

WUHAN GENERAL GROUP (CHINA), INC  
Form 10QSB  
November 14, 2007

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

**FORM 10-QSB**

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

For the quarterly period ended September 30, 2007

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 033-25350-FW

**WUHAN GENERAL GROUP (CHINA), INC.**  
(Exact Name of Small Business Issuer as Specified in Its Charter)

Nevada  
(State of other jurisdiction of  
incorporation or organization)

84-1092589  
(I.R.S. Employer  
Identification No.)

Canglongdao Science Park of Wuhan East Lake Hi-Tech Development Zone,  
Wuhan, Hubei 430200, People's Republic of China  
(Address of Principal Executive Offices)

86-138-7113-6999  
(Issuer's Telephone Number, Including Area Code)

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  No

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

State the number of shares outstanding of each of the issuer's classes of common equity as of the latest practicable date: 19,712,446 shares of Common Stock, \$.0001 par value per share, outstanding as of November 14, 2007.

Transitional Small Business Disclosure Format: Yes  No

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## PART I

## FINANCIAL INFORMATION

## Item 1. Financial Statements.

**Wuhan General Group (China), Inc.**  
**Consolidated Balance Sheets**  
**At September 30, 2007, and December 31, 2006**  
**(Stated in US Dollars)**

	Note	September 30, 2007 (unaudited)	December 31, 2006 (audited)
<b>ASSETS</b>			
Cash	2(e)	3,411,690	248,243
Restricted Cash	3	8,808,513	382,530
Notes Receivable	4	987,401	1,535,868
Accounts Receivable	2(f),5	31,412,707	12,488,083
Other Receivable		2,598,356	8,810,699
Inventory	2(g),6	9,254,143	4,544,662
Advances to Suppliers		7,921,193	2,746,325
Advances to Employees	7	291,090	255,836
Prepaid Taxes		47,188	3,889
Real Property Available for Sale		1,097,327	-
Total Current Assets		65,829,608	31,016,135
Property, Plant & Equipment, <i>net</i>	2(h),8	18,927,339	17,252,577
Land Use Rights, <i>net</i>	2(j),10	1,790,580	1,749,740
Construction in Progress	9	9,482,036	35,304
Intangible Assets, <i>net</i>	2(i),11	374,630	364,565
Total Assets		<b>\$ 96,404,193</b>	<b>\$ 50,418,321</b>
<b>LIABILITIES &amp; STOCKHOLDERS' EQUITY</b>			
<b>Liabilities</b>			
Bank Loans & Notes	12	24,828,456	13,545,059
Accounts Payable		7,962,974	8,531,852
Accrued Liabilities	13	1,374,252	354,169
Contract Payable	14	-	1,137,623
Taxes Payable		905,586	1,723,544
Other Payable		2,575,985	4,594,639
Dividend Payable		599,250	-
Customer Deposits		5,053,854	1,587,306
Total Current Liabilities		43,300,357	31,474,192
Total Liabilities		<b>43,300,357</b>	<b>31,474,192</b>



**Wuhan General Group (China), Inc.**  
**Consolidated Balance Sheets**  
**At September 30, 2007, and December 31, 2006**  
**(Stated in US Dollars)**

	Note	September 30, 2007 (unaudited)	December 31, 2006 (audited)
<u>Stockholders' Equity</u>			
Preferred Stock - \$0.0001 Par Value 50,000,000 Shares Authorized; 10,287,554 Shares of Series A Convertible Preferred Stock Issued & Outstanding at September 30, 2007	15	1,029	-
Additional Paid in Capital - Preferred Stock		13,466,990	-
Additional Paid in Capital - Warrants	15	6,572,334	-
Common Stock - \$0.0001 Par Value 100,000,000 Shares Authorized; 19,712,446 Shares Issued & Outstanding at September 30, 2007, December 31, 2006.	15	1,971	1,971
Additional Paid in Capital		12,349,602	12,349,602
Statutory Reserve	2(t),16	622,151	622,151
Retained Earnings		18,161,810	5,200,285
Accumulated Other Comprehensive Income	2(u)	1,927,949	770,120
<b>Total Stockholders' Equity</b>		<b>53,103,836</b>	<b>18,944,129</b>
<b>Total Liabilities &amp; Stockholders' Equity</b>		<b>\$ 96,404,193</b>	<b>\$ 50,418,321</b>

**See Accompanying Notes to the Financial Statements and Accountant's Report.**

**Wuhan General Group (China), Inc.**  
**Statements of Income**  
**For the three and nine months ended September 30, 2007 and 2006**  
**(Stated in US Dollars)**

Note	3 months ended 9/30/2007	3 months ended 9/30/2006	9 months ended 9/30/2007	9 months ended 9/30/2006
<b>Revenue</b>				
Sales	\$ 30,523,074	\$ 5,160,151	\$ 60,342,774	\$ 11,612,051
Cost of Sales	20,039,259	2,835,764	40,511,207	6,558,646
Gross Profit	10,483,815	2,324,387	19,831,567	5,053,405
<b>Operating Expenses</b>				
Selling Expenses	938,534	208,785	1,633,144	609,182
General & Administrative Expenses	1,480,755	443,001	3,299,901	1,184,768
Warranty Expense	2(v),13 91,059		514,520	-
Total Operating Expense	2,510,348	651,786	5,447,565	1,793,950
Operating Income	7,973,466	1,672,601	14,384,001	3,259,455
<b>Other Income (Expenses)</b>				
Other Income	17 -	7,444	-	31,167
Interest Income	94,798	-	108,923	-
Other Expenses	(383)	(1,675)	(1,426)	(2,189)
Interest Expense	(369,187)	(121,001)	(756,695)	(389,029)
Total Other Income (Loss) & Expense	(274,772)	(115,232)	(649,198)	(360,051)
Earnings before Tax	7,698,695	1,557,369	13,734,804	2,899,404
Income Tax	2(s), 18 -	-	-	-
<b>Net Income</b>	<b>\$ 7,698,695</b>	<b>\$ 1,557,369</b>	<b>\$ 13,734,804</b>	<b>\$ 2,899,404</b>
Preferred Dividends Declared	299,625	-	773,279	-
Income Available to Common Shareholders	\$ 7,399,070	\$ 1,557,369	\$ 12,961,525	\$ 2,899,404
<b>Earnings Per Share</b>				
Basic	0.38	0.08	0.66	0.15
Diluted	0.17	0.08	0.35	0.15
<b>Weighted Average Shares Outstanding</b>				
Basic	19,712,446	19,712,446	19,712,446	19,712,446
Diluted	46,200,613	19,712,446	39,122,641	19,712,446

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**See Accompanying Notes to the Financial Statements and Accountant's Report.**

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**Wuhan General Group (China), Inc.**  
**Statements of Stockholders' Equity**  
**For the nine months ended September 30, 2007 and 2006**  
**(Stated in US Dollars)**

	Preferred Stock Shares Outstanding	Preferred Stock Additional Paid in Capital Amount	Warrants Additional Paid in Capital	Common Stock Shares Outstanding	Common Stock Additional Paid in Capital Amount	Statutory Reserve	Retained Earnings	Accumul Other Comprehe Income	
Balance, January 1, 2006				19,712,446	1,971	6,033,911	-	2,620,167	282,7
Increases to Additional Paid-In Capital from Contribution of Capital Equipment					6,315,691				
Net Income							3,202,269		
Appropriations of Retained Earnings						622,151	(622,151)		
Foreign Currency Translation Adjustment									487,3
Balance, December 31, 2006				19,712,446	1,971	12,349,602	622,151	5,200,285	770,
Balance, January 1, 2007				19,712,446	1,971	12,349,602	622,151	5,200,285	770,
Issuance of Common Stock for Cash									
Issuance of Preferred Stock for Cash	10,287,554	1,029							
Increase in Additional Paid in Capital from Issuance of Preferred Stock		13,466,990							
Increase in Additional Paid in Capital			6,572,334						



from Issuance  
of Warrants

Net Income 13,734,804

Preferred  
Dividends

Declared (773,279)

Foreign  
Currency  
Translation  
Adjustment

1,157,8

Balance,  
September 30,

2007 10,287,554 1,029 13,466,990 6,572,334 19,712,446 1,971 12,349,602 622,151 18,161,808 1,927,9

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**Wuhan General Group (China), Inc.**  
**Statements of Stockholders' Equity**  
**For the nine months ended September 30, 2007 and 2006**  
**(Stated in US Dollars)**

	9/30/2007	2006	2005	2004	Total
Comprehensive Income					
Net Income	13,734,804	3,202,269	2,371,760	248,406	19,557,239
Other Comprehensive Income					
Foreign Currency Translation Adjustment	1,157,828	487,384	206,058	76,678	1,927,948
<b>Total Comprehensive Income</b>	<b>\$ 14,892,632</b>	<b>\$ 3,689,653</b>	<b>\$ 2,577,818</b>	<b>\$ 325,084</b>	<b>\$ 21,485,187</b>

**See Accompanying Notes to the Financial Statements and Accountant's Report.**

**Wuhan General Group (China), Inc.**  
**Statements of Cash Flows**  
**For the three months and nine months ended September 30, 2007 and 2006**  
**(Stated in US Dollars)**

	<b>3 months ended 9/30/2007</b>	<b>3 months ended 9/30/2006</b>	<b>9 months ended 9/30/2007</b>	<b>9 months ended 9/30/2006</b>
<b>Cash Flow from Operating Activities</b>				
Cash Received from Customers	\$ 29,180,726	2,021,163	\$ 51,098,507	5,024,072
Cash Paid to Suppliers & Employees	(25,225,990)	1,469,643	(57,904,148)	64,493
Interest Received	94,798	-	108,923	-
Interest Paid	(369,187)	(121,001)	(756,695)	(389,029)
Income Tax Paid	-	-	-	-
Miscellaneous Receipts	-	7,444	-	31,167
Cash Sourced/(Used) in Operating Activities	3,680,348	3,377,249	(7,453,412)	4,730,703
<b>Cash Flows from Investing Activities</b>				
Cash Invested in Restricted Time Deposits	794,351	(745,009)	(8,425,983)	(100,078)
Repayment/(Investment) in Notes	(225,257)	(474,397)	546,999	(758,043)
Payments for Purchases & Construction of Plant & Equipment	(3,162,369)	(40,867)	(12,595,728)	(858,636)
Payments for Purchases of Land Use Rights	(27,146)	-	(74,072)	-
Payments for Purchases of Intangible Assets	(33,850)	(9)	(44,581)	(1,871)
Cash Used/(Sourced) in Investing Activities	(2,654,271)	(1,260,282)	(21,690,692)	(1,718,628)
<b>Cash Flows from Financing Activities</b>				
Proceeds from Issuance of Preferred Stock	(726,086)	-	20,040,353	-
Proceeds from/(Repayment of) Bank Borrowings	(324,860)	(1,767,618)	2,866,342	(2,388,287)
Proceeds from Issuance of Notes	1,921,653	80,687	8,417,055	-
Dividends Paid	-	-	(174,029)	-
Cash Sourced/(Used) in Financing Activities	870,707	(1,686,931)	31,149,722	(2,388,287)
<b>Net Increase/(Decrease) in Cash &amp; Cash Equivalents for the Period</b>	<b>108,833</b>	<b>430,036</b>	<b>2,005,617</b>	<b>623,788</b>
<b>Effect of Currency Translation</b>	<b>566,953</b>	<b>10,003</b>	<b>1,157,831</b>	<b>11,291</b>
<b>Cash &amp; Cash Equivalents at Beginning of Period</b>	<b>248,243</b>	<b>361,528</b>	<b>248,243</b>	<b>166,488</b>
	<b>\$ 924,029</b>	<b>\$ 801,567</b>	<b>\$ 3,411,691</b>	<b>\$ 801,567</b>

