

CHINA EDUCATION ALLIANCE INC.  
Form 10QSB  
August 15, 2005

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

FORM 10-QSB

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
for the quarterly period ended June 30, 2005

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 for  
the transition period from \_\_\_\_\_ to \_\_\_\_\_

**CHINA EDUCATION ALLIANCE, INC.**

(Exact name of small business issuer as specified in its charter)

Employer identification No.) **North Carolina** **56-2012361** (IRS  
(State or other jurisdiction of  
incorporation or organization)

**80 Heng Shan Rd. Kun Lun Shopping Mall**  
**Harbin, P.R. China 150090**

(Address of principal executive offices)

**(86451) 8233-5794**

(Issuer's telephone number)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Number of shares of common stock outstanding as of  
August 12, 2005: 57,915,000

Number of shares of preferred stock outstanding as of

August 12, 2005: -0-



ITEM 1.

**CHINA EDUCATION ALLIANCE, INC. AND SUBSIDIARY**  
**Consolidated Balance Sheet**  
*At June 30, 2005 (Unaudited)*

ASSETSCURRENT ASSETS

|                             |    |                |
|-----------------------------|----|----------------|
| Cash and cash equivalents   | \$ | 423,298        |
| Inventories                 |    | 4,734          |
| Other receivables           |    | 302            |
| <b>TOTAL CURRENT ASSETS</b> |    | <b>428,334</b> |

PROPERTY AND EQUIPMENT

|                                   |  |                  |
|-----------------------------------|--|------------------|
| Machinery & equipment             |  | 2,407,600        |
| Accumulated depreciation          |  | (130,077)        |
| <b>NET PROPERTY AND EQUIPMENT</b> |  | <b>2,277,523</b> |

|                     |           |                  |
|---------------------|-----------|------------------|
| <b>TOTAL ASSETS</b> | <b>\$</b> | <b>2,705,857</b> |
|---------------------|-----------|------------------|

LIABILITIES AND STOCKHOLDERS' EQUITYCURRENT LIABILITIES

|  |    |                |
|--|----|----------------|
| Other payables and accrued liabilities | \$ | 11,515         |
| Convertible note payable               |    | 76,865         |
| Income taxes payable                   |    | 77,714         |
| <b>TOTAL CURRENT LIABILITIES</b>       |    | <b>166,094</b> |

STOCKHOLDERS' EQUITY

|   |  |                  |
|---|--|------------------|
| Preferred stock (\$0.001 par value, 5,000,000 shares authorized:<br>none issued and outstanding)      |  | -                |
| Common stock (\$0.001 par value, 150,000,000 shares authorized:<br>57,915,000 issued and outstanding) |  | 57,915           |
| Additional paid-in capital  |  | 2,425,469        |
| Retained earnings   |  | 35,879           |
| Due to stockholders   |  | 20,500           |
| <b>TOTAL STOCKHOLDERS' EQUITY</b>   |  | <b>2,539,763</b> |

|   |           |                  |
|---|-----------|------------------|
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b> | <b>\$</b> | <b>2,705,857</b> |
|---|-----------|------------------|

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



**CHINA EDUCATION ALLIANCE, INC. AND SUBSIDIARY**  
**Consolidated Statement of Operations**  
*For the three months and six months ended June 30, 2005 (Unaudited)*

