BANK OF NOVA SCOTIA
Form 424B2
July 02, 2018

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Registration Statement No. 333-215597
(To Prospectus dated February 1, 2017,
Prospectus Supplement dated February 13, 2017, the
Prospectus Addendum dated January 9, 2018 and
Product Prospectus Supplement EQUITY INDICES
ARN-1 dated February 23, 2017)

	Pricing Date	June 28, 2018
3,207,352 Units	Settlement Date	July 6, 2018
$10 principal amount per unit	Maturity Date	August 30, 2019
CUSIP No. 064161326		

Accelerated Return Notes® Linked to the Russell 2000® Index

§ Maturity of approximately 14 months

§ 3-to-1 upside exposure to increases in the Index, subject to a capped return of 13.17%

§ 1-to-1 downside exposure to decreases in the Index, with up to 100% of your investment at risk

§ All payments occur at maturity and are subject to the credit risk of The Bank of Nova Scotia

§ No periodic interest payments

§ In addition to the underwriting discount set forth below, the notes include a hedging-related charge of $0.075 per unit. See "Structuring the Notes"

§ Limited secondary market liquidity, with no exchange listing

§ The notes are unsecured debt securities and are not savings accounts or insured deposits of a bank. The notes are not insured or guaranteed by the Canada Deposit Insurance Corporation (the "CDIC"), the U.S. Federal Deposit Insurance Corporation (the "FDIC"), or any other governmental agency of Canada, the United States or any other jurisdiction

The notes are being issued by The Bank of Nova Scotia ("BNS"). There are important differences between the notes and a conventional debt security, including different investment risks and certain additional costs. See "Risk Factors" and "Additional Risk Factors" beginning on page TS-6 of this term sheet and "Risk Factors" beginning on page PS-6 of product prospectus supplement EQUITY INDICES ARN-1.

The initial estimated value of the notes as of the pricing date is $9.65 per unit, which is less than the public offering price listed below. See “Summary” on the following page, “Risk Factors” beginning on page TS-6 of this term sheet and

“Structuring the Notes” on page TS-12 of this term sheet for additional information. The actual value of your notes at any time will reflect many factors and cannot be predicted with accuracy.

None of the U.S. Securities and Exchange Commission (the "SEC"), any state securities commission, or any other regulatory body has approved or disapproved of these securities or determined if this Note Prospectus (as defined below) is truthful or complete. Any representation to the contrary is a criminal offense.

	Per Unit	Total
Public offering price	$10.00	$32,073,520.00
Underwriting discount	$0.20	$641,470.40
Proceeds, before expenses, to BNS	$9.80	$31,432,049.60

The notes:

Are Not FDIC Insured	Are Not Bank Guaranteed	May Lose Value

Merrill Lynch & Co.
June 28, 2018

Accelerated Return Notes®
Linked to the Russell 2000® Index, due August 30, 2019
Summary

The Accelerated Return Notes® Linked to the Russell 2000® Index, due August 30, 2019 (the “notes”) are our senior unsecured debt securities. The notes are not guaranteed or insured by the CDIC or the FDIC, and are not, either directly or indirectly, an obligation of any third party. The notes will rank equally with all of our other unsecured senior debt. Any payments due on the notes, including any repayment of principal, will be subject to the credit risk of BNS. The notes provide you a leveraged return, subject to a cap, if the Ending Value of the Market Measure, which is the Russell 2000® Index (the “Index”), is greater than the Starting Value. If the Ending Value is equal to the Starting Value, you will receive the principal amount of your notes. If the Ending Value is less than the Starting Value, you will lose all or a portion of the principal amount of your notes. Any payments on the notes will be calculated based on the $10 principal amount per unit and will depend on the performance of the Index, subject to our credit risk. See “Terms of the Notes” below.
The economic terms of the notes (including the Capped Value) are based on our internal funding rate, which is the rate we would pay to borrow funds through the issuance of market-linked notes, and the economic terms of certain related hedging arrangements. Our internal funding rate is typically lower than the rate we would pay when we issue conventional fixed rate debt securities. This difference in funding rate, as well as the underwriting discount and the hedging related charge described below, reduced the economic terms of the notes to you and the initial estimated value of the notes on the pricing date. Due to these factors, the public offering price you pay to purchase the notes is greater than the initial estimated value of the notes.
On the cover page of this term sheet, we have provided the initial estimated value for the notes. This estimated value was determined by reference to our internal pricing models, which take into consideration certain factors, such as our internal funding rate on the pricing date and our assumptions about market parameters. For more information about the initial estimated value and the structuring of the notes, see “Structuring the Notes” on page TS-12.

Terms of the Notes

Issuer:	The Bank of Nova Scotia ("BNS ")
Principal Amount:	$10.00 per unit
Term:	Approximately 14 months
Market Measure:	The Russell 2000® Index (Bloomberg symbol: "RTY Index"), a price return index
Starting Value:	1,645.017
Ending Value:	The average of the closing levels of the Market Measure on each scheduled calculation day occurring during the Maturity Valuation Period. The calculation days are subject to postponement in the event of Market Disruption Events, as described beginning on page PS-18 of product prospectus supplement EQUITY INDICES ARN-1.
Participation Rate:	300%
Capped Value:	$11.317 per unit, which represents a return of 13.17% over the principal amount.
Maturity Valuation Period:	August 21, 2019, August 22, 2019, August 23, 2019, August 26, 2019 and August 27, 2019
Fees and Charges:	The underwriting discount of $0.20 per unit listed on the cover page and the hedging related charge of $0.075 per unit described in "Structuring the

Redemption Amount Determination
On the maturity date, you will receive a cash payment per unit determined as follows:

	Notes" on page TS-12.
Calculation Agent:	Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S").

Accelerated Return Notes®
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The terms and risks of the notes are contained in this term sheet and in the following:

Product prospectus supplement EQUITY INDICES ARN-1 dated February 23, 2017:
https://www.sec.gov/Archives/edgar/data/9631/000110465917011115/a17-4372_2424b5.htm

Prospectus addendum dated January 9, 2018:
https://www.sec.gov/Archives/edgar/data/9631/000091412118000045/bn20180108-424b3.htm

Prospectus supplement dated February 13, 2017:
https://www.sec.gov/Archives/edgar/data/9631/000110465917008642/a17-4372_1424b3.htm

Prospectus dated February 1, 2017:
https://www.sec.gov/Archives/edgar/data/9631/000119312517027656/d338678d424b3.htm

These documents (together, the "Note Prospectus") have been filed as part of a registration statement with the SEC, which may, without cost, be accessed on the SEC website as indicated above or obtained from MLPF&S by calling 1-800-294-1322. Before you invest, you should read the Note Prospectus, including this term sheet, for information about us and this offering. Any prior or contemporaneous oral statements and any other written materials you may have received are superseded by the Note Prospectus. Capitalized terms used but not defined in this term sheet have the meanings set forth in product prospectus supplement EQUITY INDICES ARN-1. Unless otherwise indicated or unless the context requires otherwise, all references in this document to "we," "us," "our," or similar references are to BNS.

Investor Considerations

You may wish to consider an investment in the notes if:

- You anticipate that the Index will increase moderately from the Starting Value to the Ending Value.
- You are willing to risk a substantial or entire loss of principal if the Index decreases from the Starting Value to the Ending Value.
- You accept that the return on the notes will be capped.
- You are willing to forgo the interest payments that are paid on conventional interest bearing debt securities.
- You are willing to forgo dividends or other benefits of owning the stocks included in the Index.
- You are willing to accept a limited or no market for sales prior to maturity, and understand that the market prices for the notes, if any, will be affected by various factors, including our actual and perceived creditworthiness, our internal funding rate and fees and charges on the notes.
- You are willing to assume our credit risk, as issuer of the notes, for all payments under the notes, including the Redemption Amount.

The notes may not be an appropriate investment for you if:

- You believe that the Index will decrease from the Starting Value to the Ending Value or that it will not increase sufficiently over the term of the notes to provide you with your desired return.
- You seek principal repayment or preservation of capital.
- You seek an uncapped return on your investment.
- You seek interest payments or other current income on your investment.
- You want to receive dividends or other distributions paid on the stocks included in the Index.
- You seek an investment for which there will be a liquid secondary market.
- You are unwilling or are unable to take market risk on the notes or to take our credit risk as issuer of the notes.

We urge you to consult your investment, legal, tax, accounting, and other advisors before you invest in the notes.

Accelerated Return Notes®
Linked to the Russell 2000® Index, due August 30, 2019

Hypothetical Payout Profile and Examples of Payments at Maturity

Accelerated Return Notes®

This graph reflects the returns on the notes based on the Participation Rate of 300% and the Capped Value of $11.317 per unit. The green line reflects the returns on the notes, while the dotted gray line reflects the returns of a direct investment in the stocks included in the Index, excluding dividends.

This graph has been prepared for purposes of illustration only.

The following table and examples are for purposes of illustration only. They are based on hypothetical values and show hypothetical returns on the notes. They illustrate the calculation of the Redemption Amount and total rate of return based on a hypothetical Starting Value of 100, the Participation Rate of 300%, the Capped Value of $11.317 per unit and a range of hypothetical Ending Values. The actual amount you receive and the resulting total rate of return will depend on the actual Starting Value, Ending Value, and whether you hold the notes to maturity. The following examples do not take into account any tax consequences from investing in the notes.
For recent actual levels of the Market Measure, see "The Index" section below. The Index is a price return index and as such the Ending Value will not include any income generated by dividends paid on the stocks included in the Index, which you would otherwise be entitled to receive if you invested in those stocks directly. In addition, all payments on the notes are subject to issuer credit risk.

Ending Value	Percentage Change from the Starting Value to the Ending Value	Redemption Amount per Unit	Total Rate of Return on the Notes
0.00	-100.00%	$0.00	-100.00%
50.00	-50.00%	$5.00	-50.00%
80.00	-20.00%	$8.00	-20.00%
90.00	-10.00%	$9.00	-10.00%
94.00	-6.00%	$9.40	-6.00%
97.00	-3.00%	$9.70	-3.00%
100.00(1)	0.00%	$10.00	0.00%
102.00	2.00%	$10.60	6.00%
105.00	5.00%	$11.317(2)	13.17%
110.00	10.00%	$11.317	13.17%
120.00	20.00%	$11.317	13.17%
130.00	30.00%	$11.317	13.17%
140.00	40.00%	$11.317	13.17%
150.00	50.00%	$11.317	13.17%
160.00	60.00%	$11.317	13.17%

(1) The hypothetical Starting Value of 100 used in these examples has been chosen for illustrative purposes only. The actual Starting Value is 1,645.017, which was the closing level of the Market Measure on the pricing date.
(2) The Redemption Amount per unit cannot exceed the Capped Value.

Accelerated Return Notes®
Linked to the Russell 2000® Index, due August 30, 2019
Redemption Amount Calculation Examples

Example 1
The Ending Value is 80.00, or 80.00% of the Starting Value:
Starting Value: 100.00
Ending Value: 80.00
= $8.00 Redemption Amount per unit

Example 2
The Ending Value is 102.00, or 102.00% of the Starting Value:
Starting Value: 100.00
Ending Value: 102.00
= $10.60 Redemption Amount per unit

Example 3
The Ending Value is 130.00, or 130.00% of the Starting Value:
Starting Value:
100.00
Ending Value:
130.00
= $19.00, however, because the Redemption Amount for the notes cannot exceed the Capped Value, the Redemption Amount will be $11.317 per unit

Accelerated Return Notes®
Linked to the Russell 2000® Index, due August 30, 2019
Risk Factors

There are important differences between the notes and a conventional debt security. An investment in the notes involves significant risks, including those listed below. You should carefully review the more detailed explanation of risks relating to the notes in the "Risk Factors" sections beginning on page PS-6 of product prospectus supplement EQUITY INDICES ARN-1, page S-2 of the prospectus supplement, and page 6 of the prospectus identified above. We also urge you to consult your investment, legal, tax, accounting, and other advisors before you invest in the notes.

Depending on the performance of the Index as measured shortly before the maturity date, your investment may result in a loss; there is no guaranteed return of principal.

Your return on the notes may be less than the yield you could earn by owning a conventional fixed or floating rate debt security of comparable maturity.

Your investment return is limited to the return represented by the Capped Value and may be less than a comparable investment directly in the stocks included in the Index.

Payments on the notes are subject to our credit risk, and actual or perceived changes in our creditworthiness are expected to affect the value of the notes. If we become insolvent or are unable to pay our obligations, you may lose your entire investment.

Our initial estimated value of the notes is lower than the public offering price of the notes. Our initial estimated value of the notes is only an estimate. The public offering price of the notes exceeds our initial estimated value because it includes costs associated with selling and structuring the notes, as well as hedging our obligations under the notes with a third party, which may include MLPF&S or one of its affiliates. These costs include the underwriting discount and an expected hedging related charge, as further described in "Structuring the Notes" on page TS-12.

Our initial estimated value of the notes does not represent future values of the notes and may differ from others' estimates. Our initial estimated value of the notes is determined by reference to our internal pricing models when the terms of the notes are set. These pricing models consider certain factors, such as our internal funding rate on the pricing date, the expected term of the notes, market conditions and other relevant factors existing at that time, and our assumptions about market parameters, which can include volatility, dividend rates, interest rates and other factors. Different pricing models and assumptions could provide valuations for the notes that are different from our initial estimated value. In addition, market conditions and other relevant factors in the future may change, and any of our assumptions may prove to be incorrect. On future dates, the market value of the notes could change significantly based on, among other things, the performance of the Index, changes in market conditions, our creditworthiness, interest rate movements and other relevant factors. These factors, together with various credit, market and economic factors over the term of the notes, are expected to reduce the price at which you may be able to sell the notes in any secondary market and will affect the value of the notes in complex and unpredictable ways. Our initial estimated value does not represent a minimum price at which we or any agents would be willing to buy your notes in any secondary market (if any exists) at any time.

Our initial estimated value is not determined by reference to credit spreads or the borrowing rate we would pay for our conventional fixed-rate debt securities. The internal funding rate used in the determination of our initial estimated value of the notes generally represents a discount from the credit spreads for our conventional fixed-rate debt securities and the borrowing rate we would pay for our conventional fixed-rate debt securities. If we were to use the interest rate implied by the credit spreads for our conventional fixed-rate debt securities, or the borrowing rate we would pay for our conventional fixed-rate debt securities, we would expect the economic terms of the notes to be more favorable to you. Consequently, our use of an internal funding rate for the notes would have an adverse effect on the economic terms of the notes, the initial estimated value of the notes on the pricing date, and the price at which you may be able to sell the notes in any secondary market.

A trading market is not expected to develop for the notes. Neither we nor MLPF&S is obligated to make a market for, or to repurchase, the notes. There is no assurance that any party will be willing to purchase your notes at any price in any secondary market.

Our business, hedging and trading activities, and those of MLPF&S and our respective affiliates (including trades in shares of companies included in the Index), and any hedging and trading activities we, MLPF&S or our respective affiliates engage in for our clients' accounts, may affect the market value and return of the notes and may create conflicts of interest with you.

The Index sponsor may adjust the Index in a way that may adversely affect its level and your interests, and the Index sponsor has no obligation to consider your interests.

You will have no rights of a holder of the securities included in the Index, and you will not be entitled to receive securities or dividends or other distributions by the issuers of those securities.

While we, MLPF&S or our respective affiliates may from time to time own securities of companies included in the Index, we, MLPF&S and our respective affiliates do not control any company included in the Index, and have not verified any disclosure made by any other company.

There may be potential conflicts of interest involving the calculation agent, which is MLPF&S. We have the right to appoint and remove the calculation agent.

The U.S. federal income tax consequences of the notes are uncertain, and may be adverse to a holder of the notes. See "Summary of U.S. Federal Income Tax Consequences" below.

The conclusion that no portion of the interest paid or credited or deemed to be paid or credited on a note will be "Participating Debt Interest" subject to Canadian withholding tax is based in part on the current published administrative position of the CRA. There cannot be any assurance that CRA's current published administrative practice will not be subject to change, including potential expansion in the current administrative interpretation of Participating Debt Interest subject to Canadian withholding tax. If, at any time, the interest paid or credited or deemed to be paid or credited on a note is subject to Canadian withholding tax, you will receive an amount that is less than the Redemption Amount. You should consult your own adviser as to the potential for such withholding and the potential for reduction or refund of part or all of such withholding, including under any bilateral Canadian tax treaty the benefits of which you may be entitled. For a discussion of the Canadian federal income tax consequences of investing in the notes, see "Summary of Canadian Federal Income Tax Consequences" below, "Canadian Taxation—Debt Securities" on page 50 of the prospectus dated February 1, 2017, and "Supplemental Discussion of Canadian Federal Income Tax Consequences" on page PS-26 of product prospectus supplement EQUITY INDICES ARN-1.

Additional Risk Factors

The notes are subject to risks associated with small-size capitalization companies.

The stocks composing the Index are issued by companies with small-sized market capitalization. The stock prices of small-size companies may be more volatile than stock prices of large capitalization companies. Small-size capitalization companies may be less able to withstand adverse economic, market, trade and competitive conditions relative to larger companies. Small-size capitalization companies may also be more susceptible to adverse developments related to their products or services.

Accelerated Return Notes®
Linked to the Russell 2000® Index, due August 30, 2019

The Index

All disclosures contained in this term sheet regarding the Index, including, without limitation, its make-up, method of calculation, and changes in its components, have been derived from publicly available sources. The Index was developed by Russell Investments ("Russell") before FTSE International Limited and Russell combined in 2015 to create FTSE Russell, which is wholly owned by London Stock Exchange Group. The information reflects the policies of, and is subject to change by, FTSE Russell (the "Index sponsor"). The Index sponsor, which licenses the copyright and all other rights to the Index, has no obligation to continue to publish, and may discontinue publication of, the Index. The consequences of the Index sponsor discontinuing publication of the Index are discussed in the section entitled "Description of ARNs—Discontinuance of an Index" beginning on page PS-20 of product prospectus supplement EQUITY INDICES ARN-1. None of us, the calculation agent, or MLPF&S accepts any responsibility for the calculation, maintenance or publication of the Index or any successor index.

General

The Index measures the composite price performance of stocks of 2,000 companies in the U.S. equity market. As of April 30, 2018, the top five Russell Global Sectors were Financial Services, Health Care, Technology, Consumer Discretionary and Producer Durables. (Sector designations are determined by the Index sponsor using criteria it has selected or developed. Index sponsors may use very different standards for determining sector designations. In addition, many companies operate in a number of sectors, but are listed in only one sector and the basis on which that sector is selected may also differ. As a result, sector comparisons between indices with different index sponsors may reflect differences in methodology as well as actual differences in the sector composition of the indices.)

The Index includes approximately 2,000 of the smallest securities that form the Russell 3000® Index. The Russell 3000® Index is comprised of the 3,000 largest companies, or 98% based on market capitalization, of the investable U.S. equity market. The Index is designed to track the performance of the small capitalization segment of the U.S. equity market.

Selection of Constituent Stocks of the Index

The Index is a sub-index of the Russell 3000® Index. To be eligible for inclusion in the Russell 3000® Index, and, consequently, the Index, a company's stocks must be listed on the last trading day of May of a given year and FTSE Russell must have access to documentation verifying the company's eligibility for inclusion. Eligible initial public offerings are added to Russell U.S. Indices at the end of each calendar quarter, based on total market capitalization rankings within the market-adjusted capitalization breaks established during the most recent reconstitution. To be added to any Russell U.S. index during a quarter outside of reconstitution, initial public offerings must meet additional eligibility criteria.

A company is included in the U.S. equity markets and is eligible for inclusion in the Russell 3000® Index, and consequently, the Index, if that company incorporates in, has its headquarters in and also trades with the highest liquidity (as defined by a two-year average daily dollar trading volume from all exchanges) in the United States or its territories. If a company satisfies any one of these criteria and the primary location of that company's assets or its revenue, based on an average of two years of assets or revenues data, is also in the United States, that company will also be considered part of the U.S. equity market. In addition, if there is insufficient information to assign a company to the U.S. equity markets based on its assets or revenue, the company may nonetheless be assigned to the U.S. equity markets if the headquarters of the company is located in certain "benefit-driven incorporation countries," or "BDIs," and that company's most liquid stock exchange is also in the United States. The BDI countries are Anguilla, Antigua and Barbuda, Aruba, Bahamas, Barbados, Belize, Bermuda, Bonaire, British Virgin Islands, Cayman Islands, Channel Islands, Cook Islands, Curacao, Faroe Islands, Gibraltar, Guernsey, Isle of Man, Jersey, Liberia, Marshall Islands, Panama, Saba, Sint Eustatius, Sint Maarten and Turks and Caicos Islands. ADRs and ADSs are not eligible for inclusion in the Index.

Exclusions from the Index

FTSE Russell specifically excludes the following companies and securities from the Index: (i) preferred and convertible preferred stock, redeemable shares, participating preferred stock, warrants, rights, installment receipts and trust receipts; (ii) royalty trusts, U.S. limited liability companies, closed-end investment companies (companies that are required to report Acquired Fund Fees and Expenses, as defined by the SEC, including business development companies), blank check companies, special purpose acquisition companies and limited partnerships; (iii) companies with a total market capitalization less than $30 million; (iv) companies with only a small portion of their shares available in the marketplace (companies with 5% or less float); (v) bulletin board, pink sheets or over-the-counter traded securities; (vi) companies that generate, or have historically generated, unrelated business taxable income and have not taken steps to block their unrelated business taxable income to equity holders; and (vii) exchange traded funds and mutual funds.

