Qingdao Footwear, Inc.
Form 10-Q
August 16, 2010

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2010

Commission File Number: 000-53075

QINGDAO FOOTWEAR, INC.
(Exact name of registrant as specified in its charter)

Delaware	16-1591157
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

269 First Huashan Road
Jimo City, Qingdao, Shandong, PRC
(Address of principal executive office and zip code)

86-532-86595999
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer o	Accelerated filer o
Non-accelerated filer o	Smaller reporting company x

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at August 15, 2010
Common Stock, $0.0001 par value per share	10,000,179 shares

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PART I: FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

QINGDAO FOOTWEAR, INC.
CONSOLIDATED BALANCE SHEETS
AS OF JUNE 30, 2010 AND DECEMBER 31, 2009

	June 30, 2010 (unaudited)	December 31, 2009 (audited)
ASSETS		
Current assets		
Cash	$ 414,350	$ 61,131
Accounts receivable	360,934	98,962
Notes receivable	460,313	-
Inventories	557,031	344,512
Prepaid expenses	651,854	57,311
Total current assets	2,444,482	561,916
Long term prepaid expenses	1,668,725	-
Property, plant and equipment, net	1,022,594	930,451
Intangible assets	3,873,744	208,167
Total Assets	$ 9,009,545	$ 1,700,534
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 21,261	$ 15,727
Accrued liabilities	1,056,441	-
Short term loans	1,163,670	718,830
Taxes payable	3,043,141	2,627
Duet to related parties	-	221,871
Total current liabilities	5,284,513	959,055
Long-term debt	250,410	249,390
Total Liabilities	$ 5,534,923	$ 1,208,445
Shareholders' Equity		
Series A preferred stock, .0001 par value, 10,000,000 shares authorized, none issued and outstanding	-	-
	1,000	970

Common stock, .0001 par value, 100,000,000 shares authorized, 10,000,000 and 9,700,000 shares issued and outstanding, respectively		
Additional paid-in capital	762,091	319,510
Accumulated other comprehensive income	455,031	440,775
Retained earnings (deficits)	2,256,500	(269,166)
Total Shareholders’ Equity	$ 3,474,622	$ 492,089
Total Liabilities and Shareholders' Equity	$ 9,009,545	$ 1,700,534

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

QINGDAO FOOTWEAR, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
FOR THE TRHEE MONTHS AND SIX MONTHS ENDED JUNE 30, 2010 and 2009
UNAUDITED

	Three Months Ended		Six Months Ended	
	June 30, 2010	June 30, 2009	June 30, 2010	June 30, 2009
Net sales	$ 6,483,625	$ 5,143,578	$ 11,249,437	$ 9,599,476
Cost of sales	3,422,563	2,923,413	6,079,318	5,445,751
Gross Profit	3,061,062	2,220,165	5,170,119	4,153,725
Operating expenses:				
Selling, general and administrative expenses	844,753	230,913	1,104,863	449,460
Depreciation and Amortization Expense	41,312	13,125	59,317	26,258
Income from operations	2,174,997	1,976,127	4,005,939	3,678,007
Other income (expense)				
Rental income	22,009	21,994	44,007	43,971
Interest income	18,498	180	18,587	713
Interest expense	(26,261)	(13,892)	(49,167)	(27,391)
Income before income taxes	2,189,243	1,984,409	4,109,366	3,695,300
Income taxes	657,964	494,902	1,115,495	922,625
Net income	$ 1,531,279	$ 1,489,507	$ 2,903,871	$ 2,772,675
Earnings per share - basic and diluted	$ 0.15	$ 0.15	$ 0.29	$ 0.29
Weighted average shares outstanding-basic and diluted	10,000,000	9,700,000	10,000,000	9,700,000
Net income	$ 1,531,279	$ 1,489,507	$ 2,903,871	$ 2,772,675
Other comprehensive income				
Foreign currency translation	13,915	(1,234)	14,256	(7,939)
Comprehensive income	$ 1,545,194	$ 1,488,273	$ 2,918,127	$ 2,764,736

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

QINGDAO FOOTWEAR, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JUNE 30, 2010 AND 2009
UNAUDITED