|   | Three months ended<br>June 30, 2005 | Six months ended<br>June 30, 2005 |
|---|-------------------------------------|-----------------------------------|
| <b><u>REVENUES:</u></b>                             |                                     |                                   |
| Sales   | \$ 285,411                          | \$ 364,028                        |
| Cost of goods sold                                  | (30,656)                            | (56,294)                          |
| <b>GROSS PROFIT</b>                                 | <b>254,755</b>                      | <b>307,734</b>                    |
| <b><u>OPERATING EXPENSES:</u></b>                   |                                     |                                   |
| Selling, general and administrative                 | 5,266                               | 21,163                            |
| Professional fees                                   | 3,500                               | 7,000                             |
| Depreciation and amortization                       | 25,049                              | 50,098                            |
| <b>TOTAL OPERATING EXPENSES</b>                     | <b>33,815</b>                       | <b>78,261</b>                     |
| <b>INCOME FROM OPERATIONS</b>                       | <b>220,940</b>                      | <b>229,473</b>                    |
| <b><u>OTHER INCOME (EXPENSES):</u></b>              |                                     |                                   |
| Interest income                                     | 136                                 | 260                               |
| Interest expense                                    | (2,327)                             | (5,183)                           |
| Other   | (28)                                | (1,236)                           |
| <b>TOTAL OTHER INCOME (EXPENSES)</b>                | <b>(2,219)</b>                      | <b>(6,159)</b>                    |
| <b>INCOME BEFORE INCOME TAXES</b>                   | <b>218,721</b>                      | <b>223,314</b>                    |
| <b>INCOME TAX EXPENSE</b>                           | <b>(74,101)</b>                     | <b>(77,714)</b>                   |
| <b>NET INCOME</b>                                   | <b>\$ 144,620</b>                   | <b>\$ 145,600</b>                 |
| Basic and fully diluted net income per common share | \$ -                                | \$ -                              |
| Basic and fully diluted weighted average shares     | 57,915,000                          | 57,915,000                        |

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

**CHINA EDUCATION ALLIANCE, INC. AND SUBSIDIARY**  
**Consolidated Statement of Cash Flows**  
*For the six months ended June 30, 2005 (Unaudited)*

**CASH FLOWS FROM OPERATING ACTIVITIES:**

|   |    |                |
|---|----|----------------|
| Net income  | \$ | 145,600        |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: |    |                |
| Depreciation  |    | 97,557         |
| (Increase) decrease in operating assets   |    |                |
| Inventories   |    | 6,431          |
| Other receivables   |    | (302)          |
| Increase (decrease) in operating liabilities:   |    |                |
| Income taxes payable  |    | 75,517         |
| Other payables and accrued liabilities  |    | (11,929)       |
| <b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>  |    | <b>312,874</b> |

**CASH FLOWS FROM FINANCING ACTIVITIES**

|  |  |                |
|--|--|----------------|
| Proceeds from stockholder                        |  | 17,500         |
| Payment on convertible note                      |  | (12,317)       |
| Due to shareholders                              |  | 15,500         |
| <b>NET CASH PROVIDED BY FINANCING ACTIVITIES</b> |  | <b>20,683</b>  |
| <b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b> |  | <b>333,557</b> |

**CASH AND CASH EQUIVALENTS:**

|   |    |         |
|---|----|---------|
| Beginning of year   |    | 89,741  |
| End of period   | \$ | 423,298 |
| Supplemental disclosures of cash flow information:        |    |         |
| Cash paid for interest                                    | \$ | 5,183   |
| Cash paid for income taxes                                | \$ | 2,197   |
| Supplemental disclosures of noncash financing activities: |    |         |
| Common stock issued for services                          | \$ | -       |

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

CHINA EDUCATION ALLIANCE, INC. AND SUBSIDIARY  
NOTES TO CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS  
AS OF JUNE 30, 2005 (UNAUDITED)

**NOTE 1 BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

In the opinion of management, the unaudited condensed consolidated financial statements contain all adjustments consisting only of normal recurring accruals considered necessary to present fairly the Company's financial position at June 30, 2005, the results of operations for the three-month and six-month periods ended June 30, 2005, and cash flows for the six months ended June 30, 2005. The results for the period ended June 30, 2005 are not necessarily indicative of the results to be expected for the entire fiscal year ending December 31, 2005. These financial statements should be read in conjunction with the Company's annual report on Form 10-KSB as filed with the Securities and Exchange Commission.

**NOTE 2 REVERSE MERGER**

ABC Realty Co. was organized under the laws of the State of North Carolina on December 2, 1996. Harbin Zhong He Li Da Jiao Yu Ke Ji You Xian Gong Si ("ZHL D") was registered in the People's Republic of China ("PRC") on August 9, 2004 with its principal place of business in the PRC.

