The case of Hongli Clean Energy Technologies Corp. How a Chinese company scammed the US Stock Market

Song Wang
Saint Xavier University

David Parker
Saint Xavier University

ABSTRACT

This paper provides a case analysis of a Chinese company named Hongli Clean Energy Technologies Corporation, a company that was cross-listed on the U.S. Nasdaq stock market from 2010 to 2017 when it was delisted for suspected financial fraud. Using the Company as an example, this study reveals a number of unethical and illegal behaviors employed by foreign companies to exploit U.S. investors, including financial statement fraud, shell company schemes, false announcements, and stock price manipulation. In the end, the paper provides an outlook of Chinese IPOs and reverse mergers in the U.S., compared to their domestic peers.

Keywords**:** shell company, penny stock, price manipulation, financial statement frauds

INTRODUCTION

Hongli Clean Energy Technologies Corporation, previously known as SinoCoking Coal and Coke Chemical Industries, Inc. ("Hongli" or the "Company"), was a Chinese company listed on the U.S. Nasdaq Stock Exchange between 2010 and 2017. The Exchange delisted it for suspected fraud. This paper reveals how the Company landed on the U.S. capital market and raised millions of dollars from U.S. investors in fraudulent ways. Hongli started business in the United States as a shell company registered as a Florida corporation and an emerging producer of clean energy products located in Pingdingshan City, Henan Province, China. Although the Company claimed to control a coking factory in China through a Variable Interest Entity (VIE), little reliable evidence could be found to verify the legitimacy of its business. The IPO process for Hongli was also tricky. Hongli first acquired a Canadian company that was already traded over-the-counter and then used its shell to pass the scrutiny of U.S. regulators. Upon obtaining the public status, Hongli's management began broadcasting positive news about the Company that created a demand shock on the company stock and made the price soar in a very short time. However, the veracity of the information released was questionable and unsubstantiated and the price rocketing stalled and resulted in price plummeting. This is commonly referred to as a "Pump and Dump" scheme, and it is a type of stock manipulation through which insiders gain from uninformed retail investors.

In addition to many fraudulent behaviors, the smoking gun that caused Hongli's delisting was financial statement fraud. For many years after its IPO, the Company continued to cook its book by inflating its revenue and assets, creating an illusion of growth and success for investors. With the seemingly good financials, Hongli's stock reminded actively traded before its collapse. The Company's death trigger was its massive unexplained expenses, which cast fatal doubts on its operations and financial health. The rest of the paper discusses each of the fraudulent behaviors. Section 2 covers the shell company scheme utilized by Hongli. Section 3 discusses the Company's IPO process. Section 4 details the penny stock manipulation. Section 5 details the financial statement fraud implemented by Hongli. And Section 6 is the conclusion.

SHELL COMPANY SCHEME

Hongli was little known by the public in China. Moreover, an internet search provided little information about the Company's business operations. For example, little could be discovered about its management and leadership team, customer bases, or major suppliers. Indeed, Hongli's Chinese website, www.honglichina.net, was actually a link to an online gambling platform, a complete fraud. Hongli also had a separate English webpage http://www.cetcchina.net/ that looked more like a generic, fabricated webpage than one professionally designed and maintained. When initially listed on the Nasdaq, Hongli had the lowest market capitalization on the Exchange at approximately $700,000, half the price of a typical condo in Beijing. How could this corporation, full of doubtful facts, become listed in the U.S.?

Hongli was first registered in the United States in 1996 under the name SinoCoking Coal. Aside from the U.S. registration, everything about Hongli is Chinese. The Company's headquarters was in China, and its coking and gas businesses were operated through a Chinese domestic company with the same name but a different entity. Furthermore, the Chinese Hongli acted under a contractual arrangement with Hongyuan Limited, another Chinese company registered in the British Virgin Islands. The agreement specifies controlling interests and cash flow distribution between the two entities. In short, the Chinese company takes several shells in different places.

