

Edgar Filing: CHINA YILI PETROLEUM CO - Form 10-Q

CHINA YILI PETROLEUM CO
Form 10-Q
November 20, 2009

U. S. Securities and Exchange Commission
Washington, D. C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2009

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File No. 1-51554

China Yili Petroleum Company
(Name of Registrant in its Charter)

Nevada
(State of Other Jurisdiction of
incorporation or organization)

20-2934409
(I.R.S. Employer I.D. No.)

c/o American Union Securities, Inc., 100 Wall Street, 15th Floor, New York, NY 10005
(Address of Principal Executive Offices)

Issuer's Telephone Number: (212) 232-0120

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Sections 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 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 (§232.405 of this chapter) 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. (Check One)

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

Edgar Filing: CHINA YILI PETROLEUM CO - Form 10-Q

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

As of November 19, 2009, 29,748,348 shares of common stock, par value \$.001 per share, were outstanding.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

| CHINA YILI PETROLEUM COMPANY AND SUBSIDIARIES (A DEVELOPMENT STAGE COMPANY) CONSOLIDATED BALANCE SHEETS | | |
|--|--------------------------------------|----------------------|
| | September 30, 2009 (Unaudited) | December 31, 2008 |
| ASSETS | | |
| CURRENT ASSETS: | | |
| Cash | \$ 1,865 | \$ 6,057 |
| Other sundry current assets | 4,196 | 246 |
| TOTAL CURRENT ASSETS | 6,061 | 6,303 |
| Property and equipment, net of accumulated depreciation | 8,915,654 | 8,948,336 |
| TOTAL ASSETS | \$ 8,921,715 | \$ 8,954,639 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| CURRENT LIABILITIES: | | |
| Accounts payable | \$ 2,070,773 | \$ 1,683,564 |
| Due to shareholder | 218,209 | 365,912 |
| Accrued expenses | 113,604 | 87,280 |
| TOTAL CURRENT LIABILITIES | 2,402,586 | 2,136,756 |
| STOCKHOLDERS' EQUITY: | | |
| Common stock, \$0.001 par value, 100,000,000 shares authorized, 29,748,348 shares issued and outstanding at September 30, 2009 and December 31, 2008 | 29,748 | 29,748 |
| Preferred stock, \$0.001 par value, 4,700,000 shares authorized, 0 shares issued and outstanding | | |
| Preferred stock, Series A, \$0.001 par value, 300,000 shares authorized, 0 shares issued and outstanding at September 30, 2009 and December 31, 2008 | - | - |
| Additional paid-in capital | 6,718,841 | 6,709,768 |
| Accumulated deficit | (839,371) | (839,371) |

Edgar Filing: CHINA YILI PETROLEUM CO - Form 10-Q

| | | |
|---|---------------------|---------------------|
| Deficit accumulated during development stage | (297,896) | - |
| Accumulated other comprehensive income | 907,807 | 917,738 |
| TOTAL STOCKHOLDERS' EQUITY | 6,519,129 | 6,817,883 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | \$ 8,921,715 | \$ 8,954,639 |

