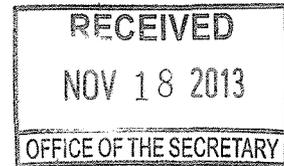


SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934

Admin. Proc. File No. 3-15508



In the Matter of the Application of

SMARTHEAT INC.

c/o James Kopecky
Kopecky, Schumacher, Bleakley, & Rosenberg, P.C.
203 N. LaSalle St.
Suite 1620
Chicago, Illinois 60601

For Review of Action Taken by
The NASDAQ Stock Market, LLC

Brief of Applicant SmartHeat, Inc.

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SmartHeat, Inc. (“Company”) seeks review of the decision of The NASDAQ Stock Market LLC (“NASDAQ”) to delist Company’s common stock from the NASDAQ Stock Market. NASDAQ based its delisting decision on the finding that the restructuring of Company violated NASDAQ Rule 5101. SmartHeat submits that this decision was an abuse of NASDAQ’s discretion, and respectfully requests that the decision be reversed.

BACKGROUND

A. SmartHeat, Inc.

Company is a Nevada corporation that was formed in 2008 through a merger between an existing Nevada shell company and a Chinese company that makes heat exchangers. At the end of the transaction, Company became a holding company, with the Chinese company as its subsidiary. Company was listed on the NASDAQ beginning in January 2009. NASDAQ Staff Delisting Determination (Aug. 23, 2012) (“Staff Determination”).

B. The May 30, 2012, Management Changes

During the period from late 2011 to the spring of 2012, the board of Company became aware of, and increasingly concerned about, certain circumstances. These include: 1) regulatory concern and public criticism of reverse merger companies; 2) perceived public market bias and inflammatory blogs and postings on internet message boards regarding Chinese companies traded in the U.S. markets and the integrity of their Chinese managements; 3) investigations regarding Mr. Ben Wey, who played a role in forming Company; 4) the quality and reliability of advice and services that the Company had been, and was being, offered by third-party advisers

and service providers; and 5) language and cultural differences that made it more difficult for Chinese speakers to deal with information requests from reporters, stockholders, regulatory and other government agencies. *See SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination at 12 (Oct. 11, 2012).*

During 2012 Q2, the Board determined that a broad brush restructuring was necessary. The restructuring was intended to reform the turnkey organizational structure inherited as part of the reverse merger and to put in place an organizational structure, management team and reporting and governance structure which would facilitate compliance with U.S. regulatory requirements and U.S. capital market expectations. To achieve the desired restructuring, the following actions were taken:

- Retention of a U.S. (English as first language) adviser to oversee all restructuring efforts. Nimbus Restructuring Manager LLC offered knowledge and experience in both the U.S. and China capital markets, legal systems and regulatory environments.

- Restructuring the Board and realigning management to enhance the ability of the Company to act in accordance with best U.S. corporate and management practices. As part of this effort, CEO James Jun Wang voluntarily resigned to take a position at the company's Chinese subsidiary. In addition, Zhijuan Gho resigned as the CFO. These persons were replaced by experienced executives of American companies, who were well-versed in U.S. management practices. Moreover, two new directors joined the company's five member board.

- Restructuring the Company's capital structure in order to optimize its borrowing capacity and overall cost and availability of capital for the Company and its subsidiaries. This included securing a \$1,000,000 line of credit from a lender affiliated with the former CEO James Jun Wang.

Id. at 12-13, 16-17, 21-23.

C. Initial Delisting Decision.

SmartHeat announced these changes on the morning of May 30, 2012. Within hours, NASDAQ Staff had halted trading on the company's shares. NASDAQ Staff later gave Requests for Additional Information on the Company. Staff Delisting Determination at 1-2. Company complied with all of Staff's requests.

