

ACL SEMICONDUCTOR INC  
Form 10-Q  
August 19, 2010

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2010

OR

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

Commission file number: 000-50140

**ACL Semiconductors Inc.**

(Exact name of Registrant as specified in its charter)

Delaware

16-1642709

\_\_\_\_\_  
(State or other jurisdiction of incorporation or organization)

\_\_\_\_\_  
(I.R.S. Employer Identification Number)

Room 1701, 17/F.,  
Tower 1, Enterprise Square, 9 Sheung Yuet Road, Kowloon Bay,  
Kowloon, Hong Kong.

\_\_\_\_\_  
(Address of principal executive offices) (Zip code)

011-852-3666-9939

\_\_\_\_\_  
(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  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. (Check one):

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Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

The Registrant had 28,729,936 shares of common stock outstanding as of August 14, 2010.

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## TABLE OF CONTENTS

	<u>Page</u>	
<u>Part I</u>	<u>FINANCIAL INFORMATION</u>	
<u>ITEM 1.</u>	<u>Financial Statements (Unaudited)</u>	1
	<u>Condensed Consolidated Balance Sheets (Unaudited)</u>	1
	<u>Condensed Consolidated Statements of Income (Unaudited)</u>	3
	<u>Condensed Consolidated Statements of Cash Flows (Unaudited)</u>	4
	<u>Notes to the Condensed Consolidated Financial Statements (Unaudited)</u>	6
<u>ITEM2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	26
<u>ITEM 3.</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	34
<u>ITEM 4T.</u>	<u>Controls and Procedures</u>	35
<u>Part II</u>	<u>OTHER INFORMATION</u>	36
<u>ITEM 1.</u>	<u>Legal Proceedings</u>	36
<u>ITEM 1A.</u>	<u>Risk Factors</u>	36
<u>ITEM 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	36
<u>ITEM 3.</u>	<u>Defaults Upon Senior Securities</u>	36
<u>ITEM 4.</u>	<u>(Removed and Reserved)</u>	36
<u>ITEM 5.</u>	<u>Other Information</u>	36
<u>ITEM 6.</u>	<u>Exhibits</u>	37
<u>SIGNATURES</u>		38
<u>EXHIBIT INDEX</u>		41

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## PART I FINANCIAL INFORMATION

## ITEM 1. Financial Statements

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Condensed Consolidated Balance Sheets (Unaudited)

	As of June 30, 2010 (Unaudited)	As of December 31, 2009
	<u>          </u>	<u>          </u>
<b>Current assets:</b>		
Cash and cash equivalents	\$ 2,986,215	\$ 2,001,805
Restricted cash	2,088,374	2,086,504
Accounts receivable, net of allowance for doubtful accounts of \$0 for 2010 and 2009	15,956,010	12,434,386
Inventories, net	5,323,246	6,048,116
Other current assets	232,453	274,351
	<u>          </u>	<u>          </u>
Total current assets	26,586,298	22,845,162
<b>Property, equipment and improvements</b> , net of accumulated depreciation and amortization	8,261,132	8,179,765
<b>Other deposits</b>	145,159	213,535
<b>Amount due from Mr. Yang</b>	11,238,556	11,233,839
	<u>          </u>	<u>          </u>
<b>Total Assets</b>	<u>46,231,145</u>	<u>42,472,301</u>

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

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Condensed Consolidated Balance Sheets (Unaudited)

## LIABILITIES AND STOCKHOLDERS EQUITY

	As of June 30, 2010 (Unaudited)	As of December 31, 2009
	<u>                    </u>	<u>                    </u>
<b>Current liabilities:</b>		
Accounts payable	\$ 22,023,418	\$ 23,838,753
Accrued expenses	451,947	527,582
Lines of credit and loan facilities	12,645,544	9,013,813
Current portion of long-term debt	319,530	318,972
Current portion of capital lease	298,434	318,135
Income tax payable	861,012	505,078
Due to stockholders for converted pledged collateral	112,385	112,385
Other current liabilities	159,863	282,475
	<u>                    </u>	<u>                    </u>
Total current liabilities	36,872,133	34,917,193
<b>Long-term liabilities</b>		
Long-term debts, less current portion	2,589,265	2,747,981
Capital lease, less current portion	73,866	146,117
Deferred tax liabilities	19,468	19,468
	<u>                    </u>	<u>                    </u>
Total long-term liabilities	2,682,599	2,913,566
	<u>                    </u>	<u>                    </u>
<b>Total Liabilities</b>	<b>39,554,732</b>	<b>37,830,759</b>
	<u>                    </u>	<u>                    </u>
<b>Stockholders equity:</b>		
Common stock - \$0.001 par value; 50,000,000 shares authorized; 28,729,936 issued and outstanding as of June 30, 2010 and December 31, 2009 respectively	28,730	28,730
Additional paid in capital	3,658,627	3,658,627
Retained earnings	2,989,056	954,185
	<u>                    </u>	<u>                    </u>
Total stockholders equity	6,676,413	4,641,542
	<u>                    </u>	<u>                    </u>
<b>Total Liabilities and Stockholders equity</b>	<b>46,231,145</b>	<b>42,472,301</b>
	<u>                    </u>	<u>                    </u>

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

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Condensed Consolidated Statements of Income (Unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2010	June 30, 2009 (Restated)	June 30, 2010	June 30, 2009 (Restated)
Net sales				
Related parties	\$ 2,119,515	\$ 159,577	\$ 3,560,951	\$ 475,999
Other	87,412,775	75,667,934	184,982,401	137,858,640
Less discounts to customers		(449)		(7,438)
	<u>89,532,290</u>	<u>75,827,062</u>	<u>188,543,352</u>	<u>138,327,201</u>
Cost of sales	<u>87,601,020</u>	<u>73,273,593</u>	<u>183,785,478</u>	<u>132,915,773</u>
Gross profit	1,931,270	2,553,469	4,757,874	5,411,428
Operating expenses				
Selling	28,586	36,256	53,388	58,434
General and administrative	1,122,719	1,232,737	2,180,589	2,522,190
	<u>779,965</u>	<u>1,284,476</u>	<u>2,523,897</u>	<u>2,830,804</u>
Income from operations				
Other income (expenses)				
Rental income	30,000	22,308	60,000	44,615
Interest expense	(110,705)	(115,918)	(205,869)	(282,810)
Management and service income	10,884	7,641	19,205	14,180
Net income on cash flow hedge		28,372	15,410	48,721
Interest income	192	2,312	285	31,022
(Loss) profit on disposal of fixed assets		21,350	(308)	21,350
Exchange differences	(8,754)	7,699	(14,957)	5,555
Miscellaneous	20,518	5,310	21,479	3,354
	<u>722,100</u>	<u>1,263,550</u>	<u>2,419,142</u>	<u>2,716,791</u>
Income before income taxes provision				
Income taxes provision	128,205	179,487	384,271	397,436
	<u>593,895</u>	<u>1,084,063</u>	<u>2,034,871</u>	<u>2,319,355</u>
Net Income				
Earnings per share - basic and diluted	\$ 0.02	\$ 0.04	\$ 0.07	\$ 0.08
Weighted average number of shares - basic and diluted	<u>28,729,936</u>	<u>28,729,936</u>	<u>28,729,936</u>	<u>28,729,936</u>

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

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Condensed Consolidated Statements of Cash Flows (Unaudited)

	Six months ended	
	June 30, 2010	June 30, 2009 (Restated)
	<u>                    </u>	<u>                    </u>
<b>Cash flows provided by (used for) operating activities:</b>		
Net income	\$ 2,034,871	\$ 2,319,355
	<u>                    </u>	<u>                    </u>
<b>Adjustments to reconcile net income (loss) to net cash provided by (used for) operating activities:</b>		
Depreciation and amortization	154,837	142,019
Change in inventory reserve	283,031	149,744
Loss (Gain) on disposal of fixed assets	308	(21,350)
Issuance of common stocks to consultant as professional fee under share option scheme		66,000
<b>Changes in assets and liabilities:</b>		
<b>(Increase) decrease in assets</b>		
Accounts receivable - other	(3,521,622)	1,002,970
Accounts receivable - related parties		1,817,321
Inventories	441,839	529,448
Other current assets	41,897	483,235
Other assets	68,376	342,038
<b>Increase (decrease) in liabilities</b>		
Accounts payable	(1,815,334)	899,347
Accrued expenses	(75,635)	455,862
Income tax payable	355,934	397,436
Other current liabilities	(122,612)	(275,980)
	<u>                    </u>	<u>                    </u>
Total adjustments	(4,188,981)	5,988,090
	<u>                    </u>	<u>                    </u>
Net cash provided by (used for) operating activities	(2,154,110)	8,307,445
	<u>                    </u>	<u>                    </u>

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

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Condensed Consolidated Statements of Cash Flows (CONTINUED) (Unaudited)

<b>Cash flows used for investing activities:</b>		
Advanced to Aristo / Mr. Yang	(4,717)	(3,486,519)
(Increase) decrease of restricted cash	(1,870)	3,083,251
Investment in restricted marketable securities		500,000
Cash proceeds from sale of fixed assets	81,154	37,820
Purchases of fixed assets	(195,453)	(57,517)
	<u>          </u>	<u>          </u>
Net cash provided by (used for) investing activities	(120,886)	77,035
	<u>          </u>	<u>          </u>
<b>Cash flows provided by (used for) financing activities:</b>		
Net borrowings on lines of credit and notes payable	3,631,731	(8,465,564)
Principal payments under long-term debt	(158,159)	(79,757)
Principal payments under capital lease obligation	(214,165)	(35,989)
	<u>          </u>	<u>          </u>
Net cash provided by (used for) financing activities	3,259,407	(8,581,310)
	<u>          </u>	<u>          </u>
<b>Net increase (decrease) in cash and cash equivalents</b>	984,411	(196,830)
<b>Cash and cash equivalents, beginning of period</b>	2,001,805	1,943,463
	<u>          </u>	<u>          </u>
<b>Cash and cash equivalents, end of period</b>	<u>\$ 2,986,216</u>	<u>\$ 1,746,633</u>

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



## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 1. The Company**

ACL Semiconductors, Inc. ( Company or ACL ) was incorporated in the State of Delaware on September 17, 2002 and acquired Atlantic Components Ltd., a Hong Kong based company ( Atlantic ) through a reverse-acquisition that was effective September 30, 2003. The Company s principal activities are distribution of electronic components under the Samsung brand name which comprise Dynamic Random Access Memory ( DRAM ), Graphic Random Access Memory ( Graphic RAM ), and Flash for the Hong Kong Special Administrative Region and Republic of China markets. Atlantic was incorporated in Hong Kong on May 30, 1991. On October 2, 2003, the Company set up a wholly-owned subsidiary, Alpha Perform Technology Limited ( Alpha ), a British Virgin Islands company, to provide services on behalf of the Company in jurisdictions outside of Hong Kong. Effective January 1, 2004, the Company ceased the operations of Alpha and all the related activities are consolidated with those of Atlantic.

