

ARISTOTLE CORP  
Form 10-Q  
August 13, 2007

AS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ON AUGUST 13, 2007

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**Form 10-Q**

(MARK ONE)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE**

**ACT OF 1934**

**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE**

**ACT OF 1934**

**FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_**

*COMMISSION FILE NUMBER 0-14669*

**THE ARISTOTLE CORPORATION**

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

**DELAWARE**

(STATE OR OTHER JURISDICTION OF  
INCORPORATION OR ORGANIZATION)

**06-1165854**

(I.R.S. EMPLOYER  
IDENTIFICATION NO.)

**96 CUMMINGS POINT ROAD, STAMFORD, CONNECTICUT**

(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)

**06902**

(ZIP CODE)

**(203) 358-8000**

(REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE)

Indicate by check mark whether 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  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. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark whether registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [X]

As of August 10, 2007, 17,929,516 shares of Common Stock, 1,089,183 shares of Series I Preferred Stock and 10,984,971 shares of Series J Preferred Stock were outstanding.

**THE ARISTOTLE CORPORATION**

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QUARTERLY PERIOD ENDED JUNE 30, 2007**

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## PART I

## ITEM 1. FINANCIAL STATEMENTS

## THE ARISTOTLE CORPORATION AND SUBSIDIARIES

## CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

Assets	June 30, 2007 (unaudited)	December 31, 2006	June 30, 2006 (unaudited)
Current assets:			
Cash and cash equivalents	\$ 7,423	5,814	3,671
Marketable securities	1,910	-	-
Investments	15,423	14,586	13,669
Accounts receivable, net	21,934	15,458	20,898
Inventories, net	45,618	37,487	42,108
Prepaid expenses and other	5,080	8,123	4,896
Deferred income taxes	2,680	4,051	7,088
Total current assets	100,068	85,519	92,330
Property, plant and equipment, net	26,839	25,426	23,215
Goodwill	14,185	13,860	14,033
Deferred income taxes	8,188	8,188	2,712
Other assets	332	328	351
Total assets	\$ 149,612	133,321	132,641

**Liabilities and Stockholders Equity**

Current liabilities:				
Current installments of long-term debt	\$	294	287	599
Trade accounts payable		12,040	9,440	12,362
Accrued expenses		6,743	6,729	5,312
Income taxes		922	1,478	386
Accrued dividends payable		2,157	2,159	2,159
Total current liabilities		22,156	20,093	20,818
Long-term debt, less current installments		15,317	11,985	24,322
Long term pension obligations		4,303	4,469	1,306
Other long-term accruals		2,410	2,383	-
Stockholders equity:				
Preferred stock, Series I, convertible, voting, 11% cumulative, \$6.00 stated value; \$.01 par value; 2,400,000 shares authorized, 1,091,565, 1,100,122 and 1,100,122 shares issued and outstanding at June 30, 2007, December 31, 2006 and June 30, 2006, respectively		6,549	6,601	6,601
Preferred stock, Series J, non-voting, 12% cumulative, \$6.00 stated value; \$.01 par value; 11,200,000 shares authorized, 10,984,971 shares issued and outstanding		65,760	65,760	65,760
Common stock, \$.01 par value; 20,000,000 shares authorized, 17,903,346, 17,248,284 and 17,269,846 shares issued and outstanding at June 30, 2007, December 31, 2006 and June 30, 2006, respectively		179	172	173
Additional paid-in capital		6,606	3,106	3,299
Retained earnings		26,360	20,057	10,034
Accumulated other comprehensive earnings (loss)		(28)	(1,305)	328
Total stockholders equity		105,426	94,391	86,195
Total liabilities and stockholders equity	\$	149,612	133,321	132,641

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





**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS**

**(in thousands, except share and per share data)**

**(Unaudited)**

		<b>Three Months Ended</b>		<b>Six Months Ended</b>	
		<b>June 30,</b>		<b>June 30,</b>	
		<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net sales	\$	56,202	53,481	104,426	99,645
Cost of sales		34,631	33,086	63,892	61,651
Gross profit		21,571	20,395	40,534	37,994
Selling and administrative expense		11,917	11,359	23,544	22,441
Earnings from operations		9,654	9,036	16,990	15,553
Other (expense) income:					
Interest expense		(363)	(501)	(689)	(948)
Other, net		412	425	763	830
		49	(76)	74	(118)
Earnings before income taxes		9,703	8,960	17,064	15,435
Income taxes:					
Current		2,383	1,033	3,906	1,755
Deferred		1,220	2,427	2,539	4,219
		3,603	3,460	6,445	5,974
Net earnings		6,100	5,500	10,619	9,461
Preferred dividends		2,157	2,159	4,316	4,318
	\$	3,943	3,341	6,303	5,143

Net earnings applicable to  
common stockholders

Earnings per common share:

Basic	\$	.23	.19	.36	.30
Diluted	\$	.23	.19	.36	.29

Weighted average common shares outstanding:

Basic	17,454,704	17,266,513	17,361,153	17,257,955
Diluted	17,487,936	17,516,190	17,392,101	17,503,199

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

**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

**(in thousands)**

**(Unaudited)**

	<b>Six Months Ended</b>	
	<b>June 30,</b>	
	<b>2007</b>	<b>2006</b>
Cash flows from operating activities:		
Net earnings	\$ 10,619	9,461
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	921	895
Stock option compensation	48	73
Loss on sale of property, plant and equipment	3	-
Earnings in equity method investment	(837)	(813)
Excess tax benefits from stock-based compensation	(1,257)	(24)
Deferred income taxes	2,557	4,219
Change in assets and liabilities:		
Accounts receivable	(6,476)	(6,368)
Inventories	(8,131)	(6,529)
Prepaid expenses and other	3,043	3,130
Other assets	(339)	(187)
Trade accounts payable	2,600	3,349
Accrued expenses and other liabilities	271	471
Net cash provided by operating activities	3,022	7,677
Cash flows from investing activities:		
Purchases of property, plant and equipment	(1,964)	(1,564)
Proceeds from the sale of plant, property and equipment	6	-

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Purchases of marketable securities	(1,910)	-
Net cash used in investing activities	(3,868)	(1,564)
Cash flows from financing activities:		
Proceeds from issuance of long-term debt	7,000	6,933
Principal payments on long-term debt	(3,661)	(6,968)
Proceeds from issuance of stock under stock option plans	3,407	108
Changes in other long-term accruals	27	-
Preferred dividends paid	(4,318)	(4,318)
Net cash used in financing activities	2,455	(4,245)
Net increase in cash and cash equivalents	1,609	1,868
Cash and cash equivalents at beginning of period	5,814	1,803
Cash and cash equivalents at end of period	\$ 7,423	3,671
Supplemental cash flow information		
Interest	\$ 495	921
Income taxes	\$ 4,462	1,559

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

**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2007**

(Unaudited)

1.

