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.

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 of Statistics of China, www.stats.gov.cn) The United Nations estimates that China's population is likely to be evenly split between rural and urban areas by 2015. ("Urbanization in the People's Republic of China," www.wikipedia.org) We expect that financial performance will continue to be driven by the positive trends in retail consumption, urbanization and increased consumer spending in the future.

Increased consumer demand for leather footwear products in the PRC

Consumer demand for leather footwear products in the PRC is a key driver of our continued growth. The success of our enterprise depends in large part on the growth in the PRC consumer market, particularly consumer demand for high quality, affordable leather shoes. As average living standards in the PRC continue to improve and a larger percentage of employment opportunities become available in an urban office or service economy setting, we expect consumer demand in the PRC to shift increasingly towards footwear appropriate to such settings, such as fine leather footwear. While Chinese per capita footwear consumption is lower than a number of other countries, China surpassed the United States in 2008 as the country that purchases the most pairs of footwear in the aggregate. Because the average Chinese consumer purchases an average of two pairs of shoes annually, far fewer than consumption levels in Korea, Japan or the West, China's shoe consumption rate is expected to approach levels of other nations with similar cultural consumption characteristics if China's consumer wealth continues to grow. ("Footwear in China," www.datamonitor.com) For this reason, we expect the market to continue to grow for the immediate future.

Management and Expansion of Our Distribution Network

The majority of our sales are derived through third party distributors. As such, management of our brand through and collection of receivables from these parties is paramount to our success and future growth. We manage our brand by controlling how our products are placed, selecting store locations and decoration, and other qualitative measures. We regularly visit and inspect third party stores in order to ensure they meet our high standards for appearance, quality and service.

In the past, we had managed receivables from our third parties by requiring full payment for goods within one month of delivery. Beginning with our sales fair in February 2010, we extended credit to certain distributors. These distributors were selected based on outstanding track records in both sales and timely payments. We extended this credit in order to enhance their ability to increase sales responsibly and reward them for past success and loyalty. The extension of credit allows these distributors to grow cost effectively in accordance with our goal of achieving greater penetration in the Shandong retail market. It also encourages them to purchase our new models of footwear. We monitor our receivables carefully and reserve the right to terminate contracts with any supplier whose payments are not timely. We have maintained strong and positive long term relationships with all the distributors that we extended credit periods to and have rarely encountered any difficulties on collection of accounts receivable and do not anticipate collection issues in the future. We encourage such timely repayment by maintaining regular communication with these distributors. Management believes that it has already taken adequate measures to ensure timely settlement by the distributors, and the extended credit period has not and will not materially adversely affected our liquidity or working capital.

Effective cost management and quality control in our supply chain

Our footwear is designed in house, but production of our footwear is entirely outsourced. To meet production requirements and to remain profitable, we must be able to count on our suppliers for quality product at reasonable prices delivered in a timely manner at commercially reasonable prices. Therefore, it is vital to our success that we are able to maintain control of our supply chain. We believe that we will be able to offset a portion of any such increased costs through improvement of production efficiency and use of economies of scale. Historically, we have been successful in containing cost of goods sold as a percentage of total cost of sales. For 2008 and 2009 our cost of goods sold accounted for 59% and 57% of total sales, respectively. We seek to capitalize on overcapacity in the footwear manufacturing industry in the PRC and leverage our purchasing power to continue to obtain favorable prices from our major suppliers. Should costs increase in the markets from which we currently source products, we are confident that we will be able to find alternative footwear providers throughout Southeast Asia. We actively work with our suppliers to maintain quality and reserve the right to return goods that do not meet our standards.

Competitive Pricing Points and Attractive Product Designs

We have been able to maintain strong gross profit margins through competitive pricing of our products and effective cost management. To increase sales volumes, our pricing policy is to offer a range of products set at different price points with the aim of targeting different segments within the mid-range market. In order to maintain our price competitiveness and sales volumes, we review our pricing strategy regularly to make adjustments based on various factors, including the market response to existing recommended retail prices, the level of sales, the expected product margin on individual products, the prices of our competitors' products and the anticipated market trends and expected demand from customers.