ZHL D is principally engaged in the on-line education business serving the students in China.

On September 15, 2004, ABC Realty Co. executed a Plan of Exchange with ZHL D and Duane C. Bennett, Chairman of ABC Realty Co. pursuant to which ZHL D exchanged all of its registered capital of \$60,386 for 55,000,000 shares or approximately 95% of the common stock of China Education Alliance, Inc. ("China Education"). On December 13, 2004, China Education consummated the Plan of Exchange with ZHL D. As a result of the Plan of Exchange, the transaction was treated for accounting purposes as a capital transaction and recapitalization by the accounting acquirer (ZHL D) and as a re-organization by the accounting acquiree (China Education).

On November 17, 2004, ABC Realty changed its name to China Education Alliance, Inc.

Accordingly, the financial statements include the following:

- (1) The balance sheet consists of the net assets of the acquirer at historical cost and the net assets of the acquiree at historical cost.
- (2) The statement of operations includes the operations of the acquirer for the periods presented and the operations of the acquiree from the date of the merger.

China Education and its wholly owned subsidiary ZHL D are hereafter referred to as (the "Company").

**NOTE 3 PRINCIPLES OF CONSOLIDATION**

The accompanying consolidated financial statements do not include the financial information for 2004 due to the merger commencing in the fourth quarter of 2004 and its wholly owned subsidiary of ZHLD set up on August 9, 2004.

The accompanying unaudited consolidated financial statements for 2005 include the accounts of China Education and its wholly owned subsidiary of ZHLD.

All significant intercompany transactions and balances have been eliminated on consolidation.

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CHINA EDUCATION ALLIANCE, INC. AND SUBSIDIARY  
 NOTES TO CONDENSED CONSOLIDATED  
 FINANCIAL STATEMENTS  
AS OF JUNE 30, 2005 (UNAUDITED)

**NOTE 4 USE OF ESTIMATES**

The preparation of the financial statements in conformity with US GAAP requires the Company's management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of financial statements and the reported amounts of revenues and expenses during the reported periods. Actual amounts could differ from those estimates.

**NOTE 5 EARNINGS (LOSS) PER SHARE**

Basic earnings (loss) per share exclude dilution and are computed by dividing earnings (loss) available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share are computed by dividing earnings (loss) available to common shareholders by the weighted average number of common shares outstanding adjusted to reflect potentially dilutive securities. The company does not have any dilutive securities outstanding as of June 30, 2005.

**NOTE 6 INVENTORIES**

Inventories at June 30, 2005 (unaudited) and December 31, 2004 consisted of the following:

|                                 | 2005<br>(Unaudited) | 2004      |
|---------------------------------|---------------------|-----------|
| Debit cards                     | \$ 4,734            | \$ 11,165 |
| Less: provision of obsolescence | -                   | -         |
|                                 | \$ 4,734            | \$ 11,165 |

For the six months ended June 30, 2005 (unaudited), no provision for obsolete inventories was recorded by the Company.

**NOTE 7 NOTE PAYABLE**

Balance at June 30, 2005 (unaudited) and December 31, 2004:

|              | 2005<br>(Unaudited) | 2004      |
|--------------|---------------------|-----------|
| Note payable | \$ 76,865           | \$ 89,182 |

Note payable is due to a third party, is unsecured and bears interest at a rate of approximately 9% per annum. The Company scheduled monthly payments included in interest, each in the amount of \$2,500 starting on October 15, 2004 and ending on September 15, 2005, with the balance of \$70,000 due and payable on September 15, 2005, at the option of the Company, in cash or in an equivalent amount of free trading common stock of the Company.

CHINA EDUCATION ALLIANCE, INC. AND SUBSIDIARY  
NOTES TO CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS  
AS OF JUNE 30, 2005 (UNAUDITED)

**NOTE 8 SHAREHOLDERS' EQUITY**

During the six months ended June 30, 2005, the Company recorded additional paid in capital of \$17,500 being amount owed to and waived by the stockholders.

