CHINA NORTH EAST PETROLEUM HOLDINGS LTD
Form 10QSB
May 21, 2007

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

FORM 10-QSB

x

x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
for the quarterly period ended March 31, 2007

o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
for the transition period from _______ to ______

Commission file number 0-49846

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED
(Exact name of small business issuer as specified in its charter)

Nevada	87-0638750
(State of other jurisdiction of incorporation or organization)	(IRS Employer identification No.)

20337 Rimview Place, Walnut, California 91789
(Address of principal executive offices)

(909) 468-2840
(Issuer's telephone number)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 o No o

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

Number of shares of common stock outstanding as of May 18, 2007: 29,224,080

Transitional Small Business Disclosure Format: Yes o No x

1

INDEX TO FORM 10-QSB

SPECIAL NOTE REGARDING FORWARD—LOOKING STATEMENTS

On one or more occasions, we may make forward-looking statements in this Quarterly Report on Form 10-QSB regarding our assumptions, projections, expectations, targets, intentions or beliefs about future events. Words or phrases such as “anticipates,” “may,” “will,” “should,” “believes,” “estimates,” “expects,” “intends,” “plans,” “predicts,” “proj “will likely result,” “will continue” or similar expressions identify forward-looking statements. These forward-looking statements are only our predictions and involve numerous assumptions, risks and uncertainties, including, but not limited to those listed below and those business risks and factors described elsewhere in this report and our other Securities and Exchange Commission filings.

Forward-looking statements involve risks and uncertainties which could cause actual results or outcomes to differ materially from those expressed. We caution that while we make such statements in good faith and believe such statements are based on reasonable assumptions, including without limitation, management’s examination of historical operating trends, data contained in records and other data available from third parties, we cannot assure you that our projections will be achieved. Factors that may cause such differences include but are not limited to:

- Our expectation of continued growth in the demand for our oil;
- Our expectation that we will have adequate liquidity from cash flows from operations;
- A variety of market, operational, geologic, permitting, labor and weather related factors; and
- The other risks and uncertainties which are described below under “RISK FACTORS”, including, but not limited to, the following:
  - Unanticipated conditions may cause profitability to fluctuate.
  - Decreases in purchases of oil by our customer will adversely affect our revenues.

We have attempted to identify, in context, certain of the factors that we believe may cause actual future experience and results to differ materially from our current expectation regarding the relevant matter or subject area. In addition to the items specifically discussed above, our business and results of operations are subject to the uncertainties described under the caption “Risk Factors” which is a part of the disclosure included in Item 2 of this Report entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

From time to time, oral or written forward-looking statements are also included in our reports on Forms 10-KSB, 10-QSB and 8-K, Proxy Statements on Schedule 14A, press releases, analyst and investor conference calls, and other communications released to the public. Although we believe that at the time made, the expectations reflected in all of these forward looking statements are and will be reasonable, any or all of the forward-looking statements in this quarterly report on Form 10-QSB, our reports on Forms 10-KSB and 8-K, our Proxy Statements on Schedule 14A and any other public statements that are made by us may prove to be incorrect. This may occur as a result of inaccurate assumptions or as a consequence of known or unknown risks and uncertainties. Many factors discussed in this Quarterly Report on Form 10-QSB, certain of which are beyond our control, will be important in determining our future performance. Consequently, actual results may differ materially from those that might be anticipated from forward-looking statements. In light of these and other uncertainties, you should not regard the inclusion of a forward-looking statement in this Quarterly Report on Form 10-QSB or other public communications that we might make as a representation by us that our plans and objectives will be achieved, and you should not place undue reliance on such forward-looking statements.

We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. However, your attention is directed to any further disclosures made on related subjects in our subsequent annual and periodic reports filed with the SEC on Forms 10-KSB, 10-QSB and 8-K and Proxy Statements on Schedule 14A.

Unless the context requires otherwise, references to “we,” “us,” “our,” the “Company” and “CNEH” refer specifically to China North East Petroleum Holdings Limited and its subsidiaries.

3

PART I

Item 1 - Financial Statements (Unaudited)

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED AND SUBSIDIARIES
Condensed Consolidated Balance Sheet
At March 31, 2007 (Unaudited)

ASSETS

CURRENT ASSETS		
Cash and cash equivalents	$	526,058
Accounts receivable, net		391,753
Prepaid expenses and other current assets		953,748
Due from related parties		113,867
Value added tax recoverable		388,702
Total Current Assets		2,374,128
PROPERTY AND EQUIPMENT		
Oil and gas properties, net		25,421,324
Fixed assets, net		860,091
Oil and gas properties under construction		8,885,909
Total Property and Equipment		35,167,324
INTANGIBLE ASSETS, NET		50,496
TOTAL ASSETS	$	37,591,948

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES		
Accounts payable	$	21,726,953
Other payables and accrued liabilities		1,395,565
Note payable		129,184
Income tax and other tax payable		770,236
Due to a stockholder		1,746,128
Due to related parties		29,712
Total Current Liabilities		25,797,778
LONG-TERM LIABILITIES		
Due to a related party		5,451,685
Note payable		258,368
Total Long-term Liabilities		5,710,053
TOTAL LIABILITIES		31,507,831
COMMITMENTS AND CONTINGENCIES		-
MINORITY INTERESTS		453,464
STOCKHOLDERS' EQUITY		
Common stock, $0.001 par value, 150,000,000 shares authorized,		

29,224,080 shares issued and outstanding		29,224
Additional paid-in capital		4,078,430
Deferred stock compensation		(108,500)
Retained earnings		
Unappropriated		984,318
Appropriated		287,634
Accumulated other comprehensive income		359,547
Total Stockholders' Equity		5,630,653
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$	37,591,948

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

4

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED AND SUBSIDIARIES
Condensed Consolidated Statements of Operations and Comprehensive Income
For the three months ended March 31, 2007 and 2006 (Unaudited)

	Three months ended March 31, 2007	Restated 2006
NET SALES	$ 1,879,947	$ 1,106,878
COST OF SALES		
Production costs	336,790	260,519
Depreciation - oil and gas properties	389,227	346,984
Amortization of intangible assets	2,624	2,541
Total Cost of Sales	728,641	610,044
GROSS PROFIT	1,151,306	496,834
OPERATING EXPENSES		
Selling, general and administrative expenses	220,265	193,664
Government oil surcharge	157,131	-
Professional fees	16,000	30,773
Consulting fees	27,125	-
Depreciation - fixed assets	36,027	21,698
Total Operating Expenses	456,548	246,135
INCOME FROM OPERATIONS	694,758	250,699
OTHER INCOME (EXPENSE)		
Other income	-	14,762
Interest expense	(10,591)	(13,319)
Imputed interest expense	(131,846)	(40,548)
Interest income	248	99
Total Other Expenses, net	(142,189)	(39,006)
NET INCOME BEFORE TAXES AND MINORITY INTERESTS	552,569	211,693
Income tax expenses	(221,407)	(128,256)
Minority interests	(43,799)	5,136
NET INCOME	287,363	88,573
OTHER COMPREHENSIVE INCOME (LOSS)		
Foreign currency translation gain (loss)	87,251	(8,590)
COMPREHENSIVE INCOME	$ 374,614	$ 79,983