**Cash & Cash Equivalents at End of Period**

**Non-Cash Investing Activity:**

Contribution of equipment to capital	-	6,272,028	-	6,272,028
Value of residential property surrendered by Hubei Dilong Industrial Group Co., Ltd.	989,168	-	989,168	-

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**Wuhan General Group (China), Inc.**  
**Reconciliation of Net Income to Cash Flow Sourced/(Used) in Operating Activities**  
**For the three months and nine months ended September 30, 2007 and 2006**  
**(Stated in US Dollars)**

	3 months ended 9/30/2007	3 months ended 9/30/2006	9 months Ended 9/30/2007	9 months ended 9/30/2006
Net Income	7,698,695	1,557,369	13,734,804	2,899,404
<i>Adjustments to Reconcile Net Income to Net Cash Provided by Cash Activities:</i>				
Amortization	26,000	18,010	67,748	53,527
Depreciation	(430,594)	379,043	336,611	748,054
Provision for Bad Debt on Note Receivable	537	-	1,467	-
Decrease/(Increase) in Accounts Receivable	(8,260,400)	(11,538,994)	(18,924,625)	(7,815,346)
Decrease/(Increase) in Other Receivable	6,456,082	(315,430)	6,212,343	(352,153)
Decrease/(Increase) in Inventory	(300,822)	(651,645)	(4,709,482)	(444,465)
Decrease/(Increase) in Advances to Suppliers	(45,259)	(1,566,449)	(5,174,868)	(77,631)
Decrease/(Increase) in Advances to Employees	(28,788)	12,736	(35,254)	12,736
Decrease/(Increase) in Prepaid Local & VAT Taxes	(15,379)	(296,385)	(43,299)	(296,385)
Increase/(Decrease) in Accounts Payable	(3,279,865)	3,947,356	(568,878)	4,383,607
Increase/(Decrease) in Taxes Payable	(356,450)	449,874	(817,959)	801,996
Increase/(Decrease) in Other Payable	1,258,971	2,587,972	(2,018,652)	3,159,480
Increase/(Decrease) in Accrued Liabilities	496,186	78,359	1,020,083	78,359
Increase/(Decrease) in Customer Deposits	461,433	8,715,433	3,466,548	1,579,520
Total of all adjustments	(4,018,347)	1,819,880	(21,188,216)	1,831,299
<b>Net Cash Provided by Operating Activities</b>	<b>\$ 3,680,348</b>	<b>\$ 3,377,249</b>	<b>\$ (7,453,412)</b>	<b>\$ 4,730,703</b>

**See Accompanying Notes to the Financial Statements and Accountant's Report.**

**Wuhan General Group (China) Inc.**  
**Notes to Financial Statements**  
**(Stated in US Dollars)**

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES**

Wuhan General Group (China), Inc. (the “Company”) is a holding company whose primary business operations are conducted through its operating subsidiaries Wuhan Blower Co., Ltd. (“Wuhan Blower”) and Wuhan Generating Equipment Co., Ltd. (“Wuhan Generating Equipment”). Wuhan Blower is a China-based manufacturer of industrial blowers that principally are components of steam driven electrical power generation plants. Wuhan Generating Equipment is a China-based manufacturer of industrial steam and water turbines, also principally for use in electrical power generation plants.

The Company was formed under the laws of the State of Colorado on July 19, 1988 as Riverside Capital, Inc. On March 18, 1992, the Company changed its name to United National Film Corporation. In June 2001, the Company suspended all business activities and became a “shell company.”

In 2006, the Company effectively dissolved or abandoned all subsidiaries, which may or may not have been active in periods prior to June 2001. On October 20, 2006, the Company changed its state of incorporation from Colorado to Nevada by means of a merger with and into a Nevada corporation formed on September 12, 2006 solely for the purpose of effecting the reincorporation.

On February 7, 2007, the Company entered into a share exchange agreement with Fame Good International Limited (“Fame”) and Universe Faith Group Limited (“UFG”). Prior to the share exchange, Fame was the sole stockholder of UFG, which is the parent company of Wuhan Blower and Wuhan Generating Equipment. Pursuant to the share exchange, UFG became a wholly owned subsidiary of the Company and Fame became the Company’s controlling stockholder. On March 13, 2007, the Company changed its name from United National Film Corporation to Wuhan General Group (China), Inc.

The share exchange transaction has been accounted for as a recapitalization of UFG where the Company (the legal acquirer) is considered the accounting acquiree and UFG (the legal acquiree) is considered the accounting acquirer. As a result of this transaction, the Company is deemed to be a continuation of the business of UFG.

Accordingly, the financial data included in the accompanying consolidated financial statements for all periods prior to February 7, 2007 is that of the accounting acquirer (UFG). The historical stockholders’ equity of the accounting acquirer prior to the share exchange has been retroactively restated as if the share exchange transaction occurred as of the beginning of the first period presented. See also Note 15 - Capitalization.

**Wuhan General Group (China) Inc.**  
**Notes to Financial Statements**  
**(Stated in US Dollars)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*(a) Method of Accounting*

The Company maintains its general ledger and journals with the accrual method of 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, which are compiled on the accrual basis of accounting.

*(b) Consolidation*

The interim consolidated financial statements include the accounts of the Company and its subsidiaries, UFG, Wuhan Blower, and Wuhan Generating Equipment. Inter-company transactions, such as sales, cost of sales, due to/due from balances, investment in subsidiaries, and subsidiaries' capitalization have been eliminated.

*(c) Economic and Political Risks*

The Company's operations are conducted in the People's Republic of China (the "PRC"). Accordingly, the Company's business, financial condition and results of operations may be influenced by the political, economic and legal environment in the PRC, and by the general state of the PRC economy.

*(d) Use of Estimates*

In preparing the financial statements in conformity with accounting principles generally accepted in the United States of America, management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the dates of the financial statements, as well as the reported amounts of revenues and expenses during the reporting years. These estimates and assumptions include, but are not limited to, the valuation of accounts receivable, inventories, deferred income taxes and the estimation of useful lives of property, plant, and equipment. Actual results could differ from these estimates.

*(e) Cash and Cash Equivalents*

The Company considers all cash and other highly liquid investments with initial maturities of three months or less to be cash equivalents. The company maintains bank accounts in the People's Republic of China, and an escrow account in the United States of America.

*(f) Accounts Receivable-Trade*

Trade receivables are recognized and carried at the original invoice amount less allowance for any uncollectible amounts. An allowance for doubtful accounts is made when collection of the full amount is no longer probable. Bad debts are written-off as incurred.

**Wuhan General Group (China) Inc.**  
**Notes to Financial Statements**  
**(Stated in US Dollars)**

*(g) Inventory*

Inventory, consisting of raw materials, work in progress, and finished products, is stated at the lower of cost or market value. Finished products are comprised of direct materials, direct labor and an appropriate proportion of overhead.

*(h) Property, Plant, and Equipment*

Property, plant and equipment are carried at cost less accumulated depreciation. Depreciation is provided over their estimated useful lives, using the straight-line method with 5% salvage value. Estimated useful lives of the property, plant and equipment are as follows:

Buildings	30 years
Machinery and Equipment	10 years
Furniture and Fixtures	5 years
Motor Vehicles	5 years

*(i) Intangible Assets*

Intangible assets are stated at cost less accumulated amortization. Amortization is provided over the respective useful lives, using the straight-line method. Estimated useful lives of intangibles are as follows:

Technical License	10 years
Trademark	20 years

*(j) Land Use Rights*

The Company carries land use rights at cost less accumulated amortization. Land use rights are amortized straight-line over its useful life of 50 years.

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

The Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"), which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company periodically evaluates the carrying value of long-lived assets to be held and used in accordance with SFAS 144. SFAS 144 requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amounts. In that event, a loss is recognized based on the amount by which the carrying amount exceeds the fair market value of the long-lived assets. Loss on long-lived assets to be disposed of is determined in a similar manner, except that fair market values are reduced for the cost of disposal. Based on its review, the Company believes that, as of September 30, 2007, and 2006, there were no significant impairments of its long-lived assets.

*(l) Revenue Recognition*

Revenue from the sale of blower products and generating equipment is recognized at the time of the transfer of risks and rewards of ownership, which generally occurs when the goods are delivered to customers and the title passes.





**Wuhan General Group (China) Inc.**  
**Notes to Financial Statements**  
**(Stated in US Dollars)**

*(m) Cost of Sales*

The Company's cost of sales is comprised of raw materials, factory worker salaries and related benefits, machinery supplies, maintenance supplies, depreciation, utilities, inbound freight, purchasing and receiving costs, inspection and warehousing costs.

*(n) Selling Expenses*

Selling expenses are comprised of outbound freight, salary for the sales force, client entertainment, commissions, depreciation, advertising, and travel and lodging expenses.

*(o) General & Administrative Expenses*

General and administrative costs include outside consulting services, research & development, executive compensation, quality control, and general overhead such as the finance department, administrative staff, and depreciation and amortization expense.

*(p) Advertising*

The Company expenses all advertising costs as incurred. For the nine months ended September 30, 2007, the total advertising expense was \$30,596.

*(q) Research and Development*

The Company expenses all research and development costs as incurred. For the nine months ended September 30, 2007, the total research and development cost was \$103,975.

*(r) Foreign Currency Translation*

The Company maintains its financial statements in the functional currency. The functional currency of the Company is the Renminbi (RMB). Monetary assets and liabilities denominated in currencies other than the functional currency are translated into the functional currency at rates of exchange prevailing at the balance sheet dates. Transactions denominated in currencies other than the functional currency are translated into the functional currency at the exchanges rates prevailing at the dates of the transaction. Exchange gains or losses arising from foreign currency transactions are included in the determination of net income for the respective periods.

