
|---|----------------------|------------|--------------------------|-----------|
|   | <b>(Unaudited)</b>   |            |                          |           |
| Raw material                              | \$                   | 2,305,961  | \$                       | 1,737,211 |
| Work-in-progress                          |                      | 9,552,283  |                          | 3,898,950 |
| Finished goods                            |                      | 1,696,386  |                          | 1,110,793 |
|   |                      | 13,554,630 |                          | 6,746,954 |
| Less: reserve for slow moving inventories |                      | -          |                          | (72,487)  |
| Inventories, net                          | \$                   | 13,554,630 | \$                       | 6,674,467 |

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**NOTE 11 - NOTES RECEIVABLE**

Notes receivable are summarized as follows:

|   | <b>June 30,<br/>2012<br/>(Unaudited)</b> | <b>December<br/>31,<br/>2011</b> |
|---|--|----------------------------------|
| Notes receivable from unrelated companies:                      |  |                                  |
| Due April 7, 2012, interest at 9.6% per annum <sup>1</sup>      | \$ -                                     | \$ 4,713,498                     |
| Due September 30, 2012, interest at 9.6% per annum <sup>2</sup> | 15,004,641                               | 33,165,745                       |
|   | 15,004,641                               | 37,879,243                       |

Bank acceptance notes:

|                       |               |               |
|-----------------------|---------------|---------------|
| Bank acceptance notes | -             | -             |
| Notes receivable      | \$ 15,004,641 | \$ 37,879,243 |

Details of Notes receivable from unrelated parties as of December 31, 2011

| Index | Amount (\$) | Counter party                          | Relationship                | Purpose of Loan         | Manner of settlement |
|-------|-------------|--|-----------------------------|-------------------------|----------------------|
| 1     | 4,713,498   | Zhejiang XinNeng Auto System Co., Ltd. | No relationship beyond loan | Receive interest income | Repaid in cash       |
| 2     | 33,165,745  | Yongkang HuiFeng Guarantee Co., Ltd    | No relationship beyond loan | Receive interest income | Not Due              |

Details of Notes receivable from unrelated parties as of June 30, 2012

| Index | Amount (\$) | Counter party                       | Relationship                | Purpose of Loan         | Manner of settlement |
|-------|-------------|-------------------------------------|-----------------------------|-------------------------|----------------------|
| 2     | 15,004,641  | Yongkang HuiFeng Guarantee Co., Ltd | No relationship beyond loan | Receive interest income | Not due              |

For the six months ended June 30, 2012, the interest income generated from the notes receivable issued to third parties was \$1,212,874.

**NOTE 12 LAND USE RIGHTS**

Land use rights consist of the following:

|                                | <b>June 30, 2012<br/>(Unaudited)</b> | <b>December 31, 2011</b> |
|--------------------------------|--------------------------------------|--------------------------|
| Cost of land use rights        | \$ 15,688,190                        | \$ 11,997,512            |
| Less: Accumulated amortization | (1,185,282)                          | (1,004,743)              |
| Land use rights, net           | \$ 14,502,908                        | \$ 10,992,769            |

As of June 30, 2012 and December 31, 2011, the net book value of land use rights pledged as collateral for the Company's bank loans was \$4,012,970 and \$4,057,640, respectively. Also see Note 14.



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**NOTE 12 LAND USE RIGHTS (CONTINUED)**

As of June 30, 2012 and December 31, 2011, the net book value of land use rights pledged as collateral for bank loans borrowed by Zhejiang Mengdeli Electronic Co., Ltd. ( ZMEC ), an unrelated party of the Company was \$6,926,507 and \$6,935,129 respectively. Also see Note 19.

It is a common business practice among companies in the region of China where Kandi is located to exchange guarantees for bank debt with no consideration given. It is considered a favor for favor business practice and is commonly required by the lending banks as in these cases. ZMEC has provided a guarantee for certain of the Company's bank loans. As of June 30, 2012, ZMEC had guaranteed bank loan of the Company for a total of \$12,658,829. In exchange, the Company provided guarantee for bank loans being borrowed by ZMEC and allowing ZMEC to pledge the Company's assets for ZMEC's bank loans. Also see Note 14 and Note 19.

The amortization expense for the six months ended June 30, 2012 and 2011 was \$173,226 and \$126,977 respectively.

Amortization expense for the next five years and thereafter is as follows:

|                   |    |            |
|-------------------|----|------------|
| 2012 (six months) | \$ | 173,226    |
| 2013              |    | 346,452    |
| 2014              |    | 346,452    |
| 2015              |    | 346,452    |
| 2016              |    | 346,452    |
| Thereafter        |    | 12,943,874 |
| Total             | \$ | 14,502,908 |

**NOTE 13 PLANT AND EQUIPMENT**

Plant and equipment consist of the following:

|                                 | <b>June 30, 2012</b> |              | <b>December 31, 2011</b> |              |
|---------------------------------|----------------------|--------------|--------------------------|--------------|
|                                 | <b>(Unaudited)</b>   |              |                          |              |
| At cost:                        |                      |              |                          |              |
| Buildings                       | \$                   | 14,029,790   | \$                       | 13,698,216   |
| Machinery and equipment         |                      | 10,367,216   |                          | 10,138,064   |
| Office equipment                |                      | 223,736      |                          | 199,021      |
| Motor vehicles                  |                      | 249,790      |                          | 246,243      |
| Moulds                          |                      | 15,431,766   |                          | 15,286,217   |
|                                 |                      | 40,302,298   |                          | 39,567,761   |
| Less : Accumulated depreciation |                      |              |                          |              |
| Buildings                       | \$                   | (2,201,223)  | \$                       | (1,949,251)  |
| Machinery and equipment         |                      | (8,620,113)  |                          | (8,032,798)  |
| Office equipment                |                      | (150,635)    |                          | (131,813)    |
| Motor vehicles                  |                      | (190,494)    |                          | (175,578)    |
| Moulds                          |                      | (9,855,484)  |                          | (8,296,428)  |
|                                 |                      | (21,017,949) |                          | (18,585,868) |
| Plant and equipment, net        | \$                   | 19,284,349   | \$                       | 20,981,893   |



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**NOTE 13 PLANT AND EQUIPMENT (CONTINUED)**

As of June 30, 2012 and December 31, 2011, the net book value of plant and equipment pledged as collateral for the bank loans was \$7,012,941 and \$7,124,618, respectively.

As of June 30, 2012 and December 31, 2011, the net book value of plant and equipment pledged as collateral for bank loans borrowed by ZMEC, a supplier but unrelated party of the Company was \$4,589,755 and \$4,624,347, respectively. Also see Note 19.

Depreciation expense for six months ended June 30, 2012 and 2011 was \$2,300,379 and \$2,190,463 respectively.

**NOTE 14 SHORT TERM BANK LOANS**

Short-term loans are summarized as follows:

|   | <b>June 30,<br/>2012<br/>(Unaudited)</b> | <b>December<br/>31,<br/>2011</b> |
|---|--|----------------------------------|
| <b>Loans from China Communication Bank-Jinhua Branch</b>  |  |                                  |
| Monthly interest only payments at 7.87% per annum, due September 19, 2012, guaranteed by Kandi Investment Group Co.   | \$ 791,177                               | \$ 785,583                       |
| <b>Loans from Commercial Bank-Jiangnan Branch</b>   |  |                                  |
| Monthly interest only payments at 5.81% per annum, due January 3, 2012, guaranteed by Zhejiang Kangli Metal Manufacturing Company, Mr. Hu Xiaoming, Lv Qingjiang, and Ms. Ling Yueping. and pledged by the assets of Jingdezheng De'er Investment Industrial Co., Ltd.    | -  | 3,142,332                        |
| Monthly interest only payments at 6.56% per annum, due October 15, 2012, guaranteed by Mr. Hu Xiaoming, and Ms. Ling Yueping, and secured by Company's assets. Also see Note 12 and Note 13.  | 1,582,354                                | 1,571,166                        |
| Monthly interest only payments at 6.89% per annum, due December 5, 2012, secured by Company's asset. Also see Note 12 and Note 13.  | 791,177                                  | 785,583                          |
| Monthly interest only payments at 6.89% per annum, due January 5, 2013, guaranteed by Zhejiang Kangli Metal Manufacturing Company, Mr. Hu Xiaoming, Ms. Ling Jiajia, and Ms. Ling Yueping. and pledged by the assets of Jingdezheng De'er Investment Industrial Co., Ltd. | 3,164,707                                | -                                |
| <b>Loans from Huaxia Bank</b>   |  |                                  |
|   | 4,430,590                                | 4,399,265                        |



Monthly interest only payments at 7.22% per annum, due September 23, 2012, secured by the assets of the Company, guaranteed by Mr. Hu Xiaoming, Ms. Ling Yueping, Zhejiang Kangli Metal Manufacturing Company and Kandi Investment Group Co. Also see Note 12 and Note 13.

**Loans from China Ever-bright Bank**

|  |   |           |
|--|---|-----------|
| Interest only payment at 6.71% per annum, due February 15, 2012. | - | 3,142,332 |
|--|---|-----------|

|  |   |           |
|--|---|-----------|
| Monthly interest only payments at 6.10% per annum, due May 15, 2012, secured by the Company's time deposit. Also see Note 6. | - | 2,121,073 |
|--|---|-----------|

|  |           |   |
|--|-----------|---|
| Interest only payment at 7.02% per annum, due June 28, 2012. | 3,133,060 | - |
|--|-----------|---|

|   |           |           |
|---|-----------|-----------|
| Monthly interest only payments at 7.74% per annum, due August 27, 2012, secured by the assets of the Company, guaranteed by Mr. Hu Xiaoming, Ms. Ling Yueping, Nanlong Group Co., Ltd. and Zhejiang Mengdeli Electric Co., Ltd. Also see Note 12 and Note 13. | 4,747,061 | 4,713,498 |
|---|-----------|-----------|

|   |           |           |
|---|-----------|-----------|
| Monthly interest only payments at 7.74% per annum, due August 27, 2012, secured by the assets of the Company, guaranteed by Mr. Hu Xiaoming, Nanlong Group Co., Ltd. and Zhejiang Mengdeli Electric Co., Ltd. Also see Note 12 and Note 13. | 4,747,061 | 4,713,498 |
|---|-----------|-----------|

|   |           |   |
|---|-----------|---|
| Monthly interest only payments at 6.71% per annum, due November 25, 2012, secured by the Company's time deposit. Also see Note 6. | 2,136,177 | - |
|---|-----------|---|

