STEPHAN CO
Form 10QSB
November 19, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-QSB

[x] Quarterly Report Under Section 13 or 15(d) of The Securities Exchange Act of 1934

For the quarterly period ended: September 30, 2007

[ ] Transition Report Under Section 13 or 15(d) of the Exchange Act

For the transition period from _______ to ________

Commission File No. 1-4436

THE STEPHAN CO.
(Exact Name of Small Business Issuer 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

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

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 October 31, 2007:

4,389,781

Transitional Small Business Disclosure Format (Check One)   YES   NO X

The Stephan Co. and Subsidiaries
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The Stephan Co. and Subsidiaries
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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

	September 30, 2007	December 31, 2006

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Cash and cash equivalents	$ 7,431,477	$ 7,064,332
Restricted cash	1,110,000	1,110,000
Accounts receivable, net	1,841,363	1,716,733
Inventories	4,968,905	4,792,357
Prepaid expenses and other current assets	401,131	335,429
TOTAL CURRENT ASSETS	15,752,876	15,018,851
Restricted cash	370,000	1,206,392
Property, plant and equipment, net	1,487,403	1,573,560
Deferred income taxes	542,981	864,471
Goodwill, net	2,602,802	2,602,802
Trademarks, net	3,069,507	3,069,507
Deferred acquisition costs, net	76,161	76,161
Other assets, net	2,345,466	2,354,295
TOTAL ASSETS	$ 26,247,196	$ 26,766,039

Liabilities and Stockholders' Equity

	September 30, 2007	December 31, 2006
Current portion of long-term debt	$ 1,110,000	$ 1,110,000
Accounts payable and accrued expenses	2,134,754	2,215,449
TOTAL CURRENT LIABILITIES	3,244,754	3,325,449
Long-term debt	277,500	1,110,000
TOTAL LIABILITIES	3,522,254	4,435,449
Commitments and Contingencies		
Common stock, $.01 par value	43,898	43,898
Additional paid-in capital	17,714,581	17,646,069
Retained earnings	4,966,463	4,640,623

TOTAL STOCKHOLDERS' EQUITY	22,724,942	22,330,590
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 26,247,196	$ 26,766,039

See notes to unaudited condensed consolidated financial statements.

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The Stephan Co. and Subsidiaries
Unaudited Condensed Consolidated Statements of Operations

	Nine Months Ended September 30,	
	2007	2006
Revenue	$15,194,200	$17,091,655
Cost Of Goods Sold	8,490,661	9,910,822
Gross Profit	6,703,539	7,180,833
Selling, General And Administrative Expenses	5,983,440	6,309,038
Operating Profit	720,099	871,795
Other Income (Expense)		
Interest income	277,610	155,312
Interest expense on long-term debt	(19,739)	(32,641)
Income Before Income Taxes	977,970	994,466
Income Tax Expense	388,743	414,979
Net Income	$ 589,227	$ 579,487
Net Income Per Share:		
Basic	$ .13	$ .13
Diluted	$ .13	$ .13
Dividends Per Share:	$ .06	$ .06

	Three Months Ended September 30,	
	2007	2006
Revenue	$ 5,382,581	$ 6,109,738

Cost Of Goods Sold	2,959,631	3,525,412
Gross Profit	2,422,950	2,584,326
Selling, General And Administrative Expenses	1,846,405	1,977,771
Operating Profit	576,545	606,555
Other Income (Expense)		
Interest income	91,939	48,919
Interest expense on long-term debt	(5,555)	(9,854)
Income Before Income Taxes	662,929	645,620
Income Tax Expense	259,569	279,368
Net Income	$ 403,360	$ 366,252
Net Income Per Share:		
Basic	$ .09	$ .08
Diluted	$ .09	$ .08
Dividends Per Share:	$ .04	$ .02

See notes to unaudited condensed consolidated financial statements.