A shell company, or corporation, is an entity that exists only on paper; it has no active business operations or significant assets. It is typically an entity created to hold funds and manage another entity's financial transactions. These types of entities are not necessarily illegal. Generally speaking, a shell company is a legal tool used in different business transactions to reduce tax liability, access financing, store funds, or maintain anonymity. Other legitimate reasons for a shell corporation include such things as a startup using the business entity as a vehicle to raise funds, conduct a hostile takeover, go public with a reverse merger, hide dealings, protect assets from legal actions, invest in foreign markets, and as tax avoidance vehicles. Shell corporations are utilized by many large well-known public companies, shady business dealers, and private individuals alike. However, they are sometimes used illegitimately, such as to disguise business ownership from law enforcement or the public. The shell company created by Hongli is a variable interest entity (VIE). VIEs are a legal business structure in which an investor has a controlling interest despite not having a majority of voting rights and are often established as special purpose vehicles (SPVs) to hold financial assets passively or actively conduct research and development. To U.S. investors, investment in a VIE is very similar to holding stocks, just without ownership.

Why does Hongli need shell companies? Because the only way for a Chinese private company to go public overseas is to create a shell corporation offshore since the Chinese government forbids its domestic firms from being controlled by foreign entities. While the use of shell companies is an acceptable and common practice in the U.S. stock market, the shell techniques employed by the Hongli group utilize an unusually complicated structure, as Figure 1 shows. On the U.S. side, in 2010, Hongli Florida acquired a small Canadian company, Ableauction.com, which ran an online auction business that has nothing to do with Hongli's coking business. However, it does not matter. What matters is that the Canadian company was already traded over-the-counter at Nasdaq, one step further from formally listed on the Exchange. What Hongli wanted was the public status of Ableauction.com. Two weeks after Hongli acquired the auction company, the merged entity controlled by Hongli soon became approved for initial public offering (IPO) on the Nasdaq stock exchange. The whole process is called a reverse merger (R.M.) when a private company purchases a public-listed (or ready to become public) company and possesses the latter's public status. The benefit of a R.M. is quick access to the capital market without detailed scrutiny by the U.S. regulators.

RAISING CAPITAL

Whether legitimate companies or fraudsters, either through IPO or R.M., the purpose of going public in the U.S. market is to raise capital from its investors. Original shareholders, usually the company's founders, often become rich by selling their shares in the process. The public market also opens up a tremendous opportunity for millions of investors to buy shares in the company and contribute capital to a company's equity, which funds its development. The public consists of any individual or institutional investor who is interested in investing in the company.

Ironically, Hongli only raised $11,385 for its IPO, a ridiculously small amount, as Column 1 of Table 1 shows. Nevertheless, it is just the beginning. Since then, throughout seasoned offerings afterward, Hongli raised over $6 million in additional capital. The purpose of raising money was well served.

Hongli could not raise that large amount of capital unless its stock price is highly inflated after the IPO. On average, each additional share during seasoned offering was sold at around $0.6 per share, with a tremendous increase from its original price of $0.001, by 60000%; At the peak of its trading in 2017, the price reached $4.64, as Figure 1 shows, 423000% higher than the original price. Table 3 shows that at the IPO, Hongli issued 11,384,566 shares. In 2015, the total amount of registered shares was 23,960,217. An additional 12,575,651 shares were issued after IPO. These shares were sold at market price above the par value ($0.001/share) and gained the Company $6,846,397 for "Additional paid-in capital." The additional paid-in capital is the amount of cash raised by Hongli by issuing shares "AFTER IPO" or seasoned offering. The value of the "Common stock" also increases due to the new shares. The increase is $12,576 at $0.001/share. So, in total, Hongli raised $6,858,955 (or $6,846,397 + $12,576) after IPO.

How could Hongli stock reach a price that high when the Company is fake? The primary reasons are (a) trading manipulation and (b) false financial statements.

