



# GLAUCUS RESEARCH GROUP

Things gained through unjust fraud are never secure. — *Sophocles*

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COMPANY:

**L&L ENERGY, INC.** | NASDAQ: LLEN

INDUSTRY: Coal Mining and Production

Recommendation:

**Strong Sell**

Estimated Value:

**<\$1.00**

Per Share

Report Date:

**8.2.11**

Price:

**\$4.17**

As of Market Close 8/1/11

Float:

**23.41**

Million

Avg. 3 Mo. Volume:

**~467,000**

Shares/day

- SAIC reports show that a coal coking factory purportedly owned by LLEN is legally owned by Dickson Lee, CEO, founder and Chairman of the company and that he holds the entity in a sole proprietorship.
- Chinese government filings also show that the equity of a coal washing factory was not transferred to LLEN as the company has stated, but is still held in a sole proprietorship by a third party.
- LLEN has also failed to disclose significant minority shareholders in two major subsidiaries and certain material risks associated with its ownership of mining rights.
- LLEN's stunning margin profile and meteoric growth rate are the envy of its competitors, even other Chinese coal companies. This is remarkable because apparently three executives with respective backgrounds in finance, insurance sales/Chinese restaurants and career services for the elderly turned a fledgling firm into, adjusted for size, one of the most profitable and efficient coal mining companies in the world in just three years. In our opinion, this is not credible.
- SAIC filings suggest that the Company has been greatly exaggerating its net sales, net income and the value of its assets.
- As if to lend credence to our arguments, on July 29, 2011, LLEN's auditor gave an **adverse opinion** on the company's internal controls over financial reporting, stating that there is a reasonable possibility that a material misstatement of the company's financial statements will not be prevented or detected on a timely basis.
- LLEN's CEO and founder Dickson Lee boasts a checkered past. Five different regulators have charged Lee (acting through an agent or through LLEN) with securities violations on five separate occasions in connection with the sale of LLEN securities.
- LLEN has had five auditors in the last ten years, including Jaspers + Hall, PC, which resigned from LLEN when the PCAOB suspended the registration of its only two partners and barred them from auditing publicly listed companies for a minimum of five years.
- LLEN has only had a non-'acting' Chief Financial Officer (CFO) for an aggregate of four months in its history. Suspiciously, three of its past four CFOs have resigned after the end of the company's fiscal year but before the CFO would have had to sign off on the company's audited financial statements.

## Executive Summary

L&L Energy, Inc. (“LLEN” or the “company”) operates a coal mining, coal washing, coal coking and coal wholesaling business out of the remote Yunnan and Guizhou provinces in the People’s Republic of China (“China”). LLEN also maintains a corporate office in Seattle, Washington. Like many other Chinese companies that have been investigated and delisted by U.S. securities regulators for fraud, LLEN went public through a [reverse merger transaction](#) (“RTO”).

On paper, LLEN’s performance appears too good to be true. In three years, with little to no experience in operating a coal mine among its executive officers, LLEN has purportedly become one of the most profitable pound for pound coal mining companies in the world.

The adage goes that ‘things that are too good to be true usually are.’ We believe that LLEN is no different. According to publicly available SAIC filings obtained from China, LLEN has greatly exaggerated its net sales and the value of its assets. Apparently we were not the only ones questioning the authenticity of LLEN’s financials.

On July 29, 2011, LLEN’s auditor submitted a report to the board of directors of the company giving an **adverse opinion** on LLEN’s internal controls over financial reporting. For those who do not speak accounting, an adverse opinion from an **auditor** indicates that there is a reasonable possibility that a material misstatement of the company’s financial statements will not be prevented or detected on a timely basis.

In this report, we carve through the company’s SEC financial statements and highlight many suspicious features of the company’s ostensible record, including the fact that LLEN easily outperforms its competitors (including Chinese firms) despite its small size and despite the fact that its executive management team had little experience operating a coal mine prior to achieving such spectacular results.

We also present compelling evidence that contrary to claims in its SEC filings, the company does not legally own certain assets. Chinese filings indicate that corporate funds were used to acquire a coal coking factory that is currently held in a sole proprietorship under the sole ownership of LLEN’s CEO and chairman. We have also found evidence that LLEN has not properly disclosed the company’s ownership stake in other assets and subsidiaries.

In addition, we explore the trustworthiness of management. Five different regulators have charged LLEN’s CEO and chairman (acting through agents or the company) with securities violations in connection with the sale of LLEN securities. Further, LLEN has a troubled history of auditor and CFO turnover, casting further doubt on the credibility of its SEC financials.

## Company Assets Under the Chairman’s Personal Ownership

According to publicly available SAIC filings, Dickson Lee, the CEO, founder and Chairman of LLEN, is the sole owner of Zone Lin, a coal coking factory purportedly acquired by LLEN in the third quarter of 2009. Holding assets acquired with corporate funds in a sole proprietorship is at best a major violation of SEC disclosure rules and at worst textbook fraud.

On February 6, 2010, L&L Yunnan Tianneng Industry Co. Ltd. (“TNI”), a direct subsidiary of LLEN, purportedly [acquired 100%](#) of the equity of Luoping County Zone Lin Coal Coking Factory (“Zone Lin”), a sole proprietorship, from Lao Zhong Yang (“Lao Yang”) for \$2 million.

Below, we present an SAIC filing from June 2, 2010, showing that Zone Lin is a sole proprietorship and that Lao Yang is the registered owner of all of the outstanding equity interests of the firm. This in itself is problematic. LLEN [purported](#) to acquire “100% of the equity” of Zone Lin, yet even after the acquisition date, the business was still held in a sole proprietorship by a related party.

## 私营企业从业人员及经营状况统计表

(此表由私营企业填写)

企业名称: 罗平县忠林焦化厂 营业执照注册号: 530324100001586  
 企业类型: 个体独资企业 Sole Proprietorship 法定代表人(负责人): 杨老忠 Yang Lao Zhong

	项 目	编 号	人 数 (人)
	从业人员	1	135
人员 状况	1、下岗失业人员	2	0
	其中: 省外下岗失业人员	3	0
	2、残疾人	4	49
	3、云南省自谋职业的城镇退役士兵	5	1
	4、2003年应届普通高校毕业生	6	0
	5、两劳释放人员	7	0
	6、离退休人员	8	0
	7、退职人员	9	0
	8、其他(指上述7类人员以外的从业人员)	10	85
	合 计	11	135
文化 程度	1、研究生以上	12	0
	2、大学本科	13	1
	3、大专	14	4
	4、中专	15	3
	5、高中	16	20
	6、初中以下	17	107
	合 计	18	28
政治 面貌	1、党员	19	4
	2、团员	20	0
产值	(万元)	21	
全年利润总 额	(万元)	22	
全年净利润	(万元)	23	

填表人: 侯时林 (签字)

填表日期: 2010年6月2日

填表说明

- 1、编号1=11=18
- 2、编号 11=2+4+5+6+7+8+9+10 编号 18=12+13+14+15+16+17
- 3、此表“从业人员”指参加经营活动并领取报酬的所有从业人员
- 4、此表“产值”指以货币表现的农林牧渔业、采掘业、制造业、建筑业的生产量
- 5、“销售总额或营业收入”指交通运输仓储业、批发和零售贸易餐饮业、社会服务业及其他行业的销售总额或营业收入
- 6、此表“社会消费品零售额”指私营企业对城乡居民和社会集团的消费品零售额

June 2, 2010

This SAIC filing clearly shows that as of June 2, 2010, Lao Yang, not LLEN (or its subsidiary) was the sole owner of Zone Lin and held the business in a sole proprietorship.