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The Stephan Co. and Subsidiaries
Unaudited Condensed Consolidated Statements of Cash Flows

	Nine Months Ended September 30,	
	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 589,227	$ 579,487
Adjustments to reconcile net income to net cash flows provided by operating activities:		
Depreciation	102,156	108,931
Stock-based compensation	68,596	67,004
Amortization	-	49,518
Deferred income taxes	321,490	313,566
Changes in operating assets and liabilities:		
Accounts receivable	(124,630)	(861,025)
Inventories	(176,548)	51,560

Prepaid expenses and other current assets	(65,700)	(11,560)
Change in other assets	8,829	350,142
Accounts payable and accrued expenses	(80,695)	186,810
Net cash flows provided by operating activities	642,725	834,433
CASH FLOWS FROM INVESTING ACTIVITIES:		
Reduction in restricted cash	836,392	835,983
Purchase of property, plant and equipment	(15,999)	(38,223)
Net cash flows provided by investing activities	820,393	797,760
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayments of long-term debt	(832,500)	(740,000)
Dividends paid	(263,389)	(263,389)
Purchase & retirement of common stock	(84)	--
Net cash flows used in financing activities	(1,095,973)	(1,003,389)
INCREASE IN CASH AND CASH EQUIVALENTS	367,145	628,804
Cash And Cash Equivalents, Beginning Of Period	7,064,332	5,602,762
Cash And Cash Equivalents, End Of Period	$ 7,431,477	$ 6,231,566
Supplemental Disclosures of Cash Flow Information:		
Interest paid	$ 19,975	$ 32,641
Income taxes paid	$ 82,128	$ 35,178

See notes to unaudited condensed consolidated financial statements.

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The Stephan Co. and Subsidiaries
Notes To Unaudited Condensed Consolidated Financial Statements
Quarters Ended September 30, 2007 and 2006

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

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

BASIS OF PRESENTATION: In our opinion, 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 condensed consolidated financial statements. Certain reclassifications of prior year amounts have been made to effect comparability with current year classifications.

The results of operations for the nine- and three-month periods ended September 30, 2007 are not necessarily indicative of the results to be achieved for the year ending December 31, 2007. The December 31, 2006 condensed consolidated balance sheet was derived from the audited consolidated financial statements, but does not include all disclosures required by generally accepted accounting principles in the United States of America. These interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes in our Annual Report on Form 10-K for the year ended December 31, 2006, 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 us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the dates of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

CASH AND CASH EQUIVALENTS: Cash and cash equivalents include cash, CDs, money market investments and floating rate notes with maturities of 90 days or fewer when acquired. The Company maintains cash deposits at certain financial institutions in amounts in excess of the federally insured limit.

REVENUE RECOGNITION: We recognize revenue upon shipment.

CLASSIFICATION OF CERTAIN COSTS AND EXPENSES: In Cost of Goods Sold, we include raw materials, packaging, labor and overhead related to manufacturing, shipping and warehousing our products.

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

	September 30, 2007	December 31, 2006
Raw materials	$ 1,217,681	$ 1,457,575
Packaging and components	2,023,654	2,138,017
Work-in-process	486,449	605,848
Finished goods	3,522,509	2,872,305
	7,250,293	7,073,745
Less: Amount included in other assets	(2,281,388)	(2,281,388)
	$ 4,968,905	$ 4,792,357

Raw materials include chemicals and fragrances used in the production process. Packaging and components include cartons, inner sleeves, boxes, bottles, containers, jars, caps, pumps and similar items. Finished goods are comprised of manufactured and purchased "wet" goods and purchased "hard" goods including hair dryers, electric clippers, lather machines, scissors and salon accessories.

Packaging, components and finished goods that are not anticipated to be used within one year are categorized as other assets. We reduce the value of inventory included in other assets by an allowance for inventory obsolescence to provide for the cost, including the estimated costs of disposal of slow moving goods that may ultimately become unusable or obsolete.

BASIC AND DILUTED NET INCOME PER SHARE: Basic net income per share was computed by dividing net income by the weighted average shares of common stock outstanding (4,389,801 shares). Diluted net income per share was computed by dividing net income by the weighted average shares of common stock outstanding increased by shares assumed to be outstanding after the exercise of certain stock options.

The inclusion of dilutive stock options in the calculation of diluted net income per share was not significant for the nine- or three-month periods ended September 30, 2007 and 2006. We have approximately 400,000 stock options outstanding, of which approximately 150,000 are "in the money" and therefore used in the calculation of diluted net income per share. The additional shares assumed to be outstanding using the treasury stock method are immaterial.

In late June 2007 we purchased 22 shares of common stock as an accommodation to a shareholder. The stock was later retired and the shares are no longer outstanding.