The accompanying notes are integral part of the financial statements

| CHINA YILI PETROLEUM COMPANY AND SUBSIDIARIES | | | | | |
|--|----------------------------|---------------------|---------------------------|----------------------|-----------------------|
| (A DEVELOPMENT STAGE COMPANY) | | | | | |
| CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS | | | | | |
| (Unaudited) | | | | | |
| | For the three months ended | | For the nine months ended | | From |
| | September 30, | | September 30, | | Inception |
| | 2009 | 2008 | 2009 | 2008 | May 27, |
| | | | | | 2005 |
| | | | | | To |
| | | | | | September |
| | | | | | 30, 2009 |
| SALES | \$ - | \$ - | \$ - | \$ - | \$ - |
| COSTS AND EXPENSES | | | | | |
| General and administrative expenses | 97,974 | 47,714 | 288,823 | 167,887 | 1,168,339 |
| Interest expense | 2,382 | - | 9,073 | | 26,358 |
| TOTAL COSTS AND EXPENSES | 100,356 | 47,714 | 297,896 | 167,887 | 1,194,697 |
| NET LOSS FROM CONTINUING OPERATIONS | (100,356) | (47,714) | (297,896) | (167,887) | (1,194,697) |
| INCOME (LOSS) FROM DISCONTINUED OPERATIONS | - | (42,295) | - | (297,386) | 57,430 |
| NET LOSS | \$ (100,356) | \$ (90,009) | \$ (297,896) | \$ (465,273) | \$ (1,137,267) |
| OTHER COMPREHENSIVE LOSS | | | | | |
| Foreign currency translation adjustments | 7,197 | 19,429 | (9,931) | 446,613 | 907,807 |
| TOTAL COMPREHENSIVE LOSS | \$ (93,159) | \$ (70,580) | \$ (307,827) | \$ (18,660) | \$ (229,460) |
| Basic and diluted loss per common share: | | | | | |
| Continuing operations | \$ (0.003) | \$ (0.002) | \$ (0.010) | \$ (0.008) | |
| Discontinued operations | \$ - | \$ (0.002) | \$ - | \$ (0.014) | |
| Weighted average number of shares outstanding | 29,748,348 | 22,139,994 | 29,748,348 | 21,582,039 | |

The accompanying notes are integral part of the financial statements

3

CHINA YILI PETROLEUM COMPANY AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| | For the nine months ended September 30, | | From Inception May 27, 2005 To September 30, 2009 |
|--|--|-------------------|--|
| | 2009 | 2008 | |
| OPERATING ACTIVITIES: | | | |
| Net loss from continued operations | \$ (297,896) | \$ (167,887) | \$ (1,194,697) |
| Income (loss) from discontinued operations | - | (297,386) | 57,430 |
| Net loss | (297,896) | (465,273) | (1,137,267) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: | | | |
| Depreciation | 31,207 | 30,543 | 135,964 |
| Imputed interest | 9,073 | - | 26,358 |
| Changes in operating assets and liabilities: | | | |
| Other sundry current assets | (3,945) | 32,751 | (4,196) |
| Accounts payable | (5,373) | 14,630 | 2,070,773 |
| Accrued expenses | 26,445 | (17,410) | 113,604 |
| Net effect of discontinued operations | - | 40,362 | - |
| NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES | (240,489) | (364,397) | 1,205,236 |
| INVESTING ACTIVITIES: | | | |
| Acquisition of property and equipment | (11,256) | (22,083) | (9,051,619) |
| NET CASH USED IN INVESTING ACTIVITIES | (11,256) | (22,083) | (9,051,619) |
| FINANCING ACTIVITIES: | | | |
| Loan received from stockholder | 247,553 | 106,214 | 218,209 |
| Capital contributions | - | - | 6,722,232 |
| Net effect of discontinued operations | - | 255,830 | - |
| NET CASH PROVIDED BY FINANCING ACTIVITIES | 247,553 | 362,044 | 6,940,441 |
| EFFECT OF EXCHANGE RATE ON CASH | - | 1,112 | 907,807 |
| INCREASE (DECREASE) IN CASH | (4,192) | (23,324) | 1,865 |
| CASH - BEGINNING OF PERIOD | \$ 6,057 | 47,091 | \$ - |
| CASH - END OF PERIOD | \$ 1,865 | \$ 23,767 | \$ 1,865 |

Supplemental disclosures of cash flow information:

Non-cash financing activities for continued operations

| | | |
|---|------------|------|
| Transfer shareholder loan to accounts payable | \$ 394,630 | \$ - |
|---|------------|------|

Cash paid during the period for discontinued operations

| | | |
|---------------|------|-----------|
| Interest paid | \$ - | \$ 97,012 |
|---------------|------|-----------|

Non-cash financing activities for discontinued operations

| | | |
|---|------|------------|
| Loan receivable from affiliated company paid by stockholder | \$ - | \$ 289,693 |
|---|------|------------|

The accompanying notes are integral part of the financial statements

CHINA YILI PETROLEUM COMPANY AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2009

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of China Yili Petroleum Company and subsidiaries (the "Company") reflect all material adjustments consisting of only normal recurring adjustments which, in the opinion of management, are necessary for a fair presentation of results for the interim periods. Certain information and footnote disclosures required under accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission, although the Company believes that the disclosures are adequate to make the information presented not misleading. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2008 as filed with the Securities and Exchange Commission.