Initial List of Eligible Securities

The primary criterion FTSE Russell uses to determine the initial list of securities eligible for the Russell 3000® Index and consequently, the Index, is total market capitalization, which is calculated by multiplying the total outstanding shares for a company times the market price as of the "rank day" (typically the last trading day in May but a confirmed timetable is announced each spring) in May. All common stock share classes are combined in determining market capitalization. If multiple share classes have been combined, the pricing vehicle will be designated as the share class with the highest two-year trading volume as of the rank day in May. In cases where the common stock share classes act independently of each other (e.g., tracking stocks), each class is considered for inclusion separately. Stocks must have a closing price at or above $1.00 on their primary exchange on the last trading day of May of each year to be eligible for inclusion in the Index. In order to reduce unnecessary turnover, if an existing member's closing price is less than $1.00 on the last trading day of May, it will be considered eligible if the average of the daily closing prices from their primary exchange during the month of May is equal to or greater than $1.00.

Annual Reconstitution

The Index is reconstituted annually by FTSE Russell to reflect changes in the marketplace. The list of companies is ranked based on total market capitalization on the rank day in May, with the actual reconstitution effective on the first trading day following the final Friday of June each year, unless the final Friday in June is the 29th or 30th, in which case reconstitution will be effective on the preceding Friday. Changes in the constituents are preannounced and subject to change if any corporate activity occurs or if any new information is received prior to release.

Index Calculation and Capitalization Adjustments

As a capitalization-weighted index, the Index reflects changes in the capitalization, or market value, of the underlier stocks relative to the capitalization on a base date. This discussion describes the "price return" calculation of the Index. The current Index value is the compounded result of the cumulative daily (or monthly) return percentages, where the starting value of the Index is equal to the base value (100) and base date (December 31, 1978). Returns between any two dates can then be derived by dividing the ending period index value (IV_1) by the beginning period (IV_0) index value, so that the return equals $[(IV_1 / IV_0) – 1] * 100$. The ending period index value, for purposes of calculating the Index value, on any date is determined by adding the market values of the underlier stocks, which are derived by multiplying the primary closing price of each stock by the number of available shares, to arrive at the total market capitalization of the 2,000 stocks.

Constituent stocks of the Index are weighted in the Index by their free-float market capitalization, which is calculated by multiplying the primary closing price by the number of free-float shares. Free-float shares are shares that are available to the public for purchase as determined by FTSE Russell. FTSE Russell determines shares available to the public for purchase based on information recorded in corporate filings with the SEC and other reliable sources in the event of missing or questionable data. FTSE Russell removes the following types of shares from total market capitalization to arrive at free-float market capitalization:

Officers and directors' holdings — shares held by officers and directors.

Large private holdings — shares held by an individual, a group of individuals acting together or a corporation (that is included in the Index) if such holdings constitute 10% or more of the shares outstanding.

Institutional holdings — shares held by investment companies, partnerships, insurance companies, mutual funds or banks are excluded if the holding is greater than 30%. If a firm has a direct relationship to the company, such as board representation, they are considered strategic holdings and excluded regardless of the size of holding per the officers and directors' exclusion rule.

Publicly listed companies — shares held by publicly listed companies. Holdings considered as Institutional will be considered as available unless the 30% threshold is surpassed, regardless of listing.

ESOP or LESOP shares — shares held by employee stock ownership plans and leveraged employee stock ownership plans.

Initial public offering lock-ups — shares locked-up during an initial public offering are not available to the public and will be excluded from the market value at the time the initial public offering enters the Index.

Government holdings — shareholdings listed as "government of." Shares held by government investment boards and/or investment arms are treated like shares held by large private shareholdings and are excluded if the number of shares is greater than 10% of outstanding shares. Shares held by a government pension plan are considered institutional holdings and will not be excluded unless the holding is greater than 30%.

Corporate Actions Affecting the Index

FTSE Russell adjusts the Index on a daily basis in response to certain corporate actions and events. Therefore, a company's membership in the Index and its weight in the Index can be impacted by these corporate actions. The adjustment is applied based on sources of public information, including press releases and SEC filings. Prior to the completion of a corporate action or event, FTSE Russell estimates the effective date. FTSE Russell will then adjust the anticipated effective date based on public information until the date is considered final. Depending on the time on a given day that an action is determined to be final, FTSE Russell will generally either (1) apply the action before the open on the ex-date or (2) apply the action after providing appropriate notice to its clients regarding the impact of the action and the effective date. FTSE Russell applies the following methodology guidelines when adjusting the Index in

response to corporate actions and events:
"No Replacement" Rule — Securities that are deleted from the Index between reconstitution dates, for any reason (e.g., mergers, acquisitions or other similar corporate activity) are not replaced. Thus, the number of securities in the Index over the past year will fluctuate according to corporate activity.
Mergers and Acquisitions — Between constituents: When mergers and acquisitions take place between companies that are both constituents of a Russell index, the target company is deleted and its market capitalization simultaneously moves to the acquiring company's stock. In the absence of an active market for the target company at the time of index implementation, the target company will be deleted from the Index using a synthetic price based on the offer terms. Given sufficient market hours after confirmation, FTSE Russell effects this action after the close on the last day of trade of the target company, or at an appropriate time once the transaction has been deemed to be final (implementation may occur prior to the last day of trade to avoid potential delays with the associated synthetic pricing).
Between a constituent and a non-constituent: If the target company is a member of the Index, it is deleted from the Index after FTSE Russell determines that the action or event is final. If the acquiring company is a member of the Index, its shares are adjusted by adding the target company's market capitalization (if the increase in shares is greater than 5%). If the target company is not a member of a

Russell index shares of the acquiring company will remain unchanged. If a non-index member acquires an index member, the acquired member will be deleted from the Index once the action is final.
Reincorporation — Members of the Index that reincorporate to another country and continue to trade in the United States and companies that reincorporate to the United States during the year are analyzed for assignment by FTSE Russell during annual reconstitution. Members that reincorporate in another country and no longer trade in the United States are immediately deleted from the Russell U.S. indices.
Reclassification of shares (pricing vehicles) — Pricing vehicles will not be assessed or changed outside of a reconstitution period unless the existing class ceases to exist. In the event of extenuating circumstances signaling a necessary pricing vehicle change, proper notification will be made.
Rights Offerings — Rights offered to shareholders are reflected in the Index only if the subscription price of the rights is at a discount to the market price. Provided that FTSE Russell has been alerted to the rights offer prior to the ex-date, it will adjust the price of the stock for the value of the rights and increased shares according to the terms of the offering before the open on the ex-date. Where the Rights Issue / Entitlement offer subscription price remains unconfirmed on the ex-date, an estimated price will be used. FTSE Russell will estimate the subscription price using the value being raised and the offer terms. This treatment applies for both transferable and non-transferable rights. Rights issued as part of a poison pill arrangement or entitlements that give shareholders the right to purchase ineligible securities such as convertible debt are excluded from this treatment.
Changes to Shares Outstanding — Changes to shares outstanding due to buybacks (including Dutch auctions), secondary offerings, and other potential changes are generally updated at the end of each month. FTSE Russell only applies month-end changes to available shares outstanding if the cumulative change in the number of shares outstanding is greater than 5%. Share changes that are confirmed by their vendors and verified by FTSE Russell by use of an SEC filing at least six days prior to month end are implemented and communicated to clients who subscribe at the Premier level five trading days prior to month end. The float factor last determined (either at reconstitution or due to a corporate action implementation) is applied to the new shares. No such changes are made in June due to the most recent annual reconstitution. Month-end changes in November and December will be processed as one event after the close on the third Friday of each December along with fourth quarter initial public offerings additions due to low liquidity in the financial markets at the end of the year and the proximity of a separate November month-end process.
Spin-offs — Spin-offs will be valued using an estimate prior to ex-date. When a spin-off results in an eligible security type being listed on an eligible exchange, the spin-off company will remain in the Index until the next index review, regardless of size. When an index constituent spins off an ineligible security type or the spin-off company is listed on an ineligible exchange only, the security will be added to the Index on the ex-date and subsequently removed with notice at market price once "regular way" trade has commenced.
Tender Offers — A company acquired as a result of a cash tender offer is removed if (i) Where offer acceptances are below 90%, there is reason to believe that the remaining free float is under 5% based on information available at the time; or (ii) Following completion of the offer the acquirer has stated intent to finalize the acquisition via a short-form merger, squeeze-out, top-up option or any other compulsory mechanism; or (iii) Offer acceptances reach 90% (initial, extension or subsequent); and (iv) Shareholders have validly tendered and the shares have been irrevocably accepted for payment; and all pertinent offer conditions have been reasonably met and the acquirer has not explicitly stated that it does not intend to acquire the remaining shares.
Voluntary Exchange Offers — A publicly traded company may offer to exchange or split-off some or all of its ownership in a separate publicly traded company. Once the offer expires, FTSE Russell will decrease the available shares in the offering company, and increase the available shares of 'split-off' company, based on the results of the offering. FTSE Russell will effect this change based on, but not limited to, preliminary results, company filings, and exchange notices.
Bankruptcy and Voluntary Liquidations — Companies that file for a Chapter 7 liquidation bankruptcy or have filed a liquidation plan will be removed from the Index at the time of the bankruptcy filing; whereas companies filing for a Chapter 11 reorganization bankruptcy will remain a member of the Index, unless the company is de-listed from the primary exchange, in which case normal de-listing rules apply. If a company files for bankruptcy, is delisted and it can be confirmed that it will not trade OTC, FTSE Russell may remove the stock at a nominal price of $0.0001.

Stock Distributions — A price adjustment for stock distributions is applied on the ex-date of the distribution. When the number of shares for the distribution is fixed, FTSE Russell increases the number of shares on the ex-date. When the number of shares is an undetermined amount based on future earnings and profits, FTSE Russell increases the number of shares on the pay-date.

Dividends — FTSE Russell includes gross dividends in the daily total return calculation of the Index on the basis of their ex-dates. If a dividend is payable in stock and cash and the number of shares to be issued cannot be determined by the ex-date, the dividend is treated as all cash. Regular cash dividends are reinvested across the Index at the close on the dividend ex-date, while special cash dividends are subtracted from the price of the stock before the open on the ex-date.

Halted Securities — Halted securities are not removed from the Index until the time they are actually delisted from the exchange. If a security is halted and declared bankrupt without any indication of compensation to shareholders, the last traded price will be adjusted down to zero value and it will subsequently be removed from the Index with T+2 notice. In all other cases, the security will continue to be included in the Index for a period of up to 20 business days at its last traded price. If the security continues to be suspended at the end of a period of up to 20 business days, FTSE Russell will review it to decide whether to remove it at zero value, repeating such review as applicable at successive 20 business day intervals until trading recommences or specified time limits expire and the security is removed.

The following graph shows the daily historical performance of the Index in the period from January 1, 2008 through June 28, 2018. We obtained this historical data from Bloomberg L.P. We have not independently verified the accuracy or completeness of the information obtained from Bloomberg L.P. On the pricing date, the closing level of the Index was 1,645.017.

Historical Performance of the Index

This historical data on the Index is not necessarily indicative of the future performance of the Index or what the value of the notes may be. Any historical upward or downward trend in the level of the Index during any period set forth above is not an indication that the level of the Index is more or less likely to increase or decrease at any time over the term of the notes.

Before investing in the notes, you should consult publicly available sources for the levels of the Index.

License Agreement

FTSE Russell has entered into a non-exclusive license agreement with us, granting us, and certain of our affiliates, in exchange for a fee, permission to use the Index in connection with the offer and sale of the notes. We are not affiliated with FTSE Russell; the only relationship between FTSE Russell and us is the licensing of the use of the Russell 2000® Index (a trademark of FTSE Russell) and trademarks relating to the Index. We do not accept any responsibility for the calculation, maintenance or publication of the Index or any successor index.

The notes are not sponsored, endorsed, sold or promoted by FTSE Russell. FTSE Russell makes no representation or warranty, express or implied, to the owners of the notes or any member of the public regarding the advisability of investing in securities generally or in the notes particularly or the ability of the Index to track general stock market performance or a segment of the same.

FTSE Russell's publication of the Index in no way suggests or implies an opinion by FTSE Russell as to the advisability of investment in any or all of the securities upon which the Index is based. FTSE Russell's only relationship to us is the licensing of certain trademarks and trade names of FTSE Russell and of the Index which is determined, composed and calculated by FTSE Russell without regard to us or the notes. FTSE Russell is not responsible for and has not reviewed the notes nor any associated literature or publications and FTSE Russell makes no representation or warranty express or implied as to their accuracy or completeness, or otherwise. FTSE Russell reserves the right, at any time and without notice, to alter, amend, terminate or in any way change the Index. FTSE Russell has no obligation or liability in connection with the administration, marketing or trading of the notes.

FTSE RUSSELL DOES NOT GUARANTEE THE ACCURACY AND/OR THE COMPLETENESS OF THE RUSSELL 2000® INDEX OR ANY DATA INCLUDED THEREIN AND FTSE RUSSELL SHALL HAVE NO LIABILITY FOR ANY ERRORS, OMISSIONS, OR INTERRUPTIONS THEREIN. FTSE RUSSELL MAKES NO WARRANTY, EXPRESS OR IMPLIED, AS TO RESULTS TO BE OBTAINED BY US, INVESTORS, HOLDERS OF THE NOTES, OR ANY OTHER PERSON OR ENTITY FROM THE USE OF THE RUSSELL 2000® INDEX OR ANY DATA INCLUDED THEREIN. FTSE RUSSELL MAKES NO EXPRESS OR IMPLIED WARRANTIES, AND EXPRESSLY DISCLAIMS ALL WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE WITH RESPECT TO THE RUSSELL 2000® INDEX OR ANY DATA INCLUDED THEREIN. WITHOUT LIMITING ANY OF THE FOREGOING, IN NO EVENT SHALL FTSE RUSSELL HAVE ANY LIABILITY FOR ANY SPECIAL, PUNITIVE, INDIRECT, OR CONSEQUENTIAL DAMAGES (INCLUDING LOST PROFITS), EVEN IF NOTIFIED OF THE POSSIBILITY OF SUCH DAMAGES.

Accelerated Return Notes®
Linked to the Russell 2000® Index, due August 30, 2019

Supplement to the Plan of Distribution

Under our distribution agreement with MLPF&S, MLPF&S will purchase the notes from us as principal at the public offering price indicated on the cover of this term sheet, less the indicated underwriting discount.

We will deliver the notes against payment therefor in New York, New York on a date that is greater than two business days following the pricing date. Under Rule 15c6-1 of the Securities Exchange Act of 1934, trades in the secondary market generally are required to settle in two business days, unless the parties to any such trade expressly agree otherwise. Accordingly, purchasers who wish to trade the notes more than two business days prior to the original issue date will be required to specify alternative settlement arrangements to prevent a failed settlement.

The notes will not be listed on any securities exchange. In the original offering of the notes, the notes will be sold in minimum investment amounts of 100 units. If you place an order to purchase the notes, you are consenting to MLPF&S acting as a principal in effecting the transaction for your account.

MLPF&S may repurchase and resell the notes, with repurchases and resales being made at prices related to then-prevailing market prices or at negotiated prices, and these prices will include MLPF&S's trading commissions and mark-ups. MLPF&S may act as principal or agent in these market-making transactions; however, it is not obligated to engage in any such transactions. At MLPF&S's discretion, for a short, undetermined initial period after the issuance of the notes, MLPF&S may offer to buy the notes in the secondary market at a price that may exceed the initial estimated value of the notes. Any price offered by MLPF&S for the notes will be based on then-prevailing market conditions and other considerations, including the performance of the Index and the remaining term of the notes. However, none of us, MLPF&S, or any of our respective affiliates is obligated to purchase your notes at any price or at any time, and we cannot assure you that we, MLPF&S or any of our respective affiliates will purchase your notes at a price that equals or exceeds the initial estimated value of the notes.

The value of the notes shown on your account statement produced by MLPF&S will be based on MLPF&S's estimate of the value of the notes if MLPF&S or another of its affiliates were to make a market in the notes, which it is not obligated to do. That estimate will be based upon the price that MLPF&S may pay for the notes in light of then-prevailing market conditions, and other considerations, as mentioned above, and will include transaction costs. At certain times, this price may be higher than or lower than the initial estimated value of the notes.

The distribution of the Note Prospectus in connection with these offers or sales will be solely for the purpose of providing investors with the description of the terms of the notes that was made available to investors in connection with their initial offering. Secondary market investors should not, and will not be authorized to, rely on the Note Prospectus for information regarding BNS or for any purpose other than that described in the immediately preceding sentence.

Structuring the Notes

The notes are our unsecured senior debt securities, the return on which is linked to the performance of the Index. As is the case for all of our debt securities, including our market-linked notes, the economic terms of the notes reflect our actual or perceived creditworthiness at the time of pricing. The internal funding rate we use in pricing the market-linked note is typically lower than the rate we would pay when we issue conventional fixed-rate debt securities of comparable maturity. This generally relatively lower internal funding rate, which is reflected in the economic terms of the notes, along with the fees and charges associated with market-linked notes, resulted in the initial estimated value of the notes on the pricing date being less than their public offering price.

At maturity, we are required to pay the Redemption Amount to holders of the notes, which will be calculated based on the performance of the Index and the $10 per unit principal amount. In order to meet these payment obligations, at the time we issue the notes, we may choose to enter into certain hedging arrangements (which may include call options, put options or other derivatives) with MLPF&S or one of its affiliates. The terms of these hedging arrangements are determined by seeking bids from market participants, including MLPF&S and its affiliates, and take into account a number of factors, including our creditworthiness, interest rate movements, the volatility of the Index, the tenor of the notes and the tenor of the hedging arrangements. The economic terms of the notes and their initial estimated value depend in part on the terms of these hedging arrangements.

MLPF&S has advised us that the hedging arrangements will include a hedging related charge of approximately $0.075 per unit, reflecting an estimated profit to be credited to MLPF&S from these transactions. Since hedging entails risk

and may be influenced by unpredictable market forces, additional profits and losses from these hedging arrangements may be realized by MLPF&S or any third party hedge providers.
For further information, see "Risk Factors—General Risks Relating to ARNs" beginning on page PS-6 and "Use of Proceeds and Hedging" on page PS-16 of product prospectus supplement EQUITY INDICES ARN-1.
Summary of Canadian Federal Income Tax Consequences
An investor should read carefully the description of principal Canadian federal income tax considerations under "Canadian Taxation" in the accompanying prospectus relevant to a holder (as defined on page 19 of the prospectus) owning debt securities, and the description

of principal Canadian federal income tax considerations under "Supplemental Discussion of Canadian Federal Income Tax Consequences" in the applicable product prospectus supplement.

Summary of U.S. Federal Income Tax Consequences

The following is a general description of certain U.S. federal tax considerations relating to the notes. Prospective purchasers of the notes should consult their tax advisors as to the consequences under the tax laws of the country of which they are residents for tax purposes and the tax laws of the U.S. of acquiring, holding and disposing of the notes and receiving payments under the notes. This summary is based upon the law as in effect on the date of this pricing supplement and is subject to any change in law that may take effect after such date.

We urge you to read the more detailed discussion in the "Supplemental Discussion of U.S. Federal Income Tax Consequences" section beginning on page PS-27 of product prospectus supplement EQUITY INDICES ARN-1.

No statutory, regulatory, judicial or administrative authority directly discusses how the notes should be treated for U.S. federal income tax purposes. As a result, the U.S. federal income tax consequences of your investment in the notes are uncertain. Accordingly, we urge you to consult your tax advisor as to the tax consequences of your investment in the notes (and of having agreed to the required tax treatment of your notes described below) and as to the application of state, local or other tax laws to your investment in your notes and the possible effects of changes in federal or other tax laws.

Pursuant to the terms of the notes, BNS and you agree, in the absence of a statutory or regulatory change or an administrative or judicial ruling to the contrary, to characterize your notes as a pre-paid derivative contract with respect to the Index. If your notes are so treated, you should generally recognize long-term capital gain or loss if you hold your notes for more than one year (and otherwise, short-term capital gain or loss) upon the taxable disposition of your notes in an amount equal to the difference between the amount you receive at such time and the amount you paid for your notes. The deductibility of capital losses is subject to limitations.

In the opinion of our counsel, Cadwalader, Wickersham & Taft LLP, it would be reasonable to treat your notes in the manner described above. However, because there is no authority that specifically addresses the tax treatment of the notes, it is possible that your notes could alternatively be treated for tax purposes as a single contingent payment debt instrument or pursuant to some other characterization, such that the timing and character of your income from the notes could differ materially from the treatment described above.

Notice 2008-2. In 2007, the Internal Revenue Service (the "IRS") released a notice that may affect the taxation of holders of the notes. According to the notice, the IRS and the U.S. Treasury Department (the "Treasury") are actively considering whether a holder of an instrument such as the notes should be required to accrue ordinary income on a current basis, and they are seeking taxpayer comments on the subject. It is not possible to determine what guidance they will ultimately issue, if any. It is possible, however, that under such guidance, holders of the notes will ultimately be required to accrue income currently and this could be applied on a retroactive basis. The IRS and the Treasury are also considering other relevant issues, including whether additional gain or loss from such instruments should be treated as ordinary or capital, whether foreign holders of such instruments should be subject to withholding tax on any deemed income accruals, and whether the special "constructive ownership rules" of Section 1260 of the Internal Revenue Code of 1986, as amended (the "Code") should be applied to such instruments.