We pursue a variety of designs that offer a diversified product mix and provide a wide range of leather footwear styles to our customers, which we believe to be vital to attracting customers and to increasing our revenue. Our designers have historically produced more than 300 unique designs annually which vary by season and target demographic. We strive to find innovative styles and technologies to incorporate into our shoes and always meet the highest and most popular styles for our customers. In the coming years, we will monitor demand and adjust our products accordingly to maximize sales and profit.

Ability to maintain brand recognition and marketing success

We believe that brand recognition drives consumer product selection. We will continue to invest our efforts in brand building and establishing Hongguan as a quality affordable footwear brand rising to the highest fashion standards while remaining within reach of a smaller budget consumer. We place great emphasis on our brand and promote Hongguan products through advertisements in the media, sales fairs and various other promotional activities. We intend to increase our marketing budgets for promotional activities in the future in order to further strengthen our brand and market position.

Previous Organization and Reverse Acquisition

During fiscal year 2009, our company's corporate entity, Datone, Inc., was a provider of both privately owned and company owned payphones and stations in New York. Datone, Inc. received revenues from the collection of the payphone coinage, a portion of usage of service from each payphone and a percentage of long distance calls placed from each payphone from the telecommunications service providers. In addition, Datone, Inc. also received revenues from the service and repair of privately owned payphones and sales of payphone units.

On February 12, 2010, our company completed a reverse acquisition transaction through a share exchange with Glory Reach and the shareholders of Glory Reach (the "Glory Reach Shareholders"), whereby Qingdao Footwear (Datone, Inc. at the time) acquired 100% of the issued and outstanding capital stock of Glory Reach in exchange for 10,000 shares of Datone, Inc.'s Series A Preferred Stock. This preferred stock 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. As a result of the reverse acquisition, Glory Reach became our wholly-owned subsidiary and the Glory Reach Shareholders became our beneficially 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. In connection with this acquisition, Datone, Inc. changed its name to "Qingdao Footwear, Inc." and changed its operations from serving as a provider of payphones and stations in New York to serving as a holding company for a designer and retailer of branded footwear in Northern China.

As a result of our acquisition of Glory Reach, we now own all of the issued and outstanding capital stock of Glory Reach, which in turn owns all of the outstanding capital stock of QHS.

Results of Operations

Comparison of Three Months Ended September 30, 2010 and September 30, 2009

The following table sets forth key components of our results of operations during the three months ended September 30, 2010 and 2009, both in dollars and as a percentage of our net sales.

	Three Months Ended September 30, 2010		Three Months Ended September 30, 2009	
	Amount	% of Net Sales	Amount	% of Net Sales
Net Sales	$ 3,715,217	100%	$ 2,918,275	100%
Cost of sales	2,001,078	54%	1,656,918	57%
Gross profit	1,714,139	46%	1,261,357	43%
Operating Expenses	488,505	13%	210,927	7%
Operating Income	1,225,634	33%	1,050,430	36%
Other income /(interest expense)	(540)	0%	7,586	0%

Income Before Income Taxes		1,225,094	33%		1,058,016	36%
Income taxes		306,273	8%		265,704	9%
Net income	$	918,821	25%	$	792,312	27%

Net Sales. Our net sales increased to $3,715,217 in the three months ended September 30, 2010 from $2,918,275 in the same period in 2009, representing 27.3% revenue growth. As retail sales trends and broader economic growth in the PRC have been positive despite a global economic downturn, during the three months ended September 30, 2010, we promoted higher price products in order to achieve higher gross profit. In addition, our retail sales contributed 21.3 % of total sales amount during the three months ended September 30, 2010, as compared to 15.4 % of total sales during the same period of 2009. Our retail selling price is about 30%-40% markup on the selling price to wholesalers. As a result, the average selling price per pair for the third quarter of 2010 and 2009 was $19.3 and $16.1 respectively, representing an increase of 19.9%. Despite of the price increase, the volume of footwear sold increased by 6.7% to approximately 193 thousand pairs for the three months ended September 30, 2010 as compared to approximately 180 thousand pairs for the same period last year. We believe our pricing policy for this quarter was a success given the overall growth in revenue. In the future, we may adjust pricing strategy to meet market demand and satisfy our financial goals.

