CHINA EDUCATION ALLIANCE INC.
Form 10-Q
August 14, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2013

¨ TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from ______________ to _____________

Commission file number: **001-34386**

CHINA EDUCATION ALLIANCE, INC.

(Exact name of registrant as specified in its charter)

North Carolina	**56-2012361**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

58 Heng Shan Road, Kun Lun Shopping Mall
Harbin, People's Republic of China **150090**
(Address of principal executive offices) (Zip Code)

86-451-8233-5794
(Registrant's telephone number,
including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨ Accelerated filer ¨

Non-accelerated filer ¨ Smaller reporting company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY

PROCEEDINGS DURING THE PRECEDING FIVE YEARS

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes ¨ No ¨

APPLICABLE ONLY TO CORPORATE ISSUERS

Indicate the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date:

As of August 13, 2013, there were 10,582,530 shares of $0.001 par value common stock issued and outstanding.

FORM 10-Q

CHINA EDUCATION ALLIANCE, INC.

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PART I –FINANCIAL INFORMATION

Item 1. Financial Statements

China Education Alliance, Inc. and Subsidiaries

Consolidated Balance Sheets

	June 30, 2013 (Unaudited)	December 31, 2012
ASSETS		
Current Assets		
Cash and cash equivalents	$68,894,359	$64,172,917
Accounts receivable	76,946	-
Other receivables	484,881	841,003
Prepaid expenses and other current assets	806,536	660,054
Total current assets	70,262,722	65,673,974
Non-current Assets		
Note receivable	-	7,935,122
Property and equipment, net	9,435,680	11,349,025
Intangibles and capitalized software, net	7,994,254	9,213,515
Total non-current assets	17,429,934	28,497,662
Total Assets	$87,692,656	$94,171,636
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Accounts payable and accrued expenses	$288,159	$420,434
Deferred revenue	1,261,387	1,332,620
Income tax and other taxes payable	111,560	179,544
Total current liabilities	1,661,106	1,932,598
Commitments and Contingent Liabilities	-	-
Stockholders' Equity		
Common stock ($0.001 par value, 150,000,000 shares authorized, 10,582,530 and 10,582,530 issued as of June 30, 2013 and December 31, 2012, respectively; 137,512	10,583	10,583

and 137,512 shares held in treasury, as of June 30, 2013 and December 31, 2012, respectively)		
Additional paid-in capital	40,942,009	40,941,215
Statutory reserve	3,792,161	3,792,161
Retained earnings	28,743,569	36,186,436
Accumulated other comprehensive income	12,111,774	10,322,490
Less: Treasury stock	(977,072)	(977,072)
Stockholders' equity - CEAI and Subsidiaries	84,623,024	90,275,813
Noncontrolling interests in subsidiaries	1,408,526	1,963,225
Total stockholders' equity	86,031,550	92,239,038
Total Liabilities and Stockholders' Equity	$ 87,692,656	$ 94,171,636

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

China Education Alliance, Inc. and Subsidiaries

Consolidated Statements of Operations and Comprehensive Income

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Revenue				
Online education revenue	$ 767,888	$ 1,248,318	$ 1,394,599	$ 3,311,407
Training center revenue	1,142,759	1,822,569	2,958,580	4,569,087
Total revenue	1,910,647	3,070,887	4,353,179	7,880,494
Cost of Revenue				
Online education costs	1,409,183	1,667,990	2,763,504	3,434,765
Training center costs	570,107	736,920	1,286,952	1,578,116
Total cost of revenue	1,979,290	2,404,910	4,050,456	5,012,881
Gross Profit/(Loss)				
Online education gross profit/(loss)	(641,295)	(419,672)	(1,368,905)	(123,358)
Training center gross profit	572,652	1,085,649	1,671,628	2,990,971
Total gross profit/(loss)	(68,643)	665,977	302,723	2,867,613
Operating Expenses				
Selling expenses	1,236,637	1,209,551	2,336,139	2,278,386
Administrative expenses	1,846,937	1,367,628	3,496,898	2,392,613
Depreciation and amortization	785,847	834,979	1,594,219	1,659,590
Total operating expenses	3,869,421	3,412,158	7,427,256	6,330,589
Loss from operations	(3,938,064)	(2,746,181)	(7,124,533)	(3,462,976)
Other Income (Expense)				
Other expenses, net	(1,090)	4,680	(2,807)	(3,065)
Loss on disposal of property and equipment	(7,363)	-	(10,132)	(15,818)
Impairment loss on intangible assets	-	(1,447,334)	(606,032)	(1,447,334)
Interest income	58,678	479,709	110,394	962,645
Total other income/(Expense), net	50,225	(962,945)	(508,577)	(503,572)
Net Loss Before Provision for Income Tax Income taxes:	(3,887,839)	(3,709,126)	(7,633,110)	(3,966,548)
Current	-	(32)	-	(32)
Deferred	-	(436,350)	-	(319,290)
Net Loss	(3,887,839)	(4,145,508)	(7,633,110)	(4,285,870)