On August 23, 2012, NASDAQ Staff informed the Company that it has determined to delist the Company's shares pursuant to NASDAQ Rule 5101. *Id.* This rule states:

Nasdaq, therefore, in addition to applying the enumerated criteria set forth in the Rule 5000 Series, has broad discretionary authority over the initial and continued listing of securities in Nasdaq in order to maintain the quality of and public confidence in its market, to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and to protect investors and the public interest. Nasdaq may use such discretion to deny initial listing, apply additional or more stringent criteria for the initial or continued listing of particular securities, or suspend or delist particular securities based on any event, condition, or circumstance that exists or occurs that makes initial or continued listing of the securities on Nasdaq inadvisable or unwarranted in the opinion of Nasdaq, even though the securities meet all enumerated criteria for initial or continued listing on Nasdaq. In all circumstances where the Listing Qualifications Department (as defined in Rule 5805) exercises its authority under Rule 5101, the Listing Qualifications Department shall issue a Staff Delisting Determination under Rule 5810(c)(1), and in all circumstances where an Adjudicatory Body (as defined in Rule 5805) exercises such authority, the use of the authority shall be described in the written decision of the Adjudicatory Body.

NASDAQ Listing Rule 5101.

Although Staff did not find that Company failed any of the qualitative requirements for listing, it nonetheless determined that delisting was warranted under Rule 5101's authority to impose "additional or more stringent criteria." Staff Delisting Determination. Staff cited four concerns as the basis for delisting:

- Concerns concerning Company's liquidity and the line of credit

- Changes in management
- Company's structure as a holding company
- Company's association with Ben Wey

Id. at 2-8.

D. Appeal to NASDAQ Hearing Panel

Company appealed Staff's decision to the NASDAQ Hearing Panel. Before the Panel Company argued that Staff identified nothing that was illegal, improper, fraudulent or self-dealing, careless, or unfair to stockholders, and that the decision to delist was unwarranted, unnecessary, and contrary to the public interest. SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination (Oct. 11, 2012).

In particular, Company pointed out that the events that triggered Staff's decision – changes in officers and directors and obtaining a line of credit – are actions that are commonplace in a corporation's life. They are further actions assigned to management, not to NASDAQ, which are to be undertaken according to management's business judgment. Moreover, the changes to management did not warrant delisting, as these new managers and directors were indisputably highly-competent persons who were making Company better. *Id.* at 7-10.

Company also noted that its structure, which was shared by many other listed companies, was required by Chinese law, and it was disclosed to Staff prior to listing. Further, the concerns about liquidity and the line of credit were inconsequential, as the situation that had led to liquidity issues had passed. The Company's prior association with Ben Wey also was irrelevant, as that association ended long ago and had no effect on current operations. *Id.*

Finally, Company argued that Staff's decision to delist was contrary to the public interest. Delisting the shares only harmed current investors, most of whom had never heard of Ben Wey, and provided no protection to future investors. In addition, by invoking "additional and more stringent" criteria for listing, staff introduced an element of discretion into the listing decision, leading to uncertainty as to the rules that govern the operation of the exchange. *Id.*

The NASDAQ Hearing Panel affirmed the Staff's decision to delist. Decision of NASDAQ Hearings Panel, Docket No. NQ 5969N-12 (Nov. 7, 2012) ("Hearing Panel Decision). The Panel acknowledged that Company was taking steps to address concerns raised by Staff, and further appeared to be distancing itself from Ben Wey. *Id.* at 5. Nonetheless, the Panel concluded that several factors "compel[led]" the delisting of the Company. First, the Panel noted that the Company's financial situation suffered from "extreme fragility" and Company had not created a "cogent plan" for restructuring that would allow company to gain access to funds held by its subsidiaries, notwithstanding the fact that the Company had submitted a plan with contemplated actions and timetable. Second, the Company's management "face[d] a steep learning curve regarding operations, internal controls and finances of the Company," notwithstanding the fact that the newly appointed officers had substantial management and governance experience and were certainly more experienced than the officers that they replaced. *Id.* at 5-6.