Medicare Tax on Net Investment Income. U.S. holders that are individuals or estates and certain trusts are subject to an additional 3.8% tax on all or a portion of their "net investment income," or "undistributed net investment income" in the case of an estate or trust, which may include any income or gain with respect to the notes, to the extent of their net investment income or undistributed net investment income (as the case may be) that, when added to their other modified adjusted gross income, exceeds $200,000 for an unmarried individual, $250,000 for a married taxpayer filing a joint return (or a surviving spouse), $125,000 for a married individual filing a separate return or the dollar amount at which the highest tax bracket begins for an estate or trust. The 3.8% Medicare tax is determined in a different manner than the regular income tax. U.S. holders should consult their advisors with respect to the 3.8% Medicare tax.

Specified Foreign Financial Assets. U.S. holders may be subject to reporting obligations with respect to their notes if they do not hold their notes in an account maintained by a financial institution and the aggregate value of their notes and certain other "specified foreign financial assets" (applying certain attribution rules) exceeds an applicable threshold. Significant penalties can apply if a U.S. holder is required to disclose its notes and fails to do so.

Backup Withholding and Information Reporting. The proceeds received from a taxable disposition of the notes will be subject to information reporting unless you are an "exempt recipient" and may also be subject to backup withholding at the rate specified in the Code if you fail to provide certain identifying information (such as an accurate taxpayer number, if you are a U.S. holder) or meet certain other conditions.

Amounts withheld under the backup withholding rules are not additional taxes and may be refunded or credited against your U.S. federal income tax liability, provided the required information is furnished to the IRS.

Non-U.S. Holders. This section applies only if you are a non-U.S. holder. For these purposes, you are a non-U.S. holder if you are the beneficial owner of the notes and are, for U.S. federal income tax purposes:

a non-resident alien individual;

a foreign corporation; or

an estate or trust that, in either case, is not subject to U.S. federal income tax on a net income basis on income or gain from the notes.

If you are a non-U.S. holder, subject to Section 871(m) of the Code and FATCA, discussed below, you should generally not be subject to generally applicable information reporting and backup withholding requirements with respect to payments on your notes if you comply with certain certification and identification requirements as to your foreign status including providing us (and/or the applicable withholding agent) a properly executed and fully completed applicable IRS Form W-8. Subject to Section 897 of the Code and Section 871(m) of the Code discussed below, gain from the taxable disposition of the notes or settlement at maturity generally will not be subject to U.S. tax unless (i) such gain is effectively connected with a trade or business conducted by you in the U.S., (ii) you are a non-resident alien individual and are present in the U.S. for 183 days or more during the taxable year of such sale, exchange or settlement and certain other conditions are satisfied, (iii) you fail to provide the relevant, correct, completed and executed IRS Form W-8 or (iv) you have certain other present or former connections with the U.S.

Section 897. We will not attempt to ascertain whether the issuer of any underlying equity constituent of the Index would be treated as a "United States real property holding corporation" ("USRPHC") within the meaning of Section 897 of the Code. We also have not attempted to determine whether the notes should be treated as "United States real property interests" ("USRPI") as defined in Section 897 of the Code. If an issuer of any underlying equity constituent of the Index or the notes were so treated, certain adverse U.S. federal income tax consequences could possibly apply, including subjecting any gain realized by a non-U.S. holder in respect of the notes upon a taxable disposition (including cash settlement) of the notes to U.S. federal income tax on a net basis, and the proceeds from such a taxable disposition to a withholding tax. Non-U.S. holders should consult their tax advisors regarding the potential treatment of any underlying equity constituent for their notes as a USRPHC or the notes as USRPI.

Section 871(m). A 30% withholding tax (which may be reduced by an applicable income tax treaty) is imposed under Section 871(m) of the Code on certain "dividend equivalents" paid or deemed paid to a non-U.S. holder with respect to a "specified equity-linked instrument" that references one or more dividend-paying U.S. equity securities or indices containing U.S. equity securities. The withholding tax can apply even if the instrument does not provide for payments that reference dividends. Treasury regulations provide that the withholding tax applies to all dividend equivalents paid or deemed paid on specified equity-linked instruments that have a delta of one ("delta one specified equity-linked instruments") issued after 2016 and to all dividend equivalents paid or deemed paid on all other specified equity-linked instruments issued after 2018.

Based on our determination that the notes are not "delta-one" with respect to the Index or any U.S. Index components our counsel is of the opinion that the notes should not be delta one specified equity-linked instruments and thus should not be subject to withholding on dividend equivalents. Our determination is not binding on the IRS, and the IRS may disagree with this determination. Furthermore, the application of Section 871(m) of the Code will depend on our determinations made upon issuance of the notes. If withholding is required, we will not make payments of any additional amounts.

Nevertheless, after issuance, it is possible that your notes could be deemed to be reissued for tax purposes upon the occurrence of certain events affecting the Index or Index components or your notes, and following such occurrence your notes could be treated as delta one specified equity-linked instruments that are subject to withholding on dividend equivalents. It is also possible that withholding tax or other tax under Section 871(m) of the Code could apply to the notes under these rules if you enter, or have entered, into certain other transactions in respect of the Index or Index components or the notes. If you enter, or have entered, into other transactions in respect of the Index or Index components or the notes, you should consult your tax advisor regarding the application of Section 871(m) of the Code to your notes in the context of your other transactions.

Because of the uncertainty regarding the application of the 30% withholding tax on dividend equivalents to the notes, you are urged to consult your tax advisor regarding the potential application of Section 871(m) of the Code and the 30% withholding tax to an investment in the notes.

U.S. Federal Estate Tax Treatment of Non-U.S. Holders. A note may be subject to U.S. federal estate tax if an individual non-U.S. holder holds the note at the time of his or her death. The gross estate of a non-U.S. holder domiciled outside the U.S. includes only property situated in the U.S. Individual non-U.S. holders should consult their

tax advisors regarding the U.S. federal estate tax consequences of holding the notes at death.
FATCA. The Foreign Account Tax Compliance Act ("FATCA") was enacted on March 18, 2010, and imposes a 30% U.S. withholding tax on "withholdable payments" (i.e., certain U.S.-source payments, including interest (and original issue discount), dividends, other fixed or determinable annual or periodical gain, profits, and income, and on the gross proceeds from a disposition of property of a type which can produce U.S.-source interest or dividends) and "passthru payments" (i.e., certain payments attributable to withholdable payments) made to certain foreign financial institutions (and certain of their affiliates) unless the payee foreign financial institution agrees (or is required), among other things, to disclose the identity of any U.S. individual with an account at the institution (or the relevant affiliate) and to annually report certain information about such account. FATCA also requires withholding agents making withholdable payments to certain foreign entities that do not disclose the name, address, and taxpayer identification number of any substantial U.S. owners (or do not certify that they do not have any substantial U.S. owners) to withhold tax at a rate of 30%. Under certain circumstances, a holder may be eligible for refunds or credits of such taxes.
Pursuant to final and temporary Treasury regulations and other IRS guidance, the withholding and reporting requirements under FATCA will generally apply to certain "withholdable payments" made on or after July 1, 2014, certain gross proceeds on a sale or disposition occurring after December 31, 2018, and certain foreign passthru payments made after December 31, 2018 (or, if later, the date that final regulations defining the term "foreign passthru payment" are published). If withholding is required, we (or the applicable paying agent) will not be required to pay additional amounts with respect to the amounts so withheld. Foreign financial institutions and non-

financial foreign entities located in jurisdictions that have an intergovernmental agreement with the U.S. governing FATCA may be subject to different rules.

Investors should consult their own advisors about the application of FATCA, in particular if they may be classified as financial institutions (or if they hold their notes through a non-U.S. entity) under the FATCA rules.

Both U.S. and non-U.S. holders should consult their tax advisors regarding the U.S. federal income tax consequences of an investment in the notes, as well as any tax consequences arising under the laws of any state, local or non-U.S. taxing jurisdiction (including that of BNS).

Validity of the Notes

In the opinion of Cadwalader, Wickersham & Taft LLP, as special counsel to the issuer, when the notes offered by this term sheet have been executed and issued by the issuer and authenticated by the trustee pursuant to the indenture and delivered, paid for and sold as contemplated herein, the notes will be valid and binding obligations of the issuer, enforceable against the issuer in accordance with their terms, subject to applicable bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium, receivership or other laws relating to or affecting creditors' rights generally, and to general principles of equity (regardless of whether enforcement is sought in a proceeding at law or in equity). This opinion is given as of the date hereof and is limited to the laws of the State of New York. Insofar as this opinion involves matters governed by Canadian law, Cadwalader, Wickersham & Taft LLP has assumed, without independent inquiry or investigation, the validity of the matters opined on by Osler, Hoskin & Harcourt LLP, Canadian legal counsel for the issuer, in its opinion expressed below. In addition, this opinion is subject to customary assumptions about the trustee's authorization, execution and delivery of the indenture and, with respect to the Securities, authentication of the Securities and the genuineness of signatures and certain factual matters, all as stated in the opinion of Cadwalader, Wickersham & Taft LLP dated January 18, 2017 filed with the Securities and Exchange Commission as Exhibit 5.3 to the Registration Statement on Form F-3 on January 18, 2017.

In the opinion of Osler, Hoskin & Harcourt LLP, the issue and sale of the notes has been duly authorized by all necessary corporate action of BNS in conformity with the Indenture, and when the notes have been duly executed, authenticated and issued in accordance with the Indenture, the notes will be validly issued and, to the extent validity of the notes is a matter governed by the laws of the Province of Ontario, or the laws of Canada applicable therein, and will be valid obligations of BNS, subject to the following limitations (i) the enforceability of the Indenture may be limited by the Canada Deposit Insurance Corporation Act (Canada), the Winding-up and Restructuring Act (Canada) and bankruptcy, insolvency, reorganization, receivership, moratorium, arrangement or winding-up laws or other similar laws affecting the enforcement of creditors' rights generally; (ii) the enforceability of the Indenture may be limited by equitable principles, including the principle that equitable remedies such as specific performance and injunction may only be granted in the discretion of a court of competent jurisdiction; (iii) pursuant to the Currency Act (Canada) a judgment by a Canadian court must be awarded in Canadian currency and that such judgment may be based on a rate of exchange in existence on a day other than the day of payment; and (iv) the enforceability of the Indenture will be subject to the limitations contained in the Limitations Act, 2002 (Ontario), and such counsel expresses no opinion as to whether a court may find any provision of the Indenture to be unenforceable as an attempt to vary or exclude a limitation period under that Act. This opinion is given as of the date hereof and is limited to the laws of the Province of Ontario and the federal laws of Canada applicable thereto. In addition, this opinion is subject to customary assumptions about the Trustees' authorization, execution and delivery of the Indenture and the genuineness of signatures and certain factual matters, all as stated in the letter of such counsel dated January 18, 2017, which has been filed as Exhibit 5.2 to BNS's Form F-3 filed with the SEC on January 18, 2017.

Where You Can Find More Information

We have filed a registration statement (including a product prospectus supplement, a prospectus supplement, a prospectus addendum and a prospectus) with the SEC for the offering to which this term sheet relates. Before you invest, you should read the Note Prospectus, including this term sheet, and the other documents that we have filed with the SEC, for more complete information about us and this offering. You may get these documents without cost by visiting EDGAR on the SEC website at www.sec.gov. Alternatively, we, any agent, or any dealer participating in this offering will arrange to send you these documents if you so request by calling MLPF&S toll-free at 1-800-294-1322.

Market-Linked Investments Classification

MLPF&S classifies certain market-linked investments (the "Market-Linked Investments") into categories, each with different investment characteristics. The following description is meant solely for informational purposes and is not intended to represent any particular Enhanced Return Market-Linked Investment or guarantee any performance.

Enhanced Return Market-Linked Investments are short- to medium-term investments that offer you a way to enhance exposure to a particular market view without taking on a similarly enhanced level of market downside risk. They can be especially effective in a flat to moderately positive market (or, in the case of bearish investments, a flat to moderately negative market). In exchange for the potential to receive better-than market returns on the linked asset, you must generally accept market downside risk and capped upside potential.

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As these investments are not market downside protected, and do not assure full repayment of principal at maturity, you need to be prepared for the possibility that you may lose all or part of your investment.
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odwill impairments occurring after the initial adoption of the amendments should be included in earnings. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In December 2010, FASB issued ASU No. 2010-29, *Business Combinations (Topic 805): Disclosure of Supplementary Pro Forma Information for Business Combinations.* The amendments in this Update specify that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The amendments also expand the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments in this Update are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The Company intends to adopt the disclosure requirements for any business combinations in 2011and thereafter.

On March 5, 2010, the FASB issued ASU No. 2010-11 Derivatives and Hedging Topic 815 "Scope Exception Related to Embedded Credit Derivatives." This ASU clarifies the guidance within the derivative literature that exempts certain credit related features from analysis as potential embedded derivatives requiring separate accounting. The ASU specifies that an embedded credit derivative feature related to the transfer of credit risk that is only in the form of subordination of one financial instrument to another is not subject to bifurcation from a host contract under ASC 815-15-25, Derivatives and Hedging — Embedded Derivatives — Recognition. All other embedded credit derivative features should be analyzed to determine whether their economic characteristics and risks are "clearly and closely related" to the economic characteristics and risks of the host contract and whether bifurcation is required. The ASU is effective for the Company on July 1, 2010. Early adoption is permitted. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In January 2010, FASB issued ASU No. 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements.* This update provides amendments to ASC Topic 820 that will provide more robust disclosures about (1) the different classes of assets and liabilities measured at fair value, (2) the valuation techniques and inputs used, (3) the activity in Level 3 fair value measurements, and (4) the transfers between Levels 1, 2, and 3. This standard is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In January 2010, FASB issued ASU N0. 2010-01, *Equity (Topic 505): Accounting for Distributions to Shareholders with Components of Stock and Cash.* The update clarifies that the stock portion of a distribution to shareholders that allows them to elect to receive cash or stock with a potential limitation on the total amount of cash that all shareholders can elect to receive in the aggregate is considered a share issuance that is reflected prospectively in earnings per share and is not considered a stock dividend for purposes of ASC Topic 505 and Topic 260, *Earnings Per Share*. This standard is effective for interim and annual periods ending on or after December 15, 2009, and should be applied on a retrospective basis. The adoption of this standard did not have a material impact to the Company's financial position or results of operations.

3. NET INVESTMENT IN SALES-TYPE LEASES

Under sales-type leases, Shanghai TCH leased TRT systems to Xingtai and Zhangzhi with terms of five and thirteen years, respectively and leased CHPG systems to Tong Chuan Shengwei and Jin Yang Shengwei respectively for five years, WGPG systems to Shenmu for ten years, BMPG systems to Pucheng for fifteen years, and a power and steam generating system from waste heat from metal refining to Erdos for twenty years. The components of the net investment in sales-type leases as of March 31, 2011 and December 31, 2010 are as follows:

	2011	2010
Total future minimum lease payments receivable	$420,879,568	$379,641,671
Less: executory cost	(112,327,484)	(99,866,170)
Less: unearned interest income	(172,385,526)	(154,564,733)
Net investment in sales - type leases	136,166,558	125,210,768
Current portion	8,046,236	7,624,637
Noncurrent portion	$128,120,322	$117,586,131

As of March 31, 2011, the future minimum rentals to be received on non-cancelable sales-type leases by years are as follows:

2012	$36,944,340
2013	35,218,714
2014	34,406,765
2015	28,246,325
2016	27,163,098
Thereafter	258,900,326
Total	$420,879,568

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4. RESTRICTED CASH, NOTES PAYABLE – BANK ACCEPTANCES

Restricted cash as of March 31, 2011 and December 31, 2010 was $0 and $2,151,690, respectively, held by the bank as collateral to issue bank acceptances. The Company endorses bank acceptances to vendors as payment of their own obligations. Most of the bank acceptances have maturities of less than six months. As of March 31, 2011 and December 31, 2010, the Company had bank acceptances of $0 and $2,868,921, respectively.

5. PREPAID EXPENSES

Prepaid expenses mainly consisted of prepayment for supplies, office rental, parking space, insurance and legal fees.

6. CONSTRUCTION IN PROGRESS

"Construction in progress" is the amount paid for constructing power generation systems. During the first quarter of 2011, Erdos power generation system Phase II, the third 9MW Capacity Electricity power generation system was completed and put into operation. At March 31, 2011, the Company had paid approximately $18.19 million for Phase III of the Erdos TCH power generation system projects, and $5.34 million for Shannxi Datong Coal Group Power Generation project (See Note 20). The Company was committed to pay additional $0.72 million for Phase III projects excluding quality deposits of $120,000 in 2011, and $22.12 million for Shannxi Datong Coal Group Power Generation project.

7. TAXES PAYABLE

"Taxes payable" consisted of the following at March 31, 2011 and December 31, 2010:

	2011	2010
Income tax	$1,004,657	$1,237,823
Business tax	203,304	347,654
Other taxes	24,702	46,423
	$1,232,663	$1,631,900

8. ACCRUED LIABILITIES AND OTHER PAYABLES

“Accrued liabilities and other payables” consisted of the following as of March 31, 2011 and December 31, 2010:

	2011	2010
Employee training, labor union expenditure and social insurance payable	$247,497	$245,019
Consulting and legal expenses	372,679	541,638
Payable to Yingfeng	1,705,243	1,730,451
Payable to Pucheng	289,793	286,892
Accrued payroll and welfare	258,238	259,120
Accrued system maintenance expense	73,142	72,409
Other	17,783	25,421
Total	$2,964,375	$3,160,950

“Payable to Yingfeng” is the cost of obtaining the ownership of two TRT projects (Zhangzhi and Xingtai) that were previously owned by Yingfeng. This amount is non-interest bearing and is payable on demand. “Payable to Pucheng” is the deposit for rental payments by Pucheng.

9. ADVANCE FROM RELATED PARTY, NET

As of March 31, 2011, “Advance from related party” was $2,056,233, including $1,342,200 from Erdos (the minority shareholder of Erdos TCH) as an advance for the capital needs of Erdos TCH, and $725,000 advance from a shareholder of the Company with no interest, payable on demand, reduced by $10,967 which was the quick advance the Company made to its manager. At December 31, 2010, “Advance from related party” was $1,365,877, including $1,328,763 from Erdos (the minority shareholder of Erdos TCH) as an advance for the capital needs of Erdos TCH and a $37,114 payment by the Company’s management for paying certain operating expenses on behalf of the Company.

10. NONCONTROLLING INTEREST

"Non-controlling interest" was a 7% equity interest of Erdos JV owned by Erdos Metallurgy Co., Ltd. According to Xi'an TCH and Erdos' agreement on profit distribution, Xi'an TCH and Erdos will receive 80% and 20% of the profit from the JV, respectively, until Xi'an TCH has received a complete return on its investment. Xi'an TCH and Erdos will then receive 60% and 40% of the profit from the JV, respectively.

As of March 31, 2011, the total registered capital of Erdos JV is RMB 120,000,000 ($17.55 million), of which, $16.37 million (RMB112 million) was contributed by Xi'an TCH and $1.18 million (RMB 8 million) was from Erdos. Erdos TCH engages in a business similar to that of Xi'an TCH.

Erdos TCH allocates its income to Xi'an TCH and Erdos at a proportion of 80% and 20% based on net income calculated under Chinese GAAP. The main difference between US GAAP and Chinese GAAP with respect to Erdos is that the Erdos agreement is treated as a sales-type lease under US GAAP and as an operating lease under Chinese GAAP. The following is the profit and loss statement of Erdos TCH, prepared under Chinese GAAP for the three months ended March 31, 2011:

Net Revenue	$2,834,715
Cost of Revenue	(1,626,852)
Gross Profit	1,207,863
Operating expenses	8,251
Income from operations	1,199,612
Non-operating income	1,057
Income tax expense	(300,167)
Net Income	$900,502

The following is a reconciliation of net income per Chinese GAAP to net income per US GAAP:

Net income per Chinese GAAP	$900,502
Adjustments under US GAAP	
Revenue per sales-type lease	8,498,505
Cost of revenue	(7,048,919)
Income from operation	2,350,088
Interest income	808,888
Income before income tax	3,158,976
Deferred income tax expense	(563,287)

Net income per US GAAP	$2,595,689

The following is the balance sheet of Erdos TCH, prepared under Chinese GAAP at March 31, 2011:

Assets	
Cash and equivalents	$3,115,711
Other current assets	956,580
Property and equipment	49,049,398
Construction in process	18,720,089
Total Assets	$71,841,778
Liabilities	
Accounts payable	$2,568,483
Other current liabilities	2,737,878
Long term loan	45,756,818
Total liabilities	51,063,179
Equity	
Paid in capital	17,573,578
Statutory reserve	153,147
Other comprehensive income	782,222
Retained earnings	2,269,652
Total stockholders’ equity	20,778,599
Total liabilities and stockholders’ equity	$71,841,778

11. DEFERRED TAX

Deferred tax asset was a result of the accrued maintenance cost on power generation systems that can be deducted for tax purposes in the future; and difference between tax and accounting basis of cost of fixed assets which was capitalized for tax purposes and expensed as part of cost of systems in the book. Deferred tax liability arose from the difference between tax and accounting basis of net investment in sales-type leases.

As of March 31, 2011 and December 31, 2010, deferred tax asset (liability) consisted of the following:

	2011	2010
Deferred tax asset — noncurrent (accrual of system maintenance cost)	$156,029	$23,161
Deferred tax asset — noncurrent (depreciation of fixed assets)	24,584,087	22,571,649
Deferred tax liability — noncurrent (net investment in sales-type leases)	(31,817,926)	(29,023,949)
Deferred tax liability, net of deferred tax asset – noncurrent	$(7,077,810)	$(6,429,139)
Deferred tax liability — current (net investment in sales-type leases)	$(1,252,526)	$(1,188,504)

12. INCOME TAX

Effective January 1, 2008, the PRC government implemented a new corporate income tax law with a maximum rate of 25%. The Company is governed by the Income Tax Law of the PRC concerning privately-run enterprises, which are generally subject to tax at 25% (33% prior to 2008) on income reported in the statutory financial statements after appropriate tax adjustments. Under the 2008 Chinese tax law, the tax treatment of finance and sales-type leases is similar to US GAAP. However, the local tax bureau continues to treat CREG sales-type leases as operating leases. Accordingly, the Company recorded deferred income taxes.

