NOVACK DEBORAH S
Form 4
April 28, 2010

FORM 4

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. *See* Instruction 1(b).

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

STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

OMB APPROVAL

OMB Number:	3235-0287
Expires:	January 31, 2005
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(Print or Type Responses)

1. Name and Address of Reporting Person *
NOVACK KENNETH M
(Last) (First) (Middle)
3200 NW YEON AVENUE
(Street)
PORTLAND, OR 97210
(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
SCHNITZER STEEL INDUSTRIES INC [SCHN]

3. Date of Earliest Transaction (Month/Day/Year)
04/26/2010

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer
(Check all applicable)
__X__ Director __X__ 10% Owner
_____ Officer (give title below) _____ Other (specify below)

6. Individual or Joint/Group Filing(Check Applicable Line)
___ Form filed by One Reporting Person
_X_ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1.Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Class A Common Stock								300	I	See Note (1)
Class A Common Stock								13,958.295	I	See Note (2)
Class A Common Stock	04/26/2010		C		10,000	A	$ 0	10,000	I	By Voting Trust (4)
Class A Common	04/26/2010		Z	V	10,000	D	$ 0	0	I	By Voting Trust (4)

Stock										
Class A Common Stock	04/26/2010		Z	V	10,000	A	$ 0	10,000	I	By Trust (4)
Class A Common Stock	04/26/2010		S		100	D	$ 59.26	9,900	I	By Trust (4)
Class A Common Stock	04/26/2010		S		100	D	$ 59.27	9,800	I	By Trust (4)
Class A Common Stock	04/26/2010		S		400	D	$ 59.28	9,400	I	By Trust (4)
Class A Common Stock	04/26/2010		S		200	D	$ 59.29	9,200	I	By Trust (4)
Class A Common Stock	04/26/2010		S		500	D	$ 59.3	8,700	I	By Trust (4)
Class A Common Stock	04/26/2010		S		200	D	$ 59.33	8,500	I	By Trust (4)
Class A Common Stock	04/26/2010		S		200	D	$ 59.35	8,300	I	By Trust (4)
Class A Common Stock	04/26/2010		S		100	D	$ 59.37	8,200	I	By Trust (4)
Class A Common Stock	04/26/2010		S		300	D	$ 59.38	7,900	I	By Trust (4)
Class A Common Stock	04/26/2010		S		100	D	$ 59.39	7,800	I	By Trust (4)
Class A Common Stock	04/26/2010		S		600	D	$ 59.4	7,200	I	By Trust (4)
Class A Common Stock	04/26/2010		S		100	D	$ 59.41	7,100	I	By Trust (4)
Class A Common Stock	04/26/2010		S		300	D	$ 59.42	6,800	I	By Trust (4)

Class A Common Stock	04/26/2010		S	200	D	$ 59.43	6,600	I	By Trust (4)
Class A Common Stock	04/26/2010		S	200	D	$ 59.44	6,400	I	By Trust (4)
Class A Common Stock	04/26/2010		S	100	D	$ 59.46	6,300	I	By Trust (4)
Class A Common Stock	04/26/2010		S	100	D	$ 59.47	6,200	I	By Trust (4)
Class A Common Stock	04/26/2010		S	200	D	$ 59.48	6,000	I	By Trust (4)
Class A Common Stock	04/26/2010		S	2,910	D	$ 59.5	3,090	I	By Trust (4)
Class A Common Stock	04/26/2010		S	379	D	$ 59.51	2,711	I	By Trust (4)
Class A Common Stock	04/26/2010		S	400	D	$ 59.52	2,311	I	By Trust (4)
Class A Common Stock	04/26/2010		S	100	D	$ 59.53	2,211	I	By Trust (4)
Class A Common Stock	04/26/2010		S	400	D	$ 59.54	1,811	I	By Trust (4)
Class A Common Stock	04/26/2010		S	711	D	$ 59.55	1,100	I	By Trust (4)
Class A Common Stock	04/26/2010		S	400	D	$ 59.56	700	I	By Trust (4)

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)		6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and Amount of Underlying Securities (Instr. 3 and 4)		8. P Deri Secu (Ins
				Code	V	(A)	(D)	Date Exercisable	Expiration Date	Title	Amount or Number of Shares	
Class B Common Stock	(3)	04/26/2010		C			10,000	(3)	(3)	Class A Common Stock	10,000	
Class B Common Stock	(3)							(3)	(3)	Class A Common Stock	19,302	
Class B Common Stock	(3)							(3)	(3)	Class A Common Stock	12,556	
Class B Common Stock	(3)							(3)	(3)	Class A Common Stock	25,333	

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
NOVACK KENNETH M 3200 NW YEON AVENUE PORTLAND, OR 97210	X	X		
NOVACK DEBORAH S 3200 NW YEON AVENUE PORTLAND, OR 97210		X		

Signatures

Richard C. Josephson, Attorney-In-Fact	04/27/2010
**Signature of Reporting Person	Date

Explanation of Responses:

* If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).

** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

(1) Shares are held by Kevin P. Novack, an immediate family member of the reporting persons who may be deemed to share the same household.

(2)

Deferred Shares that have been or will be credited to the reporting person's account under the issuer's Deferred Compensation Plan for Non-Employee Directors.

(3) Class B Common Stock is immediately convertible on a one-for-one basis into Class A Common Stock and has no expiration date.

(4) Voting trust certificates or shares, as the case may be, are held by Kenneth M. Novack and Deborah S. Novack, Trustees of the Hidden Valley Trust Agreement, under Trust Agreement dated December 11, 2006.

(5) Voting trust certificates or shares, as the case may be, are held by the 1997 Melanie Novack Trust, dated 8/17/97, Deborah S. Novack and Kenneth M. Novack, collectively as Trustees.

(6) Voting trust certificates or shares, as the case may be, are held by the 1997 Kevin Novack Trust, dated 8/17/97, Deborah S. Novack and Kenneth M. Novack, collectively as Trustees.

(7) Voting Trust Certificates or shares, as the case may be, are held by Gary A. Schnitzer and Deborah Novack, Trustees, Gary A. Schnitzer Family Trust dated May 15, 1991.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure.
Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. bottom" style="PADDING-BOTTOM: 2px">

2008

CASH FLOWS FROM OPERATING ACTIVITIES:

Net income

$

8,064,379

$

6,321,463

Adjustments to reconcile net income to net cash

provided by operating activities:

Depreciation and amortization

2,782,209

1,358,378

Loss on disposal of equipment

21,370

12,134

Amortization of discount on senior notes

217,196

459,473

Amortization of financing costs

	52,435	122,592
Stock based compensation	100,758	38,896
Change in fair value of warrants	1,115,783	-
Change in assets and liabilities:		
Accounts receivable	(74,409)	(513,994)
Other receivable - employee advances	109,963	101,267
Inventories	(487,908)	(269,136)
Advances to suppliers	(268,922)	(279,741)
Prepaid expense and other current assets	157,372	(637,244)

Accounts payable and accrued liabilities	822,997	(11,440)
Other payables	73,210	8,525
Unearned revenue	1,026,693	530,551
Accrued interest	376,664	454,164
Taxes payable	306,975	430,244
Net cash provided by operating activities	14,396,765	8,126,132
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(21,033)	(12,471,764)
Proceeds from sales of property and equipment	41,305	-

Proceeds from short term investments	-	246,802
Additions to construction in progress	(10,372,858)	(11,736,887)
Change in prepayment on long term assets	(110,836)	(3,559,485)
Return of acquisition deposit	449,910	
Payment for intangible assets	(66,971)	-
Payment for land use rights	(463,870)	(36,341)
Increase in stockholder receivable	-	(2,836,800)
Net cash used in investing activities	(10,544,353)	(30,394,475)

CASH FLOWS FROM FINANCING ACTIVITIES:

Proceeds from senior notes

-

40,000,000

Payment for offering costs

-

(2,122,509
)

Net cash provided by financing activities

-

37,877,491

Effect of exchange rate changes on cash and cash equivalents

(5,619
)

279,438

NET INCREASE IN CASH & CASH EQUIVALENTS

3,846,793

15,888,586

CASH & CASH EQUIVALENTS, BEGINNING OF PERIOD

5,854,383

13,291,729

CASH & CASH EQUIVALENTS, END OF PERIOD

$
9,701,176

$
29,180,315

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

Interest paid, net of capitalized interest

$	237,641
$	-
Income taxes paid	
$	1,934,887
$	1,203,048

The accompanying notes are an integral part of these statements

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China Natural Gas, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
June 30, 2009
(Unaudited)

Note 1 - Organization

Organization and Line of Business

China Natural Gas, Inc. (the "Company" or "CHNG") was incorporated in the state of Delaware on March 31, 1999. The Company through its wholly-owned subsidiaries and variable interest entities, located in Shaanxi and Henan Province in the People's Republic of China ("PRC"), engages in sales and distribution of natural gas and gasoline to commercial, industrial and residential customers, construction of pipeline networks, installation of natural gas fittings and parts for end-users, and modification of automobiles services for vehicles to be able to use natural gas.

Recent Developments

On March 18, 2008, Shaanxi Xilan Natural Gas Equipment Co., Ltd ("SXNGE") increased its registered capital from $30,000,000 to $53,929,260. The additional $14,429,260 of registered capital was contributed by China Natural Gas, Inc. on April 17, 2008 and $9,500,000 of registered capital was contributed by China Natural Gas, Inc. as a payment to Chemtex International Inc. on January 31, 2008, for the purchase of license, know-how, and design of constructing the Liquefied Natural Gas ("LNG") processing plant.

On April 22, 2008, Jingbian Liquefied Natural Gas Co., Ltd. ("JBLNG") increased its registered capital by $2,862,000. JBLNG is 100% owned by Xi'an Xilan Natural Gas Co., Ltd.

On April 30, 2008, the Industrial and Commercial Administration Bureau approved Xi'an Xilan Natural Gas Co., ("XXNGC") to increase registered capital from $8,336,856 to $43,443,640 as an additional contribution by the shareholders of XXNGC under PRC Law. $15,513,526 was approved by the Industrial and Commercial Administration Bureau to be transferred out from the surplus reserve and retained earnings as an increase of registered capital. Another $19,593,258 was contributed by SXNGE cumulatively prior to April 30, 2008, which was previously classified as an intercompany payable in XXNGC and was eliminated in the consolidated financial statements. The increase in registered capital in XXNGC was in compliance with the Addendum to Option Agreement entered by the Company through SXNGE and XXNGC, Mr. Qinan Ji, chairman and shareholder of XXNGC, and each of the shareholders of XXNGC (hereafter collectively referred to as the "Transferor") on August 8, 2008, and made retroactive to June 30, 2008. See "Consolidation of Variable Interest Entity" section for further detail on the Addendum to Option Agreement.

On July 3, 2008, XXNGC formed Henan Xilan Natural Gas Co., Ltd. ("HXNGC") as a wholly owned limited liability company, with registered capital of $4,383,000 in Henan province, PRC. HXNGC was established for the purpose of natural gas city gasification engineering design, construction and technical advisory work services in Henan, PRC.

On October 2, 2008, China Natural Gas, Inc. (the "Company") through its wholly-owned subsidiary, XXNGC, entered into an Equity Ownership Transfer Agreement (the "Acquisition Agreement") with Lingbao Yuxi Natural Gas Co., Ltd. ("LBNGC") and the shareholders of LBNGC (the "Sellers"). Pursuant to the term of the Acquisition Agreement, XXNGC acquired for cash consideration of approximately $19,604,200 (RMB 134 million), 100% of all outstanding registered equity interest in LBNGC and all assets held by LBNGC, including the land use right to 0.44 acres and all of LBNGC's local business' exclusive operating rights. LBNGC owns the exclusive rights to operate CNG fueling stations and pipelines in Lingbao City. In conjunction with this acquisition, XXNGC has also secured an abundant supply of

natural gas to support its future expansion in the Henan province. The Acquisition Agreement was fully executed in November, 2008.

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Note 2 – Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America. The Company's functional currency is the Chinese Renminbi ("RMB"); however, the Company's reporting currency is the United States Dollar ("USD"); therefore, the accompanying consolidated financial statements have been translated and presented in USD.

In the opinion of management, the unaudited consolidated financial statements furnished herein include all adjustments, all of which are of a normal recurring nature, necessary for a fair statements of the results for the interim period presented. Operating results for the period ended June 30, 2009 are not necessary indicative of the results that may be expected for the year ended December 31, 2009. The information included in this Form 10-Q should be read in conjunction with information included in the 2008 annual report filed on Form 10-K/A.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of China Natural Gas, Inc. and its wholly owned subsidiary, Shaanxi Xilan Natural Gas Equipment Co., Ltd and its 100% variable interest entities ("VIE"), Xi'an Xilan Natural Gas Co. Ltd., Jingbian Liquefied Natural Gas Co., Ltd., Shaanxi Xilan Auto Bodyshop Co., Ltd. ("SXABC"), Henan Xilan Natural Gas Co., Ltd., and Lingbao Yuxi Natural Gas Co., Ltd. All inter-company accounts and transactions have been eliminated in the consolidation.

Consolidation of Variable Interest Entity

In accordance with Financial Interpretation No. 46R, Consolidation of Variable Interest Entities ("FIN 46R"), VIEs are generally entities that lack sufficient equity to finance their activities without additional financial support from other parties or whose equity holders lack adequate decision making ability. All VIEs with which the Company is involved must be evaluated to determine the primary beneficiary of the risks and rewards of the VIE. The primary beneficiary is required to consolidate the VIE for financial reporting purposes.

On February 21, 2006, the Company formed Shaanxi Xilan Natural Gas Equipment Co., Ltd as a wholly-owned foreign enterprise (WOFE). Then through SXNGE, the Company entered into exclusive arrangements with Xi'an Xilan Natural Gas and its shareholders that give the Company the ability to substantially influence Xi'an Xilan Natural Gas' daily operations and financial affairs, appoint its senior executives and approve all matters requiring shareholder approval. The Company memorialized these arrangements on August 17, 2007 and made retroactive to March 8, 2006. As a result, the Company consolidates the financial results of Xi'an Xilan Natural Gas as variable interest entity pursuant to Financial Interpretation No. 46R, "Consolidation of Variable Interest Entities." The arrangements consist of the following agreements:

a. Xi'an Xilan Natural Gas holds the licenses and approvals necessary to operate its natural gas business in China.

b. SXNGE provides exclusive technology consulting and other general business operation services to Xi'an Xilan Natural Gas in return for a consulting services fee which is equal to Xi'an Xilan Natural Gas's revenue.

c. Xi'an Xilan Natural Gas' shareholders have pledged their equity interests in Xi'an Xilan Natural Gas to the Company.

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d. Irrevocably granted the Company an exclusive option to purchase, to the extent permitted under PRC law, all or part of the equity interests in Xi'an Xilan Natural Gas and agreed to entrust all the rights to exercise their voting power to the person appointed by the Company.