E. Appeal to NASDAQ Listing Council

Company appealed that decision to the NASDAQ Listing and Hearing Review Council. In a lengthy opinion, the Council affirmed the decision to delist SmartHeat's shares, citing the "broad discretionary" authority of NASDAQ under its Rule 5101. NASDAQ Listing and

Hearing Review Council Decision, Docket No. NQ 5969N-12, at 12 (Feb. 25, 2013) (“Review Council Decision”). Council cited several concerns in support of its decision: 1) the liquidity issues that existed in May 2012; 2) the Company’s decision to obtain a line of credit from employees of its subsidiary; 3) “significant” management turnover in the Company, and 4) lack of contractual arrangements with the Company’s Chinese subsidiaries that allow transfers of funds to the U.S. *Id.* The NASDAQ Board of Directors did not review the Listing Council’s decision, thus making it NASDAQ’s final decision and allowing this appeal.

ARGUMENT

The Commission’s review is governed by § 19(f) of the Securities Exchange Act of 1934, which provides that for NASDAQ’s delisting to be sustained, the specific grounds on which NASDAQ based its decision to delist must exist in fact, the decision must be in accordance with applicable NASDAQ rules, and those rules must be consistent with and applied in a manner consistent with, the purposes of the Exchange Act. 15 U.S.C. § 78s(f); *Cleantech Innovations, Inc.*, Exchange Act Release No. 69968 at 10 (July 11, 2013) (“*CleanTech*”).

When examining this matter, it is important to note what is not in dispute. First, there is no allegation that the Company engaged in conduct that is illegal, improper, fraudulent, self-dealing, careless or unfair to stockholders. Second, NASDAQ cited no objective criterion within its rules to support delisting Company. Third, there was no contention that the Company’s disclosure was inadequate or misleading.

Instead, NASDAQ relied on its supposedly discretionary authority under Rule 5101. As will be discussed below, however, NASDAQ applied an overly expansive interpretation of its authority under Rule 5101. Further, NASDAQ cited supposed facts to support its decision to

delist Company's shares that were erroneous, irrelevant, or both. The result was a perfect storm of error, in which NASDAQ applied the wrong law to the wrong facts, to the detriment of Company, its shareholders, and the investing public.

A. NASDAQ Misapplied Its Authority Under Rule 5101

NASDAQ did not identify any enumerated requirement of its rules as grounds for delisting Company. Instead, it cited Rule 5101, which it claims grants it "broad discretion" to delist a company "in order to maintain the quality of and public confidence in the market, prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade and protect investors and the public interest." Hearing Panel Decision at 5.

Rule 5101 further states that NASDAQ may apply "additional or more stringent criteria" for the initial or continued listing of particular securities. NASDAQ Staff indicated to Company that it would apply these additional criteria to Company's case. Staff Delisting Determination at 8. The Company notes that the Staff did not identify which criteria it was applying, but only that such unspecified criteria were more stringent than the criteria applied to other NASDAQ listed companies. Therefore, it is impossible for Company to understand Staff's reasoning or to formulate a specific Plan of Compliance. Delisting a company's securities pursuant to what appears to be arbitrary rulemaking runs counter to the powers under which NASDAQ operates.

B. NASDAQ Improperly Focused On Ben Wey And His Past Connection With Company.

As in the case of other Chinese companies NASDAQ listed after "reverse mergers," a consultant named Benjamin Wey was involved early in the listing process involving Company.

Mr. Wey, however, has had no connection with Company since 2009. SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination at 15 (Oct. 11, 2012).

The name Ben Wey may be familiar to the Commission; NASDAQ previously invoked it in connection with its erroneous decision to delist a company called CleanTech Innovations. *See CleanTech*. Like Company, CleanTech was a Chinese company that listed on NASDAQ after a reverse merger. Like Company, Mr. Wey was involved in the process that led to the listing. NASDAQ became suspicious of CleanTech's listing after report came out in Barron's that termed Mr. Wey "[o]ne of the most controversial promoters of Chinese reverse takeovers." *Id.* at 3. After this report, NASDAQ requested information from CleanTech regarding its dealings with Mr. Wey, and CleanTech complied. NASDAQ then approved CleanTech's listing. After the listing, CleanTech announced a transaction with affiliates of Mr. Wey. In response, NASDAQ sought to delist CleanTech pursuant to its discretionary authority under Rule 5101 and other exchange rules because CleanTech did not previously disclose information about the transaction to NASDAQ. *Id.* at 3-8.