	Six Months Ended	
	June 30, 2010	June 30, 2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 2,903,871	$ 2,772,675
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	59,317	26,258
Stock based compensation	442,611	-
Changes in operating assets and liabilities:		
Accounts receivable	(261,567)	(40,637)
Accrued interest on notes receivable	(18,413)	-
Inventories	(211,109)	(39,869)
Prepaid expenses	(2,263,033)	(50,912)
Accounts payable and accrued liabilities	38,456	17,105
Tax payable	3,040,504	2,681,288
Net cash provided by operating activities	3,730,637	5,365,908
CASH FLOWS FROM INVESTING ACTIVITIES		
Loan made to other	(441,900)	-
Advance to related party	(222,778)	(3,243,228)
Cash paid for property and equipment	(130,127)	(373,302)
Cash paid for intangible asset	(2,659,045)	-
Net cash used in investing activities	(3,453,850)	(3,616,530)
CASH FLOWS FROM FINANCING ACTIVITIES		
Distribution to shareholders	(378,205)	(1,611,500)
Proceeds from loans	441,900	-
Net cash provided by (used in) financing activities	63,695	(1,611,500)
Effect of exchange rate changes on cash	12,737	(1,498)
Net increase in cash	$ 353,219	$ 136,380
Cash, beginning of period	61,131	118,534
Cash, end of period	$ 414,350	$ 254,914
SUPPLEMENTARY DISCLOSURE:		
Interest paid	$ 49,167	$ 27,391
Income tax paid	$ 1,149	$ 1,052

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

QINGDAO FOOTWEAR, INC.
NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1 - ORGANIZATION AND BUSINESS OPERATIONS

Qingdao Footwear, Inc. (formerly Datone, Inc.) was originally incorporated on August 9, 2000 under the laws of the State of Delaware. The Company operated as a wholly-owned subsidiary of USIP.COM, Inc. On August 24, 2006, USIP decided to spin-off its subsidiary companies, one of which was Datone, Inc. On February 1, 2008, Datone, Inc. filed a registration statement on Form 10-SB, which went effective on November 13, 2008.

On February 12, 2010, the Company completed a reverse acquisition transaction through a share exchange with Glory Reach International Limited, a Hong Kong limited company ("Glory Reach"), the shareholders of Glory Reach (the "Shareholders"), Greenwich Holdings LLC and Qingdao Shoes, whereby the Company acquired 100% of the issued and outstanding capital stock of Glory Reach in exchange for 10,000 shares of our Series A Convertible Preferred Stock which constituted 97% of our issued and outstanding capital stock on an as-converted to common stock basis as of and immediately after the consummation of the reverse acquisition. Following the effectiveness of the Reverse Stock Split (note 9) and conversion of Series A Preferred Stock into common stock (note 9), there will be approximately 10,000,000 shares of our common stock issued and outstanding and no shares of preferred stock issued and outstanding. As a result of the reverse acquisition, Glory Reach became our wholly-owned subsidiary and the former shareholders of Glory Reach became our controlling stockholders. The share exchange transaction with Glory Reach was treated as a reverse acquisition, with Glory Reach as the acquirer and Datone, Inc. as the acquired party for accounting and financial reporting purposes. After the reverse merger, Datone, Inc changed its name to Qingdao Footwear, Inc.

Datone spun off all its assets and liabilities to its prior owners before the reverse merger. For Glory Reach, reverse merger is accounted for as a reverse merger with a shell company and as a recapitalization.

Glory Reach International Limited (the "Company") was established in Hong Kong on November 18, 2009 to serve as an intermediate holding company. Mr. Tao Wang, the controlling interest holder of Qingdao Shoes also controls the Company. On February 8, 2010, also pursuant to the restructuring plan, the Company acquired 100% of the equity interests in Qingdao Shoes.

Qingdao Shoes was incorporated on March 11, 2003 in Jimo County, Qingdao City, Shandong Province, People's Republic of China (the "PRC") with registered capital of $320,480. Prior to December 18, 2009, Mr. Tao Wang owned 80% of Qingdao Shoes and the remaining 20% was owned by Mr. Renwei Ma. Starting from December 18, 2009, Mr. Tao Wang owned 80% of Qingdao Shoes, Mr. Renwei Ma owned 15% and Mr. Wenyi Chen owned the remaining 5%. Qingdao Shoes is the owner of the brand name "Hongguan" and principally engaged in the wholesale and retail sales of fashion footwear primarily in the northeast region of China.

