Qingdao Footwear, Inc.
Form 10-Q
November 15, 2010

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

FORM 10-Q

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

For the quarterly period ended September 30, 2010

Commission File Number: 000-53075

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

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

269 First Huashan Road
Jimo City, Qingdao, Shandong, PRC

(Address of principal executive office and zip code)

86-532-86595999

(Registrant’s telephone number, including area code)

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

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

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

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company x

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

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

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

QINGDAO FOOTWEAR, INC
Quarterly Period Ended September 30, 2010

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PART I:FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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

	September 30, 2010 (unaudited)	December 31, 2009
ASSETS		
Current assets		
Cash	$ 422,017	$ 61,131
Accounts receivable	251,903	98,962
Other receivable	6,764	-
Inventories	547,624	344,512
Prepaid expenses	780,514	57,311
Total current assets	2,008,822	561,916
Long term prepaid expenses	2,825,561	-
Property, plant and equipment, net	1,012,046	930,451
Construction in progress	577,776	-
Intangible assets	3,909,454	208,167
Total Assets	$ 10,333,659	$ 1,700,534
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 47,479	$ 15,727
Accrued liabilities and other payables	64,664	-
Short term loans	1,492,961	718,830
Taxes payable	16,789,481	12,551,687
Due to related parties	-	117,360
Total current liabilities	18,394,585	13,403,604
Long-term debt	253,803	249,390
Total Liabilities	$ 18,648,388	$ 13,652,994
Shareholders' Equity		
Series A preferred stock, .0001 par value, 10,000,000 shares authorized, none issued and outstanding	-	-
Common stock, .0001 par value, 100,000,000 shares authorized, 10,000,000 and 9,700,000 shares issued and outstanding, respectively	1,000	970
Additional paid-in capital	762,091	319,510
Accumulated other comprehensive income	500,367	440,775
Retained earnings (deficits)	(9,578,187)	(12,713,715)

Total Shareholders’ Equity	$ (8,314,729)	$ (11,952,460)
Total Liabilities and Shareholders' Equity	$ 10,333,659	$ 1,700,534

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

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QINGDAO FOOTWEAR, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
FOR THE THREE MONTHS AND NINE MONTHS ENDED SEPTEMBER 30, 2010 AND 2009
UNAUDITED

	Three Months Ended		Nine Months Ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Net sales	$ 3,715,217	$ 2,918,275	$ 14,964,654	$ 12,517,751
Cost of sales	2,001,078	1,656,918	8,080,396	7,102,669
Gross Profit	1,714,139	1,261,357	6,884,258	5,415,082
Operating expenses:				
Selling, general and administrative expenses	447,127	193,221	1,551,990	642,681
Depreciation and Amortization Expense	41,378	17,706	100,695	43,964
Income from operations	1,225,634	1,050,430	5,231,573	4,728,437
Other income (expense)				
Rental income	22,010	21,995	66,017	65,966
Interest income	3,714	-	22,301	-
Interest expense	(26,264)	(14,409)	(75,431)	(41,087)
Income before income taxes	1,225,094	1,058,016	5,244,460	4,753,316
Income taxes	306,273	265,704	1,421,768	1,188,329
Net income	$ 918,821	$ 792,312	$ 3,822,692	$ 3,564,987
Earnings per share - basic and diluted	$ 0.09	$ 0.08	$ 0.38	$ 0.37
Weighted average shares outstanding-basic and diluted	10,000,000	9,700,000	10,000,000	9,700,000
Net income	$ 918,821	$ 792,312	$ 3,822,692	$ 3,564,987
Other comprehensive income				
Foreign currency translation	45,336	5,466	59,592	(2,473)
Comprehensive income	$ 964,157	$ 797,778	$ 3,882,284	$ 3,562,514