The results of operations for the nine months ended September 30, 2009 are not necessarily indicative of the results to be expected for the entire year or for any other period.

Certain amounts included in the 2008 financial statements have been reclassified to conform to the September 30, 2009 financial statement presentation.

The Company's functional currency is the Chinese Renminbi ("RMB"); however, the accompanying financial statements have been translated and presented in United States Dollars ("USD").

2 BUSINESS DESCRIPTION AND HISTORY

China Yili Petroleum Company and subsidiaries ("the Company"), a development stage company, intend to refine heavy oil into asphalt, fuel oil and lubricants through its wholly-owned subsidiary.

Since inception, the Company has been developing its facilities and obtaining the requisite approvals from the Chinese government and has not earned any revenue from operations. Accordingly, the Company's activities have been accounted for as those of a Development Stage Enterprise. The Company's financial statements are identified as those of a development stage company, and the statements of operations, stockholders' equity and cash flows disclose activity since the date of the Company's inception.

3 GOING CONCERN

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As shown on the accompanying financial statements, the Company's current liabilities exceeded its current assets by \$2,396,525 on September 30, 2009. The Company sustained an accumulative loss of \$ 1,137,267 from its inception to date. The Company has not earned any revenues from continuing operations since inception. These factors, among others, raise substantial doubt about the Company's ability to continue as a going concern. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of consolidation

The accompanying consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant inter-company balances and transactions have been eliminated in consolidation.

Uses of estimates in the preparation of financial statements

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

Property and equipment

Property and equipment are recorded at cost. Depreciation is provided in amounts sufficient to amortize the cost of the related assets over their useful lives using the straight line method for financial reporting purposes.

Maintenance, repairs and minor renewals are charged to expense when incurred. Replacements and major renewals are capitalized.

Impairment of long-lived assets

Long-lived assets are reviewed for impairment when circumstances indicate the carrying value of an asset may not be recoverable. For assets that are to be held and used, an impairment is recognized when the estimated undiscounted cash flows associated with the asset or group of assets is less than their carrying value. If impairment exists, an adjustment is made to write the asset down to its fair value, and a loss is recorded as the difference between the carrying value and fair value. Fair values are determined based on quoted market values, discounted cash flows or internal and external appraisals, as applicable. Assets to be disposed of are carried at the lower of carrying value or estimated net realizable value.

Deferred income taxes

Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases. In addition, recognition of future tax benefits, such as carryforwards, to the extent that realization of such benefits is more likely than not and that a valuation allowance be provided when it is more likely than not that some portion of the deferred tax assets will not be realized.

Foreign currency translation

The assets and liabilities of the Company's subsidiary, using the local currency as its functional currency, are translated to U.S. Dollars based on the current exchange rate prevailing at each balance sheet date and any resulting translation adjustments are included in Accumulated Other Comprehensive Income (Loss). The Company's revenues and expenses are translated into U.S. Dollars using the average exchange rates prevailing for each period presented.

New accounting pronouncements

In May 2009, the FASB issued guidance related to subsequent events under ASC 855-10, Subsequent Events. This guidance sets forth the period after the balance sheet date during which management or a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure, the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date, and the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. It requires disclosure of the date through which an entity has evaluated subsequent events and the basis for that date, whether that date represents the date the financial statements were issued or were available to be issued. This guidance is effective for interim and annual periods ending after June 15, 2009. We have included the required disclosures in our consolidated condensed financial statements.

In June 2009, the FASB issued Accounting Standards Update No. 2009-01 which amends ASC 105, Generally Accepted Accounting Principles. This guidance states that the ASC will become the source of authoritative U.S. GAAP recognized by the FASB to be applied by nongovernmental entities. Once effective, the Codification's content will carry the same level of authority. Thus, the U.S. GAAP hierarchy will be modified to include only two levels of U.S. GAAP: authoritative and non-authoritative. This is effective for financial statements issued for interim and annual periods ending after September 15, 2009. We adopted ASC 105 as of September 30, 2009 and thus have incorporated the new Codification citations in place of the corresponding references to legacy accounting pronouncements.