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**NOTE 14 - SHORT TERM BANK LOANS (CONTINUED)**

|  | June 30,<br>2012<br>(Unaudited) | December<br>31,<br>2011 |
|--|---------------------------------|-------------------------|
| <b>Loans from Shanghai Pudong Development Bank</b>   |                                 |                         |
| Monthly interest only payments at 6.71% per annum, due June 26, 2012, secured by the property of Ms. Ling Yueping, guaranteed by Nanlong Group Co., Ltd. and Mr. Hu Xiaoming   | -                               | 3,142,332               |
| Monthly interest only payments at 6.94% per annum, due June 27, 2013, secured by the property of Ms. Ling Yueping, guaranteed by Yongkang KangBang auto parts Co., Ltd. and Mr. Hu Xiaoming                              | 3,164,707                       | -                       |
| <b>Loans from Bank of Shanghai</b>   |                                 |                         |
| Monthly interest only payments at 6.56% per annum, due December 4, 2012, guaranteed by Mr. Hu Xiaoming, Ms. Ling Yueping, Zhejiang Kangli Metal Manufacturing Company and Zhejiang Taiping Shengshi Industrial Co., Ltd. | 4,747,061                       | 4,713,498               |
| <b>Loans from China Ever-growing Bank</b>  |                                 |                         |
| Monthly interest only payments at 7.57% per annum, due April 27, 2012, guaranteed by Mr. Hu Xiaoming, Ms. Ling Yueping, Zhejiang Shuguang industrial Co., Ltd. and Zhejiang Mengdeli Electric Company.                   | -                               | 3,142,332               |
| Monthly interest only payments at 7.87% per annum, due April 24, 2013, guaranteed by Mr. Hu Xiaoming, Ms. Ling Yueping, Zhejiang Shuguang industrial Co., Ltd. and Zhejiang Mengdeli Electric Company.                   | 3,164,707                       | -                       |
| <b>Total</b>   | <b>\$ 36,599,839</b>            | <b>\$ 36,372,492</b>    |

Interest expense for the six month ended June 30, 2012 and 2011 was \$1,313,868, and \$870,597, respectively.

As of June 30, 2012, the aggregate amount of short-term loans that were guaranteed by various third parties was \$30,539,425,

- \$12,658,829 is guaranteed by Zhejiang Mengdeli Electric Co Ltd ( ZMEC ), whose bank note of \$1,265,883 is guaranteed by the Company, and ZMEC 's bank loans of \$7,057,297 are secured by a pledge, or by the Company 's plant and equipment and the land use right for which net book values are \$4,589,755, and \$6,926,507, respectively. Also see Note 19.

- \$12,342,358 is guaranteed by Zhejiang Kangli Metal Manufacturing Company, whose bank loans of \$4,747,061 is guaranteed by the Company. Also see Note 19.

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- \$3,164,707 is guaranteed by Zhejiang Shuguang industrial Co., Ltd., whose bank loans of \$7,911,768 are guaranteed by the Company. Also see Note 19.
- \$4,747,061 is guaranteed by Zhejiang Taiping Shengshi Industrial Co., Ltd. whose bank loans of \$3,164,707 is also guaranteed by the Company. Also see Note 19.
- \$5,221,767 is guaranteed by Kandi Investment Group Co.
- \$9,494,122 is guaranteed by Nanlong Group Co., Ltd.
- \$3,164,707 is guaranteed by Yongkang KangBang auto parts Co., Ltd.

This is a common business practice among companies in the region of China where Kandi is located to exchange guarantees for bank debt with no consideration given. It is considered a "favor for favor" business practice and is commonly required by the lending banks as in these cases.

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**NOTE 15 NOTES PAYABLE**

By issuing bank note payables rather than paying cash to suppliers, the Company can defer the payments until the date the bank note payable is due. Simultaneously, the Company needs to deposit restricted cash in banks to back up the bank note payable, while the restricted cash deposited in banks will generate interest income.

Notes payable are summarized as follows:

|                        | June 30,2012<br>(Unaudited) | December 31,<br>2011 |
|------------------------|-----------------------------|----------------------|
| Bank acceptance notes: |                             |                      |
| Due January 19,2012    | \$ -                        | \$ 149,262           |
| Due March 26, 2012     | -                           | 14,140               |
| Due March 26, 2012     | -                           | 15,712               |
| Due March 26, 2012     | -                           | 37,708               |
| Due March 26, 2012     | -                           | 15,712               |
| Due March 26, 2012     | -                           | 17,283               |
| Due March 26, 2012     | -                           | 15,712               |
| Due March 26, 2012     | -                           | 14,140               |
| Due March 26, 2012     | -                           | 7,856                |
| Due March 26, 2012     | -                           | 6,285                |
| Due March 26, 2012     | -                           | 15,712               |
| Due March 26, 2012     | -                           | 15,712               |
| Due March 26, 2012     | -                           | 7,856                |
| Due March 26, 2012     | -                           | 31,423               |
| Due March 26, 2012     | -                           | 9,741                |
| Due March 26, 2012     | -                           | 9,427                |
| Due March 26, 2012     | -                           | 10,998               |
| Due March 26, 2012     | -                           | 31,423               |
| Due March 26, 2012     | -                           | 51,848               |
| Due March 26, 2012     | -                           | 47,135               |
| Due March 26, 2012     | -                           | 15,712               |
| Due March 26, 2012     | -                           | 4,713                |
| Due March 26, 2012     | -                           | 3,142                |
| Due March 26, 2012     | -                           | 3,142                |
| Due March 26, 2012     | -                           | 12,569               |
| Due March 26, 2012     | -                           | 15,712               |
| Due March 26, 2012     | -                           | 3,142                |
| Due March 26, 2012     | -                           | 3,142,332            |
| Due May 10, 2012       | -                           | 78,558               |
| Due May 10, 2012       | -                           | 157,117              |
| Due May 10, 2012       | -                           | 188,540              |
| Due May 10, 2012       | -                           | 94,270               |
| Due May 10, 2012       | -                           | 31,423               |
| Due June 19, 2012      | -                           | 235,675              |
| Due June 19, 2012      | -                           | 1,335,491            |

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|                        |               |              |
|------------------------|---------------|--------------|
| Due July 12, 2012      | 3,164,707     | -            |
| Due September 14, 2012 | 2,373,530     | -            |
| Due September 20, 2012 | 3,148,884     | -            |
| Due October 16, 2012   | 1,582,354     | -            |
| Due October 18, 2012   | 949,412       | -            |
| Due November 11, 2012  | 3,955,884     | -            |
| Subtotal               | \$ 15,174,771 | \$ 5,846,623 |

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**NOTE 15 NOTES PAYABLE (CONTINUED)**

Notes payable to unrelated companies:

|   |      |          |
|---|------|----------|
| Due January 20, 2012 (Interest rate 6.0% per annum) | -    | 1,000    |
| Subtotal  | \$ - | \$ 1,000 |

|       |               |              |
|-------|---------------|--------------|
| Total | \$ 15,174,771 | \$ 5,847,623 |
|-------|---------------|--------------|

The bank acceptance notes do not bear interest; however, these notes are subject to bank charges of 0.05% of the principal as commission on each transaction. Bank charges for notes payable were \$7,580 for the first six months ended June 30, 2012.

Restricted cash of \$13,608,241 is held as collateral for the following notes payable at June 30, 2012:

|                        |               |
|------------------------|---------------|
| Due July 12, 2012      | 3,164,707     |
| Due September 14, 2012 | 2,373,530     |
| Due September 20, 2012 | 3,148,884     |
| Due October 16, 2012   | 1,582,354     |
| Due October 18, 2012   | 949,412       |
| Due November 11, 2012  | 3,955,884     |
| Total                  | \$ 15,174,771 |

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**KANDI TECHNOLOGIES, CORP.  
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**NOTE 16 TAX**

**(a) Corporation Income Tax ( CIT )**

On March 16, 2007, the National People's Congress of China approved the Corporate Income Tax Law of the People's Republic of China (the new CIT law), which went into effect on January 1, 2008. In accordance with the relevant tax laws and regulations of the PRC, the applicable corporate income tax rate is 25%.

Prior to January 1, 2008, the CIT rate applicable to the Company was 33%. Kandi's first profitable tax year for income tax purposes as a foreign-invested company was 2007. As a foreign-invested company, the income tax rate of Kandi was entitled to a 50% tax holiday based on 25% for years 2009 through 2011. During the transition period, the above tax concession granted to the Company, prior to the new CIT law, will be grandfathered according to the interpretations of the new CIT law. After the tax holiday period is ended, the tax rate applicable to Kandi Vehicle changes to 15% since 2012 because of Kandi Vehicle's high technology enterprise qualification.

Kandi New Energy and Yongkang Scrou Electric Co., Ltd., are subsidiaries of the Company and their applicable corporate income tax rate is 25%.

According to the PRC corporation income tax ( CIT ) reporting system, the CIT sales cut-off base is concurrent with the value added tax ( VAT ) which will be reported to the State Administration of Taxation ( SAT ) on a quarterly basis. Since the VAT and CIT are accounted for on a VAT tax basis that recorded all sales on a State provided official invoices reporting system, the Company is reporting the CIT according to the SAT prescribed tax reporting rules. Under the VAT tax reporting system, sales cut-off did not take the accrual base but rather on a VAT taxable reporting basis. Therefore, when the company adopted US GAAP on accrual basis, the sales cut-off CIT timing difference which derived from the VAT reporting system will create a temporary sales cut-off timing difference and this difference is reflected in the deferred tax assets or liabilities calculations on the income tax estimation reported in the Form 10-K.

Effective January 1, 2007, the Company adopted ASC 740, Income Taxes. The interpretation addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements.

Under ASC 740, the Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. ASC 740 also provides guidance on de-recognition, classification, interest and penalties on income taxes, accounting in interim periods and requires increased disclosures. As of June 30, 2012, the Company does not have a liability for unrecognized tax benefits. The Company files income tax returns to the Internal Revenue Services ( IRS ) and states where the Company has operation. The Company is subject to U.S. federal or state income tax examinations by IRS and relevant state tax authorities for years after 2006. During the periods open to examination, the Company has net operating loss carry forwards ( NOLs ) for U.S. federal and state tax purposes that have attributes from closed periods. Since these NOLs may be utilized in future periods, they remain subject to examination. The Company also files certain tax returns in China. As of June 30, 2012 the Company was not aware of any pending income tax examinations by China tax authorities. The Company's policy is to record interest and penalties on uncertain tax provisions as income tax expense. As of June 30, 2012, the Company has no accrued interest or penalties related to uncertain tax

positions. The Company has not recorded a provision for U.S federal income tax for the three months ended June 30, 2012 due to the net operating loss carry forward in the United States.