Net Loss attributable to the noncontrolling interests	(147,991)	(165,773)	(190,243)	(191,976)
Net Loss - attributable to CEAI and Subsidiaries	$(3,739,848)	$(3,979,735)	$(7,442,867)	$(4,093,894)
Net Loss per common stock-basic and diluted	$(0.35)	$(0.38)	$(0.70)	$(0.39)
Weighted Average Shares Outstanding-basic and diluted	10,582,530	10,582,530	10,582,530	10,582,530
The Components of Other Comprehensive Income				
Net Loss	$(3,739,848)	$(3,979,735)	$(7,442,867)	$(4,093,894)
Foreign currency translation adjustment	1,271,719	66,061	1,789,284	733,556
Comprehensive Loss	$(2,468,129)	$(3,913,674)	$(5,653,583)	$(3,360,338)

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

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China Education Alliance, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(Unaudited)

	Six Months ended June 30, 2013	Six Months ended June 30, 2012
Cash flows from operating activities		
Net loss	$(7,633,110)	$(4,285,870)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization - operating expenses	1,496,222	1,659,590
Depreciation and amortization - cost of revenue	1,375,335	1,421,674
Loss on disposal of fixed assets	10,132	15,818
Bad debt written off on other receivables	-	18,889
Impairment loss on intangible assets	606,032	1,447,334
Stock based compensation	794	3,919
Net changes in operating assets and liabilities		
Accounts receivable	(76,128)	(183,255)
Prepaid expenses and other receivables	237,990	162,980
Deferred tax assets	-	319,290
Accounts payable and accrued liabilities	(137,570)	(908,897)
Income tax and other taxes payable	(67,984)	(363,880)
Deferred revenue	(97,793)	(1,669,664)
Net cash used in operating activities	(4,286,080)	(2,362,072)
Cash flows from investing activities		
Purchases of property and equipment	(35,235)	(40,531)
Loan received back from NIT	8,013,462	-
Proceeds from disposal of property and equipment	1,186	4,097
Net cash (used in) provided by investing activities	7,979,413	(36,434)
Cash flows from financing activities		
Advance to a stockholder	-	18,624
Dividend paid to noncontrolling shareholders	(352,592)	(158,662)
Net cash used in financing activities	(352,592)	(140,038)
Effect of exchange rate changes on cash	1,380,701	477,941
Net increase (decrease) in cash and cash equivalents	4,721,442	(2,060,603)
Cash and cash equivalents at beginning of period	64,172,917	73,597,159
Cash and cash equivalents at end of period	$68,894,359	$71,536,556

Supplemental disclosure of cash flow information		
Income tax paid	$93,858	$92,917

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

China Education Alliance, Inc. and Subsidiaries

Notes to Unaudited Consolidated Financial Statements

1. Description of Business

Nature of organization - China Education Alliance, Inc. (the “Company”), formerly known as ABC Realty Co., was organized under the laws of the State of North Carolina on December 2, 1996. ABC Realty Co.’s primary purpose was to act as a broker or agent in residential real estate transactions. On September 15, 2004, ABC Realty Co., pursuant to a Plan of Exchange, acquired Harbin Zhong He Li Da Education Technology, Inc. (“ZHLD”), a corporation formed on August 9, 2004 in the City of Harbin in the Heilongjiang Province, People’s Republic of China (the “PRC”), with an authorized capital of $60,386 (Renminbi (“RMB”) 500,000).

On September 15, 2004, ABC Realty Co. entered into a Plan of Exchange with ZHLD and Duane C. Bennett, the former Chairman of ABC Realty Co., pursuant to which the shareholders of ZHLD exchanged all of their registered capital of $60,386 for 18,333,334 shares of common stock of the Company, or approximately 95% of the Company’s common stock. On November 17, 2004, ABC Realty Co. changed its name to China Education Alliance, Inc. On December 13, 2004, China Education Alliance, Inc. consummated the Plan of Exchange with ZHLD and ZHLD’s shareholders. As a result of the Plan of Exchange, the transaction was treated for accounting purposes as a recapitalization of ZHLD.

ZHLD is a technology company engaged in the online education industry in the PRC. Its mission is to promote online exam preparation services in the PRC, to improve the efficiency and effectiveness of elementary education, secondary education, vocational education, skill education, continuing education, and professional training programs, and to integrate with the international education system.

ZHLD’s subsidiary, Heilongjiang Zhonghe Education Training Center (“ZHTC”) was registered in the PRC on July 8, 2005 with a registered capital of $60,386 and is accounted for as a wholly owned subsidiary of ZHLD. ZHLD owns 99% of ZHTC with 1% held in trust by Mr. Xiqun Yu, the Company’s CEO, for the benefit of ZHLD.