Net sales from our wholesale operations increased $456,778, or 18.5%, to $2,925,494 for the three months ended September 30, 2010, from $2,468,716 for the three months ended September 30, 2009. The average selling price per pair within our wholesale operations increased to $18.2 per pair for the three months ended September 30, 2010 from $15.3 per pair in the same period last year, an increase of 19%, primarily due to acceptance of new designs and styles for our in-season products. However, our sales volume decreased 0.4% resulted from the increase of selling price. We may, from time to time, adjust our selling price policy to test market to achieve higher gross profit.

Net sales from our retail operations increased $340,164 to $789,723 for the three months ended September 30, 2010, an 75.7% increase over sales of $449,559 for the three months ended September 30, 2009. The average selling price per pair within our retail operations increased 6.0% to $24.7 per pair for the three months ended September 30, 2010 compared to $23.3 for the same period in 2009. The increase of selling price is mainly resulted from the company's promotion policy and high-end products policy during this period, meanwhile, lots of types of summer shoes with lower price were sold during the same period of 2009. To achieve our sales strategy, we invested extensive advertisements in our stores and surrounding areas. Apart from the increase of selling price, our sales volume from retail outlets also increased 65.7% to 32,000 pairs of shoes during the three months ended September 30, 2010. The increase of sales volume is mainly resulted from increase of our outlets to 13 during the three months ended September 30, 2010 from 8 in the same period of 2009, which represent 62.5% increase. The total size of our stores was 1,340 and 900 square meters as of September 30, 2010 and 2009, respectively. The average size per store was 103 and 113 square meters as of September 30, 2010 and 2009, respectively. The average size of our newly opened stores is 75 square meters which is lower than our older stores due to limited available locations. Our sales volume per square meter per month was 8 and 7 pairs for the three months ended September 30, 2010 and 2009, respectively, representing a 14% increase. Our sales volume per outlet per month was 820 and 804 pairs for the three months ended September 30, 2010 and 2009, respectively.

Cost of Sales. For the three months ended September 30, 2010, cost of sales amounted to $2,001,078 or approximately 53.9 % of net revenues as compared to cost of sales of $1,656,918 or approximately 56.8% of net revenues for the same period of 2009. The average unit cost per pair increased to $10.4 for the third quarter of 2010 from $9.2 for the same period of 2009, an increase of 13%. Compared to 6.0% selling price increase in retail outlets and 19% selling price increase in wholesale business, it is generally in line with the increase. The increase is mainly resulted from selling more high-unit price model products during this period, compared to lower price products sold during the same period of 2009. We may continue to promote more high-unit price models, but, we do not expect that the unit price growth in following periods is as high as this quarter.

Gross Profit and Gross Margin. Gross profit for the three months ended September 30, 2010 increased $452,782 to $1,714,139 from $1,261,357 for the same period in 2009. Gross profit as a percentage of net sales, or gross margin, increased to 46.1% for the three months ended September 30, 2010 from 43.2% for the same period in 2009. The gross margin increase was primarily attributable to increased margins for both our retail and wholesale operations.

Gross profit for wholesale operations increased $133,953, or 11.86%, to $1,263,599 for the three months ended September 30, 2010 from $1,129,646 for the same period in 2009. Wholesale margins were 43.2% for the period ended September 30, 2010 and 45.8% for the same comparable period of 2009. Gross profit for retail operations increased $318,829, or 242% to $450,540 for the three months ended September 30, 2010 from $131,711 for the same period in 2009. Retail margins were 57% for the period ended September 30, 2010 and 29% for the same comparable period of 2009.

Operating Expenses. Our selling, general and administrative expenses grew to $488,505 in the three months ended September 30, 2010 from $201,927 in the same period in 2009. This was mainly due to increased advertising costs, rent for shopping mall spaces and increased payroll due to the expansion of the Registrant's business.

Other Income & Interest Expense. Other expenses were $540 in the three months ended September 30, 2010 and other income of $7,586 for the same comparable period of 2009. Other Income and Interest Expense is a negligible percentage of our revenue.

Income before Income Taxes. Our income before income taxes increased to $1,225,094 in the three months ended September 30, 2010 from $1,058,016 in the same period of 2009. The increase is mainly resulted from increase in gross profit offset by increased operating expenses.