Net income per share-basic and diluted	$	0.01	$	0.00
Weighted average number of shares outstanding during the period basic and diluted		29,224,080		28,346,302

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

5

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
For the three months ended March 31, 2007 and 2006 (Unaudited)

	2007	Restated 2006
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 287,363	$ 88,573
Adjusted to reconcile net income to cash provided by operating activities:		
Depreciation of oil and gas properties	389,227	346,984
Depreciation of fixed assets	36,027	21,698
Amortization of intangible assets	2,624	2,541
Minority interests	43,799	(5,136)
Stocks issued for services	27,125	27,773
Imputed interest expenses	131,846	40,548
Changes in operating assets and liabilities		
(Increase) decrease in:		
Accounts receivable	358,931	(83,986)
Prepaid expenses and other current assets	(28,390)	145,953
Due from related parties	(49,836)	29,919
Value added tax recoverable	58,901	39,827
Increase (decrease) in:		
Accounts payable	490,089	(380,619)
Other payables and accrued liabilities	2,296	18,494
Income tax and other tax payable	462,572	173,204
Net cash provided by operating activities	2,212,574	465,773
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of oil and gas properties	(2,742,832)	(210,479)
Purchase of fixed assets	(123,925)	(20,416)
Net cash used in investing activities	(2,866,757)	(230,895)
CASH FLOWS FROM FINANCING ACTIVITIES		
Decrease in other loans payable	(25,612)	(18,371)
Increase in amount due to a stockholder	89,193	27,091
Increase (decrease) in amounts due to related parties	1,170,121	(597,717)
Net cash provided by (used in) financing activities	1,233,702	(588,997)
EFFECT OF EXCHANGE RATE ON CASH	(67,207)	(84,767)
	512,312	(438,886)

NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS				
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD		13,746		633,307
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$	526,058	$	194,421
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:				
Cash paid during the period for:				
Income tax expenses	$	60,462	$	19,849
Interest expenses	$	10,591	$	13,319

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

6

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED
AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL
STATEMENTS AS OF MARCH 31, 2007
(UNAUDITED)

NOTE 1 BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

In the opinion of management, the unaudited condensed consolidated financial statements contain all adjustments consisting only of normal recurring accruals considered necessary to present fairly the Company's financial position at March 31, 2007, the results of operations for the three months ended March 31, 2007 and 2006 and cash flows for the three months ended March 31, 2007 and 2006. The results for the three months ended March 31, 2007 are not necessarily indicative of the results to be expected for the entire fiscal year ending December 31, 2007.

These financial statements should be read in conjunction with the Company's annual report on Form 10-KSB as filed with the Securities and Exchange Commission.

NOTE 2 ORGANIZATION

China North East Petroleum Holdings Limited (“North East Petroleum”) is a US listed company which was incorporated in Nevada on August 20, 1999 under the name of Draco Holding Corporation (“Draco”). Draco was authorized to issue 20,000,000 shares of common stock of $0.001 par value per share.

Hong Xiang Petroleum Group Limited ("Hong Xiang Petroleum Group") was incorporated in the British Virgin Islands (“BVI”) on August 28, 2003 as an investment holding company.

On December 5, 2003, Song Yuan City Hong Xiang Petroleum Technical Services Co., Ltd. (“Hong Xiang Technical”) was incorporated in the People’s Republic of China (“PRC”) as a limited liability company with a registered capital of $484,000. Hong Xiang Technical provided technical advisory services to oil and gas exploration companies in the PRC.

During 2004, Hong Xiang Petroleum Group acquired a 100% ownership of Hong Xiang Technical.

During 2004, Hong Xiang Technical acquired a 100% interest in Song Yuan City Yu Qiao Qianan Hong Xiang Oil and Gas Development Co., Ltd. (“Hong Xiang Oil Development”), a limited liability company incorporated on April 1, 2003 in the PRC with a registered capital of $604,800. Hong Xiang Oil Development is engaged in the exploration and production of crude oil in the Jilin Oil Region, of the PRC.

During 2004, Draco executed a Plan of Exchange to acquire 100% of Hong Xiang Petroleum Group.

On January 26, 2007, Song Yuan Technical entered into an agreement with the stockholders of Yu Qiao to acquire 100% of the equity interest of Yu Qiao. In consideration for the acquisition, the Company issued to the stockholders of Yu Qiao an aggregate of 10,000,000 shares of the Company’s common stock having a fair value of $3,100,000 based on the preceding 30-day average of the high bid and the low ask price for the Company’s common stock as quoted on the Over-the-Counter Bulletin Board as of the date of the closing of the transaction. Before this transaction, Yu Qiao was owned 70% by a related party.

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED
AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL
STATEMENTS AS OF MARCH 31, 2007
(UNAUDITED)

NOTE 2 ORGANIZATION (CONTINUED)

Yu Qiao was incorporated in Song Yuan City, Jinlin Province, People’s Republic of China (“PRC”) on May 24, 2002 as a limited liability company. Yu Qiao is engaged in the extraction and production of crude oil in Jilin Province, PRC and operates 3 oilfields with a total exploration area of 39.2 square kilometers. Pursuant to a 20-year exclusive Cooperative Exploration Contract (the “Oil Lease”) which was entered into on May 28, 2002 with PetroChina Group, a corporation organized and existing under the laws of PRC (“PetroChina”), the Company has the right to explore, develop and extract oil at Qian’an 112, Da 34 and Gu 31 area. Pursuant to the Oil Lease, PetroChina is entitled to 20% of the Company’s oil production for the first ten years of the Oil Lease term and 40% of the Company’s oil production for the remaining ten years of the Oil Lease term. On May 28, 2002, the Company also executed an Agreement of leasing 20.7 square kilometers of Qian’an 112 area to Songyuan Yu Qiao Qianan Hong Xiang Oil and Gas Development Co., Ltd. (‘Hong Xiang Oil Development”) and the Company is entitled to 2% of total sale revenues as consideration.

The acquisition of Yu Qiao was accounted for as a reorganization of entities under common control. Accordingly, the operations of Yu Qiao for the three months ended March 31, 2007 and 2006 were included in the unaudited condensed consolidated financial statements as if the transactions had occurred retroactively.