Then things get even fishier. Below is a screenshot taken yesterday from the SAIC website showing that Dickson Lee, LLEN's founder, CEO and chairman (not LLEN or its subsidiaries) is the sole owner of the Zone Lin coal-coking business and that he holds the business in a sole proprietorship.



企业名称: 罗平县忠林焦化厂 Entity Name: Luo Ping County ZoneLin Coking  
 住所: 罗平县阿鲁乡清平绍村 Address: Luo Ping County A Lu Township Qing Ping Shao Village  
 负责人: DICKSON V .LEE Person In Charge: Dickson V. Lee  
 企业类型: 个人独资企业 Entity Type: Sole Proprietorship  
 经营范围: 焦煤生产 Business Scope: Coking Coal Production  
 成立日期: 2004-9-8 0:00:00 Date of Establishment: September 8, 2004  
 核准日期: 2008-5-15 0:00:00 Date of Approval: May 15 2008  
 经营期限起: 2008-5-15 0:00:00 Operation Period (Start): May 15, 2008  
 经营期限止: 2018-5-15 0:00:00 Operation Period (End): May 15, 2018  
 注册资本: 1500.0000 (万元) Paid-In Capital: 15 Million CNY  
 所属登记机关: 罗平县工商行政管理局 Registration Authority: Luo Ping County Administration of Industry & Commerce  
 企业登记状态: 正常 Entity Registration Condition: Normal

以上信息为 2008-5-15 企业登记注册信息,鉴于数据更新的周期性,上述信息仅供参考。若需查询企业最新详细信息,请与企业登记机关联系。

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We corroborated this screenshot with a second independent SAIC report. Put simply, the above SAIC screenshot shows that Lee deployed corporate funds to acquire an asset that he (not the company) now holds in a sole proprietorship. Holding assets acquired with corporate funds in a sole proprietorship is at best a material omission of a related party transaction from SEC financials and at worst textbook fraud.

# Who Legally Owns Hong Xing?

Local Chinese filings also reveal that LLEN does not legally own another important asset.

According to LLEN's SEC filings, the company purportedly acquired 100% of the equity of the Hong Xing coal washing facility ("Hong Xing") on November 30, 2009, through its subsidiary TNI.<sup>1</sup>

Based on our conversations with Chinese lawyers and accountants, it is our belief that under Chinese law, LLEN's subsidiary TNI, as a sino-foreign JV entity, would not be permitted to acquire Hong Xing as long as the entity remains a sole proprietorship. It is our understanding that under Chinese law, (a) the interests in a sole proprietorship may only be owned by a Chinese national, (b) all assets, investments and income from the sole proprietorship belong to the natural person who owns the interest in the sole proprietorship and (c) such natural person is responsible for all liabilities and debts of the sole proprietorship.

Even though LLEN states that it "owns 100% of the equity of Hong Xing" in fact the equity could not have been transferred to TNI so long as Hong Xing remained a sole proprietorship. SAIC filings corroborate this conclusion.

According to an SAIC filing signed April 15, 2010, Hong Xing remained a sole proprietorship that was wholly owned by Hong Xing Li, the same individual who was supposed to have sold the factory to LLEN.

**私营企业从业人员及经营状况统计表**  
(此表由私营企业填写)

企业名称: **Hong Xing Coal Washing** 营业执照注册号: 5303232000269  
 法定代表人(负责人): **李红星 Li Hong Xing**  
 企业类型: 个体独资企业 **Sole Proprietorship**

**Legal Rep**

	项 目	编号	人 数 (人)
	从业人员	1	
人员 状况	1、下岗失业人员	2	0
	其中: 省外下岗失业人员	3	0
	2、残疾人	4	0
	3、云南省自谋职业的城镇退役士兵	5	0
	4、2003年应届普通高校毕业生	6	0
	5、两劳释放人员	7	0
	6、离退休人员	8	0
	7、退职人员	9	0
	8、其他(指上述7类人员以外的从业人员)	10	47
	合 计	11	
文化 程度	1、研究生以上	12	0
	2、大学本科	13	0
	3、大专	14	0
	4、中专	15	0
	5、高中	16	7
	6、初中以下	17	40
	合 计	18	
政治 面貌	1、党员	19	0

7

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<sup>1</sup>Without any interim disclosure, according to LLEN's FY 2011 Form 10-K, the company transferred Hong Xing from TNI to a newly formed subsidiary, Yunnan L&L Tai Fung ("Tai Fung") in March of 2011.

## 二、经营情况

全年销售营业收入:	150 (元)
全年利润总额	0 (元)
全年亏损额:	36 (元)
全年纳税总额:	21 (元)
年末资产总额	200 (元)
年末负债总额:	150 (元)

注: 本表内容应根据资产负债表和损益表填写, 并附在资产负债表之前。

本人确认公司提交的年检报告书所填写内容属实。

Legal Rep 公司法定代表人签名:

Li Hong Xing

2010 年 4 月 15 日  
April 15, 2010

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[http://www.qjgs.gov.cn/nj/template/t\\_grdz\\_bottom.asp?bz=23&qyxh=530300D00065...](http://www.qjgs.gov.cn/nj/template/t_grdz_bottom.asp?bz=23&qyxh=530300D00065...) 2010/4/14

The above filing shows that as of April 2010, five months after the consummation of the purported sale, the company did not legally own the equity of the Hong Xing coal washing factory even though LLEN claimed to have acquired 100% of the equity of the entity in its SEC filings.

Because a third party is the legal owner of the Hong Xing business, LLEN or its shareholders may have to litigate against him to obtain legal title to the assets. A dispute between shareholders and a local Chinese businessman over assets located in China is an unappetizing prospect.

Chinese courts are notoriously corrupt, arbitrary and protective of local businesses and industry.<sup>2</sup> Notions of judicial independence do not apply. As a result, for foreign investors or a Sino-foreign JV such as TNI, we suspect that litigating against a local Chinese businessman in a Chinese court would be a Sisyphean task. Further hindering any prospect of recovery are any relationships Hong Xing Li may have with the local government and state owned enterprises, which would only magnify his influence over the judicial system.

Together, Zone Lin and Hong Xing provided approximately \$10 million in net cash to the company's operations in FY 2010. Yet the company does not have legal title to the equity of either of these businesses. Zone Lin is held by the CEO and Chairman in a sole proprietorship and Hong Xin is held by a third party in a sole proprietorship. In each case, LLEN claims to own 100% of the businesses' equity. This is at best a major omission from the company's SEC disclosures and at worst fraud.

<sup>2</sup>[http://www.bc.edu/bc\\_org/avp/law/lwsch/journals/bciclr/25\\_1/02\\_TXT.htm](http://www.bc.edu/bc_org/avp/law/lwsch/journals/bciclr/25_1/02_TXT.htm)

## Undisclosed Minority Shareholders

SAIC filings also show that contrary to the company's claims, LLEN's two sino-foreign joint ventures are not wholly-owned.

According to the company's 2011 Form 10-K, LLEN owns 100% of Kunming Biaoyu Industrial Boiler Ltd. ("**KMC**") and has a 98% "controlling interest" in TNI.

But SAIC records for TNI show that it is only 70% owned by LLEN. The other 30% of TNI's equity is owned by an entity called Yunnan Tianneng Industry, which is wholly owned by **an unrelated** third party, Yunnan Xinzhongan Fire Engineering Installation Co., LTD.

Strangely, we found support for our evidence buried in LLEN's SEC filings. A January 1, 2010, [acquisition agreement](#) states that TNI is in fact a sino-foreign JV "(which L&L owns 70% voting equity and Tianneng Co. owns 30%)."