Income Taxes. Income tax increased to $306,273 in the three months ended September 30, 2010 from $265,704 in the same period of 2009. The increase was due to an increase in taxable income, as our tax rate remained constant.

Net Income. In the three months ended September 30, 2010, we generated net income of $918,821, an increase from $792,312 in the same period of 2009. This increase was primarily due to the increase in gross profit of $1,714,139 in the three months ended September 30, 2010 from $1,261,357 for the same comparable period of 2009.

Comparison of Nine Months Ended September 30, 2010 and September 30, 2009

The following table sets forth key components of our results of operations during the nine months ended September 30, 2010 and 2009, both in dollars and as a percentage of our net sales.

	Nine Months Ended September 30, 2010		Nine Months Ended September 30, 2009	
	Amount	% of Net Sales	Amount	% of Net Sales
Net Sales	$ 14,964,654	100%	$ 12,517,751	100%
Cost of sales	8,080,396	54%	7,102,669	57%
Gross profit	6,884,258	46%	5,415,082	43%
Operating Expenses	1,652,685	11%	686,645	5%
Operating Income	5,231,573	35%	4,728,437	38%
Other income & interest expense	12,887	0%	24,879	0%
Income Before Income Taxes	5,244,460	35%	4,753,316	38%
Income taxes	1,421,768	10%	1,188,329	9%
Net income	$ 3,822,692	26%	$ 3,564,987	28%

Net Sales. Our net sales increased to $14,964,654 in the nine months ended September 30, 2010 from $12,517,751 in the same period in 2009, representing 19.6% revenue growth. As retail sales trends and broader economic growth in the PRC have been positive despite a global economic downturn, during the nine months ended September 30, 2010, we increased prices by 26% in order to achieve higher gross profit, which resulted in a decrease in sales volume of 5% as compared to the same period of 2009.

Net sales from our wholesale operations increased $997,370, or 8.8%, to $12,269,229 for the nine months ended September 30, 2010, from $11,271,859 for the nine months ended September 30, 2009. The average selling price per pair within our wholesale operations increased to $18.2 per pair for the nine months ended September 30, 2010 from $14.7 per pair in the same period last year, an increase of 23.8%, primarily due to acceptance of new designs and higher pricing of the products we promoted. However, it resulted in a sales volume decrease of 12.1% to 674 thousand pairs of shoes during the nine months ended September 30, 2010.

Net sales from our retail operations increased $1,449,533 to $2,695,425 for the nine months ended September 30, 2010, a 116.3% increase over sales of $1,245,892 for the nine months ended September 30, 2009. The average selling price per pair within our retail operations increased 10.8% to $25.7 per pair for the nine months ended September 30, 2010 compared to $23.2 for the same period in 2009. Apart from the increase of our selling price, our sales volume also contributed a 95.3% increase as compared to the same period of 2009, which was mainly the result of an increase in the number of our sales outlets from 8 as of September 30, 2009 to 13 as of September 30, 2010 respectively. The increase in our unit selling price was mainly the result of our sales strategy to promote more high-unit price products to the market to achieve higher gross profit. The total size of our stores was 1,340 and 900 square meters as of September 30, 2010 and 2009, respectively. The average size per store was 103 and 113 square meters as of September 30, 2010 and 2009, respectively. The average size of our newly opened stores is 75 square meters which is lower than our older stores due to limited available locations. Our sales volume per square meter per month was 13 and 10 pairs for the nine months ended September 30, 2010 and 2009, respectively. Our sales volume per outlet per month was 1,345 and 1,119 pairs for the nine months ended September 30, 2010 and 2009, respectively.

Cost of Sales. For the nine months ended September 30, 2010, cost of sales amounted to $8,080,396 or approximately 54% of net revenues as compared to cost of sales of $7,102,669 or approximately 56.7% of net revenues for the same period of 2009. The increase of cost of sales of 13.8% over the same period of 2009 was mainly caused by an increase in sales of 19.6%. The higher increase ratio in sales was mainly the result of a change in our sales mixture resulting in our retail sales increased to 18% of total sales as of September 30, 2010 compared to 10% during the same period of 2009. Retail sales contribute approximately same margin as wholesale operations.

