STEPHAN CO
Form 10-Q
May 26, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

# FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934

For the Quarterly Period Ended: March 31, 2006

Commission File No. 1-4436

THE STEPHAN CO.
(Exact Name of Registrant as Specified in its Charter)

| | |
|---|---|
| Florida | 59-0676812 |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification No.) |

| | |
|---|---|
| 1850 West McNab Road, Fort Lauderdale, Florida | 33309 |
| (Address of Principal Executive Offices) | (Zip Code) |

Registrant's Telephone Number, including Area Code: (954) 971-0600

Indicate by check mark whether the Registrant (1) has filed all 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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act).
Large accelerated filer[ ] Accelerated filer[ ] Non-accelerated filer[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

Approximate number of shares of Common Stock outstanding
as of April 30, 2006:

4,389,805

THE STEPHAN CO. AND SUBSIDIARIES

QUARTERLY REPORT PURSUANT TO SECTION 13
OF THE SECURITIES EXCHANGE ACT OF 1934
MARCH 31, 2006

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THE STEPHAN CO. AND SUBSIDIARIES
QUARTERLY REPORT PURSUANT TO SECTION 13
OF THE SECURITIES EXCHANGE ACT OF 1934
MARCH 31, 2006

CAUTIONARY STATEMENT FOR PURPOSES OF THE SAFE HARBOR
PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This quarterly report contains certain "forward-looking" statements. The Stephan Co. ("Stephan" or the "Company") desires to take advantage of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995 and is including this statement for the express purpose of availing itself of the protections of such safe harbor with respect to all such forward-looking statements. Such forward-looking statements involve risks, uncertainties and other factors which may cause the actual results, condition (financial or otherwise), performance, trends or achievements of the Company and its subsidiaries to be materially different from any results, condition, performance, trends or achievements projected, anticipated or implied by such forward-looking statements.

Words such as "projects," "believe," "anticipates," "estimate," "plans," "expect," "intends," and similar words and expressions are intended to identify forward-looking statements and are based on our current expectations, assumptions, and estimates about us and our industry. In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances are forward-looking statements. Although we believe that such forward-looking statements are reasonable, we cannot assure you that such expectations will prove to be correct.

Our actual results could differ materially from those anticipated in such forward-looking statements as a result of several factors, risks and uncertainties. These factors, risks and uncertainties include, without limitation, our ability to satisfactorily address any material weaknesses in our financial controls; general economic and business conditions; competition; the relative success of our operating initiatives; our development and operating costs; our advertising and promotional efforts; brand awareness for our product offerings; the existence or absence of adverse publicity; acceptance of any new product offerings; changing trends in customer tastes; the success of any multi-branding efforts; changes in our business strategy or development plans; the quality of our management team; costs and expenses incurred by us in pursuing strategic alternatives; the availability, terms and deployment of capital; the business abilities and judgment of our personnel; the availability of qualified personnel; our labor and employee benefit costs; the availability and cost of raw materials and supplies; changes in or newly-adopted accounting principles; changes in, or our failure to comply with, applicable laws and regulations; changes in our product mix and associated gross profit margins; as well as management's response to these factors, and other factors that may be more fully described in the Company's literature, press releases and publicly-





filed documents with the Securities and Exchange Commission. You are urged to carefully review and consider these disclosures, which describe certain factors that affect our business.

We do not undertake, subject to applicable law, any obligation to publicly release the results of any revisions, which may be made to any forward-looking statements to reflect events or circumstances occurring after the date of such statements or to reflect the occurrence of anticipated or unanticipated events. Therefore, we caution each reader of this report to carefully consider the specific factors and qualifications discussed herein with respect to such forward-looking statements, as such factors and qualifications could affect our ability to achieve our objectives and may cause actual results to differ materially from those projected, anticipated or implied herein.



PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

THE STEPHAN CO. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS

| | March 31, 2006 | December 31, 2005 |
|---|---|---|

| | | |
|---|---|---|
| CURRENT ASSETS | | |
| Cash and cash equivalents | $ 5,934,540 | $ 5,602,762 |
| Restricted cash | 3,150,087 | 3,335,557 |
| Accounts receivable, net | 1,850,952 | 1,431,650 |
| Inventories | 6,111,130 | 6,148,267 |
| Income taxes receivable | - | 22,893 |
| Prepaid expenses and other current assets | 200,909 | 311,905 |
| TOTAL CURRENT ASSETS | 17,247,618 | 16,853,034 |
| PROPERTY, PLANT AND EQUIPMENT, net | 1,654,213 | 1,682,951 |
| GOODWILL, net | 4,013,458 | 4,013,458 |
| TRADEMARKS, net | 8,364,809 | 8,364,809 |
| DEFERRED ACQUISITION COSTS, net | 125,679 | 142,185 |
| OTHER ASSETS, net | 1,693,422 | 1,721,169 |
| TOTAL ASSETS | $ 33,099,199 | $ 32,777,606 |

See notes to unaudited condensed consolidated financial statements

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THE STEPHAN CO. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS' EQUITY

| | March 31, 2006 | December 31, 2005 |
|---|---|---|
| CURRENT LIABILITIES | | |
| Accounts payable and accrued expenses | $ 2,562,113 | $ 2,002,728 |
| Current portion of long-term debt | 2,960,000 | 3,237,500 |
| TOTAL CURRENT LIABILITIES | 5,522,113 | 5,240,228 |

| | | |
|---|---|---|
| DEFERRED INCOME TAXES, net | 1,373,705 | 1,343,257 |
| TOTAL LIABILITIES | 6,895,818 | 6,583,485 |
| COMMITMENTS AND CONTINGENCIES (NOTE 3) | | |
| STOCKHOLDERS' EQUITY | | |
| Common stock, $.01 par value | 43,898 | 43,898 |
| Additional paid in capital | 17,556,731 | 17,556,731 |
| Retained earnings | 8,602,752 | 8,593,492 |
| TOTAL STOCKHOLDERS' EQUITY | 26,203,381 | 26,194,121 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | $ 33,099,199 | $ 32,777,606 |

See notes to unaudited condensed consolidated financial statements



THE STEPHAN CO. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

| | Three Months Ended March 31, | |
|---|---|---|
| | 2006 | 2005 |
| NET SALES | $ 5,596,397 | $ 5,516,811 |
| COST OF GOODS SOLD | 3,378,582 | 3,157,680 |
| GROSS PROFIT | 2,217,815 | 2,359,131 |
| SELLING, GENERAL AND ADMINISTRATIVE EXPENSES | 2,078,332 | 2,242,724 |
| OPERATING INCOME | 139,483 | 116,407 |
| OTHER INCOME(EXPENSE) | | |
| Interest income | 43,463 | 27,072 |
| Interest expense | (31,798) | (31,262) |
| Royalty income | 12,500 | 12,500 |

| | | |
|---|---|---|
| INCOME BEFORE INCOME TAXES | 163,648 | 124,717 |
| INCOME TAX EXPENSE | 66,592 | 50,519 |
| NET INCOME | $ 97,056 | $ 74,198 |
| BASIC AND DILUTED EARNINGS PER SHARE: | $ .02 | $ .02 |
| WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING | 4,391,747 | 4,418,630 |

See notes to unaudited condensed consolidated financial statements

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THE STEPHAN CO. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Three Months Ended March 31, | |
|---|---|---|
| | 2006 | 2005 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | $ 97,056 | $ 74,198 |
| Adjustments to reconcile net income to cash flows provided by operating activities: | | |
| Depreciation | 37,454 | 36,659 |
| Amortization of intangible assets | 16,506 | 20,880 |
| Write-down of inventories | - | 20,000 |
| Deferred income tax expense | 30,448 | 36,200 |
| Provision for doubtful accounts | 27,177 | 9,835 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (446,479) | 167,736 |
| Inventories | 37,137 | (258,476) |

| | | |
|---|---|---|
| Income taxes payable/receivable | 22,893 | (10,681) |
| Prepaid expenses and other current assets | 110,996 | 146,840 |
| Other assets | 27,747 | 206,100 |
| Accounts payable and accrued expenses | 559,385 | 533,217 |
| Total adjustments | 423,264 | 908,310 |
| Net cash flows provided by operating activities | 520,320 | 982,508 |

See notes to unaudited condensed consolidated financial statements



THE STEPHAN CO. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Three Months Ended March 31, | |
|---|---|---|
| | 2006 | 2005 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Change in restricted cash | 185,470 | (11,208) |
| Purchase of property, plant and equipment | (8,716) | (107,197) |
| Net cash flows provided by/(used in) investing activities | 176,754 | (118,405) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Repayments of long-term debt | (277,500) | (277,500) |
| Dividends paid | (87,796) | (87,799) |
| Net cash flows used in financing activities | (365,296) | (365,299) |
| INCREASE IN CASH AND CASH EQUIVALENTS | 331,778 | 498,804 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | 5,602,762 | 4,402,463 |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | $ 5,934,540 | $ 4,901,267 |