**NOTE 9 RELATED PARTY TRANSACTIONS**

During the six months ended June 30, 2005, the Company recorded additional paid in capital of \$17,500 being amount owed to and waived by the stockholders.

**NOTE 10 COMPARATIVE FINANCIAL STATEMENTS**

On December 13, 2004, the Company acquired 100% of the capital stock of ZHLD, a corporation organized under the laws of the PRC, pursuant to a Share Exchange Agreement dated September 15, 2004. The ZHLD subsidiary, incorporated in the PRC on August 9, 2004, has commenced its business in on-line education servicing the students in China. The acquisition was accounted for as a reverse merger. Accordingly, there are no applicable financial statements for the comparable periods for the three months and six months ended June 30, 2004

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

The discussion contained in this prospectus contains “forward-looking statements” that involve risk and uncertainties. These statements may be identified by the use of terminology such as “believes”, “expects”, “may”, or “should”, or “anticipate” or expressing this terminology negatively or similar expressions or by discussions of strategy. The cautionary statements made in this prospectus should be read as being applicable to all related forward-looking statements wherever they appear in this prospectus. Our actual results could differ materially from those discussed in this prospectus. Important factors that could cause or contribute to such differences include those discussed under the caption entitled “risk factors,” as well as those discussed elsewhere in this prospectus.

OUR COMPANY

ABC Realty Co (AREY) was incorporated in North Carolina on December 2, 1996. Harbin Zhong He Li Da Jiao Yu Ke Ji You Xian Gong Si (ZHL D) was incorporated in Harbin, China on August 9, 2004 under the laws of People’s Republic of China.

On September 15, AREY executed a Plan of Exchange between and among AREY, Duane Bennett, the chairman of AREY and ZHL D. Pursuant to the Plan of Exchange, ZHL D exchanged all their registered capital of US\$60,386 for 55,000,000 shares common stock of AREY, or 95% of the outstanding common stock of AREY. On December 13, 2004, AREY consummated the exchange transaction with ZHL D. As a result of the Plan of Exchange, the transaction was treated for accounting purposes as a capital transaction and recapitalization by ZHL D and as a re-organization by AREY. On November 17, 2004, AREY changed its name to China Education Alliance, Inc.(CEDA).

ZHL D is engaged in the education business in China. Its operations include a major education website, the Greater China Occupational Education Base and sales of on-line education software and educational books media. The operations are an effective combination with the education website serving as a leading force.

We are planning to develop our business by increasing the user base, the sales of our self-developed educational software and the database which covers all levels of the basic education in China. Currently, we own [www.edu-chn.com](http://www.edu-chn.com), which is one of the few websites in China having copyrights of examination materials of Chinese primary schools and middle schools, so that we legally provide target users in the age group of 7 to 40 years with downloadable examination materials, education result appraisals and occupational license authorizations. Through cooperation with the local education committees and schools, we now have 15 million people using our online services. We have developed 15 million users in the first half of 2005 and over 50 million users over the next two years, based on demographic trends and an increase product offering on its web site. We also provide other services such as text book downloading and electronic storage management. When visits to our web site increase, and our membership base expands, we plan to expand our products into the advanced education market and Chinese language education market toward foreigners.

Results of Operations.

For the six months ended June 30, 2005 (Unaudited).

#### Sales.

Currently our business is on-line education services. The sales of \$285,411 and \$364,028 for the three-month and six-month periods ended June 30, 2005, respectively, were primarily from the sales of debit cards for use to obtain educational materials posted on the Company's website at the time of the delivery, when title to the products transfers and the customer bears the risk of loss. The sales in the second quarter of 2005 were approximately 360% of the sales in the first quarter. The remarkable increase in the second quarter was primarily due to the high quality, sufficiency and reliability of our education materials, which increased the visits to our website. The visits during the first quarter were up to 270,000 and then increased to 450,000 in April and to 900,000 in May and to 1.5 million in June, reflecting our website has gained more and more respect as its reputation grows.