ZHLD also owns 70% of Beijing Hua Yu Hui Zhong Technology Development Co., Ltd. (“BHYHZ”). BHYHZ was formed on September 30, 2006 in the PRC. At the time of its organization, we transferred a 30% interest in this subsidiary to the National Vocational Education Association of China, a non-profit, quasi-government entity, for no consideration to enable us to work with the Association’s network to expand our business.

On April 18, 2008, ZHLD entered into an agreement and supplementary agreement with Harbin Daily Newspaper Group (“Newspaper Group”) to invest in a joint venture company, Harbin New Discovery Media Co., Ltd. (“New Discovery”). ZHLD contributed RMB3,000,000 (approximately $430,000) and Newspaper Group contributed RMB3,120,000 (approximately $445,000) towards the registered capital of New Discovery. In return for their respective contributions, ZHLD owns 49.02% equity interest and Newspaper Group owns 50.98% equity interest in New Discovery. The parties are prohibited, for the duration of the joint venture from retiring or transferring their equity interests. As the Company did not foresee that the investment cost is recoverable from this joint venture in the near future, the Company provided fully impairment on the investment by the year ended December 31, 2011.

On January 4, 2009, ZHLD entered into an agreement with Mr. Guang Li to jointly incorporate and invest in a joint venture company, Zhong He Li Da (Beijing) Management Consultant Co., Ltd. (“ZHLDBJ”). ZHLD contributed RMB425,000 (approximately $62,107), and Mr. Guang Li contributed RMB 75,000 (approximately $10,960) towards the registered capital of ZHLDBJ, amounting to a total registered capital of RMB500,000 (approximately $73,067). In return for their respective contributions, ZHLD owns an 85% equity interest, and Mr. Guang Li owns a 15% equity interest in ZHLDBJ. ZHLD has entrusted Mr. Xiqun Yu to hold 20% of its equity interest of ZHLDBJ on its behalf. ZHLDBJ will be involved in the vocational training business which includes IT engineering and accounting training.

In February 2010, the Company, through ZHLD, incorporated a new company in the PRC, Beijing New Shifan Education & Technology Co., Ltd. (“New Shifan”) with a registered capital of RMB1.95 million (approximately $291,132). ZHLD owned a 65% equity interest in New Shifan and the other equity holders together owned a 35% equity interest in New Shifan. New Shifan was created to continue the operations of Beijing Shifan Culture Communication Co., Ltd. ("Beijing Shifan"). The Company paid the original owner of Beijing Shifan RMB7 million (approximately $1,056,970) to acquire their expertise, in (i) science and math education at the secondary education level, (ii) the rights to continue publishing the magazine “Senior High School Students Mathematics, Physics, and Chemistry” and (iii) the rights to a nationwide contest for middle school and high school students. In September 2011, New Shifan changed its name to Beijing Hua Yu Pin Xue Education Technology Co., Ltd ("HYPX"). In October 2011, ZHLD took over the 35% equity interest from the other equity holders of HYPX without any consideration, and entrusted Mr. Xiqun Yu to hold the 35% equity interest on behalf of ZHLD. In November 2011, HYPX increased its share capital to RMB2 million (approximately $298,567). In January 2012, due to changes in government regulations, the Company authorized Mr. Yu to hold the 100% equity interest on behalf of ZHLD. HYPX is focusing on expanding our training centers in Beijing, and developing extensive marketing strategy to establish new markets in other main cities.

On March 4, 2011, the Company entered into a management agreement with Nanchang Institute of Technology (“NIT”), a vocational training institution based in Nanchang, PRC. Pursuant to the agreement, the Company would assist in managing the daily operations of NIT for ten years for an annual management fee of RMB 10 million (approximately $1,461,347). The management fee was payable on a quarterly basis and in the event of late payment, a late fee would be imposed. Additionally, a liquidated damage of RMB 50 million (approximately $7,935,122) would be paid by any party that defaulted on the agreement.

In connection with the management agreement, the Company entered in to a loan agreement, pursuant to which the Company agreed to loan NIT RMB 50 million (approximately $7,935,122) to build training facilities and NIT would repay the RMB 50 million (approximately $7,935,112) in ten years from the date NIT received the principal. The loan had an annual interest rate of 20% and the interest would be waived by the Company if NIT made all payments under the management agreement in a timely manner. We received 20% annual interest income due each quarter, therefore, the management fee was waived. The loan was secured by the assets of certain guarantors. On March 29, 2013, NIT repaid the loan principal of RMB50 million and accrued interests and the loan agreement was terminated. On the same day, the management agreement with NIT was also terminated.

On February 25, 2011 the Company entered into a share transfer agreement with the shareholder of Harbin Tianlang Culture and Education School (“Tianlang”), a tutoring school with 5,000 students, based in Harbin, PRC. Pursuant to the share transfer agreement, the Company purchased 60% of the equity interests of Tianlang for RMB 35 million (approximately $5.3 million). The shareholder and the Company also provided RMB 2 million (approximately $0.3 million) and RMB 3 million (approximately $0.5 million) as working capital for Tianlang, respectively. Tianlang had established a new board of directors with five directors, of which three directors were appointed by the Company and two directors were appointed by the shareholder. The acquisition of Tianlang was completed in April 2011. We are currently co-managing Tianlang with the previous majority owner. The Company and the previous majority owner will be entitled to 60% and 40%, respectively, of the profits of Tianlang.