PENNY STOCK MANIPULATION

Hongli stock is a penny stock, as its price is measured in pennies, if not tenths of a penny. According to the Securities and Exchange Commission (SEC), penny stocks are often defined as shares that trade for less than $5. They come with high risks and the potential for above-average returns, and investing in them requires care and caution. Penny stocks are popular tools for stock manipulations. Back in the 1990s, stock manipulation was very pervasive on Wall Street. The usual technique was called "Pump-and-Dump." In this process, a stock price is artificially inflated by manipulators spreading misleading or false information that leads to an upswing in the share's price. Once buyers jump in, leading to an upswing in the share price, the perpetrator then dumps the shares that he bought beforehand for a profit. This sell-off typically causes the price to plummet. The victims in the process are typically the ordinary investors who trusted the misleading information and purchased the stock when the price was rising and could not sell their shares fast enough when the price was plummeting.

The price of Hongli's stock was meager, making it very affordable and attractive to investors. Also, the stock's market size and liquidity are very low. A relatively small amount of funds, say, several thousands of dollars, could cause a significant impact on the stock price. Therefore, it is very easy to manipulate the stock price and profit from it.

A stock manipulator could be anyone who holds a large portion of the stock. He can be a stockbroker who uses high-pressure selling tactics to entice investors to buy. Stock manipulators could also be the managers of the company, also hold a large portion of shares. More importantly, it is more convenient for them to release misleading information to the public. When Hongli became public in 2010, some large shareholders are American individuals who had legal records of misbehavior in their previous security trading, mostly in security frauds and manipulation. Although one cannot conclude whether these individuals are involved in the manipulation of Hongli stock or are associated with the Company, Hongli stock's performance shows red flags of manipulation. It is straightforward to observe: a manipulation is associated with substantial short-term volatility of prices and fast up-and-downs of price movements. As the price chart below shows, two large waves of manipulation occurred in late 2014 and early 2017.

Did Hongli release misleading information to the public? Yes. In 2014, Hongli announced that two institutional investors agreed to purchase its new shares at $5.10 per share, as shown in Figure 2. The size of the deal was claimed to be $14.3 million, almost the same as the Company's total equity at the time. Once this information was released, Hongli's price quadrupled from less than $2 to over $8. Immediately after the soar, the price dropped back due to the large dump of shares. Did the deal take place? According to the SEC files, it never did. Was Hongli punished for the announcement? No, because in the announcement, Hongli never disclosed the time of the deal. It could be now or in the 23rd century; technically, the announcement per se cannot be proved wrong until the entire scheme is finished. Nevertheless, it is a misleading piece of information that facilitates stock manipulations.

FINANCIAL STATEMENT FRAUD

Favorable stock price causes popularity and makes it easy for the company to issue new shares to the market. While market manipulation can only boost price in the short-run, to ensure a high price in the long term for the fake Company, Hongli did a series of financial statement fraud.

Long-term stock price is a reflection of all material information of the company. For example, if the company announces good earnings, the stock price would increase, and vice versa. Financial statement fraud is the deliberate misrepresentation of an enterprise's financial condition accomplished through the intentional misstatement or omission of amounts or disclosures in the financial statements to deceive financial statement users. Throughout the years, Hongli continuously announces good news about the firm, such as expanded gas production, more product outputs for revenue, etc. These announcements were proved to be unfounded later during its delisting period.

On the official financial statements, Hongli reports very impressive earnings. For example, at its IPO in 2010, the earnings per share (EPS) was $8.49, thousands of times the offering price. An investment of $1,000 in Hongli at the original offering would result in earnings of over $8 million in a single year, not to mention the price appreciation. With such expectation, it is not surprising that ordinary investors would swarm to buy the stock.

The reported earnings were impressive. However, the earnings were never paid out to investors as a dividend. To avoid paying a dividend on a periodical basis, Hongli uses the shield of Chinese government policy. On the SEC filing, Hongli states, "Regulations in China currently permit payment of dividends only out of accumulated profits." As a result, their Chinese subsidiaries and VIEs "are restricted in their ability to transfer a portion of their net assets to us in the form of dividends….". For other U.S. companies, a zero periodical dividend would be perfectly acceptable, as long as stockholders hold control of the company's accumulated profit and decide its use in the future, either for company investment or for a lump-sum cash dividend (e.g., Microsoft). Nevertheless, for Hongli, the situation is different because its stock buyers never control the company, not even mentioning its retained profits. Without dividends bringing the cash benefits, the stock is no more than a speculative tool.