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**NOTE 16 TAX (CONTINUED)**

Income tax expense (benefit) for the six months ended June 30, 2012 and 2011 is summarized as follows:

|                                  | <b>For the Six Months Ended</b> |             |
|----------------------------------|---------------------------------|-------------|
|                                  | <b>June 30,</b>                 |             |
|                                  | <b>(Unaudited)</b>              |             |
|                                  | <b>2012</b>                     | <b>2011</b> |
| Current:                         |                                 |             |
| Provision for CIT                | \$ 661,120                      | \$ 277,505  |
| Provision for Federal Income Tax |                                 | 0           |
| Deferred:                        | -                               | -           |
| Provision for CIT                |                                 | 0           |
| Income tax expense (benefit)     | \$ 661,120                      | \$ 277,505  |

The Company's income tax expense (benefit) differs from the expected tax expense for the six months ended June 30, 2012 and 2011 (computed by applying the CIT rate of 25%, respectively to income before income taxes) as follows:

|                                       | <b>For the Six Months Ended</b> |             |
|---------------------------------------|---------------------------------|-------------|
|                                       | <b>June 30,</b>                 |             |
|                                       | <b>(Unaudited)</b>              |             |
|                                       | <b>2012</b>                     | <b>2011</b> |
| Computed "expected" (benefit) expense | \$ 608,465                      | \$ 302,675  |
| Favorable tax rate                    | (600,060)                       | (277,505)   |
| Permanent differences                 | 650,463                         | 165,754     |
| Valuation allowance                   | 2,252                           | 86,581      |
| Income tax expense (benefit)          | \$ 661,120                      | \$ 277,505  |

The tax effects of temporary differences that give rise to the Company's net deferred tax assets and liabilities as of June 30, 2012 and December 31, 2011 are summarized as follows:

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**NOTE 16 TAX (CONTINUED)**

|   | June 30,<br>2012<br>(Unaudited) | December<br>31,<br>2011 |
|---|---------------------------------|-------------------------|
| Current portion:  |                                 |                         |
| Deferred tax assets:                                    |                                 |                         |
| Expense   | \$ 2,065                        | \$ (11,741)             |
| Subtotal  | 2,065                           | (11,741)                |
| Deferred tax liabilities:                               |                                 |                         |
| Sales cut-off (CIT tax reporting on VAT tax system)     | 17,242                          | (44,621)                |
| Other   | -                               | -                       |
| Subtotal  | 17,242                          | (44,621)                |
| Total deferred tax asset ( liabilities) current portion | 19,307                          | (56,362)                |
| Non-current portion:                                    |                                 |                         |
| Deferred tax assets:                                    |                                 |                         |
| Depreciation  | 179,282                         | 226,622                 |
| Loss carried forward                                    | 9,008                           | 1,351,513               |
| Valuation allowance                                     | (9,008)                         | (1,351,513)             |
| Subtotal  | 179,282                         | 226,622                 |
| Deferred tax liabilities:                               |                                 |                         |
| Accumulated other comprehensive gain                    | (136,642)                       | (136,624)               |
| Subtotal  | (136,642)                       | (136,624)               |
| Total deferred tax assets non-current portion           | 42,640                          | 89,998                  |
| Net deferred tax assets                                 | \$ 61,947                       | \$ 33,636               |

**(b) Tax Benefit (Holiday) Effect**

For the six months ended June 30, 2012 and 2011 the PRC corporate income tax rate was 25%. Certain subsidiaries of the Company are entitled to tax benefit (holidays) for the six months ended June 30, 2012 and 2011.

The combined effects of the income tax expense exemptions and reductions available to the Company for the six months ended June 30, 2012 and 2011 are as follows:

|                                   | For the Six Months Ended<br>June 30<br>(Unaudited) |            |
|-----------------------------------|--|------------|
|                                   | 2012   | 2011       |
| Tax benefit (holiday) credit      | \$ 600,060   | \$ 277,505 |
| Basic net income per share effect | \$ 0.02  | \$ 0.01    |



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**NOTE 17 STOCK OPTIONS, WARRANTS AND CONVERTIBLE NOTES****(a) Stock Options**

On February 11, 2009, the Compensation Committee of the Board of Directors of the Company approved the grant of stock options for 2,600,000 shares of common stock to ten of the Company's employees and directors. The stock options vest ratably over three years and expire in ten years from the grant date. The Company valued the stock options at \$2,062,964 and amortizes the stock compensation expense using the straight-line method over the service period from February 11, 2009 through February 11, 2012. The value of the options was estimated using the Black Scholes Model with an expected volatility of 164%, expected life of 10 years, risk-free interest rate of 2.76% and expected dividend yield of 0.00%. On June 30, 2011, one of the Company's directors resigned, and his 6,668 unexercised options were forfeited. As of June 30, 2012, options for 946,680 shares have been exercised.

On October 6, 2009, the Company executed an agreement ( Cooperation Agreement ) with Wang Rui and Li Qiwen, third-party consultants, whereby Mr. Wang and Mr. Li are to provide business development services in China to the Company in exchange for options to purchase 350,000 shares of the Company's common stock at an exercise price of \$1.50 per share. Per the agreement, 250,000 of these options vested and became exercisable on March 6, 2011, and 100,000 vested and became exercisable on June 6, 2011. These options will expire after ten years. The options are issued under, and are subject to, the terms of the Company's 2008 Omnibus Long-Term Incentive Plan. No required dates of service are specified on the consulting agreement. No repurchase features or cash settlement provisions are specified in the terms and conditions of the Notice of Grant of Stock Option.

The following is a summary of the stock option activities of the Company:

|                                   | Activity  | Weighted Average<br>Exercise Price |
|-----------------------------------|-----------|------------------------------------|
| Outstanding as of January 1, 2012 | 1,753,320 | \$ 0.84                            |
| Granted                           | -         | -                                  |
| Exercised                         | -         | -                                  |
| Cancelled                         | -         | -                                  |
| Outstanding as of June 30, 2012   | 1,753,320 | 0.84                               |

The following table summarizes information about stock options outstanding as of June 30, 2012:

| Options Outstanding |                   |   | Options Exercisable |                   |
|---------------------|-------------------|---|---------------------|-------------------|
| Number of<br>shares | Exercise<br>Price | Remaining<br>Contractual life<br>(in years) | Number of<br>shares | Exercise<br>Price |
| 1,653,320           | \$ 0.80           | 6.75  | 1,653,320           | \$ 0.80           |
| 100,000             | 1.50              | 7.25  | 100,000             | 1.50              |

The fair value per share of the 2,600,000 options issued to the employees and directors is \$0.7934 per share. The fair value per share of the unexercised 100,000 options issued to Wang Rui and Li Qiwen, which became exercisable on June 6, 2010, is \$3.44.

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**NOTE 17 STOCK OPTIONS, WARRANTS AND CONVERTIBLE NOTES (CONTINUED)**

**(b) Warrants and Convertible Notes**

On September 21, 2009, the Company executed an agreement ( Consulting Agreement ) with a third-party consultant, whereby the consultant is to provide management consulting and advisory services for a period of 12 months, beginning on September 22, 2009, and ending on September 22, 2010. As compensation for the services provided, the Company agreed to issue 200,000 warrants to purchase the Company's common stock, with 100,000 of these warrants issued at an exercise price of \$2.00 per share and 100,000 of these warrants issued at an exercise price of \$2.50 per share. All of the warrants have a five year contractual term and were granted on October 22, 2009. The warrants vested in full and became exercisable on January 21, 2010, upon the closing of an initial round of financing. The fair value per share of the 100,000 warrants issued under the Consulting Agreement with an exercise price of \$2.00 is \$4.56, and the fair value per share of the 100,000 warrants issued under the Consulting Agreement with an exercise price of \$2.50 is \$4.48. As of June 30, 2012, the consultant had cashless exercised the 100,000 warrants with an exercise price of \$2.5 per share.

Under a Securities Purchase Agreement, dated as of January 21, 2010, by and among the Company and certain investors thereto, the Company issued a total of \$10 million of senior secured convertible notes (the Convertible Notes ) and warrants exercisable for an aggregate of 800,000 shares of the Company's Common Stock (the Investor Warrants ), for gross proceeds of \$10 million. As of January 21, 2010, at the price of \$6.25 per share, the Convertible Notes were convertible into 1,600,000 shares of Common Stock. The Investor Warrants, which are exercisable for a period of three years following the closing date, were initially exercisable for shares of Common Stock at an exercise price of \$6.5625 per share. Included in the associated issuance costs is the fair value of 80,000 warrants issued to a placement agent. These warrants have the same terms and conditions as the Investor Warrants issued to the investors.

Pursuant to the terms of the Convertible Notes and the Investor Warrants, on May 18, 2010, the conversion price of the Convertible Notes was adjusted to \$3.5924 per share and the exercise price of the Investor Warrants and warrants issued to the placement agent was adjusted to \$4.3907 per share. On August 19, 2010, the conversion price of the Convertible Notes was adjusted to \$3.1146 per share and the exercise price of the Investor Warrants and warrants issued to the placement agent was adjusted to \$3.8067 per share. As a result, the number of Investor Warrants and warrants issued to the placement agent were adjusted to 1,379,148 and 137,915 respectively. As of June 30, 2012, the investors had converted all \$10,000,000 principal amount and \$159,522 of accrued interest of the Convertible Notes into an aggregate of 3,121,121 shares of Common Stock.

As of June 30, 2012, the fair value of the Investor Warrants and the warrants issued to the placement agent was \$1.06 per share.

On December 21, 2010, the Company agreed to sell to certain institutional investors up to 3,027,272 shares of the Company's common stock and warrants to purchase up to 1,210,912 shares of the Company's common stock in fixed combination, with each combination consisting of one share of common stock and a warrant to purchase 0.40 shares of common stock in a registered direct public offering ( Second round warrants ). The warrants became exercisable immediately following the closing date of the offering and remain exercisable for three years thereafter at an exercise price of \$6.30 per share. As of June 30, 2012, the fair value of Second round warrants is \$1.13 per share.



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**NOTE 18 STOCK AWARD**

In connection with his appointment to the Board of Directors, and as compensation for serving, the Board of Directors has authorized the Company to provide Mr. Henry Yu with 5,000 shares of Company's restricted common stock every six months, par value \$0.001 from July 2011.

As compensation for his services, the Board of Directors has authorized the Company to provide Mr. Jerry Lewin with 5,000 shares of Company's restricted common stock every six months, par value \$0.001 from August 2011.

The fair value of awarded stock is determined by the closing price of our common stock on the date of stock award, or estimated by the closing price of our common stock on the reporting date if stock has not yet been awarded.

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**NOTE 19 COMMITMENTS AND CONTINGENCIES****(a) Guarantees and Pledged collateral for third party bank loans**

As of June 30, 2012, the Company provided guarantees for the following third parties:

**(1) Guarantees for bank loans**

| Guarantee provided to                          | Amount        |
|--|---------------|
| Zhejiang Kangli Metal Manufacturing Company.   | \$ 4,747,061  |
| Zhejiang Shuguang industrial Co., Ltd.         | 7,911,768     |
| Zhejiang Taiping Shengshi Industrial Co., Ltd. | 3,164,707     |
| Yongkang Angtai Trade Co., Ltd.                | 791,177       |
| Total  | \$ 16,614,713 |

On December 4, 2011, the Company entered into a guarantee contract to serve as the guarantor for the bank loan borrowed from Shanghai Bank Hangzhou branch in the amount of \$4,747,061 by Zhejiang Kangli Metal Manufacturing Company. ( ZKMMC ) for the period from December 4, 2011 to December 4, 2012. ZKMMC is not related to the Company. Under this guarantee contract, the Company shall perform all obligations of ZKMMC under the loan contract if ZKMMC fails to perform its obligations as set forth in the loan contract.