On May 31, 2011, the Company entered into share transfer agreements with the shareholders (the "Shareholders") of Changchun City Chaoyang District Nuoya Foreign Languages School ("Changchun Nuoya") and Harbin City Nangang District Nuoya Foreign Languages School ("Harbin Nuoya"), two foreign language schools based in the PRC.

Pursuant to the agreements, the Company purchased 100% of the two schools for an aggregate of RMB 16 million (approximately $2.5 million), and all consideration had been paid up. The Shareholders' obligations under the agreements are guaranteed by a guarantor who will be jointly and severally liable in the event of a breach by the Shareholders. The acquisition of Changchun Nuoya and Harbin Nuoya was completed by the end of May 2011 and their financial statements had been consolidated with the Company's financial statements since May 2011. The Company did not foresee that the investment cost in Harbin Nuoya and Changchun Nuoya is recoverable in the near future. As a result, the Company fully impaired its investment in the two schools. As there is little demand for non-English classes at the time being, the Company has suspended the operation of Changchun Nuoya.

In June 2012, the Company, through ZHLD, incorporated a new company in the PRC, Harbin Zhong He Li Da Information Technology Co., Ltd. ("ZHLDIT") with a registered capital of RMB2 million. Mr. Yu has been entrusted to hold the 100% equity interest on behalf of ZHLD. ZHLDIT was established to initiate and design a platform for online education programs, and provide this effective and efficient communication service to all the teachers and students.

2 Basis of Preparation of Financial Statements

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP"). The consolidated financial statements include the financial statements of the Company and its subsidiaries. All significant inter-company transactions and balances have been eliminated in consolidation. The portion of the income applicable to noncontrolling interests in subsidiaries undertakings is reflected in the consolidated statements of operations.

3. Summary of Significant Accounting Policies

Use of estimates - The preparation of these financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of net sales and expenses during the reported periods.

Significant estimates include values, classification, useful lives assigned to and impairment of acquired intangible assets, the useful lives and impairment of property and equipment, collectability of accounts receivable, reserves for allowances and stock option valuation. Actual results may differ from these estimates.

Cash and cash equivalents - The Company considers all highly liquid debt instruments purchased with a maturity period of three months or less to be cash or cash equivalents. The carrying amounts reported in the accompanying unaudited condensed consolidated balance sheets for cash and cash equivalents approximate their fair value. All of the Company's cash that is held in bank accounts in the PRC is not protected by Federal Deposit Insurance Corporation ("FDIC") insurance or any other similar insurance in the PRC. The cash that the Company maintains in US banks is insured up to $250,000 at each bank as of June 30, 2013 and December 31, 2012. The Company's cash at their US banks is in excess of statutorily insured limits at $3,609,189 and $4,525,820, as of June 30, 2013 and December 31, 2012, respectively.

Property and equipment - Property and equipment is stated at the historical cost, less accumulated depreciation and impairments. Depreciation on property and equipment is provided using the straight-line method over the estimated useful lives of the assets as follows:

Buildings	20 years
Communication equipment	10 years
Transportation vehicles	5 years
Furniture and fixtures	5 years

Leasehold improvements	over unexpired lease terms

Expenditures for renewals and betterments are capitalized while repairs and maintenance costs are normally charged to the statement of operations in the period/year in which they are incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the asset, the expenditure is capitalized as an additional cost of the asset.

Upon sale or disposal of an asset, the historical cost and related accumulated depreciation and impairment of such asset are removed from their respective accounts and any gain or loss is recorded in the statements of operations.

The Company reviews the carrying value of property and equipment for impairment whenever events and circumstances indicate that the carrying value of an asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where undiscounted expected future cash flows are less than the carrying value, an impairment loss is recognized equal to an amount by which the carrying value exceeds the fair value of assets. The factors considered by management in performing this assessment include current operating results, trends and prospects, the manner in which the property and equipment are used, and the effects of obsolescence, demand, competition, and other economic factors.

Intangibles - Intangibles consist of franchise rights on educational products, software, teacher list, student list, domain/brand name, course materials, goodwill, magazine rights and contest operation rights. Most intangible assets are amortized over the lives of the rights agreements, or their respective operational useful lives.

The Company evaluates the carrying value of intangible assets during the second quarter of each year and between annual evaluations if events occur, or circumstances change, that would more likely than not reduce the fair value of the intangible asset below its carrying amount. For the three months and six months ended June 30, 2013 and 2012, the Company performed the impairment test on its intangible assets, and recorded $0 and $1,447,334, $606,032 and $1,447,334, respectively, as impairment loss.