Organization

The Aristotle Corporation ( Aristotle ) and its subsidiaries (together with Aristotle, the Company ), founded in 1986, and headquartered in Stamford, CT, is a leading manufacturer and global distributor of educational, health, medical technology and agricultural products. A selection of over 80,000 items is offered, primarily through more than 45 separate catalogs carrying the brand of Nasco (founded in 1941), as well as those bearing the brands of Life/Form®, Whirl-Pak®, Simulaids, Triarco, Spectrum Educational Supplies, Hubbard Scientific, Scott Resources, Haan Crafts, To-Sew, CPR Prompt®, Ginsberg Scientific and Summit Learning. Products include educational materials and supplies for substantially all K-12 curricula, molded plastics, biological materials and items for the agricultural, senior care and food industries. In addition, the Company offers medical simulators and manikins used for training in cardiopulmonary resuscitation and the fire and emergency rescue and patient care fields. The Company also markets proprietary product lines that provide exclusive distribution rights throughout all of its catalogs. The proprietary product lines are developed internally through the Company s research and development efforts and acquired externally by licensing rights from third parties.

Geneve Corporation ( Geneve ), a privately-held diversified financial holding company, and an affiliated entity held approximately 90% of Aristotle s voting power at June 30, 2007 and 2006.

2.

Financial Statement Presentation

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles ( GAAP ) for interim financial information and the instructions to Form

10-Q and Rule 10-01 of Regulation S-X. Accordingly, the Condensed Consolidated Financial Statements do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of financial position as of June 30, 2007 and 2006, results of operations for the three and six months ended June 30, 2007 and 2006 and cash flows for the six months ended June 30, 2007 and 2006, as applicable, have been made. Operating results for the three and six months ended June 30, 2007 are not necessarily indicative of results that may be expected for any other interim period or for the year ending December 31, 2007. For further information, refer to the consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2006.

3.

#### Principles of Consolidation

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

4.

#### Recently Issued Accounting Pronouncements

In February 2007, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, Including an amendment of FASB Statement No. 115* ( SFAS No. 159 ), which allows an entity to elect, at specified election dates, to measure eligible financial instruments at fair value. An entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date, and recognize upfront costs and fees related to those items in earnings as incurred and not deferred. SFAS No. 159 applies to fiscal years beginning after November 15, 2007, with early adoption permitted for an entity that has elected to apply the provisions of SFAS No. 157, *Fair Value Measurements*. An entity is prohibited from retrospectively applying SFAS No. 159, unless it chooses early adoption. The Company does not expect the adoption of SFAS No. 159 to have a material impact on the Company's financial position or results of operations, when adopted.

**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2007**

(Unaudited)

In June 2006, the FASB ratified EITF Issue No. 06-3, *How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation)* ( Issue No. 06-3 ). The scope of this consensus includes any taxes assessed by a governmental authority that are directly imposed on a revenue producing transaction between a seller and a customer and may include, but are not limited to, sales, use, value-added, and some excise taxes. Per the consensus, the presentation of these taxes on either a gross (included in revenues and costs) or a net (exclude from revenues and costs) basis is an accounting policy decision that should be disclosed. The Company reports revenues net of sales taxes in the results of operations for the current period as well as prior interim and annual reporting periods. Issue No. 06-3 is effective for interim and annual reporting periods beginning after December 15, 2006. Adoption of Issue No. 06-3 did not have any impact on the Company's financial statements at June 30, 2007, and for the three and six months then ended.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* ( SFAS 157 ). This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value. SFAS 157 expands the disclosures about the use of fair value to measure assets and liabilities in interim and annual periods subsequent to initial recognition. The disclosures focus on the inputs used to measure fair value, the recurring fair value measurements using significant unobservable inputs and the effect of the measurement on earnings (or changes in net assets) for the period. SFAS 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently reviewing the requirements of SFAS 157 and, at this point, has not determined what impact, if any, SFAS 157 will have on the Company's financial position or results of operations, when adopted.

In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109* ( Interpretation No. 48 ), which prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Interpretation No. 48 is effective for fiscal years beginning after December 15, 2006. The Company adopted the provisions of Interpretation No. 48 on January 1, 2007. The Company does not have any uncertain income tax positions or unrecognized tax benefits at the date of adoption and, as such, the adoption did not have any impact on the Company's financial position or results of operations. The Company and its qualifying domestic subsidiaries are included in the Federal income tax return and certain state income tax returns of Geneve. The provision for income taxes for the Company is determined on a separate return basis in accordance with a tax sharing agreement with Geneve and payments for Federal and certain state income taxes are made to Geneve. The Internal Revenue Service is

currently auditing Geneva's consolidated 2004 and 2005 Federal income tax returns, which include the Company. The Company anticipates that this examination will be completed within the next twelve months.

The Company believes that it has made adequate provision for all income tax positions, such that the outcome of any issues or claims will not result in a material change in the Company's financial position or results of operations.



**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2007**

**(Unaudited)**

5.

Marketable Securities

The Company invests in marketable equity securities, which the Company classifies as available-for-sale. The marketable securities are included in current assets, and are reported at fair value based on quoted market prices as of the reporting date. All unrealized gains or losses are reflected net of tax in accumulated other comprehensive income within Stockholders' Equity.

The carrying value of the marketable equity securities at June 30, 2007 was \$1.9 million. Net unrealized loss, net of tax, included in accumulated other comprehensive income was \$5.0 thousand at June 30, 2007.

6.

Earnings per Common Share

Basic earnings per common share is calculated by dividing net earnings applicable to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per common share is calculated by dividing net earnings applicable to common stockholders by the weighted average number of common shares outstanding during the period and including each share that would have been outstanding assuming the issuance of common shares for all dilutive potential common shares outstanding during the period.

Shares of Common Stock available for issue upon conversion of the 1,091,565 and 1,100,122 shares of Series I Preferred Stock outstanding at June 30, 2007 and 2006, respectively, were not dilutive and, therefore, have not been included in the computations of diluted earnings per common share amounts for the periods then ended.

7.