STOCK-BASED COMPENSATION: As a result of adopting FAS 123R on January 1, 2006, we incurred compensation expense related to stock options granted to the CEO and certain directors of $69,000 and $21,000, net of income tax benefits, or about $.02 and $.01, respectively. For the nine- and three-month periods ended September 30, 2006, our net income was reduced by approximately $67,000 and $42,000 for the nine- and three-month periods, or about $.02 and $.01, respectively.

NEW FINANCIAL ACCOUNTING STANDARDS: In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159"), which establishes a fair value option under which entities can elect to report certain financial assets and liabilities at fair value, with changes in fair value recognized in earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact, if any, that SFAS 159 will have on our financial statements.

In September 2006, the Securities and Exchange Commission staff published Staff Accounting Bulletin ("SAB") No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements." SAB No. 108 addresses the effect on current year financial statements of prior year uncorrected errors. SAB No. 108 was effective for fiscal years ended after November 15, 2006. The adoption of SAB No. 108 by us in the fourth quarter of 2006 did not have a material impact on our consolidated financial statements.

In July 2006 the FASB issued FASB Interpretation No. 48, ("FIN 48") "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement

No. 109". FIN 48 requires that we recognize in our financial statements the impact of a tax position taken or expected to be taken in a tax return, provided that such position is more likely than not of being sustained on audit. FIN 48 was effective for fiscal years beginning after December 15, 2006. We adopted FIN 48 effective January 1, 2007 and do not anticipate that it will have an adverse effect on our financial statements.

NOTE 2: COMMITMENTS AND CONTINGENCIES

We are involved in litigation matters arising in the ordinary course of business. It is our opinion that none of these matters, at September 30, 2007, would likely, if adversely determined, have a material adverse effect on our financial position, results of operations or cash flows. Additionally, there has been no material change in the status of any pending litigation since the filing of our most recent Annual Report on Form 10-K with the Securities and Exchange Commission for the year ended December 31, 2006.

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

Adjustments Related to Prior Interim Periods of the Current Year

We recently discovered, with the aid of our system of internal controls, that a manager at our Midwest subsidiary had caused overstated results to be included in our previously reported revenue, net income and net income per share to the extent of $504,000, $124,000, and $.02 per common share, respectively, for the six months ended June 30, 2007. Cash was unaffected. The actions of the former manager were unauthorized and unilateral and resulted in the aforementioned overstatement of revenue and earnings. We do not consider the actions of the former manager to be indicative of a material weakness in our system of internal controls, but we are reviewing our control systems at this subsidiary for any weaknesses or deficiencies. Any needed strengthening of our Internal Controls over Financial Reporting will be implemented before December 31, 2007.

We plan to amend our reports on Form 10-QSB for the first and second quarters of 2007 as follows:

Quarter Ended March 31, 2007	As Filed	As Restated
Revenue	$ 5,209,364	$ 4,946,952
Net income	103,546	57,005
Net income per share	$ .02	$ .01

Quarter Ended June 30, 2007	As Filed	As Restated
Revenue	$ 5,106,714	$ 4,864,668
Net income	163,750	128,751
Net income per share	$ .04	$ .03

Six Months Ended June 30, 2007	As Filed	As Restated
Revenue	$ 10,316,078	$ 9,811,620
Net income	267,296	185,756
Net income per share	$ .06	$ .04

The "As Restated" amounts above have been included in the year-to-date results in this report on Form 10-QSB for the third quarter of 2007.

Comparison of the Nine-Month Periods ended September 30, 2007 and September 30, 2006:

Our revenue was $15.2 million for the nine months ended September 30, 2007, a decrease of 11.1% from the comparable period in 2006, principally due to shortfalls in our two main product segments: professional and retail. Revenue in our professional segment, consisting principally of lower margin hard goods (clippers, scissors, manikins, lather machines, etc.) sold to distributors, accounted for approximately 76.0% of our total revenue for the nine-month period ended September 30, 2007, representing a decline of 12.4% from the comparable period in the prior year. Revenue in our retail segment, principally comprised of sales to chain stores and mass merchandisers, accounted for approximately 17.0% of our total revenue for this nine-month period and was 15.5% less than the revenue attributed to this product segment for the comparable 2006 period. Revenue for the remaining sales categories was greater than that in 2006 by 25.3%, due principally to higher cosmetic and amenity sales. It was not practicable to determine interim profit or loss by segment; we plan to report segment profitability in our Annual Report on Form 10-KSB for the year ending December 31, 2007.