In August 2009, the FASB issued Accounting Standards Update No. 2009-05, Measuring Liabilities at Fair Value, which amends ASC 820, Fair Value Measurements and Disclosures. This Update provides clarification that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure the fair value using one or more of the following techniques: a valuation technique that uses the quoted price of the identical liability or similar liabilities when traded as an asset, which would be considered a Level 1 input, or another valuation technique that is consistent with ASC 820. This Update is effective for the first reporting period (including interim periods) beginning after issuance. Thus, we adopted this guidance as of September 30, 2009, which did not have a material impact on our consolidated condensed financial statements.

5

PROPERTY AND EQUIPMENT

A summary of property and equipment and the estimated lives used in the computation of depreciation and amortization are as follows:

| | September 30, 2009 | December 31, 2008 | Life |
|---|-----------------------|----------------------|----------|
| Right to use land | 246,854 | \$ 247,205 | 50 years |
| Building and building improvements | 1,769,309 | 1,771,826 | 39 years |
| Machinery and equipment | 4,735,786 | 4,736,644 | 7 years |
| Office equipment and furniture | 57,782 | 61,398 | 7 years |
| Automobiles | 162,797 | 154,092 | 7 years |
| | 6,972,528 | 6,971,165 | |
| Accumulated depreciation and amortization | (135,964) | (104,878) | |
| | 6,836,564 | 6,866,287 | |
| Construction in progress | 2,079,090 | 2,082,048 | |
| | \$ 8,915,654 | \$ 8,948,335 | |

6 DUE TO STOCKHOLDER

Amounts due to certain stockholders of China Yili Petroleum Company are non-interest bearing and are due on demand. Interest was imputed at 5% per annum for the nine months ended September 30, 2009.

7

INCOME TAXES

The Company has net operating loss carry-forwards in China of approximately \$1,000,000 which expire between 2012 and 2014.

The Company has a deferred tax asset resulting from the tax loss carry-forwards of approximately \$300,000 for which the Company has provided a 100% valuation allowance.

8

RISK FACTORS

Vulnerability due to Operations in PRC

The Company's operations may be adversely affected by significant political, economic and social uncertainties in the PRC. Although the PRC government has been pursuing economic reform policies for more than 20 years, no assurance can be given that the PRC government will continue to pursue such policies or that such policies may not be significantly altered, especially in the event of a change in leadership, social or political disruption or unforeseen circumstances affecting the PRC's political, economic and social conditions. There is also no guarantee that the PRC government's pursuit of economic reforms will be consistent or effective.

8

Substantially all of the Company's business is transacted in RMB, which is not freely convertible. The People's Bank of China or other banks are authorized to buy and sell foreign currencies at the exchange rates quoted by the People's Bank of China. Approval of foreign currency payments by the People's Bank of China or other institutions requires submitting a payment application form together with suppliers' invoices, shipping documents and signed contracts.

Since the Company has its primary operations in the PRC, the majority of its revenues will be settled in RMB, not U.S. Dollars. Due to certain restrictions on currency exchanges that exist in the PRC, the Company's ability to use revenue generated in RMB to pay any dividend payments to its shareholders may be limited.

Environmental concerns

The refining of petroleum involves the production of pollutants. In addition, the transportation of petroleum products entails a risk of spills that may result in long-term damage to the environment. There is increasing concern in China, however, over the degradation of the environment that has accompanied its recent industrial growth. It is likely that additional government regulation will be introduced in order to protect the environment. Compliance with such new regulations could impose substantial additional costs to the Company.

9 SUBSEQUENT EVENTS

We have evaluated events after the date of these financial statements through November 19, 2009, the date that these financial statements were issued. There were no material subsequent events as of that date.