NOTE 3 PRINCIPLES OF CONSOLIDATION

The accompanying unaudited condensed consolidated financial statements for 2007 include the unaudited financial statements of North East Petroleum and its wholly owned subsidiary, Hong Xiang Petroleum Group Limited ("Hong Xiang Petroleum Group") and 90% equity interest owned subsidiaries, Song Yuan North East Petroleum Technical Service Co., Ltd. (“Song Yuan Technical”), LongDe Oil & Gas Development Co. Ltd. (“LongDe”) and Sonyuan City Yu Qiao Oil And Gas Development Limited Corporation (“Yu Qiao”) (collectively, “the Company”). The minority interests represent the minority shareholders’ 10% share of the results of Song Yuan Technical, LongDe and Yu Qiao.

The accompanying unaudited condensed consolidated financial statements for 2006 include the unaudited financial statements of North East Petroleum and its wholly owned subsidiaries, Hong Xiang Petroleum Group, Song Yuan City Hong Xiang Petroleum Technical Services Co., Ltd. (“Hong Xiang Technical”) and Song Yuan City Yu Qiao Qianan Hong Xiang Oil and Gas Development Co., Ltd. (“Hong Xiang Oil Development”) and 90% equity interest owned subsidiaries, Song Yuan Technical, LongDe and Yu Qiao. The minority interests represent the minority shareholders’ 10% share of the results of Song Yuan Technical, LongDe and Yu Qiao.

All significant inter-company accounts and transactions have been eliminated in consolidation.

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED
AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL
STATEMENTS AS OF MARCH 31, 2007
(UNAUDITED)

NOTE 4 TERMINATION OF SUBSIDIARIES

In March 2007, the Company approved the dissolution of its wholly owned subsidiaries, Hong Xiang Technical and Hong Xiang Oil Development. Hong Xiang Oil Development, a wholly owned subsidiary of Hong Xiang Technical, leases the rights to explore, develop and extract oil in Qian'an 112 from Yu Qiao which holds a 20-year exclusive Cooperative Exploration Contract with PetroChina for the rights to explore, develop and extract oil in Qian'an 112 (see note 2).

On January 26, 2007, the Company's 90% owned subsidiary, Song Yuan Technical acquired 100% of the equity interests of Yu Qiao from the stockholders of Yu Qiao. As a result of the acquisition, the lease agreement became unnecessary, as the Company became, effectively, both the lessor and lessee under the lease agreement pertaining to Qian'an 112 and may now exploit the rights under the Exploration Contract through Yu Qiao. The Board of the Company therefore determined that Hong Xiang Technical and Hong Xiang Oil Development are no longer necessary elements of its corporate structure and accordingly approved the dissolution of these companies.

The Company has not incurred any material costs in connection with the dissolution of Hong Xiang Technical and Hong Xiang Oil Development nor does the dissolution of Hong Xiang Technical and Hong Xiang Oil have a significant financial impact on the Company's operations or financial condition as all the assets, liabilities, retained profit and operations of Hong Xiang Oil Development were transferred to Yu Qiao at the book values upon Yu Qiao becoming a subsidiary of the Company.

A summary of the net assets transferred from Hong Xiang Technical and Hong Xiang Oil Development to Yu Qiao is as follows:

Oil and gas properties and fixed assets, net	$ 9,204,498
Oil and gas properties under construction	5,694,059
Total assets	14,898,557
Less: Accounts payable and accrued liabilities	(7,389,421)
Due to related parties	(3,936,528)
Notes payable	(387,552)
Book value of net assets transferred	3,185,056

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED
AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL
STATEMENTS AS OF MARCH 31, 2007
(UNAUDITED)

NOTE 5 REVENUE RECOGNITION

The Company recognizes revenue upon the delivery of its share of crude oil extracted to its sole customer, PetroChina at which time title is passed; there are no uncertainties regarding customer acceptance; persuasive evidence of an arrangement exists; the sales price is fixed and determinable; and collectability is deemed probable.

Pursuant to the Oil Lease entered into on May 28, 2002 with PetroChina Group, the Company is entitled to 80% of the Company's oil production for the first ten years to 2012 and 60% of the Company's oil production for the remaining ten years to 2022.

NOTE 6 PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid expenses and other current assets at March 31, 2007 consist of the following:

		(Unaudited)
Prepaid expenses	$	285,502
Deposits paid to suppliers		636,426
Other receivables		31,820
	$	953,748

NOTE 7 RELATED PARTY TRANSACTIONS

a) As of March 31, 2007, two related parties owed the Company $71,051 and $42,816 respectively. The amounts are interest-free and are repayable on demand.

b) As of March 31, 2007, the Company owed a stockholder $1,746,128 for short-term advances. Imputed interest is computed at 7% per annum on the amount due.

c) As of March 31, 2007, the Company owed a related party $5,451,685 for advances without fixed repayment terms. Imputed interest is computed at 7% per annum on the amount due.

d) As of March 31, 2007, the Company owed two related parties of $12,918 and $16,794 respectively for short-term advances. Imputed interest is computed at 7% per annum on the amounts due.

e) Total interest expenses payable to a stockholder and related parties amounted to $131,846 and $40,548 for the three months ended March 31, 2007 and 2006 respectively.

f) The Company paid a stockholder $3,088 for leased office spaces for the three months ended March 31, 2007.

g) On January 26, 2007, Song Yuan Technical entered into an agreement with a related party and third parties who are the stockholders of Yu Qiao to acquire 100% of the equity interest of Yu Qiao. In consideration for the acquisition, the Company issued to the stockholders of Yu Qiao an aggregate of 10,000,000 shares of the Company's common stock having a fair value of $3,100,000.

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED
AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL
STATEMENTS AS OF MARCH 31, 2007
(UNAUDITED)

NOTE 8 NOTES PAYABLE

Notes payable consist of the following:

		(Unaudited)
Note payable to a bank, interest rate of 10.60% per annum, guaranteed by a subsidiary, due June 2007	$	129,184
Note payable to a bank, interest rate of 11.16% per annum, secured by a property owned by a stockholder, due July 2006 and extended to July 2008		258,368
		387,552
Less: current maturities		129,184
Long-term portion	$	258,368

Interest expense for the three months ended March 31, 2007 was $10,591.

NOTE 9 COMMITMENTS AND CONTINGENCIES

(A) Lease commitment

The Company leases office spaces from a stockholder and land spaces from a third party under two operating leases which expire on June 30, 2015 and September 20, 2023 respectively at an annual rental of $12,402 and $161 respectively.

As of March 31, 2007, the Company had outstanding commitments with respect to the above non-cancelable operating leases, which are due as follows:

2007	$	9,423
2008		12,563
2009		12,563
2010		12,563
Thereafter		57,862
	$	104,974

(B) Capital commitment

According to the amended Articles of Association of Song Yuan Technical, the Company has to fulfill registered capital contribution of $1 million. As of March 31, 2007, the Company has fulfilled $490,000 of the registered capital requirement and has outstanding capital contributions of $510,000.