The Commission overturned the delisting decision, concluding that NASDAQ never asked for information from CleanTech concerning this transaction. Accordingly, the Commission "conclude[d] that the record does not show the grounds on which NASDAQ relied in delisting CleanTech exist in fact." *Id.* at 16. In short, CleanTech's mere association with Wey was insufficient to delist its shares, absent some independent violation by the company of NASDAQ's rules.

In this case, NASDAQ staff cited Mr. Wey in its decision delisting the shares. Staff Delisting Determination. Indeed, Staff went so far as to term him a "notorious stock promoter with a regulatory history." *Id.* at 6. NASDAQ, however, has cited no wrongdoing by the

Company with respect to Wey. Moreover, Wey has never held a position with Company. His dealings with Company through the listing process ended years ago, and they were disclosed to NASDAQ. Indeed, as NASDAQ's Listing Council observed, the steps that Company took further distanced Company from Wey. Review Council Decision at 12.

NASDAQ cited Company's past connection with Mr. Wey apparently to imply guilt by association. The decision in CleanTech makes clear that the discretion afforded by Rule 5101 does not extend to this degree. Citing the past connection with Mr. Wey was an improper factor in NASDAQ's decision to delist.

C. NASDAQ Based its Decision on a Corporate Structure that Existed when the Company was Listed and is a Structure Shared by Numerous Listed Companies and Fully Described in the Company's SEC Filings.

Among the grounds NASDAQ cited delisting Company was the fact that it was a holding company which had limited ability to obtain funds from its foreign subsidiaries. Review Council Decision at 12. There are, however, hundreds of companies structured as holding companies, including virtually every listed Chinese company (and some very large domestic companies like Berkshire Hathaway, AMR and United Continental). China (like many nations with developing economies or currency controls) does not permit direct ownership by foreign investors of assets in China--hence the *holding company structure is necessary*. In fact, many (perhaps most) listed Chinese companies are structured with even more indirect ownership since most have an intervening sub-holding company (typically incorporated in the BVI or Caymans) between the U.S. holding company and the China operating companies. Many others are structured as Variable Interest Entities (VIEs) in which the parent company and its Board have far less control.

See SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination at 25-26 (Oct. 11, 2012).

The Limitations on gaining capital from subsidiaries noted by NASDAQ are not unique to the Company and they are the effect of law--not choice or omission. Even when financial statements are consolidated (as required by GAAP), each corporation is governed by its own respective charter and bylaws and the laws pursuant to which it is organized. The directors of every subsidiary corporation in a corporate hierarchy owe duties to creditors and others under the applicable governing law before the interests of its parent company (i.e., its stockholder) can be served. The rights of a parent corporation towards its subsidiaries are strictly limited to the rights of a stockholder and not the rights of a manager. *Id.*

The rights of the parent company of a Chinese subsidiary are somewhat greater and somewhat more limited than if the subsidiary would be, for example, a U.S. corporation. The rights are *greater* because the parent has the right not only to elect the Board of the subsidiary, but to appoint the Supervisor and the Registered Representative (which are statutory positions in China for which there is nothing comparable in U.S. governance). These governance rights are more comparable to governance under the laws of Germany or Japan. The rights are *somewhat more limited* because to effect the rights it is necessary to make filings with a Chinese governmental agency. *Id.*

Moreover, this structure and the limitations that it creates are matters which the Company has consistently fully described in its public filings. The limitations are matters of common knowledge to lawyers and investment professionals and are not unique to the Company. They were specifically brought to the attention of NASDAQ staff in very forthright and complete disclosures. There is no reason to punish Company and its investors with delisting based on a

corporate structure that was legally mandated and fully disclosed prior to Company being listed in the first place. *Id.*

D. NASDAQ Further Based its Decision on Changes in Company's Management, Which Were Made in the Ordinary Course of Business, Had the Effect of Strengthening the Company Management, and Were Approved by Stockholders.