**NOTE 2. Summary of Significant Accounting Policies***(a) Method of Accounting*

The Company maintains its general ledger and journals with the accrual method accounting for financial reporting purposes. The consolidated financial statements and notes are representations of management. Accounting policies adopted by the Company conform to generally accepted accounting principles in the United States of America and have been consistently applied in the presentation of consolidated financial statements.

*(b) Principles of Consolidation*

The consolidated financial statements are presented in US Dollars and include the accounts of the Company and its subsidiary. All significant inter-company balances and transactions are eliminated in consolidation.

The Company owned its subsidiary soon after its inception and continued to own the equity s interests through June 30, 2010. The following table depicts the identity of the subsidiary:

Name of Subsidiary	Place of Incorporation	Attributable Equity Interest %	Registered Capital
Alpha Perform Technology Limited	BVI	100	\$ 1,000
Atlantic Components Limited	Hong Kong	100	\$ 384,615
* Aristo Technologies Limited	Hong Kong	100	\$ 1,282

\* Note: Deemed variable interest entity

Variable Interests Entities

According to ASC 810-10-25 which codified FASB Interpretation No. 46 (Revised December 2003), Consolidation of Variable Interest Entities an interpretation of ARB No. 51 (FIN 46R), an entity that has one or more of the three characteristics set forth therein is considered a variable interest entity. One of such characteristics is that the equity investment at risk in the relevant entity is not sufficient to permit the entity to finance its activities without additional subordinated financial support provided by any parties, including the equity holders.

ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 2. Summary of Significant Accounting Policies (Continued)**

ASC 810-05-08A specifies the two characteristics of a controlling financial interest in a variable interest entity (VIE): (1) the power to direct the activities of a VIE that most significantly impact the VIE's economic performance; and (2) the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. The Company is the primary beneficiary of Aristo because the Company can direct the activities of Aristo through the common director and major shareholder. Also, the Company extended substantial account receivable to Aristo and created an obligation to absorb losses if Aristo failed. Moreover, ASC 810-25-42 & 43 provides guidance on related parties treatment of VIE and specifies the relationship of de-facto agent and principal. Those guidance will help to determine whether the Company will consolidate Aristo.

Owing to the extent of outstanding large amounts of accounts receivable since 2007 together with the nominal amount of paid-up capital contributed by Mr. Yang when Aristo was formed, it has been determined that Aristo cannot finance its operations without subordinated financial support from ACL and accordingly, ACL is considered to be the de facto principal of Aristo, Aristo is considered to be the de facto subsidiary of the Company and Mr. Yang is considered to be the related party of both the Company and Aristo.

By virtue of the above analysis, it has been determined that the Company is the primary beneficiary of Aristo.

*Aristo Technologies Limited*

The Company sells Samsung memory chips to Aristo and allows long grace periods for Aristo to repay the open accounts receivable. Being the biggest creditor, the Company does not require Aristo to pledge assets or enter into any agreements to bind Aristo to specific repayment terms. The Company does not provide any bad debt provision or experience derived from Aristo. Although, the Company is not involved in Aristo's daily operation, it believes that there will not be significant additional risk derived from the trading relationship and transactions with Aristo.

Aristo is engaged in the marketing, selling and servicing of computer products and accessories including semiconductors, LCD products, mass storage devices, consumer electronics, computer peripherals and electronic components for various brands such as Samsung, Hynix, Micron, Elpida, Qimonda, Lexar, Dane-Elec, Elixir, SanDisk and Winbond. Aristo 2009 and 2008 sales was around 30 million and 20 million; it was only a small distributor that accommodated special requirements for specific customers.

The Company sells to Aristo in order to fulfill Aristo's periodic need for Samsung memory products based on prevailing market prices, which products Aristo, in turn, sells to its customers. The sales to Aristo during the second quarter of 2010 were \$440,555 with accounts receivable of \$11,486,467 as of June 30, 2010. For fiscal year 2009, sales to Aristo were \$13,160,521 with accounts receivable of \$10,315,388 as of December 31, 2009. For fiscal year 2008, sales to Aristo were \$9,076,034 with accounts receivable of \$6,695,409 as of December 31, 2008.

The Company purchases from Aristo, from time to time, LCD panels, Samsung memory chips, DRAM, Flash memory, central processing units, external hard disks, DVD readers and writers that the Company cannot obtain from Samsung directly due to supply limitations.

(c) *Use of estimates*

The preparation of the consolidated financial statements in conformity with generally accepted accounting principles in the United States of America 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 consolidated financial statements and the reported amounts 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.

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 2. Summary of Significant Accounting Policies (Continued)***(d) Economic and political risks*

The Company's operation is conducted in Hong Kong. A large amount of customers are located in Southern China. Accordingly, the Company's business, financial condition and results of operations may be influenced by the political, economic and legal environment in Hong Kong and China, and by the general state of the economy in Hong Kong and China.

The Company's operations in Hong Kong and have large amount of customers from Southern China who are subject to special considerations and significant risks not typically associated with companies in North America and Western Europe. These include risks associated with, among others, the political, economic and legal environment and foreign currency exchange. The Company's results may be adversely affected by changes in the political and social conditions in Hong Kong and China, and by changes in governmental policies with respect to laws and regulations, anti-inflationary measures, currency conversion, remittances abroad, and rates and methods of taxation, among other things.

*(e) Property, plant and equipment*

Plant and equipment are carried at cost less accumulated depreciation. Depreciation is provided over their estimated useful lives, using the straight-line method. Estimated useful lives of the plant and equipment are as follows:

Automobiles	3 1/3 years
Computers	5 years
Leasehold improvement	5 years
Land and buildings	By estimated useful life
Office equipment	5 years
Machinery	10 years

The cost and related accumulated depreciation of assets sold or otherwise retired are eliminated from the accounts and any gain or loss is included in the statement of income.

*(f) Account receivable*

Accounts receivable is carried at the net invoiced value charged to customer. The Company records an allowance for doubtful accounts to cover estimated credit losses. Management reviews and adjusts this allowance periodically based on historical experience and its evaluation of the collectability of outstanding accounts receivable. The Company evaluates the credit risk of its customers utilizing historical data and estimates of future performance.

*(g) Accounting for impairment of long-lived assets*

The Company periodically evaluates the carrying value of long-lived assets to be held and used, including intangible assets subject to amortization, when events and circumstances warrant such a review, pursuant to the guidelines established in ASC No. 360 (formerly Statement of Financial Accounting Standards No. 144). The carrying value of a long-lived asset is considered impaired when the anticipated undiscounted cash flow from such asset is separately identifiable and is less than its carrying value. In that event, a loss is recognized based on the amount by which the carrying value exceeds the fair market value of the long-lived asset. Fair market value is determined primarily using the anticipated cash flows discounted at a rate commensurate with the risk involved. Losses on long-lived assets to be disposed of are determined in a similar manner, except that fair market values are reduced for the cost to dispose.

During the reporting years, there was no impairment loss.

ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 2. Summary of Significant Accounting Policies (Continued)**

*(h) Cash and cash equivalents*

The Company considers all highly liquid investments purchased with original maturities of three months or less to be cash equivalents. The Company maintains bank accounts in Hong Kong. The Company does not maintain any bank accounts in the United States of America.

*(i) Inventories*

Inventories are stated at the lower of cost or market and are comprised of purchased computer technology resale products. Cost is determined using the first-in, first-out method. The reserve for obsolescence was decreased by \$283,031 during the first six months of 2010 and decreased by \$149,744 for the same period of 2009. Inventory obsolescence reserves totaled \$64,102 as of June 30, 2010 and \$347,133 as of December 31, 2009.

*(j) Lease assets*

Leases that substantially transfer all the benefits and risks of ownership of assets to the company are accounted for as capital leases. At the inception of a capital lease, the asset is recorded together with its long term obligation (excluding interest element) to reflect the purchase and the financing.

Leases which do not transfer substantially all the risks and rewards of ownership to the company are classified as operating leases. Payments made under operating leases are charged to income statement in equal installments over the accounting periods covered by the lease term. Lease incentives received are recognized in income statement as an integral part of the aggregate net lease payments made. Contingent rentals are charged to income statement in the accounting period which they are incurred.

*(k) Income taxes*

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets, including tax loss and credit carry forwards, and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred income tax expense represents the change during the period in the deferred tax assets and deferred tax liabilities. The components of the deferred tax assets and liabilities are individually classified as current and non-current based on their characteristics. Realization of the deferred tax asset is dependent on generating sufficient taxable income in future years. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The Company did not have any interest and penalty recognized in the income statements for the period ended June 30, 2010 and June 30, 2009 or balance sheet as of June 30, 2010 and December 31, 2009. The Company did not have uncertainty tax positions or events leading to uncertainty tax position within the next 12 months. The Company's 2007, 2008 and 2009 U.S. federal income tax returns are subject to U.S. Internal Revenue Service examination and the Company's 2003/4, 2004/5, 2005/6, 2006/7, 2007/8, 2008/9, 2009/2010 Hong Kong Company Income Tax filing are subject to Hong Kong Inland Revenue Department examination.

ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 2. Summary of Significant Accounting Policies (Continued)**

*(l) Foreign currency translation*

The accompanying consolidated financial statements are presented in United States dollars. The functional currency of the Company is the Hong Kong Dollar (HK\$). The consolidated financial statements are translated into United States dollars from HK\$US\$1.00=HKD7.80, a fixed exchange rate maintained between Hong Kong and United States derived from the Hong Kong Monetary Authority pegging HKD and USD monetary policy.

*(m) Revenue recognition*

The Company derives revenues from resale of computer memory products. The Company recognizes revenue in accordance with the SEC Staff Accounting Bulletin No. 104, Revenue Recognition (SAB 104). Under SAB 104, revenue is recognized when there is persuasive evidence of an arrangement, delivery has occurred or services are rendered, the sales price is determinable, and collectability is reasonably assured. Revenue typically is recognized at time of shipment. Sales are recorded net of discounts, rebates, and returns, which historically were not material.

*(n) Advertising*

The Group expensed all advertising costs as incurred. Advertising expenses included in general and administrative expenses were \$1,471 as of June 30, 2010 and \$948 for the years ended June 30, 2009.

*(o) Segment reporting*

The Company's sales are generated from Hong Kong and the rest of China and substantially all of its assets are located in Hong Kong.

*(p) Fair value of financial instruments*

The carrying amount of the Company's cash and cash equivalents, accounts receivable, lines of credit, convertible debt, accounts payable, accrued expenses, and long-term debt approximates their estimated fair values due to the short-term maturities of those financial instruments.

*(q) Comprehensive income*

Comprehensive income is defined to include all changes in equity except those resulting from investments by owners and distributions to owners. Among other disclosures, all items that are required to be recognized under current accounting standards as components of comprehensive income are required to be reported in a financial statement that is presented with the same prominence as other consolidated financial statements. The Company has no items that represent other comprehensive income and, therefore, has not included a schedule of comprehensive income in the consolidated financial statements.

*(r) Basic and diluted earnings (loss) per share*

In accordance with ASC No. 260 (formerly SFAS No. 128), Earnings Per Share, the basic earnings (loss) per common share is computed by dividing net earnings (loss) available to common stockholders by the weighted average number of common shares outstanding. Diluted earnings (loss) per common share is computed similarly to basic earnings (loss) per common share, except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive.

ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 2. Summary of Significant Accounting Policies (Continued)**

*(s) Reclassification*

Certain amounts in the prior period have been reclassified to conform to the current consolidated financial statement presentation.

*(t) Recently implemented standards*

ASC 105, Generally Accepted Accounting Principles ( ASC 105 ) (formerly Statement of Financial Accounting Standards No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB Statement No. 162) reorganized by topic existing accounting and reporting guidance issued by the Financial Accounting Standards Board ( FASB ) into a single source of authoritative generally accepted accounting principles ( GAAP ) to be applied by nongovernmental entities. All guidance contained in the Accounting Standards Codification ( ASC ) carries an equal level of authority. Rules and interpretive releases of the Securities and Exchange Commission ( SEC ) under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. Accordingly, all other accounting literature will be deemed non-authoritative . ASC 105 is effective on a prospective basis for financial statements issued for interim and annual periods ending after September 15, 2009. The Company has implemented the guidance included in ASC 105 as of July 1, 2009. The implementation of this guidance changed the Company s references to GAAP authoritative guidance but did not impact the Company s financial position or results of operations.

ASC 855, Subsequent Events ( ASC 855 ) (formerly Statement of Financial Accounting Standards No. 165, Subsequent Events) includes guidance that was issued by the FASB in May 2009, and is consistent with current auditing standards in defining a subsequent event. Additionally, the guidance provides for disclosure regarding the existence and timing of a company s evaluation of its subsequent events. ASC 855 defines two types of subsequent events, recognized and non-recognized . Recognized subsequent events provide additional evidence about conditions that existed at the date of the balance sheet and are required to be reflected in the financial statements. Non-recognized subsequent events provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date and, therefore; are not required to be reflected in the financial statements. However, certain non-recognized subsequent events may require disclosure to prevent the financial statements from being misleading. This guidance was effective prospectively for interim or annual financial periods ending after June 15, 2009. The Company implemented the guidance included in ASC 855 as of April 1, 2009. The effect of implementing this guidance was not material to the Company s financial position or results of operations.

ASC 805, Business Combinations ( ASC 805 ) (formerly included under Statement of Financial Accounting Standards No. 141 (revised 2007), Business Combinations) contains guidance that was issued by the FASB in December 2007. It requires the acquiring entity in a business combination to recognize all assets acquired and liabilities assumed in a transaction at the acquisition-date fair value, with certain exceptions. Additionally, the guidance requires changes to the accounting treatment of acquisition related items, including, among other items, transaction costs, contingent consideration, restructuring costs, indemnification assets and tax benefits. ASC 805 also provides for a substantial number of new disclosure requirements. ASC 805 also contains guidance that was formerly issued as FSP FAS 141(R)-1, Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies which was intended to provide additional guidance clarifying application issues regarding initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets and liabilities arising from contingencies in a business combination. ASC 805 was effective for business combinations initiated on or after the first annual reporting period beginning after December 15, 2008. The Company implemented this guidance effective January 1, 2009. Implementing this guidance did not have an effect on the Company s financial position or results of operations; however it will likely have an impact on the Company s accounting for future business combinations, but the effect is dependent upon acquisitions, if any, that are made in the future.

ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 2. Summary of Significant Accounting Policies (Continued)**

*(t) Recently implemented standards (Continued)*

ASC 810, Consolidation ( ASC 810 ) includes new guidance issued by the FASB in December 2007 governing the accounting for and reporting of noncontrolling interests (previously referred to as minority interests). This guidance established reporting requirements which include, among other things, that noncontrolling interests be reflected as a separate component of equity, not as a liability. It also requires that the interests of the parent and the noncontrolling interest be clearly identifiable. Additionally, increases and decreases in a parent's ownership interest that leave control intact shall be reflected as equity transactions, rather than step acquisitions or dilution gains or losses. This guidance also requires changes to the presentation of information in the financial statements and provides for additional disclosure requirements. ASC 810 was effective for fiscal years beginning on or after December 15, 2008. The Company implemented this guidance as of January 1, 2010 and made all necessary changes accordingly including but not limited to filing amendments for the prior relevant periods to comply with all applicable requirements.

ASC 825, Financial Instruments ( ASC 825 ) includes guidance which was issued in February 2007 by the FASB and was previously included under Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115. The related sections within ASC 825 permit a company to choose, at specified election dates, to measure at fair value certain eligible financial assets and liabilities that are not currently required to be measured at fair value. The specified election dates include, but are not limited to, the date when an entity first recognizes the item, when an entity enters into a firm commitment or when changes in the financial instrument causes it to no longer qualify for fair value accounting under a different accounting standard. An entity may elect the fair value option for eligible items that exist at the effective date. At that date, the difference between the carrying amounts and the fair values of eligible items for which the fair value option is elected should be recognized as a cumulative effect adjustment to the opening balance of retained earnings. The fair value option may be elected for each entire financial instrument, but need not be applied to all similar instruments. Once the fair value option has been elected, it is irrevocable. Unrealized gains and losses on items for which the fair value option has been elected will be reported in earnings. This guidance was effective as of the beginning of fiscal years that began after November 15, 2007. The Company does not have eligible financial assets and liabilities, and, accordingly, the implementation of ASC 825 did not have an effect on the Company's results of operations or financial position.

ASC 820, Fair Value Measurements and Disclosures ( ASC 820 ) (formerly included under Statement of Financial Accounting Standards No. 157, Fair Value Measurements) includes guidance that was issued by the FASB in September 2006 that created a common definition of fair value to be used throughout generally accepted accounting principles. ASC 820 applies whenever other standards require or permit assets or liabilities to be measured at fair value, with certain exceptions. This guidance established a hierarchy for determining fair value which emphasizes the use of observable market data whenever available. It also required expanded disclosures which include the extent to which assets and liabilities are measured at fair value, the methods and assumptions used to measure fair value and the effect of fair value measures on earnings. ASC 820 also provides additional guidance for estimating fair value when the volume and level of activity for the asset or liability have significantly decreased. The emphasis of ASC 820 is that fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between willing market participants, under current market conditions. ASC 820 also further clarifies the guidance to be considered when determining whether or not a transaction is orderly and clarifies the valuation of securities in markets that are not active. This guidance includes information related to a company's use of judgment, in addition to market information, in certain circumstances to value assets which have inactive markets.



ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 2. Summary of Significant Accounting Policies (Continued)**

*(t) Recently implemented standards (Continued)*

Fair value guidance in ASC 820 was initially effective for fiscal years beginning after November 15, 2007 and for interim periods within those fiscal years for financial assets and liabilities. The effective date of ASC 820 for all non-recurring fair value measurements of nonfinancial assets and nonfinancial liabilities was fiscal years beginning after November 15, 2008. Guidance related to fair value measurements in an inactive market was effective in October 2008 and guidance related to orderly transactions under current market conditions was effective for interim and annual reporting periods ending after June 15, 2009.

The Company applied the provisions of ASC 820 to its financial assets and liabilities upon adoption at January 1, 2008 and adopted the remaining provisions relating to certain nonfinancial assets and liabilities on January 1, 2009. The difference between the carrying amounts and fair values of those financial instruments held upon initial adoption, on January 1, 2008, was recognized as a cumulative effect adjustment to the opening balance of retained earnings and was not material to the Company's financial position or results of operations. The Company implemented the guidance related to orderly transactions under current market conditions as of April 1, 2009, which also was not material to the Company's financial position or results of operations.