The Company's subsidiaries generate all of their net income from their PRC operations. Shanghai TCH's effective income tax rates for 2011 and 2010 are 24% and 22%, respectively. Xi'an TCH's effective income tax rate for 2011 and 2010 is 15% as a result of its high tech enterprise status that was approved by the taxing authority. Xingtai Huaxin's effective income tax rate for 2011 and 2010 is 25%. Huahong and Erdos TCH's effective income tax rate for 2011 and 2010 is 25%. Pingshan Shengda's effective income tax rate for 2011 is 25%. Shanghai TCH, Xi'an TCH, Xingtai Huaxin, Huahong, Pingshan Shengda and Erdos TCH file separate income tax returns. If Xi'an TCH had not been granted high tech enterprise status, income tax expense for the three months ended March 31, 2011, would have been increased by $357,578 and earnings per share would have been reduced by $0.01.

Shanghai TCH, as a business in a Development Zone, was subject to a 15% income tax rate. According to the new income tax law that became effective January 1, 2008, for those enterprises to which the 15% tax rate was applicable previously, the applicable rates shall increase over five-years as follows:

Year	Tax Rate	
2007	15	%
2008	18	%
2009	20	%
2010	22	%
2011	24	%
2012	25	%

There is no income tax for companies domiciled in the Cayman Islands. Accordingly, the Company’s consolidated financial statements do not present any income tax provisions related to Cayman Islands tax jurisdiction where Sifang Holding is domiciled.

The parent company, China Recycling Energy Corporation, is taxed in the U.S. and has net operating loss carry forwards for income taxes of $5.51 million at March 31, 2011, which may be available to reduce future years’ taxable income as NOLs can be carried forward up to 20 years from the year the loss is incurred. Management believes the realization of benefits from these losses appears uncertain due to the Company’s limited operating history and continuing losses. Accordingly, a 100% deferred tax asset valuation allowance was provided.

The following table reconciles the U.S. statutory rates to the Company's effective tax rate for the three months ended March 31, 2011 and 2010, respectively:

	2011	2010
US statutory rates	34.0%	34.0 %
Tax rate difference – current provision	(8.6)%	(13.0)%
Effect of tax holiday	(4.7)%	(7.2)%
Non tax-deductible expenses (non-taxable income), net	(0.2)%	4.2 %
Other	(0.7)%	(0.4)%
Valuation allowance on NOL (utilization of NOL)	(1.3)%	11.0 %
Tax per financial statements	18.5%	28.6 %

The provision for income tax expenses for the three months ended March 31, 2011 and 2010 consisted of the following:

	2011	2010
Income tax expense - current	$762,856	$491,948
Income tax benefit - deferred	633,074	544,818
Total income tax expenses	$1,395,930	$1,036,766

13. LOANS PAYABLE

Collective Capital Trust Plan

On December 3, 2009, the Company and Beijing International Trust Co., Ltd. ("Beijing Trust") formed a Low Carbon Fortune-Energy Recycling No. 1 Collective Capital Trust Plan ("Plan"). Under the Plan, Beijing Trust raised RMB 181,880,000 ($26.75 million) through sale of 181,880,000 trust units at RMB 1 per unit. All amounts raised under the Plan were loaned to Erdos TCH in connection with its waste heat power generation projects Phase II and Phase III construction and operation.

The Plan included 145,500,000 category A preferred trust units ($21.4 million), consisting of category A1 preferred trust 12,450,000 units ($1.8 million), category A2 preferred trust 15,000,000 units ($2.2 million), category A3 preferred trust 118,050,000 units ($17.4 million); and 36,380,000 category B secondary trust units ($5.35 million), consisting of category B1 secondary trust 9,100,000 units ($1.34 million) and category B2 secondary trust 27,280,000 units ($4.01 million). The B1 units were purchased by members of management of Erdos TCH and the B2 units were purchased by Xi'an TCH. Under the Agreement, the annual base interest rate is 9.94% for A1 preferred trust fund units with a term of two years, 11% for A2 preferred trust fund units with a term of three years, 12.05% for A3 preferred trust fund units and 8.35% for the category B secondary trust fund units, each with a term of four years.

Erdos TCH provided a lien on its equipment, assets and accounts receivable to guarantee the loans under the Agreement. Xi'an TCH and Mr. Guohua Ku (the Company's CEO) also provided unconditional and irrevocable joint liability guarantees to Beijing Trust for Erdos TCH's performance under the Agreement. Erdos (the minority shareholder and customer of Erdos TCH) provided a commitment letter on minimum power purchase from Erdos TCH.

On December 18, 2009, an additional RMB 25,000,000 ($3.7 million) was raised to support the Company's Erdos Power Generation Projects. The Company sold 25,000,000 trust units at RMB 1 per unit which included 20,000,000 category A1 preferred trust units ($ 2.9 million) and 5,000,000 category B2 secondary trust units ($ 0.7 million). The B2 units were purchased by Xi'an TCH.

During December 2009, the Plan sold aggregate 206,880,000 units for RMB 206,880,000 ($30.3 million), of which, 9,100,000 units ($1.3 million) were purchased by the management of Erdos TCH; the 32,280,000 units purchased by Xi'an TCH, the amount of $4.7 million was considered as investment by Xi'an TCH into Erdos TCH and, accordingly, was eliminated in the consolidated financial statements. The net long term loan payable under this trust plan was $25.6 million at December 31, 2009.

On April 15, 2010, Beijing Trust completed the second expansion of the Plan. The second expansion raised RMB 93,120,000 ($13.7 million) through the sale of 93,120,000 trust units at RMB 1 per unit. All amounts raised under the Second Expansion were loaned to Erdos TCH. The second expansion included 2,800,000 category A1 preferred trust units ($0.4 million), 5,000,000 category A2 preferred trust units ($0.7 million), 66,700,000 category A3 preferred trust units ($9.8 million), 4,650,000 category B1 preferred trust units ($0.7 million), and 13,970,000 category B2 secondary trust units ($2.1 million). The B1 units were purchased by members of management of Erdos TCH and the B2 units were purchased by Xi'an TCH.

With the completion of the second expansion, the Low Carbon Fortune-Energy Recycling No. 1 Collective Capital Trust Plan reached RMB 300,000,000 ($44.1 million) and completed all its trust plan raising work, of which, 13,750,000 units ($2.0 million) were purchased by the management of Erdos TCH; 47,850,000 units were purchased by Xi’an TCH, of which, 46,250,000 ($6.8 million) was B2 units and 1,600,000 ($235,600) units was A1 units, the amount was considered as investment by Xi’an TCH into Erdos TCH and, accordingly, was eliminated in the consolidated financial statements. The net long term loan payable under this trust plan was RMB 252,150,000 ($38.5 million) at March 31, 2011. Interest expense accrued on this trust loan was $5.9 million and $4.5 million at March 31, 2011 and December 31, 2010, respectively.

In addition to the above, under the Loan Agreement, Erdos TCH must pay a management incentive benefit to Beijing Trust upon maturity of the category A3 and category B trust units in December 2013 if the ratio of Erdos TCH’s profit to its registered capital exceeds a base amount. If this criterion is met, the amount of the management incentive benefit is calculated based on a formula tied to Erdos TCH’s net profit and the average registered capital for the 2012 fiscal year. Under this formula the management incentive benefit could range between 0% and 100% of the net profit of Erdos TCH in the 2012 fiscal year.

The management incentive benefit was structured to provide an incentive to management to make the joint venture profitable. Under the Plan, Beijing Trust will distribute the entire amount of the management incentive benefit it receives to the holders of the category B trust units. As previously disclosed, the holders of the category B trust units are the management of Erdos TCH and Xi’an TCH. Category B trust units receive a lower base interest rate than the category A trust units but the economic return to the holders of category B trust units will be enhanced by any management incentive benefit.

Erdos TCH also will share the benefits from Clean Development Mechanism ("CDM") under the Kyoto Protocol equally with Beijing Trust during the term of the loan. Any benefit received from CDM will be paid to Erdos Metallurgy first. Under the agreement with Xi’an TCH, Erdos Metallurgy agrees to deliver to Xi’an TCH 50% of the benefit Erdos Metallurgy receives. Xi’an TCH agrees to share 50% of the benefit it receives from Erdos Metallurgy with Erdos TCH. Under the Capital Trust Loan Agreement between Erdos TCH and Beijing Trust, Erdos TCH agrees that 50% of any benefit it receives will be delivered to Beijing Trust. Pursuant to the Plan, Beijing Trust will distribute 70% of the CDM benefit it receives to the holders of the category B trust units. The receipt of any CDM benefit is subject to a process of evaluation and certification of the project by the CDM Executive Board and is under the guidance of the Conference of the Parties of the United Nations Framework Convention on Climate Change. The first stages of the certification process have been completed successfully.

Bank Long Term Loans - Industrial Bank

The Company entered a loan agreement with Industrial Bank Co., Ltd., Xi'an Branch (the "Lender") for a loan designed for energy saving and emission reduction projects, whereby the Lender agreed to loan RMB 30,000,000 ($4,575,682) to Xi'an TCH for three years from April 6, 2010 to April 6, 2013. The proceeds of the loan are required to be used in payment for equipment for Xi'an TCH's energy saving and emission reduction projects. The Loan Agreement has a floating interest rate that resets at the beginning of each quarter at 110% of the national base interest rate for the same term and same level loan (currently 7.015%). Under the loan, Xi'an TCH is required to make quarterly interest payments and, beginning six months after the date of the release of the funds, to make minimum quarterly principal payments of RMB 3,000,000 ($457,568) each quarter. The Loan Agreement contains standard representations, warranties and covenants, and the loan is guaranteed by Xi'an TCH, Shaanxi Shengwei Construction Material Group and Mr. Guohua Ku. At March 31, 2011, $457,568 of the principal was repaid and $1,830,273 will be repaid within one year which was classified as current liability.

The loan has the following covenants during the loan period: 1) maintain the current assets and net assets not less than RMB500million; 2) assets to liability ratio not less than 80%; and 3) the current ratio not less than 2.5. The borrower was Xi'an TCH. As of March 31, 2011, the amount of net assets and the current ratio of Xi'an TCH were not in compliance with the covenants; however, the Company received a waiver letter from the lender from the bank.

The Company entered another loan agreement with the same Industrial Bank for energy saving and emission reduction projects, whereby the Lender agreed to loan RMB 30,000,000 ($4,575,682) to Xi'an TCH for three years from March 31, 2011 to March 30, 2014. As of March 31, 2011, the Company received RMB 27,000,000 ($4,118,114) of the loan. The proceeds of the loan are required to be used in payment for construction and equipment purchase for Xi'an TCH's energy saving and emission reduction projects. The Loan Agreement has a floating interest rate that resets at the beginning of each quarter at 115% of the national base interest rate for the same term and same level loan (currently 7.015%). Under the loan, Xi'an TCH is required to make quarterly interest payments and, beginning six months after the date of the release of the funds, to make minimum quarterly principal payments of RMB 3,000,000 ($457,568) each quarter. The Loan Agreement contains standard representations, warranties and covenants, and the loan is guaranteed by Xi'an TCH, Mr. Guohua Ku and Ms Chaoying Zhang.

The loan has the following covenants during the loan period: 1) maintain the current assets and net assets not less than RMB500million; 2) assets to liability ratio not less than 80%; and 3) the current ratio not less than 1. The borrower was Xi'an TCH. As of March 31, 2011, the amount of net assets of Xi'an TCH was not in compliance with the covenants; however, the Company received a waiver letter from the lender from the bank.

14. CONVERTIBLE NOTES PAYABLE

Convertible Notes from Caryle

On November 16, 2007, the Company entered into a Stock and Notes Purchase Agreement ("Purchase Agreement") with Carlyle Asia Growth Partners III, L.P. ("CAGP") and CAGP III Co. Investment, L.P. (together with CAGP, the "Investors"). Under the terms of the Purchase Agreement, the Company sold the Investors a 10% Secured Convertible Promissory Note of $5,000,000 (the "First Note"). Additionally, the Purchase Agreement provides for two subsequent transactions to be effected by the Company and the Investors, which include (i) the issuance by the Company of and subscription by the Investors for 4,066,706 shares of common stock of Company, at $1.23 per share for $5,000,000, and (ii) the issuance and sale by the Company to the Investors of a 5% Secured Convertible Promissory Note of $15,000,000 (the foregoing transactions, together with sale and purchase of the First Note, are hereinafter referred to as the "Offering"). The subsequent transactions are contingent upon the satisfaction of certain conditions specified in the Purchase Agreement, including entry into specified energy and recycling project contracts and the purchase of certain energy recycling systems.

The First Note bore interest at 10% and was due November 16, 2009. The principal amount of the First Note, together with any interest thereon, converted, at the option of the holders at any time on or prior to maturity, into shares of the Company's common stock at an initial conversion price of $1.23 per share (subject to anti-dilution adjustments). The First Note was subject to mandatory conversion upon the consummation of the aforementioned issuance and subscription of shares of the Company's common stock under the Purchase Agreement. The obligations of the Company under the First Note ranked senior to all other debt of the Company.

As collateral for the First Note, the President and a major shareholder of the Company pledged 9,653,471 shares of the Company's common stock held by him to secure the First Note. This pledge was released during the fiscal quarter ended March 31, 2011 and is of no further force or effect.

The First Note was considered to have a beneficial conversion feature ("BCF") because the conversion price was less than the quoted market price at the time of issuance. Accordingly, the beneficial conversion feature of $5,000,000 was recorded separately as unamortized beneficial conversion feature based on the intrinsic value method. As the BCF was greater than the face value of the note, all of the proceeds were allocated to the BCF. No value was assigned to the note option or the equity option (two subsequent transactions discussed above). The First Note was recorded in the balance sheet at face value less the unamortized beneficial conversion feature. The terms for the First Note were amended on April 29, 2008 and the First Note was repaid in full on June 25, 2008, as described below.

On April 29, 2008, the Company entered into an Amendment to the Purchase Agreement with the Investors. Under the terms of the Amendment, (i) the Company issued and the Investors subscribed for 4,066,706 shares of common stock of the Company, at $1.23 per share for $5,002,048, as originally contemplated under the Agreement; (ii) the Investors converted the principal under the First Note (and waived any accrued interest thereon) into 4,065,040 shares of common stock of the Company at $1.23, pursuant to the terms and conditions of the First Note issued under the Agreement; (iii) the Company issued and sold to the Investors a new 5% Secured Convertible Promissory Note of $5,000,000 (the "Second Note" and collectively with the First Note, the "Notes"); and (iv) the Company granted to the Investors an option to purchase a 5% Secured Convertible Promissory Note of $10,000,000, exercisable by the Investors at any time within nine (9) months following the date of the closing of the transactions contemplated by the Amendment (the "Option Note").

The Second Note bears interest at 5% and matured on April 29, 2011. The principal face amount of the Second Note, together with any interest thereon, converts, at the option of the holders at any time on or after March 30, 2010 (or such earlier date if the audited consolidated financial statements of the Company for the fiscal year ending December 31, 2009 are available prior to March 30, 2010) and prior to maturity, into shares of the Company's common stock at an initial conversion price that is tied to the after-tax net profits of the Company for the year ending December 31, 2009, as described in the Second Note. As more fully described in the Second Note, the obligations of the Company under the Second Note are senior to all other debt of the Company.

The Second Note and the 8% Note described below are both secured by a security interest granted to the Investors pursuant to the Share Pledge Agreement.

The Second Note was not considered to have a beneficial conversion feature prior to the year ended December 31, 2009 because the conversion price and convertible shares were contingent upon 2009 audited net profits.

On June 25, 2008, the Company and investors entered into a Rescission and Subscription Agreement to rescind the conversion of the First Note and the issuance of conversion shares of Common Stock at the Second Closing pursuant to Amendment to Stock and Notes Purchase Agreement dated April 29, 2008. The Company and the Investors rescinded the conversion of the principal amount ($5,000,000) under the First Note into 4,065,040 shares of Common Stock, and the Investors waived accrued interest on the First Note. Accordingly, the interest expense which had accrued on the note was recorded as a decrease in interest expense for the period. At the Rescission and Subscription Closing, the Company repaid in full the First Note and issued to the Investors, 4,065,040 shares of Common Stock at $1.23 per share for $5,000,000. This was done through a cross receipt arrangement; the BCF was reversed to additional paid in stock. The Company has now concluded that in substance the transaction resulted in the conversion of the first $5,000,000 note into common stock, and based on substance over form, the remaining BCF of $3,472,603 at the date of conversion should have been expensed.

On April 29, 2009, CREG issued an 8% Secured Convertible Promissory Note of $3 million to CAGP with a maturity of April 29, 2012. The note holder has the right to convert all or any part of the outstanding principal amount of this note, together with interest, if any, into shares of the Company’s common stock, at any time on or after March 30, 2010 (or such earlier date if the audited consolidated financial statements of the Company for the fiscal year ending December 31, 2009 are available on a date prior to March 30, 2010) and prior to the maturity date (or such later date on which this note is paid in full), at a conversion price per share of common stock equal to US $0.80. The conversion feature of this note is not beneficial to the holder as the stock price on April 29, 2009 was $0.47.

On April 29, 2009, CREG amended and restated the 5% secured convertible promissory note (the “Second Note”), which was issued as part of the amendment of the First Note on April 28, 2008. Accordingly the Conversion Rights and Conversion Price were amended so that the holder of the Second Note has the right, but not the obligation, to convert all or any part of the aggregate outstanding principal amount of the Second Note, together with interest, into shares of the Company’s common stock, at any time on or after March 30, 2010 (or such earlier date if the audited consolidated financial statements of the Company for the fiscal year ending December 31, 2009 are available on a date prior to March 30, 2010) and prior to the maturity date (or such later date on which this Note is paid in full), at the following conversion price: (a) an amount equal to (i) the Company’s net profit, adjusted in accordance with the Second Note, multiplied by (ii) 5.5, and less (iii) the principal amount of the Second Note, together with accrued interest, divided by (b) the then total shares of the Company’s common stock outstanding on a fully-diluted basis. This note is considered to have a beneficial conversion feature starting from January 1, 2010 because the conversion price for this note was $1.148 as of March 31, 2011, based on 2009 audited net profits and the stock price on April 29, 2008 was $1.88. This note was convertible in full into 4,577,851 shares of our common stock as of March 31, 2011. Prior to the maturity date, the Investors informally expressed their intent to exercise their conversion rights on the terms and conditions set forth herein; however, as of May 16, 2011, the Company has not yet received formal notice from the Investors, indicating that the Investors have elected to exercise their conversion rights, and, as such, the formal conversion process has not yet commenced and the shares to be issued upon conversion to the Investors have not been issued. Accordingly, the beneficial conversion feature of $3.35 million was recorded separately as unamortized beneficial conversion feature based on the intrinsic value method and the Second Note was recorded in the balance sheet at face value less the unamortized beneficial conversion feature as of March 31, 2011. During 2011, the Company amortized $623,441 from unamortized BCF.

The interest on the convertible debts is payable annually, in arrears, provided the holder gives 30-day notice before each April 29 that it requires the interest payment. Unpaid interest is due and payable at maturity. At the holder's election, at the time the holder elects to convert the debt into shares, shares can be issued as paid-in-kind interest to the extent that there is unpaid interest at the time of conversion. To date, the Company has timely paid all interest payable, in cash.

On April 29, 2009, the Company also agreed with the Investors to amend and restate the Registration Rights Agreement for the convertible notes to amend the rights for demand registration by the Investors and the applicable liquidated damages for the Company if it fails to timely comply with the demand for registration.

Registration Rights Agreement

Under the registration rights agreement, the Company must file the registration statement within 90 days of receipt of a demand notice to convert (the "Filing Date"), and the registration statement must have become effective within 120 days after filing (the "Effective Date") or the Company must pay damages to the holders of the shares to be registered. The Company must also pay damages if the registration statement ceases for any reason to remain continuously effective as to all Registrable Shares for which it is required to be effective, or the holders are not permitted to utilize the prospectus to resell shares for thirty (30) consecutive calendar days during any 12-month period.

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The damages for failure to meet any of these requirements are equal to 1% of the sum of:

(x) the purchase price of the unconverted notes;

(y) the purchase price of shares of Company Common Stock purchased under a related agreement; and

(z) the conversion price of shares of Common Stock received on conversion of notes, for each 30 days, or a pro rata portion of such 1% for a period less than 30 days.

The liquidated damages must be paid in cash; the registration rights agreement does not provide for any alternative payment arrangement. The maximum potential amount of consideration, undiscounted, that the Company could be required to transfer under the registration payment arrangement cannot exceed 1% of the sum described above in any thirty (30) calendar day period.