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

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

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009 (Restated)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 3,822,692	$ 3,564,987
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	100,695	43,964
Stock based compensation	442,611	-
Changes in operating assets and liabilities:		
Accounts receivable	(151,190)	(69,020)
Inventories	(197,015)	(409,040)
Prepaid expenses	(3,554,514)	(37,961)
Accounts payable and accrued liabilities	67,249	26,519
Tax payable	4,015,673	3,471,783
Net cash provided by operating activities	4,546,201	6,591,232
CASH FLOWS FROM INVESTING ACTIVITIES		
Advance on note receivable	(447,888)	-
Proceeds from note receivable	447,888	-
Advance to related party	(119,437)	-
Cash paid for property and equipment	(132,804)	(376,899)
Cash paid for construction in progress	(548,887)	-
Cash paid for intangible asset	(3,732,402)	-
Net cash used in investing activities	(4,533,530)	(376,899)
CASH FLOWS FROM FINANCING ACTIVITIES		
Distribution to shareholders	(484,565)	(6,173,583)
Proceeds from loans	1,194,369	718,830
Repayments on loans	(432,959)	(410,760)
Net cash provided by (used in) financing activities	276,845	(5,865,513)
Effect of exchange rate changes on cash	71,370	(2,440)
Net increase in cash	$ 360,886	$ 346,380
Cash, beginning of period	61,131	118,534
Cash, end of period	$ 422,017	$ 464,914
SUPPLEMENTARY DISCLOSURE:		
Interest paid	$ 75,431	$ 41,087
Income tax paid	$ 1,149	$ 3,760

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

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

NOTE 1 - ORGANIZATION AND BUSINESS OPERATIONS

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

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

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

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

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

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

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

These accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission, and should be read in conjunction with the December 31, 2009 audited financial statements of the Company and the notes thereto as included in the Company's Form PRER14C filed on April 19, 2010 and 10-K/A filed on November 4, 2010. In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for fair presentation of financial position and results of operations for the interim periods presented have been reflected herein. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year. Notes to the consolidated financial statements, which would substantially duplicate the disclosure required in the Company's December 31, 2009 annual financial statements have been omitted.

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

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

Use of Estimates

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

Concentration of Credit Risk

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

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

Land Use Rights

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

The Company paid in advance for the lease of two parcels of land consisting of approximately $246,000 and $3,732,000 for 50-year and 60-year time period, respectively. The lease period began during 2003 and 2010 and expire during 2053 and 2070, respectively. The amount is being amortized and recorded as expense over the 50-year and 60-year terms of the leases, respectively.

Comprehensive Income

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

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

Value Added Tax

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

The Company has not paid substantial amount of VAT it owes, which carries on its balance sheet as taxes payable.

Revenue Recognition

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

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

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

Earnings per Share

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

NOTE 3 – NOTES RECEIVABLE

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

NOTE 4 – PREPAID EXPENSES

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

	September 30, 2010	December 31, 2009
Prepaid rent	$ 2,090,514	$ 18,778
Prepaid advertising fee	1,152,756	-
Prepaid maintenance fee	335,916	-
Prepaid miscellaneous fee	26,889	38,533
	$ 3,606,075	$ 57,311
Minus: current portion	780,514	57,311
Long term portion	2,825,561	-

Long term prepaid rent is for three retail store leases with lease terms arranging from 3, 10, and 15 years, respectively. Long term advertising prepayment is for advertisement contracts with period ranging from two to five years. Long term maintenance prepayment is for a five-year landscaping maintenance contract and the whole contract was paid in advance.

NOTE 5 – INTANGIBLE ASSETS

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

	September 30, 2010	December 31, 2009
Cost of land use right	3,978,740	242,055

Less: accumulated amortization		69,286		33,888
Land use rights, net	$	3,909,454	$	208,167

Amortization expense for the three and nine months ended September 30, 2010 and 2009 was $16,493 and $34,194, $1,208 and $3,628, respectively.

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

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

2010 (for the remaining three months)	$ 16,783
2011	67,133
2012	67,133
2013	67,133
2014	67,133
2015	67,133
Thereafter	3,557,006
Total	$ 3,909,454

In April 2010, the Company purchased land use rights in Jimo, Shandong Province for $3,732,402. By September 30, 2010, the amount has been paid off. The company is still in the process of obtaining the title of the land use right.

NOTE 6 - SHORT TERM LOANS

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

	September 30, 2010	December 31, 2009
JMRB, two 12-month bank loans both due in November 2010, bears annual interest at 7.965% average, secured by third parties	298,593	293,400
BOQ, 12-month bank loan due in September 2011, bears annual interest at 6.372% average, pledged by Company's building and land use right	746,480	-
BOQ, 12-month bank loan matured in September 2010, bears annual interest at 6.372% average, pledged by Company's building and land use right	-	425,430
JMRB, 12-month bank loan due in December 2010, bears annual interest at 7.965% average, secured by third parties	447,888	-
Total short-term debt	$ 1,492,961	$ 718,830

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

NOTE 7 – LONG TERM LOANS

On December 16, 2009, the Company entered into a 2-year loan agreement with JMRB. The Company borrowed $253,803 with an annual interest rate equal to 7.02% and is due in December 2011. The loan is guaranteed by the relatives of Mr. Tao Wang, the CEO and major shareholder of the Company and is collateralized by the property of his relatives.