9

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

Economic and Industry Trend

In past years, China has experienced a real estate boom, which also triggered the rapid development of the construction industry, which uses asphalt as a major material. However, in 2007, the Chinese government implemented a series of policies and regulations to curb inflation and the property market. These policies, together with the worldwide financial crisis in late 2008, have resulted a slowdown of the real estate market in China and our business, in turn, has been affected in 2008 and 2009. Recently, the Chinese government has changed its policy and prioritized boosting of the economy. The Chinese government has adopted new policies to address the slowdown of the real estate market, such as reducing stamp duties and transactions fees, lowering interest rates. The Chinese government has also decided to inject a stimulus package to boost the overall economy. From all of these, we have seen signs of recovery of the market in China.

Result of Operations

For the three months ended September 30, 2009 and 2008

During the three months ended September 30, 2009 and 2008, the Company did not generate any revenue or start profitable operation. As a result, there is no cost of goods sold incurred during the three-month periods ended September 30, 2009 and 2008.

Total operating expenses reported by the Company for the three months ended September 30, 2009 were mainly attributable to the general and administrative expenses which generally consisted of the facilities maintenance and depreciation cost. Compared to the operating expenses of \$47,714 incurred during the three months ended September 30, 2008, our total operating expenses have increased by \$52,642 or 110% to \$100,356 for the quarter ended September 30, 2009. The Company's operating expenses primarily involved expenses related to its activities in completing its factory, finalizing the development of its products, and securing the government licenses necessary for it to carry out its business plan. In addition, the Company also incurred expenses resulting from its status as a U.S. public company and its efforts to enter into the U.S. capital market.

Net loss was \$100,356 for the quarter ended September 30, 2009. For the quarter ended September 30, 2008, the Company incurred a net loss of \$47,714 from its continuing operations. And for the quarter ended September 30, 2008, net loss attributed to the Company's discontinued business of ASAP Expo was \$42,295.

For the nine months ended September 30, 2009 and 2008

During the nine months ended September 30, 2009 and 2008, the Company did not generate any revenue or start profitable operation. As a result, there is no cost of goods sold incurred during both nine months ended September 30, 2009 and 2008.

Total operating expenses reported by the Company of the nine months ended September 30, 2009 were mainly attributable to the general and administrative expenses which generally consisted of the facilities maintenance and depreciation cost. Compared to the operating expenses of \$167,887 incurred during the nine months ended September 30, 2008, our total operating expenses have increased by \$130,009 or 77% to \$297,896. The Company's operating expenses primarily involved expenses related to its activities in completing its factory, finalizing the development of its products, and securing the government licenses necessary for it to carry out its business plan. In addition, the Company also incurred expenses resulting from its status as a U.S. public company and its

efforts to enter into the U.S. capital market.

Net loss was \$297,896 for the nine months ended September 30, 2009. For the same period of 2008, the Company incurred a net loss of \$167,887 from its continuing operations. And for the nine months ended September 30, 2008, net loss attributed to the Company's discontinued business of ASAP Expo was \$297,386.

Liquidity and Capital Resources

Management anticipates that Yili Asphalt will commence revenue-producing operations in the near future. In order to do so, however, Yili Asphalt will have to obtain approximately \$500,000 in working capital to fund the initiation of operations. Management plans to approach a Chinese bank in order to borrow those funds on a secured basis, since Yili Asphalt has \$8.9 million in capital assets on its books that are currently free of liens. To date, however, it has not obtained a commitment for the funds. If there is a delay in securing the necessary funds, the date for initiation of revenue-producing operations will be likewise delayed.

Because the Company's refining process yields three different end products (asphalt, diesel fuel, lubricants), the Company's initial operations will entail a sudden increase in working capital demands. Among the more significant funding demands will be:

- **Marketing.** Yili Asphalt intends to engage in direct marketing of all products lines. Management expects that its direct marketing program will prove to be more efficient over the long term than a distribution network. However, the initial burden on its working capital will be considerable, as Yili Asphalt will have to carry the full cost of a sales staff, the expenses of their marketing activities, such as travel, entertainment, and promotion, and the expenses attendant to sales accounting.
- **Potentially Inefficient Use of Facilities.** To optimize the utilization of our refinery, we will have to generate sales of our products in the proportions in which the refinery is designed to produce them: roughly 6:3:2 for fuel, asphalt and lubricants respectively. It is unlikely that sales will occur naturally in those proportions. If sales in one or two of the categories lag the other(s), management will face the Hobson's choice of delaying production in the faster selling category, thus losing the benefit of the demand for that category, or tolerating excess inventories of the slower selling categories. This situation would result in additional demands on our working capital.