Investments

The Company has invested in a limited partnership, the general partner of which is an affiliate of the Company. The assets of this limited partnership are managed exclusively by a non-affiliate of the Company. The purpose of the limited partnership is to manage a diversified investment portfolio. No additional amounts were invested during the six months ended June 30, 2007 and 2006. The Company's investment is accounted for under the equity method of accounting, which equates the carrying value of the investment to the Company's equity in the partnership's underlying book value. Assets in the partnership are carried at fair value. The Company's equity earnings or loss is credited or charged, as appropriate, to other income within the Condensed Consolidated Statements of Earnings. For the three months ended June 30, 2007 and 2006, equity earnings amounted to \$.5 million and \$.4 million, respectively. For each of the six months ended June 30, 2007 and 2006, equity earnings amounted to \$.8 million.

8.

Inventories

The classification of inventories is as follows (in thousands):

		<b>June 30, 2007</b>	<b>December 31, 2006</b>	<b>June 30, 2006</b>
Raw materials	\$	7,320	6,281	5,852
Work in process		1,758	1,552	1,427
Finished goods		37,898	30,935	36,226
Less inventory reserves		(1,358)	(1,281)	(1,397)
Net inventories	\$	45,618	37,487	42,108

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**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2007**

(Unaudited)

9.

Stockholders' Equity and Comprehensive Earnings

Changes in stockholders' equity for the six months ended June 30 are as follows (in thousands):

	<b>2007</b>	<b>2006</b>
Balance at January 1	\$ 94,391	80,446
Net earnings	10,619	9,461
Exercise of stock options, including related tax benefit of \$1,257 and \$24 for 2007 and 2006, respectively	3,407	108
Stock option compensation	48	73
Other comprehensive earnings:		
Amortization of pension prior service cost and unrecognized net actuarial loss	121	-
Unrealized loss on marketable securities	(5)	-
Foreign currency translation adjustment	1,161	425
Preferred dividends	(4,318)	(4,318)
Balance at June 30	\$ 105,426	86,195

Comprehensive earnings for the three and six months ended June 30 are as follows (in thousands):

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net earnings	\$ 6,100	5,500	10,619	9,461
Amortization of pension prior service cost and unrecognized net actuarial loss	121	-	121	-
Unrealized loss on marketable securities	(5)	-	(5)	-
Foreign currency translation adjustment	1,043	447	1,161	425
Comprehensive earnings	\$ 7,259	5,947	11,896	9,886

**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2007**

(Unaudited)

10.

Stock Options

The Company established the 1997 Employee and Director Stock Plan in 1997 ( "1997 Plan" ). The 1997 Plan provides for granting up to 150,000 options to employees and directors of the Company to purchase shares of Common Stock. The exercise term of the options and vesting requirements shall be for such period as the Board of Directors (or a committee thereof, appointed to administer the 1997 Plan, if any) designates. Following the merger with Nasco International, Inc. on June 17, 2002 (the "Merger" ), each option to purchase one share of the Company's Common Stock granted under the 1997 Plan became an option to purchase one share of Common Stock and one share of Series I Preferred Stock of the Company. The Company does not currently intend to grant any additional options under the 1997 Plan.

The Company established the 2002 Employee, Director and Consultant Stock Plan in 2002 ( "2002 Plan" ) under which employees, directors and consultants of the Company are eligible to receive nonincentive and incentive options and stock grants of up to 1,500,000 shares of Common Stock. Options granted under the 2002 Plan generally vest over a three year period and have an exercise term of no longer than five years from the issue date.

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model. The risk-free interest rate is based on United States Treasury yields in effect at the date of grant consistent with the estimated life of the options. The estimated life of options granted represents the period of time that the options are expected to be outstanding. The expected volatility is based on an analysis of historical prices of the Company's stock over a period of time consistent with the estimated life of the options.

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A summary of option activity during the six months ended June 30, 2007 is presented below (in thousands, except share and per share data):

	<b>Number of Options</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Term</b>	<b>Aggregate Intrinsic Value</b>
Outstanding at December 31, 2006	750,675	\$ 3.55		
Granted	-	-		
Expired	-	-		
Forfeited	-	-		
Exercised	(649,425)	3.31		
Outstanding at June 30, 2007	101,250	5.11	1.46	\$ 590
Exercisable at June 30, 2007	89,584	4.88	1.29	543

**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2007**

(Unaudited)

No options were granted during each of the three and six months ended June 30, 2007 and 2006. The intrinsic value of options exercised during each of the three months ended June 30, 2007 and 2006 totaled \$1.1 million and \$.1 million, respectively. The intrinsic value of options exercised during each of the six months ended June 30, 2007 and 2006 totaled \$1.2 million and \$.1 million, respectively. Cash received from option exercises for each of the three months ended June 30, 2007 and 2006 totaled \$2.0 million and less than \$.1 million, respectively. Cash received from option exercises for the six months ended June 30, 2007 and 2006 totaled \$2.1 million and \$.1 million, respectively.

A summary of the status of the Company's nonvested options at June 30, 2007, and changes during the six months then ended, is presented below:

	<b>Number of Options</b>	<b>Weighted Average Grant Date Fair Value</b>
Nonvested at December 31, 2006	21,334	\$ 4.55
Granted	-	-
Vested	(9,668)	4.53
Forfeited	-	-
Nonvested at June 30, 2007	11,666	4.58

At June 30, 2007, there was less than \$.1 million of total unrecognized compensation costs related to options. These costs are expected to be recognized within the Condensed Consolidated Statements of Earnings over a weighted average period of approximately six months. The total fair value of options vested during each of the three and six months ended June 30, 2007 was less than \$.1 million.

Stock option compensation recognized within the Condensed Consolidated Statements of Earnings amounted to less than \$.1 million for each of the three months ended June 30, 2007 and 2006. For each of the six months ended June 30, 2007 and 2006, stock option compensation amounted to less than \$.1 million.



**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2007**

(Unaudited)

11.

Defined Benefit Pension Plan

On December 31, 2005, the Company froze the benefits under its pension plan for all hourly employees and certain salaried employees.

The Company contributed \$.3 million to the pension plan for the three months ended June 30, 2007. No contributions were made to the pension plan for the three months ended June 30, 2006. The Company contributed \$.3 million and \$.2 million to the pension plan for the six months ended June 30, 2007 and 2006, respectively. The Company expects to contribute a total of approximately \$2.5 million to the pension plan in 2007.

The following table presents the components of net periodic benefit cost for the three and six months ended June 30 (in thousands):

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Service cost	\$ 76	87	153	175
Interest cost	201	224	402	447
Expected return on plan assets	(194)	(237)	(387)	(473)
Amortization of prior service cost	-	-	(1)	(1)

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Recognized net actuarial loss		101	104	201	208
Net periodic benefit cost	\$	184	178	368	356

12.