In April 2011, the Company purchased 60% of Tianlang for RMB 35 million (approximately $5.3 million) and 100% ownership of Changchun Nuoya and Harbin Nuoya. These three schools' net assets included identifiable intangible assets such as domain name/brand name, cost of materials, student list, course materials and teacher lists. The economic useful life for domain name/brand name is estimated to be 10 years and the others are estimated to be 3 years.

Long-lived assets - The Company reviews its long-lived assets for impairments when changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Long-lived assets under certain circumstances are reported at the lower of carrying amount or fair value. Assets to be disposed of and assets not expected to provide any future service potential to the Company are recorded at the lower of carrying amount or fair value less cost to sell. To the extent carrying values exceed fair values; an impairment loss is recognized in operating results.

Foreign Currency - The Company's principal country of operations is the PRC. The financial position and results of operations of the Company are recorded in USD as the functional currency, and the financial position and results of operations of the Company's PRC subsidiaries are recorded in RMB as the functional currency. The results of operations denominated in foreign currency are translated at the average rate of exchange during the respective reporting period.

Assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the market rate of exchange at that date. The registered equity capital denominated in the functional currency is translated at the historical rate of exchange at the time of capital contribution. All translation adjustments resulting from the translation of the financial statements into the reporting currency ("U.S. Dollars" or "US$") are recorded in accumulated other comprehensive income, a separate component within shareholders' equity. The accompanying consolidated financial statements are presented in US$. The functional currency of the Company is RMB. The consolidated financial statements are translated into US$ from RMB at year-end exchange rates as to assets and liabilities and average exchange rates as to revenues and expenses. Capital accounts are translated at their historical exchange rates when the capital transactions occurred. The resulting translation adjustments are recorded as a component of shareholders' equity included in other comprehensive income. Gains and losses from foreign currency transactions are included in profit or loss. There were no gains and losses from foreign currency transactions during the quarter ended June 30, 2013 and 2012.

As of

	June 30, 2013	December 31, 2012
RMB: US$ exchange rate	6.1732	6.3011

	Six Months Ended June 30,	
	2013	2012
Average RMB: US$ exchange rate	6.2395	6.3027

The RMB is not freely convertible into foreign currency and all foreign exchange transactions must take place through authorized institutions. No representation is made that the RMB amounts could have been, or could be, converted into US$ at the rates used in translation.

Noncontrolling interest - Noncontrolling interest in the Company's subsidiaries are recorded in accordance with the provisions of Financial Accounting Standard Board ("FASB") Codification 810 Consolidation ("ASC 810") and are reported as a component of equity, separate from the parent's equity. Purchase or sales of equity interests that do not result in a change of control are accounted for as equity transactions. Results of operations attributable to the noncontrolling interest are included in our consolidated results of operations and, upon loss of control, the interest sold, as well as interest retained, if any, will be reported at fair value with any gain or loss recognized in earnings.

Revenue recognition - Revenue is recognized when the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) the service has been rendered; (3) the selling price is fixed or determinable; and (4) collection of the resulting receivable is reasonably assured. The Company believes that these criteria are satisfied when customers download prepaid study materials.

Prepaid debit cards allow the Company's subscribers to purchase a predetermined monetary amount of download materials downloadable from its website. The Company tracks usage of the debit card and records revenue when the debit card is used.

At the time that the prepaid debit card is purchased, the receipt of cash is recorded as deferred revenue. Revenues are recognized in the month when card is used. Unused value relating to debit cards is recognized as revenues when the prepaid debit card expires.

Tuition from courses is recognized ratably over the period that fees are earned, typically the life of the course. The Company offers credits to students if they should withdraw, or are unable to complete their courses. Historically the issuances of credits have not been high with regards to tuition fees. The Company offers cash refunds on a limited basis based on individual circumstances.

The Company engages an advertisement agency to manage its on-line advertisement revenue. Pursuant to the contract with this agency, upon posting of an on-line advertisement on the Company's website, the Company is entitled to share with the agency 50% of the amount charged to the on-line advertiser.

The Company recognizes advertising revenue monthly on receipt of the confirmation from the agent. The agency is responsible for collection of all ad revenue from advertisers. The agency is required to make their remittance for on-line advertising six months after on-line ads are posted on the Company's website.

Deferred revenue reflects the unearned portion of debit cards sold and tuition payments received. Tuition is recognized as revenue ratably over the periods in which it is earned, generally the term of the program or as the debit card is used.

Deferred revenue - Deferred revenue reflects the unearned portion of debit cards sold and tuition payments received. Deferred revenue as of June 30, 2013 and December 31, 2012 was $1,261,387 and $1,332,620, respectively.

Advertising - The Company expenses advertising costs at the time they are published on the newspaper and for all other advertising the first time the respective advertising takes place. These costs are included in selling and administrative expenses. The total advertising expenses incurred for the three and six months ended June 30, 2013 and 2012 were $459,152 and $73,857, $915,936 and $89,736, respectively.

Taxation - Taxation on profits earned in the PRC are calculated on the estimated assessable profits for the year at the rates of taxation prevailing in the PRC after taking into effect the benefits from any special tax credits or “tax holidays” allowed in the PRC.