Supplemental Disclosures of Cash Flow Information:

| | | |
|---|---|---|
| Interest paid | $ 11,798 | $ 15,960 |
| Income taxes paid | $ - | $ - |

See notes to unaudited condensed consolidated financial statements



THE STEPHAN CO. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
QUARTERS ENDED MARCH 31, 2006 AND 2005

NOTE 1: NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

NATURE OF OPERATIONS: The Stephan Company (the "Company") is engaged in the manufacture, sale, and distribution of hair and personal care grooming products principally throughout the United States. The Company has allocated substantially all of its business into three segments, which include professional hair care products and distribution, retail personal care products and manufacturing.

BASIS OF PRESENTATION: In the opinion of management, all adjustments (consisting only of normal accruals) necessary for a fair presentation of the Company's financial position and results of operations are reflected in these unaudited interim financial statements.

The results of operations for the three-month period ended March 31, 2006 is not necessarily indicative of the results to be achieved for the year ending December 31, 2006. The December 31, 2005 condensed consolidated balance sheet was derived from the audited consolidated financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America ("generally accepted accounting principles"). These interim financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes appearing in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, previously filed with the Securities and Exchange Commission.

USE OF ESTIMATES: The preparation of consolidated financial statements in conformity with generally accepted accounting principles 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 date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

CASH AND CASH EQUIVALENTS: Cash and cash equivalents include cash, money market investment accounts and short-term municipal bonds having maturities of 90 days or less when acquired. The Company maintains cash deposits at certain financial institutions in amounts in excess of the federally insured limit. Cash and cash equivalents held in interest-bearing accounts as of March 31, 2006 and December 31, 2005 were approximately $ 5,498,000 and $5,095,000, respectively.





NOTE 1: NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

INVENTORIES: Inventories are stated at the lower of cost (determined on a first-in, first-out basis) or market, and are as follows:

| | March 31, 2006 | December 31, 2005 |
|---|---|---|
| Raw materials | $ 1,612,291 | $ 1,692,277 |
| Packaging and components | 2,193,836 | 2,238,763 |
| Work in progress | 461,040 | 454,217 |
| Finished goods | 3,457,568 | 3,402,742 |
| | 7,724,735 | 7,787,999 |
| Less: Amount included in other assets | (1,613,605) | (1,639,732) |
| | $ 6,111,130 | $ 6,148,267 |

Raw materials include surfactants, chemicals and fragrances used in the production process. Packaging materials include cartons, inner sleeves and boxes used in the actual product, as well as outer boxes and cartons used for shipping purposes. Components are the actual bottles or containers (plastic or glass), jars, caps, pumps and similar materials that become part of the finished product. Finished goods also include hair dryers, electric clippers, lather machines, scissors and salon furniture.

Included in other assets is inventory not anticipated to be utilized within one year and is comprised primarily of packaging, components and finished goods. The Company reduces the carrying value of inventory to provide for these slow moving goods that includes the estimated costs of disposal of inventory that may ultimately become unusable or obsolete.

BASIC AND DILUTED EARNINGS PER SHARE: Basic and diluted earnings per share are computed by dividing net income by the weighted average number of shares of common stock outstanding. The weighted average number of shares outstanding was 4,391,747 for the three months ended March 31, 2006 and 4,418,630 for the three months ended March 31, 2005. For the three months ended March 31, 2006 and 2005, the Company had 391,116 and 341,822 outstanding stock options, respectively, a significant portion of which were anti-dilutive. The inclusion of dilutive stock options in the calculation of earnings per share did not have any impact on the earnings per share for the three months ended March 31, 2006 and 2005.