This is staggering. LLEN claims to own a 98% controlling interest in a subsidiary in its Form 10-K but states that it only owns 70% in another SEC filing. Filings in China indicate the real number is 70% and that LLEN has been misrepresenting the percentage of ownership of its subsidiaries.

In addition, SAIC records obtained in May 2011 show that LLEN only owns 60% of KMC. Four minority shareholders own the other 40%.

The following table summarizes the evidence:

SUBSIDIARY	LLEN'S OWNERSHIP ACCORDING TO SEC FILINGS	LLEN'S OWNERSHIP ACCORDING TO SAIC FILINGS
KMC	100%	60%
TNI	98%	70%

At best, this is a material omission from LLEN's SEC disclosures. At worst, this is fraud.

## Mining Rights – Risky Business

As LLEN discloses to shareholders in its public filings, two of the company's most important mining assets are owned not by the company but are held (surprise!) by individuals in sole proprietorships. Although the company is forthright in alerting shareholders to this arrangement with respect to the mines, we believe that the company has downplayed the material risk of this legal structure to LLEN's shareholders. This is a risk we believe is only highlighted by the fact that LLEN purportedly acquired an additional "20% ownership" interest in its two primary mining assets for **no consideration**.

The core of LLEN's business is the DaPuAn Mine and the TuSong Mine (collectively, the "2 Mines").

According to LLEN's SEC filings, in 2008, the company acquired a 60% interest in the 2 Mines from two individuals, Xu Ban-Sheng (who owned the DaPuAn Mine) and Yang Xiao-Shu. These two individuals are Chinese nationals, and according to the [Joint Venture Contract](#) provided by LLEN, held their respective coal mines in sole proprietorships. SAIC filings indicate that both mines are still held in sole proprietorships and that each of their respective owners, not LLEN, will each have the legal title to the ownership interests in the mines. To be fair to LLEN, it does disclose that it does not technically "own" either mine under Chinese law.

But LLEN's prior disclosures made it seem as though the company could, and indeed was on the verge of, registering an ownership interest in the equity of the mines with the Chinese government. According to the company's 2010 **Form 10-K**, LLEN was **"in the process of registering our equity ownership interest in the DaPuAn and SuTsong Mines with the Chinese government, under the provisional name "L & L Coal Partners" through a nominee who is a Chinese citizen that holds our equity ownership in trust for the benefit of the Company under an agency agreement executed in April 2008."** This sentence made the company's claims to the future rights of the coal at 2 Mines appear more stable and legitimate to investors.



Troublingly, the above sentence appeared in the company's Form 10-K's for FY 2009 and FY 2010. **It was omitted from the company's FY 2011 Form 10-K.** It is our opinion that this omission was not by accident. In its FY 2009 and FY 2010 Form 10-Ks, this sentence conveyed **to shareholders that its interest in the mining rights at the 2 Mines** could be registered with the government and would thus be more secure. Instead, because both mines are owned in sole proprietorships, LLEN could not directly own or register such an equity interest.

Make no mistake; the company has disclosed that it does not directly own an interest in the mine. But we believe that its FY 2009 and FY 2010 disclosures that it "was in the process of registering" an equity ownership interest in the 2 Mines with the Chinese government was misleading and downplayed the risks that would be obvious to shareholders if the company had stated clearly that an equity ownership interest in a sole proprietorship could not be registered.

What bothers us about LLEN's rights to the 2 Mines is that they seem to acquire them **cheaply** and that the company does not disclose the terms of the deals. On August 1, 2009, the company increased its ownership of the 2 Mines from 60% to 80% with "**no consideration given by the company to the non-controlling interest holders.**" Despite the importance of these assets to its business, LLEN did not file a Form 8-K detailing this transaction.

As of Q3 2009, according to LLEN, the 2 Mines were already incredibly profitable. **Why would the minority shareholder transfer 20% of an amazingly profitable business to LLEN for free?** What did the company get for nothing? Would a sole proprietor who owns a mine be willing to give up another "20%" because they knew at the end of the day, the mine is owned only by the proprietorship and not LLEN?

Support for our argument that sole proprietorships present significant undisclosed risks to investors comes from LLEN itself. In March 2011, the company **acquired** an interest in the DaPing Mine. The Equity Transfer Agreement governing the transaction requires the seller to "change the existing proprietorship business format to a corporation format" upon consummation of the acquisition. In fact, under the **Equity Transfer Agreement**, the failure to change the DaPing Coal Mine from a proprietorship to a corporation is **considered a "default"** under the contract, releasing LLEN from its obligation to pay the seller.

The fact that LLEN required the seller to change the structure of the DaPing Mine to a corporation from a sole proprietorship at the risk of a default under the contract should tell investors that the legal structure of a target entity is of paramount importance.

But the company does not disclose the risks of its legal structure in its public filings. A risk we believe is only highlighted by the fact that LLEN purportedly acquired an **extra 20% ownership stake in its most profitable business for free.** If LLEN can get something for nothing, what does it really own?



## LLEN's By the Numbers

One of the common characteristics of Chinese reverse mergers that are fabricating their SEC financial statements is that the company's performance appears too good to be true. LLEN is no exception. In fact, LLEN's financial performance is so far superior to its competitors that it leaves only two choices: either LLEN is so much more efficient and profitable (adjusted for size) than its competitors that it has revolutionized the coal mining business or LLEN is fabricating its SEC filed financial statements.

According to the SEC filings, LLEN is one of the most efficient and profitable (pound for pound) coal mining companies in the world:

	LLEN	YZC	PCX	ACI	WLB	ANR
Gross Margins	46%	46%	18%	24%	N/S	20%
Return on Average Equity	57%	22%	5%	5%	N/S	4%
Return on Average Assets	40%	12%	2%	2%	3%	2%
Net Income Margins	26%	24%	4%	6%	4%	4%
Inventory Turnover	13	14	20	10	N/S	16

Notes:

LLEN Info from May 1, 2008 – January 31, 2011

All other company information from January 1, 2008 – December 31, 2010

WLB – coal only segment was broken out and reflected above

As depicted in the table above, LLEN's gross margins and net income margins were incredible as compared to U.S.-based coal mining companies, but in line with YZC, its Chinese competitor. What does not make sense is that YZC, PCX, ACI, WLB and ANR are much larger companies than LLEN. We would expect that bigger companies would achieve economies of scale in a capital-intensive industry such as coal mining. Yet with the exception of YZC, LLEN outperforms all of its larger brethren.

We will concede that certain financial metrics vary across geographic markets depending on the number of competitors, the maturity of the market, costs of labor etc... so in order to be fair to LLEN, we compared financial metrics between LLEN and YCZ, a much larger Chinese-based coal mine operator.