Segment Reporting

The Company's business activities are organized into two business segments, educational and commercial. The educational segment relates to instructional teaching aids and materials, which are distributed to educational institutions principally in North America, for kindergarten through grade 12 classes, and for nursing school and emergency medical instructors. Products in the educational segment are marketed primarily through catalogs. The growth potential of the educational segment is directly related to school enrollments and the strength of government funding of education. The commercial segment relates to agricultural products, sterile sampling containers and systems, materials for nursing home activities and novelty and gift products. Products in the commercial segment are marketed through catalogs nationwide and through a worldwide dealer network covering more than 60 countries. Market growth in the commercial segment is principally impacted by the general economic conditions of world agriculture, the increasing size of the aged population, as well as increasing global awareness of food and water quality standards. The Company evaluates the performance of these segments based on segment net sales and gross profit.

**THE ARISTOTLE CORPORATION AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2007**

(Unaudited)

The following table presents segment information for the three and six months ended June 30 (in thousands):

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net sales:				
Educational	\$ 47,696	45,151	87,543	83,128
Commercial	8,506	8,330	16,883	16,517
Net sales	\$ 56,202	53,481	104,426	99,645
Gross profit:				
Educational	\$ 19,491	18,249	36,089	33,477
Commercial	3,394	3,221	6,794	6,581
Other costs of sales	(1,314)	(1,075)	(2,349)	(2,064)
Gross profit	\$ 21,571	20,395	40,534	37,994

Other costs of sales primarily include freight costs incurred in the procurement of inventories and shipment of customer orders not allocable to a particular segment.

The following table presents segment identifiable asset information as of June 30, 2007, December 31, 2006 and June 30, 2006 (in thousands):

**June 30,                  December 31,                  June 30,**

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		<b>2007</b>	<b>2006</b>	<b>2006</b>
Identifiable assets:				
Educational	\$	72,424	66,102	67,701
Commercial		6,220	5,929	5,819
Other corporate assets		70,968	61,290	59,121
Identifiable assets	\$	149,612	133,321	132,641

Educational assets include \$14.2 million, \$13.9 million and \$14.0 million of goodwill at June 30, 2007, December 31, 2006 and June 30, 2006, respectively. Other corporate assets include cash, marketable securities, investments, certain accounts receivable, deferred tax assets and property, plant and equipment, all of which service both the educational and commercial segments.

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

### **GENERAL**

This discussion and analysis of financial condition and results of operations reviews the results of operations of the Company, on a consolidated basis, for the three and six months ended June 30, 2007, as compared to the three and six months ended June 30, 2006. This discussion and analysis of financial condition and results of operations has been derived from, and should be read in conjunction with, the unaudited Condensed Consolidated Financial Statements and Notes to Condensed Consolidated Financial Statements contained herein.

The Company is a leading manufacturer and global distributor of educational, health, medical technology and agricultural products, primarily offered through more than 45 separate catalogs.

The following is a summary of key events for the three and six months ended June 30, 2007:

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increase in net sales of 5.1% and 4.8% in the three and six months ended June 30, 2007, respectively, as compared to the same periods in 2006;

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increase in gross profit of 5.8% and 6.7% in the three and six months ended June 30, 2007, respectively, as compared to the same periods in 2006;

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increase in earnings before income taxes of 8.3% and 10.6% in the three and six months ended June 30, 2007, respectively, as compared to the same periods in 2006;

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increase in quarterly net earnings of 10.9%, resulting in a 21.1% increase in diluted earnings per common share to \$.23 in the second quarter of 2007, as compared to the same period in 2006; as a percentage of net sales, net earnings amounted to 10.9% in the second quarter of 2007, compared to 10.3% in the same period in 2006; increase in net earnings of 12.2%, resulting in a 24.1% increase in diluted earnings per common share to \$.36 in the six months ended June 30, 2007, as compared to the same period in 2006; as a percentage of net sales, net earnings amounted to 10.2% in the six months ended June 30, 2007, compared to 9.5% in the same period in 2006;

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EBITDA<sub>(1)</sub> increase of 6.7% to \$10.1 million in the second quarter of 2007, as compared to the same period in 2006; EBITDA increase of 8.9% to \$17.9 million in the six months ended June 30, 2007, as compared to the same period in 2006;

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investment in marketable securities of \$1.9 million in the second quarter of 2007, compared to no investment in marketable securities in the second quarter of 2006; and an increase in other investments of \$1.8 million at June 30, 2007, compared to other investments at June 30, 2006;

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semi-annual dividend payments on March 31, 2007 totaling \$4.3 million on the Company's Series I Preferred Stock and Series J Preferred Stock; and

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relocation of the Nasco plastics operations to a new 60,000 square foot manufacturing facility.

A key strength of the Company's business is its ability to generate cash consistently. The Board of Directors and management use cash generated as a measure of the Company's performance. The Company uses the cash generated from operations to strengthen the balance sheet, including making investments and reducing liabilities such as pension and debt obligations, paying dividends on its preferred stocks and completing prudent acquisition opportunities. The Company's management believes that examining the ability to generate cash provides investors with additional insight into the Company's performance.



The following table sets forth selected financial data (i) as a percentage of net sales for the three and six months ended June 30, 2007 and 2006 and (ii) the percentage change in those reported items from the comparable period in 2006:

	Three Months Ended June 30,			Six Months Ended June 30,		
	2007	2006	% Change	2007	2006	% Change
Net sales	100.0 %	100.0 %	5.1 %	100.0 %	100.0 %	4.8 %
Cost of sales	61.6	61.9	4.7	61.2	61.9	3.6
Gross profit	38.4	38.1	5.8	38.8	38.1	6.7
Selling and administrative expense	21.2	21.2	4.9	22.5	22.5	4.9
Earnings from operations	17.2	16.9	6.8	16.3	15.6	9.2
Other (expense) income:						
Interest expense	(.6)	(.9)	27.2	(.7)	(1.0)	27.3
Other, net	.7	.8	(6.8)	.6	.8	(15.4)
	.1	(.1)	***	.1	(.2)	***
Earnings before income taxes	17.3	16.8	8.3	16.4	15.4	10.6
Income taxes:						
Current	4.2	1.9	130.7	3.7	1.8	122.6
Deferred	2.2	4.5	(49.7)	2.4	4.2	(39.8)
	6.4	6.4	4.1	6.1	6.0	7.9
Net earnings	10.9 %	10.4 %	10.9	10.3 %	9.4 %	12.2