Convertible Note Agreement with China Cinda

On August 18, 2010, the "Company and its wholly-owned subsidiaries Sifang, Shanghai TCH and Xi'an TCH entered into a Notes Purchase Agreement (the "Note Agreement") with China Cinda (HK) Asset Management Co., Ltd, a company organized under the laws of the Hong Kong Special Administrative Region of China ("Cinda"). Under the terms of the Note Agreement, the Company will issue to Cinda two tranches of convertible notes (the "Notes"), each having a principal amount equal to the US Dollar equivalent of RMB 50 million. Also on August 18, 2010, Xi'an TCH and China Jingu International Trust Co. Ltd. ("Jingu"), an affiliate of Cinda also entered into a Capital Trust Loan Agreement ("Trust Loan Agreement"), in which Jingu will raise 100 million RMB under a Jingu CREG Recycling Economy No. 1 Collective Fund Trust Plan ("Trust Plan") and lend such amount under the Trust Plan to Xi'an TCH (the "Loans"). If the Loans under the Trust Loan Agreement do not occur, then under the Note Agreement the principal amount of the Notes to be issued in each tranche will be the US dollar equivalent of RMB 100 million. All proceeds from the Notes and the Loans will be used to complete the Phases IV and V of the Erdos TCH Energy Saving Development Co., Ltd. ("Erdos TCH") project, a joint venture between Xi'an TCH and Erdos Metallurgy Co., Ltd. to recycle waste heat from Erdos Metallurgy's refining plants to generate power and steam and sell them back to Erdos Metallurgy, as well as other working capital needs.

Under the Trust Loan Agreement and separate agreements entered by Jingu, Erdos TCH, Shanghai TCH, Xi'an TCH and Mr. Guohua Ku on August 18, 2010, Erdos TCH shall pledge the accounts receivable, equipment and assets of its Phases IV and V projects to Jingu as a guarantee to the Loans, Xi'an TCH shall pledge its 80% equity in Erdos TCH to Jingu as a guarantee to the Loans, Shanghai TCH shall provide a joint liability guarantee to Jingu for the Loans, and Mr. Guohua Ku shall provide his personal joint liability to Jingu for the Loans.

Under the Note Agreement the Notes shall be issued before August 18, 2011. The Notes have a three year maturity date from the date of the issuance of the first tranche. The exchange rate between RMB and US Dollar for each issue of Notes is the middle rate published by the PBOC for the second business day prior to each issuance. Each Note bears interest at a rate equal to that of PBOC base interest rate for the relevant interest period (the period commencing on and including January 1 of each year and ending on and including December 31 of such year) plus two percent (2%). If Cinda does not convert or fully convert the Notes to shares prior to maturity, the Company will pay the difference between the interest rate described above and 18% on the outstanding amount.

The loan has the following covenants: 1) maintain at all time a fixed charge coverage ratio of not less than 2.0:1.0; 2) obtain consent from the lender prior to pay or declare any cash dividends or distributions on outstanding common stock; and 3) maintain at all time a consolidated leverage ratio of not less than 65%. The Company was in compliance with these covenants as of March 31, 2011.

Each Note has a conversion price at the lower of (i) US$2.46 per share or (ii) an amount equal to the Company's earnings per share based upon the consolidated earnings of the Company for 2010 on a weighted average fully diluted basis, multiplied by 7. In connection with the Trust Loan Agreement, the Company also entered into an Exchange Rights Agreement pursuant to which the Loans can be exchanged (on the same terms as the Notes can be converted) for shares of the Company's common stock which can in turn be registered under the Registration Rights Agreement. The Notes will have a contingent beneficial conversion feature which will be recorded when the contingency is resolved.

As collateral for the Notes, Mr. Guohua Ku, the CEO and a major shareholder of the Company, has entered into a Share Pledge Agreement with Cinda, on August 18, 2010, to pledge 4,500,000 shares of the Company's common stock held by him to secure the first Note. The Agreement also calls for an additional 4,500,000 shares of the Company's common stock held by Mr. Ku to secure the second Note before its issuance.

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As of December 31, 2010, the Company received proceeds of RMB 50,000,000 ($7,533,391) from the first tranche of the loan. As of January 30, 2011, the Company received proceeds of RMB 50,000,000 ($7,533,391) from the second tranche of the loan. Under ASC 815 – Derivatives and Hedging, the fair value of the conversion option is a derivative that has been bifurcated and treated as liability at the date of inception. Based on AU 560 - subsequent events, the conversion feature has been accounted for at March 31, 2011 and December 31, 2010 using the conversion price of $2.46. The conversion feature is akin to a call option, therefore, the Black-Scholes option pricing model was used by using the maximum conversion price of $2.46 as a the strike price. Since the conversion option is an embedded derivative and is bifurcated from the host contact, BCF analysis is not required. The fair value of the conversion feature has been recorded as a liability and will be marked to market until the conversion rate is set. As the loan has a reset clause in the event the Company issues shares below the conversion price, it will be treated as a liability as long as the loan is outstanding. The unamortized discount due to beneficial conversion feature will continue to be amortized over the term of the loan; during the three months ended March 31, 2011, the Company amortized $901,454 from unamortized discount due to beneficial conversion feature.

For the first tranche of the loan, the Company recorded the derivative liability of $5.19 million for conversion option at March 31, 2011 based on the Black-Scholes model by using the following assumptions: estimated life of three years, volatility of 100%, risk free interest rate of 1.07%, and dividend yield of 0%. For the second tranche, the Company recorded the derivative liability of $5.17 million for conversion option at March 31, 2011 based on the Black-Scholes model by using the following assumptions: estimated life of three years, volatility of 100%, risk free interest rate of 0.96%, and dividend yield of 0%.

15. STOCK-BASED COMPENSATION PLAN

Options to Employees

On November 13, 2007, the Company approved the 2007 Non-statutory Stock Option Plan, which was later amended and restated in August 2008 (the “2007 Plan”), and granted 3,000,000 options to acquire the Company’s common stock at $1.23 per share to twenty (20) managerial and non-managerial employees under the 2007 Plan.

The vesting terms of options granted under the 2007 Plan are subject to the Non-Statutory Stock Option Agreements for managerial and non-managerial employees. For managerial employees, no more than 15% of the total stock options shall vest and become exercisable on the six month anniversary of the grant date. An additional 15% and 50% of the total stock options shall vest and become exercisable on the first and second year anniversary of the grant date, respectively. The remaining 20% of the total stock options shall vest and become exercisable on the third year anniversary of the grant date. For non-managerial employees, no more than 30% of the total stock options shall vest and become exercisable on the first year anniversary of the grant date. An additional 50% of the total stock options shall vest and become exercisable on the second year anniversary of the grant date. The remaining 20% of the total stock options shall vest and become exercisable on the third year anniversary of the grant date. Each stock option shall become vested and exercisable over a period of no longer than five years from the grant date.

Based on the fair value method under SFAS No. 123 (Revised) “Share Based Payment” (“SFAS 123(R)”), codified in FASB ASC Topic 718, the fair value of each stock option granted is estimated on the date of the grant using the Black-Scholes option pricing model. The Black-Scholes option pricing model has assumptions for risk free interest rates, dividends, stock volatility and expected life of an option grant. The risk free interest rate is based upon market yields for United States Treasury debt securities at a maturity near the term remaining on the option. Dividend rates are based on the Company’s dividend history. The stock volatility factor is based on the historical volatility of the Company’s stock price. The expected life of an option grant is based on management’s estimate as no options have been exercised in the Plan to date. The fair value of each option grant to employees is calculated by the Black-Scholes method and is recognized as compensation expense over the vesting period of each stock option award. For stock options issued, the fair value was estimated at the date of grant using the following range of assumptions:

The options vest over three years and have a life of 5 years. The fair value of the options was calculated using the following assumptions, estimated life of five years, volatility of 100%, risk free interest rate of 3.76%, and dividend yield of 0%. No estimate of forfeitures was made as the Company has a short history of granting options.

Effective June 25, 2008, the Company cancelled all vested shares and accepted optionees’ forfeiture of any unvested shares underlying the currently outstanding options.

On August 4, 2008, the Company granted stock options to acquire 3,000,000 shares of the Company’s common stock, par value $0.001, at $0.80 per share to 17 employees under the 2007 Plan. The options vest over a period of three years and have a life of 5 years. The fair value of the options was calculated using the following assumptions, estimated life of five years, volatility of 100%, risk free interest rate of 2.76%, and dividend yield of 0%. No estimate of forfeitures was made as the Company has a short history of granting options. The options were accounted for as a modification to the options that were cancelled on June 25, 2008. The grant date fair value of options was $5.04 million.

On November 9 and 11, 2009, the Company and three optionees agreed to cancel vested but unexercised options for 87,000 vested but not exercised shares and forfeit unvested options for 203,0000 unvested shares. On November 11, 2009, the Company granted options to two other employees for 290,000 shares of the Company's common stock at $2.35 per share. The options vest over three years and have a life of 5 years. The fair value of the options was calculated using the following assumptions, estimated life of five years, volatility of 100%, risk free interest rate of 3.84%, and dividend yield of 0%. The grant date fair value of options was $518,513.

On August 13, 2010, the Company granted 2,200,000 options to acquire the Company's common stock at $3.05 per share to thirty six (36) managerial and non-managerial employees as new equity awards pursuant to the Corporation's Amended and Restated 2007 plan.

According to the vesting terms, the options granted were divided into three tranches, (i) 1/3 (one third) of the total number of shares subject to the options shall vest and become exercisable if the Corporation meets its minimum revenue and earnings goals in the Corporation's guidance for 2010 as delivered in its earnings releases and/or conference calls in the first quarter of 2010, such vesting to occur immediately upon completion of the annual audit confirming the financial results for 2010; and (ii) an additional 1/3 (one third) of the total number of shares subject to the options shall vest and become exercisable if the Corporation meets certain financial goals of 2011 which will be set out and decided by the Compensation Committee, such vesting to occur immediately upon Compensation Committee's determination that the Corporation has met such goals for 2011; and (iii) the remaining 1/3 (one third) of the total number of shares subject to the options shall vest and become exercisable if the Corporation meets certain financial goals of 2012 which will be set out and decided by the Compensation Committee, such vesting to occur immediately upon Compensation Committee's determination that the Corporation has met such goals for 2012. The Option may only be exercised to the extent that the Option has become vested and exercisable. The management used its estimates for determining the probability of achieving each year's financial goals; these were 100%, 50% and 50% for 2010, 2011 and 2012, respectively.

The options have a life of 5 years. The fair value of the options was calculated using the following assumptions; estimated life of five years, volatility of 92%, risk free interest rate of 3.54%, and dividend yield of 0%. No estimate of forfeitures was made as the Company has a short history of granting options. Each tranche of the options was deemed independent of the others; therefore, the fair value of each tranche of the options will be fully expensed within each year.

The following table summarizes activity for employees in the Company's Plan:

	Number of Shares	Average Exercise Price per Share	Weighed Average Remaining

				Contractual Term in Years
Outstanding at January 1, 2009	3,000,000	$	0.80	4.59
Granted	290,000		2.35	5.00
Exercised	-		-	-
Cancelled vested options	(87,000)		0.80	-
Forfeited	(203,000)		0.80	-
Outstanding at December 31, 2009	3,000,000		0.95	3.71
Exercisable at December 31, 2009	813,000		0.80	3.59
Granted	2,200,000		3.05	5.00
Exercised	-		-	-
Forfeited	-		-	-
Outstanding at December 31, 2010	5,200,000		1.84	3.52
Exercisable at December 31, 2010	2,255,000	$	0.86	2.59
Granted	-		-	-
Exercised	-		-	-
Forfeited	-		-	-
Outstanding at March 31, 2011	5,200,000		1.84	3.27
Exercisable at March 31, 2011	2,255,000	$	0.86	2.34

The Company recorded $1,069,080 and $506,126 compensation expense for stock options to employees during the three months ended March 31, 2011 and 2010, respectively. There were no options exercised during the three months ended March 31, 2011.

Options to Independent Directors

On October 30, 2009, the Company granted stock options for 130,000 shares of the Company's common stock, par value $0.001, at $1.85 per share to three independent directors. The options vested and became exercisable on the six-month anniversary of the grant date with a life of 5 years. The fair value of the options was calculated using the following assumptions: estimated life of five years, volatility of 100%, risk free interest rate of 3.54%, and dividend yield of 0%. The grant date fair value of options was $183,000.

On January 20, 2010, the Company granted stock options for 40,000 shares of the Company's common stock, par value $0.001, at $4.68 per share to another independent director. The options vest and become exercisable on the six-month anniversary of the grant date with a life of 5 years. The fair value of the options was calculated using the following assumptions: estimated life of five years, volatility of 100%, risk free interest rate of 3.54%, and dividend yield of 0%. The grant date fair value of options was $142,000.

On October 7, 2010, the Board of Directors ("BOD") of the Company approved the increase in its size from seven to nine members as a result of entering the Loan and Note agreements with Cinda on August 18, 2010 as described in Note 16 above. At the same time, the BOD appointed Mr. Yilin Ma and Mr. Chungui Shi as new members of the Board to fill the vacancies on the BOD until their successors have been duly elected and qualified. Mr. Shi is also appointed as a member of the Compensation Committee of the BOD. In connection with the appointment, the BOD of the Company has authorized the Company to provide Mr. Shi with (i) compensation of $2,000 per month and (ii) the grant of an option to purchase 40,000 shares of the Company's Common Stock, par value $0.001, at an exercise price equal to the closing price per share of the Company's Common Stock on October 7, 2010. The options vested and became exercisable on the six-month anniversary of the grant date with a life of 5 years. The fair value of the options was calculated using the following assumptions: estimated life of five years, volatility of 87%, risk free interest rate of 3.54%, and dividend yield of 0%. The grant date fair value of options was $83,000.

The following table summarizes option activity with respect to the independent directors:

	Number of Shares	Average Exercise Price per Share	Weighed Average Remaining

			Contractual Term in Years
Outstanding at January 1, 2009	-	$ -	-
Granted	130,000	1.85	5.00
Exercised	-	-	-
Forfeited	-	-	-
Outstanding at December 31, 2009	130,000	1.85	4.83
Exercisable at December 31, 2009	-	-	-
Granted	80,000	3.83	5.00
Exercised	-	-	-
Forfeited	-	-	-
Outstanding at December 31, 2010	210,000	2.60	4.05
Exercisable at December 31, 2010	170,000	$ 2.52	3.89
Granted	-	-	-
Exercised	-	-	-
Forfeited	-	-	-
Outstanding at March 31, 2011	210,000	2.60	3.80
Exercisable at March 31, 2011	170,000	$ 2.52	3.64

The Company recorded $41,013 and $146,525 compensation expense for stock options to independent directors during the three months ended March 31, 2011 and 2010, respectively. There were no options exercised during the three months ended March 31, 2011.

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Warrants to Investor Relation Firms

On October 1, 2009, the Company granted warrants to acquire 200,000 shares of the Company's common stock, par value $0.001, at $1.50 per share to certain investor relations firms. The warrants are exercisable, in whole or in part, at any time from July 1, 2010 (the "Vesting Date") to October 1, 2014 (the "Expiration Date"). The Company accounted for warrants issued to investor relations firms based on ASC 505-50 at each balance sheet and expense recorded based on the period elapsed at each balance sheet date, which is the date at which the counterparty's performance is deemed to be completed for the period. The fair value of each warrant granted is estimated on the date of the grant using the Black-Scholes option pricing model under ASC 505-30-11 and is recognized as compensation expense over the service term of the investor relations agreement as it is a better matching of cost with services received. Under that Agreement, the issuance of the warrants was irrevocable and the Company agreed to take no action to cause the warrants to be void or revoked or their issuance to be otherwise terminated. The warrants are classified as equity instruments and are exercisable into a fixed number of common shares. There is no commitment or requirement to change the quantity or terms based on conditions to the counterparty's performance or market conditions. The fair value of the warrants was calculated using the following assumptions: estimated life of five years, volatility of 100%, risk free interest rate of 3.54%, and dividend yield of 0%.

The following table summarizes activity for the warrants to certain investor relations firms:

	Number of Shares	Average Exercise Price per Share	Weighed Average Remaining Contractual Term in Years
Outstanding at January 1, 2009	-	$ -	-
Granted	200,000	1.50	5.00
Exercised	-	-	-
Forfeited	-	-	-
Outstanding at December 31, 2009	200,000	1.50	4.75
Exercisable at December 31, 2009	-	-	-
Granted	-	-	-
Exercised	150,000	1.50	-
Forfeited	-	-	-
Outstanding at December 31, 2010	50,000	1.50	3.75
Exercisable at December 31, 2010	50,000	$ 1.50	3.75
Granted	-	-	-
Exercised	-	-	-
Forfeited	-	-	-
Outstanding at March 31, 2011	50,000	1.50	3.50
Exercisable at March 31, 2011	50,000	$ 1.50	3.50

The Company recorded $0 and $90,749 compensation expense for warrants to the IR during the three months ended March 31, 2011 and 2010, respectively. There were no warrants exercised during the three months ended March 31, 2011.

16. SHAREHOLDERS' EQUITY

On June 29, 2010, Xi'an TCH entered into a Biomass Power Generation Asset Transfer Agreement (the "Transfer Agreement") with Dong, a natural person with Chinese citizenship. Under the Transfer Agreement, Dong transferred the Biomass Systems to Xi'an TCH, and Xi'an TCH will pay Dong RMB 100,000,000 ($14,705,900) for the systems, including RMB 20,000,000 in cash and RMB 80,000,000 with equivalent shares of the Company's common stock. The stock price will be the same price as the Company's public offering price in the first public offering which occurs in 2010 or 2011 but in no circumstance less than $4 per share. The exchange rate between U.S. Dollar and Chinese RMB in connection with the stock issuance is 1:6.8. At March 31, 2011, the Company recorded shares to be issued of $7.91 million (the fair value at March 31, 2011) in connection with this transaction.

During the three months ended March 31, 2011, the Company recorded a gain of $1.06 million, which is the change of the fair value of 2,941,176 maximum numbers of shares to be issued to Dong.

ARC Settlement

The Company and investment relationship company ARC China, Inc ("ARC") entered into a Share Purchase Binding Letter of Intent dated as of July 17, 2009 regarding ARC's purchase of certain Preferred Stock Units of the Company (the "LOI"). Disputes arose between the Parties regarding the LOI, and a lawsuit was pending in federal court. On September 27, 2010, the Company approved the settlement of the lawsuit and the related disputes, claims or disagreements regarding the LOI and the Preferred Stock Units. Pursuant to the settlement, the Company will issue to ARC up to 520,000 shares of the Company's Common Stock at $1.23 per share. The Company issued 350,000 of these shares upon the execution of the settlement agreement. Upon satisfaction of certain conditions of the settlement agreement, the Company may issue to ARC or its affiliates up to an additional 170,000 shares at a price of $1.23 per share. ARC has agreed to provide consulting and investor relations services from November 1, 2010 to February 28, 2011. The Company received $430,500 from issuance of 350,000 shares in October 2010, which was recorded as subscription receivable as of September 30, 2010. The difference between the stock price at the settlement date and the issuance price for the 350,000 settlement shares was recorded as stock compensation expense for investor relations services in the amount of $602,000. A copy of the dismissal of the lawsuit with prejudice was filed by ARC China in Nevada federal court on November 10, 2010. The conditions for the issuance of the additional 170,000 shares were not met; consequently, 150,000 of those shares, which had been issued and delivered to an escrow agent, were returned to the Company and cancelled on March 29, 2011, and the other 20,000 shares were never issued.

17. STATUTORY RESERVES

Pursuant to the corporate law of the PRC effective January 1, 2006, the Company is only required to maintain one statutory reserve by appropriating from its after-tax profit before declaration or payment of dividends. The statutory reserve represents restricted retained earnings.

Surplus Reserve Fund

The Company is required to transfer 10% of its net income, as determined under PRC accounting rules and regulations, to a statutory surplus reserve fund until such reserve balance reaches 50% of the Company's registered capital.

The surplus reserve fund is non-distributable other than during liquidation and can be used to fund previous years' losses, if any, and may be utilized for business expansion or converted into share capital by issuing new shares to existing shareholders in proportion to their shareholdings or by increasing the par value of the shares currently held by them, provided that the remaining reserve balance after such issuance is not less than 25% of the registered capital.

Common Welfare Fund

The common welfare fund is a voluntary fund to which the Company can elect to transfer 5% to 10% of its net income. This fund can only be utilized on capital items for the collective benefit of the Company's employees, such as construction of dormitories, cafeteria facilities, and other staff welfare facilities. This fund is non-distributable other than upon liquidation. The Company does not participate in this voluntary fund.

18. CONTINGENCIES

The Company's operations in the PRC are subject to specific 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 environments and foreign currency exchange. The Company's results may be adversely affected by changes in governmental policies with respect to laws and regulations, anti-inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation, among other things.

The Company's sales, purchases and expense transactions are denominated in RMB and all of the Company's assets and liabilities are also denominated in RMB. The RMB is not freely convertible into foreign currencies under the current law. In China, foreign exchange transactions are required by law to be transacted only by authorized financial institutions. Remittances in currencies other than RMB may require certain supporting documentation in order to make the remittance.

19. COMMITMENTS

Erdos Phase III of Power Generation Projects

In April 2009, Erdos TCH signed a contract with Erdos Metallurgy to recycle heat from groups of furnaces of Erdos Metallurgy's metal refining plants to generate power and steam, to be sold back to Erdos Metallurgy. According to the contract, Erdos TCH will install a group of power generation projects with a total of 70MW power capacity, which may grow up to 120MW, and 30-ton steam per hour, with an estimated total investment in excess of $75 million (RMB 500 million). The Company split the construction of the projects into three phases, two units of power generation in Phase I with a total of 18MW power capacity, three units in Phase II with a total of 27MW power capacity and one unit in Phase III with 25MW power capacity. For each phase of the project, the lease term is 20 years starting from the date of completion of the phase. During the lease term, Erdos TCH will be responsible for operating the projects and charge Erdos Metallurgy for supply of electricity and steam. Erdos Metallurgy agreed to pay a fixed minimum of $0.22 million (RMB 1.5 million) per month for each 9MW capacity power generation system.