	L&L ENERGY, INC. (IN USD)				YANZHOU COAL MINING CO. LTD. (IN USD)			
	9 Mos Ended	Year Ended	Year Ended	Year Ended	Year Ended	Year Ended	Year Ended	Year Ended
	1/31/11	4/30/10	4/30/09	4/30/08	12/31/10	12/31/09	12/31/08	12/31/07
Gross Profit	\$59,267,645	\$52,180,951	\$22,991,922	\$1,387,079	\$2,214,357	\$1,342,699	\$1,831,101	\$1,063,047
Net Revenues	\$178,642,209	\$109,217,838	\$40,938,128	\$23,381,508	\$4,991,801	\$3,040,755	\$3,718,738	\$2,222,126
Gross Margins	33%	48%	56%	6%	44%	44%	49%	48%
Comprehensive Income	\$38,951,020	\$32,937,534	\$10,526,817	\$1,074,808	\$1,384,427	\$641,771	\$907,899	\$475,066
Total Stockholders' Equity	\$126,752,800	\$78,222,442	\$22,432,979	\$12,238,137	\$5,489,983	\$4,287,030	\$3,934,577	\$3,149,637
Return on Average Equity	50%	65%	61%		28%	16%	26%	
Comprehensive Income	\$38,951,020	\$32,937,534	\$10,526,817	\$1,074,808	\$1,384,427	\$641,771	\$907,899	\$475,066
Total Assets	\$158,540,241	\$116,567,433	\$41,543,388	\$21,872,061	\$10,683,720	\$9,166,191	\$4,746,638	\$3,840,636
Return on Average Assets	37%	42%	33%		14%	9%	21%	
Comprehensive Income	\$38,951,020	\$32,937,534	\$10,526,817	\$1,074,808	\$1,384,427	\$641,771	\$907,899	\$475,066
Net Revenues	\$178,642,209	\$109,217,838	\$40,938,128	\$23,381,508	\$4,991,801	\$3,040,755	\$3,718,738	\$2,222,126
Net Income Margins	22%	30%	26%	5%	28%	21%	24%	21%
Cost of Revenues	\$119,374,564	\$57,036,887	\$17,946,206	\$21,994,429	\$2,777,444	\$1,698,056	\$1,887,636	\$1,159,079
Inventories	\$10,520,770	\$9,605,103	\$1,524,493	\$1,336,489	\$242,075	\$130,347	\$120,529	\$64,725
Inventory Turnover	16	10	13		15	14	20	

The above chart is incredible. Keep in mind that YCZ is almost 10 times larger than LLEN if measured by revenue. Surprisingly, LLEN's gross margins and net income margins are similar to YCZ's despite the benefit of economies of scale that YCZ should enjoy.

More suspiciously, LLEN's return on average equity and return on average assets were double the returns for YCZ. For the most recent 9 months ending January 31, 2011, LLEN enjoyed a Return on Average Equity of 50% and a Return on Average Assets of 37% while YCZ had a ROAE of 28% and a ROAA of 14%. If we look at the 2009 numbers the ROAE and ROAA difference is even more shocking.

LLEN's phenomenal ROAE indicates that the company is acquiring its assets for much cheaper than YCZ. This corroborates our findings discussed above, which suggest that LLEN does not actually own all of the assets it purports to have acquired.

Further, the company's incredible ROAA indicates that it is almost twice as efficient as YCZ at deriving net income from its assets. Given that the company is a recent entrant into the market, we do not find such performance credible.

In short, LLEN is one of the most efficient and profitable (adjusted for size) coal mining companies in the world. It boasts even more impressive returns on equity and returns on assets than **even its Chinese** competitor. This seems ridiculous. What makes this story even harder to believe is that LLEN conjured its spectacular coal mining business . . .

## Out of Thin Air

LLEN's success on paper is nothing short of a miracle. In just **3 years** LLEN went from a fledgling turnaround firm primarily selling air compressors to a coal mining business that purportedly generates higher margins and a better return on assets and equity than almost **any other coal mining company in the world**. To boot, LLEN achieved these results without any top-level executive having **any prior experience whatsoever** in operating a coal mine. How can a company come out of nowhere, led by a founder and chairman with no direct experience in operating a mining business, and effectively become one of the most profitable pound-for-pound coal mining companies in the world?

Prior to 2008, LLEN's business model was, according to the company's [2007 Form 10-K](#), to acquire an interest in privately held Chinese companies and then leverage western management and accounting techniques to improve stodgy and archaic Chinese business practices. The company's primary focus was an air compressor business.

More importantly, prior to 2008, LLEN's business model **was not to mine coal**.<sup>3</sup> In fact, in 2007, LLEN positioned itself as a broker of coal mining rights when its subsidiary, KMC, **sold the rights to a coal mine to a third party for cash rather than establish an operation**.

Suddenly, in May 2008, LLEN acquired rights in two operating coal mines (DaPuAn Mine and Su Tsong Mine) and in 3 years, LLEN boasts more impressive returns on assets and equity than companies that have been in the coal mining business for **over 100 years**. Does that pass the smell test?

Even more suspiciously, other than CFOs (discussed below), until this year LLEN has only had **three executive level officers in its history, none of whom, prior to joining LLEN, had any experience in the coal mining business**. According to the company's Form 10-K filings for FY 2008, 2009 and 2010 LLEN's only non-CFO executive officers were (i) the founder and chairman, Dickson Lee, (ii) his brother Paul Lee (who served as chairman and CEO for a short time) and (iii) Clayton Fong.

Dickson Lee's **background** is in accounting and finance. Prior to his brief stint in charge of LLEN, Paul Lee was an **insurance salesman** and president of the Chinese Restaurant Association of Michigan. Clayton Fong, prior to joining LLEN, was the executive director for 13 years of a not for profit organization in Seattle that placed Asian American senior citizens in the workforce. Other than a smattering of "interim" CFOs, LLEN's 2008, 2009, and 2010 Form 10-Ks do not mention any other executive officers.

This is remarkable because apparently three executives with respective backgrounds in finance, insurance sales/Chinese restaurants and career services for the elderly turned a fledging firm into, adjusted for size, one of the most efficient and profitable coal mining companies in the world in just three years. The alternative explanation, and our opinion, is that LLEN has been fabricating its financial statements.

## SAIC Filings

SAIC filings corroborate our suspicion that LLEN's incredible financial performance is simply not credible. According to publicly available SAIC filings for the calendar year 2009, LLEN's revenues are much smaller and its assets are worth considerably less than the company claims in its SEC financial statements.<sup>4</sup>

2009 SAIC FILING INFO	KMC	L&L COAL		TNI		TOTALS		SEC Filing info	2009
	Kunming Biaoyu Industrial Boiler Co., LTD	DaPuAn Mine	SuTsong Mine	ZoneLin Coal Coking	HongXing Coal Washing	TOTAL	TOTAL	L&L Energy (Nasdaq: LLEN), *Feb 1, 2009 thru Jan 31, 2010	Discrepancy
	"KMC"	"L&L Coal"	"L&L Coal"	"ZoneLin"	"HongXing"		\$1 =¥6.8	"LLEN"	
INCOME STATEMENT	CNY	CNY	CNY	CNY	CNY	CNY	USD	USD	
Net sales	¥14,505,077	¥42,730,753	¥27,000,000	¥45,947,831	¥1,500,697	¥131,684,358	\$19,365,346	\$85,221,700	\$65,856,353
Net profit/(loss)	¥476,933	¥8,950,515	¥12,000,000	¥2,418,152	¥362,171	¥17,693,259	\$2,601,949	\$22,452,970	\$19,851,020
BALANCE SHEET									
Total Assets	¥24,392,521	¥82,111,443	¥60,000,000	¥34,651,828	¥2,006,897	¥203,162,689	\$29,876,866	\$111,506,630	\$81,629,763

**According to 2009 calendar year SAIC filings, LLEN's assets are only 25% of the value that the company claims in its SEC filings and the company's net sales are four times smaller than the company claims in its SEC filings.**

<sup>3</sup> Prior to entering the mining business, LLEN owned a majority equity interest in two energy and power subsidiaries - LEK, (Liuzhou Luerkong Machinery Co., Ltd), an air compressor subsidiary, and KMC, an energy (coal) consolidator in China. Prior to 2008, LLEN had also invested in a computer software company and an agriculture company.