\*\*\*

Not meaningful

(1)

EBITDA, which is considered a non-GAAP financial measure, is defined as earnings before income taxes, interest expense, other income and expense, depreciation and amortization. A non-GAAP financial measure is a numerical



measure of a company's historical or future financial performance, financial position or cash flows that either excludes or includes amounts that are normally included or excluded in a comparable measure calculated and presented under GAAP. EBITDA is not presented as an alternative measure of operating results (such as earnings from operations or net earnings) or cash flow from operations, as determined in accordance with GAAP, but is presented because the Company's management believes it is a widely accepted indicator of the Company's current financial performance and ability to incur and service debt. EBITDA does not give effect to cash used for debt service requirements or capital expenditures and thus does not reflect funds available for dividends, reinvestment or other discretionary uses. In addition, EBITDA as presented herein may not be comparable to similarly titled measures reported by other companies. The following table provides a reconciliation of net earnings to EBITDA for the three and six months ended June 30 (in thousands):

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net earnings	\$ 6,100	5,500	10,619	9,461
Add:				
Income taxes	3,603	3,460	6,445	5,974
Interest expense	363	501	689	948
Other expense (income)	(412)	(425)	(763)	(830)
Depreciation and amortization	480	460	921	895
EBITDA	\$ 10,134	9,496	17,911	16,448

## **FLUCTUATIONS IN QUARTERLY RESULTS OF OPERATIONS**

The Company is subject to seasonal influences with peak levels occurring in the second and third quarters of the fiscal year primarily due to increased educational shipments coinciding with the start of new school years in the Fall. As a result, the Company typically recognizes approximately 65% of its annual net earnings in the second and third quarters of its fiscal year. Inventory levels increase in March through June in anticipation of the peak shipping season. The majority of shipments are made between June and August and the majority of cash receipts are collected from August through October.

Quarterly results may also be materially affected by the timing of acquisitions, the timing and magnitude of costs related to such acquisitions, variations in costs of products sold, the mix of products sold and general economic conditions. Results for any quarter are not indicative of the results for any subsequent fiscal quarter or for a full fiscal year.

## **RESULTS OF OPERATIONS - THREE MONTHS ENDED JUNE 30, 2007 AS COMPARED TO THREE MONTHS ENDED JUNE 30, 2006**

### Net Sales

Net sales for the second quarter of 2007 increased 5.1% to \$56.2 million from \$53.5 million for the comparable period in 2006. The growth in net sales for the second quarter of 2007 is attributable to organic growth in U.S. shipments to the Company's domestic and international markets, offset by a decrease in net sales in Canada of more than 6% as Canadian provincial funding for K-12 curricula has declined from 2006 funding levels.

Net sales in the educational segment, totaling \$47.7 million, increased 5.6% in the second quarter of 2007 from \$45.2 million in the comparable period in 2006. The commercial segment recorded net sales of \$8.5 million in the second quarter of 2007, increasing 2.1% from \$8.3 million in the second quarter of 2006. Sales growth in both the educational and commercial segments relates to organic growth in existing product lines, including the Company's proprietary products.

### Gross Profit

Gross profit for the second quarter of 2007 increased 5.8% to \$21.6 million from \$20.4 million for the comparable period in 2006. The increase in gross profit for the second quarter of 2007 is primarily attributable to (i) the 5.1% increase in net sales, and (ii) growth in net sales of higher-margin proprietary product lines. The gross profit margin increased to 38.4% in the second quarter of 2007 from 38.1% in the comparable period in 2006. The increase in consolidated gross margin is attributed to the sales strength of the Company's proprietary product lines, which have higher gross margins.

The educational segment gross profit for the second quarter of 2007 increased 6.8% to \$19.5 million from \$18.2 million for the comparable period in 2006. The educational segment gross profit margin increased to 40.9% in the second quarter of 2007 from 40.4% in the second quarter of 2006. The increase in the educational segment gross profit margin is attributed to sales growth of proprietary products, supported by new manufacturing facilities at Nasco and Simulaids where significant numbers of proprietary products are manufactured. The commercial segment gross profit for the second quarter of 2007 increased 5.4% to \$3.4 million from \$3.2 million for the comparable period in 2006. The commercial segment yielded a gross profit margin of 39.9% in the second quarter of 2007, as compared to 38.7% in the second quarter of 2006. The increase in the commercial segment gross profit margin is also attributed to strength in proprietary sales, particularly the Whirl-Pak product lines.

#### Selling and Administrative Expenses

Selling and administrative expenses for the second quarter of 2007 increased 4.9% to \$11.9 million from \$11.4 million in the comparable period in 2006. As a percent of net sales, selling and administrative expenses amounted to 21.2% for each of the second quarters of 2007 and 2006. Selling and administrative expenses include advertising and catalog costs, warehouse and shipping activities, customer service and general administrative functions. Selling and administrative expenses for the second quarter of 2007 were primarily impacted by: (i) an increase in salaries and wages of \$.6 million, or 8.7%, as a result of increases in annual employee compensation, employee performance incentives and the number of employees; and (ii) an increase in group health care costs by 9.6%, or \$.1 million.

The Company recorded less than \$.1 million in compensation expense for each of the second quarters of 2007 and 2006 related to grants of stock options to certain employees and directors.

The Company incurred expenses of \$.2 million to Geneve for certain administrative services for each of the second quarters of 2007 and 2006.

### Interest Expense

Interest expense for the second quarter of 2007 decreased to \$.4 million from \$.5 million for the second quarter of 2006. The decrease in interest expense is principally due to the decrease in the average balance outstanding on the primary line of credit to \$7.3 million during the second quarter of 2007, compared to \$22.8 million in the second quarter of 2006. Interest expense of \$.1 million in the second quarter of 2007 relates to other long-term accruals incurred in the fourth quarter of 2006 in connection with the transfer of ownership of certain assets.

The Company's credit agreements assessed interest at a weighted average rate of 7.1%, 6.9% and 6.8% at June 30, 2007, December 31, 2006 and June 30, 2006, respectively.

### Income Tax Provision

Aristotle and its qualifying domestic subsidiaries are included in the Federal income tax return and certain state income tax returns of Geneve. The provision for income taxes for the Company is determined on a separate return basis in accordance with the terms of a tax sharing agreement with Geneve, and payments for current Federal and certain state income taxes are made to Geneve.