Revenue by Segment
($ in thousands)

	Nine Months 2007	Nine Months 2006	% Increase (Decrease)
Professional	$ 11,535	$ 13,172	(12.4%)
Retail	2,594	3,070	(15.5%)
Manufacturing/Other	1,065	850	25.3%
Total	$ 15,194	$ 17,092	(11.1%)

While sales of certain of our brands, sold principally to retail chains and sales of amenities and cosmetics, outperformed results in the prior year, revenue in our largest category, professional hard goods, was below that in the nine-month period ended September 30, 2006. We believe that several factors contributed to this shortfall including: 1) a decrease in the number of distributors resulting from industry consolidation, 2) increased competitive pressures, 3) lower beauty school sales and 4) general economic conditions.

Our operating profit declined 17.4%, to $720,000, in the first three quarters of 2007 compared to the comparable period in 2006. Our gross profit percentage was higher, 44.1% compared to 42.0% in the first nine months of 2006, and our selling, general and administrative ("SG&A") expenses were lower, as described below, partially offsetting the effect of the revenue decline. The gross margin percentage improved due in part to 1) a shift in the mix of products sold as fewer lower margin hard goods were sold in the first three quarters of 2007 compared to those sold in the comparable period of 2006 and 2) our emphasis on controlling our inventory levels by utilizing raw materials and components more efficiently.

Lower SG&A expenses contributed to better operating profit as our payroll and freight costs, two of the principal components of our SG&A expenses, were $109,000 and $75,000, respectively, less in the nine-month period ended September 30, 2007 compared to the same period in 2006. SG&A expenses in the first three quarters of 2006 included legal costs of $78,000, classified in previous reports as a component of interest expense and lower amortization costs of $50,000; these costs were not incurred in 2007.

Income before income taxes decreased 1.8% as the decline in operating profit was offset by the impact of higher interest income. Net income was 1.7% better than that in the first three quarters of 2006.

Comparison of the Three-Month Periods ended September 30, 2007 and September 30, 2006:

Our revenue was $5.4 million for the three months ended September 30, 2007, a decrease of 11.9% from the comparable period in 2006 principally due to shortfalls in our two main segments: professional and retail. Revenue in our professional segment, consisting principally of lower margin hard goods, accounted for approximately 80.0% of our total revenue for the three-month period ended September 30, 2007, representing a decline of 14.4% from the comparable period in the prior year. Revenue in the retail segment, principally comprised of sales to chain stores and mass merchandisers, accounted for approximately 16.0% of our total revenue for this three-month period and was 13.3% less than revenue attributed to this product segment for the comparable 2006 period. Revenue for our remaining product segment increased in 2007 over that in 2006 due to higher cosmetic and amenity sales. It was not practicable to determine profit or loss by segment for the subject period.

Revenue by Segment
($ in thousands)

	Three Months 2007	Three Months 2006	% Increase (Decrease)
Professional	$ 4,296	$ 5,023	(14.4%)
Retail	836	964	(13.3%)
Manufacturing/Other	251	123	104.1%
Total	$ 5,383	$ 6,110	(11.9%)

(See above for a description of revenue shortfalls from the third quarter of 2006.)

Our operating profit decreased 4.9% in the third quarter of 2007 as lower SG&A expenses helped to offset the effect of the revenue decline. Our gross profit percentage was higher, 45.0% in the third quarter of 2007 compared to 42.2% in the comparable period of 2006. We incurred lower payroll, professional fees and freight costs, principal components of our SG&A expense, during this third quarter period compared to the comparable period last year. SG&A expenses in the third quarter of 2006 included legal costs of $52,000 classified in 2006 reports as a component of interest expense.

Income before income taxes for the three-month period ended September 30, 2007 increased 2.6% from that in the third quarter of 2006, primarily due to increased interest income that offset the effect of lower operating profit. Net income for the period improved by 10.1% from the comparable period in 2006.

LIQUIDITY & CAPITAL RESOURCES

For the nine months ended September 30, 2007, we generated cash flow from operating activities of $643,000. In the comparable period in 2006 we generated $834,000; the decline from 2006 to 2007 was the result of changes in non-cash working capital. Most of our revenue and cash flow comes from our Professional market segment. This segment markets non-manufactured barber and beauty supplies to distributors, barbershops, beauty schools and salons. We had $7.4 million cash and cash equivalents at September 30, 2007, up from $7.1 million at December 31, 2006. Over and above our $7.4 million we had cash of $1.7 million pledged as security for a bank loan of a like amount. Other than this bank loan, which has been fully funded by pledged ("restricted") cash, we have no long-term debt.