<sup>4</sup> Our review of SAIC filings was limited to filings for the calendar year 2009 because the company has not submitted 2010 filings at the time of our request.

There has been much debate recently about the validity of SAIC filings. The SAIC is a government agency that, among other functions, issues business licenses to Chinese firms. In order to obtain and renew a business license, which is required to operate in China, a Chinese company must file an annual inspection report with a local government office containing a balance sheet and an income statement.

Brokers pumping small cap Chinese stocks often argue that SAIC filings do not match SEC filings because the SAIC is a business registrar and it does not review the accuracy of submitted financial statements. This makes no sense. Why would a government agency ask a company to submit a balance sheet or income statement and then not care if it is blatantly false? More importantly, what would a company gain by lying on financial statements submitted to the SAIC?

Some small cap brokers have argued that Chinese companies understate revenue in SAIC filings so as to avoid the attention of corrupt government officials. This argument is weak. Nothing should attract more attention from potentially corrupt government officials than raising tens of millions of dollars in cash through American capital markets. Regardless, why are investors comfortable with a company that lies on any financial statement filed with any governmental agency, in the U.S. or China?

Western investors defending the discrepancy between financial statements filed with the SAIC and those filed with the SEC should consider the following decision box:

DECISION	UPSIDE	DOWNSIDE
LLEN lies on financial statements filed with the SAIC	?	Fines or criminal prosecution of officers and directors (including capital punishment) by the Chinese government with jurisdiction over the assets and operations of the business
LLEN lies on financial statements filed with the SEC	Tens of millions of dollars from investors looking for next hot Chinese stock.	None (other than delisting). Neither the SEC nor the US government has jurisdiction over LLEN or Dickson Lee (provided he remains in the PRC).

Whereas for a Chinese company there is large upside and limited downside to lying to the SEC, there is by comparison no upside and a potentially large downside to lying to the SAIC. So if there is a discrepancy between SEC and SAIC filings, it is logically more likely that the SEC filings are false. Deductive reasoning aside, empirical evidence shows that there are [many examples of legitimate companies](#) that file financial statements with the SAIC which are consistent with their SEC financials. The company's Chinese SAIC filings show that LLEN's revenues and net income are much smaller than reported and its assets are much less valuable than the company claims in its SEC financials.

## Judge a Company By the Company It Keeps

Dickson Lee, LLEN's founder, CEO and Chairman boasts a checkered history of allegedly making material misrepresentations to investors in connection with the sale of LLEN stock. In addition, the only other key executive officer at LLEN other than a smattering of CFOs landed at the company after apparently being dismissed for misconduct from his previous position as director of a charitable organization.

### DICKSON LEE'S TRAIL OF TEARS

Regulators have charged Dickson Lee and/or LLEN with violating securities laws in connection with the sale of LLEN stock on **five separate occasions**.<sup>5</sup> Public documents reveal that prior to listing LLEN on the NASDAQ, Dickson Lee was able to raise at least **\$2.8 million** through the sale of unregistered private stock and warrant offerings. Lee was able to [attract](#) investors thanks to incredible financial projections contained in a series of Private Placement Memoranda ("PPMs"). Four different state securities regulators and FINRA initiated enforcement actions against Lee, his agent and/or LLEN, in most cases alleging **material misrepresentations of fact** in connection with offerings of LLEN securities. In plain English, law enforcement charged Dickson Lee with lying to prospective investors.

<sup>5</sup> A report summarizing these charges can be found at <http://brokercheck.finra.org>



## WASHINGTON

In April 2009, the Securities Division for the State of Washington **charged** that, in connection with the offering of LLEN securities, Lee:

1. Misrepresented to investors the percentage of the gross proceeds of the offering that certain retained referral agents and brokers could receive as a commission for their services; and
2. Failed to provide a reasonable basis upon which the projected operating results were made in [Private Placement Memorandas (“PPM”) marketed over the phone to investors.]

Lee’s pitch to investors was that LLEN would acquire state-owned Chinese enterprises and, after a touch of American business acumen and management expertise, such businesses would quickly turn profitable. Lee’s PPMs projected **profits** of **\$5.6 million** by the end of 2004 despite the fact that LLEN’s SEC filings indicated that the company’s **revenues** were less than \$300,000 at the close of its April 30, **2003 fiscal year**.

In addition, the Securities Division for the State of Washington charged that Lee’s PPM deceived investors by stating that brokers or referral agents could only receive a commission up to 20% of the gross proceeds of any capital committed by the investor, when in fact, Lee had promised a **35% commission to Steven Johnston**, who was **not even a licensed broker-dealer**.

Essentially, the State of Washington accused Lee of (1) lying to investors about the percentage of their dollars that would go to his agents and (2) making wild claims about future performance of LLEN that had no basis in fact. These types of accusations should sound hauntingly familiar to investors in U.S.-listed Chinese securities. But the State of Washington was not alone in alleging that Lee and/or LLEN violated the law.

## FINRA

On January 12, 2007, Lee **entered** into a Letter of Acceptance, Waiver and Consent with FINRA whereby FINRA **fined Lee \$65,000 and suspended him from associating** with any NASD member in any capacity for one year. **FINRA** concluded that “in connection with his company’s offers and sales of securities, **Lee caused his company to make untrue statements of material fact and omitted to state material facts necessary in order to make the statements that it made, in light of the circumstances in which they were made, not misleading.**”

## CALIFORNIA

On May 16, 2006, the State of California, Department of Corporations issued a Desist and Refrain Order against Lee, LLEN and Johnston in connection with the sale of LLEN common stock. The State of California **alleged** “that the securities offered and sold by Johnston ... Lee and LLEN were offered and sold in this state by means of written or oral communications that included **untrue statements of material fact or omitted to state material facts** necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, in violation of section 25401 of the CSL.” Again, in layman’s terms, the State of California accused Lee (through his agent) of lying to investors.

## CONNECTICUT

On April 26, 2007, the Banking Commissioner of the State of Connecticut **entered into a consent** order with LLEN for violations of state securities laws in connection with the offering and/or sale of unregistered LLEN securities and of the use of an unregistered agent. Pursuant to such order, the Commissioner fined the company and **barred LLEN** for a period of **ten years** from selling securities in the State of Connecticut. This punishment was no mere “parking ticket.” For regulators to ban LLEN from selling securities in the state of Connecticut for a decade, clearly regulators believed that LLEN’s conduct was a serious violation.

## NEW MEXICO

On March 14, 2006, the State of New Mexico, Securities Division, entered into a consent agreement with Dickson Lee, LLEN, and Johnston. The allegations included the use of an unregistered securities salesperson and failure to adequately supervise Johnston in connection with the sale of securities.

In sum, securities enforcement agencies around the U.S. have charged Lee and/or LLEN with violations on **five separate occasions**. According to these charges, Lee engaged in a pattern of behavior that looks remarkably similar to accusations leveled at other Chinese RTOs accused of, or found to have been committing, fraud.

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**CLAYTON FONG**

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Clayton Fong, LLEN's Executive Vice President of US operations and Lee's right hand man, also has a history of troubled allegations. From 1996 to 2009, Fong served as the CEO of National Asian Pacific Center on Aging ("NAPCA"), a Seattle-area non-profit organization.

According to an investigative report by the *Seattle Times*, NAPCA dismissed Fong in 2009 following an internal review, which, according to the NAPCA board chairman, "**uncovered a pattern of behavior and conduct of great concern to [the board]**." The chairman stated that the board "lost confidence in [Fong] to lead our organization."