Most of our sales was achieved in March as the first two months in the first quarter were the Spring Festival in China. On the other hand, we began our promotion program in March before the middle-term examination.

#### Cost of Sales.

The cost of goods sold includes the purchase price and printing expenses for our debit cards and the cost of copy rights of the exam materials plus other direct costs associated with making the products available for resale. It is customary to experience variations in the cost of sales as a percentage of net sales based on the types of products sold.

The cost of goods sold for the three months ended June 30, 2005 was \$30,656, which was approximately 10.7% of sales. The cost of goods sold for the six months ended June 30, 2005 was \$56,294, which was approximately 15.5% of sales. We expect our cost of good sold percentage to remain relatively low due to the downloadable nature of our products and materials.

We also expect to keep cost of sales as a percentage of sales relatively low as our new services provided on our website become more popular. We are seeking the co-operation of well known schools which have quality guarantee on the exam materials due to their experiences and restricted systems. If we can successfully grow our revenues through providing download services for the exam materials of named schools, we can meet the expectation in future periods due to higher margin of these services. In addition, volume discounts will be available if we are successful in achieving sales growth in the future, which will further reduce our cost of sales as a percentage of sales.

#### Expenses.

Selling, general and administrative expenses for the three-month and six-month periods ended June 30, 2005 were \$5,266 and \$21,163, respectively. The expenses were primarily attributable to the salaries, the initial set up costs and website creation. The decrease in selling, general and administrative expenses in the second quarter was due primarily to better control of administrative expense.

We expect increases in expenses through the year 2005 as we move towards developing our business plan in the following aspects:

- v Buildup the infrastructure to ensure fast access and to satisfy the volume coming with increasing demand ;
  - v Boost market shares via nation-wide advertising campaigns;
  - v Invest in human resources to improve the quality of services;
  - v Open branch offices in key cities.

## Income Taxes

Income taxes are provided in accordance with Statement of Financial Accounting Standards No. 109 (SFAS No. 109), "Accounting for Income Taxes." A deferred tax asset or liability is recorded for all temporary differences between financial and tax reporting and net operating loss-carry forwards.

Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that, some portion or all of the deferred tax asset will not be realized. Deferred tax assets and liabilities are adjusted for the effect of changes in tax laws and rates on the date of enactment. We currently do not have any deferred tax assets.

## Income / Losses.

We had net income of \$144,620 and \$145,600 for the three-month and six-month periods ended June 30, 2005, respectively. The remarkable increase in net income in the second quarter of 2005 was due primarily to the increase in sales and expenses control. We will attempt to keep the upward trend of our revenues during 2005.

## Impact of Inflation.

We believe that inflation has had a negligible effect on operations since inception. We believe that we can offset inflationary increases in the cost of operations by increasing sales and improving operating efficiencies.

## Liquidity and Capital Resources.

Cash flows provided by operations were \$312,874 for the six months ended June 30, 2005. Cash flows provided by operations were primarily attributable to \$97,557 in depreciation of our fixed assets for the six months ended June 30, 2005 and the taxes payable of \$75,517.

There were no cash flows from investing activities in the six-month period ended June 30, 2005.

Cash flows generated by financing activities were \$20,683 for the six months ended June 30, 2005. Cash flows from the six months of 2005 were from a \$17,500 shareholder loan, offset by the payment of \$12,317 on the convertible note.

The company's future for more profits is optimistic due to the significant increase in the visits to our website and the types of other services.

Our success will be dependent upon implementing our plan of operations and the risks associated with our business plans. We plan to strengthen our position in educational markets in China. We also plan to expand our operations through aggressively marketing our on-line business and Company concept.