Gross Profit and Gross Margin. Gross profit for the nine months ended September 30, 2010 increased $1,469,176 to $6,884,258 from $5,415,082 for the same period in 2009. Gross profit as a percentage of net sales, or gross margin, increased to 46% for the nine months ended September 30, 2010 from 43.3% for the same period in 2009. The gross margin increase was primarily attributable to increased margins for both our retail and wholesale operations and the change in our sales mixture as explained above.

Gross profit for wholesale operations increased $768,150, or 15.8%, to $5,644,269 for the nine months ended September 30, 2010 from $4,876,119 for the same period in 2009. Wholesale margins increased to 46% for the nine months ended September 30, 2010 from 43.3% for the same period in 2009. The increase in wholesale gross profit was primarily due to the increased selling price for wholesale operations offset by decreased sales volume due to the highly competitive local footwear market.

Gross profit for retail operations increased $701,026, or 130%, to $1,239,989 for the nine months ended September 30, 2010 from $538,963 for the same period in 2009. Retail margins increased to 46% for the nine months ended September 30, 2010 from 43% for the same period in 2009. The increase of gross profit was mainly caused by increased unit selling prices and sales volume in retail operations as explained above. The increase in gross margin mainly resulted from increased acceptance of our high-end products in the market, which have higher margin.

Operating Expenses. Our selling, general and administrative expenses grew to $1,652,685 in the nine months ended September 30, 2010 from $686,645 in the same period in 2009. This was mainly due to stock compensation and a payment of shares to service providers for services provided in connection with our reverse merger as well as increased advertising costs, rent for shopping mall space and increased payroll due to the expansion of our business.

Other Income & Interest Expense. Other income and interest expense decreased to $12,887 in the nine months ended September 30, 2010 from $24,879 in the same period in 2009. Other income and interest expense is a negligible percentage of our revenue.

Income before Income Taxes. Our income before income taxes increased to $5,244,460 in the nine months ended September 30, 2010 from $4,753,316 in the same period in 2009. The increase was mainly due to an increase in gross profit offset by increased operating expenses.

Income Taxes. Income tax increased to $1,421,768 in the nine months ended September 30, 2010 from $1,188,329 in the same period in 2009. The increase was due to an increase in taxable income, as our tax rate remained constant.

Net Income. In the nine months ended September 30, 2010, we generated net income of $3,822,692, an increase from $3,564,987 in the same period in 2009. This increase was primarily due to increased profit before tax as explained above.

Liquidity and Capital Resources

As of September 30, 2010, we had cash and cash equivalents of $422,017, primarily consisting of cash on hand and demand deposits. This compares with September 30, 2009, when we had cash and cash equivalents of $464,914, primarily consisting of cash on hand and demand deposits. The following table provides detailed information about our net cash flow for all financial statement periods presented in this report. To date, we have financed our operations primarily through cash flows from operations and equity contributions by our shareholders. We do not expect our daily operations to be constrained by cash flow as we are currently able to fund our operations through our existing cash flow from operations. However, our future expansion plans (which include increasing the number of sales points, advertising actively, and increasing inventory) rely entirely on the completion of an offering of our common stock. If an offering is not completed then we will need to rely on organic growth or commercial loans to facilitate our expansion plans and we cannot guarantee that we will be successful at obtaining loans or growing organically at a rate sufficient to support our expansion plans.

The following table sets forth a summary of our cash flows for the periods indicated:

Cash Flows

(all amounts in U.S. dollars)

	Nine Months Ended September 30, 2010	2009
Net cash provided by operating activities	$ 4,546,201	$ 6,591,232
Net cash used in investing activities	(4,533,530)	(376,899)
Net cash provided by (used in) financing activities	276,845	(5,865,513)
Effects of exchange rate change in cash	71,370	(2,440)
Net increase in cash and cash equivalents	360,886	346,380
Cash and cash equivalent at beginning of the period	61,131	118,534
Cash and cash equivalent at end of the period	422,017	464,914

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Operating activities

Net cash provided by operating activities was $4,546,201 for the nine months ended September 30, 2010, compared to $6,591,232 for the same period in 2009.