When pressed for additional details, the NAPCA's chairman *stated* that the board "concluded that a number of [Fong's] actions and conduct fell short of the standards we set in [the NAPCA's] policies and bylaws". In connection with Fong's dismissal, the Chairman also *stated* that "we have a fiduciary duty here to look after the **organization's** and **funders' resources**." It does not take much to read between the lines: Fong appears to have been fired for misconduct potentially related to the misuse of a charitable organization's funds.

This was not the first time Fong came under scrutiny for his use of the charity's money. In 1999, Federal auditors working at the behest of the Labor Department issued a highly-critical report on the NAPCA which questioned \$330,000 in expenditures and *accused* the NAPCA of "**misusing taxpayer money to pay for golf balls, tobacco products, a Christmas party and a trip to Las Vegas for its executive director [Clayton Fong]**."

The *Seattle Times* *reported* that the federal audit investigation uncovered the following questionable transactions:

- **Fong** told employees that the NAPCA would pay a bonus of \$1,300 to 21 workers, each of whom agreed to donate \$1,000 back to the agency to use at its discretion.
- The NAPCA spent nearly \$35,000 on travel and miscellaneous expenses that were inappropriately charged to federal grants, with **most of the costs incurred by Fong**.
- The NAPCA also incurred \$13,700 in questionable travel expenses and credit-card charges, including a side trip by **Fong** to Las Vegas from Los Angeles, where NAPCA also has offices.

In sum, in order to be long LLEN, an investor would have to have confidence in the credibility and trustworthiness of a founder and chairman that has been charged by multiple different regulators for securities violations in connection with the sale of LLEN stock and his lieutenant who appears to have been fired from his previous position as a director of a charity for misconduct.

A lot of the above information has already been discussed in the public forum, but we wanted to reiterate some of management's troubling background because we believe that the trustworthiness of management is of paramount importance when evaluating the credibility of Chinese RTOs.

## If This Is How You Treat Your Friends...

LLEN's transparency and the quality of the company's disclosures has consistently been a grim joke at investors' expense. One example stands out in a crowded field. Between 2008 and 2010, LLEN engaged in a series of private placement transactions with accredited investors that were favorable to purchasers and dilutive of existing shareholders. LLEN did not disclose the terms and conditions of most of these private placements to investors in an 8-K filing, as we believe should be customary for a transparent public company performing capital raises. Although not technically in violation of the SEC's disclosure rules (Reg D Rule 506), the opacity of these transactions is troubling. Perhaps the company was tight lipped because the terms of the deal would have been wildly offensive to any existing shareholder.

On October 8, 2009, LLEN sold 1,371,021 units to accredited investors at \$3.90/unit. The previous day's closing price of LLEN's common stock was \$5.50/share, meaning that LLEN sold the stock at 29% discount to the previous day's close.

Each unit sold was comprised of 1 share of common stock and 0.6 warrants (i.e. 60% warrant coverage). The warrants had a 5-year term to expiration and a \$5.62 strike price. Using the Black Scholes option-pricing model, a 75% implied volatility, and the warrant inputs listed above, the implied value of the warrants sold in this capital raise equate to \$3.36/share. Multiplying this value by the 60% warrant coverage per unit equates to a per share value of \$2.02/share. Netting off this free embedded option value from the original unit purchase price of \$3.90 equates to a net purchase price per share of \$1.88. If you did not follow the math do not worry.

The bottom line is that management was effectively selling shares of common stock through this private placement at only one third of the price<sup>6</sup> that public investors would have paid in the open market. LLEN made the same deal again on November 6, 2009, when LLEN issued 835,389 units at the same price and under the same terms as the October 8 issuance. In other words, management was diluting existing shareholders and offering sweetheart deals to a select group of private investors.

In the aggregate, the company issued 5.3 million warrants through direct private placements in FY2010, which equates to nearly 25% of the Company's 2009 fiscal year end fully diluted shares outstanding. Thanks for investing existing shareholders! Allow the company to repay you by diluting the value of your investment.

More offensive, one hedge fund [participated](#) in a series of direct private placements from 2008–2010 timeframe in which it acquired approximately 280,000 shares at heavily discounted prices relative to market price of the stock. The **associated warrant coverage with respect to these purchases could have been as high as 15 times the number of underlying shares** (approximately 4.25 million warrants received for purchasing 280,000 share of stock)! In layman's terms, LLEN diluted existing investors to give a hedge fund what appears to be as close to free money as exists on Wall Street.

To be clear, we are not alleging that these transactions violated any securities laws or Reg D specifically. We are however, gravely concerned over the transparency of the company and the quality of LLEN's disclosures with respect to these transactions. If LLEN had an interest in transparency, it would issue an 8-K describing the terms and conditions of each one of its private placements. Are these deals not being fully disclosed because they are offensive to shareholders?

## LLEN's Auditors: Who Watches the Watchmen?

The absence of internal controls has also been a consistent issue with reverse-merged Chinese companies accused of committing fraud. During a [recent speech](#), SEC commissioner Luis A. Aguilar stated a common denominator among Chinese RTOs was systematic concerns with the quality of the auditing and financial reporting. Aguilar warned:

*I am worried by the systematic concerns surrounding the quality of the financial reporting by these companies. In particular, according to a recent report by the staff of the Public Company Accounting Oversight Board (PCAOB), U.S. auditing firms may be issuing audit opinions on the financials, but not engaging in any of their own work.<sup>37</sup> Instead, the U.S. firm may be issuing an opinion based almost entirely on work performed by Chinese audit firms. If this is true, it could appear that the U.S. audit firms are simply selling their name and PCAOB-registered status because they are not engaging in independent activity to confirm that the work they are relying on is of high quality. This is significant for a lot of reasons, including that the PCAOB has been prevented from inspecting audit firms in China.*

LLEN has **never** retained an auditor that made Inside Public Accounting's [list of top 100 firms](#). More troubling, it appears that

<sup>6</sup>\$1.88 in the private placement vs. \$5.50 in the open market.

with the exception of Kabani, LLEN's auditors have another thing in common: they are all small firms headquartered in the US who for the most part, it appears, outsource accounting work to Chinese auditors. Just as Aguilar warned, such auditors may have been issuing audit opinions based almost entirely on work performed by Chinese audit firms.

DATES	NAME	NUMBER OF AUDITORS	OFFICES IN CHINA	NOTES
April 2, 2001 – April 3, 2002	Braverman & Company, PC (Braverman)	As of 2006: 1 Partner 0 Staff	No Offices in China. One office in Prescott Arizona	Audited Royal Coronado Form 10 SB filing; was later dismissed by L&L as it appears the firm was not SEC qualified.
April 24, 2002 – August 12, 2002	Moore Rowland International			Rowland contentiously resigned. The auditing firm apparently spent 5 months auditing LLEN FY 2002 financial statements, after which it apparently refused to sign off on the company's financial statements and then sent a letter to the SEC highlighting various accounting issues.
August 12, 2002 – February 28, 2006	Epstein, Weber & Conover, PLC	As of 2005, 5 Partners 19 Staff	No Offices in China. One office in Scottsdale Arizona	PCAOB inspection questioned policies and procedures and ability of partners to adequately supervise and review audit engagements.
February 28, 2006 – October 29, 2008	Jaspers + Hall, PC (Jaspers)	2 Partners 3 Staff	No Offices in China. 2 offices in Colorado (Colorado Springs and Denver)	Firm's registration suspended and its two partners each barred 5 years for numerous and repeated violations and failing to perform the most audit basic procedures
November 9, 2008 – Present	Kabani & Company, Inc (Kabani)	1 Partner 20 Staff	1 Office in China 1 Office in Los Angeles, California	Subject of two negative PCAOB inspections; former client Bodisen Biotech a well documented scandal; former client CAGC accused of fraud, under SEC investigation, and subject of class action lawsuits

Given the record of certain of the audit firms listed above, we believe investors should have great concerns over the validity of LLEN's financials.