Critical Accounting Policies and Estimates

We have identified the following policies as critical to our business operations and the understanding of our results of operations. This listing is not a comprehensive list of all of our accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by accounting principles generally accepted in the United States, with no need for management's judgment in their application. There are also areas in which management's judgment in selecting any available alternative would not produce a materially different result. However, certain of our accounting policies are particularly important to the portrayal of our financial position and results of operations and may require the application of significant judgment by our management; as a result, they are subject to an inherent degree of uncertainty. In applying those policies, our management uses its judgment to determine the appropriate assumptions to be used in the determination of certain estimates. Those estimates are based on our historical experience, our observance of trends in the industry, and information available from other outside sources, as appropriate. For a more detailed discussion on the application of these and other accounting policies, see "Note 1 - Summary of significant account policies" in our financial statements and related notes on Form 10-K. Our critical accounting policies and estimates are as follows:

Revenue recognition

We recognize revenue from the sale of debit cards for use to obtain educational materials posted on our website at the time of delivery, when title to the products transfers and the customer bears the risk of loss.

The debit cards are sold to distributors who sell the predetermined debit cards to individuals. We recognize revenue on the debit cards at the time of sale to the distributors as we have no record of when and the extent the debit cards purchased were used by the customers. Unused debit cards have no cash value after their purchase and we do not refund purchases by distributors.

Property and equipment

Property and equipment are stated at cost, less accumulated depreciation. Expenditures for additions, major renewals and betterments are capitalized and expenditures for maintenance and repairs are charged to expense as incurred.

Depreciation is provided on a straight-line basis, less estimated residual value over the assets' estimated useful lives. The estimated useful lives are as follows:

|                                   |          |
|-----------------------------------|----------|
| Buildings                         | 20 Years |
| Communication equipment           | 10 Years |
| Motor vehicles                    | 5 Years  |
| Furniture, fixtures and equipment | 5 Years  |

Long-lived assets

In accordance with Statement of Financial Accounting Standards No. 121 and 142, "Accounting for the impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of", long-lived assets and certain identifiable intangible assets held and used by us are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. For purposes of evaluating the recoverability of long-lived assets, the recoverability test is performed using undiscounted net cash flows related to the long-lived assets. We review long-lived assets to determine that carrying values are not impaired.

### ITEM 3. CONTROLS AND PROCEDURES

#### Quarterly Evaluation of Controls

As of the end of the period covered by this quarterly report on Form 10-Q, we evaluated the effectiveness of the design and operation of (i) our disclosure controls and procedures ("Disclosure Controls"), and (ii) our internal control over financial reporting ("Internal Controls"). This evaluation ("Evaluation") was performed by our President and Chief Executive Officer, Yu, Xi Qun ("CEO"), and Wang, Chungqing, our Chief Financial Officer. In this section, we present the conclusions of our CEO based on and as of the date of the Evaluation, (i) with respect to the effectiveness of our Disclosure Controls, and (ii) with respect to any change in our Internal Controls that occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect our Internal Controls.

#### CEO and CFO Certifications

Attached to this quarterly report, as Exhibits 31.1 and 31.2, are certain certifications of the CEO and CFO, which are required in accordance with the Exchange Act and the Commission's rules implementing such section (the "Rule 13a-14(a)/15d-14(a) Certifications"). This section of the quarterly report contains the information concerning the Evaluation referred to in the Rule 13a-14(a)/15d-14(a) Certifications. This information should be read in conjunction with the Rule 13a-14(a)/15d-14(a) Certifications for a more complete understanding of the topic presented.

#### Disclosure Controls and Internal Controls

Disclosure Controls are procedures designed with the objective of ensuring that information required to be disclosed in our reports filed with the Commission under the Exchange Act, such as this quarterly report, is recorded, processed, summarized and reported within the time period specified in the Commission's rules and forms. Disclosure Controls are also designed with the objective of ensuring that material information relating to the Company is made known to the CEO and the CFO by others, particularly during the period in which the applicable report is being prepared. Internal Controls, on the other hand, are procedures which are designed with the objective of providing reasonable assurance that (i) our transactions are properly authorized, (ii) our assets are safeguarded against unauthorized or improper use, and (iii) our transactions are properly recorded and reported, all to permit the preparation of complete and accurate financial statements in conformity with accounting principals generally accepted in the United States.