The cash provided by operating activities for the nine months ended September 30, 2010 was mainly derived from our net profit of $3,822,692, stock-based compensation of $442,611, and an increase of tax liabilities of $4,015,673, offset by an increase of accounts receivable of $151,190 and an increase of prepayments of $3,554,514. The increase of accounts receivable was due to an increased credit period policy designed to enhance sales following a sales fair held in February. We have granted short-term credit extensions as a strategic incentive to our most loyal and profitable distributors to increase our market share following such a sales fair, largely in order to introduce our new models of footwear. In order to balance our operating cash flow, we also ask for a longer payment term on our payables, which resulted in an increase of accounts payables. Increase of prepayment mainly represents payment during the period for advertising and long term leasing for our newly established outlets. These prepaid amounts are related to rent for operating stores, advertisement board and pole and landscaping maintenance contracts. These prepaid amounts are amortized based on the lease terms (for the prepaid rent), contracted terms for advertisement board and pole and contract terms for landscaping maintenance contract. The amortization expense for the nine months ended September 30, 2010 is $100,695.We may choose to lease or buy outlets in future. We may also continue to do advertising to promote our sales and increase our brand acceptance.

The cash provided by operating activities for the nine months ended September 30, 2009 was the result of net profit of $3,564,987, and increase in tax payable of $3,471,783, offset by the increase of accounts receivable, inventory and prepayment of $516,021 in total.

Investing activities

Net cash used in investing activities for the nine months ended September 30, 2010 was $4,533,530 as compared to $376,899 net cash used in investing activities during the same period of 2009. The cash used by investing activities during the nine months ended September 30, 2010 represents payment of $3,732,402 to acquire land use rights, payment of property and equipment of $132,804, payment for construction in progress of $548,887 and advance to related party of $119,437. The cash used in investing activities during the nine months ended September 30, 2009 represents the payment of property and equipment of $376,899.

Financing activities

Net cash provided by financing activities for the nine months ended September 30, 2010 was $276,845, as compared to $5,865,513 used in the same period of 2009. The cash provided by financing activities during the nine months ended September 30, 2010 represents the cash proceeds from bank loans of $1,194,369 offset by the distribution to owner of $484,565 and repayment on loans of $432,959. The cash used in financing activities during the nine months ended September 30, 2009 represents distribution to owner of $6,173,583.

Bank loans

Our bank loans include short-term loans and long-term loans. In our industry, it is customary to obtain such loans to meet cash flow and inventory needs.

Short term loans of $1,492,961 as at September 30, 2010, were issued by Bank of Qingdao and JiMo Rural Bank, with annual interest rates ranging from 6.372% to7.965%, and with terms of 12 months which will mature in September, November and December 2010 respectively. All bank loans were secured either by the property of the Company or third parties.

Capital resources

We believe that our cash on hand and cash flow from operations will meet part of our present cash needs and we will require additional cash resources, to meet our expected capital expenditure and working capital for the next 12 months. We may, however, in the future, require additional cash resources due to changed business conditions, implementation of our strategy to ramp up our marketing efforts and increase brand awareness, or acquisitions we may decide to pursue. If our own financial resources are insufficient to satisfy our capital requirements, we may seek to sell additional equity or debt securities or obtain additional credit facilities. The sale of additional equity securities could result in dilution to our stockholders. The incurrence of indebtedness would result in increased debt service obligations and could require us to agree to operating and financial covenants that would restrict our operations. Financing may not be available in amounts or on terms acceptable to us, if at all. Any failure by us to raise additional funds on terms favorable to us, or at all, could limit our ability to expand our business operations and could harm our overall business prospects.

Inflation

Inflation and changing prices have not had a material effect on our business and we do not expect that inflation or changing prices will materially affect our business in the foreseeable future. However, our management will closely monitor the price change in the industry and continually maintain effective cost control in operations.

Off Balance Sheet Arrangements

We do not have any off balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity or capital expenditures or capital resources that is material to an investor in our securities.