In addition to our need for working capital to initiate production, our business plan calls for substantial capital investment over the next twelve months. The primary purposes for which we anticipate a need for capital are:

- **Additional Working Capital for Growth.** We believe there is a high demand for our products in Inner Mongolia and the neighboring provinces. If we are correct, then demand could enable us to quickly expand our operations to full capacity. Growth at that rapid rate would require a commitment of many millions of Dollars for working capital. Our management will have to assess the value of the market opportunities that present themselves, and weight them against the cost of such capital as may be made available to us.
- **Construction of Dedicated Rail Line.** The government of Inner Mongolia has committed to construct a rail line that will have a siding at our refinery. Construction is rescheduled in 2009. The benefit to us in terms of reduced transportation costs would be substantial. The government's proposal, however, contemplates that Yili Asphalt will make a substantial capital contribution toward the construction project. The amount of the contribution has not been determined.
 - **Acquisition of Refinery.** Chunshi Li, our Chairman, has committed to purchase Mongolia Kailu Yili Asphalt Co., Ltd., an asphalt company with a production capacity of 100,000 tons. He intends to assign his rights in Mongolia Kailu to Yili Asphalt if we are able to fund the cost. The purchase price will be 20 million RMB (approximately \$2.7 million). In addition, Mongolia Kailu is currently unproductive due to deterioration of its facilities. In order to bring it back online, we will have to fund the construction of a waterproof coiled material production line at its plant, which will entail an investment of several million more Renminbi.

At the present time, we have received no commitments for the funds required for our planned capital investments. Obtaining those funds, if we can do so, will require that we issue substantial amounts of equity securities or incur significant debts. We believe that the expected return on those investments will justify the cost. Without additional funding, the Company will not be able to pursue its business model. If adequate funds are not available or are not available on acceptable terms when required, we would be required to significantly curtail our operations and would not be able to fund the development of the business envisioned by our business model. These circumstances could have a material adverse effect on our business and result in our inability to continue to operate as a going concern.

Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on its financial condition or results of operations.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Not applicable.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures.

The Company's management under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, performed an evaluation of the effectiveness of the design, maintenance and operation of the Company's disclosure controls and procedures as of September 30, 2009. Pursuant to Rule 13a-15(e) promulgated by the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934, "disclosure controls and procedures" means controls and other procedures that are designed to insure that information required to be disclosed by China Yili in the reports that it files with the Securities and Exchange Commission is recorded, processed, summarized and reported within the time limits specified in the Commission's rules. "Disclosure controls and procedures" include, without limitation, controls and procedures designed to insure that information China Yili is required to disclose in the reports it files with the Commission is accumulated and communicated to our Chief Executive Officer and Chief Financial Officer as appropriate to allow timely decisions regarding required disclosure. Based on his evaluation, our Chief Executive Officer and Chief Financial Officer concluded that China Yili's system of disclosure controls and procedures was effective as of September 30, 2009 for the purposes described in this paragraph.

Changes in Internal Control over Financial Reporting

During the three months ended September 30, 2009, there has been no change in our internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) under the Exchange Act) that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The company is not party to any material legal proceeding.

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

(c) Unregistered sales of equity securities

None.

(e) Purchases of equity securities

The Company did not repurchase any of its equity securities that were registered under Section 12 of the Securities Exchange Act during the 3rd quarter of fiscal 2009.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

31 Rule 13a-14(a) Certification

32 Rule 13a-14(b) Certification

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.

China Yili Petroleum Company

Date : November 20, 2009

/s/Chunshi Li
Chunshi Li, Chief Executive Officer
and Chief Financial Officer