The Company does not accrue United States income tax on unremitted earnings from foreign operations, as it is the Company’s intention to invest these earnings in foreign operations for the foreseeable future. All of the Company’s revenues are generated in the PRC. The Company’s US operations provide corporate and administrative functions for the entire Company. The Company’s tax provisions for the three and six months ended June 30, 2013 and 2012 are related to the Company’s PRC operations.

If the Company should have an uncertainty in accounting for income taxes, the Company evaluates a tax position in a two-step process. The first step is to determine whether it is more-likely-than-not that a tax position will be sustained upon examination, including the resolution of any related appeals or litigation based on the technical merits of the position. The second step is to measure the tax position that meets the more-likely-than-not threshold to determine the amount of provision or benefit to be recognized in the financial statements. A tax position is measured at the largest amount of provision or benefit where there is a greater than 50% likelihood of being realized upon ultimate settlement.

Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent period in which the threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not criteria should be de-recognized in the first subsequent reporting period in which the threshold is no longer met.

Income Tax

Private schools or colleges operated for reasonable returns, such as our subsidiary Tianlang, are subject to income taxes at 25% after January 1, 2008, but were sometimes subject to deemed amounts or preferential tax arrangement of income tax to be determined by the relevant tax authorities. Our subsidiary Tianlang had not yet been charged income taxes under current regulation. The Company is unable to accurately estimate the chance of having the Tianlang’s tax position being challenged by PRC tax authorities; therefore the Company did not record any tax liabilities in respect of Tianlang’s profits.

Based on all known facts and circumstances and current tax law, the Company believes that the total amount of unrecognized tax provisions or benefits as of June 30, 2013, is not material to its results of operations, financial condition or cash flows. The Company also believes that the total amount of unrecognized tax provisions or benefits as of June 30, 2013, if recognized, would not have a material effect on its effective tax rate. The Company further believes that there are no tax positions for which it is reasonably possible, based on current PRC tax laws and policies, that the unrecognized tax provisions or benefits will significantly increase or decrease over the next 12 months producing, individually or in the aggregate, a material effect on the Company’s results of operations, financial condition or cash flows.

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets, including tax loss and credit carry forwards, and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

The effect of deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred income tax expense represents the change during the period in the deferred tax assets and deferred tax liabilities. The components of the deferred tax assets and liabilities are individually classified as current and non-current based on their characteristics. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company had deferred tax assets of $0 as of June 30, 2013 and December 31, 2012, respectively.

Value added tax

The Provisional Regulations of the People's Republic of China Concerning Value Added Tax ("VAT") promulgated by the State Council came into effect on January 1, 1994. Under these regulations and the Implementing Rules of the Provisional Regulations of the PRC Concerning VAT is imposed on goods sold in or imported into the PRC and on processing, repair and replacement services provided within the PRC.

VAT payable in the PRC is charged on an aggregated basis at a rate of 13% or 17% (depending on the type of goods involved) on the full price collected for the goods sold or, in the case of taxable services provided, at a rate of 17% on the charges for the taxable services provided, but excluding, in respect of both goods and services, any amount paid in respect of VAT included in the price or charges, less any deductible VAT already paid by the taxpayer on purchases of goods and services. The Company records all revenues net of VAT.

Stock-based compensation - The Company records compensation expense associated with stock-based awards and other forms of equity compensation. Such compensation would include the recording of cost resulting from all stock-based payment transactions including shares issued under its stock option plans. The Company records expense over the vesting period in connection with stock options granted. The compensation expense for stock-based awards includes an estimate for forfeitures and is recognized over the expected term of the award on a straight-line basis.

The Company recorded stock-based compensation expenses of $199 and $1,277, respectively, for the three months ended June 30, 2013 and 2012. The Company also recorded stock-based compensation expenses of $794 and $3,919 for the six months ended June 30, 2013 and 2012, respectively.

Fair value of financial instruments - The Company has adopted newly issued generally accepted accounting principles with regards to fair value measurement for assets and liabilities that establishes a common definition for fair value to be applied to existing generally accepted accounting principles that require the use of fair value measurements, establishes a framework for measuring fair value and expands disclosure about such fair value measurements. The adoption of these principles did not have an impact on the Company's financial position or operating results, but did expand certain disclosures.

Fair value is defined fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Additionally, current standards require the use of valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. These inputs are prioritized below:

Level 1:	Observable inputs such as quoted market prices in active markets for identical assets or liabilities
Level 2:	Observable market-based inputs or unobservable inputs that are corroborated by market data
Level 3:	Unobservable inputs for which there is little or no market data, which require the use of the reporting entity's own assumptions.

The Company did not have any assets or liabilities valued using Level 2 or Level 3 inputs as of June 30, 2013 and December 31, 2012, respectively.

Treasury stock - We account for treasury stock under the cost method and include treasury stock as a component of stockholders' equity. When retired, the excess of the cost of treasury stock over its par value is allocated between retained earnings and additional paid-in capital.