The income tax provision for the second quarter of 2007 was \$3.6 million versus \$3.5 million for the comparable period in 2006. These tax provisions reflect effective tax rates of 37.1% and 38.6 % for the second quarters of 2007 and 2006, respectively. For each of the second quarters of 2007 and 2006, the difference between the Federal statutory income tax rate of 35% and the effective income tax rate results principally from state income taxes, net of the Federal benefit, and the differential between the Federal tax rate and the tax rates in the foreign jurisdictions in which the Company operates. Approximately \$2.4 million of cash from operations was retained in the Company primarily as a result of the utilization of Federal net operating tax loss carryforwards ( NOLs ) during the three months ended June 30, 2006. The Company no longer has NOLs to utilize; thus, the Company will utilize cash to pay its Federal income tax obligations in future quarters.

**RESULTS OF OPERATIONS - SIX MONTHS ENDED JUNE 30, 2007 AS COMPARED TO SIX MONTHS ENDED JUNE 30, 2006**

Net Sales

Net sales for the six months ended June 30, 2007 increased 4.8% to \$104.4 million from \$99.6 million for the comparable period in 2006. The growth in net sales for the six months ended June 30, 2007 is attributable to organic growth in U.S. shipments to the Company's domestic and international markets, offset by a decrease in net sales in Canada of more than 9% as Canadian provincial funding for K-12 curricula has declined from 2006 funding levels.

Net sales in the educational segment, totaling \$87.5 million, increased 5.3% in the six months ended June 30, 2007 from \$83.1 million in the comparable period in 2006. The commercial segment recorded net sales of \$16.9 million in the six months ended June 30, 2007, increasing 2.2% from \$16.8 million in the comparable period in 2006. Sales growth in both the educational and commercial segments relates to organic growth in existing product lines, including the Company's proprietary products.

Gross Profit

Gross profit for the six months ended June 30, 2007 increased 6.7% to \$40.5 million from \$38.0 million for the comparable period in 2006. The increase in gross profit for the six months ended June 30, 2007 is primarily attributable to the 4.8% increase in net sales. The gross profit margin increased to 38.8% in the six months ended June 30, 2007 from 38.1% in the comparable period in 2006. The increase in consolidated gross margin is attributed to the sales strength of the Company's proprietary product lines, which have higher gross margins.

The educational segment gross profit for the six months ended June 30, 2007 increased 7.8% to \$36.1 million from \$33.5 million for the comparable period in 2006. The educational segment gross profit margin increased to 41.2% in the six months ended June 30, 2007 from 40.3% in the six months ended June 30, 2006. The commercial segment gross profit for the six months ended June 30, 2007 increased 3.2% to \$6.8 million from \$6.6 million for the comparable period in 2006. The commercial segment gross profit margin increased to 40.2% in the six months ended June 30, 2007, as compared to 39.8% in the six months ended June 30, 2006. The increase in the commercial segment gross profit margin is primarily attributable to an increase in the sales mix of certain proprietary commercial products, which have higher gross margins.

### Selling and Administrative Expenses

Selling and administrative expenses for the six months ended June 30, 2007 increased 4.9% to \$23.5 million from \$22.4 million in the comparable period in 2006. As a percent of net sales, selling and administrative expenses amounted to 22.5% for each of the six months ended June 30, 2007 and 2006. Selling and administrative expenses include advertising and catalog costs, warehouse and shipping activities, customer service and general administrative functions. Selling and administrative expenses for the six months ended June 30, 2007 were primarily impacted by: (i) an increase in salaries and wages of \$.9 million, or 6.9%, as a result of increases in annual employee compensation, employee performance incentives and the number of employees; and (ii) an increase in group health care costs by 12.9%, or \$.3 million.

The Company recorded less than \$.1 million in compensation expense for each of the six months ended June 30, 2007 and 2006 related to grants of stock options to certain employees and directors.

The Company incurred expenses of \$.4 million to Geneve for certain administrative services for each of the six months ended June 30, 2007 and 2006.

### Interest Expense

Interest expense for the six months ended June 30, 2007 decreased to \$.7 million from \$.9 million for the comparable period in 2006. The decrease in interest expense is principally due to the decrease in the average balance outstanding on the primary line of credit to \$6.8 million during the six months ended June 30, 2007, compared to \$22.0 million in the six months ended June 30, 2006. Interest expense of \$.2 million in the six months ended June 30, 2007 relates to other long-term accruals incurred in the fourth quarter of 2006 in connection with the transfer of ownership of certain assets.

The Company's credit agreements assessed interest at a weighted average rate of 7.1%, 6.9% and 6.8% at June 30, 2007, December 31, 2006 and June 30, 2006, respectively.

### Income Tax Provision

Aristotle and its qualifying domestic subsidiaries are included in the Federal income tax return and certain state income tax returns of Geneve. The provision for income taxes for the Company is determined on a separate return basis in accordance with the terms of a tax sharing agreement with Geneve, and payments for current Federal and certain state income taxes are made to Geneve.

The income tax provision for the six months ended June 30, 2007 was \$6.4 million versus \$6.0 million for the comparable period in 2006. These tax provisions reflect effective tax rates of 37.8% and 38.7% for the six months ended June 30, 2006 and 2005, respectively. For the six months ended June 30, 2007, the difference between the Federal statutory income tax rate of 35% and the effective income tax rate results principally from state income taxes, net of the Federal tax benefit, certain manufacturing tax credits provided by Section 199 of the Internal Revenue Tax Code, and the differential between the Federal tax rate and the tax rates in the foreign jurisdictions in which the Company operates. For the six months ended June 30, 2006, the difference between the Federal statutory income tax rate of 35% and the effective income tax rate results principally from state income taxes, net of the Federal tax rate and the tax rates in the foreign jurisdictions in which the Company operates. Approximately \$1.3 million and \$4.2 million, respectively, of cash from operations was retained in the Company primarily as a result of the utilization of NOLs during the six months ended June 30, 2007 and 2006, respectively. In future quarters, the Company will no longer have its historical NOLs to utilize; thus, the Company will utilize cash to pay its Federal income tax obligations.

## LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2007, the Company had working capital of \$77.9 million, increasing from \$65.4 million at December 31, 2006. At June 30, 2006, the Company had working capital of \$71.5 million. Cash and cash equivalents increased \$1.6 million in the six months ended June 30, 2007, ending the period at \$7.4 million. The increase in the generation of cash and cash equivalents during the six months ended June 30, 2007 as compared to the same period in 2006 is primarily due to the following:

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The Company generated cash of \$3.0 million from operations during the six months ended June 30, 2007 compared to \$7.7 million for the comparable period of 2006. The decrease in cash generated from operations in the six months ended June 30, 2007 compared to the same period in 2006 was principally the result of a \$1.2 million increase in net earnings, offset by \$1.6 million more cash used to purchase inventory, \$.7 million more cash used in payment of trade accounts payable and other changes in working capital.