In August 2009, the FASB issued ASC Update No. 2009-05, Fair Value Measurements and Disclosures (Topic 820): Measuring Liabilities at Fair Value (ASC Update No. 2009-05). This update amends ASC 820, Fair Value Measurements and Disclosures and provides further guidance on measuring the fair value of a liability. The guidance establishes the types of valuation techniques to be used to value a liability when a quoted market price in an active market for the identical liability is not available, such as the use of an identical or similar liability when traded as an asset. The guidance also further clarifies that a quoted price in an active market for the identical liability at the measurement date and the quoted price for the identical liability when traded as an asset in an active market when no adjustments to the quoted price of the asset are required are both Level 1 fair value measurements. If adjustments are required to be applied to the quoted price, it results in a level 2 or 3 fair value measurement. The guidance provided in the update is effective for the first reporting period (including interim periods) beginning after issuance. The Company does not expect that the implementation of ASC Update No. 2009-05 will have a material effect on its financial position or results of operations.

In September 2009, the FASB issued ASC Update No. 2009-12, Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent) (ASC Update No. 2009-12). This update sets forth guidance on using the net asset value per share provided by an investee to estimate the fair value of an alternative investment. Specifically, the update permits a reporting entity to measure the fair value of this type of investment on the basis of the net asset value per share of the investment (or its equivalent) if all or substantially all of the underlying investments used in the calculation of the net asset value is consistent with ASC 820. The update also requires additional disclosures by each major category of investment, including, but not limited to, fair value of underlying investments in the major category, significant investment strategies, redemption restrictions, and unfunded commitments related to investments in the major category. The amendments in this update are effective for interim and annual periods ending after December 15, 2009 with early application permitted. The Company does not expect that the implementation of ASC Update No. 2009-12 will have a material effect on its financial position or results of operations.

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 2. Summary of Significant Accounting Policies (Continued)***(t) Recently implemented standards (Continued)*

In June 2009, FASB issued Statement of Financial Accounting Standards No. 167, Amendments to FASB Interpretation No. 46(R) ( Statement No. 167 ). Statement No. 167 amends FASB Interpretation No. 46R, Consolidation of Variable Interest Entities an interpretation of ARB No. 51 ( FIN 46R ) to require an analysis to determine whether a company has a controlling financial interest in a variable interest entity. This analysis identifies the primary beneficiary of a variable interest entity as the enterprise that has a) the power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance and b) the obligation to absorb losses of the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity. The statement requires an ongoing assessment of whether a company is the primary beneficiary of a variable interest entity when the holders of the entity, as a group, lose power, through voting or similar rights, to direct the actions that most significantly affect the entity's economic performance. This statement also enhances disclosures about a company's involvement in variable interest entities. Statement No. 167 is effective as of the beginning of the first annual reporting period that begins after November 15, 2009. Although Statement No. 167 has not been incorporated into the Codification, in accordance with ASC 105, the standard shall remain authoritative until it is integrated. The Company is in the process of evaluating Statement No. 167 and will make necessary changes if required.

**NOTE 3. Inventories**

Inventories consisted of the following at June 30, 2010 and December 31, 2009:

	<u>June 30, 2010</u>	<u>December 31, 2009</u>
Finished goods	\$ 5,232,246	\$ 6,395,249
Less allowance for excess and obsolete inventory	(64,102)	(347,133)
Inventories, net	<u>\$ 5,168,144</u>	<u>\$ 6,048,116</u>

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 4. Property and Equipment, net**

Property and equipment, net consisted of the following at June 30, 2010 and December 31, 2009:

	<u>June 30, 2010</u>	<u>December 31, 2009</u>
Land and Buildings	\$ 7,663,340	\$ 7,663,340
Furniture and fixtures	29,454	13,273
Office equipment	189,855	168,181
Leasehold improvements	314,616	218,462
Automobiles	540,900	449,713
Machinery	499,614	499,614
	<u>                    </u>	<u>                    </u>
Total property and equipment	9,237,779	9,012,583
Less accumulated depreciation and amortization	(976,647)	(832,818)
	<u>                    </u>	<u>                    </u>
Property and equipment, net	8,261,132	8,179,765
	<u>                    </u>	<u>                    </u>

Depreciation and amortization expense totaled \$82,539 and \$67,030 for the three months ended June 30, 2010 and 2009, respectively, and \$154,837 and \$142,019 for the six months ended June 30, 2010 and 2009, respectively.

Automobiles and machinery include the following amounts under capital leases:

	<u>June 30, 2010</u>	<u>December 31, 2009</u>
Cost	\$ 812,887	\$ 716,855
Less accumulated depreciation	(166,207)	(106,393)
	<u>                    </u>	<u>                    </u>
Total	646,680	610,462
	<u>                    </u>	<u>                    </u>

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 5. Capital Lease Obligation**

The Company leases automobiles and machinery under seven capital leases that expire between August 2010 and August 2013. Aggregate future obligations under the capital leases in effect as of June 30, 2010 are as follows:

	<u>Capital Lease</u>
Year ending June 30,	
2010	320,107
2011	43,017
2012	36,832
	<hr/>
Total minimum lease obligations	399,956
Less amounts representing interest	(27,656)
	<hr/>
Present value of future minimum lease payments	372,300
Less current portion of capital lease obligation	(298,434)
	<hr/>
Capital lease obligation, less current portion	73,866
	<hr/>

Interest expense related to capital leases totaled \$6,496, \$1,396, 14,972 and \$3,810 for the three months ended June 30, 2010 and 2009, and for six months ended June 30, 2010 and 2009, respectively.

**NOTE 6. Stock Options**

On March 31, 2006, the Board of Directors adopted the 2006 Equity Incentive Stock Plan (the "Plan") and the majority stockholder approved the Plan by written consent. The purpose of the Plan is to provide additional incentive to employees, directors and consultants and to promote the success of the Company's business. The Plan permits the Company to grant both incentive stock options ( "Incentive Stock Options" or "ISOs") within the meaning of Section 422 of the Internal Revenue Code (the "Code"), and other options which do not qualify as Incentive Stock Options (the "Non-Qualified Options") and stock awards.

Unless earlier terminated by the Board of Directors, the Plan (but not outstanding options) terminates on March 31, 2016, after which no further awards may be granted under the Plan. The Plan is administered by the full Board of Directors or, at the Board of Directors' discretion, by a committee of the Board of Directors consisting of at least two persons who are "disinterested persons" defined under Rule 16b-2(c)(ii) under the Securities Exchange Act of 1934, as amended (the "Committee").

Recipients of options under the Plan ( "Optionees") are selected by the Board of Directors or the Committee. The Board of Directors or Committee determines the terms of each option grant, including (1) the purchase price of shares subject to options, (2) the dates on which options become exercisable and (3) the expiration date of each option (which may not exceed ten years from the date of grant). The minimum per share purchase price of options granted under the Plan for Incentive Stock Options and Non-Qualified Options is the fair market value (as defined in the Plan) on the date the option is granted.

Optionees will have no voting, dividend or other rights as stockholders with respect to shares of Common Stock covered by options prior to becoming the holders of record of such shares. The purchase price upon the exercise of options may be paid in cash, by certified bank or cashier's check, by tendering stock held by the Optionee, as well as by cashless exercise either through the surrender of other shares subject to the option or through a broker. The total number of shares of Common Stock available under the Plan, and the number of shares and per share exercise price under outstanding options will be appropriately adjusted in the event of any stock dividend, reorganization, merger or recapitalization or similar corporate event.



ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 6. Stock Options (Continued)**

The Board of Directors may at any time terminate the Plan or from time to time make such modifications or amendments to the Plan as it may deem advisable and the Board of Directors or Committee may adjust, reduce, cancel and regrant an unexercised option if the fair market value declines below the exercise price except as may be required by any national stock exchange or national market association on which the Common Stock is then listed. In no event may the Board of Directors, without the approval of stockholders, amend the Plan if required by any federal, state, local or foreign laws or regulations or any stock exchange or quotation system on which the Common Stock is listed or quoted and the applicable laws of any other country or jurisdiction where options or stock purchase rights are granted under the Plan.

Subject to limitations set forth in the Plan, the terms of option agreements will be determined by the Board of Directors or Committee, and need not be uniform among Optionees.

As of June 30, 2010, there were no options outstanding under the Plan.

**NOTE 7. Related Party Transactions**

Related party receivables are payable on demand upon the same terms as receivables from unrelated parties.

**Transactions with Aristo Technologies Limited / Mr. Yang**

As of June 30, 2010 and December 31, 2009, we had an outstanding receivable from Mr. Yang, the President and Chairman of our Board of Directors, totaling \$11,238,556 and \$11,233,839, respectively. These advances bear no interest and are payable on demand. The receivable due from Mr. Yang to the Company is derived from the consolidation of the financial statements of Aristo, a variable interest entity, with the Company. A repayment plan has been entered with Mr. Yang.

For the three months ended June 30, 2010 and 2009, we recorded compensation to Mr. Yang of \$290,000 and \$434,615 respectively, and paid \$290,000 and \$434,615 respectively to Mr. Yang as compensation to him.

For the six months ended June 30, 2010 and 2009, we recorded compensation to Mr. Yang of \$606,667 and \$900,000 respectively, and paid \$606,667 and \$900,000 respectively to Mr. Yang as compensation to him.

**Transactions with Solution Semiconductor (China) Limited**

Mr. Yang is a director and the sole beneficial owner of the equity interests of Solution Semiconductor (China) Ltd. ( Solution ). On April 1, 2009, we entered into a lease agreement with Solution pursuant to which we lease one facility. The lease agreement for this facility expires on March 31, 2012. The monthly lease payment for this lease is \$1,090. We incurred and paid an aggregate rent expense of \$3,270 to Solution during the three months ended June 30, 2010 and 2009, respectively, and \$6,540 for the six months ended June 30, 2010 and 2009, respectively.