#### Limitations on the Effectiveness of Controls

Our management does not expect that our Disclosure Controls or our Internal Controls will prevent all error and all fraud. A control system, no matter how well developed and operated, can provide only reasonable, but not absolute assurance that the objectives of the control system are met. Further, the design of the control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances so of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision -making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of a system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated objectives under all potential future conditions. Over time, control may become inadequate because of changes in conditions, or because the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.





## Scope of the Evaluation

The CEO and CFO's evaluation of our Disclosure Controls and Internal Controls included a review of the controls' (i) objectives, (ii) design, (iii) implementation, and (iv) the effect of the controls on the information generated for use in this quarterly report. In the course of the Evaluation, the CEO and CFO sought to identify data errors, control problems, acts of fraud, and they sought to confirm that appropriate corrective action, including process improvements, was being undertaken. This type of evaluation is done on a quarterly basis so that the conclusions concerning the effectiveness of our controls can be reported in our quarterly reports on Form 10-QSB and annual reports on Form 10-KSB. The overall goals of these various evaluation activities are to monitor our Disclosure Controls and our Internal Controls, and to make modifications if and as necessary. Our external auditors also review Internal Controls in connection with their audit and review activities. Our intent in this regard is that the Disclosure Controls and the Internal Controls will be maintained as dynamic systems that change (including improvements and corrections) as conditions warrant.

Among other matters, we sought in our Evaluation to determine whether there were any significant deficiencies or material weaknesses in our Internal Controls, which are reasonably likely to adversely affect our ability to record, process, summarize and report financial information, or whether we had identified any acts of fraud, whether or not material, involving management or other employees who have a significant role in our Internal Controls. This information was important for both the Evaluation, generally, and because the Rule 13a-14(a)/15d-14(a) Certifications, Item 5, require that the CEO and CFO disclose that information to our Board (audit committee), and to our independent auditors, and to report on related matters in this section of the quarterly report. In the professional auditing literature, "significant deficiencies" are referred to as "reportable conditions". These are control issues that could have significant adverse affect on the ability to record, process, summarize and report financial data in the financial statements. A "material weakness" is defined in the auditing literature as a particularly serious reportable condition where the internal control does not reduce, to a relatively low level, the risk that misstatement cause by error or fraud may occur in amounts that would be material in relation to the financial statements and not be detected within a timely period by employee in the normal course of performing their assigned functions. We also sought to deal with other controls matters in the Evaluation, and in each case, if a problem was identified, we considered what revisions, improvements and/or corrections to make in accordance with our ongoing procedures.

## Conclusions

Based upon the Evaluation, the Company's CEO and CFO have concluded that, subject to the limitations noted above, our Disclosure Controls are effective to ensure that material information relating to the Company is made known to management, including the CEO and CFO, particularly during the period when our periodic reports are being prepared, and that our Internal Controls are effective to provide reasonable assurance that our financial statements are fairly presented in conformity with accounting principals generally accepted in the United States. Additionally, there has been no change in our Internal Controls that occurred during our most recent fiscal quarter that has materially affected, or is reasonably likely to affect, our Internal Controls.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 2. Changes in Securities

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

3. Articles of Incorporation with amendments and bylaws are incorporated by reference to Exhibit No. 1 of Form SB-2 as amended filed April 2001.

31.1 CEO Certification pursuant to Section 302

31.2 CFO Certification pursuant to Section 302

32.1 CEO Certification pursuant to Section 906

32.2 CFO Certification pursuant to Section 906

(b) Reports on Form 8-K

An amended Form 8-K/A was filed on April 15, 2005 to provide financial statements in connection with the acquisition of the foreign subsidiary Zhong He Li Da.

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 EDUCATION ALLIANCE, INC.  
(Registrant)

Date: August 15, 2005

By: /s/ Yu, Xi Qun

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Yu, Xi Qun  
President