NOTE 10 STOCKHOLDERS' EQUITY

Stock issued for acquisition a subsidiary

On January 26, 2007, Song Yuan Technical entered into an agreement with a related party and third parties who are the stockholders of Yu Qiao to acquire 100% of the equity interest of Yu Qiao. In consideration for the acquisition, the Company issued to the stockholders of Yu Qiao an aggregate of 10,000,000 shares of the Company’s common stock having a fair value of $3,100,000.

NOTE 11 CONCENTRATIONS AND RISKS

During 2007, 100% of the Company's assets were located in the PRC and 100% of the Company's revenues were derived from one customer located in the PRC. The lease require the Company to sell crude oil to PetroChina only.

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

We are engaged in the extraction and production of crude oil in Jilin Province, PRC, through Songyuan City Yu Qiao Qianan Hong Xiang Oil and Gas Development Co., Ltd. (“Hong Xiang Oil Development”), a wholly-owned subsidiary of the Company’s 100% owned subsidiary Hong Xiang Technical Services Co., Ltd. (“Hong Xiang Technical”) organized and existing under the laws of PRC. The oil field is called Jilin Qian’an Oil Field Zone 112 (“Qian’an 112”), located approximately 9 kilometers southwest of Qian’an City with a total exploration area of 20.7 square kilometers. Pursuant to a 20-year exclusive Cooperative Exploration Contract (the “Contract”) among PetroChina Group, a corporation organized and existing under the laws of the People’s Republic of China (“PetroChina”), Song Yuan City Yu Qiao Oil and Gas Exploration Limited Corp., a corporation organized and existing under the laws of the People’s Republic of China (“Yu Qiao”) and the Company, we have the right to explore, develop (including well logging, drill-stem testing and core sampling) and pump oil at Qian’an 112. Pursuant to the Contract, PetroChina is entitled to 20% of our output in the first ten years and 40% of our output thereafter until the end of the Contract; and Yu Qiao is entitled to 2% of our output as a management fee for managing the process of oil production. The Company sells all of its current oil production to PetroChina.

Pursuant to the terms of the Exploration Contract, all payments by PetroChina for sales of the Company’s crude oil are paid to Yu Qiao, who forwards the payment to the Company after deduction of its management fee.

On July 26, 2006, the Company entered into a joint venture agreement with a stockholder of the Company and a related party to contribute to the increased registered capital of a limited liability company under the Laws of the PRC, named Song Yuan North East Petroleum Technical Service Co., Ltd. (“Song Yuan Technical”). The purpose of Song Yuan Technical is to acquire oil and gas properties and to engage in the exploration of crude oil in the PRC. The Company owns 90% membership interest in Song Yuan Technical, the related party owns the remaining 10% membership interest in Song Yuan Technical.

Song Yuan Technical owned 100% equity interest of LongDe Oil & Gas Development Co. Ltd. (“LongDe”). LongDe was incorporated in May, 2003 under the PRC laws and is a party to a 20 year Exploration Contract with PetroChina, pursuant to which LongDe has the right to explore, develop and pump oil at Hetingbao Oilfield 301 Area in the PRC (“Hetingbao 301”). Pursuant to the Exploration Contract, PetroChina is entitled to 20% of LongDe’s output in the first ten years and 40% of LongDe’s output thereafter until the end of the Exploration Contract.

On January 26, 2007, Song Yuan Technical, the Company’s, 90% owned joint venture, completed the acquisition of 100% of the equity interests of Yu Qiao. In consideration for this acquisition, the Company, as the 90% owner of Song Yuan Technical, will issue to the three former shareholders of Yu Qiao (one of whom is Ms. Ju, who owns 70% equity interest of Yu Qiao) an aggregate of ten million (10,000,000) shares of the Company’s unregistered common stock, in exchange for their equity interests. Such shares have a market value of approximately US$3.1 million based on the preceding 30-day average of the high bid and the low ask price for Registrant’s common stock as quoted on the Over-the-Counter Bulletin Board as of the Closing. As a result of this acquisition, the Company controls 90% ownership of Yu Qiao, through its 90% owned joint venture, Song Yuan Technical. As the majority shareholder of Yu Qiao, the Company may exploit the rights to extract and develop Qian’an 112 under the Exploration Contract through Yu Qiao and other oil fields under Exploration Contracts that Yu Qiao entered into with PetroChina in May 2003. These oil fields include Da 34 oilfield and Gu 31 oilfield in Jilin province and cover a total of 3,207 acres and consist of approximately 227 oil wells.

As a result of Yu Qiao acquisition, the Oil Lease became unnecessary, as the Company became, effectively, both the lessor and lessee under the lease agreement pertaining to the Qian’an 112 oil fields. In particular, the management fee paid by Hong Xiang Oil Development to Yu Qiao became redundant as both entities are controlled by the Company. In addition, all operations, assets and liabilities of Hong Xiang Oil Development will be transferred to Yu Qiao. As such, on March 19, 2007, the Company dissolved Hong Xiang Oil Development and Hong Xiang Technical as both subsidiaries have no assets other than the lease agreement, are no longer necessary elements of its corporate structure. The Company did not incur any material costs in connection to the closure of Hong Xiang Technical and Hong Xiang Oil Development.

As the majority shareholder of Yu Qiao, the Company now has the rights to extract and develop Qian’an 112 under the Exploration Contract through Yu Qiao and PetroChina under three different Exploration Contracts that Yu Qiao entered into with PetroChina in May 2003. These oil fields include Da 34 oilfield and Gu 31 oilfield in Jilin province and cover a total of 3,207 acres and consist of approximately 227 oil wells.

The Company is paid the FOB price on the first day of each month established by the Singapore crude oil spot market.

Results of Operations

Three Months Ended March 31, 2007 Compared To Three Months Ended March 31, 2006

Revenues. Revenues for the quarter ended March 31, 2007 were $1,879,947 compared to $1,106,878 for the quarter ended March 31, 2006, an increase of $773,069, or 70%. This increase was due to an increase in crude oil production as well as an increase in the average selling price of crude oil. Our output of crude oil for the three months ended March 31, 2007 was 4367 tons compared to 2502 tons for the same quarter in 2006. The increase in production mainly because of the new wells being taken into production.

Cost of sales. Cost of sales increased by 19% from $610,044 for the three months ended March 31, 2006 to $728,641 for the three months ended March 31, 2007. The increase in cost of sales resulted primarily from the increase in production.