On August 8, 2008, the Company through SXNGE entered into an Addendum to Option Agreement with Mr. Qinan Ji, chairman and shareholder of XXNGC, and each of the shareholders of XXNGC (hereafter collectively referred to as the "Transferor"), and made retroactive to June 30, 2008. According to the Agreement, the Chairman and the Shareholders of XXNGC irrevocably grants to SXNGE an option to purchase each Transferor's Purchased Equity Interest at $1.00 or the lowest price permissible under the applicable laws at the time that SXNGE exercises the Option. The Agreement limits XXNGC and the transferors' right to make all equity interest related decisions.

Foreign Currency Translation

As of June 30, 2009 and December 31, 2008, the accounts of the Company were maintained, and their consolidated financial statements were expressed in RMB. Such consolidated financial statements were translated into USD in accordance with Statement of Financial Accounts Standards ("SFAS") 52, "Foreign Currency Translation," with the RMB as the functional currency. According to SFAS 52, all assets and liabilities were translated at the exchange rate as of the balance sheet date, stockholders' equity were translated at the historical rates and statement of income and cash flow items were translated at the weighted average exchange rate for the year. The resulting translation adjustments are reported under other comprehensive income in accordance with SFAS 130, "Reporting Comprehensive Income." In accordance with SFAS 95, "Statement of Cash Flows," cash flows from the Company's operations are calculated based upon the local currencies and translated to USD at average translation rates for the period. As a result, translation adjustments amount related to assets and liabilities reported on the consolidated statement of cash flows will not necessarily agree with changes in the corresponding consolidated balances on the balance sheet.

The balance sheet amounts with the exception of equity at June 30, 2009, were translated 6.83 RMB to $1.00 as compared to 6.82 RMB at December 31, 2008. The equity accounts were stated at their historical rate. The average translation rates applied to income and cash flow statement amounts for the six months ended June 30, 2009 and 2008, were 6.82 RMB and 7.05 RMB to $1.00, respectively.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and demand deposits in accounts maintained with state-owned banks within the PRC and the United States. The Company considers all highly liquid investments with original maturities of three months or less at the time of purchase to be cash equivalents.

Certain financial instruments, which subject the Company to concentration of credit risk, consist of cash. The Company maintains balances at financial institutions which, from time to time, may exceed Federal Deposit Insurance Corporation insured limits for the banks located in the United States. Balances at financial institutions or state-owned banks within the PRC are not covered by insurance. As of June 30, 2009 and December 31, 2008, the Company had total deposits of $9,528,913 and $5,604,383 without insurance coverage. And as of June 30, 2009 and December 31, 2008, the Company had deposits in the United States of $0 and $1,273,639 in excess of federally insured limits, respectively. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant risks on its cash in bank accounts.

Accounts Receivable

Accounts and other receivable are netted against an allowance for uncollectible accounts, as needed. The Company maintains reserves for potential credit losses on accounts receivable. Management reviews the composition of accounts receivable and analyzes historical bad debts, customer concentrations, customer credit worthiness, current economic trends and changes in customer payment patterns to evaluate the adequacy of these reserves. Reserves are recorded primarily on a specific identification basis in the period of the related sales. Delinquent account balances are written-off after management has determined that the likelihood of collection is not probable, and known bad debts are written off against allowance for doubtful accounts when identified. The Company's management has determined that all receivables are collectible and there is no need for an allowance for uncollectible accounts as of June 30, 2009, and December 31, 2008.

Other Receivable – Employee Advances

From time to time, the Company advances predetermined amounts based upon internal Company policy to certain employees and internal units to ensure certain transactions are performed in a timely manner. The Company has full oversight and control over the advanced accounts. As of June 30, 2009 and December 31, 2008, no allowance for the uncollectible accounts was deemed necessary.

Inventory

Inventory is stated at the lower of cost, as determined on a first-in, first-out basis, or market. Management compares the cost of inventories with the market value, and an allowance is made for writing down the inventories to their market value, if lower. Inventory consists of material used in the construction of pipelines and material used in repairing and modifying vehicles. Inventory also consists of gasoline.

The following are the details of the inventories:

	June 30, 2009 (Unaudited)	December 31, 2008
Materials and supplies	$ 829,466	$ 318,069
Gasoline	367,325	201,670
	$ 1,196,791	$ 519,739

Advances to Suppliers

The Company advances to certain vendors for purchase of its materials. The advances are interest-free and unsecured.

Loan Receivable

Loan receivable consists of the following:

	June 30, 2009 (Unaudited)	December 31, 2008
Shanxi Yuojin Mining Company, due on November 26, 2008, extended to November 30, 2009, annual interest at 6.57%	$ 293,000	$ 293,400

Property and Equipment

Property and equipment are stated at cost. Expenditures for maintenance and repairs are charged to earnings as incurred while additions, renewals and betterments are capitalized. When property and equipment are retired or otherwise disposed of, the related cost and accumulated depreciation are removed from the respective accounts, and any gain or loss is included in operations. Depreciation of property and equipment is provided using the straight-line method for substantially all assets with estimated lives as follows:

Office equipment	5 years
Operating equipment	5-20 years
Vehicles	5 years
Buildings and improvements	5-30 years

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Explanation of Responses:

The following are the details of the property and equipment:

	June 30, 2009 (Unaudited)	December 31, 2008
Office equipment	$ 422,892	$ 412,490
Operating equipment	59,396,860	59,473,283
Vehicles	2,295,579	2,414,756
Buildings and improvements	21,167,110	21,190,599
Total property and equipment	83,282,441	83,491,128
Less accumulated depreciation	(10,177,671)	(7,462,856)
Property and equipment, net	$ 73,104,770	$ 76,028,272

Depreciation expense for the three months ended June 30, 2009 and 2008 was $1,390,017 and $701,854, respectively. Depreciation expense for the six months ended June 30, 2009 and 2008 was $2,779,582 and $1,358,378, respectively.

Construction in Progress

Construction in progress ("CIP") consists of the cost of constructing property and equipment for the Company's gas stations and a new project of processing, distribution and sale of LNG. The major cost of construction in progress relates to technology licensing fees, equipment purchase, land use rights requisition cost, capitalized interest and other construction fees. No depreciation is provided for construction in progress until such time as the assets are completed and placed into service. Interest incurred during construction is capitalized into construction in progress. All other interest is expensed as incurred.

As of June 30, 2009 and December 31, 2008, the company had construction in progress in the amount of $33,644,992 and 22,061,414, respectively. Interest cost capitalized into construction in progress for the three months ended June 30, 2009 and 2008, amounted to $1,172,547 and $491,856, respectively. Interest cost capitalized into construction in progress for the six months ended June 30, 2009 and 2008, amounted to $2,030,926 and $682,504, respectively

Construction in progress at June 30, 2009 consisted of the following:

No.	Project Description	Location	June 30, 2009 (Unaudited)	Commencement date	Expected completion date	Estimated additional cost to be completed
1	Jingbian LNG	JBLNG	$ 26,794,348	Dec-06	Dec-09	$ 13,000,000
2	Shuan Fu mother station	HXNGC	722,802	Jul-08	Jun-11	6,680,000
3	Zijing Energy mother station	XXNGC	4,087,998	Sep-08	May-11	3,440,000
4	Xi'an Cangsheng mother station	XXNGC	1,835,428	Sep-08	May-11	3,220,000
5	Other CIP projects	XXNGC	204,416	Various	Oct-09	2,250,000
			$ 33,644,992			$ 28,590,000

Long-Lived Assets

The Company applies the provision of SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" to all long lived assets. SFAS 144 addresses accounting and reporting for impairment and disposal of long-lived assets. The Company evaluates at least annually, more often when circumstances require, 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 June 30, 2009, there were no significant impairments of its long-lived assets.

Unearned Revenue

Unearned revenue represents prepayments by customers for gas purchases and advance payments on installation of pipeline contracts. The Company records such prepayment as unearned revenue when the payments are received.

Fair Value of Financial Instruments

FAS 107, “Disclosure About Fair Value of Financial Instruments” defines financial instruments and requires fair value disclosure of applicable financial instruments. FAS 157, “Fair Value Measurements,” adopted January 1, 2008, defines fair value, establishes a three-level valuation hierarchy for disclosures of fair value measurement and enhances disclosure requirements for fair value measures. The carrying amounts reported in the consolidated balance sheets for current receivables and payables qualify as financial instruments. Management concluded the carrying values are a reasonable estimate of fair value because of the short period of time between the origination of such instruments and their expected realization and if applicable, their stated interest rate approximates current rates available. The three levels are defined as follows:

Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Company analyzes all financial instruments with features of both liabilities and equity under SFAS 150, “Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity,” SFAS 133, “Accounting for Derivative Instruments and Hedging Activities” and EITF 00-19, “Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company’s Own Stock.”

Effective January 1, 2009, the Company adopted the provisions of EITF 07-5, "Determining Whether an Instrument (or Embedded Feature) is Indexed to an Entity’s Own Stock”, which is effective for financial statements for fiscal years beginning after December 15, 2008 and which replaced the previous guidance on this topic in EITF 01-6. Paragraph 11(a) of FAS 133 specifies that a contract that would otherwise meet the definition of a derivative but is both (a) indexed to the Company’s own stock and (b) classified in stockholders’ equity in the statement of financial position would not be considered a derivative financial instrument. EITF 07-5 provides a new two-step model to be applied in determining whether a financial instrument or an embedded feature is indexed to an issuer’s own stock and thus able to qualify for the FAS 133 paragraph 11(a) scope exception.

As a result of adopting EITF 07-5, 383,654 warrants previously treated as equity pursuant to the derivative treatment exemption are no longer afforded equity treatment because the strike price of the warrants is denominated in US dollar, a currency other than the Company’s functional currency, the Chinese Renminbi. As a result, the warrants are not considered indexed to the Company’s own stock, and as such, all future changes in the fair value of these warrants will be recognized currently in earnings until such time as the warrants are exercised or expire.

As such, effective January 1, 2009, the Company reclassified the fair value of these warrants from equity to liability, as if these warrants were treated as a derivative liability since their issuance in October 2007. On January 1, 2009, the Company reclassified from additional paid-in capital, as a cumulative effect adjustment, $5,844,239 to beginning retained earnings and $1,014,308 to warrant liabilities to recognize the fair value of such warrants. The fair value of

the warrants was $2,130,091 on June 30, 2009. The Company recognized a $1,312,834 loss from the change in fair value of the three months ended June 30, 2009. The Company recognized a $1,115,783 loss from the change in fair value of warrants for the six months ended June 30, 2009.

These common stock purchase warrants do not trade in an active securities market, and as such, we estimate the fair value of these warrants using the Black-Scholes Option Pricing Model using the following assumptions:

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	June 30, 2009 (Unaudited)	January 1, 2009
Annual dividend yield	-	-
Expected life (years)	3.32	3.82
Risk-free interest rate	1.50%	1.13%
Expected volatility	90%	90%

Expected volatility is based on historical volatility. Historical volatility was computed using daily pricing observations for recent periods that correspond to the term of the warrants. The Company believes this method produces an estimate that is representative of our expectations of future volatility over the expected term of these warrants. The Company has no reason to believe future volatility over the expected remaining life of these warrants is likely to differ materially from historical volatility. The expected life is based on the remaining term of the warrants. The risk-free interest rate is based on U.S. Treasury securities according to the remaining term of the warrants.

As required by SFAS 157, financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Depending on the product and the terms of the transaction, the fair value of the notes payable and derivative liabilities were modeled using a series of techniques, including closed-form analytic formula, such as the Black-Scholes Option Pricing Model, which does not entail material subjectivity because the methodology employed does not necessitate significant judgment, and the pricing inputs are observed from actively quoted markets.

The following table sets forth by level within the fair value hierarchy of the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis as of June 30, 2009.

	Carrying Value at June 30, 2009 (Unaudited)	Fair Value Measurement at June 30, 2009 (Unaudited)		
		Level 1	Level 2	Level 3
Senior notes	$ 25,832,666	$ -	$ -	$ 34,660,250
Redeemable liability - warrants	17,500,000	-	-	14,911,024
Derivative liability - warrants	2,130,091	-	2,130,091	-
Total liability measured at fair value	$ 45,462,757	$ -	$ 2,130,091	$ 49,571,274

Other than the derivative liabilities - warrants carried at fair value, the Company did not identify any other assets and liabilities that are required to be presented on the balance sheet at fair value in accordance with SFAS 157.

Revenue Recognition

The Company's revenue recognition policies are in accordance with Staff Accounting Bulletin (SAB) 104. Revenue is recognized when services are rendered to customers when a formal arrangement exists, the price is fixed or determinable, the delivery is completed, no other significant obligations of the Company exist and collectability is reasonably assured. Payments received before all of the relevant criteria for revenue recognition are satisfied are recorded as unearned revenue. Revenue from gas and gasoline sales is recognized when gas and gasoline is pumped through pipelines to the end users. Revenue from installation of pipelines is recorded when the contract is completed and accepted by the customers. The construction contracts are usually completed within one to two months. Revenue from repairing and modifying vehicles is recorded when services are rendered to and accepted by the customers.

Enterprise Wide Disclosure

The Company's chief operating decision-makers (i.e. chief executive officer and his direct reports) review financial information presented on a consolidated basis, accompanied by disaggregated information about revenues by business lines for purposes of allocating resources and evaluating financial performance. There are no segment managers who are held accountable for operations, operating results and plans for levels or components below the consolidated unit level. Based on qualitative and quantitative criteria established by SFAS 131, "Disclosures about Segments of an Enterprise and Related Information", the Company considers itself to be operating within one reportable segment.

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Advertising Costs

The Company expenses the cost of advertising as incurred or, as appropriate, the first time the advertising takes place. Advertising costs for the three and six months ended June 30, 2009 and 2008, were insignificant.

Stock-Based Compensation

The Company records and reports stock-based compensation pursuant to SFAS 123R "Accounting for Stock-Based Compensation", which defines a fair-value-based method of accounting for stock-based employee compensation and transactions in which an entity issues its equity instruments to acquire goods and services from non-employees. Stock compensation for stock granted to non-employees has been determined in accordance with SFAS 123R and EITF 96-18, "Accounting for Equity Instruments that are issued to Other than Employees for Acquiring, or in Conjunction with Selling Goods or Services", as the fair value of the consideration received or the fair value of equity instruments issued, whichever is more reliably measured.

Income Taxes

The Company utilizes SFAS 109, "Accounting for Income Taxes," which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred income taxes are recognized for the tax consequences in future years of temporary differences between the tax bases of assets and liabilities and their financial reporting amounts at each period end based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized. At June 30, 2009 and December 31, 2008, there was no significant book to tax differences. There is no difference between book depreciation and tax depreciation as the Company uses the same method for both book and tax. The Company adopted FASB Interpretation 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"), as of January 1, 2007. A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded. The adoption had no affect on the Company's consolidated financial statements.