The changes in current assets and liabilities are typical for the first six months of the fiscal year as the Company is preparing for its peak business cycle, which occurs during the second and third quarters of the fiscal year. For more information on the seasonality of the Company's business, please refer to the Fluctuations in Quarterly Results of Operations section above.

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The Company used cash of \$3.9 million for investing activities in the six months ended June 30, 2007, compared to \$1.6 million for the comparable period in 2006. In the six months ended June 30, 2007, the Company used \$.8 million of cash to fund a portion of the construction of a 60,000 square foot facility for Nasco's plastics operations. In the six months ended June 30, 2006, the Company used \$.6 million of cash to fund a portion of the construction of an 80,000 square foot office and manufacturing facility for the Company's Simulaid operations. The Company began operations at Nasco's new plastics facility in the first quarter of 2007. At June 30, 2007, the Company had recorded aggregate construction costs of \$3.5 million. The final construction cost of the new facility will be approximately \$3.8 million. The Company is funding the construction costs through working capital.

Capital expenditures to replace and upgrade existing capital equipment and install new equipment and fixtures to provide additional operating efficiencies totaled \$1.2 million and \$.8 million in the six months ended June 30, 2007 and 2006, respectively.



During the six months ended June 30, 2007, the Company invested \$1.9 million in marketable securities (see Note 5 of the Notes to Condensed Consolidated Financial Statements included in Item 1 of this Form 10-Q). No such investment was made during the six months ended June 30, 2006.

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Financing activities provided cash of \$2.5 million in the six months ended June 30, 2007, and used cash of \$4.2 million for the comparable period in 2006. In the six months ended June 30, 2007, proceeds from borrowings under the Company's primary credit facility of \$3.5 million was due to seasonal working capital requirements, including the payment of Preferred Stock cash dividends on March 31, 2007. In the six months ended June 30, 2006, there were no material changes in the Company's outstanding debt.

Proceeds from the exercise of stock options totaled \$3.4 million in the six months ended June 30, 2007 compared to \$.1 million in the six months ended June 30, 2006.

The Company paid dividends of \$4.3 million in each of the six months ended June 30, 2007 and 2006 on its Series I Preferred Stock and Series J Preferred Stock.

On October 15, 2003, the Company entered into a five-year, non-amortizing, \$45.0 million Revolving Credit Facility. The Revolving Credit Facility provides the Company with seasonal working capital, letters of credit and funds for appropriate acquisitions of businesses similar in nature to the Company's current business segments. This debt carries a variable rate of interest that is based on Prime or LIBOR rates plus applicable margins. At June 30, 2007, the weighted average interest rate on this debt was 7.4%. The Revolving Credit Facility currently has a committed weighted average rate of interest (including applicable margins) of approximately 7.4%. Such rate commitments expire on various dates through August 22, 2007. Subsequent to this date, the rate commitments will be renewed at interest rates based on the then-current LIBOR rates. The Company's Revolving Credit Facility is collateralized by certain accounts receivable, inventories and property, plant and equipment, and shares of a certain subsidiary's outstanding capital stock and ownership interests of certain of the Company's limited liability subsidiaries. The Revolving Credit Facility contains various financial and operating covenants, including, among other things, requirements to maintain certain financial ratios and restrictions on additional indebtedness, common stock dividend payments, capital disposals and intercompany management fees. The Company was in compliance with all financial covenants as of June 30, 2007.

In 2007, capital expenditures to replace and upgrade existing equipment and install new equipment and fixtures to provide additional operating efficiencies are expected to approximate \$1.5 million.

Capital resources in the future are expected to be used for the development of catalogs and product lines, to acquire additional businesses and for other investing activities. The Company anticipates that there will be sufficient financial resources to meet projected working capital and other cash requirements for at least the next twelve months. Management of the Company believes it has sufficient capacity to maintain current operations and support a sustained level of future growth.

## **INFLATION**

Inflation has had and is expected to have only a minor effect on the Company's operating results and its sources of liquidity. Inflation, including as it related to the increased cost of fuel and plastic materials, did not significantly impact the Company's operating results and its sources of liquidity in each of the three and six months ended June 30, 2007 and 2006.

## **SIGNIFICANT ACCOUNTING POLICIES**

The preparation of the Condensed Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the Condensed Consolidated Financial Statements and notes thereto. Actual results could differ from those estimates. The Company believes the following accounting policies affect the more significant judgments and estimates used in the preparation of the Condensed Consolidated Financial Statements:

Prepaid Catalog Costs and Amortization - The Company accumulates all direct costs, less applicable vendor rebates, incurred in the development, production and circulation of catalogs on the Condensed Consolidated Balance Sheets until the related catalog is mailed, at which time such catalog costs are amortized into selling and administrative expense over the estimated sales realization cycle of one year, using the straight-line method.

Deferred Income Taxes - At June 30, 2007 the Condensed Consolidated Balance Sheet contains a net deferred tax asset of approximately \$10.9 million. The realizability of this asset is dependent upon the Company's generation of sufficient levels of future taxable income.

Goodwill - The Company evaluates goodwill for impairment at least annually, or more frequently if events or circumstances indicate that the assets may be impaired, by applying a fair value based test and, if impairment occurs, the amount of impaired goodwill is written off immediately. The Company evaluates goodwill for impairment based on the expected future cash flows or earnings projections. Goodwill is deemed impaired if the estimated discounted cash flows or earnings projections do not substantiate the carrying value. The estimation of such amounts requires significant management judgment with respect to revenue and expense growth rates, changes in working capital and selection of an appropriate discount rate, as applicable. The use of different assumptions would increase or decrease discounted future operating cash flows or earnings projections and could, therefore, change the impairment determination. The Company evaluated its goodwill at December 31, 2006, and determined that there was no impairment of goodwill.

Defined Benefit Plans - The Company accounts for the benefits under its defined benefit pension plan using actuarial models required by SFAS No. 87, *Employers Accounting for Pensions*. These models use an attribution approach that generally spreads individual events over the service lives of the employees in the plan. Examples of events are plan amendments and changes in actuarial assumptions such as discount rate, expected return on plan assets and rate of compensation increases. The principle underlying the required attribution approach is that employees render service over their service lives on a relatively consistent basis and, therefore, the statement of earnings effects of pension benefits are earned in, and should be expensed in, the same pattern.