Operating Expenses. Operating expenses increased by 85% from $246,135 for the three months ended March 31, 2006 to $456,548 for the three months ended March 31, 2007 primarily as a result of an additional consulting fee of $27,125 paid to a third party consultant, where no such fee was paid in the same quarter of 2006. In addition, the payment of government oil surcharge did not occurred in the same quarter 2006. For the three months ended March 31, 2007, the Company paid government oil surcharge of $157,131 to the PRC government as a result of the increase in average selling price of crude oil.

Net Income. Net income increased by 224 % from $88,573 for the three months ended March 31, 2006 to $287,363 for the three months ended March 31, 2007, primarily as a result of a 70% increase in sales as described above.

LIQUIDITY AND CAPITAL RESOURCES

As March 31, 2007, the Company had cash and cash equivalents of $526,058, other current assets of $1,848,070 and current liabilities of approximately $26 million. To date, company accomplishes growth in production and cash flow through developing new wells by leasing properties through our subsidiaries. These activities require substantial capital expenditures. Over the last year, we have successfully grown our reserve base and production, resulting in growth in our net cash flow from operating activities. Cash flow provided by operating activities was $2,212,574 for the three months ended March 31, 2007, compared to $465,773 for the same period 2006.

Management believes the Company will be able to meet its current operating needs through internally generated cash from operations, including Yu Qiao. Management believes that oil property investing activities in 2007 can be financed through operating cash flow (installment). In order to develop additional wells, the Company may also consider a number of different financing opportunities. Adequate funds may not be available on terms acceptable to us. If additional funds are raised through the issuance of equity securities, dilution to existing stockholders may result.

Capital Commitments.

Pursuant to the Joint Venture Agreement, the Company is obligated to contribute $1 million as registered capital of Song Yuan Technical. On October 8, 2006, the Company made a capital contribution of $490,000 to Song Yuan Technical and received 90% of Song Yuan Technical’s membership and profit interests. The Company remains obligated to contribute an additional $510,000 in capital to Song Yuan Technical. The Company will contribute the remaining $510,000 during the second quarter of 2007.

RISK FACTORS

Our business is subject to certain risks, and we want you to review these risks while you are evaluating our business and our historical results. Please keep in mind that any of the following risks discussed below and elsewhere in this Annual Report could materially and adversely affect us, our operating results, our financial condition and our projections and beliefs as to our future performance. As such, our results could differ materially from those projected in our forward-looking statements. Additional risks and uncertainties not currently known to us or those we currently deem to be immaterial may also materially and adversely affect our business.

RISKS RELATED TO OUR BUSINESS

Oil prices fluctuate significantly, and lower prices for an extended period of time are likely to have a material adverse impact on our business.

Our revenues, profitability and future growth depend substantially on prevailing prices for crude oil. We sell to one customer, PetroChina, and we are paid a price per barrel equal to the Singapore crude oil spot market price on the first day of every month. These prices also affect the amount of cash flow available for capital expenditures and our ability to borrow and raise additional capital. The lower prices may reduce the amount of crude oil that we can economically produce.

Among the factors that can cause fluctuations are:

- the price and availability of alternative fuels;
- disruptions in supply and changes in demand caused by weather conditions;
- changes in demand as a result of changes in price;
- political conditions in oil and gas producing regions; and
- domestic governmental regulations.

Our future success depends on our ability to find, develop and acquire oil and gas reserves.

To maintain production levels, we must locate and develop or acquire new crude oil reserves to replace those depleted by production. Without successful exploration or acquisition activities, our reserves, production and revenues will decline rapidly. We may be unable to find and develop or acquire additional reserves at an acceptable cost. In addition, substantial capital is required to replace and grow reserves. If lower crude oil price or operating constraints or production difficulties result in our cash flow from operations being less than expected, we may be unable to expend the capital necessary to locate and develop or acquire new crude oil reserves.

We may need to raise substantial additional capital, which may result in substantial dilution to existing stockholders.

In order to fully develop and exploit the Company's oil reserves and to execute on our business plan, the Company may need substantial additional capital. The Company is currently considering possible sources of this additional capital, including raising capital through the issuance of debt or equity securities. There can be no assurance that we will be able to raise sufficient additional capital at all or on terms favorable to our stockholders or us. If we issue equity securities in order to raise additional capital in the amounts currently contemplated, the stockholders will experience immediate and substantial dilution in their ownership percentage of the combined company. In addition, to raise the capital we need, we may need to issue additional shares at a discount to the current market price. If the terms of such financing are unfavorable to us or our stockholders, the stockholders may experience substantial dilution in the net tangible book value of their stock. In addition, any new equity securities may have rights, preferences or privileges senior to those of existing holders of common stock. If we cannot raise funds on acceptable terms, we may not be able to fully develop or exploit our existing oil reserves, take advantage of future opportunities or respond to competitive pressures or unanticipated requirements all of which could have a material adverse effect on us.

Environmental and regulatory factors

The oil drilling industry in China to date has not been subject to the type and scope of regulation seen in Europe and the United States. However, the possibility exists that new legislation or regulations may be adopted or that the enforcement of existing laws could become more stringent, either of which may have a significant impact on our mining operations or our customers' ability to use oil and may require us or our customers to significantly change operations or to incur substantial costs. We believe that our operations in China are in compliance with China's applicable legal and regulatory requirements. However, there can be no assurance that China's central or local governments will not impose new, stricter regulations or interpretations of existing regulations that would require additional expenditures.

Reserve degradation and depletion may negatively effect our results.

Our profitability depends substantially on our ability to exploit our oil reserves at competitive costs. Replacement reserves may not be available when required or, if available, may not be capable of being drilled at costs comparable to those characteristics of the depleting oil field. We may in the future acquire oil reserves from third parties. We may not be able to accurately assess the geological characteristics of any reserves that we acquire, which may adversely affect our profitability and financial condition. Exhaustion of reserves at Qian'an 112, Hetingbao 301 and at oil fields that we may acquire in the future can also have an adverse effect on operating results that is disproportionate to the percentage of overall production represented by such mines.

Our reserve estimates may prove to be incorrect.

Any material inaccuracies in our reserve estimates or assumptions underlying our reserve estimates could cause the quantities and net present value of our reserves to be overstated or understated.

There are numerous uncertainties inherent in estimating quantities of proved reserves, including many factors beyond our control that could cause the quantities and net present value of our reserves to be overstated. The reserve information included or incorporated by reference in this report represents estimates prepared by our internal engineers and examined by independent petroleum consultants. Estimation of reserves is not an exact science. Estimates of economically recoverable oil and natural gas reserves and of future net cash flows necessarily depend upon a number of variable factors and assumptions, any of which may cause these estimates to vary considerably from actual results, such as:

- historical production from an area compared with production from similar producing areas;
- assumed effects of regulation by governmental agencies;
- assumptions concerning future oil and natural gas prices, future operating costs and capital expenditures; and
- estimates of future severance and excise taxes, workover and remedial costs.