If Hongli did not pay a dividend, what did it do with its accumulated profit? As Table 2 shows, on its balance sheet, Hongli's retained earnings kept increasing from $29 million in 2009 to $109 million in 2015. This trend created an optimistic illusion that draws investors to buy its stock. To investors, Hongli had accumulated profits that can be eventually paid as a lump-sum dividend. However, in 2016, right before Hongli's final play, almost all of its retained earnings are gone for no reason. The large wipeout of the retained earnings is due to a large impairment expense. This expense causes both Hongli's assets and equity to shrink massively. Worse than that, Hongli never provides an explanation of the impairment expense, casting huge suspicion of frauds. Multiple requests for an explanation from investors and Nasdaq were made to Hongli.

Furthermore, numerous complaints were filed due to Hongli's false financial statements. Lack of response was the reason that Hongli was delisted, and Hongli has remained silent ever since.

The U.S. Securities Exchange Commission received numerous complaints against Hongli. Victims claim that its financial statements "were false and misleading because the company did not properly record the impairment of certain of its assets." "The idea is that the company did not take impairments when it should have and concealed material information, in violation of Securities Exchange Act of 1934".

According to the investor complaints, the most questionable part is the Impairment expenses, which is the reduced value of assets, such as equipment explosion, inventory theft, forfeited land, etc. This item is located in the income statement. Hongli's impairment expenses increased from $2.4 mil in 2015 to $97 mil in 2016. Accordingly, nearly all assets are gone on Hongli's balance sheet: For current assets, accounts receivable reduced from $13 mil to 0; Inventory reduced from $3.1 mil to $102 thousand; Advances to suppliers, from $8 mil to 0; Other receivable and deposits, from $5 mil to 0. For fixed assets, $18 mil of Plant and equipment is all gone with only $26 thousand salvage value left. $19 mil of prepaid assets and $56 mil of intangible assets are all gone to 0, with no reason whatsoever.

It is quite strange that Hongli, as a mining company, has nearly one-third of its total assets in intangible assets. Such a ratio is incredibly high even for technology companies. Hongli is not a technology company because there are no research and development activities. Given that intangible assets are tough to track and verify, Hongli's books' number raises a red flag and suspicions of accounting fraud.

On the equity side, once a company suffers a net loss, it will record a deduction in the retained earnings. During its final play, Hongli's Retained earnings decreased from $108 mil to $18 mil. As mentioned earlier, retained earnings are accumulated profits over years, and it is the measurement of the wealth created by the company for its shareholders. The increased earnings drew investors to buy Hongli's stock initially, and now it is gone.

The U.S. Congress authorizes the United States Securities and Exchange Commission (SEC) to seek a number of remedies, including civil money penalties and disgorgement, from those who commit fraud. (While the Securities and Exchange Commission is a law enforcement agency, only the Department of Justice has authority to seek criminal sanctions, such as imprisonment.)

Injured investors may be able to use in recovering funds, including Receiverships, Fair Funds and Disgorgement Funds, Brokerage Account Customer Protections, Corporate Bankruptcy Proceedings, and Private Class Action Lawsuits. It should be noted that, in many cases, victims of fraud may recover only a fraction of what was stolen or, in some cases, may recover nothing at all.

A class-action lawsuit against Hongli was filed in the United States District Court for the Central District of California on behalf of purchasers of Hongli Clean Energy Technologies Corp. securities (NASDAQ: CETC) from October 13, 2015 through April 7, 2017. The lawsuit seeks recovery of investor losses. However, the victims are unlikely to win. The reason is that Hongli was established through many layers of shells located in China and BVI, out of the jurisdiction of the United States. Also, the responsible individuals of the Hongli group have Chinese or Singapore nationality that complicates the indictment process.

Moreover, the size of the damages is relatively small compared to other financial frauds in the U.S. It may not attract enough attention from law enforcement. Up until today, there is no news of any progress of the lawsuit.