On October 9, 2011 and December 8, 2011, the Company entered into two guarantee contracts to serve as the guarantor for the bank loans borrowed from Shenzhen Development Bank Hangzhou branch and Huaxia Bank Hangzhou branch in the amount of \$4,747,061 and \$3,164,707 by Zhejiang Shuguang industrial Co., Ltd. ( ZHICL ) for the period from October 9, 2011 to October 9, 2012 and from December 8, 2011 to December 8, 2012 respectively. ZHICL is not related to the Company. Under these guarantee contracts, the Company shall perform all obligations of ZHICL under the loan contracts if ZHICL fails to perform its obligations as set forth in the loan contracts.

On December 4, 2011, the Company entered into a guarantee contract to serve as the guarantor for the bank loans borrowed from Shanghai Bank Hangzhou branch in the amount of \$3,164,707 by Zhejiang Taiping Shengshi Industrial Co., Ltd. ( ZTSICL ) for the period from December 4, 2011 to December 4, 2012. ZTSICL is not related to the Company. Under this guarantee contract, the Company shall perform all obligations of ZTSICL under the loan contract if ZTSICL fails to perform its obligations as set forth in the loan contract.

On January 7, 2011, the Company entered into two guarantee contracts to serve as the guarantor for the bank loans borrowed from China Communication Bank Jinhua Branch in the amount of \$158,235 and \$632,942 respectively by Yongkang Angtai Trade Co., Ltd. ( YATCL ) for the period from January 7, 2011 to December 31, 2012. YATCL is not related to the Company. Under these guarantee contracts, the Company shall perform all obligations of YATCL under the loan contracts if YATCL fails to perform its obligations as set forth in the loan contracts.

**(2) Guarantees for Bank notes:**

| Guarantee provided to                | Amount       |
|--------------------------------------|--------------|
| Zhejiang Mengdeli Electric Co., Ltd. | \$ 1,265,883 |
| Total                                | \$ 1,265,883 |





**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 (UNAUDITED)**

**NOTE 19 COMMITMENTS AND CONTINGENCIES (CONTINUED)**

On August 24, 2010, the Company entered into a guarantee contract to serve as guarantor for the bank note borrowed from Huaxia Bank Hangzhou branch in the amount of \$1,265,883 by Zhejiang Mengdeli Electric Co., Ltd. ( ZMEC ) for the period from August 24, 2010 to August 24, 2012. ZMEC is a supplier but not related to the Company. Under this guarantee contract, the Company shall perform all obligations of ZMEC under the loan contract if ZMEC fails to perform its obligations as set forth in the loan contract.

(3) Pledged collateral for a third party's bank loans

As of June 30, 2012, the Company provided the land use rights and plant and equipment pledged as collateral for the following third party:

Zhejiang Mengdeli Electric Co., Ltd.:

|                                    |              |
|------------------------------------|--------------|
| Land use rights net book value     | \$ 6,926,507 |
| Plant and equipment net book value | \$ 4,589,755 |

It is a common business practice among companies in the region of China where Kandi is located to exchange guarantees for bank debt with no consideration given. It is considered a favor for favor business practice and is commonly required by the lending banks as in these cases. These companies provided guarantees for the Company's bank loans as well. The banks involved in these guarantee transactions typically allow a maximum loan amount based on a 30% to 70% discount on the net book value of the pledged collateral. Also see Note 14.

**(b) Pending litigations**

There are two lawsuits currently pending in Ripley County, Missouri against the Company and its subsidiary Zhejiang Kandi Vehicles Co., Ltd. ( Kandi Vehicles ) as well as other parties, Kandi Investment Group and SunL, and they are related to two persons who died in an accident on March 3, 2006 while operating a go-cart allegedly manufactured by Kandi Vehicles. Kandi Investment Group was a major shareholder of Kandi Vehicles but it transferred all its equity in Kandi Vehicles to Continental Development Limited in November 2006. Since then, Kandi Investment Group is unrelated to the Company or its affiliates.

The cases were filed in 2009 and are known as Elder vs. SunL Group and Griffen vs. SunL Group. In March, 2010, the local trial court entered two default judgments in the amount of \$20,000,000 each against Kandi Vehicles and other parties including Kandi Investment but not the Company. The lawsuit and default judgments didn't come to the Company or Kandi Vehicles' attention until May or June 2010. The Company had not been served or notified of the lawsuits and learned of their existence and of the default judgment in the course of commercial discussions with another of the defendants in the cases. Currently, the Company and Kandi Vehicles have filed answers to the complaint denying any culpability. In addition, the Company requested that the court set aside the default judgments against Kandi Vehicles, a request granted, by the court, on February 28, 2011. On March 3, 2011, the plaintiffs subsequently appealed the court order vacating the default judgments; however, the plaintiffs have since voluntarily withdrawn their appeal.

The Company intends to propound discovery on the plaintiffs. The Company and Kandi Vehicles each filed a Motion for Summary Judgment in an attempt to have the cases dismissed by summary judgment. The plaintiffs also filed a Motion for Summary Judgment. All of the Motions for Summary Judgment were argued before the court on July 2, 2012. The judge has not ruled on any of the Motions for Summary Judgment.

The Company intends to defend these cases vigorously and expects to prevail in this lawsuit since the Company including its subsidiaries did not manufacture the subject vehicle in the accident.

**(c) Capital Commitment**

During the previous year, certain mold manufacturing contracts were executed. As of June 30, 2012, the remaining unpaid balance was \$2,705,271; we plan on paying \$2,238,477 within the next twelve months and the rest in June of 2014.

**KANDI TECHNOLOGIES, CORP.  
AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 (UNAUDITED)**

**NOTE 20 ACQUISITION OF YONGKANG SCROU ELECTRIC CO**

The Company acquired Yongkang Scrou Electric Co on April 25, 2012. The Company issued 2,354,212 shares of its common stock, which was valued at \$3.66 per share (market value on the date of acquisition). The total purchase price for the acquisition was approximately \$8.6 million which was primarily allocated to working capital, tangible property and equipment, identifiable intangible assets and goodwill. The Company anticipates finalizing our purchase accounting for the acquisition no later than the end of 2012, upon the finalization of appraisals primarily related to fixed assets and intangible assets.

The preliminary purchase price allocation based on qualified independent valuation is as follows:

|                                     |                     |
|-------------------------------------|---------------------|
| Working Capital                     | \$ 3,651,648        |
| Tangible Property                   | 880,942             |
| Identifiable Intangible Property    | -                   |
| Land use right                      | 3,622,650           |
| Tradename                           | 164,463             |
| Goodwill                            | 437,525             |
| Deferred tax liability created, net | (140,812)           |
| <b>Total Purchase Price</b>         | <b>\$ 8,616,416</b> |

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## **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

This report contains forward-looking statements within the meaning of the federal securities laws that relate to future events or our future financial performance. In some cases, you can identify forward-looking statements by terminology, such as "may," "will," "should," "could," "expect," "plan," "anticipate," "believe," "estimate," "project," "predict," "intend," "potential" or "continue" or the negative of such terms or other comparable terminology, although not all forward-looking statements contain such terms.

In addition, these forward-looking statements include, but are not limited to, statements regarding implementing our business strategy; development and marketing of our products; our estimates of future revenue and profitability; our expectations regarding future expenses, including research and development, sales and marketing, manufacturing and general and administrative expenses; difficulty or inability to raise additional financing, if needed, on terms acceptable to us; our estimates regarding our capital requirements and our needs for additional financing; attracting and retaining customers and employees; sources of revenue and anticipated revenue; and competition in our market.

Forward-looking statements are only predictions. Although we believe that the expectations reflected in these forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. All of our forward-looking information is subject to risks and uncertainties that could cause actual results to differ materially from the results expected. Although it is not possible to identify all factors, these risks and uncertainties include the risk factors and the timing of any of those risk factors described in the Company's Form 10-K for the year ended December 31, 2011 and those set forth from time to time in our filings with the Securities and Exchange Commission (SEC). These documents are available on the SEC's Electronic Data Gathering and Analysis Retrieval System at <http://www.sec.gov>.

### **Critical Accounting Policies and Estimates**

#### *Policy affecting options, and warrants*

The Company's stock option cost is recorded in accordance with ASC 718 and ASC 505.

The fair value of stock options is estimated using the Black-Scholes-Merton model. The Company's expected volatility assumption is based on the historical volatility of the Company's stock. The expected life assumption is primarily based on the expiration date of the option. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Stock option expense recognized is based on awards expected to vest, and there were no estimated forfeitures. ASC standards requires forfeitures to be estimated at the time of grant and revised in subsequent periods, if necessary, if actual forfeitures differ from those estimates.

The Company's warrant costs are recorded in liabilities and equities, respectively, in accordance with ASC 480, ASC 505 and ASC 815.

The fair value of warrants, which is classified as a liability, is estimated using a Black-Scholes-Merton model. The Company's expected volatility assumption is based on the historical volatility of the Company's stock. The expected life assumption is primarily based on the expiration date of the warrant. The risk-free interest rate for the expected term of the warrant is based on the U.S. Treasury yield curve in effect at the time of measurement. The warrants, which are freestanding derivatives and are classified as liabilities on the balance sheet, will be measured at fair value on each reporting date, with decreases in fair value recognized in earnings and increases in fair values recognized in expenses.

The Company determined that the fair value of equity based warrants, which are not considered derivatives under ASC 815, is estimated using the Black-Scholes-Merton model. The Company's expected volatility assumption is based on the historical volatility of the Company's stock. The expected life assumption is primarily based on the expiration

date of the warrant. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

*Estimates affecting accounts receivable and inventories*

The preparation of our consolidated financial statements requires management to make estimates and assumptions that affect our reporting of assets and liabilities (and contingent assets and liabilities). These estimates are particularly significant where they affect the reported net realizable value of the Company's accounts receivable and inventories.

Accounts receivable are recognized and carried at net realizable value. An allowance for doubtful accounts will be recorded in the period when a loss is probable based on an assessment of specific evidence indicating troubled collection, historical experience, accounts aging, ongoing business relation and other factors. Accounts are written off after exhaustive efforts at collection. If accounts receivable are to be provided for, or written off, they would be recognized in the consolidated statement of operations within operating expenses. At June 30, 2012 and December 31, 2011, the Company has an allowance for doubtful accounts of \$0 and \$0 respectively, as per the management's judgment based on their best knowledge.