NOTE 1: NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

STOCK-BASED COMPENSATION: Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised), "Share-Based Payment" ("FAS 123R"), and chose to utilize the modified prospective transition method. Under this method, compensation costs recognized at March 31, 2006 relate to the estimated fair value at the grant date of 50,000 stock options granted subsequent to January 1, 2006 in accordance with FAS 123R. Prior to the adoption of FAS 123R the Company accounted for stock options in accordance with APB Opinion No. 25, "Accounting for Stock Issued to Employees," and recognized no compensation expense in net income for stock options granted and has elected the disclosure only provisions of FAS 123. In accordance with the provisions of FAS 123R, options granted prior to January 1, 2006, have not been restated to reflect the adoption of FAS 123R. The required services for awards prior to January 1, 2006 had been rendered prior to December 31, 2005.

As a result of adopting FAS 123R on January 1, 2006, the Company's net income for the period ended March 31, 2006 was lower because the Company recognized approximately $21,000 of compensation expense (included in Selling, General and Administrative Expenses) in the period for the stock options granted. The impact on basic and diluted earnings per share for the quarter ended March 31, 2006 was not material and the per share earnings remained at $.02. For the quarter ended March 31, 2005, no compensation expense was recorded for options granted in the period, as indicated above. The Company has used the Black-Scholes option pricing model to estimate the fair value of stock options using the following assumptions as at March 31, 2006:

| | |
|---|---|
| Life expectancy | 10 years |
| Risk-free interest rate | 4.4% |
| Expected volatility | 61.2% |
| Dividends per share | 2.3% |
| Weighted average fair value at grant date | $1.98 |

The above assumptions are based on a number of factors as follows: (i) expected volatility was determined using the historical volatility of the Company's stock price, (ii) the expected term of the options is based on the period of time that the options granted are expected to be outstanding, and (iii) the risk free rate is the U.S. Treasury rate effective at the time of grant for the duration of the options granted. Compensation cost is recognized on a straight-line basis over the vesting period.



THE STEPHAN CO. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
QUARTERS ENDED MARCH 31, 2006 AND 2005

NOTE 1: NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

NEW FINANCIAL ACCOUNTING STANDARDS: In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3", effective for accounting changes and corrections of errors made in fiscal year 2006 and beyond. The effect of this statement on the Company's consolidated financial statements will be determined based upon the nature and significance of future accounting changes or errors that would be subject to this statement.

In November 2004, the FASB issued SFAS No. 151, "Inventory Costs, an amendment of ARB No. 43, Chapter 4", effective for fiscal years beginning after June 15, 2005. SFAS No. 151 requires that the costs associated with certain abnormal expenditures be recognized in the current period. It also requires that the amount of fixed production overhead allocated to inventory be based upon normal capacity of production facilities. The effect this statement would have on the Company's consolidated financial statements is not expected to be material.

NOTE 2: SEGMENT INFORMATION

The Company has identified three reportable operating segments based upon how its management evaluates its business. These segments are Professional Hair Care Products and Distribution ("Professional"), Retail Personal Care Products ("Retail") and "Manufacturing". The Professional segment has a customer base consisting generally of distributors that purchase the Company's hair products and beauty and barber supplies for sale to salons and barbershops. The customer base for the Retail segment consists of mass merchandisers, chain drug stores and supermarkets that sell products to end-users. The Manufacturing segment manufactures products for different subsidiaries of the Company and manufactures private label brands for customers.

The Company conducts operations principally in the United States and sales to international customers are not material to its consolidated net sales. Income Before Income Taxes as shown below reflects an allocation of corporate overhead expenses (based upon sales) incurred by the Manu- facturing segment. The following tables, in thousands, summarize Net Sales and Income Before Income Taxes by reportable segment:

THE STEPHAN CO. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
QUARTERS ENDED MARCH 31, 2006 AND 2005

NOTE 2: SEGMENT INFORMATION (continued)

| | NET SALES | | INCOME BEFORE INCOME TAXES | |
|---|---|---|---|---|
| | Three Months Ended March 31, | | Three Months Ended March 31, | |
| | 2006 | 2005 | 2006 | 2005 |
| Professional | $ 4,252 | $ 4,255 | $ 345 | $ 316 |
| Retail | 1,009 | 1,127 | 47 | 34 |
| Manufacturing | 1,241 | 1,155 | (185) | (181) |
| Total | 6,502 | 6,537 | 207 | 169 |
| Intercompany Manufacturing | (906) | (1,020) | (43) | (44) |
| Consolidated | $ 5,596 | $ 5,517 | $ 164 | $ 125 |

NOTE 3: COMMITMENTS AND CONTINGENCIES

The Company is involved in litigation matters arising in the ordinary course of business. It is the opinion of management that none of these matters, at March 31, 2006, would likely, if adversely determined, have a material adverse effect on the Company's financial position, results of operations or cash flows. Additionally, there has been no material change in the status of any other pending litigation since the Company's last filing of Form 10-K with the Securities and Exchange Commission for the year ended December 31, 2005.