#### JASPERS

Of particular concern is Jaspers, an accountant instrumental in LLEN's entry into the coal mining business. Jaspers bore many of the characteristics that Aguilar warned of in his recent speech: it only had two partners and three staff members working out of two offices in Colorado. Jaspers did not have any offices in China, but it was responsible for verifying the validity of LLEN's acquisitions of the DaPuAn Mine and the TuSong Mine, which have become the core of LLEN's business.

Jaspers only quits LLEN's auditors when the PCAOB sentenced the two partner firm to the accounting equivalent of the death penalty. On October 21, 2008, [PCAOB revoked](#) Jaspers' registration and barred its only two partners from being associated with a registered public accounting firm **for five years**. The PCAOB determined that Jaspers and both its name partners repeatedly violated PCAOB auditing standards from 2005 through 2007.

Among other sins, the PCAOB stated that Jaspers failed to “perform adequate, or sometimes **any, audit procedures** in areas such as cash, deferred revenue, business acquisition accounting, equity, income taxes, related party transactions, and using the work of specialists.”

Notably, in connection with a publicly listed company named Bio-Warm, the PCAOB found that Jaspers “failed to perform any procedures to test the values Bio-Warm assigned to the tangible assets acquired and the liabilities assumed in the business combination and failed to test in any way management's representation that Bio-Warm was the acquiring entity in the business combination.”



If Jaspers was not performing any work to verify the value of assets acquired by Bio-Warm, a California company, can investors have confidence that Jaspers was performing any work to verify the value of the coal mines that LLEN acquired in China? If Jaspers failed to verify management's representations regarding a purported acquisition by a California company, can investors have confidence that Jaspers was independently verifying the representations of a management team operating a business in China?

Alarming for investors in LLEN, Jaspers was instrumental in LLEN's start on the fast track to becoming a profitable coal mining company. Jaspers audited LLEN's financial statements for three crucial years and signed off on the company's 2006 10-KSB, as well as its 2007 and 2008 Form 10-K filings. Jaspers audited the company when it acquired its first coal asset and transformed itself from a middling Chinese turnaround firm into a flashy high-growth mining company, despite an executive management team with no discernable experience or expertise in operating a coal mine.

Jaspers is just the type of auditor about which SEC Commissioner Aguillar recently warned investors: it had no presence in China and according to the PCAOB it routinely failed to engage in independent activity to confirm its representations of its clients. In other words, Jaspers bore the characteristics of an accounting firm commonly associated with fraudulent Chinese companies.

#### KABANI

LLEN replaced Jaspers with Kabani, a firm that has audited a number of U.S.-listed Chinese companies accused of, or found to have been committing, fraud. Kabani's roster includes:

COMPANY	SYMBOL	NOTES	EXCHANGE	ALL TIME HIGH PRICE	CURRENT PRICE	% OFF ITS HIGH
China Green Agriculture	CGA	Ongoing SEC investigation; Accused of fraud	NYSE	18.7	4.93	-73.64%
Bodison Biotech	BBCZ	Accused of fraud; delisted from AMEX	OTC BB	21.97	0.46	-97.91%
Shengtai Pharmaceutical	SGTI	Material weaknesses and deficiencies in disclosure controls and procedures	OTC BB	6	1.65	-72.50%
Fuwei Films (Holdings)	FFHL	Settled a securities class action accusing FFHL of fraud	NASDAQ	18.43	3.98	-78.40%
China Agritech	CAGC	Kabani audited 2005-07 fiscal years before being dismissed; Stock later halted and delisted amid a flurry of fraud allegations	Pink Sheets	30.45	1.45	-95.24%

The above table should not engender confidence in any investor relying on Kabani as a bulwark against fraud. Neither should the PCAOB assessment of Kabani's 2010 auditing process, despite the fact that Kabani can boast a Beijing office.

The PCAOB's 2010 inspection of Kabani found, in over 60% of the audits performed by the firm, **"deficiencies of such significance that it appeared to the inspection team that the Firm did not obtain sufficient competent evidential matter to support its opinion on the issuer's financial statements."**

#### ADVERSE ACCOUNTING OPINIONS

Kabani may have noticed that its reputation was negatively affected by the adverse PCAOB inspection and its association with Chinese companies accused of fraud.

On July 29, 2011, LLEN's auditor submitted a report to the board of directors of the company giving an **adverse opinion** on LLEN's internal control over financial reporting. For those who do not speak accounting, an adverse opinion from an **auditor** indicates that there is a reasonable possibility that a material misstatement of the company's financial statements will not be prevented or detected on a timely basis.

Kabani found the following material weaknesses in the company's internal controls:

- The Company did not maintain effective controls over the process of **ensuring timely preparation of its consolidated financial statements to allow for sufficient review prior to its filing deadline.**
- Additionally, the Company did not maintain effective controls over the process of ensuring appropriate reconciliation of several account balances, which resulted in several adjustments to the Company's consolidated financial statements, principally including presentation of related party balances; **disaggregation of assets and liabilities on the face of the balance sheet, as well as reconciliations of cash.**
- Lastly, the Company did not correctly characterize the **accounting transaction related to treasury stock**, which occurred during the period under audit.

In plain English, Kabani is accusing the company of not giving auditors enough time to properly review the company's financial statements and not properly maintaining controls over the process of reconciling cash and account balances and the process of breaking out the value of specific assets and liabilities on the balance sheet. In a profession known for mild manners and bookish subtlety, an accountant's warning to investors does not come much clearer.

Thus Kabani issued an adverse opinion on LLEN's internal control over financial reporting, indicating that there is a reasonable possibility that a material misstatement of the company's financial statements will not be prevented or detected on a timely basis.

Nor can investors place their faith in the company's litany of "interim" CFOs, most of whom suspiciously resigned just before they would have been asked to sign off on LLEN's financial statements.

## Woe Be the CFO

In its history, LLEN has only had a full time CFO (that is, a CFO who was not saddled with an "Interim" or "Acting" CFO label) **for an aggregate of less than 4 months.** We believe LLEN's high turnover at the CFO position should deeply concern investors. In total, LLEN has had **5 CFOs in the last 3 years.**

DATES	TENURE	NAME	COMMENTS
June 30, 2011 – present	< 2 months	Ian Robinson	Appointed at the age of 72
January 18, 2011 – June 29, 2011	5 months	David Lin	Only an "Acting" CFO
June 22, 2009 – January 18, 2011	17 months	Jung Mei (Rosemary) Wang	Only an "Acting" CFO
May 6, 2008 – June 22, 2009	13 months	Nicol Leung	Only an "Acting" CFO
March 19, 2008 – May 6, 2008	< 2 months	Gene Michael Bennett	A research firm, <a href="#">Absaroka capital</a> , exposed Bennett for lying about his qualifications and his experiences on his resume.
None Prior to March 2008			Dickson Lee, Founder and Current CEO appears to have been the only officer of the company from inception until March 2008.

### TIMING IS EVERYTHING

Look again at the left column of the table above. Notice a pattern? Alarming, **3 of LLEN's 4 former CFOs resigned** soon after the end of the company's fiscal year (April 30) **but before** the CFO would have been required to certify the company's audited financial statements to the SEC.