Inventories are stated at the lower of cost, determined on a weighted average basis, or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business less the estimated cost of completion and the estimated costs necessary to make the sale. When inventories are sold, their carrying amount is charged to expense in the year in which the revenue is recognized. Write-downs for declines in net realizable value or for losses of inventories are recognized as an expense in the year the impairment or loss occurs. There were no declines in net realizable value of inventory for the six months ended June 30, 2012.

While the Company currently believes that there is little likelihood that actual results will differ materially from these current estimates, if customer demand for our products decreases significantly in the near future, or if the financial condition of our customers deteriorates in the near future, the Company could realize significant write downs for slow-moving inventories or uncollectible accounts receivable.

*Revenue Recognition*

Revenues represent the invoiced value of goods sold, recognized upon the shipment of goods to customers. Revenues are recognized when all of the following criteria are met:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred or services have been rendered;
- The seller's price to the buyer is fixed or determinable; and
- Collectability is reasonably assured.

**Results of Operations***Comparison of Six Months Ended June 30, 2012 and 2011*

The following table sets forth the amounts and percentage relationship to revenue of certain items in our condensed consolidated statements of income and comprehensive income

|  | <b>For Six<br/>Months<br/>Ended<br/>June 30,<br/>2012</b> | <b>% Of<br/><u>Revenue</u></b> | <b>For Six<br/>Months<br/>Ended<br/>June 30,<br/>2011</b> | <b>% Of<br/><u>Revenue</u></b> | <b>Change<br/>In<br/>Amount</b> | <b>Change<br/>In<br/>%</b> |
|--|---|--------------------------------|---|--------------------------------|---------------------------------|----------------------------|
| <b>REVENUES, NET</b>   | \$ 25,416,517   | 100%                           | \$ 18,479,208   | 100%                           | \$ 6,937,309                    | 37.5%                      |
| <b>COST OF GOODS SOLD</b>  | (20,287,410)  | (79.8%)                        | (14,076,060)  | (76.2%)                        | (6,211,350)                     | 44.1%                      |
| <b>GROSS PROFIT</b>  | 5,129,107   | 20.2%                          | 4,403,148   | 23.8%                          | 725,959                         | 16.5%                      |
| Research and development   | (1,376,186)   | (5.4%)                         | (1,086,540)   | (5.9%)                         | (289,646)                       | 26.7%                      |
| Selling and distribution<br>expenses                             | (173,036)   | (0.7%)                         | (149,615)   | (0.8%)                         | (23,421)                        | 15.7%                      |
| General and administrative<br>expenses                           | (1,579,670)   | (6.2%)                         | (1,501,396)   | (8.1%)                         | (78,274)                        | 5.2%                       |
| <b>INCOME FROM<br/>OPERATIONS</b>                                | 2,000,215   | 7.9%                           | 1,665,597   | 9.0%                           | 334,618                         | 20.1%                      |
| Interest income (expense),<br>net                                | (56,940)  | (0.2%)                         | (21,804)  | (0.1%)                         | (35,136)                        | 161.1%                     |
| Change in fair value of<br>financial instruments                 | 1,961,526   | 7.7%                           | 7,752,772   | 42.0%                          | (5,791,246)                     | (74.7%)                    |
| Government grants  | 25,308  | 0.1%                           | 280,727   | 1.5%                           | (255,419)                       | (91.1%)                    |
| Investment (loss) income   | (27,411)  | (0.1%)                         | (7,276)   | (0.1%)                         | (20,135)                        | 276.7%                     |
| Other income, net  | 46,602  | 0.2%                           | 167,232   | 0.9%                           | (120,630)                       | (72.1%)                    |
| <b>(LOSS) INCOME FROM<br/>OPERATIONS BEFORE<br/>INCOME TAXES</b> | 3,949,300   | 15.5%                          | 9,837,248   | 53.2%                          | (5,887,948)                     | (59.9%)                    |
| <b>INCOME TAX<br/>(EXPENSE)</b>                                  | (661,120)   | (2.6%)                         | (277,505)   | (1.5%)                         | (383,615)                       | 138.2%                     |
| <b>NET (LOSS) INCOME</b>   | 3,288,180   | 12.9%                          | 9,559,743   | 51.7%                          | (6,271,563)                     | (65.6%)                    |



**(a) Revenue**

For the six months ended June 30, 2012, our revenue increased by 37.5%, from \$18,479,208 to \$25,416,517 as compared to the six months ended June 30, 2011.

The following table lists the number of vehicles sold, categorized by vehicle types, within the six months ended June 30, 2012 and 2011:

|                             | Six Months Ended June 30 |                   |               |                   |
|-----------------------------|--------------------------|-------------------|---------------|-------------------|
|                             | 2012                     |                   | 2011          |                   |
|                             | Unit                     | Sales             | Unit          | Sales             |
| ATV                         | 7,078                    | \$ 2,961,947      | 2,665         | \$ 1,725,754      |
| Super-mini car <sup>1</sup> | 639                      | 2,636,852         | 542           | 3,407,857         |
| Go-Kart                     | 16,982                   | 15,733,057        | 11,394        | 11,153,315        |
| Utility vehicles ( UTVs )   | 35                       | 133,382           | 393           | 1,220,237         |
| Three wheeled motorcycle    | 498                      | 683,966           | 284           | 681,923           |
| Refitted car                | 64                       | 1,734,629         | 11            | 290,122           |
| Auto generator              | 28,298                   | 1,532,684         | -             | -                 |
| <b>Total</b>                | <b>53,594</b>            | <b>25,416,517</b> | <b>15,289</b> | <b>18,479,208</b> |

1) include the products called CoCo, EV in the previous filing.

**Off-Road Vehicles**

During the six months ended June 30, 2012, the market condition for ATV products continued to recover. The Company developed some price competitive products to meet markets demands, which has caused good results and successfully increased the Company's sales. Revenues from our ATVs experienced a significant increase of \$1,236,193, or 71.6% in the six months ended June 30, 2012 over the comparable period, which was attributable to a 165.6% increase in units sold, from 2,665 units in the first six months of 2011 to 7,078 units in 2012. This increase was partially caused by a 35.4% unit price reduction.

In the first six months of 2012, our Go-Karts experienced a significant increase in revenue of \$4.6 million or 41.1% over the same period of last year, which was mainly attributable to a 49.0% increase in unit sales from 11,394 units in the six months ended June 30, 2011 to 16,982 units in 2012. Just as with ATVs, the Company's successful development of meet-market-demands price competitive products has achieved good results.

The sales of three-wheeled motorcycle (TT) continued the good performance started from the second half of 2011. In the first six months ended June 30, 2012, the sales of TT increased \$2,043, or 0.3% from the same period of last year, which was attributable to an increase in unit sales from 284 units to 498 units, with the average unit price dropped 42.8%.

Utility vehicles (UTVs) experienced a significant decrease in revenues from \$1,220,237 to \$133,382. This 89.1% decrease is mainly due to the 91.1% drop in unit sales in the six months ended June 30, 2012 compared to the same period of 2011. This significant drop is primarily because of the continuing high competition in this UTV market, while the UTV manufactured by the Company is relatively high end and more expensive, which caused the average unit price to increase significantly compared to the same period of last year.

**Super-mini-Car Products**

For the EV products, the Company has not realized mass unit sales during this reporting period. For the six months ended June 30, 2012, revenues from our Super-mini car decreased by \$771,005, or 22.6% from the same period of

2011, which was attributable to an increase in unit sales of 17.9% from 542 units in the first six months of 2011 to 639 units in 2012. For the six months ended June 30, 2012, the average unit price of our super-mini-cars decreased 34.4%, because during this reporting period, the Company adopted the sales mode of charging or exchanging batteries to sell the super-mini-cars without batteries.

**Refitted car**

For the six months ended June 30, 2012, the Company also refitted other companies' vehicles to meet special requirements for certain customers. The Company expects this new business to expand the Company's business scope and stimulate the Company's development.

**Auto generator**

On April 25, 2012, the Company acquired Yongkang Scrou Electric Co. (Yongkang Scrou), whose main business is producing various auto generators. From April 25, 2012 to June 30, 2012, a total 28,298 sets of auto generators were sold with sales totaling \$1,532,684.

The following table shows the breakdown of Kandi's revenues from its customers by geographical markets based on the location of the customer during the 6 months ended June 30, 2012 and 2011:

|                       | Six Months Ended June 30 |            |               |            |
|-----------------------|--------------------------|------------|---------------|------------|
|                       | 2012                     |            | 2011          |            |
|                       | Sales                    | Percentage | Sales         | Percentage |
| North America         | \$ 3,195,806             | 13%        | \$ 2,184,124  | 12%        |
| China                 | 21,675,976               | 85%        | 15,772,767    | 85%        |
| Europe & other region | 544,735                  | 2%         | 522,317       | 3%         |
| Total                 | \$ 25,416,517            | 100%       | \$ 18,479,208 | 100%       |

For the six months ended June 30, 2012, about 85% of our sales in China were to Chinese export agents, who resell the company's products to markets around the world.

**(b) Cost of goods sold**

Cost of goods sold during the six months ended June 30, 2012 was \$20,287,410, representing an increase of \$6,211,350, or 44.1% from the six months ended June 30, 2011, corresponding to the Company's significant increase of revenue.

**(c) Gross profit**

Gross profit for the first half of 2012 increased 16.5% to \$5,129,107 compared to \$4,403,148 at the same period of last year, as a result of increased revenue. However, gross margin decreased to 20.2% compared to 23.8% for the same period of 2011. This was primarily due to the fact that processing techniques for refitted cars are relatively simple; therefore its gross margin is comparatively lower, in addition, Yongkang Scrou's adjustment to its product structure and disposal of its old products affected the gross margin, all of which reduced the overall gross margin of the Company for this reporting period.

**(d) Selling and distribution expenses**

Selling and distribution expenses were \$173,036 for the six months ended June 30, 2012, as compared to \$149,615 for the same period in 2011, representing a 15.7% increase. The significant increase is primarily because of the increase in fees related to exhibition, higher transportation fees and advertising fees.

**(e) General and administrative expenses**

General and administrative expenses were \$1,579,670 for the six months ended June 30, 2012, as compared to \$1,501,396 for the same period in 2011, representing a 5.2% increase. For the six months ended June 30, 2012, the general and administrative expenses included \$19,053 in stock-based compensation cost for the options issued to the

Company's executives and managerial level employees, while for the same period of last year, the stock based compensation cost was \$138,315. In addition, general and administrative expenses also included \$27,808 in expenses for common stock awards to employees and consultants for financing and investor relations services, while for the same period of last year, this cost was \$28,826. Excluding the effect of stock based compensation cost and stock award cost, the net general and administrative expenses for the six months ended June 30, 2012 was \$1,532,809, an increase of 14.9% from \$1,334,255 for the same period of 2011. This increase was primarily due to the higher product insurance fee, directors and officers liability insurance fee and the increase of employee welfare.