For financial reporting purposes, the financial statements of the Company, which are prepared using the functional currency, have been translated into United States dollars. Assets and liabilities are translated at the exchange rates at the balance sheet dates and revenue and expenses are translated at the average exchange rates and stockholders' equity is translated at historical exchange rates. Translation adjustments are not included in determining net income but are included in foreign exchange adjustment to other comprehensive income, a component of stockholders' equity.

<b>Exchange Rates</b>	<b>September 30, 2007</b>	<b>December 31, 2006</b>	<b>September 30, 2006</b>
Period end RMB : US\$ exchange rate	7.5176	7.8175	7.9168
Average 9 & 12 month RMB : US\$ exchange rate	7.67576	7.98189	7.97711



**Wuhan General Group (China) Inc.**  
**Notes to Financial Statements**  
**(Stated in US Dollars)**

RMB is not freely convertible into foreign currency and all foreign exchange transactions must take place through authorized institutions. No representation is made that the RMB amounts could have been, or could be, converted into US\$ at the rates used in translation.

*(s) 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. 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.

All of the Company's operations are in the PRC, and in accordance with the relevant tax laws and regulations of PRC, the corporation income tax rate is 33%. However, the Company was approved as a highly advanced technology foreign investment enterprise in November 2005, and in accordance with the relevant regulations regarding the favorable tax treatment for high technology companies, the Company is entitled to a two year tax exemption. Following the expiration of this tax exemption, the Company will be required to pay a 7.5% tax rate for the next three years. Beginning November 2010, the Company will be allowed a 15% tax rate as long as the Company is located and registered in the high and advanced technology development zone.

The Company's foreign subsidiaries are subject to U.S. income tax liability; however, the tax is deferred until foreign source income is repatriated to the Company.

The Company is subject to United States income tax according to Internal Revenue Code Sections 951 and 957. Corporate income tax is imposed on graduated rates based on the ranges shown in the following table: -

**Taxable Income**

<i>Rate</i>	<i>Over</i>	<i>But not over</i>	<i>Of Amount Over</i>
15%	0	50,000	0
25%	50,000	75,000	50,000
34%	75,000	100,000	75,000
39%	100,000	335,000	100,000
34%	335,000	10,000,000	335,000
35%	10,000,000	15,000,000	10,000,000
38%	15,000,000	18,333,333	15,000,000
35%	18,333,333	-	0

*(t) Statutory Reserve*

In accordance with PRC laws, statutory reserve refers to the appropriation from net income, to the account "statutory reserve" to be used for future company development, recovery of losses, and increase of capital, as approved, to expand production or operations. PRC laws prescribe that an enterprise operating at a profit, must appropriate, on an annual basis, an amount equal to 10% of its profit. Such an appropriation is necessary until the reserve reaches a maximum that is equal to 50% of the enterprise's PRC registered capital.



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*(u) Other 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. The Company's current component of other comprehensive income is the foreign currency translation adjustment.

*(v) Warranty Policy*

The estimation of warranty obligations is determined in the same period that revenue from the sale of the related products is recognized. The warranty obligation is based on historical experience and reflects management's best estimate of expected costs at the time products are sold. Warranty accruals are adjusted for known or anticipated warranty claims as new information becomes available. Future events and circumstances could materially change our estimates and require adjustments to the warranty obligation. New product launches require a greater use of judgment in developing estimates until historical experience becomes available.

*(w) Earnings Per Share*

Basic earnings per share is computed on the basis of the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is computed on the basis of the weighted average number of shares of common stock plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method for warrants and the as-if method for convertible securities. Dilutive potential common shares include outstanding warrants, and convertible preferred stock.

*(x) Recent Accounting Pronouncements*

In February 2006, the FASB issued SFAS 155, "Accounting for Certain Hybrid Financial Instruments" to amend FASB Statements No. 133, "Accounting for Derivative Instruments and Hedging Activities," and No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". This statement permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation and eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. This statement is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006.

In July 2006, the FASB issued FIN 48, Accounting for Uncertainty in Income Taxes—an Interpretation of FASB Statement No. 109, which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that the Company recognize in its consolidated financial statements the impact of a tax position if that position is more likely than not to be sustained upon an audit, based on the technical merits of the position. The provisions of FIN 48 are effective for the Company on January 1, 2007, with the cumulative effect of the change in accounting principle, if any, recorded as an adjustment to opening retained earnings.

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In September 2006, the FASB issued SFAS 157, “Fair Value Measurements”, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 applies under other accounting pronouncements that require or permit fair value measurements, where fair value is the relevant measurement attribute. The standard does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years.

In September 2006, the SEC issued SAB No. 108, which provides guidance on the process of quantifying financial statement misstatements. In SAB No. 108, the SEC staff establishes an approach that requires quantification of financial statement errors, under both the iron-curtain and the roll-over methods, based on the effects of the error on each of the Company’s financial statements and the related financial statement disclosures. SAB No.108 is generally effective for annual financial statements in the first fiscal year ending after November 15, 2006. The transition provisions of SAB No. 108 permits existing public companies to record the cumulative effect in the first year ending after November 15, 2006 by recording correcting adjustments to the carrying values of assets and liabilities as of the beginning of that year with the offsetting adjustment recorded to the opening balance of retained earnings.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities—Including an Amendment of SFAS 115” (SFAS No. 159), which allows for the option to measure financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. The objective of SFAS 159 is to provide opportunities to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply hedge accounting provisions. SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of SFAS No. 159 on our consolidated financial statements.

The Company does not anticipate that the adoption of the above standards will have a material impact on these consolidated financial statements.

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**3. RESTRICTED CASH**

Restricted Cash represents cash placed with banks to secure banking facilities, which are comprised of loans and notes payables in addition to other collateral.

An escrow account held in the United States is also included as a part of restricted cash. The funds in the escrow account were designated for the payment of fees or expenses in connection with investor or public relations or securities law compliance, including related legal fees.

**4. NOTES RECEIVABLE**

	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Notes Receivable	\$ 1,025,645	\$ 1,572,644
<i>Less:</i> Allowance for Bad Debts	38,244	36,776
	\$ 987,401	\$ 1,535,868

The Company entered into a financing agreement with Hubei Dilong Industrial Group Co., Ltd. (“Hubei”) on December 31, 2004. Under such agreement, the Company provided to Hubei an unsecured loan of \$2,413,564 (RMB 20,000,000) for a two-year term from January 1, 2005 to December 31, 2006 at 0.5115% per month. After servicing the debt for two years, the Company determined that Hubei was in default because no further debt service had been made by Hubei, and as such the Company accrued provision for bad debts on the outstanding balance of the Note of \$1,485,615 (RMB 11,500,000). Additionally, Hubei surrendered real property to the Company to partially settle its outstanding debt. The property was valued at approximately \$989,167 (RMB 7,542,202); accordingly the outstanding balance of principal was \$526,471 (RMB 3,957,798). The Company also accrued interest receivable of \$138,530 (RMB 1,041,414) to Hubei’s outstanding balance. The Company also had \$159,982 (RMB 1,202,677) of tender deposits carried in the Other Receivables line item on the balance sheet with Hubei. The Company has reclassified that balance from Other Receivables into Hubei outstanding Notes Receivable’s balance. As of September 30 2007, the total outstanding balance for Notes Receivables from Hubei was \$824,983 (RMB 6,201,889). The entire outstanding balance of Notes Receivable had been re-formalized by a new repayment contract entered into by the Company and Hubei on May 24, 2007.

The remaining balance carried in the Notes Receivable account is \$200,662 (RMB 1,508,500). This balance is composed of bank drafts drawn by the Company’s customers against the customer’s margin deposits with their banks. These bank drafts are liquid instruments that can be either (a) endorsed to the Company vendors, or (b) discounted to the Company’s own bank. The Company chooses to carry these instruments as notes receivable instead of cash primarily because of the associated time element of these notes, as they are normally due at a later point in time; therefore, these bank drafts represent slightly different risk and reward characteristics.



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**5. ACCOUNTS RECEIVABLE**

	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Total Accounts Receivable-Trade	\$ 32,062,803	\$ 12,807,824
<u>Less: Allowance for Bad Debt</u>	650,096	319,741
	<b>\$ 31,412,707</b>	<b>\$ 12,488,083</b>

**Allowance for Bad Debts**

Beginning Balance	319,741	13,528
Allowance Provided	330,355	306,213
Charged Against Allowance	-	-
Ending Balance	650,096	319,741

**6. INVENTORY**

	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Raw Materials	\$ 2,089,577	\$ 1,116,066
Work in Progress	3,720,085	2,058,889
Finished Goods	3,444,481	1,369,707
	<b>\$ 9,254,143</b>	<b>\$ 4,544,662</b>

**7. ADVANCES TO EMPLOYEES**

Advances to Employees of \$291,090, and \$255,836 as of September 30, 2007 and December 31, 2006, respectively, consisted of advances to salespeople for salary, travel, and expenses over extended periods as they work to procure new sales contracts or install and perform on existing contracts. These advances are deducted from future sales commissions earned by these salespeople. In the event that a salesperson leaves the Company prior to earning sales commission sufficient to offset advances paid to the salesperson, the Company immediately expenses any outstanding balance to the income statement. None of the employees who have received these advances is a director or executive officer of the Company.

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**8. PROPERTY, PLANT AND EQUIPMENT**

Property, plant, and equipment, which is stated at cost less depreciation, was composed of the following as of September 30:

<u>Category of Asset</u>	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Buildings	\$ 9,966,010	\$ 9,597,812
Machinery & Equipment	9,961,669	8,353,453
Furniture & Fixtures	269,032	259,092
Auto	677,175	652,156
	<b>20,873,886</b>	<b>18,862,513</b>
<u>Less: Accumulated Depreciation</u>	1,946,547	1,609,936
	<b>\$ 18,927,339</b>	<b>\$ 17,252,577</b>

The Company's real property consisted of approximately 440,000 square feet (44,233.40 square meters) of building floor space.

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**9. CONSTRUCTION IN PROGRESS**

The Company is in the process of developing a new 1,170,000 square feet turbine manufacturing facility within its factory campus.

Construction in progress represents the direct costs of design, acquisition, construction of buildings, building improvements, and land improvement. These costs are capitalized in the Construction-in-Progress account until substantially all activities necessary to prepare the assets for their intended use are completed. At such point, the Construction-in-Progress account is closed and the capitalized costs are transferred to their appropriate asset classification. No depreciation is provided until it is completed and ready for the intended use.