The timing of these CFO resignations is noteworthy and suspicious. If any of the former CFOs were disturbed by the audit process or suspected that LLEN was falsifying its financial statements, he or she would certainly want to resign before certifying to the SEC that such financial statements fairly presented, in all material respects, the financial condition and results of the operations of the company. To our knowledge, none of the CFOs have ever stated that they resigned from LLEN because they suspected that the company was committing fraud; but we believe that it is inherently suspicious that almost all of them resigned almost immediately prior to the time when they would have had to vouch for the accuracy of the company's financials.

A recent study of public company accounting fraud shows that, in the three years prior to the discovery of fraud, companies manipulating financial statements experienced higher CFO turnover than non-manipulating firms.<sup>7</sup> The study suggests that turnover is high at fraudulent companies because CFOs who refuse to bury their head in the sand either leave or are fired. In LLEN's case, the shoe certainly fits.

We believe that the history of CFO turnover at LLEN and the suspicious timing of the resignations of many of the company's CFOs is a serious red flag to investors. In fact, the only CFO in the history of the company to sign off on consecutive annual reports was Rosemary Wang...

## Rosemary's Baby

Confucius once said that "he who wishes to secure the good of others, has already secured his own." We are suspicious that Dickson Lee applied a Machiavellian bent to this old proverb about charity.

On April 10, 2009 Lee [donated one million](#) of his personal shares, at the time roughly valued at \$1 million, to ChungYuan Christian University Development Foundation of North America (the "ChungYuan Charity"), a California non-profit organization.

According to [publicly available tax records](#), the ChungYuan Charity was founded in 2008. In 2008, the charity received only \$51,623 in grants. However, the following year, the ChungYuan Charity received \$3,288,396 in grants, almost a third of which came from Dickson Lee. No doubt a banner year.

But a mere **two months after Dickson Lee's** unusually gracious donation, Rosemary Wang agreed to become the acting CFO of LLEN.

Suspiciously, there are numerous documents linking Rosemary Wang to the charity that received the timely and large donation from Dickson Lee. First, we believe that Rosemary Wang is the name partner of Wang and Chou Accountancy Corp., the accounting firm that prepared the Chun Yuan Charity's tax returns. Second, multiple [public records](#) list Rosemary Wang as the principal and primary contact of the [Chun Yuan Charity](#).

To be clear, we have no evidence that Rosemary Wang directly benefited from the donation, or that Dickson Lee made the donation in order to secure her loyalty, services or willful ignorance to fraud. However, we believe it is inherently suspicious that Rosemary Wang, the **only CFO in the history of LLEN to ever sign off on two of the company's annual audited financial statements**, was affiliated with, and possibly a principal of, a newly-formed charity which received an enormous and unusual donation immediately prior to her becoming acting CFO of LLEN.

## Hiding in Plain Sight

Because of the negative publicity surrounding Chinese RTOs and the fact that many such U.S.-listed Chinese companies have been accused of, or have been committing, fraud, LLEN has recently waged a public relations campaign to shirk the "reverse merger" label. Recently, RedChipCompanies, LLEN's investor-relations gurus, went so far as to state that LLEN was "[not really a reverse merger](#)." This is disingenuous to say the least.

According to LLEN's [FY 2003 Form 10-KSB filing](#): "in May of 2001, the Company, **through a reverse merger, becomes a SEC public reporting company.**"

Like many of the U.S.-listed Chinese companies that have been accused of, or have been committing, fraud, LLEN circumvented a traditional Initial Public Offering (IPO), which requires auditors, underwriters and prospective buyers to conduct a deeper due diligence investigation, in favor of an RTO. It is offensive to the investing community that LLEN now tries to conceal its true identity.

<sup>7</sup>"Why Do CFOs Become Involved in Material Accounting Manipulations?" is forthcoming in the *Journal of Accounting and Economics*. It is the work of Weili Ge and Terry Shevlin of the University of Washington Foster School of Business, and Mei Feng and Shuqing Luo of the University of Pittsburgh Katz Graduate School of Business.

## Valuation

Based on its auditor's adverse opinion of the company's internal controls, the fact that the company only reports to have less than \$5 million in cash, and the fact that various Chinese third parties have legal title to significant assets of the company located in China, we value LLEN's equity at less than \$1.00 per share.



## Conclusion

No section of this report should be read in isolation. In our view, the strength of each piece of evidence or argument reinforces the inferences we can draw from the other pieces of evidence or arguments. We are undoubtedly biased (very), but in our opinion, the cumulative evidence that LLEN is committing fraud or at least omitting material information from its SEC financial statements is overwhelming.

To review:

- SAIC reports show that a coal coking factory purportedly owned by LLEN is legally owned by Dickson Lee, CEO, founder and Chairman of the company and that he holds the entity in a sole proprietorship.
- Chinese government filings also show that the equity of a coal washing factory was not transferred to LLEN as the company has stated, but is still held in a sole proprietorship by a third party.
- LLEN has also failed to disclose significant minority shareholders in two major subsidiaries and certain material risks associated with its ownership of mining rights.
- LLEN's stunning margin profile and meteoric growth rate are the envy of its competitors, even other Chinese coal companies. This is remarkable because apparently three executives with respective backgrounds in finance, insurance sales/Chinese restaurants and career services for the elderly turned a fledgling firm into, adjusted for size, one of the most profitable and efficient coal mining companies in the world in just three years. In our opinion, this is not credible.
- SAIC filings suggest that the Company has been greatly exaggerating its net sales, net income and the value of its assets.
- As if to lend credence to our arguments, on July 29, 2011, LLEN's auditor gave an **adverse opinion** on the company's internal controls over financial reporting, stating that there is a reasonable possibility that a material misstatement of the company's financial statements will not be prevented or detected on a timely basis.
- LLEN's CEO and founder Dickson Lee boasts a checkered past. Five different regulators have charged Lee (acting through an agent or through LLEN) with securities violations on five separate occasions in connection with the sale of LLEN securities.
- LLEN has had five auditors in the last ten years, including Jaspers + Hall, PC, which resigned from LLEN only when the PCAOB suspended the registration of its only two partners and barred them from auditing publicly listed companies for a minimum of five years.
- LLEN has only had a non-'acting' Chief Financial Officer (CFO) for an aggregate of four months in its history. Suspiciously, three of its past four CFOs have resigned after the end of the company's fiscal year but before the CFO would have had to sign off on the company's audited financial statements.

We therefore issue a strong sell rating on LLEN's publicly traded securities.

## We Stand Behind Our Report

According to Greek mythology, Glaucus, a god of the sea blessed with the power of prophecy, frequently came to the rescue of distressed sailors and fisherman. We founded Glaucus Research Group California, LLC, to help capital markets investors navigate treacherous financial waters in search of great investment opportunities.

We live in turbulent times. Over the past few years, companies from all over the world have rushed to raise capital on U.S. securities markets. We believe that the temptation of public capital has lured disreputable management teams and over-zealous brokers who seek to take advantage of unsuspecting investors and their appetite for seemingly hot stocks. Glaucus Research Group California, LLC, is a California limited liability company that was formed to prod opportunities that appear “too good to be true” in an effort to alert investors and regulators to companies providing misleading public disclosures and inaccurate financial statements.

Glaucus Research Group California, LLC offers a unique combination of experience in U.S. capital markets, the Chinese business community and investigative journalism. Matthew Wiechert, our research director and California resident, has a background in investment banking.

Glaucus, the Greek god, provided pivotal assistance to Jason and the Argonauts in their quest for the Golden Fleece. At Glaucus Research Group California, LLC, we hope that our guidance can help investors in their pursuits, whatever they may be.

To contact us, please visit our website at <http://www.glaucusresearch.com/>.