Seasonality

We may experience seasonal fluctuations in our revenue in some regions in the PRC, based on the seasonal changes in the weather and the tendency of customers to make purchases relating to their apparel suitable for the time of year. Any seasonality may cause significant pressure on us to monitor the development of materials accurately and to anticipate and satisfy these requirements. Our revenues are usually higher in the first and fourth quarters due to seasonal purchases.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires our management to make assumptions, estimates and judgments that affect the amounts reported, including the notes thereto, and related disclosures of commitments and contingencies, if any. We have identified certain accounting policies that are significant to the preparation of our financial statements. These accounting policies are important for an understanding of our financial condition and results of operation. Critical accounting policies are those that are most important to the portrayal of our financial conditions and results of operations and require management's difficult, subjective, or complex judgment, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods. Certain accounting estimates are particularly sensitive because of their significance to financial statements and because of the possibility that future events affecting the estimate may differ significantly from management's current judgments. We believe the following critical accounting policies involve the most significant estimates and judgments used in the preparation of our financial statements:

Revenue Recognition

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

Retail sales are recognized at the point of sale to customers. Wholesales to our 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. We do not allow any discounts, credits, rebates or similar privileges.

We do not grant any inventory pricing protection or other inventory adjusting policies to our distributors. The distributors are responsible for their purchased products types and volumes, unless any quality problems arise. If quality issues arise with our products, the products will be fully replaced by our manufacturers in accordance with the purchase agreement. As a result, we recognize our sales on delivery of our products to our wholesalers. For the retail customers, we only allow returns due to quality problems. We do not permit returns based on any other reason, and we do not believe such liberal return policies are common in China. Should there be any quality defects; customers have the right to return the shoes to the stores from which they purchased them. The stores then return them to our company, and we negotiate an acceptable solution with the manufacturers, which tend to vary with the facts in each case. According to our historical data, such returns are at approximately 0.01% of total sales and are not material to our financial statements.

In light of the low level of revenue dilution, we do not generally assess returns of products, levels of inventory, expected introductions of new products or external sources.

We have not experienced any purchases of products in excess of ordinary course of business levels as a result of any incentives. In our experience, customers merely purchase their seasonal footwear needs more quickly—but not in greater numbers—than they might otherwise purchase in the absence of such incentives. This result is not surprising in an industry like the footwear industry, which is marked by seasonal sales on, for example, sandals during summer and boots during winter. As a result of such seasonal fluctuations, our customers endeavor not to maintain excessive inventory but do try to purchase seasonally-specific shoes shortly before the season.

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.

Accounts Receivable

Accounts receivable consists of unpaid balances due from the whole-sale customers. Such balances generally are cleared in the subsequent month when the whole-sale customers place another order. The Company does not provide an allowance for doubtful accounts because the Company has not experienced any credit losses in collecting these amounts from whole-sale customers.

Impairment of Long-Lived Assets

The Company accounts for impairment of property and equipment and amortizable intangible assets in accordance with ASC 360, “Accounting for Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed of”, which requires the Company to evaluate a long-lived asset for recoverability when there is an event or circumstance that indicates the carrying value of the asset may not be recoverable. An impairment loss is recognized when the carrying amount of a long-lived asset or asset group is not recoverable (when the carrying amount exceeds the gross, undiscounted cash flows from use and disposition) and is measured as the excess of the carrying amount over the asset’s (or asset group’s) fair value. There was no impairment of long-lived assets for the years ended December 31, 2009 and 2008 or for the nine month period ended September 30, 2010.

Inventories

Merchandise inventories are stated at the lower of cost or market. Cost is determined on a weighted average basis and includes all expenditures incurred in bringing the goods to the point of sale and putting them in a salable condition. In assessing the ultimate realization of inventories, the management makes judgments as to future demand requirements compared to current or committed inventory levels. Our reserve requirements generally increase as our projected demand requirements; or decrease due to market conditions and product life cycle changes. The Company estimates the demand requirements based on market conditions, forecasts prepared by its customers, sales contracts and orders in hand.

In addition, the Company estimates net realizable value based on intended use, current market value and inventory ageing analyses. The Company writes down inventories for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventories and their estimated market value based upon assumptions about future demand and market conditions.

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.

Foreign Currency Translation

The Company's functional currency is Chinese Renminbi ("RMB") and its reporting currency is the U.S. dollar. Transactions denominated in foreign currencies are translated into U.S. dollar at exchange rate in effect on the date of the transactions. Exchange gains or losses on transaction are included in earnings.