Since there is common control between the Glory Reach and Qingdao Shoes, for accounting purposes, the acquisitions of Qingdao Shoes has been treated as a recapitalization with no adjustment to the historical basis of their assets and liabilities. The restructuring has been accounted for using the "as if" pooling method of accounting and the operations were consolidated as if the restructuring had occurred as of the beginning of the earliest period presented in our consolidated financial statements and the current corporate structure had been in existence throughout the periods covered by our consolidated financial statements.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

These accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission, and should be read in conjunction with the December 31, 2009 audited financial statements of the Company and the notes thereto as included in the Company's Form PRER14C filed on April 19, 2010. In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for fair presentation of financial position and results of operations for the interim periods presented have been reflected herein. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year. Notes to the consolidated financial statements, which would substantially duplicate the disclosure required in the Company's December 31, 2009 annual financial statements have been omitted.

All significant inter-company balances and transactions have been eliminated in consolidation. Certain prior period numbers are reclassified to conform to current period presentation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“US GAAP”) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the amount of revenues and expenses during the reporting periods. Management makes these estimates using the best information available at the time the estimates are made. However, actual results could differ materially from those estimates.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash and trade receivables. As of June 30, 2010 and December 31, 2009, substantially all of the Company’s cash were held by major financial institutions located in the PRC, which management believes are of high credit quality. With respect to trade receivables, the Company generally does not require collateral for trade receivables and has not experienced any credit losses in collecting the trade receivables.

The Company operates principally in the PRC and grants credit to its customers in this geographic region. Although the PRC is economically stable, it is always possible that unanticipated events in foreign countries could disrupt the Company’s operations.

Land Use Rights

According to the laws of China, the government owns all the land in China. Companies or individuals are authorized to possess and use the land only through land use rights granted by the Chinese government. Land use rights are being amortized using the straight-line method over the lease term of the rights.

The Company paid in advance for the lease of two parcels of land consisting of approximately $243,000 and $3,682,000 for 50-year and 60-year time period, respectively. The lease period began during 2003 and 2010 and expire during 2053 and 2070, respectively. The amount is being amortized and recorded as expense over the 50-year and 60-year terms of the leases, respectively.

Comprehensive Income

The Company has adopted the provisions of ASC 220 “Reporting Comprehensive Income” which establishes standards for the reporting and display of comprehensive income, its components and accumulated balances in a full set of general purpose financial statements.

ASC 220 defines comprehensive income is comprised of net income and all changes to the statements of stockholders’ equity, except those due to investments by stockholders, changes in paid-in capital and distributions to stockholders, including adjustments to minimum pension liabilities, accumulated foreign currency translation, and unrealized gains or losses on marketable securities. The Company’s other comprehensive income arose from the effect of foreign currency translation adjustments.

Value Added Taxes

The Company is subject to value added tax ("VAT") for selling merchandise. The applicable VAT rate is 17% for products sold in the PRC. The amount of VAT liability is determined by applying the applicable tax rate to the invoiced amount of goods sold (output VAT) less VAT paid on purchases made with the relevant supporting invoices (input VAT). Under the commercial practice of the PRC, the Company pays VAT based on tax invoices issued. The tax invoices may be issued subsequent to the date on which revenue is recognized, and there may be a considerable delay between the date on which the revenue is recognized and the date on which the tax invoice is issued. In the event that the PRC tax authorities dispute the date on which revenue is recognized for tax purposes, the PRC tax office has the right to assess a penalty based on the amount of the taxes which are determined to be late or deficient, and will be expensed in the period if and when a determination is made by the tax authorities that a penalty is due.

Revenue Recognition

The Company generates revenues from the retail and wholesale of shoes. Sales revenues are recognized when the following four revenue criteria are met: persuasive evidence of an arrangement exists, delivery has occurred, the selling price is fixed or determinable, and collectability is reasonably assured. Sales are presented net of value added tax (VAT). No return allowance is made as product returns have been insignificant in all periods.

Retail sales are recognized at the point of sale to customers. Wholesale to its contracted customers are recognized as revenue at the time the product is shipped and title passes to the customer on an FOB shipping point basis. Wholesale prices are predetermined and fixed based on contractual agreements. The Company does not allow any discounts, credits, rebates or similar privileges.

Earnings per Share

Basic earnings per share is computed by dividing net income by weighted average number of shares of common stock outstanding during each period. Diluted earnings per share is computed by dividing net income by the weighted average number of shares of common stock, common stock equivalents and potentially dilutive securities outstanding during each period. At June 30, 2010 and December 31, 2009, respectively, the Company had no common stock equivalents that could potentially dilute future earnings per share.