As of the date of the balance sheet, Construction in Progress of \$9,482,036 represented construction costs of the project facility paid to the project's contractor, Hubei Gongchuang Real Estate Co., Ltd. and included the following major contract jobs:

<i>Contract Date</i>	<i>Contract Description</i>	<i>Contract Amount</i>	<i>Amount Percentage</i>		<i>Measurement Date</i>	<i>Amount Paid</i>	<i>Balance Due</i>
			<i>Recognized as Completed</i>	<i>Recognized as Completed</i>			
3/27/2007	Materials for Manufacturing Workshop	\$ 3,325,529	\$ 2,826,700	85%	Mar-07	\$ 1,729,275	\$ 1,097,425
6/26/2006	Workshop Construction	5,320,847	4,522,720	85%	May-07	3,990,635	532,085
6/26/2006	Office Building Construction	3,990,635	3,192,508	80%	Jul-07	3,010,003	182,505
		\$ 12,637,012	\$ 10,541,928			\$ 8,729,914	\$ 1,812,014

**10. LAND USE RIGHTS**

<u>Category of Asset</u>	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Land Use Rights	\$ 1,930,829	\$ 1,856,757
<u>Less:</u> Accumulated Amortization	140,249	107,017
	\$ 1,790,580	\$ 1,749,740

The Company acquired through Wuhan Hi-Tech Blower Manufacturing Co. Ltd. (WBM) the Land Use Rights for three parcels of land totaling 1,170,000 square feet for a term of 50 years from March 1, 2004 to March 1, 2054 for \$1,856,757 (RMB 14,515,200). The land has been used for the Company's facilities including the blower manufacturing facilities, turbine manufacturing facility, warehouses, testing facilities, dormitories, and administrative buildings.

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**11. INTANGIBLE ASSETS**

The following categories of assets are stated at cost less amortization.

<u>Category of Asset</u>	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Trademarks	\$ 133,021	\$ 127,918
Mitsubishi License	306,331	280,571
Tianyu CAD License	4,057	3,901
Sunway CAD License	13,075	-
Microsoft License	12,704	12,217
	469,188	424,607
<u>Less: Accumulated Amortization</u>	94,560	60,042
<b>Net</b>	<b>\$ 374,628</b>	<b>\$ 364,565</b>

The weighted average amortization period for the Company's intangible assets in total is 12.93 years.

The weighted average amortization period for the Trademark is 20 years.

The weighted average amortization period for the Mitsubishi, CAD, and Microsoft technical licenses is 10 years.

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**12. BANK LOANS AND NOTES**

The following table provides the name of the lender, due date, interest rate, and amounts outstanding at September 30, 2007, and December 31, 2006, for the Company's bank loans and notes payable.

Name of Note Holder	Due Date	Interest Rate Per Annum	9/30/2007	12/31/2006
Bank of Communication	On Demand	6.62%	\$ -	\$ 4,732,971
Bank of Communication	On Demand	6.62%	-	1,343,140
Shanghai Pudong Development Bank	10/19/2007	6.03%	2,128,339	2,046,690
Shanghai Pudong Development Bank	5/22/2008	6.57%	1,330,212	-
Shanghai Pudong Development Bank	6/25/2008	6.57%	532,085	-
Citic Industrial Bank	10/12/2007	6.73%	-	2,430,445
Citic Industrial Bank	9/25/2008	7.29%	3,325,529	-
Citic Industrial Bank	9/25/2008	7.29%	16,541	-
Citic Industrial Bank	2/28/2008	6.70%	-	49,697
Agricultural Bank of China	10/31/2007	6.73%	1,330,212	1,279,181
Agricultural Bank of China	10/30/2007	6.73%	1,330,212	1,279,181
Wuhan East Lake Development District Zheng Bridge Committee	On Demand	6.00%	399,064	383,754
Bank of China	On Demand	6.83%	698,361	-
Dalian Chong Si Hydraulic Coupler Complete Sets of Equipment Ltd. (Note Payable)	On Demand	0.00%	133,021	-
Hubei Committees Properties Co., Ltd. (Note Payable)	On Demand	0.00%	6,358,412	-
Wuhan-heavy George Special Steel Co., Ltd. (Note Payable)	On Demand	0.00%	215,926	-
Wuhan Jiabao Supplies Co., Ltd. (Note Payable)	On Demand	0.00%	104,465	-
Wuhan Jiangnan District Zhongnan Supplies Station (Note Payable)	On Demand	0.00%	156,911	-
Citic Industrial Bank Wuhan Zhu Ye Shan Branch	2/17/2008	6.73%	2,660,424	-
Citic Industrial Bank Wuhan Zhu Ye Shan Branch	2/17/2008	6.73%	2,660,424	-
59 Various Other Notes	Various Dates	Various Rates	1,448,320	-
			\$ 24,828,456	\$ 13,545,059

Banking facilities extended by the Bank of Communication, CITIC Industrial Bank, Shanghai Pudong Development Bank and Agricultural Bank of China were secured by the Company's mortgage of real property and margin deposits as disclosed in Restricted Cash on the Balance Sheet.

Motor vehicle loans extended by CITIC Industrial Bank were secured by the motor vehicles.

Note payable extended by Wuhan East Lake Development District Zheng Bridge Committee unsecured and is payable on demand.

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Certain notes payable, as indicated above, do not have a stated rate of interest. These notes are payable on demand to the Company's creditors. The creditors have given extended credit terms secured by pledge of the Company's restricted cash.

### 13. WARRANTY LIABILITY

Warranty liability is accrued and carried on the balance sheet under Accrued Liabilities. The Company makes its warranty accrual based on individual assessment of each contract because terms and conditions vary. The Company's typical sales contracts provide for a warranty period of 12-18 months following product installation.

The following table summarizes the activity related to the Company's product warranty liability for the nine months ended September 30, 2007 and 2006.

	<b>Nine Months Ended September 30, 2007</b>	<b>Nine Months Ended September 30, 2006</b>
Balance at beginning of period	\$ 249,234	-
<i>Add:</i> Accruals for current & pre-existing warranties issued during period	514,520	-
<i>Less:</i> Settlements made during period	-	-
Balance at end of period	\$ 763,754	\$ -

### 14. CONTRACT PAYABLE

Contract Payable represents accounts payable to contractors and suppliers in connection with the construction of the Company's new turbine manufacturing facilities.

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**15. CAPITALIZATION**

The Company originally had common stock capitalization of \$ 12,349,602 as of December 31, 2006.

On February 7, 2007, the Company entered into a share exchange agreement with Fame Good International Limited (“Fame”) and Universe Faith Group Limited (“UFG”), which is the sole stockholder of Wuhan Blower Co. Ltd. Pursuant to the share exchange agreement, the Company issued 17,912,446 shares of common stock to Fame in exchange for all of the issued and outstanding capital stock of UFG.

As a result of the share exchange transaction, the Company retroactively restated its capitalization to reflect the effect of the share exchange.

On February 7, 2007, the Company entered into a Series A Convertible Preferred Stock Purchase Agreement with nine institutional investors pursuant to which the Company issued to the investors an aggregate of 10,287,554 shares of Series A Convertible Preferred Stock at \$2.33 per share for gross proceeds of \$23,970,000. The Preferred Stock is convertible into shares of the Company’s common stock on a one-for-one basis. Holders of Preferred Stock are entitled to a dividend equal to 5% per annum of the amount invested, subject to adjustment. These dividends are payable quarterly. As of September 30, 2007, none of the Preferred Stock had been converted into common stock.

The net proceeds of \$20,040,353 from the sale of Preferred Stock were accounted for as follows: -

i. Preferred Stock at \$0.0001 par value 10,287,554 shares issued and outstanding	\$ 1,029
ii. Additional Paid-in Capital attributable to Preferred Stock	13,466,990
iii. Additional Paid-in Capital attributable to Series A Warrants, Series J Warrants, and Series B Warrants	6,572,334
	\$ 20,040,353

As an inducement to purchase the Preferred Stock, the Company, pursuant to the Stock Purchase Agreement, agreed to issue the following warrants:

- Series A Warrants to each of the preferred stock investors to purchase shares of common stock equal to 60% of the number of shares of preferred stock purchased, (i.e., 6,172,531 shares) at an exercise price of \$2.57 per share expiring five years from the closing date.
- Series J Warrants to each of the preferred stock investors who invested at least \$2,000,000 to purchase shares of common stock equal to 100% of the number of shares of preferred stock purchased, (i.e., 9,358,370 shares) at an exercise price of \$2.33 per share for a term of 21 months from the closing date.
- Series B Warrants to each recipient of Series J Warrants to purchase shares of common stock equal to 60% of the number of shares of common stock purchased pursuant to Series J Warrants, (i.e. 5,615,021 shares) at an exercise price of \$2.57 per share for a term of five years from the closing date.

The total of the above Series A, J, and B Warrants amount to 21,145,922 shares of common stock underlying warrants.





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In consideration of services provided by 1<sup>st</sup> BridgeHouse Securities, LLC in connection with the private placement of preferred stock and warrants, the Company issued to 1<sup>st</sup> BridgeHouse the following placement agent warrants for a term of ten years from the date of issuance:

Series of Warrant	Number of Shares	Exercise Price
Series C	1,028,755	\$ 2.57
Series AA	617,253	2.83
Series BB	561,502	2.83
Series JJ	935,837	2.57
	3,143,347	

The aggregate number of shares of common stock issuable to the preferred stock purchasers and placement agent pursuant to all series of warrants is 24,289,269. As of September 30, 2007, none of these warrants had been exercised.

In conjunction with the possible preferred stock conversion and warrant exercises, the Company has reserved a number of shares of common stock equal to 150% of the number of shares of common stock necessary to effect the conversion of all of the preferred stock and exercise of all the warrants outstanding.

The value of the net proceeds raised in the private placement transaction on February 7, 2007 was ratably allocated to the preferred stock and warrants according to the following methodology. The Company priced the series A, J, and C warrants using a valuation model provided by the placement agent, which took into consideration time value, volatility, market liquidity, and an assumed risk-free rate. The Company then multiplied the per share valuation of the warrants by their total respective underlying shares to arrive at a total valuation for the warrants. The Company multiplied the total number of preferred stock in the offering by the per share sales price of \$2.33 to arrive at total valuation for the preferred stock. The Company then calculated total valuation of both securities by adding together their individual valuations. Upon determining the total valuation of both securities, the Company interpolated each individual securities pro-rata contribution of value to the entire securities offering as a whole. Using the interpolated pro-rata, the Company applied such percentages to the actual net proceeds raised in the offering to determine the entries to be recorded in the Company's general ledger.

The preferred stock is convertible into an aggregate of 10,287,554 shares of common stock.