NOTE 8- RELATED PARTY BALANCES AND TRANSCATIONS

Due to related party

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

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

Related party transactions

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

The Company leases one of its stores from Mr. Tao Wang under a four-year operating lease expiring August 2011. For the nine months ended September 2010 and 2009, related party rent expense of $17,164 and $13,153, respectively, was included in total rent expense of the year.

The Company leases one of its warehouse buildings to Weidong, Liang, brother-in-law of Mr. Tao Wang, for three years starting May 2008. Per the agreement, the lessee shall pay equal amount of advertising expense on behalf of the lessor as the lease payment. For the nine months ended September 30, 2010 and 2009, the Company recorded other income of $66,017 and $65,966 respectively, from leasing the aforementioned building and advertising expense of the same amount respectively.

NOTE 9 - INCOME TAX

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

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Income before income taxes	$ 5,244,460	$ 4,753,316
Income taxes	$ 1,421,768	$ 1,188,329

There is no significant temporary difference between book and tax income.

The Company has no United States income tax liabilities as of September 30, 2010 and December 31, 2009.

The following table reconciles the U.S. statutory corporate income rates to the Company's effective tax rate for the nine months ended September 30, 2010 and 2009:

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
U.S. statutory rate	34.0%	34.0%
Foreign income not recognized in the U.S.	-34.0%	-34.0%
PRC statutory rate	25.0%	25.0%
Other permanent differences	2.1%	-
Effective income tax rate	27.1%	25.0%

NOTE 10 – SHAREHOLDERS' EQUITY

During January 2010, the Company distributed $484,565 to its shareholders.

During February 2010, upon the closing of the reverse merger, one of the shareholders transferred 338 of the 874 shares of Series A Convertible Preferred Stock issued to him under the share exchange to certain service providers of the Company. The underlining common shares were valued at $1.35 (post-reverse split common stock price) per share resulting in stock compensation expense of $442,611 for the nine months ended September 30, 2010.

Series A Convertible Preferred Stock

The Company issued 10,000 shares of our Series A Preferred Stock in February 2010 related to the reverse merger.

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

Shares of Series A Preferred Stock had automatically convert into shares of common stock on the basis of one share of Series A Preferred Stock for 970 shares of common stock immediately subsequent to the effectiveness of a planned 1-for-27 reverse split of the Company's outstanding common stock, which had become effective on September 10, 2010. Upon the reverse split the 10,000 outstanding shares of Series A Preferred Stock had automatically convert into 9,700,000 shares of common stock, which constitutes 97% of the outstanding common stock of the Company subsequent to the reverse stock split.

Holders of Series A Preferred Stock vote with the holders of common stock on all matters on an as-converted to common stock basis, based on an assumed post 1-for-27 reverse split (to retroactively take into account the reverse stock split).

Following the effectiveness of the Reverse Stock Split and conversion of Series A Preferred Stock into common stock, there are approximately 10,000,000 shares of our common stock issued and outstanding and no shares of preferred stock issued and outstanding.

For accounting purposes, we treated the series A convertible preferred stock as being converted fully to common stock on a post reverse stock split basis.

The 1-for-27 Reverse Stock Split

The Company's board of directors unanimously approved, subject to stockholder approval, the 1-for-27 Reverse Split of our issued and outstanding common stock. The reverse split will reduce the number of issued and outstanding shares of the Company's common stock outstanding prior to the split. The reverse split increases the total number of issued and outstanding shares of the Company's common stock subsequent to the split by triggering the automatic conversion of the Company's Series A Preferred Stock into 9,700,000 shares of common stock. The reverse split had become effective on September 10, 2010, the date when the Company filed with the Secretary of State of the State of Delaware following the expiration of the 20 day period mandated by Rule 14c of the Exchange Act. On September 10, 2010, 27 shares of Common Stock had automatically been combined and changed into one share of common stock.

For counting purposes, we treated the reverse stock split as being effective and all shares are retroactively restated to reflect the reverse stock split.