**(f) Research and development**

Research and development expenses were \$1,376,186 for the six months ended June 30, 2012, as compared to \$1,086,540 from the same period in 2011, representing a 26.7% increase. This increase was primarily due to additional research and development efforts on new products and on quality improvement on existing products. In the first six months of 2012, the Company strengthened the research and development for electrical vehicles equipped with lithium battery in order to seek the leading position in EV market. In addition, the Company successfully developed price- competitive Three Wheels with gas-electric hybrid drives to meet the demand of China urban and rural markets.

**(g) Government grants**

Government grants totaled \$25,308 for the six months ended June 30, 2012, representing a 91% decrease over the same period in 2011.

**(h) Net interest income (expense)**

Net interest expenses was \$56,940 for the six months ended June 30, 2012, as compared to \$21,804 net interest expense for the same period last year, representing a significant increase. For the six months ended June 30, 2012, the interest expense for convertible notes was \$2, and the interest incurred by the amortization of debt discount was \$43. While for the same period of last year, the interest expense for the convertible notes was \$30, and the interest incurred by the amortization of debt discount was \$222. Excluding the effects of interest expense related to convertible notes, the net interest expenses for this reporting period was \$ 56,895, improved from net interest expense of \$21,552 for the same period of 2011, primarily due to the increase of interest income earned from the note receivables issued to third parties.

**(i) Change in fair value of financial instruments**

For the six months ended June 30, 2012, the interest income, which was caused by the changes of fair value of warrants issued to investors and placement agents was \$1,961,526, while for the same period of last year, the interest income, which was caused by the changes of fair value of financial instruments, was \$7,752,772. This significant decrease was primarily because the stock price was more stable in the first half of 2012 compared to the same period of last year.

**(j) Other Income, Net**

Net other income was \$46,602 for the six months ended June 30, 2012, compared to \$167,232 for the same period of last year, a decrease of \$120,630 or 72.1%. This decrease was primarily due to a fine in the amount of \$89,194 that the Company received in the first six months of 2011 as a result of a contractor not completing a construction project on time. Therefore, there was a lower net other income for the six months ended June 30, 2012 compared to the same period in 2011.

**(k) Investment (loss) income**

Investment loss was \$27,411 for the first six months ended June 30, 2012, compared to \$7,276 for the corresponding period in 2011. For the six months ended June 30, 2012, the investment loss was solely the result of our 30% equity interest investment in Jinhua Service, which was \$16,819 for the same period of 2011. During the first six months ended June 30, 2011, the \$9,543 investment income was from trading securities.

**(l) Net income**

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The operating performance of the Company for the six months ended June 30, 2012 reflected a net income of \$3,288,180, a decrease of \$6,271,563 or 65.6% from a net income of \$9,559,743 for the same period of last year, which was primarily due to changes in the fair value of certain warrants issued to investors and placement agents.

Excluding the effects of option related expenses, which was \$19,053 and \$138,315 for the six months ended June 30, 2012 and 2011, respectively; stock award expenses of \$27,808 and \$28,826 for the six months ended June 30, 2012 and 2011, respectively; Convertible Note interest expenses of \$2 and \$30 for the six months ended June 30, 2012 and 2011, respectively, which was caused by an amortization of discount on the Convertible Notes of \$43 and \$222 for the six months ended June 30, 2012 and 2011, respectively; a change in the fair value of financial derivatives to \$1,961,526 and \$7,752,772 for the six months ended June 30, 2012 and 2011, respectively; for the six months ended June 30, 2012, the Company's net income was \$1,373,560, a decrease of 30.4% compared to net income of \$1,974,364 for the same period of 2011, excluding the same effects. This decrease was primarily due to a decrease in gross profit. As of June 30, 2012, all of the Convertible Notes have been converted.

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*Comparison of Three Months Ended June 30, 2012 and 2011*

The following table sets forth the amounts and percentage relationship to revenue of certain items in our condensed consolidated statements of income and comprehensive income

|  | <b>For Three<br/>Months<br/>Ended<br/>June 30,<br/>2012</b> | <b>% Of<br/>Revenue</b> | <b>For Three<br/>Months<br/>Ended<br/>June 30,<br/>2011</b> | <b>% Of<br/>Revenue</b> | <b>Change<br/>In<br/>Amount</b> | <b>Change<br/>In<br/>%</b> |
|--|---|-------------------------|---|-------------------------|---------------------------------|----------------------------|
| <b>REVENUES, NET</b>                                     | \$ 11,060,976   | 100%                    | \$ 10,137,702   | 100%                    | \$ 923,274                      | 9.1%                       |
| <b>COST OF GOODS SOLD</b>                                | (9,272,719)   | (83.8%)                 | (7,795,987)   | (76.9%)                 | (1,476,732)                     | 18.9%                      |
| <b>GROSS PROFIT</b>                                      | 1,788,257   | 16.2%                   | 2,341,715   | 23.1%                   | (553,458)                       | (23.6%)                    |
| Research and development                                 | (620,090)   | (5.6%)                  | (574,588)   | (5.7%)                  | (45,502)                        | 7.9%                       |
| Selling and distribution expenses                        | (79,201)  | (0.7%)                  | (92,679)  | (0.9%)                  | 13,478                          | (14.5%)                    |
| General and administrative expenses                      | (896,050)   | (8.1%)                  | (827,529)   | (8.2%)                  | (68,521)                        | 8.3%                       |
| <b>INCOME FROM OPERATIONS</b>                            | 192,916   | 1.7%                    | 846,919   | 8.4%                    | (654,003)                       | (77.2%)                    |
| Interest income (expense), net                           | (188,542)   | (1.7%)                  | 275,466   | 2.7%                    | (464,008)                       | (168.4%)                   |
| Change in fair value of financial instruments            | 1,018,576   | 9.2%                    | 2,367,594   | 23.4%                   | (1,349,018)                     | (57.0%)                    |
| Government grants  | 25,308  | 0.2%                    | 273,139   | 2.7%                    | (247,831)                       | (90.7%)                    |
| Investment (loss) income                                 | (14,010)  | (0.1%)                  | (8,490)   | (0.1%)                  | (5,520)                         | 65.0%                      |
| Other income, net  | 12,134  | 0.1%                    | 53,526  | 0.5%                    | (41,392)                        | (77.3%)                    |
| <b>(LOSS) INCOME FROM OPERATIONS BEFORE INCOME TAXES</b> | 1,046,382   | 9.5%                    | 3,808,154   | 37.6%                   | (2,761,772)                     | (72.5%)                    |
| <b>INCOME TAX (EXPENSE)</b>                              | (141,154)   | (1.3%)                  | (186,811)   | (1.8%)                  | 45,657                          | (24.4%)                    |
| <b>NET (LOSS) INCOME</b>                                 | 905,228   | 8.2%                    | 3,621,343   | 35.7%                   | (2,716,115)                     | (75.0%)                    |

**(a) Revenue**

For the three months ended June 30, 2012, our revenues increased 9.1% from \$10,137,702 to \$11,060,976 as compared to the three months ended June 30, 2011.

The following table lists the number of vehicles sold, categorized by vehicle types, for the three months ended June 30, 2012 and 2011:

|                                 | Three Months Ended June 30 |            |       |            |
|---------------------------------|----------------------------|------------|-------|------------|
|                                 | 2012                       |            | 2011  |            |
|                                 | Unit                       | Sales      | Unit  | Sales      |
| ATV                             | 1,954                      | \$ 961,647 | 1,045 | \$ 311,238 |
| Super-mini car <sup>1</sup>     | 343                        | 1,450,935  | 333   | 2,375,094  |
| Go-Kart                         | 4,001                      | 6,093,381  | 6,028 | 6,205,124  |
| Utility vehicles ( UTVs )       | 15                         | 58,949     | 160   | 729,992    |
| Three wheeled motorcycle ( TT ) | 250                        | 181,611    | 93    | 226,132    |
| Refitted car                    | 29                         | 781,769    | 11    | 290,122    |
| Auto generator                  | 28,298                     | 1,532,684  | -     | -          |
| Total                           | 34,890                     | 11,060,976 | 7,670 | 10,137,702 |

1) include the products called CoCo, EV and mini-car in the previous filing.

**Off-Road Vehicles**

During the three months ended June 30, 2012, the market condition for our ATV products continued to recover. The Company developed some price competitive products to meet markets demands that caused good results and successfully increased the Company's sales. Revenues from our ATVs experienced a significant increase of \$650,409, or 209.0% in the three months ended June 30, 2012, compared to the comparable period in 2011, which was attributable to a 87.0% increase from 1,045 units in the first three months of 2011 to 1,954 units in 2012. This increase was partially caused by a 65.2% unit price increase.

During the three months ended June 30, 2012, our Go-Karts experienced a slight decrease in revenue of \$111,743 or 1.8% compared to the same period in 2011, which was attributable to a 33.6% decrease in unit sales from 6,028 units in the three months ended June 30, 2011 to 4,001 units in 2012. Just as with ATVs, the Company's successful development of price competitive products that meet market demands achieved good results.

In the three months ended June 30, 2012, sales of our TT decreased \$44,521, or 19.7% compared to the same period of last year, despite an increase in unit sales from 93 units to 250 units. This decrease was primarily caused by a 70.1% decrease in unit price. The unit price decreased because the Company developed price-competitive, gas-electric hybrid driven three wheeled motorcycles to meet the growing demand of such units in the Chinese urban and rural markets.

UTVs experienced a significant decrease in revenues from \$729,992 to \$58,949. This 91.9% decrease was mainly due to a 90.6% drop in unit sales in the three months ended June 30, 2012 compared to the same period of 2011. This significant drop was primarily due to continuing high competition in the UTV market. The UTVs manufactured by the Company are relatively high end and more expensive, which caused the average unit price to increase significantly compared to the same period of last year.

**Super-mini-Car Products**

In the three months ended June 30, 2012, the Company did not realized mass unit sales of our EV products. For the three months ended June 30, 2012, revenues from our super-mini cars decreased slightly by \$924,159, or 38.9%



compared to the same period of 2011, despite an increase in unit sales of 3.0% from 333 units in the second quarter of 2011 to 343 units in 2012. For the three months ended June 30, 2012, the average unit price of our super-mini-cars decreased 40.7%, because some of the super-mini-cars sold by the Company during this reporting period were sold without batteries.

**Refitted car**

For the three months ended June 30, 2012, the Company also refitted other companies' vehicles to meet special requirements for certain customers. The Company expects this new business to expand our current business scope and stimulate our development.

**Auto generator**

On April 25, 2012, as reported on Form 8-Ks filed on February 17, 2012 and May 2, 2012, the Company via its acquisition of KO NGA Investment Limited acquired Yongkang Scrou, whose main business is producing various auto generators. From April 25, 2012 to June 30, 2012, a total of 28,298 sets of auto generators were sold, with the sales of \$1,532,684.

