

CHINA NORTH EAST PETROLEUM HOLDINGS LTD
Form 10-Q
November 16, 2009

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

FORM 10-Q

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

For the quarterly period ended September 30, 2009

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

For the transition period from _____ to _____

Commission file number 000-49846

CHINA NORTH EAST PETROLEUM
HOLDINGS LIMITED

(Exact name of small business issuer as specified in its charter)

Nevada
(State of other
jurisdiction of
incorporation or
organization)

87-0638750
(IRS Employer
identification No.)

445 Park Avenue, New York, New York 10022
(Address of principal executive offices)

(212) 307-3568
(Registrant's telephone number, including area code)

Indicated by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the 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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerate filer, an accelerate filer, a non-accelerated filer, or a smaller reporting company. See the definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

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

Number of shares of common stock outstanding as of November 12, 2009: 25,852,181

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

On one or more occasions, we may make forward-looking statements in this Quarterly Report on Form 10-Q 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,” “projects,” “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; and

 - 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-K, 10-Q 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-Q, our reports on Forms 10-K 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-Q, 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-Q 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-K, 10-Q and 8-K and Proxy Statements on Schedule 14A.

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

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED AND SUBSIDIARIES ("NEP")

Condensed Consolidated Balance Sheets

	September 30, 2009 (Unaudited)	December 31, 2008 (Audited)
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 33,158,348	\$ 13,239,213
Accounts receivable, net	6,509,440	4,230,080
Prepaid expenses and other current assets	3,987,771	781,121
Value added tax recoverable	-	311,240
Total Current Assets	43,655,559	18,561,654
PROPERTY AND EQUIPMENT		
Oil and gas properties, net	65,847,281	70,193,852
Fixed assets, net	13,820,768	1,684,377
Oil and gas properties under construction	-	714,629
Total Property and Equipment	79,668,049	72,592,858
LAND USE RIGHTS, NET	641,204	36,198
GOODWILL	1,645,589	-
DEFERRED FINANCING COSTS, NET	716,680	939,098
TOTAL ASSETS	\$ 126,327,081	\$ 92,129,808
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$ 8,178,864	\$ 10,985,894
Current portion of secured debenture, net of discount	3,971,112	1,489,126
Other payables and accrued liabilities	5,677,494	742,264
Due to related parties	14,625	66,262
Income tax and other taxes payable	5,598,835	3,710,870
Due to a stockholder	5,602,176	738
Total Current Liabilities	29,043,106	16,995,154
LONG-TERM LIABILITIES		
Accounts payable	9,347,865	13,944,903
Secured debenture, net of discount	2,815,879	6,594,700
Deferred tax payable	64,465	762,405
Total Long-term Liabilities	12,228,209	21,302,008
TOTAL LIABILITIES	41,271,315	38,297,162
COMMITMENTS AND CONTINGENCIES	-	-
EQUITY		
NEP Stockholders' Equity		

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Common stock (\$0.001 par value, 150,000,000 shares authorized,
25,119,619 shares issued and outstanding as of
September 30, 2009; 20,784,080 shares issued and
outstanding as of December 31, 2008)

	25,120	20,784
Additional paid-in capital	39,934,062	21,384,816
Deferred stock compensation	(641,250)	(1,248,750)
Retained earnings		
Unappropriated	33,677,718	24,536,079
Appropriated	1,372,999	1,372,999
Accumulated other comprehensive income	3,365,741	3,253,068
Total NEP Stockholders' Equity	77,734,390	49,318,996
Noncontrolling interests	7,321,376	4,513,650
TOTAL EQUITY	85,055,766	53,832,646
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 126,327,081	\$ 92,129,808

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

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED AND SUBSIDIARIES
Condensed Consolidated Statements of Operations and Comprehensive Income