The financial statements of the Company are translated into United States dollars in accordance with the provisions of ASC 830 “Foreign Currency Matters”, using the year-end rates of exchange for assets and liabilities, and average rates of exchange for the period for revenues, costs, and expenses and historical rates for the equity. Translation adjustments resulting from the process of translating the local currency financial statements into U.S. dollars are included in determining comprehensive income.

Segment Reporting

We operate as a single operating segment for purposes of presenting financial information and evaluating performance. As such, the accompanying consolidated financial statements present financial information in a format that is consistent with the internal financial information used by management. We do not accumulate operating expenses by wholesale and retail operations and, therefore, it is impractical to present such information.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls.

An evaluation was conducted under the supervision and with the participation of the Company’s management, including the Chief Executive Officer (“CEO”), its principal executive officer, and Chief Financial Officer (“CFO”), its principal financial officer, of the effectiveness of the design and operation of the Company’s disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) of the Exchange Act) as of September 30, 2010. Based on that evaluation, the CEO and CFO concluded that there had been improvements of the Company’s disclosure controls and procedures and the manner in which information that is required to be disclosed in Exchange Act report is reported within the time period specified in the SEC’s rule and forms. During the course of preparing our audited financial statements, our CEO and CFO determined that our disclosure controls and procedures were not effective as of September 30, 2010.

Conclusion

The Company did not have sufficient and skilled accounting personnel with an appropriate level of technical accounting knowledge and experience in the application of generally accepted accounting principles accepted in the United States of America commensurate with the Company’s disclosure controls and procedures requirements, which resulted in a number of deficiencies in disclosure controls and procedures that were identified as being significant. The Company’s management believes that the number and nature of these significant deficiencies, when aggregated, was determined to be a material weakness. The material weaknesses existed from prior to the Company’s reverse merger, when the operating company was a privately held company in China.

Management’s Plan to Remedy Material Weaknesses

When management recognized that it lacked personnel with experience and knowledge of U.S. GAAP, it sought to remedy these deficiencies by retaining third party consultants and new management personnel with experience in U.S. GAAP.

While the Company’s experience was with Chinese GAAP and Chinese legal obligations, the Company retained third-party accountants with Big 4 U.S. GAAP accounting experience to assist with the preparation and review of financial statements. These consultants assisted the Company both with the initial preparation of financial statements and communication with the Company's auditors. In addition to these accounting consultants, the Registrant has selected an auditor that has experience in reviewing U.S. GAAP financial statements.

Finally, after the end of the reporting period, the Company retained a new chief financial officer who has experience with U.S. GAAP. In addition, the Company has invited several individuals to serve as independent directors after completion of a currently contemplated registered public offering of its common stock. Although there can be no guarantee that the offering will be completed, the Company believes that the individuals who have agreed to serve as directors after the offering have the skills and experience necessary to provide valuable advice regarding these accounting matters.

Despite the material weaknesses and deficiencies reported above, the Company's management believes that its condensed consolidated financial statements included in this report fairly present in all material respects the Company's financial condition, results of operations and cash flows for the periods presented and that this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.

Changes in internal control over financial reporting.

Other than the efforts described above to improve its internal controls both before and after the end of the reporting period, there were no changes in the Company's internal control over financial reporting during the quarter ended September 30, 2010 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

From time to time, we may become involved in various lawsuits and legal proceedings which arise in the ordinary course of business. We are currently not aware of any such legal proceedings or claims that we expect will have a material adverse affect on our business, financial condition or operating results. However, litigation is subject to inherent uncertainties, and an adverse result in these or other matters may arise from time to time that may harm our business.

ITEM 1A. RISK FACTORS

During the three months ended September 30, 2010, there were no material changes to the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2009.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. REMOVED AND RESERVED

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit No.	Description
31.1*	Certification of Principal Executive Officer pursuant to Rule 13a-14(a) and Rule15d-14(a) of the Securities Exchange Act of 1934, as amended
31.2*	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended
32.1*	Certification of Principal Executive Officer, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32.2*	Certification of Principal Financial Officer, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Filed herewith.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

QINGDAO FOOTWEAR, INC.

By: /s/ Tao Wang
Tao Wang
Chief Executive Officer

Date: November 15, 2010

By: /s/ Joseph Meuse
Joseph Meuse
Chief Financial Officer

Date: November 15, 2010