In early 2012, the Company executed a Board driven management reorganization and realignment--not meaningful turnover--which was described and explained to the Staff in detail. Company also retained Nimbus Strategies to serve as an advisor on a possible restructuring of Company. SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination at 12 (Oct. 11, 2012). In early May, the CFO, Ms. Zhijuan Guo, gave notice that she intended to resign in order to take a position with another company outside of China. Chinese middle managers frequently move to enhance their credentials and careers. There was nothing unusual or troublesome about Ms. Guo's resignation. The Board already desired to replace Ms. Guo as CFO since she did not speak English and was not knowledgeable about U.S. accounting rules and SEC reporting requirements. *Id.* at 22.

After a search, Mr. Michael Wilhelm was identified and recruited to assume the duties of CFO and Treasurer in July (in time to allow the Company to file timely its Form 10-Q for Q2). Mr. Wilhelm was an experienced U.S. executive who was well-versed in US accounting and SEC disclosure rules. He formerly served as the CFO at Bohe Bell +Howell. *Id.* at 4, 22.

In mid-May 2012, the Chairman of the Audit Committee, Mr. Arnold Staloff, tendered his resignation from the Board, and the Board accepted it. No reason was given by Mr. Staloff for his resignation, but it was not unexpected. Mr. Staloff served on the Boards, and as Chairman of their respective Audit Committees, for several companies for which (similar to the Company)

Mr. Wey or his affiliates had served in the past in a financial advisory capacity. At least one of these other NASDAQ listed companies had initiated contentious litigation and allegations regarding NASDAQ and the Staff based, in part, on an affidavit from Mr. Staloff. [Please see “CleanTech Innovations, Inc. Press Release dated January 18, 2012” in Exhibit B to SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination (Oct. 11, 2012).] When the investigation into the activities of Mr. Wey became visible in early 2012, it did not come as a surprise that Mr. Staloff offered to resign. [Please see “FBI Looks Into Adviser on Chinese Reverse Mergers” in Exhibit C to SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination (Oct. 11, 2012).] Although the Board appreciated the past service of Mr. Staloff and had no reason to question or doubt his loyalty, competence or integrity, the Board accepted Mr. Staloff’s resignation as part of its plan to restructure the management and governance of the Company and sever any appearance of an association with Mr. Wey. SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination at 22 (Oct. 11, 2012).

In July, Mr. Kenneth Scipta joined the Board and agreed to serve as Chairman of the Audit Committee. *Id.* Mr. Scipta is a CPA who was formerly president and a member of the board at two separate companies listed on NASDAQ.

As part of the Board’s plan to restructure the management and governance of the Company, the management team of the Chinese operating subsidiaries who were dual officers of the Company (Mr. Jun Wang, Mr. Wen Sha and Mr. Xudong Wang) withdrew from their positions with the parent holding company. Among other reasons for this realignment, this action allowed these individuals to refocus their efforts entirely on the management of operations without the distractions of issues relating to the publicly traded holding company. Jun Wang also

resigned from the Board. None of these individuals speak English as their first language, and they (and the Board) concluded that it was in the best interest of the Company to appoint officers who had English language fluency and familiarity with U.S. law and practice that was needed: to comprehend the nuances of language required to interpret the applicable U.S. laws and regulations, and to judge the adequacy or appropriateness of the advice being given to them by current and potential advisers. *Id.* at 22-23.

Mr. Oliver Bialowons was recommended to the Board by the Restructuring Adviser and invited by the Board to join and (based on his past experience and skills) to serve as President. Mr. Bialowons formerly served as the president of Bohe Bell+Howell. *Id.* at 4, 23.