The following table shows a breakdown of the Company's revenues from its customers by geographical markets based on the location of the customer during the 3 months ended June 30, 2012 and 2011:

|                       | Three Months Ended June 30 |            |               |            |
|-----------------------|----------------------------|------------|---------------|------------|
|                       | 2012                       |            | 2011          |            |
|                       | Sales                      | Percentage | Sales         | Percentage |
| North America         | \$ 1,556,430               | 14%        | \$ 1,124,591  | 11%        |
| China                 | 9,223,045                  | 83%        | 8,737,943     | 86%        |
| Europe & other region | 281,501                    | 3%         | 275,168       | 3%         |
| Total                 | \$ 11,060,976              | 100%       | \$ 10,137,702 | 100%       |

For the three months ended June 30, 2012, about 90% of our sales in China were sales to Chinese export agents, who resold the Company's products to markets around the world.

**(b) Cost of goods sold**

Cost of goods sold during the three months ended June 30, 2012 was \$9,272,719, representing an increase of \$1,476,732, or 18.9% from the three months ended June 30, 2011, corresponding to the Company's significant increase of revenue.

**(c) Gross profit**

Gross profit for the second quarter of 2012 decreased 23.6% to \$1,788,257 compared to \$2,341,715 at the same period of last year, as a result of increased cost of goods sold. However, the gross margin has decreased to 16.2% compared to 23.1% for the same period of 2011. This is primarily due to the fact that processing techniques for refitted cars are relatively simple; therefore the gross margin is comparatively lower. In addition, Yongkang Scrou's adjustment to its product structure and disposal on its old products affected our gross margin, all of which reduced the overall gross margin of the Company for this reporting period.

**(d) Selling and distribution expenses**

Selling and distribution expenses were \$79,201 for the three months ended June 30, 2012, compared to \$92,679 for the same period in 2011, representing a 14.5% decrease. This decrease is primarily because the Company has paid most of fees related to exhibition, transportation and advertising in the first three months of 2012, as such, the three months from April to June 2012 witnessed the reduced expenses.

**(e) General and administrative expenses**

General and administrative expenses were \$896,050 for the three months ended June 30, 2012, as compared to \$827,529 for the same period in 2011, representing a 8.3% increase. For the three months ended June 30, 2012, the general and administrative expenses included \$0 in stock-based compensation cost for the options issued to the Company's executives and managerial level employees, while for the same period of last year, this stock based compensation cost was \$52,358. In addition, general and administrative expenses also included \$14,075 in expenses for common stock awards to employees and consultants for financing and investor relations services, while for the same period of last year, this cost was \$11,034. Excluding the effect of stock based compensation cost and stock award cost, the net general and administrative expenses for the three months ended June 30, 2012 was \$881,975, an increase of 15.4% from \$764,137 for the same period of 2011. This increase was primarily due to the higher product insurance fees, directors and officers liability insurance fees, and an increase in employee welfare related fees.

**(f) Research and development**

Research and development expenses were \$620,090 for the three months ended June 30, 2012, as compared to \$574,588 for the same period in 2011, representing a 7.9% increase. This increase was primarily due to additional research and development efforts on new products and quality improvements on existing products. In the second quarter of 2012, the Company increased the amount of money it spent on research and development for electrical vehicles equipped with lithium battery in hopes of obtaining a leading position in the EV market.

**(g) Government grants**

Government grants totaled \$25,308 for the three months ended June 30, 2012, representing a 90.7% decrease over the same period in 2011.

**(h) Net interest income (expense)**

Net interest expenses was \$188,542 for the three months ended June 30, 2012, as compared to \$275,466 net interest income for the same period last year, representing a significant increase. For the three months ended June 30, 2012, the interest expense for convertible notes was \$0, and the interest incurred by the amortization of debt discount was \$0. While for the same period of last year, the interest expense for the convertible notes was \$15, and the interest incurred by the amortization of debt discount was \$130 since only \$1,000 convertible notes were outstanding at June 30, 2011. Excluding the effects of interest expense related to convertible notes, the net interest expenses for this reporting period was \$188,542, a significant change from net interest income of \$275,611 for the same period of 2011, primarily due to the decrease of interest income earned from the note receivables issued to third parties.

**(i) Change in fair value of financial instruments**

For the three months ended June 30, 2012, the interest income, which was caused by the changes of fair value of warrants issued to investors and placement agents was \$1,018,576, while for the same period of last year, the interest income, which was caused by the changes of fair value of financial instruments, was \$2,367,594. This significant decrease was primarily because the stock price was more stable in the first half of 2012 compared to the same period of last year.

**(j) Other Income, Net**

Net other income was \$12,134 for the three months ended June 30, 2012, compared to \$53,526 for the same period of last year, a decrease of \$41,392 or 77.3%. This decrease is primarily because there was a write off of other payables in the first three months of 2011.

**(k) Investment (loss) income**

Investment loss was \$14,010 for the first three months ended June 30, 2012, compared to \$8,490 for the corresponding period in 2011. For the three months ended June 30, 2012, the investment loss was purely a result of our 30% equity interest investment in Jinhua Service, which was \$16,819 for the same period of 2011. During the first three months ended June 30, 2011, the \$8,329 investment income was from trading securities.

**(l) Net income**

The operating performance of the Company for the three months ended June 30, 2012 reflected a net income of \$905,228, a decrease of \$2,716,115 or 75.0% from a net income of \$3,621,343 for the same period of last year, which was primarily due to changes in the fair value of warrants issued to certain investors and placement agents.

Excluding the effects of option related expenses, which was \$0 and \$52,358 for the three months ended June 30, 2012 and 2011, respectively; the stock award expense, which was \$14,075 and \$11,034 for the three months ended June 30, 2012 and 2011, respectively; the Convertible Note s interest expense, which was \$0 and \$15 for the three months ended June 30, 2012 and 2011, respectively; the effect caused by an amortization of discount on Convertible Notes, which was \$0 and \$130 for the three months ended June 30, 2012 and 2011, respectively; and a change in the fair value of certain financial derivatives, which was \$1,018,576 and \$2,367,594 for the three months ended June 30, 2012 and 2011, respectively; for the three months ended June 30, 2012, the Company s net loss was \$99,273, a decrease of 107.5% compared to net income of \$1,317,286 for the same period of 2011 excluding the same effects. This decrease was primarily due to a decrease in gross profit and a decrease of interest from notes receivable. As of June 30, 2012, all of the Convertible Notes have been converted.

**Financial Condition Liquidity and Capital Resources Working Capital**

The Company had a working capital surplus of \$23,371,747 as of June 30, 2012, comparable to a working capital surplus of \$23,012,284 as of June 30, 2011.

As of June 30, 2012, the Company had credit lines from commercial banks for \$41,457,664, of which \$31,330,601 was used as of June 30, 2012. The Company believes that its cash flows generated internally may not be sufficient to support growth of future operations and repay short term bank loans for the next twelve months if needed. However, the Company believes its access to existing financing sources and established relationships with PRC banks will enable it to meet its obligations and fund its ongoing operations.

The Company has historically financed itself through short-term commercial bank loans from PRC banks. The term of these loans are typically for one year, and upon the payment of all outstanding principal and interest in a respective loan, the banks have typically rolled over the loans for additional one-year terms, with adjustments made to the interest rate to reflect prevailing market rates. The Company believes this situation has not changed and the short-term bank loan will be available on normal trade terms if needed.

**Capital Requirements and Capital Provided**

Capital requirements and capital provided for the six months ended June 30, 2012 are as follows:

|   | <b>Six Months<br/>Ended June<br/>30, 2012</b> |
|---|---|
| <b><u>Capital requirements</u></b>          | <b>(In thousands)</b>                         |
| Purchase of plant and equipment             | 452   |
| Purchase of Construction in progress        | 2,091   |
| Repayments of short-term bank loans         | 14,781  |
| Repayments of notes payable                 | 5,884   |
| Increase in restricted cash                 | 20,103  |
| Internal cash used in operations            | 12,454  |
| Total capital requirements                  | \$ 55,765                                     |
| <br>  |   |
| <b><u>Capital provided</u></b>              |   |
| Proceeds from short-term bank loan          | 14,750  |
| Proceeds from notes payable                 | 15,160  |
| Repayments of notes receivable              | 23,123  |
| Other financing activities                  | 67  |
| Common Stock Issued, net of Cost of Capital | 3,740   |
| Total capital provided                      | \$ 56,840                                     |

For further information, see the Statement of Cash Flows.

The difference between capital provided and capital requirement is the effect of exchange rate changes over the past six months.

**Cash Flow**

Net cash flow used in operating activities was (\$12,454,463) for the six months ended June 30, 2012, as compared to net cash flow used in operating activities of (\$4,156,931) in the same period in 2011. The significant change of net cash flow used in operating activities was mainly due to the large amount of cash outflow caused by accounts receivable performance describe below in this paragraph and the lesser amount of cash inflow caused by prepayments and prepaid expenses. The account of accounts receivable has changed to cash outflow of (\$11,844,213) in the six months ended 2012 from cash inflow \$7,991,676 for the same period of last year. The account of prepayments and prepaid expenses has changed to cash inflow of \$30,204 in the six months ended 2012 from cash outflow of (\$9,321,749) for the same period of last year, which is mainly because of the sluggish collection of the 2<sup>nd</sup> quarter receivables as well as the rising monthly sales in the 2<sup>nd</sup> quarter 2012, all of these resulted in the reduction of cash inflow.

Net cash flow provided by investing activities was \$20,692,093 for the six months ended June 30, 2012 as compared to net cash flow provided by investing activities of \$ 4,231,582 for the same reporting period in 2011. For the six months ended June 30, 2012, the Company recorded a net cash inflow of \$23,123,103 in notes receivable, due to the \$23,123,103 repayment of notes receivable and no issuance of notes receivable. While for the same period of last year, the Company issued (\$2,733,584) in notes receivable and collected \$7,260,308 in repayment of note receivables, which caused a net cash inflow of \$4,526,724 from notes receivable.

Net cash flow used in financing activities was (\$7,049,932) for the six months ended June 30, 2012, as compared to net cash flow provided by financing activities of \$1,451,377 for the six months ended June 30, 2011. Cash flow used in financing activities in this six months is primarily due to the changes in restricted cash, which caused a cash

outflow of (\$20,103,142). While for the same period of last year, the Company recorded a net cash inflow from notes payable of \$ 10,248,955, although offset by the cash outflow of (\$8,857,647) for the restricted cash.

**Off-Balance Sheet Arrangements:**

Please see Financial Footnotes 14 and 19 for additional information relating to the following off-balance sheet arrangements.