Local PRC Income Tax

The Company's subsidiary and VIEs operate in China. Starting January 1, 2008, pursuant to the tax laws of China, general enterprises are subject to income tax at an effective rate of 25% compared to 33% prior to 2008. The Company's VIE, XXNGC, is in the natural gas industry whose development is encouraged by the government. According to the income tax regulation, any company engaged in the natural gas industry enjoys a favorable tax rate. Accordingly, except for income from SXNGE, JBLNG, SXABC, HXNGC and LBNGC which subjects to 25% PRC income tax rate, XXNGC's income is subject to a reduced tax rate of 15%. A reconciliation of tax at the United States federal statutory rate to the provision for income tax recorded in the financial statements is as follows:

	For the three months ended June 30,		For the six months ended June 30,	
	2009 (Unaudited)	2008 (Unaudited)	2009 (Unaudited)	2008 (Unaudited)
Tax provision (credit) at statutory rate	34%	34%	34%	34%
Foreign tax rate difference	(9)%	(9)%	(9)%	(9)%

Effect of favorable tax rate	(9)%	(10)%	(9)%	(10)%
Other item (1)	8%	5%	5%	5%
Total provision for income taxes	24%	20%	21%	20%

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(1) The 8% represents $2,198,394 in expenses incurred by CHNG are not deductible in PRC for the three months ended June 30, 2009. The 5% represents $1,573,125 expenses incurred by CHNG that are not deductible in PRC for the three months ended June 30, 2008. The 5% represents $3,124,589 in expenses incurred by CHNG that are not deductible in PRC for the six months ended June 30, 2009. The 5% represents $2,578,448 expenses incurred by CHNG that are not deductible in PRC for the six months ended June 30, 2008.

The estimated tax savings for the three months ended June 30, 2009 and 2008, amounted to approximately $721,445 and $531,372, respectively. The net effect on earnings per share, had the income tax been applied, would decrease basic and diluted earnings per share for the three months ended June 30, 2009 and 2008, from $0.26 to $0.21 and $0.24 to $0.20, respectively.

The estimated tax savings for the six months ended June 30, 2009 and 2008, amounted to approximately $1,231,776 and $933,423, respectively. The net effect on earnings per share, had the income tax been applied, would decrease basic and diluted earnings per share for the six months ended June 30, 2009 and 2008, from $0.55 to $0.47 and $0.43 to $0.37, respectively.

China Natural Gas, Inc. was incorporated in the United States and has incurred net operating loss for income tax purpose for the period ended June 30, 2009. The estimated net operating loss carry forwards for United States income tax purposes amounted to $1,913,731 and $1,657,473 as of June 30, 2009 and December 31, 2008, respectively, which may be available to reduce future years' taxable income. These carry forwards will expire, if not utilized, beginning in 2027 through 2029. Management believes that the realization of the benefits arising from this loss appear to be uncertain due to Company's limited operating history and continuing losses for United States income tax purposes. Accordingly, the Company has provided a 100% valuation allowance at June 30, 2009. Management reviews this valuation allowance periodically and makes adjustments as warranted. The valuation allowances were as follow:

Valuation allowance	Six months ended June 30, 2009 (Unaudited)	Year ended December 31, 2008
Balance, beginning of period	$ 563,541	$ 322,614
Increase	87,128	240,927
Balance, end of period	$ 650,669	$ 563,541

The Company has cumulative undistributed earnings of foreign subsidiaries of approximately $26,324,000 as of June 30, 2009, which is included in consolidated retained earnings and will continue to be indefinitely reinvested in international operations. Accordingly, no provision has been made for U.S. deferred taxes related to future repatriation of these earnings, nor is it practicable to estimate the amount of income taxes that would have to be provided if we concluded that such earnings will be remitted in the future.

Value added tax

Sales revenue represents the invoiced value of goods, net of a value-added tax (“VAT”). All of the Company’s variable interest entity XXNGC’s products that are sold in the PRC are subject to a Chinese value-added tax at a rate of 13% of the gross sales price. This VAT may be offset by VAT paid by the XXNGC on raw materials and other materials included in the cost of producing their finished product. XXNGC recorded VAT payable and VAT receivable net of payments in the financial statements. The VAT tax return is filed offsetting the payables against the receivables.

All revenues from SXABC are subject to a Chinese VAT at a rate of 6%. This VAT cannot offset with VAT paid for materials included in the cost of revenues.

Basic and Diluted Earnings Per Share

Earnings per share is calculated in accordance with the SFAS 128, “Earnings per share”. Basic net earnings per share is based upon the weighted average number of common shares outstanding. Diluted net earnings per share is based on the assumption that all dilutive convertible shares and stock options were converted or exercised. Dilution is computed by applying the treasury stock method. Under this method, options and warrants are assumed to be exercised at the beginning of the period (or at the time of issuance, if later), and as if funds obtained thereby were used to purchase common stock at the average market price during the period.

All share and per share amounts used in the Company's consolidated financial statements and notes thereto have been retroactively restated to reflect the 1-for-2 reverse stock split, which were effective on April 28, 2009.

Reclassifications

Certain prior period amounts have been reclassified to conform to current period’s presentation. These reclassifications had no material effect on net income or cash flows as previously reported.

Recently issued accounting pronouncements

In January 2009, the FASB issued FSP EITF 99-20-1, “Amendments to the Impairment Guidance of EITF Issue No. 99-20, “Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets.” FSP EITF 99-20-1 changes the impairment model included within EITF 99-20 to be more consistent with the impairment model of SFAS No. 115. FSP EITF 99-20-1 achieves this by amending the impairment model in EITF 99-20 to remove its exclusive reliance on “market participant” estimates of future cash flows used in determining fair value. Changing the cash flows used to analyze other-than-temporary impairment from the “market participant” view to a holder’s estimate of whether there has been a “probable” adverse change in estimated cash flows allows companies to apply reasonable judgment in assessing whether an other-than-temporary impairment has occurred. The adoption of FSP EITF 99-20-1 did not have a material impact on the Company’s consolidated financial statements.

In April 2009, the FASB issued FSP FAS 157-4, “Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly” (FSP FAS 157-4). FSP FAS 157-4 amends SFAS 157 and provides additional guidance for estimating fair value in accordance with SFAS 157 when the volume and level of activity for the asset or liability have significantly decreased and also includes guidance on identifying circumstances that indicate a transaction is not orderly for fair value measurements. This FSP shall be applied prospectively with retrospective application not permitted. The adoption of FSP FAS 157-4 did not have a material impact on the Company’s consolidated financial statements.

In April 2009, the FASB issued FSP FAS 115-2 and FAS 124-2. This FSP amends SFAS 115, “Accounting for Certain Investments in Debt and Equity Securities,” SFAS 124, “Accounting for Certain Investments Held by Not-for-Profit Organizations,” and EITF Issue No. 99-20, “Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to Be Held by a Transferor in Securitized Financial Assets,” to make the other-than-temporary impairments guidance more operational and to improve the presentation of other-than-temporary impairments in the financial statements. This FSP will replace the existing requirement that the entity’s management assert it has both the intent and ability to hold an impaired debt security until recovery with a requirement that management assert it does not have the intent to sell the security, and it is more likely than not it will not have to sell the security before recovery of its cost basis. This FSP provides increased disclosure about the credit

and noncredit components of impaired debt securities that are not expected to be sold and also requires increased and more frequent disclosures regarding expected cash flows, credit losses, and an aging of securities with unrealized losses. Although this FSP does not result in a change in the carrying amount of debt securities, it does require that the portion of an other-than-temporary impairment not related to a credit loss for a held-to-maturity security be recognized in a new category of other comprehensive income and be amortized over the remaining life of the debt security as an increase in the carrying value of the security. The adoption of FSP FAS 115-2 and FAS 124-2 did not have a material impact on the Company’s consolidated financial statements.

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In April 2009, the FASB issued FSP FAS 107-1 and APB 28-1. This FSP amends SFAS No. 107, "Disclosures about Fair Value of Financial Instruments," to require disclosures about fair value of financial instruments not measured on the balance sheet at fair value in interim financial statements as well as in annual financial statements. Prior to this FSP, fair values for these assets and liabilities were only disclosed annually. This FSP applies to all financial instruments within the scope of SFAS 107 and requires all entities to disclose the method(s) and significant assumptions used to estimate the fair value of financial instruments. The adoption of FSP FAS 107-1 and APB 28-1 did not have a material impact on the Company's consolidated financial statements.

In May 2009, the FASB issued Statement of Financial Accounting Standards No. 165, "Subsequent Events," (FAS 165, Subsequent Events [ASC 855-10-05], which provides guidance to establish general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. FAS 165 also requires entities to disclose the date through which subsequent events were evaluated as well as the rationale for why that date was selected. FAS 165 is effective for interim and annual periods ending after June 15, 2009, and accordingly, the Company adopted this Standard during the second quarter of 2009. FAS 165 requires that public entities evaluate subsequent events through the date that the financial statements are issued. The Company has evaluated subsequent events through the time of filing these consolidated financial statements with the SEC on August 10, 2009.

In June 2009, the FASB issued Statement No. 166, Accounting for Transfers of Financial Assets – an amendment of FASB No. 140 ("FAS 140"), Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities ("FAS 166") [ASC 860]. FAS 166 amends the criteria for a transfer of a financial asset to be accounted for as a sale, redefines a participating interest for transfers of portions of financial assets, eliminates the qualifying special-purpose entity concept and provides for new disclosures. FAS 166 is effective for the Company beginning in 2010. Should the Company's accounts receivable securitization programs not qualify for sale treatment under the revised rules, future securitization transactions entered into on or after January 1, 2010 would be classified as debt and the related cash flows would be reflected as a financing activity. The Company is currently assessing the impact of the standard on its securitization programs.

In June 2009, the FASB issued Statement of Financial Accounting Standards No. 167, Amendments to FASB Interpretation No. 46(R) ("FAS 167") [ASC 810-10], which modifies how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. FAS 167 clarifies that the determination of whether a company is required to consolidate an entity is based on, among other things, an entity's purpose and design and a company's ability to direct the activities of the entity that most significantly impact the entity's economic performance. FAS 167 requires an ongoing reassessment of whether a company is the primary beneficiary of a variable interest entity. FAS 167 also requires additional disclosures about a company's involvement in variable interest entities and any significant changes in risk exposure due to that involvement. FAS 167 is effective for fiscal years beginning after November 15, 2009. The Company is currently assessing the impact of the standard on its securitization programs.

In June 2009, the FASB issued Statement of Financial Accounting Standards No. 168, The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles a Replacement of FASB Statement No. 162 ("FAS 168"). This Standard establishes the FASB Accounting Standards Codification™ (the "Codification") as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with U.S. GAAP. The Codification does not change current U.S. GAAP, but is intended to simplify user access to all authoritative U.S. GAAP by providing all the authoritative literature related to a particular topic in one place. The Codification is effective for interim and annual periods ending after September 15, 2009, and as of the effective date, all existing accounting standard documents will be superseded. The Codification is effective for the Company in the third quarter of 2009, and accordingly, the Company's Quarterly Report on Form 10-Q for the quarter ending September 30, 2009 and all

subsequent public filings will reference the Codification as the sole source of authoritative literature.

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Note 3 – Other Assets

Other assets consisted of the following:

		June 30, 2009 Unaudited		December 31, 2008
Prepaid rent – natural gas stations	$	376,986	$	272,635
Prepayment for acquiring land use right		1,421,050		1,060,675
Advances on purchasing equipment and construction in progress		6,527,098		6,427,974
Refundable security deposits		530,063		981,083
Others		165,870		101,695
Total	$	9,021,067	$	8,844,062

All land in the PRC is government owned. However, the government grants users land use rights. As of June 30, 2009 and December 31, 2008, the Company prepaid $1,421,050 (unaudited) and $1,060,675, respectively, to the PRC local government to purchase land use rights. The Company is in the process of negotiating the final purchase price with the local government and the land use rights have not yet been granted to the Company. Therefore, the Company did not amortize the prepaid land use rights.

Advances on the purchase of equipment and construction in progress are monies deposited or advanced to outside vendors/subcontractors for the purchase of operating equipment or for services to be provided for constructions in progress.

Refundable security deposits are monies deposited with one of the Company's major vendors and gas station landlord. These amounts will be returned to the Company if they terminate the business relationship or at the end of the lease.

Note 4 – Senior Notes Payable

On December 30, 2007, the Company entered into a Securities Purchase Agreement with Abax Lotus Ltd. (the "Investor"). The Purchase Agreement was subsequently amended on January 29, 2008, pursuant to which the Company (i) agreed to issue 5.00% Guaranteed Senior Notes due 2014 (the "Senior Notes") of approximately $20,000,000, (ii) agreed to issue to the Investor Senior Notes in aggregate principal amount of approximately $20,000,000 on or before March 3, 2008 subject to the Company meeting certain closing conditions, (iii) granted the Investor an option to purchase up to approximately $10,000,000 in principal amount of its Senior Notes and (iv) agreed to issue to the Investor seven-year warrants exercisable for up to 1,450,000 shares of the Company's common stock (the "Warrants") at an initial exercise price equal to $14.7304 per share, subject to certain adjustments, which adjusted to $7.3652 on January 29, 2009. On January 29, 2008, the Company issued $20,000,000 Senior Notes and 1,450,000 warrants pursuant to the Purchase Agreement. On March 3, 2008, the Investor exercised its first option for an additional $20,000,000 of Senior Notes. On March 10, 2008, the Company issued $20,000,000 in additional Senior Notes resulting in total Senior Notes of $40,000,000.

At the closing, the Company entered into:

- An indenture for the 5.00% Guaranteed Senior Notes due 2014;
- An investor rights agreement;
- A registration rights agreement covering the shares of common stock issuable upon exercise of the warrants;
-

An information rights agreement that grants to the Investor, subject to applicable law, the right to receive certain information regarding the Company;

- A share-pledge agreement whereby the Company granted to the Collateral Agent (on behalf of the holders of the Senior Notes) a pledge on 65% of the Company's equity interest in Shaanxi Xilan Natural Gas Equipment Co., Ltd., a PRC corporation and wholly-owned subsidiary of the Company; and

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- An account pledge and security agreement whereby the Company granted to the Collateral Agent a security interest in the account where the proceeds from the Senior Notes are deposited.

In addition, Qinan Ji, Chief Executive Officer and Chairman of the Board of the Company, executed a non-compete agreement for the benefit of the Investor.

The Senior Notes were issued pursuant to an indenture between the Company and DB Trustees (Hong Kong) Limited, as trustee, at the closing. The Senior Notes will mature on January 30, 2014 and will initially bear interest at the stated interest rate of 5.00% per annum, subject to an increase in the event of certain circumstances. The Company is required to make mandatory prepayments on the Senior Notes on the following dates and in the following amounts, expressed as a percentage of the aggregate principal amount of Notes that will be outstanding on the first such payment date:

Date	Prepayment Percentage
July 30, 2011	8.3333%
January 30, 2012	8.3333%
July 30, 2012	16.6667%
January 30, 2013	16.6667%
July 30, 2013	25.0000%

During the twelve month period commencing January 30 of the years set forth below, the Company may redeem the Senior Notes at the following principal amount:

Year	Principal
2009	43,200,000
2010	42,400,000
2011	41,600,000
2012	40,800,000
2013 and thereafter	40,000,000

Upon the occurrence of certain events defined in the indenture, the Company must offer the holders of the Senior Notes the right to require the Company to purchase the Senior Notes in an amount equal to 105% of the aggregate principal amount purchased plus accrued and unpaid interest on the Senior Notes purchased.