During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we purchased inventories of \$0, \$0, 43,213 and \$0 respectively from Solution. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts payable to Solution.

Two facilities located in Hong Kong owned by Solution were used by the Company as collateral for loans from DBS Bank (Hong Kong) Limited ( DBS Bank ) (formerly Overseas Trust Bank Limited) and The Bank of East Asia, Limited ( BEA Bank ) respectively.

ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 7. Related Party Transactions (Continued)**

**Transactions with Systematic Information Limited**

Mr. Yang, the Company's Chief Executive Officer, majority shareholder and a director, is a director and shareholder of Systematic Information Ltd. ( Systematic Information ) with a total of 100% interest. On September 1, 2008, we entered into a lease agreement with Systematic Information pursuant to which we lease one facility. The lease agreement for this facility expires on August 31, 2010. The monthly lease payment for this lease totals \$641. We incurred and paid an aggregate rent expense of \$1,923 to Systematic Information during the three months ended June 30, 2010 and 2009, respectively, and \$3,846 for the six months ended June 30, 2010.

During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we received a management fee of \$2,038, \$1,359, \$4,076 and \$1,359 respectively from Systematic Information. The management fee was charged for back office support for Systematic Information.

During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we sold products for \$0, \$121,263, 767,981 and \$121,263 respectively, to Systematic Information. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts receivables from Systematic Information.

During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we purchased inventories of \$0, \$74,688, \$0, and \$74,688 respectively from Systematic Information. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts payable to Systematic Information.

A workshop located in Hong Kong owned by Systematic Information was used by the Company as collateral for loans from BEA Bank.

**Transactions with Global Mega Development Limited**

Mr. Yang is the sole beneficial owner of the equity interests of Global Mega Development Ltd. ( Global ). During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we sold products for \$1,839, \$0, \$5,419 and \$0 respectively, to Global. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts receivables from Global.

**Transactions with Systematic Semiconductor Limited**

Mr. Yang is a director and sole beneficial owner of the equity interests of Systematic Semiconductor Ltd. ( Systematic ). During the three months ended June 30, 2010 and 2009, and the six months ended June 30, June 2010 and 2009, we received a management fee of \$1923, \$1,923, \$3,846 and \$5,769 respectively from Systematic. The management fee was charged for back office support for Systematic.

During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we sold products for \$0, \$1,770, \$0 and \$19,914 respectively, to Systematic. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts receivables from Systematic.

**Transactions with Atlantic Storage Devices Limited**

Mr. Yang is a director and 40% shareholder of Atlantic Storage Devices Ltd. ( Atlantic Storage ). During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we sold products for \$4,780, \$128,227, \$5,220 and \$283,012 respectively, to Atlantic Storage. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts receivables from Atlantic Storage.

ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 7. Related Party Transactions (Continued)**

**Transactions with Aristo Components Limited**

Mr. Ben Wong resigned from his director position with the Company effective on June 1, 2010. He is a 90% shareholder of Aristo Components Ltd. ( Aristo Comp ). During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we received a management fee of \$3,077, \$3,077, \$6,154 and \$5,769 respectively from Aristo Comp. The management fee was charged for back office support for Aristo Comp.

During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we sold products for \$0, \$0, \$0 and \$12,060 respectively, to Aristo Comp. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts receivables from Aristo Comp.

During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we purchased inventories of \$0, \$0, \$0 and \$241,325 respectively from Aristo Comp. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts payable to Aristo Comp.

**Transactions with Rambo Technologies Limited**

Mr. Ben Wong resigned from his director position with the Company effective on June 1, 2010. He is a director and 60% shareholder of Rambo Technologies Ltd. ( Rambo ). During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we sold products for \$0, \$29,580, \$9,878 and \$39,750 respectively, to Rambo. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts receivables from Rambo. After the date of his resignation, all companies under his personal control will no longer be a related party and will not enjoy privileged treatment and will be subject to the same trading terms as other ordinary outside parties.

During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we purchased inventories of \$0, \$0, \$0 and \$54,930 respectively, from Rambo. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts payable to Rambo. After the date of his resignation, all companies under his personal control will no longer be a related party and will not enjoy privileged treatment and will be subject to the same trading terms as other ordinary outside parties.



ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 7. Related Party Transactions (Continued)**  
**Transactions with Usmart Electronic Products Limited**

Mr. Ben Wong, resigned from his director position with the Company effective on June 1, 2010. He is a director and sole beneficial owner of the equity interests of Usmart Electronic Products Ltd. ( Usmart ). After the date of his resignation, all companies under his personal control will no longer be a related party and will not enjoy privileged treatment and will be subject to the same trading terms as other ordinary outside parties. Prior to April 1, 2010, Mr. Yang, our Chief Executive Officer, was the sole beneficial owner of equity interests in Usmart before transferring these ownership interests to Mr. Ben Wong.

On October 7, 2009, we entered into a leasing payment agreement with Usmart pursuant to which we lease one lot machinery facility to Usmart. The leasing payment agreement for this facility expires on September 16, 2011. The monthly lease income for this lease totals \$3,846. We received aggregate lease income of \$11,538, \$0, \$23,076 and \$0 from Usmart during the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, respectively.

During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we sold products for \$115, \$0, \$132 and \$0 respectively, to Usmart. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts receivables from Usmart.

During the three months ended June 30 and 2009, and the six months ended June 30, 2010 and 2009, we purchased inventories of \$38, \$19,013, \$1,743 and \$19,143 respectively, from Usmart. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts payable to Usmart.

**Transactions with Kasontech Electronics Limited**

Mr. Kenneth Lap-Yin Chan, the Company's Director and Chief Operating Officer, is a 33% shareholder of Kasontech Electronics Limited ( Kasontech ). During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we received a management fee of \$3,846, \$0, \$5,128 and \$0 respectively from Kasontech. The management fee was charged for back office support for Kasontech. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts receivables from Kasontech.

**Transactions with Ibcem Electronics (HK) Limited**

Mr. Ben Wong resigned from his director position with the Company effective on June 1, 2010. He is a director and 50% shareholder of Ibcem Electronics (HK) Limited ( Ibcem ). During the three months ended June 30, 2010 and 2009, and the six months ended June 30, 2010 and 2009, we sold products for \$2,112,781, \$0, \$2,772,320 and \$0 respectively, to Ibcem. As of June 30, 2010 and December 31, 2009, there were no outstanding accounts receivables from Ibcem. After the date of his resignation, all companies under his personal control will no longer be a related party and will not enjoy privileged treatment and will be subject to the same trading terms as other ordinary outside parties.

**Transactions with City Royal Limited**

Mr. Yang is a 50% shareholder of City Royal Limited ( City ). The remaining 50% of City is owned by the wife of Mr. Yang. A residential property located in Hong Kong owned by City was used by the Company as collateral for loans from DBS Bank.

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 8. Bank Facilities**

With respect to all of the debt and credit arrangements referred to in this Note 8 and Note 9, the Company pledged its assets to a bank group in Hong Kong comprised of DBS Bank, BEA and Standard Chartered Bank, as collateral for all current and future borrowings from the bank group by the Company. In addition to the above pledged collateral, the debt is also secured by:

1. a fixed cash deposit of \$705,641 (HK\$5,504,000), a security interest on two residential properties and a workshop located in Hong Kong owned by Atlantic, a wholly owned subsidiary of ACL, a security interest on a residential property located in Hong Kong owned by City, a related party, a workshop located in Hong Kong owned by Solution, a related party, plus a personal guarantee by Mr. Yang as collateral for loans from DBS Bank;
2. a fixed cash deposit of \$1,382,733 (HK\$10,785,318), a workshop located in Hong Kong owned by Systematic Information, a related party, a workshop located in Hong Kong owned by Solution, a related party, plus an unlimited personal guarantee by Mr. Yang as collateral for loans from BEA;
3. an unlimited personal guarantee by Mr. Yang as collateral for loans from Standard Chartered Bank;
4. a security interest on residential properties located in Hong Kong owned by Aristo, a wholly owned company by Mr. Yang plus a personal guarantee by Mr. Yang as collateral for loans from Fubon.

The summary of banking facilities at June 30, 2010 is as follows:

	<u>Granted facilities</u>	<u>Utilized facilities</u>	<u>Not Utilized Facilities</u>
Lines of credit and loan facilities			
Factoring Loan	\$ 8,846,154	\$ 4,948,821	3,897,333
Import/Export Loan	8,205,128	7,696,723	508,405
	<u>17,051,282</u>	<u>12,645,544</u>	<u>4,405,738</u>
Term Loan - short term	69,979(a)	69,979	
Instalment/Term Loan - long term	2,908,795(b)	2,908,795	
Overdraft	602,564(c)	571,408	31,156
Letter of Guarantee	384,615(d)	384,615	
	<u>\$ 21,017,236</u>	<u>\$ 16,580,341</u>	<u>\$ 4,436,895</u>

(a) Loan repayment within one year, including on other current liabilities

(b) Per summary of Note (9)

(c) Including on cash and cash equivalents

(d) Guarantee granted to supplier

With the exception of the \$384,615 letter of guarantee issued by DBS Bank, which will expire on 31 October, 2010, amounts borrowed by the Company under the revolving lines of credit described above are repayable within a period of three (3) months of drawdown. Other loan facilities repayable are referred to in Note 9 Long Term Debt.