Estimates of reserves based on risk of recovery and estimates of expected future net cash flows prepared or audited by different engineers, or by the same engineers at different times, may vary substantially. Actual production, revenues and expenditures with respect to our reserves will likely vary from estimates, and the variance may be material. The net present values referred to in this report should not be construed as the current market value of the estimated oil reserves attributable to our properties. In accordance with SEC requirements, the estimated discounted net cash flows from proved reserves are generally based on prices and costs as of the date of the estimate, whereas actual future prices and costs may be materially higher or lower.

Our acquisition strategy involves inherent risks.

We are seeking to expand our operations and oil reserves in the regions in which we operate through acquisitions of businesses and assets, including leases of oil reserves. Acquisition transactions involve inherent risks, such as:

- uncertainties in assessing the value, strengths, weaknesses, contingent and other liabilities and potential profitability of acquisition or other transaction candidates;
- the potential loss of key personnel of an acquired business;
- the ability to achieve identified operating and financial synergies anticipated to result from an acquisition or other transaction;

- problems that could arise from the integration of the acquired business;
- unanticipated changes in business, industry or general economic conditions that affect the assumptions underlying the acquisition or other transaction rationale; and
- unexpected development costs, that adversely affect our profitability.

Any one or more of these factors could cause us not to realize the benefits anticipated to result from the acquisition of businesses or assets.

RISKS RELATED TO DOING BUSINESS IN CHINA

Our operations are primarily located in China and may be adversely affected by changes in the policies of the Chinese government.

The political environment in the PRC may adversely affect the Company's business operations. The PRC has operated as a socialist state since 1949 and is controlled by the Communist Party of China. In recent years, however, the government has introduced reforms aimed at creating a "socialist market economy" and policies have been implemented to allow business enterprises greater autonomy in their operations. Changes in the political leadership of the PRC may have a significant effect on laws and policies related to the current economic reforms program, other policies affecting business and the general political, economic and social environment in the PRC, including the introduction of measures to control inflation, changes in the rate or method of taxation, the imposition of additional restrictions on currency conversion and remittances abroad, and foreign investment. These effects could substantially impair the Company's business, profits or prospects in China. Moreover, economic reforms and growth in the PRC have been more successful in certain provinces than in others, and the continuation or increases of such disparities could affect the political or social stability of the PRC.

The PRC's economic, political and social conditions, as well as governmental policies, could affect the financial markets in China and our liquidity and access to capital and our ability to operate our business.

The PRC economy differs from the economies of most developed countries in many respects, including the amount of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. While the PRC economy has experienced significant growth over the past, growth has been uneven, both geographically and among various sectors of the economy. The PRC government has implemented various measures to encourage economic growth and guide the allocation of resources. Some of these measures benefit the overall PRC economy, but may also have a negative effect on us. The PRC economy has been transitioning from a planned economy to a more market-oriented economy. Although the PRC government has implemented measures since the late 1970s emphasizing the utilization of market forces for economic reform, the reduction of state ownership of productive assets and the establishment of improved corporate governance in business enterprises, a substantial portion of productive assets in China is still owned by the PRC government. In addition, the PRC government continues to play a significant role in regulating industry development by imposing industrial policies. The PRC government also exercises significant control over China's economic growth through the allocation of resources, controlling payment of foreign currency- denominated obligations, setting monetary policy and providing preferential treatment to particular industries or companies. Since late 2003, the PRC government implemented a number of measures, such as raising bank reserves against deposit rates to place additional limitations on the ability of commercial banks to make loans and raise interest rates, in order to slow down specific segments of China's economy which it believed to be overheating. These actions, as well as future actions and policies of the PRC government, could materially affect our liquidity and access to capital and our ability to operate our business.

The Chinese government exerts substantial influence over the manner in which the Company must conduct its business activities.

The PRC only recently has permitted greater provincial and local economic autonomy and private economic activities. The government of the PRC has exercised and continues to exercise substantial control over virtually every sector of the Chinese economy through regulation and state ownership. Accordingly, government actions in the future, including any decision not to continue to support recent economic reforms and to return to a more centrally planned economy or regional or local variations in the implementation of economic policies, could have a significant effect on economic conditions in the PRC or particular regions thereof, and could require the Company to divest the interests it then holds in Chinese properties or joint ventures. Any such developments could have a material adverse effect on the business, operations, financial condition and prospects of the Company.

Future inflation in China may inhibit economic activity and adversely affect the Company's operations.

In recent years, the Chinese economy has experienced periods of rapid expansion and within which some years with high rates of inflation and deflation, which have led to the adoption by the PRC government, from time to time, of various corrective measures designed to restrict the availability of credit or regulate growth and contain inflation. While inflation has moderated since 1995, high inflation may in the future cause the PRC government to impose controls on credit and/or prices, or to take other action, which could inhibit economic activity in China, and thereby adversely affect the Company's business operations and prospects in the PRC.

We may be restricted from freely converting the Renminbi to other currencies in a timely manner.

The Renminbi is not a freely convertible currency at present. The Company receives all of its revenue in Renminbi, which may need to be converted to other currencies, primarily U.S. dollars, and remitted outside of the PRC. Effective July 1, 1996, foreign currency "current account" transactions by foreign investment enterprises, including Sino-foreign joint ventures, are no longer subject to the approval of State Administration of Foreign Exchange ("SAFE," formerly, "State Administration of Exchange Control"), but need only a ministerial review, according to the Administration of the Settlement, Sale and Payment of Foreign Exchange Provisions promulgated in 1996 (the "FX regulations"). "Current account" items include international commercial transactions, which occur on a regular basis, such as those relating to trade and provision of services. Distributions to joint venture parties also are considered a "current account transaction." Other non-current account items, known as "capital account" items, remain subject to SAFE approval. Under current regulations, the Company can obtain foreign currency in exchange for Renminbi from swap centers authorized by the government. The Company does not anticipate problems in obtaining foreign currency to satisfy its requirements; however, there is no assurance that foreign currency shortages or changes in currency exchange laws and regulations by the Chinese government will not restrict the Company from freely converting Renminbi in a timely manner. If such shortages or change in laws and regulations occur, the Company may accept Renminbi, which can be held or re-invested in other projects.

We may suffer from exchange rate risks that could result in foreign currency exchange loss.

Because our business transactions are denominated in RMB and our funding and result of operations will be denominated in USD, fluctuations in exchange rates between USD and RMB will affect our balance sheet and financial results. Since July 2005, RMB is no longer solely pegged with USD but is pegged against a basket of currencies as a whole in order to keep a more stable exchange rate for international trading. With the very strong economic growth in China in the last few years, RMB is facing a very high pressure to appreciate against USD. Such pressure would result more fluctuations in exchange rates and in turn our business would be suffered from higher exchange rate risk.