Recent accounting pronouncements - Management does not believe that any recently issued, but not yet effective, accounting standards or pronouncements, if currently adopted, would have a material effect on the Company's consolidated financial statements.

4. Concentrations of business and credit risk

The majority of the Company's bank accounts are with banks located in the PRC that are not covered by any type of protection similar to that provided by the FDIC on funds held in U.S. banks.

The Company is operating in the PRC, which may give rise to significant foreign currency risks from fluctuations and the degree of volatility of foreign exchange rates between the US$ and the RMB.

Financial instruments that potentially subject the Company to concentration of credit risk consist principally of cash and accounts receivable, the balances of which are stated on the balance sheet. The Company places its cash in high credit quality financial institutions; however, such funds are not insured in the PRC. As of June 30, 2013 and December 31, 2012, the Company maintains cash in the US, in a financial institution insured by the FDIC that has approximately $3,609,189 and $4,525,820, respectively, in funds in excess of FDIC insured amounts.

For the three and six months ended June 30, 2013 and 2012, no sales to a single customer accounted for 10% or more of our revenue.

Our subsidiaries ZHTC, Changchun Nuoya and Harbin Nuoya are private schools not operated for reasonable returns; therefore, are not allowed to distribute dividends. As of June 30, 2013 and December 31, 2012, the total un-distributable net assets of ZHTC, Changchun Nuoya and Harbin Nuoya amounted to $34,385,784 and $33,169,873, respectively.

5. Cash and cash equivalents

Cash and cash equivalents consist of the following:

	June 30, 2013 (Unaudited)	December 31, 2012
Cash on Hand -China	$ 471,270	$ 38,522
Bank Deposits-China	64,510,542	59,273,602
Bank Deposits-US	3,912,547	4,860,793
	$ 68,894,359	$ 64,172,917

6. Prepaid expenses and other current assets

Prepaid expenses consist of the following:

	June 30, 2013 (Unaudited)	December 31, 2012
Prepaid rent	$ 533,593	$ 313,981
Prepaid teachers and online material	214,669	213,174
Prepaid services and professional fees	5,940	-
Prepaid advertising	35,641	104,746
Other prepaid expenses	16,693	28,153
	$ 806,536	$ 660,054

7. Property and equipment, net

Property and equipment consist of the following:

	June 30, 2013 (Unaudited)	December 31, 2012

Buildings	$1,439,775	$ 1,410,550
Transportation vehicles	106,484	112,258
Communication equipment	10,528,264	12,949,181
Furniture and fixtures	5,505,093	2,956,701
Leasehold improvement	3,042,911	2,955,891
	20,622,527	20,384,581
Less: Accumulated Depreciation	(11,186,847)	(9,035,556)
Property and Equipment, net	$9,435,680	$ 11,349,025

For the three and six months ended June 30, 2013 and 2012, depreciation expenses totaled $927,308 and $1,052,308, $2,051,529 and $2,088,191, respectively. For the three and six months ended June 30, 2013 and 2012, loss on disposal of fixed assets was $7,363 and $0, $10,132 and $15,818, respectively.

8. Intangibles and capitalized software, net

Intangibles of the Company consisted of franchise rights on educational products, software, magazine rights, contest operation rights, domain name/brand name, course materials, student list and teacher list, and goodwill.

Franchise rights

The franchise rights owned by the Company consist of the following:

- The ACCP training course is an authority for training software engineers under training procedures with textbooks;

- The BENET training course is an authority for training internet engineers under training procedures with textbooks.

Capitalized software

The capitalized software of the Company consists of all the Company’s software, among which two main ones are the following:

- The usage rights for job seekers is software to help university students to search jobs, post their resumes, and communicate with potential employers;

- The usage right for learners is software to help elementary and secondary students to do assignments, test papers, and get instructions from teachers.

Intangible assets on acquisitions

In March 2011, the Company acquired a 60% controlling interest in Tianlang for a purchase price of RMB 35 million (approximately $5.3 million). The school had insignificant tangible assets or liabilities at the acquisition date. The entire estimated fair value of approximately $8.9 million has been allocated to the net identifiable assets of Tianlang; the intangible assets recorded are all subject to amortization.

In May 2011, the Company acquired a 100% ownership in Changchun Nuoya and Harbin Nuoya. The aggregate purchase price for the two schools was RMB 16 million (approximately $2.5 million). The schools had insignificant tangible assets or liabilities at the acquisition date. The entire estimated fair value of approximately $2.5 million has been allocated to the net identifiable assets of Changchun Nuoya and Harbin Nuoya; the intangible assets recorded are all subject to amortization.

The Company did not foresee that the investment cost in Harbin Nuoya is recoverable in the near future, and concluded for the group reporting that certain triggering events had occurred which could result in it being more likely than not that the fair value of each reporting unit would be less than its carrying value. As a result, the Company conducted the impairment test for intangible assets which resulted in impairments for the three and six months ended June 30, 2013 of $0 and $606,032, respectively, for Harbin Nuoya.