CONCLUSION

Between 2001-2010, 85% of foreign R.M. in the U.S. are by Chinese firms. Nearly a third of the Chinese R.M.s in the U.S. were accused of accounting fraud (Ang et al. 2016). The Chinese firms overall, however, actually present high qualities. In Lee et al. (2019), pre-listing R.M. Chinese companies "are larger, more profitable, and less politically connected than pre-listing IPO firms." R.M. firms are also better in operations and stock returns and do not underperform the market in the long run. These firms use the U.S. market to avoid the stringent and potentially biased IPO policies of China. Pollard (2016) finds that reverse merger firms indeed exhibit lower earnings quality compared to IPO firms. However, reverse merger firms' lower financial reporting is driven by the non-Chinese reverse merger firms. Lee et al. (2015) find that Chinese R.M.s (CRMs) tend to be more mature and less speculative than their U.S. counterparts. Even considering the accused of accounting fraud, Chinese reverse mergers still outperform their matched peers. There is little evidence that Chinese R.M.s are toxic investments.

Hongli is a bad apple in the Nasdaq basket of Chinese firms. Its American journey made itself $7 million from U.S. investors. The amount is small for a typical firm but quite large for a small obsolete mining factory. It is seriously doubtful the Chinese factory ever received the capital for development. The fund is more likely to be funneled to the offshore shell companies and ended in the hands of the controlling individuals. Through the case of Hongli, we can see how a financial scheme could be crafted by exploiting the loopholes and weakness of the American financial system: First, the fast development of the Chinese economy made Chinese companies popular with U.S. investors. The impression drives some U.S. investors to buy stocks without realizing the risks. Second, the way of going public through R.M. helps bad companies avoid government scrutiny for quality. Although the SEC and the Exchange continuously warn investors about companies of such nature, investors always make bad decisions. Third, by locating overseas and using multiple shell companies, Hongli shields itself from any form of investigation by investors and regulators. There is nearly no way for investors to verify the truthfulness of Hongli's profile and statements. Fourth, collaborators are found in the Hongli scheme. These are the investment banks that filed for Hongli's registration and underwrite its shares, auditors that approved the false statements without due diligence, and unethical stock traders who manipulated Hongli's price.

The impact of the fraud wave is profound: when U.S. investors see the risk of Chinese R.M.s through bad publicity and when they cannot distinguish the good ones from the bad ones, they require higher returns for all Chinese R.M.s, no matter good ones or bad ones, under such pressure, the bad firms will not last long; the good firms, if they want to maintain in the market, they have to pay investor better returns in the forms of stock repurchases, increasing dividends, or going private, all of which increase the firms' cost of capital. In sum, some Chinese companies' fraud leads to a higher cost of capital for all Chinese companies in the U.S. market. If the trend keeps going, fewer and fewer Chinese companies would be able to access the U.S.

capital, and more existing listed Chinese companies would be pushed out of the market due to the high cost of capital.

The fundamental problem lies in auditing standards that approve firm quality. Both U.S. and China have strict standards in auditing public companies to ensure correct financial information, but only to their domestic companies. However, loopholes exist for Chinese companies listed in US. as the cross-country listing process complicates the auditing process. A translated and notarized Chinese statement can always be subject to forgery and deceive the auditors. Although some companies hire reputable external auditors, a foreign auditor is also limited to perform due diligence to conduct a full investigation in China. To this end, the only solution is the full cooperation of both countries' regulators to ensure the Chinese firms are correctly audited in China before they become listed in the U.S. In August 2020, the U.S. administrators proposed to delist the Chinese companies that fail to meet U.S. auditing requirements by January 2022. The Chinese Securities Regulatory Commission responds positively by showing "total sincerity towards cooperation." The process may require lots of effort, but it would be a great new start for Chinese companies and U.S. investors.