There are very limited hedging tools available in China to hedge our exposure in exchange rate fluctuations. They are also ineffective in the sense that these hedges cannot be freely preformed in the PRC financial market, and more important, the frequent changes in PRC exchange control regulations would limit our hedging ability for RMB.

We may be unable to enforce our rights due to policies regarding the regulation of foreign investments in China.

The PRC's legal system is a civil law system based on written statutes in which decided legal cases have little value as precedents, unlike the common law system prevalent in the United States. The PRC does not have a well-developed, consolidated body of laws governing foreign investment enterprises. As a result, the administration of laws and regulations by government agencies may be subject to considerable discretion and variation, and may be subject to influence by external forces unrelated to the legal merits of a particular

18

matter. China's regulations and policies with respect to foreign investments are evolving. Definitive regulations and policies with respect to such matters as the permissible percentage of foreign investment and permissible rates of equity returns have not yet been published. Statements regarding these evolving policies have been conflicting and any such policies, as administered, are likely to be subject to broad interpretation and discretion and to be modified, perhaps on a case-by-case basis. The uncertainties regarding such regulations and policies present risks that the Company will not be able to achieve its business objectives. There can be no assurance that the Company will be able to enforce any legal rights it may have under its contracts or otherwise.

Because our assets are located overseas, stockholders may not receive distributions that they would otherwise be entitled to if we were declared bankrupt or insolvent.

Our assets are, for the most part, located in the PRC. Because the Company's assets are located overseas, the assets of the Company may be outside of the jurisdiction of U.S. courts to administer if the Company was the subject of an insolvency or bankruptcy proceeding. As a result, if the Company was declared bankrupt or insolvent, the Company's stockholders may not receive the distributions on liquidation that they are otherwise entitled to under U.S. bankruptcy law.

Our acquisitions of LongDe and Yu Qiao (after our fiscal year) were structured to attempt to fully comply with PRC rules and regulations. However, such arrangements may be adjudicated by relevant PRC government agencies as not being in compliance with PRC governmental regulations on foreign investment in oil and gas industries and such structures may limit our control with respect to such entities.

PRC rules and regulations do not allow foreign investors to directly own 100% of a domestic oil and gas business. As such, we are ineligible to own directly 100% a domestic oil and gas business in China. We acquired Hong Xiang Oil Development through Hong Xiang Technical, our 100% owned subsidiary. We acquired a majority interest of LongDe and Yu Qiao through Song Yuan Technical, our 90% owned joint venture incorporated in the PRC. Our acquisition of Yu Qiao subsequent to our fiscal year is currently provided through a trust arrangement with two PRC citizens designated by PetroChina, a government owned entity; pursuant to which they agree to hold 30% securities of Yu Qiao for the benefit of Song Yuan Technical in compliance with the applicable law of the PRC. However, pursuant to the trust agreement, they agree, among other things, to (i) vote the securities as directed by Song Yuan technical, (ii) deliver all payments, distributions and other economic benefits received with respect to the securities to Song Yuan Technical, (iii) not transfer or encumber the securities without the consent of Song Yuan Technical and (iv) to transfer the securities to Song Yuan Technical as soon as permissible under the laws of the PRC.

Although we have been advised by our PRC counsel that our arrangements with our affiliated Chinese entities are valid under current PRC laws and regulations, we cannot assure you that we will not be required to restructure our organization structure and operations in China to comply with changing and new PRC laws and regulations. Restructuring of our operations may result in disruption of our business, diversion of management attention and the incurrence of substantial costs.

Recent PRC regulations relating to offshore investment activities by PRC residents may increase our administrative burden and restrict our overseas and cross-border investment activities. If our shareholders who are PRC residents fail to make any required applications and filings under such regulations, we may be unable to distribute profits and may become subject to liability under PRC laws.

The PRC National Development and Reform Commission, or NDRC, and SAFE recently promulgated regulations that require PRC residents and PRC corporate entities to register with and obtain approvals from relevant PRC government authorities in connection with their direct or indirect offshore investment activities. These regulations apply to our shareholders who are PRC residents and may apply to any offshore acquisitions that we make in the future.

Under the SAFE regulations, PRC residents who make, or have previously made, direct or indirect investments in offshore companies will be required to register those investments. In addition, any PRC resident who is a direct or indirect shareholder of an offshore company is required to file with the local branch of SAFE, with respect to that offshore company, any material change involving capital variation, such as an increase or decrease in capital, transfer or swap of shares, merger, division, long-term equity or debt investment or creation of any security interest over the assets located in China. If any PRC shareholder fails to make the required SAFE registration, the PRC subsidiaries of that offshore parent company may be prohibited from distributing their profits and the proceeds from any reduction in capital, share transfer or liquidation, to their offshore parent company, and the offshore parent company may also be prohibited from injecting additional capital into their PRC subsidiaries. Moreover, failure to comply with the various SAFE registration requirements described above could result in liability under PRC laws for evasion of applicable foreign exchange restrictions.

We cannot assure you that all of our shareholders who are PRC residents will comply with our request to make or obtain any registrations or approvals required under these regulations or other related legislation. Furthermore, as the regulations are relatively new, the PRC government has yet to publish implementing rules, and much uncertainty remains concerning the reconciliation of the new regulations with other approval requirements. It is unclear how these regulations, and any future legislation concerning offshore or cross-border transactions, will be interpreted, amended and implemented by the relevant government authorities. The failure or inability of our PRC resident shareholders to comply with these regulations may subject us to fines and legal sanctions, restrict our overseas or cross-border investment activities, limit our ability to inject additional capital into our PRC subsidiaries, and the ability of our PRC subsidiaries to make distributions or pay dividends, or materially and adversely affect our ownership structure. If any of the foregoing events occur, our acquisition strategy, business operations and ability to distribute profits to you could be materially and adversely affected.

PRC regulation of loans and direct investment by offshore holding companies to PRC entities may delay or prevent us from raising finance to make loans or additional capital contributions to our PRC operating subsidiaries and affiliates.

As an offshore holding company of our PRC operating subsidiaries and affiliates, we may make loans to our PRC subsidiaries and consolidated PRC affiliated entities, or we may make additional capital contributions to our PRC subsidiaries. Any loans to our PRC subsidiaries or consolidated PRC affiliated entities are subject to PRC regulations and approvals.

We may also determine to finance Song Yuan Technical, by means of capital contributions. These capital contributions to Song Yuan Technical must be approved by the PRC Ministry of Commerce or its local counterpart. We cannot assure you that we can obtain these government registrations or approvals on a timely basis, if at all, with respect to future loans or capital contributions by us to our operating subsidiaries. If we fail to receive such registrations or approvals, our ability to capitalize our PRC operations would be negatively affected which would adversely and materially affect our liquidity and our ability to expand our business.