Intangibles and capitalized software consist of the following:

	June 30, 2013 (Unaudited)	December 31, 2012
ACCP training course	$ 816,432	$ 799,859
BENET training course	57,183	56,023
Usage rights- Job Seekers	485,972	476,107
Usage rights- Learners	323,981	317,405
Others	2,500,481	2,470,238
Domain names	9,601,054	9,446,515
Course materials	543,172	534,040
Student list	803,235	790,083
Teacher list	1,058,391	1,041,949
	16,189,901	15,932,219
Less: Impairments	(1,986,433)	(1,447,703)
Less: accumulated amortization	(6,209,214)	(5,271,001)
Intangible and Capitalized Software, net	$ 7,994,254	$ 9,213,515

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For the three and six months ended June 30, 2013 and 2012, amortization expenses were $398,256 and $493,830, $820,028 and $993,075, respectively.

For the three and six months ended June 30, 2013 and 2012, impairment loss was $0 and $1,447,334, $606,032 and $1,447,334, respectively.

Amortization of intangibles and capitalized software over the next five years is as follows:

Years ending December 31,	
2013	$801,485
2014	1,142,797
2015	953,517
2016	857,339
2017	761,356
	$4,516,494

9. Accounts payable and accrued expenses

Accounts payable and accrued expenses consist of the following:

	June 30, 2013 (Unaudited)	December 31, 2012
Accounts payable	$ 4,050	$ 3,968
Accrued payroll	131,681	195,880
Accrued expenses	71,763	148,561
Other payables	80,665	72,025
	$ 288,159	$ 420,434

10. Deferred revenue

Deferred revenues include subscriber prepayments and education fee prepayments. Subscriber prepayments represent deferred revenue for the purchase of debit cards used to pay for the online downloading of education materials. The Company recognizes revenue when the card is used to download material. During the period between the purchase and use of debit cards, the unused portion of the debit card is treated as deferred revenue to the Company. Education fee prepayments represent payments for tuition for the Company’s training schools, which are amortized over the term of the course. As of June 30, 2013 and December 31, 2012, the Company had deferred revenue of $1,261,387 and

$1,332,620, respectively.

11. Stockholders’ Equity

The Company had no significant equity transactions during the quarter ended June 30, 2013.

12. Warrants and options

Throughout the report, all the number of shares is adjusted to reflect a one-for-three reverse stock split effected in 2011.

Warrants

For six months ended June 30, 2013 and the year ended December 31, 2012, the Company did not issue any warrants.

As of June 30, 2013 and December 31, 2012, all the Company's previously issued warrants have been exercised and the Company did not have any warrants outstanding.

Stock Options

During the three and six months ended June 30, 2013 and 2012, the Company did not issue any stock options. The total stock based compensation was $199 and $1,277, $794 and $3,919 respectively, related to the vesting of previously granted options.

The Company measures the fair value of options at the end of each reporting period until options are exercised, cancelled or expire unexercised. As of six months ended June 30, 2013, there were options to acquire 52,667 shares of common stock with a weighted average exercise price of $2.67 and a weighted average remaining life of 0.85 years, which remain outstanding and continue to be remeasured at the intrinsic value over their remaining vesting period of 0.85 years. Compensation expense in any given period is calculated as the difference between total earned compensation at the end of the period, less total earned compensation at the beginning of the period. Compensation earned is calculated on a straight line basis over the requisite service period for any given option award. As of June 30, 2013, there was no unrecognized compensation expense related to stock options. The intrinsic value for exercisable options as of June 30, 2013 is $0 because the market price is lower than exercise price.

Stock option activity for the three months ended June 30, 2013 is summarized as follows:

	Shares underlying options	Weighted average exercise price
Outstanding as of December 31, 2012	52,667	$ 2.67
Granted	-	-
Exercised	-	-
Expired / cancelled / forfeited	-	-
Outstanding as of June 30, 2013	52,667	$ 2.67
Exercisable and vested as of June 30, 2013	52,667	$ 2.67

The following table summarizes the Company's stock options outstanding at June 30, 2013.

Weighted average exercise price	Outstanding June 30, 2013	Weighted average remaining life in years	Number exercisable
$ 2.67	52,667	0.85	52,667
	52,667		52,667

13. Earnings per share

Per GAAP the Company reconciles the numerator and denominator of the basic and diluted earnings per share (EPS) computations.

For the three and six months ended June 30, 2013 and 2012, dilutive shares include shares attributable to exercisable options only if such inclusion would be dilutive.

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The following reconciles the components of the EPS computation:

	Six Months Ended June 30,	
	2013	2012
Net (loss) income to common shareholders	$(7,442,867)	$(4,093,894)
Weighted average shares outstanding - basic	10,582,530	10,582,530
Effect of dilutive securities	-	-
Weighted average shares outstanding - diluted	10,582,530	