THE STEPHAN CO. AND SUBSIDIARIES
QUARTERLY REPORT PURSUANT TO SECTION 13
OF THE SECURITIES EXCHANGE ACT OF 1934
MARCH 31, 2006 AND 2005

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

For the three months ended March 31, 2006, net sales were $5,596,000 compared to $5,517,000 for the three months ended March 31, 2005, an increase of $79,000. Gross profit for the three months ended March 31, 2006 was $2,218,000, compared to gross profit of $2,359,000 achieved for the corresponding three-month period in 2005. The increase in net sales was due to an increase in amenity sales as well as the inclusion of sales from American Manicure and Lee Stafford, two of the Company's newest subsidiaries, offsetting declines in net sales of both the Retail and Professional segments. Gross profit declined as a result of a continuing change in the sales mix and increased costs associated with the increase in the cost of petroleum-based products. The gross margin for the three months ended March 31, 2006 was 39.6% as compared to 42.8% for the three months ended March 31, 2005.

Net income was $97,000 for the three months ended March 31, 2006 compared to net income of $74,000 for the comparable three months ended March 31, 2005. Basic and diluted earnings per share were $.02 for both the three months ended March 31, 2006 and 2005.

Selling, general and administrative ("SG&A") expenses for the three months ended March 31, 2006 decreased $165,000 when compared to the corresponding three-month period of 2005. The Company experienced savings in rent expense as some consolidation of warehouse space took place in the latter part of 2005 and also effected decreases in payroll expenditures and professional expenses.

Interest expense for the three months ended March 31, 2006 increased slightly when compared to the corresponding three-month period in 2005 as a result of increased interest accruals on the Trevor Sorbie debt resulting from the adverse arbitration decision in 2004. Interest income for the three months ended March 31, 2006 increased approximately $16,000 when compared to the corresponding three-month period in 2005, as a result of having more cash on hand for investment purposes and an overall increase in the interest rates on invested funds.

LIQUIDITY & CAPITAL RESOURCES

Cash and cash equivalents increased $332,000 to $5,935,000 as of March 31, 2006 from $5,603,000 as of December 31, 2005. Total cash of $9,085,000 includes $3,150,000 of cash invested in a restricted money market account pledged as collateral for a bank loan. The Company has continued to secure its outstanding long-term debt with Wachovia Bank with restricted cash. In





ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

the first quarter of 2006, the Company and Wachovia Bank have agreed, in principle, to convert the balloon payment due in August 2006 to monthly principal payments under the same terms and conditions as the original obligation, through 2008. Total current assets at March 31, 2006 were $17,248,000 compared to $16,853,000 at December 31, 2005. Working capital increased $113,000 from December 31, 2005, and was approximately $11,726,000 at March 31, 2006.

The Company is currently engaged in the construction of additional warehouse facilities on the Tampa, Florida manufacturing property, estimated to cost approximately $1,000,000. The Company has reviewed construction designs and site plans, and has initiated procedures for obtaining the necessary permits. Other than the above, the Company does not anticipate any significant capital expenditures in the near term and management believes that there is sufficient cash on hand, working capital and borrowing capacity to satisfy upcoming requirements.

The Company does not have any off-balance sheet financing or similar arrangements.

NEW FINANCIAL ACCOUNTING STANDARDS

See Note 1 to the Financial Statements included in Part I, Item 1 for a discussion of new financial accounting standards.

DISCUSSION OF CRITICAL ACCOUNTING POLICIES

The preparation of consolidated financial statements in conformity with generally accepted accounting principles 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 date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results would differ significantly from those estimates if different assumptions were used or unexpected events transpire. Please see Item 7 in the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed with the Securities and Exchange Commission.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

The Company does not participate in derivative or other financial instruments for which fair value disclosure would be required under SFAS No. 107. In addition, the Company does not invest in securities that would require disclosure of market risk, nor does it have floating rate loans or foreign currency exchange rate risks.