The indenture requires the Company to pay additional interest at the rate of 3.0% per annum of the Senior Notes if the Company has not obtained a listing of its common stock on the Nasdaq Global Market, the Nasdaq Capital Market or the New York Stock Exchange by January 29, 2009 and maintained such listing continuously thereafter as long as the Senior Notes are outstanding. As of January 29, 2009, the Company has not obtained a listing of its common stock on the market stated in the agreement. However, the Company obtained a three-month waiver from AMAX for the additional interest payment. The waiver gives the Company three more months until April 28, 2009 to achieve the uplisting status. By the end of the extended period, if the Company can't get its stock uplisted, the Company would try to get another waiver or the Company will have to pay an additional interest at the rate of 3.0% starting January 30, 2009. The Company wasn't approved to be listed on Nasdaq market until May 2009. As of the reporting date, the Company didn't obtain another formal waiver but reached an agreement with the lender that the three months interest can be waived with contingency condition. For the three months and six months ended June 30, 2009, the Company has recognized the additional interest payment amounted to $203,334 and $406,667, respectively. As of June 30, 2009, none of the payment has been paid as the Company is in the processing of settling this payment.

The indenture limits the Company's ability to incur debt and liens, make dividend payments and stock repurchases, make investments, reinvest proceeds from asset sales and enter into transactions with affiliates, among other things. The indenture also requires the Company to maintain certain financial ratios.

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The Company also entered into an investor rights agreement, pursuant to which, as long as an investor holds at least 10% of the aggregate principal amount of the Senior Notes issued and outstanding or at least 3% of the Company's issued and outstanding common stock pursuant to the warrants on an as-exercised basis ("Minimum Holding"), the Company has agreed not to undertake certain corporate actions without prior Investor approval. In addition, so long as an Investor owns the Minimum Holding, such Investor shall have a right of first refusal for future debt securities offerings by the Company and the Company is subject to certain transfer restrictions on its securities and certain other properties.

From the Closing Date and as long as the Investor continues to hold more than 10% of the outstanding shares of common stock on an as-converted, fully-diluted basis, the Investor shall be entitled to appoint one of the Company's board of directors (the "Investor Director"). The Investor Director shall be entitled to serve on each committee of the board, except that, the Investor Director shall not serve on the audit committee unless it is an independent director. Mr. Ji has agreed to vote his shares for the election of the Investor Director.

The Company was required to prepare and file a registration statement covering the sales of all of the shares of common stock issuable upon exercise of the warrants or incur additional interest of 1% on the Notes. The Company's registration statement was declared effective on May 6, 2008; therefore, no penalties were incurred.

In connection with the issuance of the Securities Purchase Agreement, the Company paid $2,122,509 in debt issuance costs which is being amortized over the life of the Senior Notes. For the three months ended June 30, 2009 and 2008, the Company amortized $13,857 and $66,322 of the aforesaid issuance costs, net of capitalized interest. For the six months ended June 30, 2009 and 2008, the Company amortized $52,435 and $122,592 of the aforesaid issuance costs, net of capitalized interest.

In connection with the Securities Purchase Agreement, the Company agreed to issue to the Investor seven-year warrants exercisable for up to 1,450,000 shares of the Company's common stock at an initial exercise price equal to $14.7304 per share, subject to certain adjustments. The exercise price of the Warrants is adjusted on the first anniversary of issuance and thereafter, at every six month anniversary beginning in the fiscal year 2009 if the volume weighted average price, or VWAP, (as defined therein) for the 15 trading days prior to the applicable reset date is less than the then applicable exercise price, in which case the exercise price shall be adjusted downward to the then current VWAP; provided, however, that in no event shall the exercise price be adjusted below $7.3652 per share. The exercise price was adjusted to $7.3652 on January 29, 2009. No further adjustments of the exercise price will be required (as that is the floor price).

The warrants granted to the Investor on January 29, 2008 are considered derivative instruments that need to be bifurcated from the original security. If the Warrants have not been exercised within the seven year period, then the Investor can have the Company purchase the Warrants for $17,500,000. This amount is shown as a debt discount and is being amortized over the term of the Senior Notes. For the three months ended June 30, 2009 and 2008, the Company amortized $46,484 and $312,810 of the aforesaid discounts, net of capitalized interest. For the six months ended June 30, 2009 and 2008, the Company amortized $217,196 and $459,473 of the aforesaid discounts, net of capitalized interest.

The warrants have been determined to be derivative liabilities instruments because there is a required redemption requirement if the holder does not exercise the Warrants. However, the warrants are not required to be valued at fair value, rather, to be at its undiscounted redemption amount of $17.5 million according to FAS 150.

Note 5 – Warrants

Following is a summary of the warrant activity:

	Warrants Outstanding		Weighted Average Exercise Price	Aggregate Intrinsic Value
Outstanding, December 31, 2007	544,242	$	13.10	376,977
Granted	1,450,000	$	14.74	-
Forfeited	-		-	-
Exercised	-		-	-
Outstanding, December 31, 2008	1,994,242	$	14.28	-
Granted	-		-	-
Forfeited	(160,588)	$	7.20	-
Exercised	-		-	-
Outstanding, June 30, 2009 (Unaudited)	1,833,654	$	8.93	2,871,569

Following is a summary of the status of warrants outstanding at June 30, 2009 (Unaudited):

Outstanding Warrants		
Exercise Price	Number	Average Remaining Contractual Life
$7.37	1,450,000	5.58
$14.86	383,654	3.09
$8.93	1,833,654	5.06

Note 6 – Defined Contribution Plan

The Company is required to participate in a defined contribution plan operated by the local municipal government in accordance with Chinese law and regulations. The Company contributes 100RMB per employee per month to the plan. Starting from 2008, no minimum contribution is required but the maximum contribution cannot be more than 14% of the current salary expense. The total contribution for the above plan was $33,891 and $0 for the three months ended June 30, 2009 and 2008, respectively. The total contribution for the above plan was $81,079 and $0 for the six months ended June 30, 2009 and 2008, respectively.

Note 7 – Statutory Reserve

As stipulated by the Company Law of the People's Republic of China (PRC) as applicable to Chinese companies with foreign ownership, net income after taxation can only be distributed as dividends after appropriation has been made for the following:

i. Making up cumulative prior years' losses, if any;

ii. Allocations to the "Statutory surplus reserve" of at least 10% of income after tax, as determined under PRC accounting rules and regulations, until the fund amounts to 50% of the Company's registered capital;

iii. Allocations to the discretionary surplus reserve, if approved in the shareholders' general meeting.

As of June 30, 2009, the remaining reserve needed to fulfill the 50% registered capital requirement totaled $53,831,675.

Note 8 – Accounting for stock-based compensation

1) Options from CEO to pay for certain Company's legal expenses

On September 22, 2007, Mr. Qinan Ji, chairman and shareholder of the Company, transferred 50,000 of his personally-owned options to the Company's attorney to cover certain Company legal expenses. 30% of the options vested on September 22, 2008, 30% vest on September 22, 2009, and the remaining 40% vest on September 22, 2010. Upon termination of service to the Company, the attorney is required to return all unvested options. These options expire June 1, 2012.

The Company used the Black-Sholes Option Pricing Model to value the options at the time they were issued, based on the stock price on its grant date, the stated exercise prices and expiration dates of the instruments and using a risk-free rate of 4.10%. The estimated life is based on one half of the sum of the vesting period and the contractual life of the

option. This is the same as assuming that the options are exercised at the mid-point between the vesting date and expiration date. $14,842 and $38,896 of compensation expense was recorded during the three months ended June 30, 2009 and 2008, respectively. $29,685 and $38,896 of compensation expense were recorded during the six months ended June 30, 2009 and 2008, respectively.

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As of June 30, 2009, approximately $102,874 of estimated expense with respect to non-vested stock-based compensation has yet to be recognized and will be recognized in expense over the optionee's remaining weighted average service period of approximately 1.25 years.

2) 2009 stock option plan

On March 11, 2009, the board of directors approved by written consent the Company's stock option plan for its employees, directors and consultants. Pursuant to the plan, the total stock option pool will equal to 10% of the Company's total shares outstanding as of March 11, 2009. Among the option pool approved, 4% shall be awarded in 2009 and another 4% shall be awarded in 2010, and 2% reserved for future awards. For the 2009 stock option award, the CEO and CFO were granted total options of 1% and 0.6% of the common shares outstanding respectively, 50% as Non-qualified Stock Options (NSO) and 50% as Incentive Stock Awards (ISA), for a vesting period of four years. As Richard Wu has resigned as CFO, the Company granted to his successor, Veronica Chen, options to purchase 75,000 shares (post-split) of the Company's common stock, representing approximately 0.5% of the Company's outstanding shares as of March 11, 2009, with the same terms and conditions as specified in the stock options plan. 5,000 option shares per year will be granted to each non-executive board member and 6,000 option shares per year granted to the Audit Committee Chairman. Other senior management and employees will be granted total options of 2.11% of the Company's common shares. On April 1, 2009 and May 1, 2009, the Company issued 243,850 and 75,000 stock options, respectively, pursuant to the Company's 2009 employee stock option and stock award plan. The strike price for the options was $4.90 per share. The stock option has a term of six years and vests evenly over four years starting one year from the issuance date on an annually basis.

The Company used the Black-Sholes Option Pricing Model to value the options at the time they were issued, based on the stock price on its grant date, the stated exercise prices and expiration dates of the instruments and using risk-free rates. The estimated life is based on one half of the sum of the vesting period and the contractual life of the option. This is the same as assuming that the options are exercised at the mid-point between the vesting date and expiration date. $71,073 of compensation expense was recorded during three months and six months ended June 30, 2009.

As of June 30, 2009, approximately $1,066,094 of estimated expense with respect to non-vested stock-based compensation has yet to be recognized and will be recognized in expense over the optionee's remaining weighted average service period of approximately 3.75 years.
Following is a summary of the Stock option activity:

	Options Outstanding	Weighted Average Exercise Price	Aggregate Intrinsic Value
Outstanding, December 31, 2008	-	-	-
Granted	318,850	$ 4.9	95,655
Forfeited	-	-	-
Exercised	-	-	-
Outstanding, June 30, 2009 (Unaudited)	318,850	$ 4.9	1,785,560

Following is a summary of the status of stock options outstanding at June 30, 2009 (unaudited):

Outstanding Options			Exercisable Options		
Exercise Price	Number	Average Remaining Contractual	Exercise Price	Number	Average Remaining Contractual

		Life			Life
$4.90	243,850	5.75	-	-	-
$4.90	75,000	5.84	-	-	-

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Note 9 – Earnings per Share

Earnings per share for the periods ended June 30, 2009 and 2008 is determined by dividing net income for the periods by the weighted average number of both basic and diluted shares of common stock and common stock equivalents outstanding. The following is an analysis of the differences between basic and diluted earnings per common share in accordance with Statement of Financial Accounting Standards No. 128, "Earnings per Share."

The following demonstrates the calculation for earnings per share for the periods ended June 30, 2009 and 2008:

	For the three months ended June 30,		For the six months ended June 30,	
Basic earning per share	2009 (Unaudited)	2008 (Unaudited)	2009 (Unaudited)	2008 (Unaudited)
Net income	3,862,756	3,512,892	8,064,379	6,321,463
Weighted shares outstanding-Basic	14,600,154	14,600,154	14,600,154	14,600,154
Earnings per share-Basic	$ 0.26	$ 0.24	$ 0.55	$ 0.43
Diluted earning per share				
Net income	3,862,756	3,512,892	8,064,379	6,321,463
Weighted shares outstanding-Basic	14,600,154	14,600,154	14,600,154	14,600,154
Effect of diluted securities-Warrants	126,493	61,594	-	64,713
Weighted shares outstanding-Diluted	14,726,647	14,661,748	14,600,154	14,664,867
Earnings per share –Diluted	$ 0.26	$ 0.24	$ 0.55	$ 0.43

At June 30, 2009 and 2008, the Company had outstanding warrants of 1,833,654 and 1,994,242, respectively. For the three months ended June 30, 2009, the average stock price was greater than the exercise prices of the 1,450,000 warrants which resulted in additional weighted average common stock equivalents of 126,493; 383,654 outstanding warrants were excluded from the diluted earnings per share calculation as they are anti-dilutive. For the three months ended June 30, 2008, the average stock price was greater than the exercise prices of the 160,588 warrants which resulted in additional weighted average common stock equivalents of 61,594; 1,833,654 outstanding warrants were excluded from the diluted earnings per share calculation as they are anti-dilutive. For the six months ended June 30, 2009, all 1,833,654 outstanding warrants were excluded from the diluted earnings per share calculation as they are anti-dilutive. For the six months ended June 30, 2008, the average stock price was greater than the exercise prices of the 160,588 warrants which resulted in additional weighted average common stock equivalents of 64,713; 1,833,654 outstanding warrants were excluded from the diluted earnings per share calculation as they are anti-dilutive.

Note 10 – Current Vulnerability Due to Certain Concentrations

Concentration of natural gas vendors:

	For the three months ended June 30,		For the six months ended June 30,	
	2009 (Unaudited)	2008 (Unaudited)	2009 (Unaudited)	2008 (Unaudited)
Numbers of natural gas vendors	4	4	4	4
Percentage of total natural gas purchases	97%	99%	90%	99%

As of June 30, 2009 and December 31, 2008, the Company has $117,200 and $206,811, respectively, payable due to its major suppliers.

The Company maintains long-term natural gas minimum purchase agreements with one of its vendors as of June 30, 2009. There are no minimum purchase requirements by the Company. Contracts are renewed on an annual basis. The Company's management reports that it does not expect any issues or difficulty in continuing to renew the supply contracts with these vendors going forward. Price points for natural gas are strictly controlled by the government and have remained stable over the past three years.

The Company's operations are carried out in the People's Republic of China. Accordingly, the Company's business, financial condition and results of operations may be influenced by the political, economic and legal environments in the People's Republic of China, by the general state of the People's Republic of China's economy. The Company's business may be influenced by changes in governmental policies with respect to laws and regulations, anti-inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation, among other things.

Note 11 – Commitments and Contingencies

(a) Lease Commitments

The Company recognizes lease expense on a straight-line basis over the term of the lease in accordance to FAS 13, "Accounting for leases." The Company entered into a series of long-term lease agreements with outside parties to lease land use rights to the self-built Natural Gas filing stations located in the PRC. The agreements have terms ranging from 10 to 30 years. The Company makes annual prepayments for most lease agreements. The Company also entered into two office leases in Xi'an, PRC and New York, NY. The minimum future payment for leasing land use rights and offices is as follows:

Year ending December 31, 2009	$ 430,734
Year ending December 31, 2010	1,458,518
Year ending December 31, 2011	1,577,171
Year ending December 31, 2012	1,339,207
Year ending December 31, 2013	1,280,490
Thereafter	21,923,925
Total	$ 28,010,045

For the three months ended June 30, 2009 and 2008, the land use right and office lease expenses were $406,016 and $ 310,698, respectively. For the six months ended June 30, 2009 and 2008, the land use right and office lease expenses were $798,097 and $373,945 respectively.