NOTE 3 – NOTES RECEIVABLE

The Company advanced $440,100 to a third party in January 2010. The note receivable carries annual interest at 10% and matured in July 2010.

NOTE 4 – PREPAID EXPENSES

Prepaid expenses consist of the following as of June 30, 2010 and December 31, 2009:

	June 30,2010	December 31, 2009
Prepaid rent	$ 693,758	$ 18,778
Prepaid advertising fee	1,237,188	-
Prepaid maintenance fee	349,838	-
Prepaid miscellaneous fee	39,795	38,533
	$ 2,320,579	$ 57,311
Minus: current portion	651,854	57,311
Long term portion	1,668,725	-

Long term prepaid rent is for a new 15-year retail store lease. The whole amount of the lease was prepaid. Long term advertising prepayment is for advertisement contracts with period ranging from two to five years. The whole contracts amounts were prepaid. Long term maintenance prepayment is for a five-year landscaping maintenance contract and the whole contract was prepaid.

NOTE 5 – INTANGIBLE ASSETS

Intangible assets consist of the following land use right as of June 30, 2010 and December 31, 2009:

	June 30, 2010	December 31, 2009

Cost of land use right	3,925,545	242,055
Less: accumulated amortization	51,801	33,888
Land use rights, net	$ 3,873,744	$ 208,167

Amortization expense for the three and six months ended June 30, 2010 and 2009 was $16,491, $17,701, $1,210 and $2,420, respectively.

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

2010 (for the remaining six months)	$ 32,980
2011	65,962
2012	65,962
2013	65,962
2014	65,962
2015	65,962
Thereafter	3,510,954
Total	$ 3,873,744

In April 2010, the Company purchased land use rights in Jimo, Shandong Province for $3,682,500. By June 30, 2010, $2,659,045 has been paid in cash. The company is still in the process of obtaining the title of the land use right.

NOTE 6 - SHORT TERM LOANS

Short-term loans are due to two financial institutions which are normally due within one year. As of June 30, 2010 and December 31, 2009, the Company's short term loans consisted of the following:

	June 30, 2010	December 31, 2009
JMRB, two 12-month bank loans both due in November 2010, bears annual interest at 7.965% average, secured by third parties	294,600	293,400
BOQ, 12-month bank loan due in September 2010, bears annual interest at 6.372% average, pledged by Company's building and land use right	427,170	425,430
JMRB, 12-month bank loan due in December 2010, bears annual interest at 7.965% average, secured by third parties	441,900	-
Total short-term debt	$ 1,163,670	$ 718,830

The above indebtedness to JMRB at June 30, 2010 and December 31, 2009 has been guaranteed by two unrelated companies.

NOTE 7 – LONG TERM LOANS

On December 16, 2009, the Company entered into a 2-year loan agreement with JMRB. The Company borrowed $250,410 with an annual interest rate equal to 7.02% and is due in December 2011. The loan is guaranteed by the relatives of Mr. Tao Wang, the CEO and major shareholder of the Company and is collateralized by the property of his relatives.

NOTE 8- RELATED PARTY BALANCES AND TRANSCATIONS

Due to related party

At December 31, 2009, the amount due to Mr. Tao Wang, the CEO and major shareholder of the Company amounted to $104,511. These borrowings bear no interest and were paid off in first quarter 2010.

At December 31, 2009, the dividend payable to Mr. Renwei Ma, the shareholder of the Company was $117,360, which was paid off in the first quarter of 2010.

Due to related party at June 30, 2010 is nil.

Related party transactions

The Company leases one of its stores from Mr. Tao Wang under a four-year operating lease expiring August 2011. For the six months ended June 2010 and 2009, related party rent expense of $8,800 and $8,794, respectively, was included in total rent expense of the year.

The Company leases one of its warehouse buildings to Weidong, Liang, brother-in-law of Mr. Tao Wang, for three years starting May 2008. Per the agreement, the lessee shall pay equal amount of advertising expense on behalf of the lessor as the lease payment. For the six months ended June 30, 2010 and 2009, the Company recorded other income of $44,007 and $43,971 respectively, from leasing the aforementioned building and advertising expense of the same amount respectively.

NOTE 9 - INCOME TAX

The Company is governed by the Income Tax Law of the PRC concerning the private-run enterprises, which are generally subject to tax at a statutory rate of 25% on income reported in the statutory financial statements.

	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Income before income taxes	$ 4,019,366	$ 3,695,300
Income taxes	$	