In short, a total of 2 out of 5 directors of Company resigned and were replaced. A new CEO and CFO came on board, who were persons of undeniable talent and experience. There is no question that these changes improved Company's management. *Id.* at 23.

This type of "turnover" is generally regarded as an indicator of good governance and would be regarded by many as a Best Practice. NASDAQ instead cited it as a factor in its decision to delist Company, writing that "[i]t is unclear that such steps will adequately address the issues that gave rise to Staff's delisting determination." Review Council Decision at 10. That statement, however, is nothing more than speculation. It is equally possible (indeed likely) that the Company will benefit by skilled, experienced Board members and managers. NASDAQ's decision to delist must be based in fact. *CleanTech* at 10. At a minimum, actions by a listed company that improve the effectiveness and professionalism of management are conduct that NASDAQ should encourage, not punish with the draconian penalty of delisting. NASDAQ should not (as it did here) cite conjecture about management changes as a justification for delisting Company.

E. NASDAQ Improperly Based Its Delisting Decision on a Hypothesized Liquidity Crisis Within Company that Did Not Occur.

In its Press Release dated May 30, as filed with its Form 8-K, the Company identified a short-term liquidity issue noting that there was a proposal in place that would address this issue. In fact, *this short-term liquidity issue has been resolved*. A \$2,000,000 Line of Credit was put in place on July 27 and a copy was provided to the Staff on July 26. The Company publicly reported this event on a Form 8-K filed on August 1. SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination at 16 (Oct. 11, 2012).

NASDAQ cited this line of credit, and the liquidity issue that preceded it, as justification for delisting Company's shares. The concerns NASDAQ raised over this issue follow several different threads. First, NASDAQ raised concerns about why a line of credit was needed in the first place, and how Company's liquid funds diminished to approximately \$25,000 prior to the line of credit being put into place. Review Council Decision at 10. As the Staff confirmed after consulting with Company, the approximately \$28 million in cash that Company had in March 2011 after its shares were listed was invested into the Company's subsidiaries. The Company provided substantial data to the Staff verifying this flow and application of cash. *Id.* at 2-5.

Moreover, these outlays were reasonable exercises of business judgment. Following several years of dramatic growth in revenues and profits, the Company made substantial investments during 2011 into acquisitions and inventory. Unfortunately, as a result of several unforeseen factors, the growth did not continue. The principal factors causing this shift were explained to Staff and include:

- The Twelfth Five Year Plan (2011-2015) had different objectives than Eleventh Five Year Plan (2006-2010), namely, focusing on high tech rather than green tech businesses and the

development of western China rather than further speculative development in Eastern China. In China, money (lending/investment) tends to follow closely the Five Year Plan.

- The Chinese government's stimulus efforts in response to global recession benefitted the Company from 2008-2010. In 2011, the Chinese government reduced the amount of its stimulus investments and its focus was redirected toward developing western China.

- The principal customers for the Company's products are new developments. Following direction from the central government, in 2011 many local governments stopped supporting speculative developments in the Company's established markets.

- Competition also increased in 2011. When a market segment is perceived to be profitable in China, competition does not merely increase, it erupts.

- The overall economy of China also slowed due to higher interest rates and a strengthening currency and mild inflation.

SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination at 19-20 (Oct. 11, 2012).

Deciding how to deploy financial assets is fundamentally a decision for Company's management, not NASDAQ. The investments that Company made may not have been wholly successful, but they were reasonable. The outcome of particular investments should not allow NASDAQ, with benefit of hindsight, to punish Company and its investors with the extraordinary remedy of delisting.

Alternatively, NASDAQ takes issue with Company for supposedly failing to put in place a mechanism to obtain capital from its subsidiaries. Review Council Decision at 10. As discussed above, however, the issues relating to the ability to move cash up out of the China subsidiaries to the parent holding company are a function of Chinese law, and are not unique to

the Company. These issues are similar for many Chinese companies trading in the U.S. [Please see “Cash Flowing and Cash Trapped” in Exhibit A to SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination (Oct. 11, 2012).] Moreover, these issues were disclosed both to NASDAQ staff and the public.