ITEM 4. CONTROLS AND PROCEDURES

(a) EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES: As of the end of the period covered by this quarterly report, an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures was performed under the supervision and with the participation of our management, including our principal executive officer and principal financial officer. Based upon that evaluation, our Chief

Executive Officer and Chief Financial Officer concluded that a material weakness existed in our internal controls over financial reporting and consequently our disclosure controls and procedures were not effective, as of the end of the period covered by this quarterly report, in timely alerting them as to material information relating to our Company (including our consolidated subsidiaries) required to be included in this quarterly report.

The material weakness in our internal controls over financial reporting as of March 31, 2006 related to the fact that as a small public company, we have an insufficient number of personnel with clearly delineated and fully documented responsibilities and with the appropriate level of accounting expertise and we have insufficient documented procedures to identify and prepare a conclusion on matters involving material accounting issues and to independently review conclusions as to the application of generally accepted accounting principles. The lack of a sufficient number of accounting personnel is not considered appropriate for an internal control structure designed for external reporting purposes. The principal factors management considered in determining whether a material weakness existed in this regard was based upon management's evaluation discussed above and advice from our independent registered public accounting firm. As a result, management has determined that a material weakness in the effectiveness of the Company's internal controls over financial reporting existed as of March 31, 2006.

(b) CHANGES IN INTERNAL CONTROLS: No change in the Company's internal control over financial reporting occurred during the Company's first fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting. However, management of the Company, as well as the Audit Committee, recognizes that current staffing levels will have to be enhanced and/or institute arrangements with other accounting firms to act in a consulting capacity in an effort to satisfy our reporting obligations and over-all standards of disclosure controls and procedures.

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THE STEPHAN CO. AND SUBSIDIARIES
QUARTERLY REPORT PURSUANT TO SECTION 13
OF THE SECURITIES EXCHANGE ACT OF 1934
MARCH 31, 2006 AND 2005

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

See Note 3 to the Financial Statements included in Part I, Item 1 for a discussion of legal proceedings. There has been no significant change in the status of litigation since the issuance of the Annual Report on Form 10-K for the year ended December 31, 2005.

ITEM 5. OTHER INFORMATION

On May 25, 2006, the Company received a notification letter from the American Stock Exchange ("AMEX") that the failure to file its Quarterly Report on Form 10-Q for the quarter ended March 31, 2006 ("10-Q"), as required by Sections 134 and 1101 of the AMEX Company Guide, is a material violation of its continued listing agreement with AMEX. Pursuant to Section 1003(d) of the AMEX Company Guide, the Company is subject to suspension of trading and possibly, delisting.

In order to maintain its listing, the Company is required to submit a plan by June 8, 2006, advising the AMEX how the Company intended to bring the Company into compliance with the above-mentioned Sections 134 and 1101 by July 6, 2006.

The Company believes that the filing of this Form 10-Q satisfies the continued listing deficiency referenced in the above mentioned letter of May 25, 2006 and precludes the need to submit a plan to the AMEX.

ITEM 6. EXHIBITS

31.1 Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer.

31.2 Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer.

32.1 Certification by the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification by the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.



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.

THE STEPHAN CO.

/s/ Frank F. Ferola

Frank F. Ferola
President and Chief Executive Officer
May 26, 2006

/s/ David A. Spiegel

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David A. Spiegel
Principal Financial and
Accounting Officer
May 26, 2006



Exhibit 31.1

CERTIFICATION

I, Frank F. Ferola, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of The Stephan Co.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and we have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

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CERTIFICATION OF CHIEF EXECUTIVE OFFICER (continued)

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 26, 2006

/s/ Frank F. Ferola

Frank F. Ferola
Chief Executive Officer

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Exhibit 31.2

CERTIFICATION

I, David A. Spiegel, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of The Stephan Co.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and we have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

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CERTIFICATION OF CHIEF FINANCIAL OFFICER (continued)

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 26, 2006

/s/ David A. Spiegel

David A. Spiegel
Chief Financial Officer

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CERTIFICATION OF CHIEF EXECUTIVE OFFICER

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of The Stephan Co. (the "Company) on Form 10-Q for the period ended March 31, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Frank F. Ferola, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Frank F. Ferola

Frank F. Ferola
Chief Executive Officer
May 26, 2006

CERTIFICATION OF CHIEF FINANCIAL OFFICER

Exhibit 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of The Stephan Co. (the "Company) on Form 10-Q for the period ended March 31, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, David Spiegel, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ David A. Spiegel

David A. Spiegel
Chief Financial Officer
May 26, 2006