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 9. Long Term Debt**

Long Term Debt consisted of the following at June 30, 2010 and December 31, 2009:

	<u>June 30, 2010</u>	<u>December 31, 2009</u>
Installment loan having a maturity date in July 2026 and carrying an interest rate of 2.4% below the Hong Kong dollar Prime Rate (5.25% at June 30, 2010 and December 31, 2009) to DBS Bank. The monthly installments are approximately \$9,925 including interest through 2010 without any balloon payment Requirements	\$ 1,534,891	\$ 1,572,720
Installment loan having a maturity date in July 2011 and carrying an interest rate of 2% below the Hong Kong dollar Prime Rate (5.25% at June 30, 2010 and December 31, 2009) to DBS Bank payable in monthly installments of \$3,782 including interest through 2010 without any balloon payment requirements	48,244	69,949
Installment loan having a maturity date in July 2023 and carrying an interest rate of 2.5% below the Hong Kong dollar Prime Rate (5.25% at June 30, 2010 and December 31, 2009) to DBS Bank payable in monthly installments of \$5,240 including interest through 2010 without any balloon payment requirements	697,455	719,156
Term loan having a maturity date in July 2014 and carrying an interest rate of 0.25% plus the Hong Kong dollar Prime Rate (5.25% at June 30, 2010 and December 31, 2009) to BEA Bank payable in monthly installments of \$15,758 including interest through 2010 without any balloon payment requirements	628,205	705,128
	<u>2,908,795</u>	<u>3,066,953</u>
Less: current maturities	<u>(319,530)</u>	<u>(318,972)</u>
	\$ 2,589,265	\$ 2,747,981

An analysis of long-term debt as of June 30, 2010 and December 31, 2009 is as follows:

	<u>June 30, 2010</u>	<u>December 31, 2009</u>
Current portion	\$ 319,530	\$ 318,972
After 1 year, but within 2 years	564,085	586,013
After 2 years, but within 5 years	433,708	508,050
After 5 years	1,591,472	1,653,918
	<u>2,589,265</u>	<u>2,747,981</u>
	<u>\$ 2,908,795</u>	<u>\$ 3,066,953</u>

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Notes to the Condensed Consolidated Financial Statements (Unaudited)

**NOTE 10. Cash Flow Information**

Cash paid during the six months ended June 30, 2010 and 2009 is as follows:

	Six months ended	
	June 30, 2010	June 30, 2009 (Restated)
	<u>                    </u>	<u>                    </u>
Interest paid	\$ 205,869	\$ 282,810
	<u>                    </u>	<u>                    </u>
Income tax paid	\$ 28,337	\$
	<u>                    </u>	<u>                    </u>
<b>Non-Cash Activities:</b>		
Capital lease obligations incurred when capital leases were entered for new automobiles	\$ 122,213	\$ 32,788
	<u>                    </u>	<u>                    </u>
Income tax provision	\$ 384,271	\$ 397,436
	<u>                    </u>	<u>                    </u>

**NOTE 11. Fair Value of Financial Instruments**

Fair value measurements are determined under a three-level hierarchy for fair value measurements that prioritizes the inputs to valuation techniques used to measure fair value, distinguishing between market participant assumptions developed based on market data obtained from sources independent of the reporting entity ( observable inputs ) and the reporting entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances ( unobservable inputs ).

Fair value is the price that would be received to sell an asset or would be paid to transfer a liability (i.e., the exit price ) in an orderly transaction between market participants at the measurement date. In determining fair value, we primarily use prices and other relevant information generated by market transactions involving identical or comparable assets ( market approach ). We also consider the impact of a significant decrease in volume and level of activity for an asset or liability when compared with normal activity to identify transactions that are not orderly.

The highest priority is given to unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). Securities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

The three hierarchy levels are defined as follows:

Level 1 - Quoted prices in active markets those are unadjusted and accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2 - Quoted prices for identical assets and liabilities in markets that are not active, quoted prices for similar assets and liabilities in active markets or financial instruments for which significant inputs are observable, either directly or indirectly;

Level 3 - Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable.

## ACL SEMICONDUCTORS INC. AND SUBSIDIARIES

## Notes to the Condensed Consolidated Financial Statements (Unaudited)

Credit risk adjustments are applied to reflect the company's own credit risk when valuing all liabilities measured at fair value. The methodology is consistent with that applied in developing counterparty credit risk adjustments, but incorporates the company's own credit risk as observed in the credit default swap market.

The following table presents the Company's assets and liabilities that are measured at fair value on a recurring basis at June 30, 2010:

	Level 1	Level 2	Level 3	Total
	<u>                    </u>	<u>                    </u>	<u>                    </u>	<u>                    </u>
Cash and cash equivalents	2,986,215			2,986,215
Restricted cash	2,088,374			2,088,374
	<u>                    </u>	<u>                    </u>	<u>                    </u>	<u>                    </u>
Total assets	\$ 5,074,589	\$	\$	\$ 5,074,589
	<u>                    </u>	<u>                    </u>	<u>                    </u>	<u>                    </u>

**NOTE 12. Derivative instruments**

As of June 30, 2010, the Company does not have any outstanding foreign currency exchange agreements. All foreign currency exchange agreements have been matured before April 1, 2010.

**NOTE 13. Subsequent Events**

In preparing these financial statements, the Company evaluated the events and transactions that occurred from July 1, 2010 through August 15, 2010, the date these financial statements were issued. The Company has made the required additional disclosures in reporting periods in which subsequent events occur.

None

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

*The following discussion highlights the principal factors that have affected our financial condition and results of operations as well as our liquidity and capital resources for the periods described.*

*The information contained in this Form 10-Q is intended to update the information contained in our annual report on Form 10-K for the year ended December 31, 2009, as amended, (the "Form 10-K"), filed with the Securities and Exchange Commission, and presumes that readers have access to, and will have read, the Management's Discussion and Analysis of Financial Condition and Results of Operation, our consolidated financial statements and the notes thereto, and other information contained in the Form 10-K. The following discussion and analysis also should be read together with our condensed consolidated financial statements and the notes to the condensed consolidated financial statements and the notes thereto included elsewhere in this Form 10-Q.*

**Forward-Looking Statements**

*Information included in this Form 10-Q may contain forward-looking statements. Except for the historical information contained in this discussion of the business and the discussion and analysis of financial condition and results of operations, the matters discussed herein are forward looking statements. These forward looking statements include but are not limited to the Company's plans for sales growth and expectations of gross margin, expenses, new product introduction, and the Company's liquidity and capital needs. This information may involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from future results, performance or achievements expressed or implied by any forward-looking statements. Forward-looking statements, which involve assumptions and describe our future plans, strategies and expectations, are generally identifiable by use of the words may, will, should, expect, anticipate, estimate, believe, intend or project or the negative of these words or other variations on these words or comparable terminology. In addition to the risks and uncertainties described in Risk Factors contained in the Form 10-K, these risks and uncertainties may include consumer trends, business cycles, scientific developments, changes in governmental policy and regulation, currency fluctuations, economic trends in the United States and inflation. Forward-looking statements are based on assumptions that may be incorrect, and there can be no assurance that any projections or other expectations included in any forward-looking statements will come to pass. Our actual results could differ materially from those expressed or implied by the forward-looking statements as a result of various factors. Except as required by applicable laws, we undertake no obligation to update publicly any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.*

**Company Overview and Background**

The Company, through its wholly-owned subsidiary Atlantic Components Limited, a Hong Kong corporation ("Atlantic"), is engaged primarily in the business of distribution of memory products under Samsung brand name which principally comprise DRAM, Graphic RAM and Flash for the Hong Kong and Southern China markets. Our wholly-owned subsidiary, Alpha Perform Technology Limited ("Alpha"), which previously engaged in this business, ceased activities as of January 1, 2004, and all its operations were consolidated with those of Atlantic.

Aristo is engaged in the marketing, selling and servicing of computer products and accessories including semiconductors, LCD products, mass storage devices, consumer electronics, computer peripherals and electronic components. In addition to Samsung-branded products, Aristo sells Hynix, Micron, Elpida, Qimonda, Lexar, Dane-Elec, Elixir, SanDisk and Winbond branded products.

As of June 30, 2010, ACL had more than 150 active customers in Hong Kong and Southern China.

ACL is in the mature stage of operations. As a result, the relationships between sales, cost of sales, and operating expenses reflected in the financial information included in this document to a large extent represent future expected financial relationships. Much of the cost of sales and operating expenses reflected in our financial statements are recurring in nature.

## Overview

### *Net sales*

Sales from Samsung HK are recognized upon the transfer of legal title of the electronic components to the customers. The quantities of memory products the Company sells fluctuate with changes in demand from its customers. The suggested prices set by Samsung HK that we charged our customers are subject to change by us based on prevailing economic conditions and their impact on the market.

Net sales for the three months ended June 30, 2010 ( second quarter of 2010 ) were \$89,532,290, 18.1% greater than net sales for the three months ended June 30, 2009. This increase in net sales was mainly due to increase of sales volume to the PRC market.

The gross profit for the second quarter of 2010 was \$1,931,270, decreased by 24.6% over the gross profit for the comparable period of the prior fiscal year. The gross profit margin for the second quarter of 2010 was 2.2%, compared to 3.4% for the corresponding quarter in 2009. The decrease in gross profit and gross profit margin were mainly due to decrease in average selling prices. As the memory production volume increases, and the economy status of United States and Europe have not yet recovered, most excess supplies were pushed to the China market causing the selling price to decrease. During the second quarter of 2010, we experienced decreased gross profit as a consequence of higher cost of sales as the market saturated. As supply continued to increase throughout 2010 to the point of market saturation, marginal costs increased resulting in increased cost of sales and corresponding reduction in gross profit margin.

The Company has enhanced and optimized its internal controls to minimize unnecessary costs. The Company recorded a decrease in operating expenses of 9.3% and a decrease of 4.5% of interest expense compare to the corresponding quarter in 2009.

We expect that the global market demand and average selling price will slowly pick up in the third quarter of 2010 as a result of market recovery. However, we cannot give assurance that this will occur.