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(b) Property and Equipment

In January 2008, the Company entered into a contract with Chemtex International Inc. to purchase equipment supply for the LNG plant and storage tank located in Jingbian County, Shannxi Province China, in the total amount of $13,700,000. On May 16, 2008, JBLNG entered into an agreement with Hebei Tongchan Import and Export Co. Ltd. (Hebei) and agreed that Hebei will act as the trade agency for JBLNG. On June 16, 2008, the Company entered into an equipment supply contract with Chemtex International Inc. to supply imported equipment for a LNG plant and a storage tank to be built by Jingbian Xilan LNG Co. Ltd. As of June 30, 2009, the Company advanced $6,299,500 to the trade agency and the future commitment for equipment is $7,400,500.

(c) Natural Gas Purchase Commitments

The Company has existing long-term natural gas purchase agreements with its major suppliers. However, none of those agreements stipulate any specific purchase amount or quota each year, thus giving the Company enough flexibility to constantly look for lower-cost sources of supply. Therefore, the Company is not legally bound in purchase commitments by those agreements.

(d) Legal Proceedings

A former member of the board of directors filed a lawsuit against the Company in the New York State Supreme Court, Nassau County, in which he has sought, among other things to recover a portion of his monthly compensation plus 20,000 options that he alleges are due to him pursuant to a written agreement. After the plaintiff rejected an offer by the Company that included the options that the plaintiff alleged were due to him, the Company moved to dismiss the complaint. The judge ordered the Company to issue the 20,000 options to the plaintiff subject to any restrictions required by applicable securities laws, which was essentially what the Company had previously offered, and dismissed all of the plaintiff's remaining claims against the Company. The current board of directors has complied with the court's decision by tendering an options agreement to the plaintiff consistent with the court's decision, but the plaintiff has refused to execute the agreement, and instead has filed an appeal. Regardless of the outcome of the appeal, the Company believes that any liability it would incur will not have a materially adverse effect on its financial condition or its results of operations, and, accordingly, this matter has not been reflected on the Company's consolidated financial statements.

Note 12 – Subsequent Events

On July 22, 2009, China Natural Gas, Inc., through its variable interest entity, Xi’an Xilan Natural Gas Co., Ltd. (“Xi’an Xilan”), entered into a joint venture agreement (“Joint Venture Agreement”) with China National Petroleum Corporation Kunlun Natural Gas Co., Ltd. (“Kunlun”). Pursuant to the Joint Venture Agreement, Xi’an Xilan will form a Joint Venture Company with Kunlun (the “Joint Venture Company”) to construct and operate compressed natural gas (“CNG”) stations, conduct sales of CNG, convert gasoline fueled vehicles to hybrid (natural gas/gasoline) powered vehicles and other related technical services in Henan province, China.

The Joint Venture Company will have an initial registered capital of RMB 50,000,000 (approximately US $7,350,000). Kunlun will contribute RMB 25,500,000 in cash, representing 51% of the Joint Venture Company’s total registered capital, upon the approval of the governing officers of Kunlun.

Xi’an Xilan will contribute RMB 24,500,000, representing 49% of the Joint Venture Company’s total registered capital, in two installments. The first installment will be RMB 10,000,000 in cash and the second installment of RMB 14,500,000 will be either cash, property (currently expected to be a fleet of tankers consisting of two locomotives and four tanks)or a combination of cash and property.

Both parties will share the management responsibilities of the operations of the Joint Venture Company. The Joint Venture Company shall have a term of 20 years commencing on August 1, 2009 and terminating on July 31, 2029.

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

CAUTIONARY STATEMENT

FORWARD-LOOKING STATEMENT

The information in this report contains forward-looking statements. All statements other than statements of historical fact made in this report are forward looking. In particular, the statements herein regarding industry prospects and future results of operations or financial position are forward-looking statements. These forward-looking statements can be identified by the use of words such as "believes," "estimates," "could," "possibly," "probably," anticipates," "projects," "expects," "may," "will," or "should" or other variations or similar words. No assurances can be given that the future results anticipated by the forward-looking statements will be achieved. Forward-looking statements reflect management's current expectations and are inherently uncertain. Our actual results may differ significantly from management's expectations.

The following discussion and analysis should be read in conjunction with our financial statements, included herewith. This discussion should not be construed to imply that the results discussed herein will necessarily continue into the future, or that any conclusion reached herein will necessarily be indicative of actual operating results in the future. Such discussion represents only the best present assessment of our management.

Overview

We are a distributor of compressed natural gas ("CNG") in China, which we primarily distribute through our Company-owned CNG fueling stations. As of June 30, 2009, we operated 23 CNG fueling stations in Shaanxi province and 12 CNG fueling stations in Henan province. We own our CNG fueling stations while we lease the land upon which our CNG fueling stations operate. For the three and six months ended June 30, 2009, we sold CNG of 41,152,513 and 80,446,633 cubic meters respectively through our fueling stations, compared to 37,304,556 and 67,844,028 cubic meters for the three and six months ended June 30, 2008. We also transport, distribute and sell piped natural gas to residential and commercial customers in the Xi’an area, including Lantian County, and the districts of Lintong and Baqiao, in Shaanxi province through a high pressure pipeline network of approximately 120 kilometers.

We operate four main business lines:

- Distribution and sale of compressed natural gas through Company-owned CNG fueling stations for hybrid (natural gas/gasoline) powered vehicles (35 stations as of June 30, 2009);

- Installation, distribution and sale of piped natural gas to residential and commercial customers through Company-owned pipelines. We distributed and sold piped natural gas to 103,343 residential customers as of June 30, 2009;

- Distribution and sale of gasoline through Company-owned CNG fueling stations for gasoline and hybrid (natural gas/gasoline) powered vehicles (8 of our CNG fueling stations sold gasoline as of June 30, 2009); and

- Conversion of gasoline-fueled vehicles to hybrid (natural gas/gasoline) powered vehicles at our auto conversion sites.

We buy all of the natural gas that we sell and distribute to our customers. We do not mine or produce any of our own natural gas and have no plans to do so during the next 12 months. We currently sell our natural gas in two forms: (i) CNG and (ii) piped natural gas.

On October 24, 2006, our variable interest entity, Xi'an Xilan Natural Gas Co., Ltd. ("XXNGC"), formed a wholly-owned subsidiary, Shaanxi Jingbian Liquefied Natural Gas Co., Ltd. ("SJLNG"), for the purpose of constructing a liquefied natural gas ("LNG") facility to be located in Jingbian, Shaanxi province. We plan to invest approximately $45 million to construct this facility, a portion of which was funded through the sale of senior notes to Abax Lotus Ltd., and the remainder of which will be funded by our cash flows from operations. The LNG plant is under construction and is expected to be completed and fully operational by the end of 2009. Once completed, the plant is expected to have a LNG processing capacity of 500,000 cubic meters per day, or approximately 150 million cubic meters on an annual basis.

We had total revenues of $20,742,520 and $16,890,486 for the three months ended June 30, 2009 and 2008 respectively and revenues of $39,270,186 and $30,916,160 for the six months ended June 30, 2009 and 2008, respectively. We had net income of $3,862,756 and $3,512,892 for the three months ended June 30, 2009 and 2008 respectively and net income of $8,064,379 and $6,321,463 for the six months ended June 30, 2009 and 2008 respectively.

Factors Affecting Our Results of Operations

Significant factors affecting our results of operations are:

Successful expansion of our CNG fueling station business in our target markets. Our revenue increased by 22.8% during the three months ended June 30, 2009 from the three months ended June 30, 2008 and by 27.0% during the six months ended June 30, 2009 from the six months the June 30, 2008 largely because of the addition of 6 new fueling stations added since the second quarter of 2008, as well as the increase of pipeline natural gas customers. As of June 30, 2009, we operated 35 CNG fueling stations in total and, in Shaanxi alone, we operated 23 CNG fueling stations. We believe we are the largest provider of CNG fueling stations in Xi’an, one of our core target markets for CNG. As of June 30, 2009, we operated 12 CNG fueling stations in Henan province, another of our core target markets. The successful expansion of our CNG fueling station business in Xi’an and Henan province has been a significant factor driving our revenue growth and results of operations for the period reviewed. While we intend to expand into different provinces, we anticipate the growth of our CNG fueling business in Xi’an and Henan province will continue to significantly affect our results of operations as we intend to continue to increase the number of CNG fueling stations we operate in these areas.

Regulation of natural gas prices in the PRC. The prices at which we purchase our natural gas supplies and sell CNG and pipeline natural gas products are strictly regulated by the PRC central government, including the National Development and Reform Commission (“NDRC”), and the local state price bureaus who have the discretion to set natural gas prices within the boundaries set by the PRC central government. In addition, natural gas procurement and sale prices are not uniform across China and can vary across provinces. For example, the prices at which we procure and sell CNG and piped natural gas are lower in Shaanxi than in Henan. Accordingly, our results of operations and, in particular, our revenue, cost of revenue and gross profit and gross margin are affected significantly by factors which are outside of our control. As we expand our natural gas business into other provinces, we expect our results of operations to continue to be affected significantly by the regulation of natural gas prices in the PRC.

Government policies encouraging the adoption of cleaner burning fuels. Our results of operations for the periods reviewed have benefited from environmental regulations and programs in the PRC that promote the use of cleaner burning fuels, including natural gas for vehicles. As an enterprise engaged in the natural gas industry, our VIE benefits from a reduced income tax rate of 15% compared to the standard 25% enterprise income tax rate in the PRC. In addition, the PRC government has encouraged companies to invest in and build the necessary transportation, distribution and sale infrastructure for natural gas in various policy pronouncements such as by officially including CNG/gasoline hybrid vehicles in the country's "encouraged development" category. These policies have benefited our results of operations by encouraging the demand for our natural gas products and also by lowering our expenses. As we expand into the LNG business, we anticipate that our results of operations will continue to be affected by government policies encouraging the adoption of cleaner burning fuels and the increased adoption of CNG and LNG technology.

The overall economic growth of China’s economy. We do not export our products outside China and our results of operations are thus substantially affected by the growth of the industrial base, the increase in residential, commercial and vehicular consumption and the overall economic growth of China. While's China's economy has experienced a slowdown after the second quarter of 2007, we are currently unable to estimate the impact of such slow down on our

business; as the impact of the decline in international trade is being offset in part through domestic stimulus spending, expanded bank lending, increases in the speed of regulatory approvals of new construction projects and other economic policies. While we do not believe we have experienced reduced demand for natural gas to date, if the economic downturn continues, our results of operations may be negatively affected by any decrease in demand for natural gas in the second half of 2009.

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Taxation

United States

We are incorporated in the State of Delaware and are subject to the tax laws of the United States. We incurred a net operating loss for income tax purposes for the period ended June 30, 2009. The estimated net operating loss carry forwards for United States income tax purposes amounted to $1,913,731 and $1,657,473 as of June 30, 2009 and December 31, 2008, respectively, which may be available to reduce future years' taxable income. These carry forwards will expire, if not utilized, beginning in 2027 through 2029. Our management believes that the realization of the benefits arising from this loss appear to be uncertain due to our Company's limited operating history and continuing losses for United States income tax purposes. Accordingly, we have provided a 100% valuation allowance at June 30, 2009.

The PRC

Our subsidiary, VIE and its subsidiaries operate in China. Starting January 1, 2008, pursuant to the tax laws of China, general enterprises are subject to income tax at an effective rate of 25% compared to 33% prior to 2008. Based on certain income tax regulations adopted in 2001 to encourage the development of certain industries, including the natural gas industry, in the western portions of China such as Shaanxi Province, XXNGC is subject to a reduced tax rate of 15%. Accordingly, except for income from XXNGC, which is subject to the reduced tax rate of 15%, income from Xilan Equipment, SJLNG, XXABC, HXNGC and LBNGC are subject to the 25% PRC income tax rate. Our effective income tax rate for the three months ended June 30, 2009 and 2008 were approximately 23.5% and 19.7%, respectively.

Value Added Tax

Sales revenue represents the invoiced value of goods, net of a value-added tax ("VAT"). All of our variable interest entity XXNGC's products that are sold in the PRC are subject to a Chinese VAT at a rate of 13% of the gross sales price. This VAT may be offset by VAT paid by XXNGC on raw materials and other materials included in the cost of producing their finished products. XXNGC records VAT payable and VAT receivable net of payments in its financial statements. VAT tax returns are filed offsetting the payables against the receivables.

All revenues from XXABC are subject to a Chinese VAT at a rate of 6%. This VAT cannot be offset with VAT paid for materials included in the cost of revenues.

Internal Control Over Financial Reporting

We are subject to reporting obligations under the U.S. securities laws. The SEC, as required by Section 404 of the Sarbanes-Oxley Act, adopted rules requiring every public company to include a management report on such company’s internal control over financial reporting in its annual report, which contains management’s assessment of the effectiveness of the company’s internal control over financial reporting. In addition, an independent registered public accounting firm must report on our internal control over financial reporting. Our management has concluded that our internal control over our financial reporting is not effective as of June 30, 2009.

CONSOLIDATED RESULTS OF OPERATIONS

Three Months Ended June 30, 2009 Compared to Three Months Ended June 30, 2008

The following table represents the consolidated operating results for the three month period ended June 30, 2009 and 2008:

Sales Revenues

The following table sets forth a breakdown of our revenues for the period indicated:

	June 30, 2009	June 30, 2008	Increase in dollar amount	Increase in percentage
Natural gas from fueling stations	$ 15,051,319	$ 13,181,335	$ 1,869,984	14.2%
Natural gas from pipelines	669,360	613,531	55,829	9.1%
Gasoline	1,633,016	1,148,097	484,919	42.2%
Installation	2,690,164	1,282,400	1,407,764	109.8%
Auto conversion	698,661	665,123	33,538	5.0%
Total	$ 20,742,520	$ 16,890,486	$ 3,852,034	22.8%

Overal.: Total revenue for the three months ended June 30, 2009 increased to $20,742,520 from $16,890,486 for the three months ended June 30, 2008, an increase of $3,852,034 or 22.8%. This increase was mainly due to the addition of 6 new fueling stations added since the second quarter of 2008, and an increase in the number of residential and commercial pipeline customers to 103,343 as of June 30, 2009 from 91,967 as of June 30, 2008. We sold natural gas of 44,090,672 cubic meters during the three months ended June 30, 2009, compared to 39, 986,368 cubic meters during the three months ended June 30, 2008. For the three months ended June 30, 2009, 83.7% of our revenue was generated from the sale of natural gas and gasoline, and the other 16.3% was generated from our installation and auto conversion services.

Natural Gas from Fueling Stations. Natural gas revenue from our fueling stations increased by 14.2%, or $1,869,984, to $15,051,319 during the three months ended June 30, 2009, from $13,181,335 during the three months ended June 30, 2008, and contributed to 72.6% of our total revenue, which was the largest among our four major business lines. The increase of natural gas revenue was mainly due to the increase of sales volume generated from newly added fueling stations during the 2nd and 3rd quarters of 2008. During the three months ended June 30, 2009, we sold compressed natural gas of 41,152,513 cubic meters, compared to 37, 304,556 cubic meters during the three months ended June 30, 2008 through our fueling stations. In terms of average station sales value and volume, in the three months ended June 30, 2009, we sold approximately $430,038 and 1,175,786 cubic meters of compressed natural gas per station, compared to approximately $434,597 and 1,229,956 cubic meters in the three months ended June 30, 2008. The reason for the decline in per station sales was due to the construction of main subway lines in Xi'an, which caused certain bus routes to deviate from our stations. Unit selling price was relatively stable at $0.37 (RMB 2.5).