In calculating net periodic benefit cost and the related benefit obligation, the Company is required to select certain actuarial assumptions. These assumptions include discount rate, expected return on plan assets and rate of compensation increase. The discount rate assumptions reflect the prevailing market rates for long-term, high-quality, fixed-income debt instruments that, if the obligation was settled at the measurement date, would provide the necessary future cash flows to pay the benefit obligation when due. The Company uses long-term historical actual return experience with consideration of the expected investment mix of the plan's assets, as well as future estimates of long-term investment returns, to develop its assumptions of the expected return on plan assets. The rate of compensation increase is based on historical experience and the Company's long-term plans for such increases.

Revenues - Customarily applying FOB-shipping point terms, the Company recognizes revenue upon shipment of products to its customers, which corresponds to the time when risk of ownership transfers. The point of shipment is typically from one of the Company's distribution centers or, on occasion, a vendor's location as a drop shipment. All drop shipment sales are recorded at gross selling price.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company's financial instruments include cash and cash equivalents, marketable securities, investments, accounts receivable, accounts payable, accrued liabilities and debt. As described below, credit risk, market risk and interest rate risk are the primary sources of risk in the Company's accounts receivable, marketable securities, investments and debt.

#### **QUALITATIVE**

**Credit Risk:** The Company provides credit in the normal course of business to its customers, which are primarily educational institutions or distributors. No single customer accounted for more than 10% of the Company's sales in each of the three and six months ended June 30, 2007 and 2006. The Company performs ongoing credit evaluations of its customers, maintains allowances for potential credit losses and generally does not require collateral to support its accounts receivable balances.

**Market Risk:** The Company's exposure to market risk relates to the quality of holdings of its marketable securities and limited partnership investment. The fair market values of these investments are subject to increases or decreases in value resulting from the performance of the securities issuers, from upgrades or downgrades in the credit worthiness of the securities issuers and from changes in general market conditions. The Company seeks to manage its exposure to market risk by investing in accordance with standards established by the Investment Committee of the Board of Directors. The standards of the Investment Committee are: (i) preservation of capital; (ii) provision of adequate liquidity to meet projected cash requirements; (iii) minimization of risk of principal loss through diversified short and medium term investments; and (iv) maximization of yields in relationship to the guidelines, risk, market conditions and tax considerations.

**Interest Rate Risk:** Changes in interest rates can potentially impact the Company's profitability and its ability to realize assets and satisfy liabilities. Interest rate risk is resident primarily in debt, which typically has variable interest rates based on Prime or LIBOR rates. Assuming no other change in financial structure, an increase of 1% in the Company's variable interest rate for debt would decrease pre-tax earnings for 2007 by approximately \$.2 million. This amount is determined by considering the impact of a 1% increase in interest rates on the average debt estimated to be

outstanding in 2007.

**QUANTITATIVE**

The Company's debt as of June 30, 2007 is as follows (in millions, except percentage data):

	<b>MATURITY LESS THAN ONE YEAR</b>	<b>MATURITY GREATER THAN ONE YEAR</b>
Amount	\$ .3	\$ 15.3
Weighted average interest rate	6.9%	7.3%
Fair market value	\$ .3	\$ 15.3

The fair market value of debt equals the face amount of debt outstanding because the underlying rate of interest on substantially all of the Company's debt is variable based upon Prime or LIBOR rates.



#### **ITEM 4. CONTROLS AND PROCEDURES**

The President and the Chief Financial Officer of the Company (its principal executive officer and principal financial officer, respectively) have concluded, based on their evaluation as of the end of the period covered by this Quarterly Report on Form 10-Q, that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports filed or submitted by it under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms, and include controls and procedures designed to ensure that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including the President and the Chief Financial Officer, as appropriate, and allow timely decisions regarding required disclosure.

There have not been any changes in the Company's internal control over financial reporting during the fiscal quarter ended June 30, 2007 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.







## **PART II**

### **ITEM 1. LEGAL PROCEEDINGS**

The Company is not a party to any material legal proceedings.

### **ITEM 1A. RISK FACTORS**

#### **FORWARD-LOOKING STATEMENTS**

The Company believes that this Quarterly Report on Form 10-Q may contain forward-looking statements within the meaning of the "safe-harbor" provisions of the Private Securities Litigation Reform Act of 1995. Forward looking statements include statements concerning plans, objectives, goals, strategies, future events or performance, expectations, predictions, and assumptions and other statements which are other than statements of historical facts.

These forward-looking statements are based on management's current expectations and are subject to, and are qualified by, risks and uncertainties that could cause actual results or business conditions to differ materially from those projected or suggested in such forward-looking statements.

The Company cautions investors that there can be no assurance that actual results or business conditions will not differ materially from those projected or suggested in such forward-looking statements as a result of various factors including, but not limited to, the following: (i) the ability of the Company to obtain financing and additional capital to fund its business strategy on acceptable terms, if at all; (ii) the ability of the Company on a timely basis to find, prudently negotiate and consummate additional acquisitions; (iii) the ability of the Company to manage any to-be acquired businesses; (iv) there is not an active trading market for the Company's securities and the stock prices thereof are highly volatile, due in part to the relatively small percentage of the Company's securities which is not held by the Company's majority stockholder and members of the Company's Board of Directors and/or management; (v) the ability of the Company to retain its Federal net operating tax loss carryforward position; and (vi) other factors identified below or in Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2006. As a result, the Company's future development efforts involve a high degree of risk. For further information, please see the Company's filings with the SEC, including its Forms 10-K, 10-K/A, 10-Q and 8-K.

There have been no material changes from the risk factors previously disclosed in Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2006.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

None

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

No matters were submitted to a vote of the Company's security holders during the second quarter of 2007.

**ITEM 5. OTHER INFORMATION**

None



**ITEM 6. EXHIBITS**

The following exhibits are filed as part of this report:

<b>EXHIBIT NUMBER</b>	<b>DESCRIPTION</b>
31.1	Rule 13a-14(a)/15d-14(a) Certifications.
31.2	Rule 13a-14(a)/15d-14(a) Certifications.
32.1	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification 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.

Date: August 13, 2007

/s/ Steven B. Lapin

Steven B. Lapin

President and Chief Operating Officer

(Principal Executive Officer)

Date: August 13, 2007

/s/ Dean T. Johnson

Dean T. Johnson

Vice President and Chief Financial Officer

(Principal Financial and Accounting Officer)







**EXHIBIT INDEX**

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