NOTE 11 – COMMITMENTS AND CONTINGENCIES

Guarantees

As of December 31, 2009, the Company provided corporate guarantees for bank loans borrowed by two unrelated companies incorporated in the PRC ("Company A and B"). Associated with the corporate guarantee, Company A and B also provided cross guarantees for the JMRB bank loans of $293,400 borrowed by the Company. If Company A and B default on the repayment of their bank loans when they fall due, the Company is required to repay the outstanding balance. As of December 31, 2009, the guarantee provided for the bank loans borrowed by Company A and B were approximately RMB 1,000,000 ($293,400) and RMB 1,000,000 ($146,700), respectively.

The guarantee period is from July 2008 to December 2009. The Company's management considered the risk of default by Company A and B is remote and therefore no liability for the guarantor's obligation under the guarantee was recognized as of December 31, 2009. No fee was paid to Company A and B for their guarantee.

As of September 30, 2010, two unrelated companies incorporated in the PRC provided guarantees for the JMRB bank loans of $298,593 borrowed by the Company. The guarantees end when the loans become mature. (See Note 6)

Tax liabilities

The Company did not pay much of its significant value added tax liabilities and income tax liabilities.

The tax authority of the PRC Government conducts periodic and ad hoc tax filing reviews on business enterprises operating in the PRC after those enterprises had completed their relevant tax filings, hence the Company’s tax filings may not be finalized. It is therefore uncertain as to whether the PRC tax authority may take different views about the Company’s tax filings which may lead to additional tax liabilities. It is possible that the PRC tax authority may impose significant penalties on the Company for its failure to pay taxes timely.

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

Mr. Tao Wang entered into the contract with the Company to assume fiscal responsibilities for all tax liabilities recorded and potential penalties relating to all the tax liabilities before December 31, 2009. As of December 31, 2009, the assumed amount was $12,549,060 which mainly included VAT tax payable and income tax payable. However, these tax amounts transferred to Mr. Tao Wang were never paid to the government. As a result, the historical financial statements of the Company were restated to reflect the Company as the primary obligor of the tax liabilities. Please refer to the restatement footnote 14. According to PRC tax law, late or deficient tax payment could subject the Company to significant tax penalty.

NOTE 12 - OPERATING RISKS

(a) Country risk

The Company has significant investments in the PRC. The operating results of the Company may be adversely affected by changes in the political and social conditions in the PRC and by changes in Chinese government policies with respect to laws and regulations, anti-inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation, among other things. The Company can give no assurance that those changes in political and other conditions will not result in a material adverse effect upon the Company's business and financial condition.

(b) Exchange risk

The Company cannot guarantee the Renminbi, US dollar exchange rate will remain steady, therefore the Company could post the same profit for two comparable periods and post higher or lower profit depending on exchange rate of Renminbi and US dollars. The exchange rate could fluctuate depending on changes in the political and economic environments without notice.

(c) Interest risk

The Company is exposed to interest rate risk arising from short-term variable rate borrowings from time to time. The Company's future interest expense will fluctuate in line with any change in borrowing rates. The Company does not have any derivative financial instruments as of September 30, 2010 and December 31, 2009 and believes its exposure to interest rate risk is not material.

(d) Deposit risk

The Company holds certain bank accounts in its employees' name in order to better facilitate its daily cash needs. Balances of these accounts totaled $365,476 at September 30, 2010 and $7,870 at December 31, 2009. Highest total balance of these accounts during the nine months period ended September 30, 2010 was approximately $1,343,000 and $1,224,000 during the year ended December 31, 2009. It is possible that the Company could lose these deposits due to the fact that these accounts are not legally owned by the Company.

NOTE 13 – SUBSEQUENT EVENT

The Company renewed the loan with JMRB matured in November 2010 for another year. The principal amount is approximately $149,000 (RMB 1,000,000) with interest rate of 8.896% per annum.

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

NOTE 14 – RESTATEMENTS

As stated in Note 11 Tax Liabilities, the effects of restating the tax liabilities are shown in the following tables.