**(a) Guarantees and Pledged collateral for third party bank loans**

As of June 30, 2012, the Company provided guarantees for the following third parties:



## (1) Guarantees for bank loans

| Guarantee provided to                          | Amount        |
|--|---------------|
| Zhejiang Kangli Metal Manufacturing Company.   | \$ 4,747,061  |
| Zhejiang Shuguang industrial Co., Ltd.         | 7,911,768     |
| Zhejiang Taiping Shengshi Industrial Co., Ltd. | 3,164,707     |
| Yongkang Angtai Trade Co., Ltd.                | 791,177       |
| Total  | \$ 16,614,713 |

## (2) Guarantees for Bank notes:

| Guarantee provided to                | Amount       |
|--------------------------------------|--------------|
| Zhejiang Mengdeli Electric Co., Ltd. | \$ 1,265,883 |
| Total                                | \$ 1,265,883 |

## (3) Pledged collateral for a third party's bank loans

As of June 30, 2012, the Company provided the land use rights and plant and equipment pledged as collateral for the following third party:

## Zhejiang Mengdeli Electric Co., Ltd.:

|                                    |              |
|------------------------------------|--------------|
| Land use rights net book value     | \$ 6,926,507 |
| Plant and equipment net book value | \$ 4,589,755 |

It is a common business practice among companies in the region of China where Kandi is located to exchange guarantees for bank debt with no consideration given. It is considered a favor for favor business practice and is commonly required by the lending banks as in these cases. These companies provided guarantees for the Company's bank loans as well. The banks involved in these guarantee transactions typically allow a maximum loan amount based on a 30% to 70% discount on the net book value of the pledged collateral.

**Recent Activities:**

On March 6, 2012, the Ministry of Finance, the Ministry of State Administration of Taxation and the Ministry of Industry and Information Technology of China, collectively, issued and released a list of Energy-Saving and New EVs that qualify for the recently enacted Registration Tax Reduction and Exemption. Kandi's pure EV (model number KD5011XXYEV) was among the first vehicles included on this list. Consumers that purchase the KD5011XXYEV model are exempt from paying the annual registration tax required of other vehicle owners starting January 1, 2012.

On May 13, 2012, commissioned by the Company, the Enterprise Institute of the Development Research Center of the State Council organized and held a project seminar in Beijing. Attendees at the seminar included department leaders from the National Development and Reform Commission ( NDRC ), Ministry of Industry and Information Technology, Ministry of Finance, Ministry of Science and Technology as well as more than 30 academicians, experts, scholars from the Chinese Academy of Engineering ( CAE ), the China Society Of Automotive Engineers ( SAE ), The China Automotive Technology & Research Centre ( CATARC ), National Grid, Tsinghua University and Zhejiang University. At the seminar, the presenters had a serious discussion on China's Innovative Exploration of an EV Business Model and Corresponding Policies and The Feasibility Study of a Public Transportation Project of 100,000 Self driving Rental EVs in Five Years in Hangzhou City. The attendees and presenters agreed that innovative exploration of an EV business model is a significant way to promote the development of EV industry. The self driving rental EV project in Hangzhou is serving as a new public transportation model. With its innovation and feasibility, the implementation of this project will lead to substantial improvements in environmental contamination, traffic jams, parking and a crisis of petroleum resources. Further, this project will promote a faster development of the EV industry, since it corresponds with national and industry's development strategies of creating successful cases for Zhejiang EVs and taking the lead in achieving large-scale operation. The Company believes this may have far-reaching effects on the new energy vehicles industry in China and perhaps even all over the world.

On July 10, 2012, the Company signed a cooperative letter of intent ( LOI ) with China Aviation Lithium Battery (Luoyang) Co., Ltd. in Beijing to promote 20,000 pure electrical vehicles in Hangzhou.

On July 13, 2012, the Company signed a framework agreement with the government of Weifang Binhai Economic Development Zone in Wei Fang City of Shandong Province to produce key components and parts for 100,000 electrical vehicles annually.

On August 10, 2012, the Company participated in the 2012 China International Green Vehicle Industry Expo being held in Hangzhou , and showcased for the first time the smart charging stations and vertical parking system for pure EVs, with functions of charging and exchanging batteries, jointly developed by the Company and Zhejiang Leimeng Machinery and Equipment Co., Ltd..

On August 10, 2012, the Company executed a cooperation framework agreement with Zhejiang Guoxin Car Rental Co., Ltd in Hangzhou to promote the public transportation project of self-driving EV rentals in Hangzhou.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

#### **Exchange Rate Risk**

Our operations are conducted mainly in the PRC. As such, our earnings are subject to movements in foreign currency exchange rates when transactions are denominated in RMB, which is our functional currency. Accordingly, our operating results are affected by changes in the exchange rate between the U.S. dollar and those currencies.

#### **Economic and Political Risks**

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

### **Item 4. Controls and Procedures.**

#### **Evaluation of Disclosure Controls and Procedures**

The Company maintains a system of disclosure controls and procedures that is designed to ensure that information required to be disclosed by the Company in this Form 10-Q, and in other reports required to be filed under the Securities Exchange Act of 1934 (the Exchange Act ), is recorded, processed, summarized and reported within the time periods specified in the rules and forms for such filings. Management of the Company, under the direction of the Company's Chief Executive Officer and Chief Financial Officer, reviewed and performed an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15a(e) and 15d-15(e) under the Exchange Act) as of June 30, 2012. Based on that review and evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and is accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

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

There were no changes to our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Inherent Limitations on Effectiveness of Controls**

Our management, including the CEO and CFO, does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, have been detected. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of the effectiveness of controls to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

## **PART II OTHER INFORMATION**

### **Item 1. Legal Proceedings.**

There are two lawsuits currently pending in Ripley County, Missouri against the Company and its subsidiary Zhejiang Kandi Vehicles Co., Ltd. ( Kandi Vehicles ) as well as other parties, Kandi Investment Group and SunL, and they are related to two persons who died in an accident on March 3, 2006 while operating a go-cart allegedly manufactured by Kandi Vehicles. Kandi Investment Group was a major shareholder of Kandi Vehicles but it transferred all its equity in Kandi Vehicles to Continental Development Limited in November 2006. Since then, Kandi Investment Group is unrelated to the Company or its affiliates.

The cases were filed in 2009 and are known as Elder vs. SunL Group and Griffen vs. SunL Group. In March, 2010, the local trial court entered two default judgments in the amount of \$20,000,000 each against Kandi Vehicles and other parties including Kandi Investment but not the Company. The lawsuit and default judgments didn't come to the Company or Kandi Vehicles' attention until May or June 2010. The Company had not been served or notified of the lawsuits and learned of their existence and of the default judgment in the course of commercial discussions with another of the defendants in the cases. Currently, the Company and Kandi Vehicles have filed answers to the complaint denying any culpability. In addition, the Company requested that the court set aside the default judgments against Kandi Vehicles, a request granted, by the court, on February 28, 2011. On March 3, 2011, the plaintiffs subsequently appealed the court order vacating the default judgments; however, the plaintiffs have since voluntarily withdrawn their appeal.

The Company intends to propound discovery on the plaintiffs. The Company and Kandi Vehicles each filed a Motion for Summary Judgment in an attempt to have the cases dismissed by summary judgment. The plaintiffs also filed a Motion for Summary Judgment. All of the Motions for Summary Judgment were argued before the court on July 2, 2012. The judge has not ruled on any of the Motions for Summary Judgment.

The Company intends to defend these cases vigorously and expects to prevail in this lawsuit since the Company including its subsidiaries did not manufacture the subject vehicle in the accident.

### **Item 1A. Risk Factors.**

Other than as set forth below, as of the date of this filing, there have been no material changes from the risk factors previously disclosed in our Risk Factors in the Form 10-K for the period ended December 31, 2011. An investment in our common stock involves various risks. When considering an investment in our company, you should carefully consider the risk factor set forth below and all of the risk factors described in our most recent Form 10-K. These risks and uncertainties are not the only ones facing us and there may be additional matters that we are unaware of or that we currently consider immaterial. All of these could adversely affect our business, financial condition, results of operations and cash flows and, thus, the value of an investment in our company.

#### **Risks Related to Our Business Operations**

*The audit report included in our annual report, which is incorporated by reference herein, is prepared by auditors who are not currently inspected by the Public Company Accounting Oversight Board ( PCAOB ) and, as such, you do not have the benefit of such inspection.*

Our independent registered public accounting firm, Albert Wong & Co., issues the audit reports included in our annual reports filed with the SEC, as auditors of companies that are traded publicly in the United States and a firm registered with the PCAOB; our auditors are required by the laws of the United States to undergo regular inspections by the PCAOB to assess its compliance with the laws of the United States and professional standards. Because our auditors perform audit work in the PRC, a jurisdiction where the PCAOB is currently unable to conduct inspections

without the approval of PRC authorities, our auditor, like other independent registered public accounting firms located in Hong Kong that perform work in the PRC, is not currently inspected by the PCAOB. Inspections of other firms that the PCAOB has conducted outside the PRC have identified deficiencies in those firms' audit procedures and quality control procedures, which may be addressed as part of the inspection process to improve future audit quality. The inability of the PCAOB to conduct inspections of auditors operating in the PRC makes it more difficult to evaluate the effectiveness of our auditor's audit procedures or quality control procedures as compared to auditors outside of the PRC that are subject to PCAOB inspections, which may cause investors to lose confidence in our reported financial information and procedures and the quality of our financial statements.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

As previously reported on Form 8-Ks filed with the SEC on February 17, 2012 and May 2, 2012, in connection with a Share Exchange Agreement, the Company, on April 25, 2012, issued, in an exempt private placement, a total of 2,354,212 shares of the Company's common stock in reliance on Regulation S of the Securities Act of 1933, as amended.

**Item 3. Defaults Upon Senior Securities.**

None

**Item 4. Mine Safety Disclosures.**

None

**Item 5. Other Information.**

None.

**Item 6. Exhibits**

Exhibit Number Description

|             |  |
|-------------|--|
| <u>31.1</u> | <u>Certification pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934*</u>                               |
| <u>31.2</u> | <u>Certification pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934*</u>                               |
| <u>32.1</u> | <u>Certification of CEO and CFO pursuant to 18 U.S.C. § 1350, as Adopted Pursuant to § 906 of the Sarbanes-Oxley Act of 2002**</u> |

Exhibit 101.INS XBRL Instance Document.\*\*

Exhibit 101.SCH XBRL Taxonomy Extension Schema Document.\*\*

Exhibit 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document.\*\*

Exhibit 101.LAB XBRL Taxonomy Extension Label Linkbase Document.\*\*

Exhibit 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.\*\*

Exhibit 101.DEF XBRL Taxonomy Definitions Linkbase Document.\*\*

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\*Filed herewith

\*\*Furnished with the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2012

**SIGNATURES**

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

**Kandi Technologies, Corp.**

Date: August 14, 2012

By: /s/ Hu Xiaoming  
Hu Xiaoming  
President and Chief Executive Officer  
(Principal Executive Officer)

Date: August 14, 2012

By: /s/ Zhu Xiaoying  
Zhu Xiaoying  
Chief Financial Officer  
(Principal Financial and Accounting Officer)