NASDAQ also chides Company for supposedly failing to address its liquidity issues sooner, writing that company was supposedly “slow to react.” Review Council Decision at 10. At the same time, NASDAQ admits that the liquidity crisis arose quickly – in approximately 14 months. Further, NASDAQ ignores the many complications that would prevent the rapid recapitalization of Company. These include: a) the time and expense needed to undertake due diligence by third-party lenders, b) the inability to refinance the whole enterprise (parent and subsidiaries) with one comprehensive credit line (as typically done for U.S. businesses); and c) the complications created by Chinese law, including currency controls, taxes and uncertainty about creating security interests in Chinese assets. In addition, Company had been requested by the SEC and US Attorney not to disclose the fact that it had been subpoenaed to produce information regarding Mr. Wey, and that severely limited the Company' ability to secure funding without disclosing this material information to any potential lender or capital source other than a source with existing inside information. The immediate and obvious option was to ask for support from insiders because there was neither time nor cash to look elsewhere for alternatives. SmartHeat Memorandum in Support of Appeal of Staff Delisting Determination at 17 (Oct. 11, 2012).

Two other facts about the line of credit further call into question NASDAQ's reasoning. Securing a Line of Credit from a significant stockholder (Jun Wang) and the managers of the China operations demonstrates their confidence in, and commitment to, the Company and

provides a powerful incentive to management (personal investment by management--"skin in the game"—is a Best Practice). In addition, through negotiation over a 2 month period following the Company's announcement of the terms in the initial proposal, the Board was able to negotiate certain terms for the definitive agreement, as executed on July 27, which reduce the cost of the borrowing and protect the Company from default. These terms were required by the Board and may not be available from a third party lender, namely: ability by the Company to prepay the loan if better terms can be found; ability at the Company's option to extend the maturity and avoid default for an additional 45 months; and ability, at the option of the Company, to repay the loan with either cash or stock. *Id.* at 18.

F. In Sum, NASDAQ's Decision was Unwarranted, Unnecessary, and Inappropriate in the Circumstances, *Ultra Vires* and Contrary to the Public Interest.

The foregoing discussion reveals the confluence of events that led to Company's delisting. NASDAQ applied vague and ultimately subjective interpretation of Rule 5101 to evaluate Company's case. The concerns that they relied upon to support delisting were either misunderstood (as in the case of Company's relationship with James Jun Wang), no longer existing (as in the case of Company's prior liquidity issues), speculative (as in the case of Company's efforts to strengthen itself by hiring experienced new management), or fully disclosed prior to listing both to NASDAQ and to investors (as in the case of Company's structure).

NASDAQ's decision, however, has lasting effects both on Company and the investing public at large. With respect to Company, NASDAQ's decision has shut Company out a major stock market. Further because the criteria used by NASDAQ are so vague, it is impossible for Company to formulate a specific plan of compliance that would meet NASDAQ's concerns.

Indeed, the decision improperly second-guesses decisions that are assigned to the business judgment of Company's management. Delisting a company's securities pursuant to what appears to Company as arbitrary rulemaking runs counter to the powers under which NASDAQ operates. And, of course, innocent shareholders have seen the value of their shares drop as a result of NASDAQ's actions.

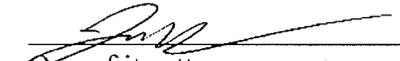
The discretionary action of NASDAQ was unnecessary to protect investors and the public interest since the actions taken by Company have improved its prospects in the year and a half since the delisting order was issued. The timing of the Staff delisting determination cannot be logically justified. The facts given as the reasons for the action were not new; they were not unique; and they were not serious. The discretionary determination by the Staff to delist the Company's securities was, in itself, conduct that was unfair to the Company's current stockholders (and, therefore, not in the public interest) and damaging to the integrity of the NASDAQ market.

CONCLUSION

Accordingly, Company requests that NASDAQ's delisting decision be reversed.

SMARTHEAT INC.

By


One of its attorneys

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