RISKS RELATED TO CORPORATE AND STOCK MATTERS

Our authorized preferred stock exposes stockholders to certain risks.

Our Articles of Incorporation authorizes the issuance of up to 50,000,000 shares of preferred stock, par value $.001 per share. To date, no shares of preferred stock have been issued. The authorized preferred stock constitutes what is commonly referred to as “blank check” preferred stock. This type of preferred stock allows the Board of Directors to divide the preferred stock into series, to designate each series, to fix and determine separately for each series any one or more relative rights and preferences and to issue shares of any series without further stockholder approval. Preferred stock authorized in series allows our Board of Directors to hinder or discourage an attempt to gain control of us by a merger, tender offer at a control premium price, proxy contest or otherwise. Consequently, the preferred stock could entrench our management. In addition, the market price of our common stock could be materially and adversely affected by the existence of the preferred stock.

The market for the Company's common stock is illiquid.

The Company's common stock is traded on the Over-the-Counter Bulletin Board. It is thinly traded compared to larger more widely known companies in its industry. Thinly traded common stock can be more volatile than stock trading in an active public market. The Company cannot predict the extent to which an active public market for its common stock will develop or be sustained.

Our stock is a penny stock. Trading of our stock may be restricted by the SEC's penny stock regulations which may limit a stockholder's ability to buy and sell our stock.

Our stock is a penny stock. The SEC has adopted Rule 15g-9 which generally defines "penny stock" to be any equity security that has a market price (as defined) less than $5.00 per share or an exercise price of less than $5.00 per share, subject to certain exceptions. Our securities are covered by the penny stock rules, which impose additional sales practice requirements on broker-dealers who sell to persons other than established customers and "accredited investors". The term "accredited investor" refers generally to institutions with assets in excess of $5,000,000 or individuals with a net worth in excess of $1,000,000 or annual income exceeding $200,000 or $300,000 jointly with their spouse. The penny stock rules require a broker-dealer, prior to a transaction in a penny stock not otherwise exempt from the rules, to deliver a standardized risk disclosure document in a form prepared by the SEC which provides information about penny stocks and the nature and level of risks in the penny stock market. The broker-dealer also must provide the customer with current bid and offer quotations for the penny stock, the compensation of the broker-dealer and its salesperson in the transaction and monthly account statements showing the market value of each penny stock held in the customer's account. The bid and offer quotations, and the broker-dealer and salesperson compensation information, must be given to the customer orally or in writing prior to effecting the transaction and must be given to the customer in writing before or with the customer's confirmation. In addition, the penny stock rules require that prior to a transaction in a penny stock not otherwise exempt from these rules, the broker-dealer must make a special written determination that the penny stock is a suitable investment for the purchaser and receive the purchaser's written agreement to the transaction. These disclosure requirements may have the effect of reducing the level of trading activity in the secondary market for the stock that is subject to these penny stock rules. Consequently, these penny stock rules may affect the ability of broker-dealers to trade our securities. We believe that the penny stock rules discourage investor interest in and limit the marketability of our common stock.

NASD sales practice requirements may also limit a stockholder's ability to buy and sell our stock.

In addition to the "penny stock" rules described above, the NASD has adopted rules that require that in recommending an investment to a customer, a broker-dealer must have reasonable grounds for believing that the investment is suitable for that customer. Prior to recommending speculative low priced securities to their non-institutional customers, broker-dealers must make reasonable efforts to obtain information about the customer's financial status, tax status, investment objectives and other information. Under interpretations of these rules, the NASD believes that there is a high probability that speculative low priced securities will not be suitable for at least some customers. The NASD requirements make it more difficult for broker-dealers to recommend that their customers buy our common stock, which may limit your ability to buy and sell our stock and have an adverse effect on the market for our shares.

Stockholders should have no expectation of any dividends.

The holders of our common stock are entitled to receive dividends when, as and if declared by the board of directors out of funds legally available therefore. To date, we have not declared nor paid any cash dividends. The board of directors does not intend to declare any dividends in the foreseeable future, but instead intends to retain all earnings, if any, for use in our business operations.

All of our directors and officers are outside the United States, with the result that it may be difficult for investors to enforce within the United States any judgments obtained against us or any of our directors or officers.

All of our directors and officers are nationals and/or residents of countries other than the United States, and all or a substantial portion of such persons' assets are located outside the United States. As a result, it may be difficult for investors to effect service of process on our directors or officers, or enforce within the United States or Canada any judgments obtained against us or our officers or directors, including judgments predicated upon the civil liability provisions of the securities laws of the United States or any state thereof. Consequently, you may be effectively prevented from pursuing remedies under U.S. federal securities laws against them. In addition, investors may not be able to commence an action in a Canadian court predicated upon the civil liability provisions of the securities laws of the United States.

If we or our independent registered public accountants cannot attest our adequacy in the internal control measures over our financial reporting, as required by Section 404 of the U.S. Sarbanes-Oxley Act, for the fiscal year ending December 31, 2007, we may be adversely affected.

As a public company, we are subject to report our internal control structure and procedures for financial reporting in our annual reports on Form 10-KSB, as a requirement of Section 404 of the U.S. Sarbanes-Oxley Act of 2002 by the U.S. Securities and Exchange Commission (the "SEC"). The report must contain an assessment by management about the effectiveness of our internal controls over financial reporting. Moreover, the independent registered public accountants of our company must attest to and report on management's assessment of the same. Even if our management attests to our internal control measure to be effective, our independent registered public accountants may not satisfy with our internal control structure and procedures. We cannot assure possible outcomes about the conclusion of the report and it could result in an adverse impact on us in the financial marketplace due to the loss of investor confidence in the reliability of our financial statements, which could negatively impact to our stock market price.

Item 3. Controls And Procedures

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, being March 31, 2007, the Company conducted an evaluation, under the supervision and with the participation of its Chief Executive Officer and President and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e)) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Based upon that evaluation, the Chief Executive Officer and President and Chief Financial Officer concluded that as of June 30, 2006 our disclosure controls and procedures were effective in timely alerting them to material information relating to the Company required to be included in our Exchange Act filings. The two Executive Officers responsible for the financial reporting and disclosure are in direct control of the books and records of the Company and are involved first-hand in the decision making process for material transactions.

There were no changes in internal controls over financial reporting that occurred during the quarter ended March 31, 2007, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

The following exhibits are filed herewith:

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

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

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

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

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CHINA NORTH EAST PETROLEUM HOLDINGS LTD.
(Registrant)

Date: May 21, 2007

By: /s/ Zhang Yang
Chief Financial Officer