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Table 1. IPO Prospectus (S-1 Form) of Hongli Clean Energy Incorporated) as of July 2010 (Source: Securities Exchange Commission)

	Amount to be registered	Proposed Maximum per Share Offering Price	Proposed Maximum Aggregated Offering Price	Amount of Registration Fee
Common stock, $0.001 par value per share	7,344,935	$17.38	$127,654,970	$9,101.80
Common stock, $0.001 par value per share (issuable upon exercise of common stock purchase warrants)	3,789,631	$12.00	$45,475,572	$3,242.41
Common stock, $0.001 par value per share (issuable upon exercise of common stock purchase warrants)	250,000	$6.00	$1,500,000	$106.95
Total	11,384,566			$12,451.16

Table 2. Financial Statements of Hongli Clean Energy Technologies, Inc. in 2015 and 2016
Income Statement

	2016	**2015**	**Change 2016 - 2015**
REVENUE	18,953,657	45,613,084	**-26,659,427**
COST OF REVENUE	11,838,252	32,973,492	-21,135,240
GROSS PROFIT	7,115,405	12,639,592	-5,524,187
OPERATING EXPENSES:			
Selling	44,282	137,858	-93,576
General and administrative	8,542,878	13,169,466	-4,626,588
Impairment expenses	97,028,507	2,431,718	**94,596,789**
Total operating expenses	105,615,667	15,739,042	89,876,625
LOSS FROM OPERATIONS	-98,500,262	-3,099,450	-95,400,812
OTHER INCOME - EXPENSE)			
Other income	13,997	0	13,997

Interest income	38	165,367	-165,329
Interest expense	-2,496,033	-5,552,467	3,056,434
Other finance expense	-168,461	-63,083	-105,378
Gain from assets transfer	5,122,075	0	5,122,075
Change in fair value of warrants	2,833,882	7,131,724	**-4,297,842**
Total other income, net	5,305,498	1,681,541	3,623,957
LOSS BEFORE INCOME TAXES	-93,194,764	-1,417,909	-91,776,855
PROVISION FOR INCOME TAXES	1,051,040	2,045,865	-994,825
NET LOSS	-94,245,804	-3,463,774	-90,782,030
Less: Net loss attributable to noncontrolling interest	-4,354,504	0	-4,354,504
NET LOSS ATTRIBUTABLE TO COMMOM SHAREHOLDERS	-89,891,300	-3,463,774	-86,427,526
OTHER COMPREHENSIVE LOSS			
Foreign currency translation adjustment	-8,226,838	1,074,431	**-9,301,269**
COMPREHENSIVE LOSS	-98,118,138	-2,389,343	-95,728,795
Less: Comprehensive income - loss) attributable to noncontrolling interest	22,904	0	22,904
COMPREHENSIVE LOSS ATTRIBUTABLE TO COMMOM SHAREHOLDERS	-98,141,042	-2,389,343	-95,751,699
WEIGHTED AVERAGE NUMBER OF COMMON SHARES			
Basic and diluted	2,396,022	2,329,183	66,839
LOSS PER SHARE			