Natural Gas from Pipelines. Natural gas revenue from our pipelines increased by 9.1%, or $55,829, to $669,360 during the three months ended June 30, 2009, from $613,531 during the three months ended June 30, 2008, and contributed to 3.2% of our total revenue. As of June 30, 2009, the Company had 103,343 pipeline customers, an

increase of 11,376 customers comparing to as of June 30, 2008. We also sold 2,938,159 cubic meters of natural gas through our pipelines during the three months ended June 30, 2009, compared to 2,681,812 cubic meters during the three months ended June 30, 2008.

Gasoline. Revenue from gasoline sales increased by 42.2%, or $484,919, to $1,633,016 during the three months ended June 30, 2009, from $1,148,097 during the three months ended June 30, 2008, and contributed 7.9% to our total revenue. The gasoline revenue increase was due to the sales volume increased 58% from 1,707,160 liters to 2,707,531 liters, offset by 11% decrease of unit sales price from $0.7 (RMB 4.63) per liter in the three months ended June 30, 2008 to $0.6 (RMB 4.11) per liter in the three months ended June 30, 2009, affected by the decrease of international oil price. The increased sales volumes was due to our two stations, Shihua and Lantian, were in operation during the three months ended June 30, 2009, but were inactive in 2008.

Installation Services. Revenue from installation services increased by 109.8%, or $1,407,764, to $ 2,690,164 during the three months ended June 30, 2009, from $1,282,400 during the three months ended June 30, 2008, and contributed 13.0% to our total revenue. The increase of installation sales was mainly due to the increase of pipeline customers in the newly acquired subsidiary - Lingbao Natural Gas, Co. since January 2009. Installation services to our top four customers contributed to 31.3%, 22.4%, 17.7% and 11.4% of our installation revenue for the three months ended June 30, 2009.

Auto Conversion Services. Revenue from our auto conversion division increased by 5.0%, or $33,538, to $698,661 during the three months ended June 30, 2009, from $665,123 during the three months ended June 30, 2008, and contributed 3.4% to our total revenue.

Cost of Revenue

The following table sets forth a breakdown of our cost of revenue for the periods indicated:

	June 30, 2009	June 30, 2008	Increase / (Decrease) in dollar amount	Increase / (Decrease) in percentage
Natural gas from fueling stations	$ 7,023,175	$ 6,783,702	$ 239,473	3.5%
Natural gas from pipelines	467,343	430,767	36,576	8.5%
Gasoline	1,529,752	1,054,978	474,774	45.0%
Installation	1,039,116	538,970	500,146	92.8%
Auto conversion	404,944	416,306	(11,362)	(2.7)%
Total	$ 10,464,330	$ 9,224,723	$ 1,239,607	13.4%

Overall. Our cost of revenue consists of the cost of natural gas and gasoline sold, installation and other costs. Cost of natural gas and gasoline sold consists of the cost for purchase from our suppliers. Cost of installation and other costs include certain expenditures for the connection of customers to our pipeline system, and the cost for converting gasoline-fueled vehicles into natural gas hybrid vehicles.

Our cost of revenue for the three months ended June 30, 2009 was $10,464,330, an increase of $1,239,607, or 13.4%, from $9,224,723 for the three months ended June 30, 2008, while our revenue increased by 22.8% during the same period.

Natural Gas from Fueling Stations. Cost of revenue of our natural gas for our fueling stations increased by 3.5%, or $239,473, to $7,023,175 during the three months ended June 30, 2009, as compared to $6,783,702 for the three

months ended June 30, 2008. The low growth rate for cost of natural gas for our fueling stations was primarily due to the decrease of procurement price in coal bed methane as we obtained better term from July 2008 in Henan province that reduced our unit cost from one of our major supplier by approximately 32%, and our overall average unit cost was reduced by 12% during the three months ended June 30, 2009.

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Natural Gas from Pipelines. Cost of revenue of our natural gas sold through our pipelines increased by 8.5%, or $36,576, to $467,343 during the three months ended June 30, 2009, as compared to $430,767 during the three months ended June 30, 2008, which was in line with the sales growth.

Gasolin.: Cost of our gasoline revenue increased by 45.0%, to $1,529,752 during the three months ended June 30, 2009, from $1,054,978 for the three months ended June 30, 2008. The increase of cost of gasoline revenue was due to the increase in sales volume, offset by the effect of the decrease of average unit cost from $0.63 (RMB 4.29) per liter during the three months ended June 30, 2008 to $0.56 (RMB 3.85) per liter during the three months ended June 30, 2009 due to the decreasing price of the international fuel market.

Installation Services. Cost of revenue from our installation services increased by 92.8%, or $500,146, to $1,039,116 during the three months ended June 30, 2009, as compared to $538,970 during the three months ended June 30, 2008, as a result of the increase of pipeline customers.

Auto Conversion Services. Cost of our auto conversion revenue decreased by 2.7%, or $11,362, to $404,944 during the three months ended June 30, 2009, as compared to $416,306 during the three months ended June 30, 2008.

Gross profit

The following table sets forth a breakdown of our gross profit for the periods indicated:

	June 30, 2009	June 30, 2008	Increase in dollar amount	Increase in percentage
Natural gas from fueling stations	$ 8,028,144	$ 6,397,633	$ 1,630,511	25.5%
Natural gas from pipelines	202,017	182,764	19,253	10.5%
Gasoline	103,264	93,119	10,145	10.9%
Installation	1,651,048	743,430	907,618	122.1%
Auto conversion	293,717	248,817	44,900	18.1%
Total	$ 10,278,190	$ 7,665,763	$ 2,612,427	34.1%

We earned a gross profit of $10,278,190 for the three months ended June 30, 2009, an increase of $2,612,427 or 34.1%, compared to $7,665,763 for the three months ended June 30, 2008. In summary, gross profit increase was mainly due to the increased sales volume of natural gas from fueling stations with lower unit purchase cost from our major suppliers; the increased sales volume of pipeline natural gas with stable unit price and cost; and the increased installation revenue from new pipeline customers.

Gross margin

Gross margin for natural gas sold through our fueling stations increased from 48.5% in the three months ended June 30, 2008 to 53.3% in the three months ended June 30, 2009, due to lower coal bed methane procurement cost. Gross margin for natural gas sold through pipelines was 30.2% during the three months ended June 30, 2009, and increased slightly as compared to 29.8% during the three months ended June 30, 2008. Gross margin for gasoline sales decreased from 8.1% during the three months ended June 30, 2008 to 6.3% during the three months ended June 30, 2009, due to the decrease of gasoline retail price exceeded the decrease of gasoline purchase cost. Gross margin for

our installation and auto conversion businesses were 61.4% and 42.0% during the three months ended June 30, 2009, respectively, and remained flat compared to 58.0% and 37.4% during the three months ended June 30, 2008. Due to the lower natural gas procurement cost, our total gross margin increased from 45.4% for the three months ended June 30, 2008 to 49.6% for the three months ended June 30, 2009.

Operating expenses

We incurred operating expenses of $3,514,138 for the three months ended June 30, 2009, an increase of $905,464 or 34.7%, compared to $2,608,674 for the three months ended June 30, 2008. Sales and marketing costs increased 48.6% from $1,568,674 for the three months ended June 30, 2008 to $2,331,739 for the three months ended June 30, 2009, primarily due to the $414,524 increase in depreciation expense as well as $129,303 and $99,288 increase in leasing and utility expense, respectively, mainly related to the acquisition of Lingbao Natural Gas, Co. in Oct. 2008 as well as the addition of 6 new fueling stations added since the second quarter of 2008. In addition, we also increased our efforts to obtain new residential and commercial customers and attract customers to our fueling stations. General and administrative expenses increased from $1,040,000 for the three months ended June 30, 2008 to $1,182,399 for the three months ended June 30, 2009 mainly due to increase of $275,583 in depreciation expense and $164,725 increase in salary expense primarily reflecting the growth of employees, the recruiting of qualified Chief Financial Officer as well as adjustment of compensation for our Chief Executive Officer to market rate, offset by $223,048 decrease in professional service fees. The transportation cost per million cubic meters of natural gas during the three months ended June 30, 2009 was approximately $2,384.

Income from Operations and Operating Margin

For the foregoing reasons, income from operations increased by $1,706,963, or 33.8%, to $6,764,052 for the three months ended June 30, 2009, from $5,057,089 for the three months ended June 30, 2008. Our operating margin for the three months ended June 30, 2009 was 32.6%, compared to 29.9% for the three months ended June 30, 2008.

Non-Operating Income (Expense)

Our non-operating expense increased by $1,033,089, or 151.6%, to $1,714,613 for the three months ended June 30, 2009, from $681,524 for the three months ended June 30, 2008, primarily due to the recognition of $1,312,834 non-operating expense related to change in fair value of the Company’s outstanding warrants.

Provision for Income Tax

Income tax was $1,186,683 for the three months ended June 30, 2009, as compared to $862,673 for the three months ended June 30, 2008 which is in line with the sales growth.

Net Income

Based on the foregoing, net income increased to $3,862,756 for the three months ended June 30, 2009, an increase of $349,864, or 10.0%, from $3,512,892 for the three months ended June 30, 2008. Net margin decreased from 20.8% during the three months ended June 30, 2008 to 18.6% during the three months ended June 30, 2009. The reduced net margin reflects the non-operating expenses related to fair value change of the Company’s outstanding warrants.

Six Months Ended June 30, 2009 Compared to Six Months Ended June 30, 2008

The following table represents the consolidated operating results for the six month period ended June 30, 2009 and 2008:

Sales Revenues

The following table sets forth a breakdown of our revenues for the period indicated:

	June 30, 2009	June 30, 2008	Increase in dollar	Increase in Percentage
Natural gas from fueling stations	$ 29,309,243	$ 23,940,566	$ 5,368,677	22.4%
Natural gas from pipelines	1,377,255	1,199,619	177,636	14.8%
Gasoline	2,807,414	2,278,847	528,567	23.2%
Installation	4,604,043	2,352,570	2,251,473	95.7%
Auto conversion	1,172,231	1,144,558	27,673	2.4%
Total	$ 39,270,186	$ 30,916,160	$ 8,354,026	27.0%

Overall. Total revenue for the six months ended June 30, 2009 increased to $39,270,186 from $30,916,160 for the six months ended June 30, 2008, an increase of $8,354,026 or 27.0%. This increase was mainly due to the addition of 9 new fueling stations added since the first quarter of 2008, and an increase in the number of residential and commercial pipeline customers to 103,343 as of June 30, 2009 from 91,967 as of June 30, 2008. We sold natural gas of 86,373,816 cubic meters during the six months ended June 30, 2009, compared to 73,255,739 cubic meters during the six months ended June 30, 2008. For the six months ended June 30, 2009, 85.3% of our revenue was generated from the sale of natural gas and gasoline, and the other 14.7% was generated from our installation and auto conversion services.

Natural Gas from Fueling Stations. Natural gas revenue from our fueling stations increased by 22.4%, or $5,368,677, to $29,309,243 during the six months ended June 30, 2009, from $ 23,940,566 during the six months ended June 30, 2008, and contributed to 74.6% of our total revenue, which was the largest among our four major business lines. The increase of natural gas revenue was mainly due to the increase of sales volume generated from the newly added fueling stations since the first quarter of 2008. During the six months ended June 30, 2009, we sold compressed natural gas of 80,446,633 cubic meters, compared to 67,844,028 cubic meters during the six months ended June 30, 2008 through our fueling stations. In terms of average station sales value and volume, in the six months ended June 30, 2009, we sold approximately $837,407 and 2,298,475 cubic meters of compressed natural gas per station, compared to approximately $886,688 and 2,512,742 cubic meters in the six months ended June 30, 2008. The reason for the decline in per station sales was due to the construction of main subway lines in Xi'an, which caused certain bus routes to deviate from our stations. Unit selling price remained constant at $ 0.36 (RMB 2.5) per cubic meter.

Natural Gas from Pipelines. Natural gas revenue from our pipelines increased by 14.8%, or $177,636, to $1,377,255 during the six months ended June 30, 2009, from $1,199,619 during the six months ended June 30, 2008, and contributed to 3.5% of our total revenue. As of June 30, 2009, the Company had 103,343 pipeline customers, an increase of 11,376 customers comparing to as of June 30, 2008. We also sold 5,927,183 cubic meters of natural gas through our pipelines during the six months ended June 30, 2009, compared to 5,411,712 cubic meters during the six months ended June 30, 2008.

Gasoline. Revenue from gasoline sales increased by 23.2%, or $528,567, to $2,807,414 during the six months ended June 30, 2009, from $2,278,847 during the six months ended June 30, 2008, and contributed 7.1% to our total revenue. The gasoline revenue increase was due to the sales volume increased 39% from 3,507,054 liters to 4,878,763 liters, offset by 17% decrease of unit sales price from $0.67 (RMB 4.59) per liter in the six months ended June 30,

2008 to $0.57 (RMB 3.93) per liter in the six months ended June 30, 2009, affected by the decrease of international fuel price since the 3rd quarter of 2008.

Installation Services. Revenue from installation services increased by 95.7%, or $2,251,473, to $4,604,043 during the six months ended June 30, 2009, from $2,352,570 during the six months ended June 30, 2008, and contributed 11.7% to our total revenue. The increase of installation revenue was mainly due to the increase of pipeline customers in the newly acquired subsidiary- Lingbao Natural Gas, Co. since January 2009. Installation services to our top four customers contributed to 18.4%, 13.2%, 11.0% and 6.7% of our installation revenue for the six months ended June 30, 2009.

Auto Conversion Services. Revenue from our auto conversion division increased by 2.4%, or $27,673, to $1,172,231 during the six months ended June 30, 2009, from $1,144,558 during the six months ended June 30, 2008, and contributed 3.0% to our total revenue.

Cost of Revenue:

The following table sets forth a breakdown of our cost of revenue for the periods indicated:

	June 30, 2009	June 30, 2008	Increase / (Decrease) in dollar amount	Increase in percentage
Natural gas from fueling stations	$ 13,267,616	$ 12,539,977	$ 727,640	5.8%
Natural gas from pipelines	969,831	856,766	113,065	13.2%
Gasoline	2,659,809	2,123,015	536,974	25.3%
Installation	1,761,979	933,201	828,778	88.8%
Auto conversion	699,109	708,962	(9,853)	(1.4)%
Total	$ 19,358,344	$ 17,161,921	$ 2,196,423	12.8%

Overall. Our cost of revenue consists of the cost of natural gas and gasoline sold, installation and other costs. Cost of natural gas and gasoline sold consists of the cost for purchase from our suppliers. Cost of installation and other costs include certain expenditures for the connection of customers to our pipeline system, and the cost for converting gasoline-fueled vehicles into natural gas hybrid vehicles.