The following table provides the total number of shares of fully diluted common stock.

	<b>Number of Shares</b>
Common Stock Outstanding	19,712,446
Common Stock Issuable upon-:	
- Conversion of Preferred Stock	10,287,554
- Exercise of Warrants	24,289,269
<b>Total Amount of Fully Diluted Common Stock</b>	<b>54,289,269</b>

In the event of a voluntary or involuntary liquidation, holders of preferred stock are entitled to a liquidation preference of \$2.33 per share. This amount is in excess of the stock's par value of \$0.0001. The convertible preferred stock is

cumulative, non-participating, and non-redeemable, and as such, there is no related sinking fund. The preferred stock contains a mandatory conversion to common stock within two years of the effective date of the registration statement related to such preferred stock if the Company's common stock at expiration is above the closing price of \$5.00.

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**16. COMMITMENTS OF STATUTORY RESERVE**

In compliance with PRC laws, the Company is required to appropriate 10% of its net income to its statutory reserve up to a maximum of 50% of an enterprise's registered paid in capital. The Company had future unfunded commitments, as provided below:

	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Common Stock Capital	\$ 12,351,573	\$ 12,351,573
50% maximum thereof	\$ 6,175,786	\$ 6,175,786
<u>Less: Amounts Appropriated to Statutory Reserve</u>	<u>622,151</u>	<u>622,151</u>
Unfunded Commitment	\$ 5,553,635	\$ 5,553,635

**17. OTHER INCOME**

	<b>Nine months ended September 30, 2007</b>	<b>Nine months ended September 30, 2006</b>
Tax Refund	\$ -	\$ -
Sundry Income	-	31,167
	\$ -	\$ 31,167

**18. INCOME TAXES**

All of the Company's operations are in the PRC, and in accordance with the relevant tax laws and regulations of PRC, the corporation income tax rate is 33%; however, the Company was approved as a highly advanced technology foreign investment enterprise in November 2005, and in accordance with the relevant regulations regarding the favorable tax treatment for high technology companies, the Company is entitled to a two year tax exemption. Following the expiration of this tax exemption, the Company will be required to pay 7.5% tax rate for the next three years. Beginning November 2010, the Company will be allowed a 15% tax rate as long as the Company is located and registered in the high and advanced technology development zone. Before expiration of the aforementioned two year tax exemption, the company also applied for a six year tax-free holiday under newly enacted PRC tax laws. Management believes it will be imminently granted such a holiday by the relevant Chinese government authorities; therefore, for the years ended December 31, 2006, 2005, and 2004 the Company made no provision for income taxes. On February 7, 2007, income from the Company's foreign subsidiaries became subject to U.S. income tax law; however, this tax is deferred until foreign source income is repatriated to the Company, which has not yet occurred.

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**19. FINANCING - ISSUANCE OF SERIES A CONVERTIBLE PREFERRED STOCK**

On February 7, 2007, the Company entered into a Series A Convertible Preferred Stock Purchase Agreement (the “Stock Purchase Agreement”) with nine institutional investors pursuant to which the Company issued to the investors an aggregate of 10,287,554 shares of Series A Convertible Preferred Stock (the “Preferred Stock”) at \$2.33 per share for gross proceeds of \$23,970,000. The Preferred Stock is convertible into shares of the Company’s common stock on a 1-for-1 basis. Holders of preferred stock are entitled to a dividend equal to 5% per annum of the amount invested, subject to adjustment. These dividends are payable quarterly.

Pursuant to the Stock Purchase Agreement, the Company issued to the investors, on a pro rata basis, warrants to purchase an aggregate of 6,172,531 shares of common stock at an exercise price of \$2.57 per share (subject to adjustment), expiring five years from the date of issuance. Certain of the investors (those investing at least \$2 million) received additional warrants to purchase an aggregate of 9,358,370 shares at a price of \$2.33 per share for a term of 21 months, as well as warrants to purchase an aggregate of 5,615,021 shares at a price of \$2.57 per share, for a term of five years.

A portion of the net proceeds from the sale of preferred stock and warrants was used to pay for part of the construction costs of the turbine manufacturing facility in Wuhan, China and the purchase of equipment to be used in that facility. The remaining net proceeds were used for working capital.

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**20. EARNINGS PER SHARE**

Components of basic and diluted earnings per share were as follows:

	<b>3 months ended September 30, 2007</b>	<b>9 months ended September 30, 2007</b>	<b>3 months ended September 30, 2006</b>	<b>9 months ended September 30, 2006</b>
Net Income (A)	\$ 7,698,695	\$ 13,734,804	\$ 1,557,369	\$ 2,899,404
Preferred Dividends (B)	\$ 299,625	\$ 773,279	\$ -	\$ -
Income Available to Common Stockholders (C)	<b>\$ 7,399,070</b>	<b>\$ 12,961,525</b>	<b>\$ 1,557,369</b>	<b>\$ 2,899,404</b>
Basic Weighted Average Shares Outstanding (D)	19,712,446	19,712,446	19,712,446	19,712,446
Dilutive Shares:				
- Addition to Common Stock from Conversion of Preferred Stock	10,287,554	8,877,778	-	-
- Addition to Common Stock from Exercise of Warrants	16,200,613	10,532,417	-	-
<b>Diluted Weighted Average Shares Outstanding: (E)</b>	<b>46,200,613</b>	<b>39,122,641</b>	<b>19,712,446</b>	<b>19,712,446</b>
Earnings Per Share				
- Basic (C)/(D)	\$ 0.38	\$ 0.66	\$ 0.08	\$ 0.15
- Diluted (A)/(E)	\$ 0.17	\$ 0.35	\$ 0.08	\$ 0.15
Weighted Average Shares Outstanding				
- Basic	19,712,446	19,712,446	19,712,446	19,712,446
- Diluted	46,200,613	39,122,641	19,712,446	19,712,446

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**21. OPERATING SEGMENTS**

The Company individually tracks the performance of its two operating subsidiaries: Wuhan Blower and Wuhan Generating Equipment. Wuhan Blower is primarily engaged in the design, manufacture, installation, and service of blowers. Wuhan Generating Equipment is primarily engaged in the design, manufacture, installation, and service of power generating equipment. Below is a presentation of the Company's Statement of Income and Balance Sheet for its operating subsidiaries at September 30, 2007, and for the nine months then ended. The Company has also provided reconciling adjustments with the Company and its intermediate holding company, UFG.

	<b>Wuhan Blower</b>	<b>Wuhan Generating Equipment</b>	<b>Company, UFG, Adjustments</b>	<b>Total</b>
Sales	30,217,094	30,125,680	-	60,342,774
Cost of Sales	18,678,246	21,832,961	-	40,511,207
Gross Profit	11,538,848	8,292,719	-	19,831,567
Operating Expenses	3,631,391	857,872	959,728	5,448,991
Other Income (Expenses)	(680,629)	(1,221)	34,079	(647,772)
Earnings before Tax	7,226,827	7,433,625	(925,649)	13,734,804
Tax	-	-	-	-
<b>Net Income</b>	<b>7,226,827</b>	<b>7,433,625</b>	<b>(925,649)</b>	<b>13,734,804</b>

	<b>Wuhan Blower</b>	<b>Wuhan Generating Equipment</b>	<b>Company, UFG, Adjustments</b>	<b>Total</b>
Current Assets	65,200,163	12,473,192	(11,843,748)	65,829,608
Non Current Assets	21,411,087	9,163,497	-	30,574,584
<b>Total Assets</b>	<b>86,611,250</b>	<b>21,636,689</b>	<b>(11,843,748)</b>	<b>96,404,192</b>
Current Liabilities	59,429,942	7,469,875	(23,599,459)	43,300,358
Total Liabilities	59,429,942	7,469,875	(23,599,459)	43,300,358
Net Assets	27,181,308	14,166,815	11,755,712	53,103,835
<b>Total Liabilities &amp; Net Assets</b>	<b>86,611,250</b>	<b>21,636,689</b>	<b>(11,843,748)</b>	<b>96,404,192</b>

**Wuhan General Group (China) Inc.**  
**Notes to Financial Statements**  
**(Stated in US Dollars)**

**22. CONTINGENCY**

A former promoter has contacted the Company claiming that it is entitled to receive shares of the company's common stock in connection with services that it purported to render. The Company disputes this assertion and denies that the promoter is entitled to this compensation. Management believes that the Company has valid defenses to the claim of the promoter and plans to defend vigorously these allegations

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Board of Directors and Stockholders  
Wuhan General Group (China), Inc.

**Report of Registered Independent Public Accounting Firm**

We have reviewed the accompanying interim consolidated Balance Sheets of Wuhan General Group (China), Inc. (the “Company”) as of September 30, 2007 and 2006, and the related statements of income, stockholders’ equity, and cash flows for the three-month and nine-month periods then ended. These interim consolidated financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying interim consolidated financial statements for them to be in conformity with U.S. generally accepted accounting principles.

/s/ Samuel H. Wong & Co., LLP

South San Francisco, California  
October 27, 2007

Samuel H. Wong & Co., LLP  
Certified Public Accountants

## Item 2. Management's Discussion and Analysis or Plan of Operation.

### Cautionary Statement Regarding Forward-Looking Statements

The information contained in this report includes some statements that are not purely historical fact and that are "forward-looking statements" as defined by the Private Securities Litigation Reform Act of 1995. Such forward-looking statements include, but are not limited to, statements regarding our management's expectations, hopes, beliefs, intentions or strategies regarding the future, including our financial condition, results of operations, growth of our blower business and establishment of our turbine business. The words "anticipates," "believes," "could," "estimates," "expects," "intends," "may," "projects," "should," and similar expressions, or the negatives of such terms, identify forward-looking statements.

The forward-looking statements contained in this report are based on our current expectations and beliefs concerning future developments. There can be no assurance that future developments actually affecting us will be those anticipated. These forward-looking statements involve a number of risks, uncertainties (some of which are beyond our control) or other assumptions that may cause actual results to be materially different from those expressed or implied by these forward-looking statements, including the following:

- vulnerability of our business to general economic downturn;
- operating in the PRC generally and the potential for changes in the laws of the PRC that affect our operations;
- our failure to meet or timely meet contractual performance standards and schedules;
- our dependence on the steel and iron markets;
- exposure to product liability and defect claims;
- our ability to obtain all necessary government certifications and/or licenses to conduct our business;
- the cost of complying with current and future governmental regulations and the impact of any changes in the regulations on our operations; and
- the other factors referenced in this report.

These risks and uncertainties, along with others, are also described in the Risk Factors section of the Company's Registration Statement on Form SB-2 (File No. 333-141372). We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as may be required under applicable securities laws.