Our changes in cash are generally driven by our profitability, dividend payments and changes in non-cash working capital. Our long-term debt is fully funded by restricted cash; the restricted cash decreases as principal payments on the loan are paid. Cash and cash equivalents, approximately $7.4 million at September 30, 2007, was in excess of the amount due for principal payments under this loan.

During the nine-month period ended September 30, 2007, we generated cash flows from operations sufficient to fund our operating, capital and dividend requirements. We do not anticipate the need for additional long-term debt or capital contributions at this time. We do not have any off-balance sheet financing or similar arrangements. We currently have sufficient cash on hand combined with cash generated from our ongoing operations to satisfy our planned operating and recurring capital requirements.

We paid our third dividend of the year, $.02 per share of common stock, on September 28, 2007. We declared our second dividend of 2007 on July 10 in the amount of $.02 per share of common stock, and it was paid on July 31, 2007. We have paid dividends every year since mid-1995.

Our cash flow from operations has been growing in the past few years; in 2004, however, we paid a special dividend of $2.00 per share of common stock that decreased cash on hand by approximately $9.0 million.

NEW FINANCIAL ACCOUNTING STANDARDS

See Note 1 to the Unaudited Condensed Consolidated 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 us 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 our Annual Report on Form 10-K for the year ended December 31, 2006 filed with the Securities and Exchange Commission.

ITEM 3. CONTROLS AND PROCEDURES

(a) EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES: As of the end of the period covered by this quarterly report, we, including our principal executive and financial officers, performed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures. 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, that our disclosure controls and procedures were not effective in timely alerting them as to material information relating to our

Company and our subsidiaries that is required to be included in this quarterly report.

The material weakness in our internal controls over financial reporting as of September 30, 2007 related to the fact that as a small public company, we, currently, have an insufficient number of personnel with clearly delineated and fully documented responsibilities and with the appropriate level of accounting expertise. We also 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 September 30, 2007.

During the second quarter of 2007 we retained a financial consultant who acted as our controller and also analyzed procedures and evaluated internal controls and reported his findings and recommendations for addressing the material weakness described above as well as other proposed changes to the Audit Committee of the Board. To the extent practicable we will implement these recommended changes by the end of 2007. So far, we have improved our method of preparing consolidated financial statements and upgraded our accounting staff. The consultant remains with us as our chief financial officer.

(b) CHANGES IN INTERNAL CONTROLS: Except as noted in Management's Discussion and Analysis or Plan of Operation, no change in the Company's internal control over financial reporting occurred during the third quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. However, the Audit Committee and we recognize that current staffing levels will have to be enhanced and/or arrangements will have to be made 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.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

There has been no significant change in the status of litigation since the issuance of our Annual Report on Form 10-K for the year ended December 31, 2006.

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

Our annual meeting of stockholders was held on September 17, 2007; our stockholders voted upon three matters:

1) To elect one (1) Class I and two (2) Class II members of the Company's Board of Directors.
   Results of voting: 3,393,893 votes were cast for Shouky A. Shaheen; 731,663 votes were withheld. 3,404,192 votes

were cast for the election of Curtis Carlson; 721,363 votes were withheld. 3,988,692 votes were cast for Elliot Ross; 136,863 votes were withheld.

2) To reclassify one (1) Class III member of the Company's Board of Directors to be a Class I member:
Results of voting: 1,997,527 votes were cast for the reclassification of William M. Gross as a Class I director. Votes against were 113,670; votes abstaining were 2,400. Broker non-votes were 2,011,958.

3) To ratify the appointment of the Company's independent public accounting firm, Goldstein Lewin & Co.
Results of voting: 4,027,739 votes were cast for the ratification of auditors. Votes against were 95,999; votes abstaining were 1,817.

After the aforementioned voting by our stockholders the following persons comprised our Board of Directors: Messrs. Richard Barone, Curtis Carlson, Frank Ferola, William Gross, Elliot Ross and Shouky Shaheen.

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.

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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
November 18, 2007

/s/ Robert C. Spindler

Robert C. Spindler
Principal Financial and
Accounting Officer
November 18, 2007