During the first quarter of 2010, Erdos power generation system Phase I project was completed and put into operation. During the fourth quarter of 2010 and first quarter of 2011, three 9MW power generation systems of Phase II were completed and put into operation. Erdos TCH outsourced to an independent third party the operation and maintenance of the power generation system for $922,000 (RMB 6.27 million) per year for each system. After 20 years, the systems will be transferred to Erdos without any charge.

As of March 31, 2011 the projects of Erdos Phase III are under construction. At March 31, 2011, the Company has paid approximately $18.19 million for Phase III. The Company expects the completion of Phase III projects no later than the end of 2011.

Shannxi Datong Coal Group Power Generation Projects

In February 2011, Xi'an TCH signed a contract with Shannxi Datong Coal Group Steel Ltd Co (Shannxi Datong) to recycle gas and steam from groups of blast-furnaces and converter of Shannxi Datong's metal refining plants to generate power. According to the contract, the Company will install two 3MW TRT and one 15MW WGPG and two 1MW steam power generation systems, with a total of 23MW power capacity for an estimated total investment of $27.45 million (RMB 180 million). The lease term is 30 years. During the lease term, Shannxi Datong will be responsible for operating the projects and pay a service fee to the Company. The service fee is based on an average of 8,000 electricity-generating hours per year and RMB 0.33 per kilowatt hour ("Kwh") for the first 5 years from the completion of each power generation station. For each of the leases, at the 6th year, 11th year and 21st year thereafter, the rate will be RMB 0.3 Kwh, 0.27 Kwh and 0.25 Kwh, respectively. After 30 years, the units will be transferred to Shannxi Datong without any charge.

On February 28,2011, Xi'an TCH entered into an agreement with Xi'an Huaxin Energy Tech Co., Ltd (the contractor for construction) for Shannxi Datong Coal projects of two 3MW TRT and one 15 MW WGPG systems described above. The project is scheduled to complete in 12 months from construction commencement.

20. RESTATEMENT OF FINANCIAL STATEMENTS

The financial statements for the periods ended March 31, 2011 and December 31, 2010 were restated to reflect the following:

According to FASB ASC 480-10-35-5, all other financial instruments recognized under the guidance in Section 480-10-25 shall be measured subsequently at fair value with changes in fair value recognized in earnings, unless either this subtopic or another subtopic specifies another measurement attribute.

Accordingly, the shares to be issued to Dong (with fixed obligation of RMB 80 million (US $11.78 million)) pursuant to Biomass Power Generation Asset Transfer Agreement entered on June 29, 2010 ("Note 16 - Shareholders' Equity") should be classified as a liability on the balance sheet and adjusted to fair value at each reporting period. Previously, the Company did not measure the changes in fair value of the liability at each reporting date.

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The following table presents the effects of the restatement adjustment on the accompanying consolidated balance sheet at March 31, 2011:

Consolidated Balance Sheet	As Previously Reported	Restated	Net Adjustment
Shares to be issued	$11,780,471	$7,911,763	$(3,868,708)
Retained earnings	$18,811,698	$22,680,406	$3,868,708

The following table presents the effects of the restatement adjustment on the accompanying consolidated statement of income and comprehensive income for the three months ended March 31, 2011:

Consolidated Statement of Income and Comprehensive Income	As Previously Reported	Restated	Net Adjustment
Changes in fair value of the liability	$ -	$1,058,823	$1,058,823
Total non-operating income (expense), net	$ 304	$1,059,127	$1,058,823
Income before income taxes	$ 6,478,035	$7,536,858	$1,058,823
Net Income	$ 5,082,105	$6,140,928	$1,058,823
Net income attributable to CREG	$ 4,562,967	$5,621,790	$1,058,823
Comprehensive income attributable to CREG	$ 5,544,839	$6,603,662	$1,058,823
Basic	$ 0.12	$0.14	$0.02
Diluted	$ 0.09	$0.10	$0.01

The following table presents the effects of the restatement adjustment on the accompanying consolidated statement of cash flows for the three months ended March 31, 2011:

	As Previously Reported	Restated	Net Adjustment
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$5,082,105	$6,140,928	$1,058,823
Changes in fair value of the liability	$-	$(1,058,823)	$(1,058,823)

The following table presents the effects of the restatement adjustment on the accompanying consolidated balance sheet at December 31, 2010:

Consolidated Balance Sheet		Restated

	As Previously Reported		Net Adjustment
Shares to be issued	$11,780,471	$8,970,587	$(2,809,884)
Retained earnings	$14,812,630	$17,622,514	$2,809,884

The following table presents the effects of the restatement adjustment on the accompanying consolidated statement of income and comprehensive income for the year ended December 31, 2010:

Consolidated Statement of Income and Comprehensive Income	As Previously Reported	Restated	Net Adjustment
Changes in fair value of the liability	$ -	$2,809,884	$2,809,884
Total non-operating income (expense), net	$(2,675,662)	$134,222	$2,809,884
Income before income taxes	$24,692,109	$27,501,993	$2,809,884
Income from operations	$17,826,069	$20,635,953	$2,809,884
Net income attributable to CREG	$16,032,597	$18,842,481	$2,809,884
Comprehensive income attributable to CREG	$18,406,947	$21,216,831	$2,809,884
Basic	$0.41	$0.49	$0.08
Diluted	$0.33	$0.38	$0.05

The following table presents the effects of the restatement adjustment on the accompanying consolidated statement of cash flows for the year ended December 31, 2010:

	As Previously Reported	Restated	Net Adjustment
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$17,826,069	$20,635,953	$2,809,884
Changes in fair value of the liability	$-	$(2,809,884)	$(2,809,884)

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

Note Regarding Forward-Looking Statements

This quarterly report on Form 10-Q and other reports filed by the Company from time to time with the SEC (collectively the "Filings") contain or may contain forward-looking statements and information that are based upon beliefs of, and information currently available to, Company's management as well as estimates and assumptions made by Company's management. Readers are cautioned not to place undue reliance on these forward-looking statements, which are only predictions and speak only as of the date hereof. When used in the filings, the words "anticipate", "believe", "estimate", "expect", "future", "intend", "plan", or the negative of these terms and similar expressions as they relate to Company or Company's management identify forward-looking statements. Such statements reflect the current view of Company with respect to future events and are subject to risks, uncertainties, assumptions, and other factors (including the statements in the section "results of operations" below), and any businesses that Company may acquire. Should one or more of these risks or uncertainties materialize, or should the underlying assumptions prove incorrect, actual results may differ significantly from those anticipated, believed, estimated, expected, intended, or planned.

Although the Company believes that the expectations reflected in the forward-looking statements are based on reasonable assumptions, the Company cannot guarantee future results, levels of activity, performance, or achievements. Except as required by applicable law, including the securities laws of the United States, the Company does not intend to update any of the forward-looking statements to conform these statements to actual results. Readers are urged to carefully review and consider the various disclosures made throughout the entirety of this report, which attempts to advise interested parties of the risks and factors that may affect our business, financial condition, results of operations, and prospects.

Our financial statements are prepared in US Dollars and in accordance with accounting principles generally accepted in the United States. See "Foreign Currency Translation and Comprehensive Income (Loss)" below for information concerning the exchange rates at which Renminbi ("RMB") were translated into US Dollars ("USD") at various pertinent dates and for pertinent periods.

OVERVIEW OF BUSINESS BACKGROUND

China Recycling Energy Corporation (the "Company" or "CREG") (formerly China Digital Wireless, Inc.) was incorporated on May 8, 1980, under the laws of the State of Colorado. On September 6, 2001, the Company re-domiciled its state of incorporation from Colorado to Nevada. The Company, through its subsidiary Shanghai TCH Energy Technology Co., Ltd. ("Shanghai TCH"), is in the business of selling and leasing energy saving systems and equipment. On March 8, 2007, the Company changed its name to “China Recycling Energy Corporation”.

In September 2001, Boulder Brewing changed its state of incorporation from Colorado to Nevada and its name to Boulder Acquisitions, Inc., or Boulder Acquisitions. From the date of reincorporation until June 23, 2004, Boulder Acquisitions had no material operations or assets.

On June 23, 2004, we completed a stock exchange transaction with the stockholders of Sifang Holdings Co., Ltd. (“Sifang Holdings”). The exchange was consummated under Nevada and Cayman Islands law pursuant to the terms of a Securities Exchange Agreement, dated June 23, 2004 by and among Boulder Acquisitions, Sifang Holdings and the stockholders of Sifang Holdings. Pursuant to the Securities Exchange Agreement, we issued 13,782,636 shares of our common stock to the stockholders of Sifang Holdings, approximately 89.7% of our post-exchange issued and outstanding common stock, for 100% of the outstanding capital stock of Sifang Holdings.

Effective August 6, 2004, we changed our name from Boulder Acquisitions, Inc. to China Digital Wireless, Inc. From August 2004 to December 2006, we primarily engaged in pager and mobile phone distribution and provided value added information services to the customers in the People’s Republic of China (“PRC”). We phased out and scaled down most of the business of mobile phone distribution and provision of pager and mobile phone value-added information services, and on May 10, 2007, the Company approved and announced that it ceased and discontinued these businesses.

In December 2006, we began to conduct business in the energy saving and recycling industry, including purchasing certain equipment, devices, hardware and software for the construction and installation of TRT systems and other renewable energy products. TRT is an electricity generating system that utilizes the exhaust pressure and heat produced in the blast furnace of steel mills to generate electricity. It has commercial value for the steel mills by using waste heat and steam to produce electricity for the operation of the mills

On March 8, 2007, we changed our name from China Digital Wireless, Inc. to China Recycling Energy Corporation.

Our current business is primarily conducted through our wholly-owned subsidiary, Sifang Holdings, its wholly-owned subsidiaries, Huahong New Energy Technology Co., Ltd. (“Huahong”) and Shanghai TCH, Shanghai TCH’s wholly-owned subsidiaries, Xi’an TCH Energy Technology Company, Ltd (“Xi’an TCH”) and Xingtai Huaxin Energy Tech Co., Ltd. (“Huaxin”), and Xi’an TCH’s subsidiary Erdos TCH Energy Saving Development Co., Ltd (“Erdos TCH”), in which 93% of the investment is from Xi’an TCH, a joint venture between Xi’an TCH and Erdos Metallurgy Co., Ltd. Shanghai TCH was established as a foreign investment enterprise in Shanghai under the laws of the PRC on May 25, 2004, currently with a registered capital of $29.80 million. Xi’an TCH was incorporated in Xi’an, Shannxi Province under the laws of the PRC on November 8, 2007. Huaxin was incorporated in Xingtai, PRC in November, 2007. Erdos TCH was incorporated in April, 2009. Huahong was incorporated in February, 2009.

On April 8, 2007, our Board of Directors approved and made effective a TRT Project Joint-Operation Agreement (“Joint-Operation Agreement”) which was conditionally entered into on February 1, 2007 between Shanghai TCH and Xi’an Yingfeng Science and Technology Co., Ltd. (“Yingfeng”). Yingfeng is a Chinese company located in Xi’an, Shaanxi Province, China, which designs, sells, installs, and operates TRT systems and other renewable energy products. Due to Yingfeng’s lack of capital in pursuing this project alone, Yingfeng sought Shanghai TCH’s cooperation. On October 31, 2007, Shanghai TCH entered an asset-transfer agreement with Yingfeng to transfer from Yingfeng to Shanghai TCH all electricity-generating related assets owned by Yingfeng. As a result, the contractual relationships between Shanghai TCH and Yingfeng under the TRT Project Joint-Operation Agreement entered on April 8, 2007 were terminated.

On April 14, 2009, the Company incorporated a joint venture (“JV”) between Xi’an TCH and Erdos Metallurgy Co., Ltd. (“Erdos”) to recycle waste heat from Erdos’ metal refining plants to generate power and steam, which will then be sold back to Erdos. The name of the JV is Inner Mongolia Erdos TCH Energy Saving Development Co., Ltd (“Erdos TCH”) with a term of 20 years. As of December 31, 2010, Erdos contributed 7% of the total investment of the project, and Xi’an TCH contributed 93% of the total investment. Xi’an TCH and Erdos will receive 80% and 20% of the profit from the JV, respectively, until Xi’an TCH has received a complete return on its investment. Xi’an TCH and Erdos will then receive 60% and 40% of the profit from the JV, respectively.

On March 15, 2011, the Company incorporated a new wholly owned subsidiary Pingshan Xi’an Shengda Energy Technology Ltd Co. (“Shengda”). Xi’an TCH contributed cash of $4,559,271(RMB 30,000,000) into Shengda as initial capital. Shengda was set up in order to undertake waste energy recycling projects from a steel and chemical company in Pingshan county as to a Recycling Economy Projects Cooperative Framework Agreement that has been developed by the parties but the final terms for the projects have not been reached and entered, and Shengda is not currently operational.

Hebei Xingtai Steel Group Project

On April 8, 2007, our Board of Directors approved and made effective a TRT Project Joint-Operation Agreement ("Joint-Operation Agreement") which was conditionally entered into on February 1, 2007 between Shanghai TCH and Xi'an Yingfeng Science and Technology Co., Ltd. ("Yingfeng"). Under the Joint-Operation Agreement, Shanghai TCH and Yingfeng jointly pursued a project to design, construct, install and operate two TRT systems for Xingtai Iron and Steel Company, Ltd. ("Xingtai"). Shanghai TCH provided various forms of investments and properties into the project including cash, hardware, software, equipment, major components and devices. In return, Shanghai TCH obtained all the rights, titles, benefits and interests that Yingfeng originally had under the Project Contract, including but not limited to the regular cash payments made by Xingtai and other property rights and interests. On October 31, 2007, Shanghai TCH entered an asset-transfer agreement with Yingfeng to transfer from Yingfeng to Shanghai TCH all electricity-generating related assets owned by Yingfeng. According to the transferred contracts, Shanghai TCH installed and owns two TRT systems and leases them to Xingtai for five years, from January 25, 2007 to January 25, 2012. During the lease, Xingtai will pay Shanghai TCH monthly rent of RMB 0.9 million ($0.13 million) to use the systems. Assuming all amounts due under the lease have been paid, Shanghai TCH will transfer the title of the systems to Xingtai free of charge.

Shanxi Zhangzhi Steel Group Project

Under the Joint-Operation Agreement discussed above, Shanghai TCH and Yingfeng also jointly pursued a project contract, which was entered into between Yingfeng and Zhangzhi Iron and Steel Company, Ltd. ("Zhangzhi") on June 22, 2006, to design, construct, install and operate a TRT system for Zhangzhi Iron. Shanghai TCH provided various forms of investments and properties into the project including cash, hardware, software, equipment, major components and devices. In return, Shanghai TCH obtained all the rights, titles, benefits and interests that Yingfeng originally had under the Project Contract, including but not limited to the regular cash payments made by Xingtai and other property rights and interests. On October 31, 2007, Shanghai TCH acquired this contract as part of its asset-transfer agreement with Yingfeng as discussed above. According to the transferred contracts, Shanghai TCH installed and owns a TRT system and leases it to Zhangzhi for 13 years, from July 25, 2007 to July 25, 2020. During the lease term, Zhangzhi will pay Shanghai TCH a monthly rent of RMB 1.1 million ($0.16 million). After the term is over and all due rents are paid, Shanghai TCH will transfer the title of the system to Zhangzhi free of charge.

Shengwei Group – Tongchuan Project

In November 2007, Shanghai TCH signed a cooperative agreement with Shengwei Group to build two sets of 12MW cement low temperature heat power generation systems for Shengwei's two 2,500-tons-per-day cement manufacturing lines in Jin Yang and for a 5,000-tons-per-day cement manufacturing line in Tong Chuan. At the end of 2008, construction of the cement low temperature heat power generation in Tong Chuan was completed at a cost of approximately $6,191,000 (RMB 43,000,000) and put into operation. Under the original agreement, the ownership of the cement low temperature heat power generation systems would belong to Shengwei from the date the projects were put into service. Shanghai TCH is responsible for the daily maintenance and repair of the projects, and charges Shengwei a monthly electricity fee based on the actual power generated by the projects at 0.4116 RMB per KWH for an operating period of five years with the assurance from Shengwei of a properly functioning 5,000-tons-per-day cement manufacturing line and not less than 7,440 heat hours per year for the electricity generator system. Shengwei Group collateralized the cement manufacturing line in Tong Chuan to guarantee its obligations to provide the minimum electricity income from the power generator system under the agreement during the operating period. At the end of the five year operating period, Shanghai TCH will have no further obligations under the cooperative agreement. On May 20, 2009, Shanghai TCH entered into a supplementary agreement with Shengwei Group to amend the timing for title transfer to the end of the lease term. In addition, the supplementary agreement provided that Shanghai TCH will charge Shengwei based on actual power usage subject to a minimum of $0.31 million (RMB 2.1 million) per month during the operating period.

Shengwei Group – Jinyang Project

On June 29, 2009, construction of the cement low temperature heat power generation system in Jin Yang was completed at a cost of approximately $7,318,000 (RMB 50,000,000) and put into operation. Shanghai TCH charges

Shengwei a technical service fee of $336,600 (RMB 2,300,000) monthly for the sixty months of the lease term. Shengwei has the right to purchase the ownership of the cement low temperature heat power generation system for $29,000 (RMB 200,000) at the end of lease term. Shengwei is required to provide assurance of properly functioning 5,000-tons-per-day cement manufacturing lines and not less than 7,440 heat hours per year for the cement low temperature heat power generation. Shengwei Group collateralized the cement manufacturing lines in Jin Yang to guarantee its obligations to provide the minimum electricity income from the waste energy power generator system under the agreement during the operating period. Effective July 1, 2009, Shanghai TCH outsourced the operation and maintenance of the cement low temperature heat power generation systems in Tong Chuan and JinYang to a third party for $732,000 (RMB 5,000,000) per year.

Shenmu Project

On September 30, 2009, Xi'an TCH delivered to Shenmu County Jiujiang Trading Co., Ltd. ("Shenmu") a set of three 6 MW capacity waste gas power generation systems pursuant to a Cooperative Contract on Coke-oven Gas Power Generation Project (including its Supplementary Agreement) and a Gas Supply Contract for Coke-oven Gas Power Generation Project. These contracts are for 10 years and provide that Xi'an TCH will recycle coke furnace gas from the coke-oven plant of Shenmu to generate power, which will be supplied back to Shenmu. Shenmu agrees to supply Xi'an TCH the coke-oven gas free of charge. Under the contracts, Shenmu will pay us an annual "energy-saving service fee" of approximately $5.6 million in equal monthly installments for the life of the contracts, as well as such additional amount as may result from the supply of power to Shenmu in excess of 10.8 million kilowatt hours per month. We are responsible for operating the projects and will do so through an unrelated third party. Shenmu guarantees that monthly gas supply will not be less than 21.6 million standard cubic meters. If gas supply is less, Shenmu agrees to pay Xi'an TCH the energy-saving service fee described above for up to 10.8 million kilowatt-hours per month. Xi'an TCH maintains the ownership of the project throughout the term of the contracts, including the already completed investment, design, equipment, construction and installation as well as the operation and maintenance of the project. At the end of the 10-year term, ownership of the projects transfers to Shenmu at no charge. Shenmu gave a lien on its production line to guarantee its performance under the Contracts. Shenmu's three major stockholders provided an unlimited joint liability guarantee to Xi'an TCH for Shenmu's performance under the Contracts and the Yulin Huiyuan Group, an independent third party, provides a guarantee to Xi'an TCH for Shenmu's performance under the Contracts.

Erdos Projects

On April 14, 2009, the Company incorporated the JV between Xi’an TCH and Erdos Metallurgy Co., Ltd. (“Erdos”) to recycle waste heat from Erdos' metal refining plants to generate power and steam, which will then be sold back to Erdos. The name of the JV is Inner Mongolia Erdos TCH Energy Saving Development Co., Ltd (“Erdos TCH”) with a term of 20 years, and initial registered capital of $2,635,000 (RMB 18,000,000). As of December 31, 2010, total registered capital was increased to $17.55 million (RMB 120 million), of which $16.37 million (RMB 112 million) was contributed by Xi’an TCH and $1.18 million (RMB 8 million) was from Erdos Metallurgy. Total investment for the project is estimated at approximately $74 million (RMB 500 million) with an initial investment of $17.55 million (RMB 120,000,000). Erdos contributed 7% of the total investment of the project, and Xi’an TCH contributed 93% of the total investment. Xi’an TCH and Erdos will receive 80% and 20% of the profit from the JV, respectively, until Xi’an TCH has received a complete return on its investment. Xi’an TCH and Erdos will then receive 60% and 40% of the profit from the JV, respectively. The profits to be distributed will be computed based on Chinese generally accepted accounting principles. The principal difference between US GAAP and Chinese GAAP with regards to the Erdos TCH project is that a sales-type lease under US GAAP is treated as an operating lease under Chinese GAAP. When the term of the JV expires, Xi’an TCH will transfer its equity in the JV to Erdos at no additional cost.

At the end of 2009, Erdos TCH completed the first 9MW power station of Phase I of the project and put it into operation. At the end of March 2010, Erdos TCH completed the construction of Phase I through completion of the second 9MW power station and delivery of it for operation. Phase I includes two 9MW systems for a combined 18MW power capacity. Pursuant to the Co-operation Agreement and the supplement agreements signed between Erdos and Erdos TCH, Erdos shall purchase all the electricity and steam to be generated from the JV’s power generation systems. Erdos TCH leased the two 9 MW systems to Erdos and is responsible for their operation and maintenance. For each phase of the project, the lease term is 20 years starting from the date of completion of the phase. Erdos agreed to pay a fixed minimum of $0.22 million (RMB 1.5 million) per month for each 9MW capacity power generation system. In addition Erdos will pay the actual amount if the actual sale of the electricity generated is more than $0.22 million (RMB 1.5 million) monthly per unit. Effective January 1, 2010 and April, 2010 respectively, Erdos TCH outsourced to an independent third party the operation and maintenance of the two 9MW power generation projects for $922,000 (RMB 6.27 million) each per year. After 20 years, the units will be transferred to Erdos without any charge.