### *Overview*

As a result of the share exchange or "reverse acquisition" transaction consummated on February 7, 2007, Wuhan General Group (China), Inc. became a holding company conducting operations through two indirect operating subsidiaries: Wuhan Blower Co., Ltd. ("Wuhan Blower") and Wuhan Generating Equipment Co., Ltd. ("Wuhan Generating"), each a company operating in China. A wholly owned subsidiary of the Company, Universe Faith Group Limited ("UFG"), owns 100% of the capital stock of Wuhan Blower, which in turn owns 100% of the capital stock of Wuhan Generating. Our corporate structure is as follows:

For accounting purposes, the share exchange transaction is treated as a reverse acquisition with UFG as the acquirer and Wuhan General Group (China), Inc. as the acquired party. As a result, the Company is deemed to be a continuation of the business of UFG. Accordingly, the accompanying consolidated financial statements are those of the accounting acquirer (UFG). The historical stockholders' equity of the accounting acquirer prior to the share exchange has been retroactively restated as if the share exchange transaction occurred as of the beginning of the first period presented.

The information and data contained in this Management's Discussion and Analysis of Financial Condition and Results of Operations reflect the operating results and financial condition for the three months ended September 30, 2007 and 2006 and the nine months ended September 30, 2007 and 2006.

***Three Months Ended September 30, 2007 Compared to Three Months Ended September 30, 2006***

*Sales.* Sales increased \$25.36 million, or 491.52%, to \$30.52 million for the three months ended September 30, 2007 from \$5.16 million for the same period in 2006. This increase was mainly attributable to increased demand for anti-pollution equipment in China, which accounted for approximately \$14 million in increased sales, and revenue from the construction of a thermal electric power plant in Jiangyin, Jiangsu, which accounted for approximately \$6 million in increased sales.

*Cost of Sales.* Our cost of sales increased \$17.20 million, or 606.66%, to \$20.04 million for the three months ended September 30, 2007 from \$2.84 million during the same period in 2006. This increase was due to the significant increase in blower sales, which accounted for approximately \$2 million in increased cost of sales, and an increase in the cost of materials, which accounted for approximately \$10 million in increased cost of sales. As a percentage of sales, the cost of sales was 65.65% during the three months ended September 30, 2007 compared to 54.96% in the same period of 2006. This increase was primarily attributable to the increase in the cost of materials.

*Gross Profit.* Our gross profit increased \$8.16 million, or 351.04%, to \$10.48 million for the three months ended September 30, 2007 from \$2.32 million for the same period in 2006. Gross profit as a percentage of sales was 34.35% for the three months ended September 30, 2007 compared to 45.04% during the same period in 2006.

*Selling Expenses.* Our selling expenses increased \$0.73 million, or 349.52%, to \$0.94 million for the three months ended September 30, 2007 from \$0.21 million for the same period in 2006. As a percentage of sales, selling expenses were 3.07% for the three months ended September 30, 2007 compared to 4.05% for the same period in 2006. This decrease as a percentage of sales was primarily attributable to the economies of scale that we achieved due to the significant increase in sales.

*General and Administrative Expenses.* Our general and administrative expenses increased \$1.04 million, or 234.26%, to \$1.48 million for the three months ended September 30, 2007 from \$0.44 million for the same period in 2006. As a percentage of sales, general and administrative expenses were 4.85% for the three months ended September 30, 2007 compared to 8.59% for the same period in 2006. This decrease as a percentage of sales was primarily attributable to the economies of scale that we achieved due to the significant increase in sales.

*Warranty Expense.* Our warranty expense increased to \$0.09 million for the three months ended September 30, 2007 from \$0 for the same period in 2006. As a percentage of sales, warranty expense was 0.30% for the three months ended September 30, 2007 compared to 0% for the same period in 2006.

*Operating Income.* Our operating income increased \$6.30 million, or 376.71% to \$7.97 million for the three months ended September 30, 2007 from \$1.67 million for the same period in 2006. As a percentage of sales, operating income was 26.12% for the three months ended September 30, 2007 compared to 32.41% for the same period in 2006. This decrease was due primarily to the increased cost of materials.

*Other Income.* We had no "other income" for the three months ended September 30, 2007 compared to \$7,444 for the same period in 2006.

*Interest Income.* Our interest income increased to \$94,798 for the three months ended September 30, 2007 from \$0 for the same period in 2006. This increase was due to an increase in bank deposits.

*Interest Expense.* Our interest expense increased \$0.25 million, or 205.11%, to \$0.37 million for the three months ended September 30, 2007 from \$0.12 million for the same period in 2006. This increase was due to the significant increase in bank loans and notes. As a percentage of sales, interest expense was 1.21% for the three months ended September 30, 2007 compared to 2.34% for the same period in 2006. This decrease as a percentage of sales was primarily attributable to our increase in the comparative use of equity financing to fund our significant growth.

*Income Tax.* Due to a tax exemption, Wuhan Blower and Wuhan Generating were not subject to PRC income tax during the three months ended September 30, 2007 or during the same period in 2006.

*Net Income.* Net income increased \$6.14 million, or 394.34%, to \$7.70 million during the three months ended September 30, 2007 from \$1.56 million during the same period in 2006, as a result of the factors described above.

***Nine Months Ended September 30, 2007 Compared to Nine Months Ended September 30, 2006***

*Sales.* Sales increased \$48.73 million, or 419.66%, to \$60.34 million for the nine months ended September 30, 2007 from \$11.61 million for the same period in 2006. This increase was mainly attributable to increased demand for anti-pollution equipment in China, which accounted for approximately \$30 million in increased sales, and revenue from the construction of a thermal electric power plant in Jiangyin, Jiangsu, which accounted for approximately \$6 million in increased sales.

*Cost of Sales.* Our cost of sales increased \$33.95 million, or 517.68%, to \$40.51 million for the nine months ended September 30, 2007 from \$6.56 million during the same period in 2006. This increase was due to the significant increase in blower sales, which accounted for approximately \$6 million in increased cost of sales, and an increase in the cost of materials, which accounted for approximately \$22 million in increased cost of sales. As a percentage of sales, the cost of sales was 67.14% during the nine months ended September 30, 2007 compared to 56.48% in the same period of 2006. This increase was primarily attributable to the increase in the cost of materials.

*Gross Profit.* Our gross profit increased \$14.78 million, or 292.44%, to \$19.83 million for the nine months ended September 30, 2007 from \$5.05 million for the same period in 2006. Gross profit as a percentage of sales was 32.86% for the nine months ended September 30, 2007 compared to 43.52% during the same period in 2006.

*Selling Expenses.* Our selling expenses increased \$1.02 million, or 168.09%, to \$1.63 million for the nine months ended September 30, 2007 from \$0.61 million for the same period in 2006. As a percentage of sales, selling expenses were 2.71% for the nine months ended September 30, 2007 compared to 5.25% for the same period in 2006. This decrease as a percentage of sales was primarily attributable to the economies of scale that we achieved due to the significant increase in sales.

*General and Administrative Expenses.* Our general and administrative expenses increased \$2.12 million, or 178.53%, to \$3.30 million for the nine months ended September 30, 2007 from \$1.18 million for the same period in 2006. As a percentage of sales, general and administrative expenses were 5.47% for the nine months ended September 30, 2007 compared to 10.20% for the same period in 2006. This decrease as a percentage of sales was primarily attributable to the economies of scale that we achieved due to the significant increase in sales.

*Warranty Expense.* Our warranty expense increased to \$0.51 million for the nine months ended September 30, 2007 from \$0 for the same period in 2006. As a percentage of sales, warranty expense was 0.85% for the nine months ended September 30, 2007 compared to 0% for the same period in 2006.

*Operating Income.* Our operating income increased \$11.12 million, or 341.30% to \$14.38 million for the nine months ended September 30, 2007 from \$3.26 million for the same period in 2006. As a percentage of sales, operating income was 23.84% for the nine months ended September 30, 2007 compared to 28.07% for the same period in 2006. This decrease was due primarily to the increased cost of materials.

*Other Income.* Our other income decreased to \$0 for the nine months ended September 30, 2007 from \$31,167 for the same period in 2006.

*Interest Income.* Our interest income increased to \$0.11 million for the nine months ended September 30, 2007 from \$0 for the same period in 2006. This increase was due to an increase in bank deposits.

*Interest Expense.* Our interest expense increased \$0.37 million, or 94.51%, to \$0.76 million for the nine months ended September 30, 2007 from \$0.39 million for the same period in 2006. This increase was due to the significant increase in bank loans and notes. As a percentage of sales, interest expense was 1.25% for the nine months ended September 30, 2007 compared to 3.35% for the same period in 2006. This decrease as a percentage of sales was primarily attributable to our increase in the comparative use of equity financing to fund our significant growth.

*Income Tax.* Due to a tax exemption, Wuhan Blower and Wuhan Generating were not subject to PRC income tax during the nine months ended September 30, 2007 or during the same period in 2006.

*Net Income.* Net income increased \$10.84 million, or 373.71%, to \$13.73 million during the nine months ended September 30, 2007 from \$2.90 million during the same period in 2006, as a result of the factors described above.

### ***Liquidity and Capital Resources***

As of September 30, 2007, we had cash and cash equivalents (including restricted cash) of \$12.22 million.

As of September 30, 2007, we had banking facilities in the form of bank loans and loan facilities from other non-bank entities totaling approximately \$24.83 million (based on an exchange rate of 7.5176 RMB per 1 U.S. dollar).

Information regarding these loans is set forth below in US \$.

<b>Name of Bank or Note Holder</b>	<b>Due Date</b>	<b>Interest Rate Per Annum</b>	<b>9/30/2007</b>
Shanghai Pudong Development Bank	10/19/2007	6.03%	\$ 2,128,339
Shanghai Pudong Development Bank	5/22/2008	6.57%	1,330,212
Shanghai Pudong Development Bank	6/25/2008	6.57%	532,085
Citic Industrial Bank	9/25/2008	7.29%	3,325,529
Citic Industrial Bank	9/25/2008	7.29%	16,541
Agricultural Bank of China	10/31/2007	6.73%	1,330,212
Agricultural Bank of China	10/30/2007	6.73%	1,330,212
Wuhan East Lake Development District Zheng Bridge Committee	On Demand	6.00%	399,064
Bank of China	On Demand	6.83%	698,361
Dalian Chong Si Hydraulic Coupler Complete Sets of Equipment Ltd. (Note Payable)	On Demand	0.00%	133,021
Hubei Committees Properties Co., Ltd. (Note Payable)	On Demand	0.00%	6,358,412
Wuhan-heavy George Special Steel Co., Ltd. (Note Payable)	On Demand	0.00%	215,926
Wuhan Jiabao Supplies Co., Ltd. (Note Payable)	On Demand	0.00%	104,465
Wuhan Jiangnan District Zhongnan Supplies Station (Note Payable)	On Demand	0.00%	156,911
Citic Industrial Bank Wuhan Zhu Ye Shan Branch	2/17/2008	6.73%	2,660,424
Citic Industrial Bank Wuhan Zhu Ye Shan Branch	2/17/2008	6.73%	2,660,424
59 Various Other Notes	Various Dates	Various Rates	1,448,320
			\$ 24,828,456

We plan to either repay this debt as it matures or refinance this debt with other debt. Since December 31, 2006, the amount of our outstanding debt from bank loans and notes has increased \$11.28 million. This significant increase in debt was necessary to fund the cost of our growth.