Our cost of revenue for the six months ended June 30, 2009 was $19,358,344, an increase of $2,196,423, or 12.8%, from $17,161,921for the six months ended June 30, 2008, while our revenue increased by 27.0% during the same period.

Natural Gas from Fueling Stations. Cost of revenue of our natural gas for our fueling stations increased by 5.8%, or $727,640, to $13,267,616 during the six months ended June 30, 2009, as compared to $12,539,977 for the six months ended June 30, 2008. The low growth rate for cost of natural gas for our fueling stations was primarily due to the decrease of procurement price in coal bed methane as we obtained better term from July 2008 in Henan province that reduced our unit cost from one of our major supplier by approximately 33%, and our overall average unit cost reduced by 16% during the six months ended June 30, 2009.

Natural Gas from Pipelines. Cost of revenue of our natural gas sold through our pipelines increased by 13.2%, or $ 113,065, to $969,831 during the six months ended June 30, 2009, as compared to $856,766 during the six months ended June 30, 2008, which was in line with the sales growth.

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Gasoline. Cost of our gasoline revenue increased by 25.3%, to $2,659,809 during the six months ended June 30, 2009, from $2,123,015 for the six months ended June 30, 2008. The increase of cost of gasoline revenue was due to the increase in sales volume, offset by the effect of the decrease of average unit cost from $0.63 (RMB 4.27) per liter during the six months ended June 30, 2008 to $0.55 (RMB 3.72) per liter during the six months ended June 30, 2009 due to the decrease price of the international fuel market.

Installation Services. Cost of revenue from our installation services increased by 88.8%, or $828,778, to $1,761,979 during the six months ended June 30, 2009, as compared to $933,201 during the six months ended June 30, 2008, as a result of the increase of pipeline customers.

Auto Conversion Services. Cost of our auto conversion revenue decreased by 1.4%, or $9,853, to $699,109 during the six months ended June 30, 2009, as compared to $708,962 during the six months ended June 30, 2008.

Gross profit

The following table sets forth a breakdown of our gross profit for the periods indicated:

	June 30, 2009	June 30, 2008	Increase in dollar amount	Increase in percentage
Natural gas from filling stations	$ 16,041,627	$ 11,400,589	$ 4,641,038	40.7%
Natural gas from pipelines	407,424	342,853	64,571	18.8%
Gasoline	147,605	155,832	(8,227)	(5.3)%
Installation	2,842,064	1,419,369	1,422,695	100.2%
Auto conversion	473,122	435,596	37,526	8.6%
Total	$ 19,911,842	$ 13,754,239	$ 6,157,603	44.8%

We earned a gross profit of $19,911,842 for the six months ended June 30, 2009, an increase of $6,157,603 or 44.8%, compared to $13,754,239 for the six months ended June 30, 2008. In summary, gross profit increase was mainly due to the increased sales volume of natural gas from fueling stations with lower unit purchase cost from our major suppliers; the increased sales volume of pipeline natural gas with stable unit price and cost; and the increased installation revenue from new pipeline customers.

Gross margin

Gross margin for natural gas sold through our fueling stations increased from 47.6% in the six months ended June 30, 2008 to 54.7% in the six months ended June 30, 2009, due to lower coal bed methane procurement cost. Gross margin for natural gas sold through pipelines was 29.6% during the six months ended June 30, 2009, and increased slightly as compared to 28.6% during the six months ended June 30, 2008. Gross margin for gasoline sales decreased from 6.8% during the six months ended June 30, 2008 to 5.3% during the six months ended June 30, 2009, due to the decrease of gasoline retail price exceeded the decrease of gasoline purchase cost. Gross margin for our installation and auto conversion businesses were 61.7% and 40.4% during the six months ended June 30, 2009, respectively, and remained flat compared to 60.3% and 38.1% during the six months ended June 30, 2008. Due to the lower natural gas procurement cost, our total gross margin increased from 44.5% for the six months ended June 30, 2008 to 50.7% for the six months ended June 30, 2009.

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Operating Expenses

We incurred operating expenses of $7,520,287 for the six months ended June 30, 2009, an increase of $2,630,674 or 53.8%, compared to $4,889,613 for the six months ended June 30, 2008. Sales and marketing costs increased 60.0% from $2,910,288 for the six months ended June 30, 2008 to $4,655,967 for the six months ended June 30, 2009, primarily due to $860,816 increase in depreciation expense as well as $436,206 and $220,088 increase in leasing and utility expense, respectively, primarily related to the acquisition of Lingbao Natural Gas, Co. as well as the addition of 9 new fueling stations since the first quarter of 2008. In addition, we also increased our efforts to obtain new residential and commercial customers and attract customers to our fueling stations. General and administrative expenses increased from $1,979,325 for the six months ended June 30, 2008 to $2,864,320 for the six months ended June 30, 2009 mainly due to $561,216 increase in depreciation expense and $407,229 increase in salary expense primarily reflecting the growth of employees, the recruiting of qualified Chief Financial Officer as well as adjustment of compensation for our Chief Executive Officer to market rate. The transportation cost per million cubic meters of natural gas during the six months ended June 30, 2009 was approximately $2,648.

Income from Operations and Operating Margin

For the foregoing reasons, income from operations increased by $3,526,929, or 39.8%, to $12,391,555 for the six months ended June 30, 2009, from $8,864,626 for the six months ended June 30, 2008. Our operating margin for the six months ended June 30, 2009 was 31.6%, compared to 28.7% for the six months ended June 30, 2008.

Non-Operating Income (Expense)

Our non-operating expense increased by $1,150,212, or 115.8%, to $2,143,237 for the six months ended June 30, 2009, from $993,025 for the six months ended June 30, 2008, primarily due to the recognition of $1,115,783 non-operating expense related to change in fair value of the Company’s outstanding warrants.

Provision for Income Tax

Income tax was $2,183,939 for the six months ended June 30, 2009, as compared to $1,550,138 for the six months ended June 30, 2008 which is in line with the sales growth.

Net Income

Based on the foregoing, net income increased to $8,064,379 for the six months ended June 30, 2009, an increase of $1,742,916, or 27.6%, from $6,321,463 for the six months ended June 30, 2008. Net margin stabilized at 20.5% in the six months ended June 30, 2009 as compared to 20.5% in the six months ended June 30, 2008. Increase in net income attributed to our increased revenues, supported by lower natural gas procurement prices. The stable net margin reflects the increase of net income, offset by the effect of non-operating expenses related to fair value change of the Company’s outstanding warrants.

LIQUIDITY AND CAPITAL RESOURCES

Historically, our primary sources of liquidity have consisted of cash generated from our operations and debt financing. In 2008, we sold senior notes with a face value of $40 million to Abax Lotus Ltd. Our principal uses of cash have been, and are expected to continue to be, for operational purposes as well as for constructing and acquiring natural gas fueling stations and constructing our LNG plant.

As of June 30, 2009, the Company had $9,701,176 of cash and cash equivalents on hand compared to $29,180,315 of cash and cash equivalents as of June 30, 2008. The decrease was primarily attributable to the sale of senior notes to Abax Lotus Ltd. in the amount of $40,000,000 during the six months ended March 31, 2008.

Net cash provided by operating activities was $14,396,765 for the six months ended June 30, 2009 compared to net cash provided by operations of $8,126,132 for the six months ended June 30, 2008. The primary reason for the change was due to the increase in net income, adjusted for non-cash expenses items of $4,289,751 and change in working capital of $2,042,635.

Net cash used investing activities decreased from $30,394,475 during the six months ended June 30, 2008 to $10,544,353 for the same period in 2009 primarily because of our addition of fueling stations, prepayment to equipment suppliers of the LNG plant and additions to our construction in progress during the six months ended June 30, 2008. For the six months ended June 30, 2009, major cash outflow were primarily to our construction in progress.

We had no net cash provided by financing activities for the six months ended June 30, 2009, compared to net cash provided by financing activities of $37,877,491 during the six months ended June 30, 2008, due to the sale of senior notes to Abax Lotus Ltd.

The Company paid $10,372,858 to the LNG processing plant as a prepayment on equipment as well as addition to construction in progress during the six months ended June 30, 2009.

Based on past performance and current expectations, we believe our cash and cash equivalents, cash generated from operations, as well as future possible cash from financing activities, will satisfy our working capital needs, capital expenditures and other liquidity requirements associated with our operations for at least the next 12 months.

The majority of our revenues and expenses were denominated primarily in RMB, the currency of the People's Republic of China. There is no assurance that exchange rates between the RMB and the USD will remain stable. Inflation has not had a material impact on our business.

OFF-BALANCE SHEET ARRANGEMENTS

None.

CAPITAL EXPENDITURES

Our planned capital expenditures as of June 30, 2009 were $35 million, which we expect to be incurred in connection with the construction of our LNG facility, joint-venture cooperation with CNPC Kunlun and the acquisition of additional CNG fueling stations. To the extent we engage in additional projects in the near future and to the extent we do not have sufficient internal financial resources to fund capital expenditures associated with such projects, we will need to obtain additional financing to fund such capital expenditures from third party sources, including from the capital markets.

CONTRACTUAL OBLIGATIONS

Our contractual obligations are as follows:

		Payments due by period			
Contractual obligations	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
			(in thousands)		
Long-Term Debt Obligations	40,000	-	6,667	33,333	$ -
Other Long-Term Liabilities Reflected on Company's Balance Sheet	17,500	-	-	-	17,500(1)
Total	57,500	-	6,667	33,333	$ 17,500

Note:

(1) The $17,500,000 reflects derivative liability related to the embedded put option in the 1,450,000 warrants we issued to Abax in January 2008. If Abax does not exercise the warrants by January 29, 2015, Abax will be entitled to require that we purchase the warrants for $17,500,000 at that time.

COMMITMENTS AND CONTINGENCIES

Lease Commitments

We recognize lease expense on a straight-line basis over the term of the lease in accordance to FAS 13, “Accounting for leases.” We entered into series of long-term lease agreements with outside parties to lease land use right to the self-built natural gas fueling stations located in the PRC. The agreements have terms ranging from 10 to 30 years. We make annual prepayment for most lease agreements. We also entered into two office leases in Xian, PRC and New York, NY. The minimum future payment for leasing land use rights and offices is as follows:

Year ending December 31, 2009	$ 430,734
Year ending December 31, 2010	1,458,518
Year ending December 31, 2011	1,577,171
Year ending December 31, 2012	1,339,207
Year ending December 31, 2013	1,280,490
Thereafter	21,923,925
Total	$ 28,010,045

For the three months ended June 30, 2009 and 2008, the land use right and office lease expenses were $406,016 and $ 310,698, respectively. For the six months ended June 30, 2009 and 2008, the land use right and office lease expenses were $798,097 and $373,945 respectively.

Property and Equipment

On January 25, 2008, we entered into a contract with Chemtex International Inc. ("Chemtex") to acquire certain exclusive rights relating to the technical know-how and designing of our LNG plant and LNG storage tank in Jingbian county, Shaanxi province, China, in the total amount of $9,500,000. On April 13, 2008, our subsidiary, XXNGC, entered into a contract with Chemtex to purchase equipment supply for the LNG plant and LNG storage tank in the total amount of $13,700,000 (the "Chemtex Purchase Agreement"). The $13,700,000 purchase price was reduced to $13,100,000 under an amendment to the Chemtex Purchase Agreement with Chemtex in September 2008. On May 16, 2008, SJLNG entered into an agreement with Hebei Tongchan Import and Export Co. Ltd. ("Hebei") and agreed that Hebei will act as the trade agency for SJLNG. On June 18, 2008, XXNGC amended the April 13, 2008 with Chemtex and assigned Hebei to purchase the LNG equipment for the LNG plant and LNG storage tank and Hebei succeeded the rights and obligations of XXNGC under Chemtex Purchase Agreement.

As of June 30, 2009, we advanced $6,299,500 to Hebei and the future commitment for equipment is $7,400,500.

Natural Gas Purchase Commitments

We have certain effective natural gas purchase agreements with our major suppliers. The natural gas purchase agreement with Shaanxi Provincial Natural Gas Co., Ltd. has been renewed annually to date and specifies a maximum amount that can be purchased but does not specify a minimum amount that must be purchased. Our natural gas purchase agreements with certain suppliers of coal-bed methane are of indefinite terms and do not contain either maximum or minimum amounts of purchase. Without minimum purchase requirements under any of our natural gas purchase agreements, we have the flexibility to constantly look for lower-cost sources of supply.

Legal Proceedings

A former member of the board of directors filed a lawsuit on June 16, 2008 against the Company in New York State Supreme Court, Nassau County, in which he has sought, among other things, to recover a portion of his monthly compensation plus 20,000 options that he alleges are due to him pursuant to a written agreement. After the plaintiff rejected an offer by the Company that included the options that plaintiff alleged were due to him, the Company moved to dismiss the complaint. The judge ordered the Company to issue the 20,000 options to the plaintiff subject to any restrictions required by applicable securities laws, which was essentially what the Company had previously offered, and dismissed all of the plaintiff's remaining claims against the Company. The current board of directors has complied with the court's decision by tendering an option agreement to the plaintiff consistent with the court's decision, but the plaintiff has refused to execute the agreement, and instead has filed an appeal. Regardless of the outcome of the appeal, we believe that any liability we would incur will not have a materially adverse effect on our financial condition or our results of operations.

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FOREIGN CURRENCY TRANSLATIONS

As of June 30, 2009 and December 31, 2008, our accounts were maintained, and our consolidated financial statements were expressed in RMB. Such consolidated financial statements were translated into USD in accordance with Statement of Financial Accounts Standards ("SFAS") 52, "Foreign Currency Translation," with the RMB as the functional currency. According to SFAS 52, all assets and liabilities were translated at the exchange rate as of the balance sheet date, stockholders' equity were translated at the historical rates and statement of income and cash flow items were translated at the weighted average exchange rate for the year. The resulting translation adjustments are reported under other comprehensive income in accordance with SFAS 130, "Reporting Comprehensive Income." In accordance with SFAS 95, "Statement of Cash Flows," cash flows from the Company's operations is calculated based upon the local currencies and translated to USD at average translation rates for the period. As a result, translation adjustments amounts related to assets and liabilities reported on the consolidated statement of cash flows will not necessarily agree with changes in the corresponding consolidated balances on the balance sheet.

The balance sheet amounts with the exception of equity at June 30, 2009 were translated RMB6.83 to $1.00 as compared to RMB6.82 at December 31, 2008. The equity accounts were stated at their historical rate. The average translation rates applied to income and cash flow statement amounts for the six months ended June 30, 2009 and 2008, were 6.82 RMB and 7.05 RMB to $1.00, respectively.

CRITICAL ACCOUNTING POLICIES

Revenue Recognition

Our revenue recognition policies are in accordance with Staff Accounting Bulletin (SAB) 104. Revenue is recognized when services are rendered to customers when a formal arrangement exists, the price is fixed or determinable, the delivery is completed, no other significant obligations of the Company exist and collectability is reasonably assured. Payments received before all of the relevant criteria for revenue recognition are satisfied are recorded as unearned revenue. Revenue from gas and gasoline sales is recognized when gas and gasoline is pumped through pipelines to the end users. Revenue from installation of pipelines is recorded when the contract is completed and accepted by the customers. The construction contracts are usually completed within one to two months. Revenue from repairing and modifying vehicles is recorded when service are rendered to and accepted by the customers.