### *Cost of sales*

Cost of sales consists of costs of goods purchased from Samsung, and purchases from other Samsung authorized distributors. Many factors affect our gross margin, including, but not limited to, the volume of production orders placed on behalf of its customers, the competitiveness of the memory products industry and the availability of cheaper Samsung memory products from overseas Samsung distributors due to regional demand and supply situations. Nevertheless, our procurement operations are supported by Samsung pursuant to a distributorship agreement between the Company and Samsung. Our cost of goods, as a percentage of total revenues, amounted to approximately 97.8% for the three months ended June 30, 2010 and approximately 96.6% for the three months ended June 30, 2009.

### *Operating expenses*

Our operating expenses for the three months ended June 30, 2010 and 2009 were comprised of sales and marketing and general and administrative expenses only.

Sales and marketing expenses consisted primarily of costs associated with advertising and marketing activities.

General and administrative expenses include all corporate and administrative functions that serve to support our current and future operations and provide an infrastructure to support future growth. Major items in this category include management and staff salaries, rent/leases, professional services, and travel and entertainment. We expect these expenses to increase as a result of increased legal and accounting fees anticipated in connection with our compliance with ongoing reporting and accounting requirements of the Securities and Exchange Commission and as a result of anticipated expansion by the Company of its business operations. Sales and marketing expenses are expected to fluctuate as a percentage of sales due to the addition of sales personnel and various marketing activities planned throughout the year.

Interest expense, including finance charges, relates primarily to the Company's short-term and long-term bank borrowings.

**Results of Operations**

	Three Months Ended		Six Months Ended	
	June 30, 2010	June 30, 2009 (Restated)	June 30, 2010	June 30, 2009 (Restated)
Net sales	\$ 89,532,290	\$ 75,827,062	\$ 188,543,352	\$ 138,327,201
Cost of sales	87,601,020	73,273,593	183,785,478	132,915,773
Gross profit	1,931,270	2,553,469	4,757,874	5,411,428
Operating expenses				
Selling	28,586	36,256	53,388	58,434
General and administrative	1,122,719	1,232,737	2,180,589	2,522,190
Income from operations	779,965	1,284,476	2,523,897	2,830,804
Other income (expenses)	(57,865)	(20,926)	(104,755)	(114,013)
Income before income taxes provision	722,100	1,263,550	2,419,142	2,716,791
Income taxes provision	128,205	179,487	384,271	397,436
Net Income	\$ 593,895	\$ 1,084,063	\$ 2,034,871	\$ 2,319,355
Earnings per share - basic and diluted	\$ 0.02	\$ 0.04	\$ 0.07	\$ 0.08



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Unaudited Comparisons for Three and Six Months ended June 30, 2010 to the Three and Six Months Ended June 30, 2009

*Net Sales*

The following table presents our net sales for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30, 2010	2009	% Change	Six Months Ended June 30, 2010	2009	% Change
\$ 89,532,290	\$ 75,827,062	18.1%	\$ 188,543,352	\$ 138,327,201	36.3%

Net sales increased by \$13,705,228 or 18.1%, from \$75,827,062 for the three months ended June 30, 2009 to \$89,532,290 in the three months ended June 30, 2010. For the six months ended June 30, 2010 net sales increased by \$50,216,151 or 36.3%, from \$138,327,201 in the six months ended June 30, 2009 to \$188,543,352. This increase in net sales was mainly due to increase of sales volume to the PRC market.

*Cost of sales*

The following table presents our cost of sales for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30, 2010	2009	% Change	Six Months Ended June 30, 2010	2009	% Change
\$ 87,601,020	\$ 73,273,593	19.6%	\$ 183,785,478	\$ 132,915,773	38.3%

Cost of sales increased by \$14,327,609, or 19.6%, from \$73,273,593 for the three months ended June 30, 2009 to \$87,601,020 for the three months ended June 30, 2010. For the six months ended June 30, 2010, cost of sales increased by \$50,869,705 or 38.3% as compared to the six months ended June 30, 2009. The increase was mainly due to increase of sales volume and higher cost of sales.

*Gross Profit*

The following table presents our gross profit for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30, 2010	2009	% Change	Six Months Ended June 30, 2010	2009	% Change
\$ 1,931,270	\$ 2,553,469	-24.4%	\$ 4,757,874	\$ 5,411,428	-12.1%

Gross profit decreased by \$622,199, or 24.4%, from \$2,553,469 for the three months ended June 30, 2009 to \$1,931,270 for the three months ended June 30, 2010. For the six months ended June 30, 2010, gross profit decreased by \$653,554 or 12.1% from \$5,411,428 for the six months ended June 30, 2009 to \$4,757,874. The decrease in gross profit was mainly due to decrease in average selling prices as the market is saturating.

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### *Sales and Marketing*

The following table presents the sales and marketing expenses for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30, 2010	2009	% Change	Six Months Ended June 30, 2010	2009	% Change
\$ 28,586	\$ 36,256	-21.2%	\$ 53,388	\$ 58,434	-8.6%

For the three months ended June 30, 2010, sales and marketing expenses decreased \$7,670, or 21.2%, as compared to the three months ended June 30, 2009. For the six months ended June 30, 2010, sales and marketing expenses decreased by \$5,046 or 8.6%, from \$58,434 for the six months ended June 30, 2009 to \$53,388. Such decrease was directly attributable to the decrease of transportation and insurance charges. Since the profit margin is relatively low, in order to maximize the Company's profit, the Company encouraged the customers to self pick up the goods to lower the sales and marketing expenses.

### *General and Administrative*

The following table presents the general and administrative expenses for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30, 2010	2009	% Change	Six Months Ended June 30, 2010	2009	% Change
\$ 1,122,719	\$ 1,232,737	-8.9%	\$ 2,180,589	\$ 2,522,190	-13.5%

For the three months ended June 30, 2010, general and administrative expenses decreased \$110,018, or 8.9%, as compared to the three months ended June 30, 2009. For the six months ended June 30, 2010, general and administrative expenses decreased \$341,601 or 13.5%, from \$2,522,190 in the six months ended June 30, 2009 to \$2,180,589. The decrease was principally attributable to a decrease in directors remuneration, staff salaries and bank charges.

### *Income from Operations*

The following table presents the income from operations for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30, 2010	2009	% Change	Six Months Ended June 30, 2010	2009	% Change
\$ 779,965	\$ 1,284,476	-39.3%	\$ 2,523,897	\$ 2,830,804	-10.8%

Income from operations for the three months ended June 30, 2010 decreased by \$504,511, or 39.3%, from \$1,284,476 for the three months ended June 30, 2009 to \$779,965 in the three months ended June 30, 2010. For the six months ended June 30, 2010 decreased by \$306,907 or 10.8%, income from operations was \$2,523,897 for the six month ended June 30, 2010 compare to \$2,830,804 for the six months ended June 30, 2009. Such decrease was mainly due to an increase in cost of sales offset by a decrease of general and administrative expenses.

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### *Interest Income*

The following table presents the interest income for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30, 2010	2009	% Change	Six Months Ended June 30, 2010	2009	% Change
\$ 192	\$ 2,312	-91.7%	\$ 285	\$ 31,022	-99.1%

For the three months ended June 30, 2010, interest income decreased \$2,120, or 91.7%, as compared to the three months ended June 30, 2009. For the six months ended June, 2010, increase income decrease \$30,737, or 99.1%, as compared to the six months ended June 30, 2009. The decrease was due to bank interest refunded by customers during the period in 2009.

### *Interest Expense*

The following table presents the interest expense for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30, 2010	2009	% Change	Six Months Ended June 30, 2010	2009	% Change
\$ 110,705	\$ 115,918	-4.5%	\$ 205,869	\$ 282,810	-27.2%

For the three months ended June 30, 2010, interest expense decreased by \$5,213 or 4.5%, from \$115,918 in the three months ended June 30, 2009 to \$110,705 in the three months ended June 30, 2010. For the six months ended June 30, 2010, interest expense decreased by \$76,941 or 27.2%, from 282,810 in the six months ended June 30, 2009 to \$205,869 in the six months ended June 30, 2010. These decreases were mainly due to a decrease in the use of letters of credit by the Company to obtain goods from suppliers.

### *Net Income on Cash Flow Hedge*

The following table presents the net income on cash flow hedge for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30, 2010	2009	% Change	Six Months Ended June 30, 2010	2009	% Change
\$	\$ 28,372	-100.0%	\$ 15,410	\$ 48,721	-68.4%

For the three months ended June 30, 2010, income on cash flow hedge decreased by \$28,372, or 100%, as compared to the three months ended June 30, 2009. For the six months ended June 30, 2010, net income on cash flow hedge decreased by \$33,311 or 68.4%, as compared to the six months ended June 30, 2009. The decreases were due to the expiration or termination of several currency hedging contracts in the first quarter of 2010 and all foreign currency exchange agreements have been matured before April 1, 2010.

*Income Tax Provision*

The following table presents the income tax provision for the three and six months ended June 30, 2010 and 2009, respectively:

Three Months Ended June 30,			Six Months Ended June 30,		
2010	2009	% Change	2010	2009	% Change
\$ 128,205	\$ 179,487	-28.6%	\$ 384,271	\$ 397,436	-3.3%

Income tax provision decreased by \$51,282 or 28.6% from \$179,487 for the three months ended June 30, 2009 to \$128,205 for the three months ended June 30, 2010. For the six months ended June 30, 2010, income tax provision decreased by \$13,165 or 3.3%, as compared to the six months ended June 30, 2009. The decreases were due to a decrease in the estimated Hong Kong taxes payable by Atlantic.

**Liquidity and Capital Resources**

Our principal sources of liquidity have been cash from operations, bank lines of credit and credit terms from suppliers. Our principal uses of cash have been for operations and working capital. We anticipate these uses will continue to be our principal uses of cash in the future.