On February 7, 2007, immediately following the consummation of the share exchange, we completed a private placement of Series A Convertible Preferred Stock and warrants to accredited investors. As a result of this private placement, we received approximately \$24.0 million in gross proceeds. After the deduction of sales commissions and offering expenses, we received approximately \$20.8 million in net proceeds.

We anticipate significant capital expenditure requirements over the next year. Specifically, we expect to spend approximately \$22.5 million on the construction of and equipment for our turbine manufacturing facility. These capital expenditures will be funded principally from the net proceeds of our February 2007 private placement and from working capital.

We expect our liquidity to increase over the next 12 months due to anticipated increased sales of our blower and turbine products.

We believe that our currently available working capital, combined with cash from operations, should be adequate to sustain our operations at our current levels through at least the next 12 months.

For the quarter ended September 30, 2007, our cash flow from operating activities was \$3.68 million. The majority of our customers pay us in installments at various stages of completion, including production, delivery, installation, and satisfactory operation for a specified period. This causes our accounts receivable cycle to be up to 18 months long. We are reviewing our standard payment terms and accounts receivable policies in order to collect on our accounts receivable in a timelier manner. At September 30, 2007, we had \$31.41 million in accounts receivable, compared to \$23.15 million at June 30, 2007.

At September 30, 2007, we also had \$2.60 million in other receivables. We also had notes receivable of \$0.99 million at September 30, 2007. These notes receivable represent the transformation of certain of the Company's accounts receivable into notes, which, as negotiable instruments, provide the Company with greater liquidity.

At September 30, 2007, we had contract payable in the amount of \$0. We had other payable of \$2.58 million at September 30, 2007 related to accruals for materials that have been provided or services rendered, but for which no invoice has been received from the vendor.

### ***Critical Accounting Policies***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires our management to make assumptions, estimates and judgments that affect the amounts reported in the financial statements, including the notes thereto, and related disclosures of commitments and contingencies, if any. We consider our critical accounting policies to be those that require the more significant judgments and estimates in the preparation of financial statements, including the following:

**Method of Accounting:** We maintain our general ledger and journals with the accrual method of accounting for financial reporting purposes. The financial statements and notes are representations of management. Accounting policies that we have adopted conform to generally accepted accounting principles in the United States of America and have been consistently applied in the presentation of financial statements, which are compiled on the accrual basis of accounting.

**Consolidation:** The interim consolidated financial statements include the accounts of the Company and its subsidiaries, UFG, Wuhan Blower, and Wuhan Generating. Inter-company transactions, such as sales, cost of sales, due to/due from balances, investment in subsidiaries, and subsidiaries' capitalization have been eliminated.



Economic and Political Risks: Our operations are conducted in the PRC. Accordingly, our business, financial condition and results of operations may be influenced by the political, economic and legal environment in the PRC and by the general state of the PRC economy.

Use of Estimates: In preparing the financial statements in conformity with accounting principles generally accepted in the United States of America, management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the dates of the financial statements, as well as the reported amounts of revenues and expenses during the reporting years. These estimates and assumptions include, but are not limited to, the valuation of accounts receivable, inventories, deferred income taxes and the estimation of useful lives of property, plant, and equipment. Actual results could differ from these estimates.

Cash and Cash Equivalents: We consider all cash and other highly liquid investments with initial maturities of three months or less to be cash equivalents. We maintain bank accounts in the PRC, and an escrow account in the United States of America.

Accounts Receivable-Trade: Trade receivables are recognized and carried at the original invoice amount less allowance for any uncollectible amounts. An allowance for doubtful accounts is made when collection of the full amount is no longer probable. Bad debts are written-off as incurred.

Inventory: Inventory, consisting of raw materials, work in progress, and finished products, is stated at the lower of cost or market value. Finished products are comprised of direct materials, direct labor and an appropriate proportion of overhead.

Property, Plant, and Equipment: Property, plant and equipment are carried at cost less accumulated depreciation. Depreciation is provided over their estimated useful lives, using the straight-line method with 5% salvage value. Estimated useful lives of the property, plant and equipment are as follows:

Buildings	30 years
Machinery and Equipment	10 years
Furniture and Fixtures	5 years
Motor Vehicles	5 years

Intangible Assets: Intangible assets are stated at cost less accumulated amortization. Amortization is provided over the respective useful lives, using the straight-line method. Estimated useful lives of intangibles are as follows:

Technical License	10 years
Trademark	20 years

Land Use Rights: We carry land use rights at cost less accumulated amortization. Land use rights are amortized straight-line over its useful life of 50 years.

Accounting for Impairment of Long-Lived Assets: We adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"), which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. We periodically evaluate the carrying value of long-lived assets to be held and used in accordance with SFAS 144. SFAS 144 requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amounts. In that event, a loss is recognized based on the amount by which the carrying amount exceeds the fair market value of the long-lived assets. Loss on long-lived assets to be disposed of is determined in a similar manner, except that fair market values are reduced for the cost of disposal. Based on its review, we believe that, as of September 30, 2007, and 2006, there were no significant impairments of long-lived assets.

Revenue Recognition: Revenue from the sale of blower products and generating equipment is recognized at the time of the transfer of risks and rewards of ownership, which generally occurs when the goods are delivered to customers and the title has passed.

Cost of Sales: Our cost of sales is comprised of raw materials, factory worker salaries and related benefits, machinery supplies, maintenance supplies, depreciation, utilities, inbound freight, purchasing and receiving costs, inspection and warehousing costs.

Selling Expenses: Selling expenses are comprised of outbound freight, salary for the sales force, client entertainment, commissions, depreciation, advertising, and travel and lodging expenses.

General & Administrative Expenses: General and administrative costs include outside consulting services, research & development, executive compensation, quality control, and general overhead such as the finance department, administrative staff, and depreciation and amortization expense.

Advertising: We expense all advertising costs as incurred. For the nine months ended September 30, 2007, the total advertising expense was \$30,596.

Research and Development: We expense all research and development costs as incurred. For the nine months ended September 30, 2007, the total research and development cost was \$103,975.

Foreign Currency Translation: We maintain our financial statements in the functional currency. Our functional currency is the Renminbi (RMB). Monetary assets and liabilities denominated in currencies other than the functional currency are translated into the functional currency at rates of exchange prevailing at the balance sheet dates. Transactions denominated in currencies other than the functional currency are translated into the functional currency at the exchanges rates prevailing at the dates of the transaction. Exchange gains or losses arising from foreign currency transactions are included in the determination of net income for the respective periods.

For financial reporting purposes, the financial statements, which are prepared using the functional currency, have been translated into U.S. dollars. Assets and liabilities are translated at the exchange rates at the balance sheet dates and revenue and expenses are translated at the average exchange rates and stockholders' equity is translated at historical exchange rates. Translation adjustments are not included in determining net income but are included in foreign exchange adjustment to other comprehensive income, a component of stockholders' equity.

<b>Exchange Rates</b>	<b>September 30, 2007</b>	<b>September 30, 2006</b>
Period end RMB: US\$ exchange rate	7.5176	7.9168
Average RMB during 9 month period: US\$ exchange rate	7.67576	7.97711

RMB is not freely convertible into foreign currency and all foreign exchange transactions must take place through authorized institutions. No representation is made that the RMB amounts could have been, or could be, converted into US\$ at the rates used in translation.

**Income Taxes:** We account for income tax using an asset and liability approach and allow 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. A valuation allowance is provided for deferred tax assets if it is more likely than not these items will either expire before we are able to realize their benefits, or that future realization is uncertain.

All of our operations are in the PRC, and in accordance with the relevant tax laws and regulations of PRC, the corporation income tax rate is 33%. However, the Company was approved as a highly advanced technology foreign investment enterprise in November 2005, and in accordance with the relevant regulations regarding the favorable tax treatment for high technology companies, the Company is entitled to a two-year tax exemption. Following the expiration of this tax exemption, we will be required to pay a 7.5% tax rate for the next three years. Beginning in November 2010, the Company will be allowed a 15% tax rate as long as the Company is located and registered in the high and advanced technology development zone.

The Company's foreign subsidiaries are subject to U.S. income tax liability; however, the tax is deferred until foreign source income is repatriated to the Company.

The Company is subject to United States income tax according to Internal Revenue Code Sections 951 and 957. Corporate income tax is imposed on graduated rates based on the ranges shown in the following table:

<b>Taxable Income</b>			
<i>Rate</i>	<i>Over</i>	<i>But not over</i>	<i>Of Amount Over</i>
15%	0	50,000	0
25%	50,000	75,000	50,000
34%	75,000	100,000	75,000
39%	100,000	335,000	100,000
34%	335,000	10,000,000	335,000
35%	10,000,000	15,000,000	10,000,000
38%	15,000,000	18,333,333	15,000,000
35%	18,333,333	-	0

**Statutory Reserve:** In accordance with PRC laws, statutory reserve refers to the appropriation from net income, to the account “statutory reserve” to be used for future company development, recovery of losses, and increase of capital, as approved, to expand production or operations. PRC laws prescribe that an enterprise operating at a profit, must appropriate, on an annual basis, an amount equal to 10% of its profit. Such an appropriation is necessary until the reserve reaches a maximum that is equal to 50% of the enterprise’s PRC registered capital.

**Other 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. Our current component of other comprehensive income is the foreign currency translation adjustment.

**Warranty Policy:** The estimation of warranty obligations is determined in the same period that revenue from the sale of the related products is recognized. The warranty obligation is based on historical experience and reflects management’s best estimate of expected costs at the time products are sold. Warranty accruals are adjusted for known or anticipated warranty claims as new information becomes available. Future events and circumstances could materially change our estimates and require adjustments to the warranty obligation. New product launches require a greater use of judgment in developing estimates until historical experience becomes available.

**Earnings Per Share:** Basic earnings per share is computed on the basis of the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is computed on the basis of the weighted average number of shares of common stock plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method for warrants and the as-if method for convertible securities. Dilutive potential common shares include outstanding warrants, and convertible preferred stock.