During the fourth quarter of 2010, Erdos power generation system Phase II two 9MW capacity electricity power generation systems were completed and put into operation. During the first quarter of 2011, Erdos power generation system Phase II the 3rd 9MW capacity electricity power generation system was completed and put into operation through sales type lease with the similar terms to the Phase I project. At March31, 2011, the Company paid approximately $18.19 million for Phase III of the Erdos TCH power generation system projects. The Company currently expects to complete Phase III in the third quarter of 2011.

Biomass Project

On January 20, 2010, Xi'an TCH entered into a Technical Reconstruction Letter of Intent with Xueyi Dong ("Dong") a natural person with Chinese citizenship for Xi'an TCH reconstructing and transforming a Thermal Power Generation Systems owned by Dong into a 12MW Biomass Power Generation Systems ("Biomass Systems" or "BMPG") for approximately RMB 15 million (approximately $2.2 million), of which, RMB 7 million (approximately $1.03 million) was payable to Dong, and RMB 8 million (approximately $1.18 million) was payable to one of the Company's shareholders, who had previously paid that amount to Dong on behalf of the Company.

After the successful transformation of the systems, Xi'an TCH entered into a Biomass Power Generation Asset Transfer Agreement (the "Transfer Agreement") with Dong on June 29, 2010. Under the Transfer Agreement, Dong transferred the Biomass Systems to Xi'an TCH, and Xi'an TCH will pay Dong RMB 100,000,000 (approximately $14,705,900) for the systems, including RMB 20,000,000 in cash and RMB 80,000,000 in shares of the Company's common stock. The stock price will be the same as in the Company's first public offering which is expected to occur in 2010 or 2011, but in no circumstance less than $4 per share. The exchange rate between U.S. Dollar and Chinese RMB in connection with the stock issuance is 1:6.8. As of March 31, 2011, the Company paid the cash portion in full; however, the shares to be issued in connection with this transaction, valued at $7.91 million (the fair value at March 31, 2011), have not been issued.

During the three months ended March 31, 2011, the Company recorded a gain of $1.06 million, which is the change of the fair value of 2,941,176 numbers of shares to be issued to Dong.

Zhongbao Project

On September 30, 2010, Xi'an TCH delivered to Zhongbao Binhai Nickel Co., Ltd. ("Zhongbao") a set of 7 megawatt capacity Waste Heat Power Generation ("WHPG") system, which is an integral part of the facilities designed to produce 80,000 tons of nickel-alloy per year according to the recovery and power generation of waste heat agreement with Zhongbao, an agreement that was transferred from China Zhonggang Binhai Enterprise Ltd. ("Zhonggang") in July 2009. Zhongbao is a nickel-alloy manufacturing joint venture between Zhonggang and Shanghai Baoshan Steel Group established in June 2009. Total investment in this project was approximately $7.8 million (RMB 55 million). The Contract is for 9 years and provided that Xi'an TCH will recycle waste heat from the nickel-alloy rotary kilns of Zhongbao to generate power and steam, which will be supplied back to Zhongbao, and help to reduce over 20,000 tons of carbon dioxide emissions every year. By the end of the term, the system shall be transferred to Zhongbao at RMB 1. Under the Contracts, Zhongbao will pay the Company a monthly "energy-saving service fee" based on the volume of the electricity and steam generated from the WHPG system in the prior month within the first five days of each month at a pre-agreed price, but no less than the minimum monthly payment of $224,000 (RMB 1.5 million). Zhongbao agrees to supply Xi'an TCH the nickel-alloy rotary kilns gas, water and compressed air free of charge, except salty water at RMB 6.3 per ton. Zhongbao also guarantees to continuously supply not less than 6800 heat hours per year for the WHPG, or the operating term will be extended accordingly. Xi'an TCH outsourced its operation and maintenance works to a third party for annual payments of RMB 2.4 million (approximately $352,000) for the whole operation period. In addition, Xi'an TCH shall be responsible for applying Clean Development Mechanism ("CDM") and the net proceeds from CDM will be distributed between Zhonggang and Xi'an TCH at 60% and 40%, respectively. The CDM work has not commenced as of March 31, 2011.

Shannxi Datong Coal Group Power Generation Projects

In February 2011, Xi'an TCH signed a contract with Shannxi Datong Coal Group Steel Ltd Co (Shannxi Datong) to recycle gas and steam from groups of blast-furnaces and converter of Shannxi Datong's metal refining plants to generate power. According to the contract, the Company will install two 3MW TRT and one 15MW WGPG and two 1MW steam power generation systems, with a total of 23MW power capacity for an estimated total investment of $27.45 million (RMB 180 million). The lease term is 30 years. During the lease term, Shannxi Datong will be responsible for operating the projects and pay service fee to the Company. The service fee is based on an average of 8,000 electricity-generating hours per year and RMB 0.33 per kilowatt hour ("Kwh") for the first 5 years from the completion of each power generation station. For each of the leases, at the 6th year, 11th year and 21st year thereafter, the rate will be RMB 0.3 Kwh, 0.27 Kwh and 0.25 Kwh, respectively. After 30 years, the units will be transferred to Shannxi Datong without any charge.

Related Party Transactions

Erdos TCH sold all power generation stations through sales type leases to Erdos Metallurgy Co., Ltd., the noncontrolling interest. Total sales and interest income for this noncontrolling interest was $11.3 million and $1.4 million for the three months ended March 31, 2011, and $10.1 million and $0.3 million for the same period of 2010, respectively.

Critical Accounting Policies and Estimates

Our management's discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which were prepared in accordance with accounting principles generally accepted in the United States ("US GAAP"). The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements as well as the reported net sales and expenses during the reporting periods. On an ongoing basis, we evaluate our estimates and assumptions. We base our estimates on historical experience and on various other factors that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

While our significant accounting policies are more fully described in Note 2 to our consolidated financial statements, we believe that the following accounting policies are the most critical to aid you in fully understanding and evaluating this management discussion and analysis.

Basis of presentation

These accompanying consolidated financial statements were prepared in accordance with US GAAP and pursuant to the rules and regulations of the SEC for annual financial statements.

Basis of consolidation

The consolidated financial statements include the accounts of CREG and, its subsidiary, Sifang Holdings; Sifang Holdings' wholly owned subsidiaries, Huahong and Shanghai TCH; Shanghai TCH's subsidiaries Xi'an TCH and Huaxin; and Xi'an TCH's subsidiary, Shengda and Erdos TCH, in which 93% of Erdos TCH's investment is from Xi'an TCH. Substantially all of the Company's revenues are derived from the operations of Shanghai TCH and its subsidiaries, which represent substantially all of the Company's consolidated assets and liabilities as of March 31, 2011 and December 31, 2010, respectively. All significant inter-company accounts and transactions were eliminated in the consolidation.

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Use of estimates

In preparing these consolidated financial statements, management makes estimates and assumptions that affect the reported amounts of assets and liabilities in the balance sheets and revenues and expenses during the year reported. Actual results may differ from these estimates.

Accounts receivable and concentration of credit risk

Accounts receivable are recorded at the invoiced amounts and do not bear interest. The Company extends unsecured credit to its customers in the ordinary course of business but mitigates the associated risks by performing credit checks and actively pursuing past due accounts. An allowance for doubtful accounts is established and determined based on managements' assessment of known requirements, aging of receivables, payment history, the customer's current credit worthiness and the economic environment.

Financial instruments that potentially subject the Company to credit risk primarily are accounts receivable, receivables on sales-type leases and other receivables. The Company does not require collateral or other security to support these receivables. The Company conducts periodic reviews of its clients' financial condition and customer payment practices to minimize collection risk on accounts receivable.

The operations of the Company are located in the PRC. Accordingly, the Company's business, financial condition, and results of operations may be influenced by the political, economic, and legal environments in the PRC, as well as by the general state of the PRC economy.

Inventory

Inventory is valued at the lower of cost or market. Cost of work in progress and finished goods comprises direct material cost, direct production cost and an allocated portion of production overheads.

Property and equipment

Property and equipment are stated at cost, net of accumulated depreciation. Expenditures for maintenance and repairs are expensed as incurred; additions, renewals and betterments are capitalized. When property and equipment are retired or otherwise disposed of, the related cost and accumulated depreciation are removed from the respective accounts, and any gain or loss is included in operations. Depreciation of property and equipment is provided using the straight-line method over estimated lives as follows:

Building	20 years
Vehicle	2 - 5 years
Office and Other Equipment	2 - 5 years
Software	2 - 3 years

Revenue Recognition

Sales-type Leasing and Related Revenue Recognition

The Company constructs and then leases waste energy recycling power generating projects to its customers. The Company usually transfers ownership of the waste energy recycling power generating projects to its customers at the end of each lease. Investment in these projects is recorded as investment in sales-type leases in accordance with Statement of Financial Accounting Standards (“SFAS”) No. 13, “Accounting for Leases” (codified in Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) Topic 840) and its various amendments and interpretations. The Company manufactures and constructs the waste energy recycling power generating projects and finances its customers for the price of the projects. The sales and cost of sales are recognized at the time of sale or inception of the lease. The investment in sales-type leases consists of the sum of the total minimum lease payments receivable less unearned interest income and estimated executory cost. Unearned interest income is amortized to income over the lease term so as to produce a constant periodic rate of return on the net investment in the lease. While a portion of revenue is recognized at the inception of the lease, the cash flow from the sales-type lease occurs over the course of the lease. Revenue is net of Value Added Tax.

Contingent Rental Income

The Company records the income from actual electricity usage in addition to minimum lease payment of each project as contingent rental income in the period earned. Contingent rent is not part of minimum lease payments.

Foreign Currency Translation and Comprehensive Income (Loss)

The Company's functional currency is the Renminbi ("RMB"). For financial reporting purposes, RMB were translated into United States dollars ("USD") as the reporting currency. Assets and liabilities are translated at the exchange rate in effect at the balance sheet date. Revenues and expenses are translated at the average rate of exchange prevailing during the reporting period. Translation adjustments arising from the use of different exchange rates from period to period are included as a component of stockholders' equity as "Accumulated other comprehensive income". Gains and losses from foreign currency transactions are included in income. There has been no significant fluctuation in exchange rate for the conversion of RMB to USD after the balance sheet date.

The Company uses SFAS 130 "Reporting Comprehensive Income." Comprehensive income is comprised of net income and all changes to the statements of stockholders' equity, except those due to investments by stockholders, changes in paid-in capital and distributions to stockholders.

Recent Accounting Pronouncements

In April 2010 the FASB issued Accounting Standards Update (ASU) No. 2010-13, *Compensation – Stock Compensation (Topic 718): Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Currency of the Market in Which the Underlying Equity Security Trades.* This Update provides amendments to Accounting Standards Codification (ASC) Topic 718 to clarify that an employee share-based payment award with an exercise price denominated in the currency of a market in which a substantial portion of the entity's equity securities trades should not be considered to contain a condition that is not a market, performance, or service condition. Therefore, an entity would not classify such an award as a liability if it otherwise qualifies as equity. The amendments in this Update are effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2010. The amendments in this Update should be applied by recording a cumulative-effect adjustment to the opening balance of retained earnings. The cumulative-effect adjustment should be calculated for all awards outstanding as of the beginning of the fiscal year in which the amendments are initially applied, as if the amendments had been applied consistently since the inception of the award. The cumulative-effect adjustment should be presented separately. Earlier application is permitted. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In December 2010, FASB issued ASU No. 2010-28, *Intangibles – Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts.* The amendments in this Update affect all entities that have recognized goodwill and have one or more reporting units whose carrying amount for purposes of performing Step 1 of the goodwill impairment test is zero or negative. The amendments in this Update modify Step 1 so that for those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that impairment may exist. The qualitative factors are consistent with existing guidance, which requires that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The amendments in this Update are effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. Early adoption is not permitted. Upon adoption of the amendments, any resulting goodwill impairment should be recorded as a cumulative-effect adjustment to beginning retained earnings in the period of an adoption. Any goodwill impairments occurring after the initial adoption of the amendments should be included in earnings. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In December 2010, FASB issued ASU No. 2010-29, *Business Combinations (Topic 805): Disclosure of Supplementary Pro Forma Information for Business Combinations.* The amendments in this Update specify that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The amendments also expand the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments in this Update are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The Company intends to adopt the disclosure requirements for any business combinations in 2011and thereafter.

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On March 5, 2010, the FASB issued ASU No. 2010-11 Derivatives and Hedging Topic 815 "Scope Exception Related to Embedded Credit Derivatives." This ASU clarifies the guidance within the derivative literature that exempts certain credit related features from analysis as potential embedded derivatives requiring separate accounting. The ASU specifies that an embedded credit derivative feature related to the transfer of credit risk that is only in the form of subordination of one financial instrument to another is not subject to bifurcation from a host contract under ASC 815-15-25, Derivatives and Hedging — Embedded Derivatives — Recognition. All other embedded credit derivative features should be analyzed to determine whether their economic characteristics and risks are "clearly and closely related" to the economic characteristics and risks of the host contract and whether bifurcation is required. The ASU is effective for the Company on July 1, 2010. Early adoption is permitted. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In January 2010, FASB issued ASU No. 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements.* This update provides amendments to ASC Topic 820 that will provide more robust disclosures about (1) the different classes of assets and liabilities measured at fair value, (2) the valuation techniques and inputs used, (3) the activity in Level 3 fair value measurements, and (4) the transfers between Levels 1, 2, and 3. This standard is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In January 2010, FASB issued ASU N0. 2010-01, *Equity (Topic 505): Accounting for Distributions to Shareholders with Components of Stock and Cash.* The update clarifies that the stock portion of a distribution to shareholders that allows them to elect to receive cash or stock with a potential limitation on the total amount of cash that all shareholders can elect to receive in the aggregate is considered a share issuance that is reflected prospectively in earnings per share and is not considered a stock dividend for purposes of ASC Topic 505 and Topic 260, *Earnings Per Share*. This standard is effective for interim and annual periods ending on or after December 15, 2009, and should be applied on a retrospective basis. The adoption of this standard did not have a material impact to the Company's financial position or results of operations.

RESULTS OF OPERATIONS

Comparison of Three Months Ended March 31, 2011 and 2010

The following table sets forth the results of our operations for the periods indicated as a percentage of net sales:

	2011			2010		
	$	% of Sales		$	% of Sales	
Sales	$11,563,149	100	%	$10,125,436	100	%
Sales of products	11,271,254	97	%	10,125,436	100	%
Contingent rental income	291,895	3	%	-	-	
Cost of sales	(8,456,032)	73	%	(7,798,245)	77	%
Cost of products	(8,456,032)	73	%	(7,798,245)	77	%
Gross profit	3,107,117	27	%	2,327,191	23	%
Interest income on sales-type lease	5,138,303	44	%	3,094,568	31	%
Total operating income	8,245,420	71	%	5,421,759	54	%
Total operating expenses	(1,767,689)	15	%	(1,359,697)	14	%
Income from operations	6,477,731	56	%	4,062,062	40	%
Total non-operating income (expenses), net	1,059,127	9	%	(439,896)	(4	)%
Income before income tax	7,536,858	65	%	3,622,166	36	%
Income tax expense	1,395,930	12	%	1,036,766	10	%
Less: net income attributable to noncontrolling interest	519,138	4	%	394,441	4	%
Net income attributable to China Recycling Energy Corp	$5,621,790	49	%	$2,190,959	22	%

SALES. Net sales of systems for the three months ended March 31, 2011 were $11.56 million while our net sales for the same period of 2010 were $10.13 million, an increase of $1.44 million. The increase was primarily due to the completion and sale of the 3rd 9MW capacity power station of Erdos Phase II project through sales-type leasing arrangements in the first quarter of 2011; in comparison, net sales for the same period, in fiscal year 2010, reflected the completion and sale of the 2nd 9MW capacity power station of Erdos Phase II project through sales-type leasing arrangements. For the three months ended March 31, 2011, the Company received contingent rental income of $0.29 million, compared to no contingent rental income for the same period in fiscal year 2010. The increase in contingent rental income resulted from actual usage of the electricity, in addition to the minimum lease payments we received in the first quarter of 2011 from our Shengwei Group - Tongchuan Project, Erdos Project and Shenmu Project. For the sales-type lease, sales and cost of sales are recorded at the time of leases; the interest income from the sales-type leases is our other major revenue source in addition to sales revenue.

COST OF SALES. Cost of sales for the first quarter of 2011 was $8.46 million while our cost of sales for the comparable period of 2010 was $7.80 million, an increase of $0.66 million. Our cost of sales for the first quarter of 2011 consisted of the 3rd 9MW recycling waste heat power generation system of Erdos Phase II project. For the first quarter of 2010, the cost of sales was for Erdos Phase I the second 9MW recycling wasted heat power generation system.

GROSS PROFIT. Gross profit was $3.11 million for the three months ended March 31, 2011 compared to $2.33 million for the same period of 2010, a gross margin of 27% and 23% for the comparable period of 2011 and 2010, respectively. The gross profit was mainly from the selling of the Erdos Phase II 3rd 9MW capacity power station in the first quarter of 2011, and contingent rental income of $0.29 million, while in the first quarter of 2010, it was mainly for the selling of the Erdos Phase I second 9 MW power generation system.

OPERATING INCOME. Operating income was $8.25 million for the first quarter of 2011 while our operating income for the first quarter of 2010 was $5.42 million, an increase of $2.82 million. The growth in operating income was mainly due to the increase in interest income from selling and leasing our energy saving systems through sales-type leasing.

INTEREST INCOME ON SALES TYPE LEASES. Interest income on sales-type leases for the three months ended March 31, 2011 was $5.14 million, a $2.05 million increase from $3.09 million for the comparable period of 2010. During the first quarter of 2011, the interest income was derived from eleven systems: two TRT systems, two CHPG systems, one WGPG system, two waste heat power generating systems associated with our Erdos Phase I project and two systems of Erdos Phase II project, the Pucheng biomass power generation system and Zhongbao WHPG system. The 3rd 9MW waste heat power generating system of Erdos Phase II project was sold at the first quarter of 2011 and will start to generate interest income in April of 2011. During the first quarter of 2010, the interest income was from seven systems: two TRT systems, two CHPG systems, one WGPG system, and two waste heat power generating systems associated with our Erdos Phase I project.

OPERATING EXPENSES. Operating expenses consisted of selling, general and administrative expenses totaling $1.77 million for the first quarter of 2011 as compared to $1.36 million for the same period of 2010, an increase of $0.41 million or 30%. The increase was due to proportional increases in our payroll, welfare, business trip and marketing expenses as a result of the sale of the 3rd 9MW recycling waste heat power generation system of Erdos Phase II project and continuous expansion of our business; in addition, we recorded $1.11 million compensation expense for stock options during the first quarter of 2011, compared to $0.74 million for the same period of 2010.

NON-OPERATING INCOME (EXPENSES). Non-operating expenses consisted of non sales-type lease interest income, interest expense, bank charges and some miscellaneous expenses. For the three months ended March 31, 2011, net non-operating income was $1.06 million as compared to net non-operating expense of $439,896 for the comparable period of 2010. In the first quarter of 2011, we had $1 million interest expense on loans, $1.52 million interest expense arising from the beneficial conversion feature of the convertible note from Carlyle and China Cinda, but offset by $2.53 million from changes in fair value of conversion feature liability of the convertible note from China Cinda, and $1.06 million from changes in fair value of the liability for shares to be issued to Dong; while in the same period of 2010, the interest expense was $567,474, offset by interest and other income of $127,000.

INCOME TAX EXPENSE. The income tax expense was $1.40 million for the first quarter of 2011, an increase of $0.36 million from $1.04 million for the comparable period of 2010. The increase was mainly due to the increase of income before income tax from $3.62 million for the first quarter of 2010 to $7.54 million for the same period of 2011. The consolidated effective income tax rate for the first quarter of 2011 and 2010 was 18.5% and 28.6%, respectively. The change in the consolidated effective tax rate was mainly due to effective tax holiday, valuation allowance on NOL, and permanent non-tax deductible interest expense resulting from amortization of a beneficial conversion feature for a convertible note, but offset with non-taxable income from changes in fair value of conversion feature liability and changes in fair value of the liability for shares to be issued to Dong, which accounted for net (0.2)% and 4.2% of pretax income for the three months ended March 31, 2011 and 2010, respectively; non-tax deductible expenses were added back to taxable income for US income tax return purposes and non-taxable income were subtracted from taxable income. The income tax rate for Shanghai TCH was 24% and 22% for 2011 and 2010, respectively. Xi'an TCH's effective income tax rate for 2011 and 2010 is 15% as a result of its high tech enterprise status that was approved by the taxing authority. Xingtai Huaxin's effective income tax rate for 2011 and 2010 is 25%. Huahong, Erdos TCH and Shengda's effective income tax rate for 2011 is 25%.

NET INCOME. Our net income for the three months ended March 31, 2011 was $5.62 million compared to $2.19 million for the same period of 2010, an increase of $3.43 million. This increase in net income was mainly due to increased interest income from lease payments for energy saving systems compared with the first quarter of 2010, changes in fair value of the liability for shares to be issued to Dong, as well as the sale of the 3rd 9MW recycling waste heat power generation system of the Erdos Phase II project.

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Liquidity and Capital Resources

Comparison of Three Months Ended March 31, 2011 and 2010

As of March 31, 2011, the Company had cash and cash equivalents of $21.91 million, other current assets were $9.43 million and current liabilities were $28.06 million. Working capital was $3.28 million. The debt-to-equity ratio was 0.66:1 at March 31, 2011.