As of June 30, 2010, we had revolving lines of credit and loan facilities in the aggregate amount of \$21,017,236, of which \$4,436,895 was available (representing an approximately 24.4% increase in our borrowing lines of credit from December 31, 2009), which was attributable to the increase of factoring loan. In connection therewith, \$996,613 of restricted bank deposits were released to the Company. Other detailed disclosures on credit facilities are made in Note 8 and Note 9 of the Condensed Consolidated Financial Statements for the quarter ended June 30, 2010, including the amounts of facilities, outstanding balances, maturity date, and pledges of assets.

Our ability to draw down under our various credit and loan facilities is, in each case, subject to the prior consent of the relevant lending institution to make advances at the time of the requested advance and each facility (other than with respect to certain long term mortgage loans) is payable within 90 days of drawdown. Accordingly, on a case by case basis, we may elect to terminate or not renew several of our credit facilities if significant reduction in our available short term borrowings that we do not deem it is commercially reasonable. The Company has obtained a \$20 million purchase credit from Samsung. The Company plans to obtain an additional \$30 million line of credit from various lenders.

We will continue to seek additional sources of available financing on acceptable terms; however, there can be no assurance that we will be able to obtain the necessary additional capital on a timely basis or on acceptable terms, if at all. In addition, if the results are negatively impacted and delayed as a result of political and economic factors beyond management's control, our capital requirements may increase.

The short-term borrowings from banks to finance the cash flow required to finance the purchase of Samsung memory products from Samsung HK must be made a day in advance of the release of goods from Samsung HK's warehouse before receiving payments from customers upon physical delivery of such goods in Hong Kong which, in most instances, take approximately two days from the date of such delivery.

The following factors, among others, could have negative impacts on our results of operations and financial position: the termination or change in terms of the Distributorship Agreement; pricing pressures in the industry; a continued downturn in the economy in general or in the memory products sector; an unexpected decrease in demand for Samsung's memory products; our ability to attract new customers; an increase in competition in the memory products market; and the ability of some of our customers to obtain financing.

Although we believe our expectations of future growth are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We are under no duty to update our expectations to conform them to actual results or to reflect changes in expectations.

*Net Cash Used for Operating Activities*

In the six months ended June 30, 2010, net cash used for operating activities was \$2,154,110 while in the six months ended June 30, 2009, net cash provided by operating activities was \$8,307,445, an increase in cash used of \$10,461,555. This increase was primarily due to an increase of accounts receivable and decrease of accounts payable as of June 30, 2010.

*Net Cash Used for Investing Activities*

For the six months ended June 30, 2010, net cash used for investing activities was \$120,886 while in the six months ended June 30, 2009, net cash provided by investing activities was \$77,035, an increase in cash used of \$197,921. This increase was primarily due to the decrease of amounts due from Aristo / Mr. Yang net of decrease of restricted cash as of June 30, 2010.

*Net Cash Provided by Financing Activities*

In the six months ended June 30, 2010, net cash provided by financing activities was \$3,259,407 while in the six months ended June 30, 2009, net cash used for financing activities was \$8,581,310 an increase of \$11,840,717. This increase was due to an increase in the balance of bank lines of credit and notes payable as of June 30, 2010.

**Principles of Consolidation**

The consolidated financial statements of ACL Semiconductors Inc. include the accounts of Atlantic Components Ltd., a Hong Kong subsidiary and Alpha Perform Technology Limited, a BVI subsidiary, and Aristo Technologies Ltd., a Hong Kong company, a variable interest entity deemed to be a subsidiary after consideration of ASC 810-10-05 and 810-10-25 on the fact that the Company is primary beneficiary of Aristo while Aristo relied on the Company to finance its operation; was consider to have de-facto principal and agent relationship; was controlled by the Company through the participation of Mr. Yang, a related party of both the Company and Aristo. All significant inter-company transactions and balances are eliminated in consolidation.

**Critical Accounting Polices**

The U.S. Securities and Exchange Commission ( SEC ) recently issued Financial Reporting Release No. 60, *Cautionary Advice Regarding Disclosure About Critical Accounting Policies* ( FRR 60 ), suggesting companies provide additional disclosure and commentary on their most critical accounting policies. In FRR 60, the SEC defined the most critical accounting policies as the ones that are most important to the portrayal of a company's financial condition and operating results, and require management to make its most difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Based on this definition, our most critical accounting policies include: inventory valuation, which affects cost of sales and gross margin; policies for revenue recognition, allowance for doubtful accounts, and stock-based compensation. The methods, estimates and judgments we use in applying these most critical accounting policies have a significant impact on the results we report in our consolidated financial statements.

*Inventory Valuation*

Our policy is to value inventories at the lower of cost or market on a part-by-part basis. In addition, we write down unproven, excess and obsolete inventories to net realizable value. This policy requires us to make a number of estimates and assumptions including market and economic conditions, product lifecycles and forecast demand for our product to value our inventory. To the extent actual results differ from these estimates and assumptions, the balances of reported inventory and cost of products sold will change accordingly.

*Allowance for Doubtful Accounts.*

We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. Our allowance for doubtful accounts is based on our assessment of the collectability of specific customer accounts, the aging of accounts receivable, our history of bad debts, and the general condition of the industry. If a major customer's credit worthiness deteriorates, or our customers' actual defaults exceed our historical experience, ACL's estimates could change and impact our reported results.

**New Accounting Pronouncements**

ASC 105, Generally Accepted Accounting Principles ( ASC 105 ) (formerly Statement of Financial Accounting Standards No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB Statement No. 162) reorganized by topic existing accounting and reporting guidance issued by the Financial Accounting Standards Board ( FASB ) into a single source of authoritative generally accepted accounting principles ( GAAP ) to be applied by nongovernmental entities. All guidance contained in the Accounting Standards Codification ( ASC ) carries an equal level of authority. Rules and interpretive releases of the Securities and Exchange Commission ( SEC ) under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. Accordingly, all other accounting literature will be deemed non-authoritative . ASC 105 is effective on a prospective basis for financial statements issued for interim and annual periods ending after September 15, 2009. We have implemented the guidance included in ASC 105 as of July 1, 2009. The implementation of this guidance changed our references to GAAP authoritative guidance but did not impact our financial position or results of operations.

ASC 805, Business Combinations ( ASC 805 ) (formerly included under Statement of Financial Accounting Standards No. 141 (revised 2007), Business Combinations) contains guidance that was issued by the FASB in December 2007. It requires the acquiring entity in a business combination to recognize all assets acquired and liabilities assumed in a transaction at the acquisition-date fair value, with certain exceptions. Additionally, the guidance requires changes to the accounting treatment of acquisition related items, including, among other items, transaction costs, contingent consideration, restructuring costs, indemnification assets and tax benefits. ASC 805 also provides for a substantial number of new disclosure requirements. ASC 805 also contains guidance that was formerly issued as FSP FAS 141(R)-1, Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies which was intended to provide additional guidance clarifying application issues regarding initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets and liabilities arising from contingencies in a business combination. ASC 805 was effective for business combinations initiated on or after the first annual reporting period beginning after December 15, 2008. We implemented this guidance effective January 1, 2009. Implementing this guidance did not have an effect on our financial position or results of operations; however it will likely have an impact on our accounting for future business combinations, but the effect is dependent upon acquisitions, if any, that are made in the future.

ASC 810, Consolidation ( ASC 810 ) includes new guidance issued by the FASB in December 2007 governing the accounting for and reporting of noncontrolling interests (previously referred to as minority interests). This guidance established reporting requirements which include, among other things, that noncontrolling interests be reflected as a separate component of equity, not as a liability. It also requires that the interests of the parent and the noncontrolling interest be clearly identifiable. Additionally, increases and decreases in a parent s ownership interest that leave control intact shall be reflected as equity transactions, rather than step acquisitions or dilution gains or losses. This guidance also requires changes to the presentation of information in the financial statements and provides for additional disclosure requirements. ASC 810 was effective for fiscal years beginning on or after December 15, 2008. We implemented this guidance as of January 1, 2010 and made all necessary changes accordingly including but not limited to file amendment for the prior relevant periods to comply with all applicable requirements.

**ITEM 3. Quantitative and Qualitative Disclosures about Market Risk**

We are a smaller reporting company as defined by Rule 12b-2 of the Exchange Act and are not required to provide the information required under this item

**ITEM 4T. Controls and Procedures**

**(a) Disclosure Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Securities Exchange Act of 1934, as amended (the Exchange Act), is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission (SEC) rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), as appropriate, to allow timely decisions regarding required disclosure.

Limitations on the Effectiveness of Disclosure Controls. In designing and evaluating the Company's disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, Company management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Evaluation of Disclosure Controls and Procedures. The Company's CEO and CFO have evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) as of June 30, 2010, and based on this evaluation, the Company's principal executive and financial officers have concluded that the Company's disclosure controls and procedures were not effective to ensure that material information is recorded, processed, summarized and reported by management of the Company on a timely basis in order to comply with the Company's disclosure obligations under the Exchange Act and the rules and regulations promulgated thereunder. The Company's principal executive and financial officers conclusion regarding the Company's disclosure controls and procedures is based on management's conclusion that the Company's internal control over financial reporting are ineffective based on their evaluation as described in the Company's annual report on Form 10-K for the fiscal year ended December 31, 2009.

**Changes in Internal Control over Financial Reporting**

There have been no changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended June 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**

None

**ITEM 1A. Risk Factors**

There are no material changes from the risk factors set forth in Part I, Item 1A, in our Annual Report on Form 10K 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**

Exhibits:

- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification by Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

**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.

ACL SEMICONDUCTORS INC.

Date: August 19, 2010

By: /s/Chung-Lun Yang

\_\_\_\_\_  
Chung-Lun Yang  
Chief Executive Officer

Date: August 19, 2010

By: /s/ Kun Lin Lee

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Kun Lin Lee  
Chief Financial Officer

38

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