**Recent Accounting Pronouncements:** In February 2006, the FASB issued SFAS 155, “Accounting for Certain Hybrid Financial Instruments” to amend FASB Statements No. 133, “Accounting for Derivative Instruments and Hedging Activities,” and No. 140, “Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.” This statement permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation and eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. This statement is effective for all financial instruments acquired or issued after the beginning of an entity’s first fiscal year that begins after September 15, 2006.



In July 2006, the FASB issued FIN 48, Accounting for Uncertainty in Income Taxes—an Interpretation of FASB Statement No. 109, which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that the Company recognize in its consolidated financial statements the impact of a tax position if that position is more likely than not to be sustained upon an audit, based on the technical merits of the position. The provisions of FIN 48 are effective for the Company on January 1, 2007, with the cumulative effect of the change in accounting principle, if any, recorded as an adjustment to opening retained earnings.

In September 2006, the FASB issued SFAS 157, “Fair Value Measurements”, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 applies under other accounting pronouncements that require or permit fair value measurements, where fair value is the relevant measurement attribute. The standard does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years.

In September 2006, the SEC issued SAB No. 108, which provides guidance on the process of quantifying financial statement misstatements. In SAB No. 108, the SEC staff establishes an approach that requires quantification of financial statement errors, under both the iron-curtain and the roll-over methods, based on the effects of the error on each of the Company’s financial statements and the related financial statement disclosures. SAB No.108 is generally effective for annual financial statements in the first fiscal year ending after November 15, 2006. The transition provisions of SAB No. 108 permits existing public companies to record the cumulative effect in the first year ending after November 15, 2006 by recording correcting adjustments to the carrying values of assets and liabilities as of the beginning of that year with the offsetting adjustment recorded to the opening balance of retained earnings.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities—Including an Amendment of SFAS 115” (SFAS No. 159), which allows for the option to measure financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. The objective of SFAS 159 is to provide opportunities to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply hedge accounting provisions. SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of SFAS No. 159 on our consolidated financial statements.

We do not anticipate that the adoption of the above standards will have a material impact on our consolidated financial statements.

### *Off-Balance Sheet Arrangements*

We do not have any off-balance arrangements.

### **Item 3. Controls and Procedures**

#### *Disclosure Controls and Procedures*

As required by Rule 13a-15 under the Securities Exchange Act, our management has carried out an evaluation, with the participation and under the supervision of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of September 30, 2007. Disclosure controls and procedures refer to controls and other procedures designed to ensure that information required to be disclosed in the reports we file or submit under the Securities Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating and implementing possible controls and procedures.

Management conducted its evaluation of disclosure controls and procedures under the supervision of our Chief Executive Officer and our Chief Financial Officer. Based upon, and as of the date of this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures contained significant deficiencies and material weaknesses. We believe that the deficiencies and weaknesses in our disclosure controls and procedures result from weaknesses in our internal controls over financial reporting. In connection with the audit of our financial statements as of and for the year ended December 31, 2006, our independent auditors identified and communicated significant deficiencies and material weaknesses with respect to our internal controls over financial reporting.

As we have disclosed in our prior SEC filings, we conduct all of our operations through our Chinese operating subsidiaries, which were privately owned until February 2007. At the time of their acquisition, these Chinese companies did not have in place the financial controls and procedures required of a U.S. public company. Now as a public company, we have implemented and continue to implement remediation initiatives and interim measures with respect to our internal controls over financial reporting during the quarter ended September 30, 2007 and through the current date.

In the absence of full implementation of the remediation initiatives described below, we have undertaken additional measures in the interim to ensure that our consolidated financial statements included in this report were prepared in accordance with accounting principles generally accepted in the United States. Accordingly, the Company's management believes that the consolidated financial statements included in this report fairly present in all material respects the Company's financial condition, results of operations and cash flows for the periods presented and that this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.

***Management's Remediation Initiatives and Interim Measures***

The following is a description of each deficiency or weakness with respect to our internal controls over financial reporting identified by our outside auditors and the remediation initiatives that we have implemented or intend to implement in the near future.

- 1) Our board of directors and audit committee have not yet taken an active role in the oversight of our policies and procedures.

*Remediation Initiative*

Our outside legal counsel has met with our new board of directors to discuss the role and responsibilities of the board of a U.S. public company. In addition, our outside legal counsel has held a separate meeting with the members of the audit committee to discuss the role and responsibilities of the audit committee of a U.S. public company. We intend to hold additional meetings with our outside legal counsel in order to increase the knowledge and understanding of our board and audit committee members.

We also have increased the frequency of board and audit committee meetings. Our audit committee has adopted a written charter. We intend to increase coordination between our accounting staff, outside auditors and audit committee in conjunction with the preparation of future financial statements.

In addition, we plan to document our policies and procedures regarding our business practices, management, administration, accounting and financial reporting, which we believe will increase transparency and accountability.

- 2) The current staff in the accounting department is relatively new and inexperienced, and needs substantial training due to staff turnover, organizational changes, and the higher demands of being a U.S. public company. The accounting skills and understanding necessary to fulfill the requirements of U.S. GAAP-based reporting, including the skills of subsidiary financial statements consolidation, are inadequate.

*Remediation Initiative*

We have recently expanded our internal accounting staff and intend to continue this effort in the future. In particular, we are seeking accountants experienced in several key areas of accounting, including persons with experience in Chinese and U.S. GAAP, U.S. GAAP consolidation requirements, and SEC financial reporting requirements. In addition, we plan to allocate additional resources to train our existing accounting staff.



3) Our internal audit team is currently understaffed. In addition, the scope and effectiveness of the internal audit function have yet to be developed.

*Remediation Initiative*

We plan to expand the size of our recently created internal audit group. We also plan to enhance the training of our internal audit team in order to increase the effectiveness of this group.

4) The Company does not have an organization level information system. The major system of record is the K/3 ERP (Version 10), the middle range enterprise resource planning package developed by Kingdee International Software Group Co., Ltd. Although capable of supporting other operational functions, K/3 is only deployed as an accounting back office application.

*Remediation Initiative*

The Company plans to continue to enhance its accounting software and implement an organization level information system.

5) There is a lack of integration and automation for data entry in our accounting software. Lack of integration in this key area has potentially problematic implications. The manual data entry procedures do not include critical accounting checks and balances, such as control totals and batch numbers, and are subject to clerical errors. There are currently no mechanisms in the workflows for verifying and monitoring the completeness and accuracy of the data inputted.

*Remediation Initiative*

We intend to develop policies and procedures to enhance the integration and automation for data entry in our accounting software. In the interim, we have improved the verification of data entered into our accounting software. The Chief Financial Officer of our two Chinese subsidiaries has taken a more active role in reviewing and verifying accounting documents.

6) Costing journal entries are supported by an Excel worksheet prepared and adjusted based on the monthly master work-in-progress detail report by job. There is a lack of an audit trail or documentation to show the reasons and sources for the adjustments made on the worksheets. This supporting Excel worksheet is not printed out and attached to the journal entry vouchers. Proper review and authorization of the worksheet and the entries are not evidenced.

*Remediation Initiative*

We intend to develop policies and procedures to require our accounting staff to maintain hard copy printouts of accounting documents in a central location.

7) The costing module of our accounting software has been customized, but the functionality of the customizations is rudimentary and unrefined, such that the system cannot fulfill the intended purposes, and therefore, requires alternative, manual solutions.

*Remediation Initiative*

We intend to continue to refine our accounting software to improve functionality.

8) There are insufficient policies and procedures for the development, modification, and use of computer programs and data files. We do not have comprehensive management policies and procedures for critical applications and systems. We have outsourced support for our accounting software. In addition, application and database servers are located in a semi-public area of our corporate offices. Therefore, there are security and information integrity risks associated with our use of accounting software.

*Remediation Initiative*

We intend to develop and adopt policies designed to increase the security and integrity of our computer programs and data files.

9) The accounting department does not maintain hard copy printouts of the general ledgers, sub-ledgers, and supporting worksheets. Many electronic source documents and worksheets are stored in the staff's local computers in a disorganized manner.

*Remediation Initiative*

We intend to develop policies and procedures to require our accounting staff to maintain hard copy printouts of accounting documents in a central location.

***Changes in Internal Controls over Financial Reporting***

Other than the remediation measures described above, during the quarter ended September 30, 2007, there was no change in our internal controls over financial reporting that has materially affected, or that is reasonably likely to materially affect, our internal control over financial reporting.

**PART II**

**OTHER INFORMATION**

**Item 1. Legal Proceedings.**

A former promoter has contacted the Company claiming that it is entitled to receive shares of the Company's common stock in connection with services that it purported to render. The Company disputes this assertion and denies that the promoter is entitled to this compensation. Management believes that the Company has valid defenses to the claim of the promoter and plans to defend vigorously these allegations. As of November 14, 2007, the former promoter has not brought any formal legal proceedings.

In addition, from time to time, the Company may become involved in various lawsuits and legal proceedings which arise in the ordinary course of business.

**Item 6. Exhibits.**

**Exhibit**

<b>Number</b>	<b>Description of Exhibit</b>
10.1*	Construction Contract (Turbine Manufacturing Facilities) between Wuhan Generating Equipment Co., Ltd. and Hubei Gongchuang Real Estate Co., Ltd.
10.2*	Supplementary Agreement to Construction Contract (Turbine Manufacturing Facilities), dated March 21, 2007, between Wuhan Blower Co., Ltd. and Hubei Gongchuang Real Estate Co., Ltd.
10.3*	Construction Contract (Administrative Building for Turbine Facilities), dated March 26, 2007, between Wuhan Generating Equipment Co., Ltd. and Hubei Gongchuang Real Estate Co., Ltd.
10.4*	Construction Contract for Thermal Electric Plant, dated July 8, 2007, between Wuhan Generating Equipment Co., Ltd. and Jiangsu Huangli Paper Industry Co., Ltd.
31.1*	Certification of Principal Executive Officer pursuant to Rule 13a-14(a).
31.2*	Certification of Principal Financial Officer pursuant to Rule 13a-14(a).
32.1*	Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350.
32.2*	Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350.

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\* Filed herewith

**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.

Date: November 14, 2007

WUHAN GENERAL GROUP (CHINA), INC.

By: /s/ Xu Jie

\_\_\_\_\_  
Name: Xu Jie

Title: President and Chief Executive Officer

(principal executive officer and duly authorized officer)

By: /s/Kuang Yuandong

\_\_\_\_\_  
Name: Kuang Yuandong

Title: Chief Financial Officer and Treasurer

(principal financial officer)

**Exhibit Index**

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