Accounts Receivables

Accounts and other receivables are recorded at net realizable value consisting of the carrying amount less an allowance for uncollectible accounts, as needed. The Company allowance for uncollectible accounts is not significant.

We maintain reserves for potential credit losses on accounts receivable. Management reviews the composition of accounts receivable and analyzes historical bad debts, customer concentrations, customer credit worthiness, current economic trends and changes in customer payment patterns to evaluate the adequacy of these reserves. Reserves are recorded primarily on a specific identification basis. Our management determined that all receivables are good and there is no need for a bad debt reserve as of June 30, 2009.

Other Receivable – Employee Advances

From time to time, we advance predetermined amounts based upon internal Company policy to certain employees and internal units to ensure certain transactions to be performed in a timely manner. We have full oversight and control over the advanced accounts. Therefore, no allowance for the uncollectible accounts is needed.

Inventory

Inventory is stated at the lower of cost, as determined on a first-in, first-out basis, or market. Management compares the cost of inventories with the market value, and allowance is made for writing down the inventories to their market value, if lower. Inventory consists of material used in the installation of pipelines and material used in repairing and modifying of vehicles. Inventory also consists of gasoline.

Fair Value of Financial Instruments

FAS 107, “Disclosure About Fair Value of Financial Instruments” defines financial instruments and requires fair value disclosure of applicable financial instruments. FAS 157, “Fair Value Measurements,” adopted January 1, 2008, defines fair value, establishes a three-level valuation hierarchy for disclosures of fair value measurement and enhances disclosure requirements for fair value measures. The carrying amounts reported in the consolidated balance sheets for current receivables and payables qualify as financial instruments. Management concluded the carrying values are a reasonable estimate of fair value because of the short period of time between the origination of such instruments and their expected realization and if applicable, their stated interest rate approximates current rates available. The three levels are defined as follows:

- Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

- Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

- Level 3 inputs to the valuation methodology are unobservable and significant to the fair value measurement.

We analyze all financial instruments with features of both liabilities and equity under SFAS 150, “Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity,” SFAS 133, “Accounting for Derivative Instruments and Hedging Activities” and EITF 00-19, “Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company’s Own Stock.”

As required by SFAS 157, financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Depending on the product and the terms of the transaction, the fair value of our notes payable and derivative liabilities were modeled using a series of techniques, including closed-form analytic formula, such as the Black-Scholes option-pricing model, which does not entail material subjectivity because the methodology employed does not necessitate significant judgment, and the pricing inputs are observed from actively quoted markets.

Effective January 1, 2009, we adopted the provisions of EITF 07-5, "Determining Whether an Instrument (or Embedded Feature) is Indexed to an Entity’s Own Stock”, which is effective for financial statements for fiscal years beginning after December 15, 2008 and which replaced the previous guidance on this topic in EITF 01-6. Paragraph 11(a) of FAS 133 specifies that a contract that would otherwise meet the definition of a derivative but is both (a) indexed to the Company’s own stock and (b) classified in stockholders’ equity in the statement of financial position would not be considered a derivative financial instrument. EITF 07-5 provides a new two-step model to be applied in determining whether a financial instrument or an embedded feature is indexed to an issuer’s own stock and thus able to qualify for the FAS 133 paragraph 11(a) scope exception.

Unearned Revenue

Unearned revenue represents prepayments by customers for gas purchases and advance payments on installation of pipeline contracts. We record such prepayment as unearned revenue when the payments are received.

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RECENT ACCOUNTING PRONOUNCEMENTS

In January 2009, the FASB issued FSP EITF 99-20-1, “Amendments to the Impairment Guidance of EITF Issue No. 99-20, “Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets”. FSP EITF 99-20-1 changes the impairment model included within EITF 99-20 to be more consistent with the impairment model of SFAS 115. FSP EITF 99-20-1 achieves this by amending the impairment model in EITF 99-20 to remove its exclusive reliance on “market participant” estimates of future cash flows used in determining fair value. Changing the cash flows used to analyze other-than-temporary impairment from the “market participant” view to a holder’s estimate of whether there has been a “probable” adverse change in estimated cash flows allows companies to apply reasonable judgment in assessing whether an other-than-temporary impairment has occurred. The adoption of FSP EITF 99-20-1 did not have a material impact on our consolidated financial statements because all of our investments in debt securities are classified as trading securities.

In April 2009, the FASB issued FSP FAS 157-4, “Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly” (FSP FAS 157-4). FSP FAS 157-4 amends SFAS 157 and provides additional guidance for estimating fair value in accordance with SFAS 157 when the volume and level of activity for the asset or liability have significantly decreased and also includes guidance on identifying circumstances that indicate a transaction is not orderly for fair value measurements. This FSP shall be applied prospectively with retrospective application not permitted. The adoption of FSP FAS 157-4 did not have a material impact on our consolidated financial statements.

In April 2009, the FASB issued FSP FAS 115-2 and FAS 124-2. This FSP amends SFAS 115, “Accounting for Certain Investments in Debt and Equity Securities,” SFAS 124, “Accounting for Certain Investments Held by Not-for-Profit Organizations,” and EITF Issue No. 99-20, “Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to Be Held by a Transferor in Securitized Financial Assets,” to make the other-than-temporary impairments guidance more operational and to improve the presentation of other-than-temporary impairments in the financial statements. This FSP will replace the existing requirement that the entity’s management assert it has both the intent and ability to hold an impaired debt security until recovery with a requirement that management assert it does not have the intent to sell the security, and it is more likely than not it will not have to sell the security before recovery of its cost basis. This FSP provides increased disclosure about the credit and noncredit components of impaired debt securities that are not expected to be sold and also requires increased and more frequent disclosures regarding expected cash flows, credit losses, and an aging of securities with unrealized losses. Although this FSP does not result in a change in the carrying amount of debt securities, it does require that the portion of an other-than-temporary impairment not related to a credit loss for a held-to-maturity security be recognized in a new category of other comprehensive income and be amortized over the remaining life of the debt security as an increase in the carrying value of the security. The adoption of FSP FAS 115-2 and FAS 124-2 did not have a material impact on our consolidated financial statements.

In April 2009, the FASB issued FSP FAS 107-1 and APB 28-1. This FSP amends SFAS No. 107, “Disclosures about Fair Value of Financial Instruments,” to require disclosures about fair value of financial instruments not measured on the balance sheet at fair value in interim financial statements as well as in annual financial statements. Prior to this FSP, fair values for these assets and liabilities were only disclosed annually. This FSP applies to all financial instruments within the scope of SFAS 107 and requires all entities to disclose the method(s) and significant assumptions used to estimate the fair value of financial instruments. The adoption of FSP FAS 107-1 and APB 28-1 did not have a material impact on our consolidated financial statements.

In May 2009, the FASB issued Statement of Financial Accounting Standards No. 165, “Subsequent Events,” (FAS 165, Subsequent Events [ASC 855-10-05], which provides guidance to establish general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available

to be issued. FAS 165 also requires entities to disclose the date through which subsequent events were evaluated as well as the rationale for why that date was selected. FAS 165 is effective for interim and annual periods ending after June 15, 2009, and accordingly, we adopted this Standard during the second quarter of 2009. FAS 165 requires that public entities evaluate subsequent events through the date that the financial statements are issued. We have evaluated subsequent events through the time of filing these consolidated financial statements with the SEC on August 10, 2009.

In June 2009, the FASB issued Statement No. 166, Accounting for Transfers of Financial Assets – an amendment of FASB No. 140 (“FAS 140”), Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities (“FAS 166”) [ASC 860]. FAS 166 amends the criteria for a transfer of a financial asset to be accounted for as a sale, redefines a participating interest for transfers of portions of financial assets, eliminates the qualifying special-purpose entity concept and provides for new disclosures. FAS 166 is effective for the Company beginning in 2010. Should the Company’s accounts receivable securitization programs not qualify for sale treatment under the revised rules, future securitization transactions entered into on or after January 1, 2010 would be classified as debt and the related cash flows would be reflected as a financing activity. We are currently assessing the impact of the standard on its securitization programs.

In June 2009, the FASB issued Statement of Financial Accounting Standards No. 167, Amendments to FASB Interpretation No. 46(R) (“FAS 167”) [ASC 810-10], which modifies how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. FAS 167 clarifies that the determination of whether a company is required to consolidate an entity is based on, among other things, an entity’s purpose and design and a company’s ability to direct the activities of the entity that most significantly impact the entity’s economic performance. FAS 167 requires an ongoing reassessment of whether a company is the primary beneficiary of a variable interest entity. FAS 167 also requires additional disclosures about a company’s involvement in variable interest entities and any significant changes in risk exposure due to that involvement. FAS 167 is effective for fiscal years beginning after November 15, 2009. We are currently assessing the impact of the standard on its securitization programs.

In June 2009, the FASB issued Statement of Financial Accounting Standards No. 168, The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles a Replacement of FASB Statement No. 162 (“FAS 168”). This Standard establishes the FASB Accounting Standards Codification™ (the “Codification”) as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with U.S. GAAP. The Codification does not change current U.S. GAAP, but is intended to simplify user access to all authoritative U.S. GAAP by providing all the authoritative literature related to a particular topic in one place. The Codification is effective for interim and annual periods ending after September 15, 2009, and as of the effective date, all existing accounting standard documents will be superseded. The Codification is effective for us in the third quarter of 2009, and accordingly, our Quarterly Report on Form 10-Q for the quarter ending September 30, 2009 and all subsequent public filings will reference the Codification as the sole source of authoritative literature.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Natural Gas Price Risk

Our major market risk exposure continues to be the pricing applicable to our purchases and value-added reselling of CNG. Our revenues and profitability depend substantially upon the applicable prices of natural gas, which in China are regulated and fixed by central and local governments and doesn’t fluctuate much at all. Such a price involatility situation is expected to continue for operations in China. We currently don’t have any hedge positions in place to reduce our exposure to changes in natural gas whole sale and retail prices.

Interest Rate Risk

We are subject to interest rate risk on our long-term fixed-interest rate debt. Fixed rate debt, where the interest rate is fixed over the life of the instrument, exposes us to changes in market interest rates reflected in the fair value of the debt and to the risk that we may need to refinance maturing debt with new debt at a higher rate. All other things being equal, the fair value of our fixed rate debt will increase or decrease as interest rates change. We had long-term debt outstanding of $40 million at June 30, 2009, all of which bears interest at fixed rates. The $40 million of fixed-rate debt is due on 2014. We currently have no interest rate hedge positions in place to reduce our exposure to changes in interest rates.

Foreign Currency Exchange Rates Risk

We operate in China local currency and the effects of foreign currency fluctuations are largely mitigated because local expenses in China are also denominated in the same currency.

Our assets and liabilities of which the functional currency is the China local currency are translated into U.S. dollars using the exchange rates in effect at the balance sheet date, resulting in translation adjustments that are reflected as Cumulative Translation Adjustment in the shareholders' equity section on our Consolidated Balance Sheets. A portion of our net assets are impacted by changes in foreign currencies in relation to the U.S. dollar. We recorded a $2,997 adjustment to decrease our equity account for the quarter ended June 30, 2009 to reflect the net impact of the fluctuating of Chinese currency against the U.S. dollar.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The Company's management has evaluated, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, the effectiveness of the design and operations of the Company's disclosure controls and procedures (as defined in Securities Exchange Act Rule 13a-15(e)), as of the end of the period covered by this quarterly report. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the evaluation of the effectiveness of our disclosure controls and procedures was completed; our disclosure controls and procedures were not effective.

Changes in internal control over financial reporting

We are devoting significant resources to remediating and improving our internal controls. From the second quarter of 2009, the Company has started to independently completing the consolidation of its financial statements in accordance with U.S. GAAP through recruiting of U.S. GAAP proficient accounting personnel. We are also allocating additional resources to train our existing accounting staff and will continue this effort in the future. Most of the policies, procedures and practices are already in place and being implemented. These initiatives include the following:

- Identifying and hiring additional personnel with U.S. GAAP and SEC reporting experience, including our new CFO Veronica Jing Chen and one ACCA (Association of Chartered Certified Accountants) affiliate, and starting to independently completing the U.S. GAAP based reporting in the second quarter of 2009;
- Recruiting of additional qualified accounting personnel to form a competent SEC reporting team;
- Hiring outside consultant to provide training to our finance personnel;
- Based on COSO framework, developing the scope of the Company's internal control system and enhancing the internal control function by establishing the Company's internal audit team containing one corporate control director and two full time employees;
- Introducing and implementing policies and procedures to effectively control daily cash transactions and recording;

Except as described above, there were no changes in our internal control over financial reporting during the quarter ended June 30, 2009 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

A former member of the board of directors filed a lawsuit against the Company in New York State Supreme Court, Nassau County, in which he has sought, among other things; to recover a portion of his monthly compensation plus 20,000 options that he alleges are due to him pursuant to a written agreement. After the plaintiff rejected an offer by the Company that included the options that plaintiff alleged were due to him, the Company moved to dismiss the complaint. The judge ordered the Company to issue the 20,000 options to the plaintiff subject to any restrictions required by applicable securities laws, which was essentially what the Company had previously offered, and dismissed all of the plaintiff's remaining claims against the Company. The current board of directors has complied with the

court's decision by tendering an options agreement to the plaintiff consistent with the court's decision, but the plaintiff has refused to execute the agreement, and instead has filed an appeal. Regardless of the outcome of the appeal, the Company believes that any liability it would incur will not have a materially adverse effect on its financial condition or its results of operations.

Item 1A. Risk Factors

As of the date of this filing, there have been no material changes from the risk factors disclosed in the Company's Annual Report on Form 10-K/A filed on July 20, 2009. We operate in a changing environment that involves numerous known and unknown risks and uncertainties that could materially affect our operations. The risks, uncertainties and other factors set forth in our Annual Report on Form 10-K/A may cause our actual results, performances and achievements to be materially different from those expressed or implied by our forward-looking statements. If any of these risks or events occur, our business, financial condition or results of operations may be adversely affected.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None

Item 6. Exhibits

(a) Exhibits

Exhibit Number	Description of Exhibit
31.1*	Certification of Principal Executive Officer pursuant to Rule 13a-14 and Rule 15d-14(a), promulgated under the Securities and Exchange Act of 1934, as amended
31.2*	Certification of Principal Financial Officer pursuant to Rule 13a-14 and Rule 15d 14(a), promulgated under the Securities and Exchange Act of 1934, as amended
32.1*	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer)
32.2*	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Financial Officer)

*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.

China Natural Gas, Inc.

August 10, 2009	By:	/s/ Qinan Ji
		Qinan Ji Chief Executive Officer (Principal Executive Officer)
August 10, 2009	By:	/s/ Veronica Chen
		Veronica Chen Chief Financial Officer (Principal Financial and Accounting Officer)

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