QINGDAO FOOTWEAR, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
UNAUDITED

	Nine Months Ended		
	September 30, 2009 (Original)	Adjustment	September 30, 2009 (Restated)
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$ 3,564,987		$ 3,564,987
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	43,964		43,964
Changes in operating assets and liabilities:			
Accounts receivable	(69,020)		(69,020)
Inventories	(409,040)		(409,040)
Prepaid expenses	(37,961)		(37,961)
Accounts payable	26,519		26,519
Tax payable	3,471,783		3,471,783
Net cash provided by operating activities	6,591,232		6,591,232
CASH FLOWS FROM INVESTING ACTIVITIES			
Collection from related party	686,829	(686,829)	-
Cash paid for property and equipment	(376,899)		(376,899)
Net cash provided by (used) in investing activities	309,930	(686,829)	(376,899)
CASH FLOWS FROM FINANCING ACTIVITIES			
Distribution to shareholders	(6,860,412)	686,829	(6,173,583)
Proceeds from loans	718,830		718,830
Repayments on loans	(410,760)		(410,760)
Net cash used in financing activities	(6,552,342)	686,829	(5,865,513)
Effect of exchange rate changes on cash	(2,440)		(2,440)
Net increase in cash	$ 346,380		$ 346,380
Cash, beginning of period	118,534		118,534
Cash, end of period	$ 464,914		$ 464,914
SUPPLEMENTARY DISCLOSURE:			

Interest paid	$	41,087	$	41,087
Income tax paid	$	3,760	$	3,760

As a result of the restatement, the net cash provided by investing activities decreased by $686,829 from $309,930 as originally reported, to net cash used $376,899; the net cash used in financing activities decreased by $686,829 from $6,552,342 as originally reported, to $5,865,513.

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

This Quarterly Report on Form 10-Q for the three months ended September 30, 2010 contains "forward-looking statements" within the meaning of Section 21E of the Securities and Exchange Act of 1934, as amended, including statements that include the words "believes," "expects," "anticipates," or similar expressions. These forward-looking statements include, among others, statements concerning our expectations regarding our working capital requirements, financing requirements, business, growth prospects, competition and results of operations, and other statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. The forward-looking statements in this Quarterly Report on Form 10-Q for the three months ended September 30, 2010 involve known and unknown risks, uncertainties and other factors that could cause our actual results, performance or achievements to differ materially from those expressed in or implied by the forward-looking statements contained herein.

Throughout this report, the terms "we," "us," "our company," "our" and "Qingdao Footwear" refer to the combined business Qingdao Footwear, Inc., formerly Datone, Inc., and its wholly owned direct and indirect subsidiaries, (i) Glory Reach International Limited, or "Glory Reach," a Hong Kong limited company; and (ii) Qingdao Hongguan Shoes Co., Ltd., a PRC limited company, or "QHS," as the case may be.

Overview

We are a designer and retailer of branded footwear in Northern China. We were organized to service what we believe is an unmet and increasing demand for high quality formal and casual footwear throughout the PRC. We are focused on providing footwear that rises to the style, quality and comfort demands of a high-end consumer at affordable prices within reach of middle market office employees. Our products can be divided into men's and women's casual and formal footwear. Along with the growth in urbanization and individual purchasing power in China, the demand for leather footwear has also grown. Since our organization in 2003, we have grown rapidly throughout Shandong province, a province that has approximately one-third the numbers of people of the United States.

Our principal business includes (1) designing and selecting designs for men's and women's leather shoe lines; (2) sourcing and purchasing contract-manufactured footwear; and (3) selling these lines of footwear under our proprietary brand, " " (Hongguan, sometimes presented as "HonGung"). We do not manufacture or assemble any shoes. We operate a number of flagship stores throughout greater Qingdao. Our products are also brought to market through our extensive distribution network of authorized independent distributors as well as through third party retailers selected to operate exclusive Hongguan brand stores on our behalf. We believe that the sale of our products through distributors and third parties has enabled us to grow by exploiting their local retail expertise and economies of scale while minimizing our expenditure on fixed asset and human resources. Our company headquarters and main sales office is located in Shandong province in northern China, in the city of Jimo, less than 25 miles from the major urban center of Qingdao.

Principal Factors Affecting Our Financial and Operational Results

Our financial results of operations have been and will continue to be affected by a number of factors, including but not limited to the following factors:

Growth in the broader PRC economy

Our financial condition and results of operations have been driven by macro-economic conditions, increased disposable income and consumer spending in the PRC. Since our formation, we have derived 100% of our income from operations in China. Along with growth in the economy as a whole, Chinese domestic consumption has increased in line with rapid urbanization and increases in disposable income over the past 15 years. Per capita urban disposable income has increased by an annualized rate of 12.9% over the 5 years ending in 2008 and is anticipated to top $2,000 in 2012. The urban population as a percentage of the total population increased from 40.6% in 2003 to 46.6% at the end of 2009, and this trend is expected to continue into the future. (National Bureau o