	(Unaudited)		(Unaudited)	
	Three months ended September		Nine months ended September	
	2009	2008	2009	2008
	30	30	30	30
NET SALES	\$ 14,403,921	\$ 19,060,007	\$ 34,654,549	\$ 44,051,519
COST OF SALES				
Production costs	1,103,163	895,155	2,769,762	2,390,432
Depreciation of oil and gas properties	2,824,981	3,774,327	8,283,230	8,155,321
Amortization of land use rights	2,982	2,975	8,943	8,743
Government oil surcharge	1,655,000	4,480,955	2,273,167	9,865,655
Total Cost of Sales	5,586,126	9,153,412	13,335,102	20,420,151
GROSS PROFIT	8,817,795	9,906,595	21,319,447	23,631,368
OPERATING EXPENSES				
Selling, general and administrative expenses	749,204	793,479	1,932,541	1,339,404
Professional fees	98,261	42,850	323,309	140,180
Consulting fees	142,332	91,926	298,627	319,764
Depreciation of fixed assets	69,947	50,445	209,748	160,930
Total Operating Expenses	1,059,744	978,700	2,764,225	1,960,278
INCOME FROM OPERATIONS	7,758,051	8,927,895	18,555,222	21,671,090
OTHER INCOME (EXPENSE)				
Other income	7,134	809	7,134	66,651
Other expense	(20,780)	(2,000)	(22,581)	(107,601)
Interest expense	(236,931)	(296,761)	(777,595)	(721,805)
Amortization of deferred financing cost	(74,139)	(74,140)	(222,418)	(172,992)
Amortization of discount on debenture	(513,415)	(486,803)	(1,515,473)	(1,135,874)
Imputed interest expense	(70,210)	(16,794)	(120,127)	(49,535)
Interest income	25,141	4,238	44,905	34,204
Total Other Expense, net	(883,200)	(871,451)	(2,606,155)	(2,086,952)
NET INCOME BEFORE INCOME TAXES	6,874,851	8,056,444	15,949,067	19,584,138
Income tax expense	(2,186,156)	(2,390,961)	(5,273,823)	(5,695,498)
NET INCOME	4,688,695	5,665,483	10,675,244	13,888,640
Less: net income attributable to noncontrolling interests	(635,986)	(711,301)	(1,533,605)	(1,687,394)
NET INCOME ATTRIBUTABLE TO NEP COMMON STOCKHOLDERS	4,052,709	4,954,182	9,141,639	12,201,246
OTHER COMPREHENSIVE INCOME				
Total other comprehensive income	41,798	152,651	125,193	2,020,632
Less: foreign currency translation gain attributable to noncontrolling interests	(4,180)	(15,265)	(12,520)	(202,063)
Foreign currency translation gain attributable to NEP common stockholders	37,618	137,386	112,673	1,818,569

COMPREHENSIVE INCOME
 ATTRIBUTABLE TO NEP COMMON
 STOCKHOLDERS

	\$	4,090,327	\$	5,091,568	\$	9,254,312	\$	14,019,815
Net income per share								
- basic	\$	0.19	\$	0.25	\$	0.43	\$	0.63
- diluted	\$	0.17	\$	0.24	\$	0.41	\$	0.62
Weighted average number of shares outstanding during the period								
- basic		21,780,364		19,987,123		21,143,560		19,480,284
- diluted		24,025,976		20,676,711		22,266,408		19,642,216

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

CHINA NORTH EAST PETROLEUM HOLDINGS LIMITED AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

For the nine months ended September 30, 2009 and 2008 (Unaudited)

	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$9,141,639	\$12,201,246
Adjusted to reconcile net income to cash provided by operating activities:		
Depreciation of oil and gas properties	8,283,230	8,155,321
Depreciation of fixed assets	209,748	160,930
Amortization of land use rights	8,943	8,743
Amortization of deferred financing costs	222,418	172,992
Amortization of discount on debenture	1,515,473	1,135,874
Amortization of stock option compensation	475,207	163,402
Warrants issued for services	280,737	154,171
Noncontrolling interests	1,533,605	1,687,394
Stocks issued for consulting services	88,000	27,125
Stock-based compensation for employee services	607,500	168,750
Imputed interest expense	120,127	49,535
Gain on disposal of fixed assets	(7,134)	-
Changes in operating assets and liabilities		
(Increase) decrease in:		
Accounts receivable	(2,279,360)	