The following is a summary of cash provided by or used in each of the indicated types of activities during the three month ended March 31, 2011and 2010:

	2011	2010
Cash provided by (used in):		
Operating Activities	$(475,487)	$652,729
Investing Activities	2,164,601	(357,812)
Financing Activities	9,020,273	1,830,783

Net cash flow used in operating activities was $475,487 during the first quarter of 2011, as compared to $652,729 provided by the comparable period of 2010. The increase in net cash outflow was mainly from the sale of our 3rd 9MW recycling waste heat power generation system of the Erdos Phase II project through sales-type lease for $11.56 million. This project commenced construction in 2010 and was completed in the first quarter of 2011, which resulted in cash inflow from construction in progress in 2011, but we paid $5.34 million for constructing Shannxi Datong Coal Group Power Generation Projects. The construction was considered an operating activity due to the similar nature of producing inventory for sale. Cash received from collection of principal on sales type leases was $1.91 million in the first quarter of 2011 compared with $0.96 million in the same period of 2010, an increase of $0.95 million.

Net cash flow provided by investing activities was $2.16 million in the first quarter of 2011, compared to $0.36 million used in the comparable period of 2010. The increase of net cash flow provided by investing activities was mainly due to the release of restricted cash of 2.16 million from the bank which we previously deposited in the bank as collateral for the bank acceptances. While in the same period of 2010, we deposited into bank of $0.27 million as restricted cash and purchased equipment for $91,879.

Net cash flow provided by financing activities was $9.02 million for the quarter ended March 31, 2011 compared to net cash provided by financing activities of $1.83 million for the comparable period in 2010. The increase was mainly due to the $7.58 million proceeds from convertible notes from China Cinda, $4.1 million proceeds from a bank loan, despite repayment on notes payable (bank acceptances) of $2.89 million and repayment of bank loan for $0.46 million.

On June 29, 2010, Xi'an TCH entered into a Biomass Power Generation Asset Transfer Agreement (the "Transfer Agreement") with Dong, a natural person with Chinese citizenship. Under the Transfer Agreement, Dong transferred the Biomass Systems to Xi'an TCH, and Xi'an TCH will pay Dong RMB 100,000,000 ($14,705,900) for the systems, including RMB 20,000,000 in cash and RMB 80,000,000 with equivalent shares of the Company's common stock. The stock price will be the same price as the Company's public offering price in the first public offering which occurs in 2010 or 2011 but in no circumstance less than $4 per share. The exchange rate between U.S. Dollar and Chinese RMB in connection with the stock issuance is 1:6.8. As of March 31, 2011, the Company recorded shares to be issued of $7.91 million (the fair value at March 31, 2011) in connection with this transaction, although the shares have not yet been issued.

We believe we have sufficient cash to continue our current business through 2011 due to stable recurring receipts from interest income from sales-type leases in place. As of March 31, 2011, we have two TRT systems, two CHPG systems, one WGPG system, five recycling waste heat power generating systems from the Erdos projects, one BMPG and one WHPG of Zhongbao, currently generating net cash inflow. In addition, we have access to bank loans in case of an immediate need for working capital. We believe we have sufficient cash resources to cover our anticipated capital expenditures in 2011.

We do not believe inflation has had a significant negative impact on our results of operations during 2011.

Off-Balance Sheet Arrangements

We have not entered into any other financial guarantees or other commitments to guarantee the payment obligations of any third parties. We have not entered into any derivative contracts that are indexed to our shares and classified as stockholder's equity or that are not reflected in our consolidated financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. We do not have any variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

Contractual Obligations

Convertible Notes Payable - Carlyle

On April 29, 2008, we issued and sold to Carlyle Asia Growth Partners III, L.P. (“CAGP”) and CAGP III Co. Investment, L.P. (together with CAGP, the “Investors”) a 5% Secured Convertible Promissory Note of $5,000,000. The terms for the Note were amended and restated on April 29, 2009.

This note bears interest at 5% and matured on April 29, 2011. The principal amount of the note, together with any interest thereon, convert, at the option of the holders at any time on or after March 16, 2010 and prior to maturity, into shares of the Company’s common stock at an initial conversion price tied to the after-tax net profits of the Company for the fiscal year ending December 31, 2009. Based on our after-tax profits in 2009, the conversion price is $1.148 per share, and this note was convertible in full into 4,577,851 shares of our common stock as of March 31, 2011. Prior to the maturity date, the Investors informally expressed their intent to exercise their conversion rights on the terms and conditions set forth herein; however, as of May 16, 2011, the Company has not yet received formal notice from the Investors, indicating that the Investors have elected to exercise their conversion rights, and, as such, the formal conversion process has not yet commenced and the shares to be issued upon conversion to the Investors have not been issued. The obligation of the Company under this note is ranked senior to all other debt of the Company. The note is secured by a security interest granted to the investors pursuant to a share pledge agreement. This pledge was released during the fiscal quarter ended March 31, 2011 and is of no further force or effect

On April 29, 2009, we issued an 8% Secured Convertible Promissory Note of $3 million to Carlyle Asia Growth Partners III, L.P. with a maturity date of April 29, 2012. The note holder has the right to convert all or any part of the aggregate outstanding principal amount of this note, together with interest, if any, into shares of our common stock, at any time on or after March 16, 2010 and prior to the maturity date (or such later date on which this note is paid in full), at a conversion price per share of common stock equal to US $0.80, and this note was convertible in full into 3,750,000 shares of our common stock as of March 31, 2011. These conversion shares rank pari-passu with those issuable under the 5% Secured Convertible Promissory Note.

Loan Payable – Collective Capital Trust Plan

On December 3, 2009, Beijing International Trust Co., Ltd. (“Beijing Trust”) formed a Low Carbon Fortune-Energy Recycling No. 1 Collective Capital Trust Plan (“Plan”), pursuant to the Capital Trust Loan Agreement entered into by Erdos TCH Energy Saving Development Co., Ltd and Beijing Trust dated November 19, 2009. Under the Plan, Beijing Trust raised RMB 181,880,000 ($26.75 million) through the sale of 181,880,000 total trust units at RMB 1 per unit. All amounts raised under the Plan are loaned to Erdos TCH in connection with the construction and operation of

Phases II and III of the Erdos Power Generation Projects. These projects, when completed, will recycle waste heat from Erdos Metallurgy's metal refining plants to generate electric power and steam, which will then be sold back to Erdos Metallurgy.

The Plan included 145,500,000 category A preferred trust units ($21.4 million), consisting of 12,450,000 category A1 preferred trust units ($1.8 million), 15,000,000 category A2 preferred trust units ($2.2 million), 118,050,000 category A3 preferred trust units ($17.4 million); and 36,380,000 category B secondary trust units ($5.35 million), consisting of 9,100,000 category B1 secondary trust units ($1.34 million) and 27,280,000 category B2 secondary trust units ($4.01 million). The B1 units were purchased by members of management of Erdos TCH and the B2 units were purchased by Xi'an TCH. Under the Agreement, the annual base interest rate is 9.94% for A1 preferred trust fund units with a term of two years, 11% for A2 preferred trust fund units with a term of three years, 12.05% for A3 preferred trust fund units and 8.35% for the category B secondary trust fund units, each with a term of four years.

Erdos TCH gave a lien on its equipment, assets and accounts receivable to guarantee the loans under the Agreement. Xi'an TCH and Mr. Guohua Ku, our CEO, also gave unconditional and irrevocable joint liability guarantees to Beijing Trust for Erdos TCH's performance under the Agreement. Erdos (the minority stockholder and customer of Erdos TCH) provided a commitment letter on minimum power purchase from Erdos TCH.

On December 18, 2009, an additional RMB 25,000,000 ($3.68 million) was raised by Beijing Trust to support the Company's Erdos Power Generation Projects. Beijing Trust sold 25,000,000 trust units at RMB 1 per unit which included 20,000,000 category A1 preferred trust units ($ 2.94 million) and 5,000,000 category B2 secondary trust units ($ 0.74 million). The B2 units were purchased by Xi'an TCH.

During December 2009, the Company sold aggregate 206,880,000 units for RMB 206,880,000 ($30.30 million), of which 9,100,000 units ($1.33 million) were purchased by the management of Erdos TCH; 32,280,000 units ($4.73 million) were purchased by Xi'an TCH; the amount of $4.73 million was considered as investment by Xi'an TCH into Erdos TCH and, accordingly, was eliminated in the Company's consolidated financial statements.

On April 15, 2010, Beijing Trust completed the second expansion of the Plan. The second expansion of the Plan raised RMB 93,120,000 ($13.69 million) through the sale of 93,120,000 trust units at RMB 1 per unit. All amounts raised under the Second Expansion of the Plan are to be loaned to Erdos TCH. The second expansion of the Plan includes 2,800,000 category A1 preferred trust units ($0.41 million), 5,000,000 category A2 preferred trust units ($0.73 million), 66,700,000 category A3 preferred trust units ($9.81 million) and 4,650,000 category B1 preferred trust units ($0.68 million) and 13,970,000 category B2 secondary trust units ($2.05 million). The B1 units were purchased by members of management of Erdos TCH and the B2 units have been purchased by Xi'an TCH. With the completion of the second expansion of the Plan, the Low Carbon Fortune-Energy Recycling No. 1 Collective Capital Trust Plan has reached RMB 300,000,000 ($44.12 million) and completed its entire trust plan fund raising work. The net long term loan payable under this trust plan was RMB 252,150,000 ($38.5 million) at March 31, 2011. Interest expense accrued on this trust loan was $5.9 million and $4.5 million at March 31, 2011 and December 31, 2010, respectively.

In addition to the above, under the Loan Agreement, Erdos TCH must pay a management incentive benefit to Beijing Trust upon maturity of the category A3 and category B trust units in December 2013 if the ratio of Erdos TCH's profit to its registered capital exceeds a base amount. If this criterion is met, the amount of the management incentive benefit is calculated based on a formula tied to Erdos TCH's net profit and the average registered capital for the 2012 fiscal year. Under this formula the management incentive benefit could range between 0% and 100% of the net profit of Erdos TCH in the 2012 fiscal year.

The management incentive benefit was structured to provide an incentive to management to make the joint venture profitable. Under the Plan, Beijing Trust will distribute the entire amount of the management incentive benefit it receives to the holders of the category B trust units. As previously disclosed, the holders of the category B trust units are the management of Erdos TCH and Xi'an TCH. Category B trust units receive a lower base interest rate than the category A trust units but the economic return to the holders of category B trust units will be enhanced by any management incentive benefit.

Erdos TCH also agrees to share the benefits from Clean Development Mechanism ("CDM") under the Kyoto Protocol equally with Beijing Trust during the term of the loan. Any benefit received from CDM will be paid to Erdos Metallurgy first. Under the agreement with Xi'an TCH, Erdos Metallurgy agrees to deliver to Xi'an TCH 50% of the benefit Erdos Metallurgy receives. Xi'an TCH agrees to share 50% of the benefit it receives from Erdos Metallurgy with Erdos TCH. Under the Capital Trust Loan Agreement between Erdos TCH and Beijing Trust, Erdos TCH agrees that 50% of any benefit it receives will be delivered to Beijing Trust. Pursuant to the Plan, Beijing Trust will distribute 70% of the CDM benefit it receives to the holders of the category B trust units. The receipt of any CDM benefit is subject to a process of evaluation and certification of the project by the CDM Executive Board and is under the guidance of the Conference of the Parties of the United Nations Framework Convention on Climate Change. The first stages of the certification process have been completed successfully.

Bank Long Term Loan

The Company entered a loan agreement with Industrial Bank Co., Ltd., Xi'an Branch (the "Lender") for a loan designed for energy saving and emission reduction projects, whereby the Lender agreed to loan RMB 30,000,000 ($4,529,875) to Xi'an TCH for three years from April 6, 2010 to April 6, 2013. The proceeds of the loan are required to be used for equipment for Xi'an TCH's energy saving and emission reduction projects. The Loan Agreement has a floating interest rate that resets at the beginning of each quarter at 110% of the national base interest rate for the same term and same level loan (currently 5.4%). Under the loan, Xi'an TCH is required to make quarterly interest payments and, beginning six months after the date of the release of the funds, to make minimum quarterly principal payments of RMB 3,000,000 (approximately $452,987) each quarter. The Loan Agreement contains standard representations, warranties and covenants, and the loan is guaranteed by Xi'an TCH, Shaanxi Shengwei Construction Material Group and Mr. Guohua Ku. At March 31, 2011, $457,568 of the principal was repaid and $1,830,273 is schedule to be repaid within one year.

The Company entered another loan agreement with the same Industrial Bank for energy saving and emission reduction projects, whereby the Lender agreed to loan RMB 30,000,000 ($4,575,682) to Xi'an TCH for three years from March 31, 2011 to March 30, 2014. As of March 31, 2011, the Company received RMB 27,000,000 ($4,118,114) of the loan. The proceeds of the loan are required to be used in payment for construction and equipment purchase for Xi'an TCH's energy saving and emission reduction projects. The Loan Agreement has a floating interest rate that resets at the beginning of each quarter at 115% of the national base interest rate for the same term and same level loan (currently 7.015%). Under the loan, Xi'an TCH is required to make quarterly interest payments and, beginning six months after the date of the release of the funds, to make minimum quarterly principal payments of RMB 3,000,000 ($457,568) each quarter. The Loan Agreement contains standard representations, warranties and covenants, and the loan is guaranteed by Xi'an TCH, Mr. Guohua Ku and Ms Chaoying Zhang.

Convertible note agreement with China Cinda

On August 18, 2010, the Company and its wholly-owned subsidiaries Sifang, Shanghai TCH and Xi'an TCH entered into a Notes Purchase Agreement (the "Note Agreement") with China Cinda (HK) Asset Management Co., Ltd, a company organized under the laws of the Hong Kong Special Administrative Region of China ("Cinda"). Under the terms of the Note Agreement, the Company will issue to Cinda two tranches of convertible notes (the "Notes"), each having a principal amount equal to the US Dollar equivalent of RMB 50 million ($7.6 million). Also on August 18, 2010, Xi'an TCH and China Jingu International Trust Co. Ltd. ("Jingu"), an affiliate of Cinda also entered into a Capital Trust Loan Agreement ("Trust Loan Agreement"), in which Jingu will raise 100 million RMB under a Jingu CREG Recycling Economy No. 1 Collective Fund Trust Plan ("Trust Plan") and lend such amount under the Trust Plan to Xi'an TCH (the "Loans"). If the Loans under the Trust Loan Agreement do not occur, then under the Note Agreement the principal amount of the Notes to be issued in each tranche will be the US dollar equivalent of RMB 100 million ($15.2 million). All proceeds from the Notes and the Loans will be used to complete the Phases IV and V of the Erdos TCH Energy Saving Development Co., Ltd. ("Erdos TCH") project, a joint venture between Xi'an TCH and Erdos Metallurgy Co., Ltd. to recycle waste heat from Erdos Metallurgy's refining plants to generate power and steam and sell them back to Erdos Metallurgy, as well as other working capital needs.

The term of the Loans is for three years from the date of the first draw. The interest rate for the Loans is the People's Bank of China ("PBOC")'s three year loan base interest rate plus two percent (2%). If the Loans are not fully exchanged for shares of the Common Stock of the Company as described below prior to maturity, Xi'an TCH will pay the difference between the interest rate described above and 18% on the outstanding amount. Under the Trust Loan Agreement and separate agreements entered by Jingu, Erdos TCH, Shanghai TCH, Xi'an TCH and Mr. Guohua Ku on August 18, 2010, Erdos TCH shall pledge the accounts receivable, equipment and assets of its Phases IV and V projects to Jingu as a guarantee to the Loans, Xi'an TCH shall pledge its 80% equity in Erdos TCH to Jingu as a guarantee to the Loans, Shanghai TCH shall provide a joint liability guarantee to Jingu for the Loans, and Mr. Guohua Ku shall provide his personal joint liability to Jingu for the Loans.

Under the Note Agreement the Notes shall be issued before August 18, 2011. The Notes have a three year maturity date from the date of the issuance of the first tranche. The exchange rate between RMB and US Dollar for each issue of Notes is the middle rate published by the PBOC for the second business day prior to each issuance. Each Note bears interest at a rate equal to that of PBOC base interest rate for the relevant interest period (the period commencing on and including January 1 of each year and ending on and including December 31 of such year) plus two percent (2%). If Cinda does not convert or fully convert the Notes to shares prior to maturity, the Company will pay the difference between the interest rate described above and 18% on the outstanding amount.

As collateral for the Notes, Mr. Guohua Ku, the CEO and a major shareholder of the Company, has entered into a Share Pledge Agreement with Cinda, on August 18, 2010, to pledge 4,500,000 shares of the Company's common stock held by him to secure the first Note. The Agreement also calls for an additional 4,500,000 shares of the Company's common stock held by Mr. Ku to secure the second Note before its issuance. On December 30, 2010, the Company received proceeds of RMB50, 000,000 ($7,533,391) from the first tranche of the loan. On January 30, 2011, the

Company received proceeds of RMB 50,000,000 ($7,533,391) from the second tranche of the loan.

Commitments

Erdos Phase III of Power Generation Projects

In April 2009, Erdos TCH signed a contract with Erdos Metallurgy to recycle heat from groups of furnaces of Erdos Metallurgy's metal refining plants to generate power and steam, to be sold back to Erdos Metallurgy. According to the contract, Erdos TCH will install a group of power generation projects with a total of 70MW power capacity, which may grow up to 120MW, and 30-ton steam per hour, with an estimated total investment in excess of $75 million (RMB 500 million). The Company split the construction of the projects into three phases, two units of power generation in Phase I with a total of 18MW power capacity, three units in Phase II with a total of 27MW power capacity and one unit in Phase III with 25MW power capacity. For each phase of the project, the lease term is 20 years starting from the date of completion of the phase. During the lease term, Erdos TCH will be responsible for operating the projects and charge Erdos Metallurgy for supply of electricity and steam. Erdos Metallurgy agreed to pay a fixed minimum of $0.22 million (RMB 1.5 million) per month for each 9MW capacity power generation system.

During the first quarter of 2010, Erdos power generation system Phase I project was completed and put into operation. During the fourth quarter of 2010 and first quarter of 2011, three 9MW power generation systems of Phase II were completed and put into operation. Erdos TCH outsourced to an independent third party the operation and maintenance of the power generation system for $922,000 (RMB 6.27 million) per year for each system. After 20 years, the systems will be transferred to Erdos without any charge.

As of March 31, 2011 the projects of Erdos Phase III are under construction. At March 31, 2011, the Company has paid approximately $18.19 million for Phase III. The Company expects the completion of Phase III projects no later than the end of 2011.

Shannxi Datong Coal Group Power Generation Projects

In February 2011, Xi'an TCH signed a contract with Shannxi Datong Coal Group Steel Ltd Co (Shannxi Datong) to recycle gas and steam from groups of blast-furnaces and converter of Shannxi Datong's metal refining plants to generate power. According to the contract, the Company will install two 3MW TRT and one 15MW WGPG and two 1MW steam power generation systems, with a total of 23MW power capacity for an estimated total investment of $27.45 million (RMB 180 million). The lease term is 30 years. During the lease term, Shannxi Datong will be responsible for operating the projects and pay a service fee to the Company. The service fee is based on an average of 8,000 electricity-generating hours per year and RMB 0.33 per kilowatt hour ("Kwh") for the first 5 years from the completion of each power generation station. For each of the leases, at the 6th year, 11th year and 21st year thereafter, the rate will be RMB 0.3 Kwh, 0.27 Kwh and 0.25 Kwh, respectively. After 30 years, the units will be transferred to Shannxi Datong without any charge.

On February 28,2011, Xi’an TCH entered into an agreement with Xi’an Huaxin Energy Tech Co., Ltd (the contractor for construction) for Shannxi Datong Coal projects of two 3MW TRT and one 15 MW WGPG systems described above. The project is scheduled to complete in 12 months from construction commencement.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Not applicable.

Item 4. Controls and Procedures.

Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures which are designed to provide reasonable assurance that information required to be disclosed in the Company's periodic SEC reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to its principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's "disclosure controls and procedures," as such term is defined in Rules 13a – 15(e) and 15d – 15(e) of the Securities Exchange Act of 1934 ("Exchange Act") at the end of the period covered by the report.

Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, at March 31, 2011, the Company's disclosure controls and procedures were effective to provide reasonable assurance that (i) the information required to be disclosed by us in this Report was recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (ii) information required to be disclosed by us in our reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

With the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, the Company also conducted an evaluation of the Company's internal control over financial reporting to determine whether any changes occurred during the Company's fiscal quarter ended March 31, 2011, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Based on such evaluation, management concluded that, as of the end of the period covered by this report, there have not been any changes in the Company's 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 fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

The Company is not currently involved in any material pending legal proceedings.

Item 1A. Risk Factors

There have been no material changes in our risk factors from those disclosed in Part I, Item 1A, of our Annual Report on Form 10-K as of and for the year ended December 31, 2010.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Removed and Reserved.

None

Item 5. Other Information

None

Item 6. Exhibits

Exhibit Number	Description
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a).*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a).*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350.*
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350.*

* Filed herewith.

SIGNATURES

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

	CHINA RECYCLING ENERGY CORPORATION (Registrant)
Date: July 18, 2013	/s/ Guohua Ku Guohua Ku Chairman of the Board and Chief Executive Officer
Date: July 18, 2013	/s/ David Chong David Chong Secretary, Principal Financial Officer and Principal Accounting Officer

EXHIBIT INDEX

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*Filed herewith.