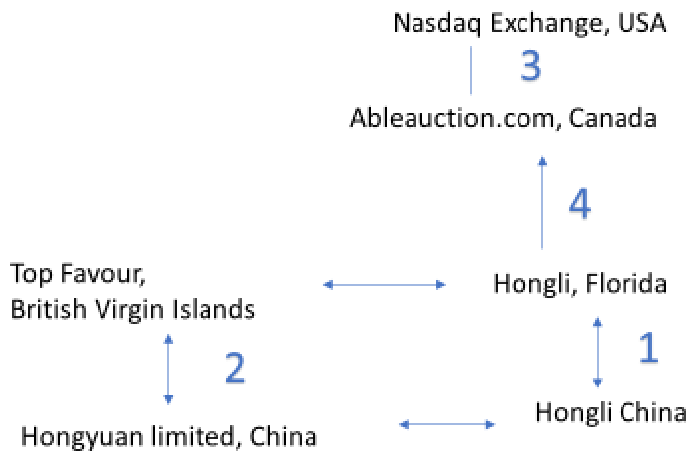
Basic and diluted	-37.52	-1.49	**-36**

Balance Sheet

ASSETS	2016	2015	Change (2016-2015)
CURRENT ASSETS			
Cash	40,523	81,605	-41,082
Accounts receivable, trade	0	13,970,451	**-13,970,451**
Other receivables and deposits	2,492	4,928,967	**-4,926,475**
Inventories	102,504	3,191,605	**-3,089,101**
Advances to suppliers	0	8,216,127	**-8,216,127**
Prepaid expenses	0	16,670	-16,670
Total current assets	145,519	30,405,425	-30,259,906
PLANT AND EQUIPMENT, net	26,631	18,750,242	**-18,723,611**
CONSTRUCTION IN PROGRESS	37,004,732	65,420,768	**-28,416,036**
OTHER ASSETS			
Prepayments	0	19,674,034	**-19,674,034**
Intangible assets, net	0	56,355,185	**-56,355,185**
Long-term investments	1,204,032	2,920,247	-1,716,215
Other assets	105,353	114,589	-9,236
Total other assets	1,309,385	79,064,055	-77,754,670
Total assets	38,486,267	193,640,490	**-155,154,223**
LIABILITIES AND EQUITY			
CURRENT LIABILITIES			
Current maturity of long term loan	0	44,471,220	**-44,471,220**
Accounts payable, trade	22,064	70,164	-48,100
Other payables and accrued liabilities	3,922,171	4,503,689	-581,518
Other payables 0 related parties	870,660	736,596	134,064
Acquisition payable	0	4,747,250	**-4,747,250**
Customer deposits	0	80,306	-80,306
Taxes payable	854,102	907,472	-53,370
Current portion of warrants liability	40,884	289,481	-248,597
Total current liabilities	5,709,881	55,806,178	-50,096,297
LONG TERM LIABILITIES			
Warranty liability	40,884	2,626,168	-2,585,284
Total long term liabilities	40,884	2,626,168	-2,585,284

Total liabilities	5,750,765	58,432,346	-52,681,581
COMMITMENTS AND CONTINGENCIES			
EQUITY			
Common stock, $0.001 par value, 100,000,000 shares authorized, 2,396,021 shares issued and outstanding (given retroactive effect to the 1for10 reverse stock split effective October 27, 2016	2,396	2,396	0
Additional paid-in capital	6,867,961	6,867,961	0
Statutory reserves	3,689,941	3,689,941	0
Retained earnings	18,940,333	108,831,633	**-89,891,300**
Accumulated other comprehensive income	3,234,871	11,484,613	-8,249,742
Total SinoCoking Coal and Coke Chemicals Industries, Inc's equity	32,735,502	130,876,544	-98,141,042
NONCONTROLLING INTERESTS	0	4,331,600	-4,331,600
Total equity	32,735,502	135,208,144	-102,472,642
Total liabilities and equity	38,486,267	193,640,490	**-155,154,223**

Figure 1. The Steps of Hongli's IPO Process



Hongli's path to US listing

1.a. In 1996, Hongli Clean Energy (named "SinoCoking" then) is incorporated in Florida, USA. It is a shell company with all its operating-related businesses in Henan, China as a coking and gas company

1.b. In 1996, Hongli Coking is incorporated in Henan, China. It is the fully-owned subsidiary of the Florida shell company.

2.a. Between 2007-2009 (estimated), A shell company in British Virgin Islands (BVI) is registered, owned by a Chinese individual related to the Hongli group.

2.b. The BVI company sets a subsidiary in China, called Hongyuan limited. Hongyuan is in contractual agreement with Hongli China.

2.c. A Variable Interest Entity (VIE) is set up between the BVI company and Hongli, Florida. Supposedly, when Hongli's Chinese operations make profit, the money will be funneled to Hongyuan, China, and then to the BVI shell company, and then to Hongli, Florida.

3. A Canadian auction company, Ableauction.com, is traded OTC Nasdaq. It is ripe for IPO on Nasdaq.

4. Hongli, Florida acquired Ableauction.com with unknown price and unknown method of payment (either by cash, or by leverage, or by Hongli's equity shares). Two weeks after the acquisition, Hongli Clean Energy, the Florida company, becomes public on Nasdaq.

Source: www.sec.gov; Tonghuashun.com

Figure 2. A Snapshot of Hongli Stock Performance
Source: Barchart.com