

ARISTOTLE CORP
Form 10-K
March 24, 2006

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(MARK ONE)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE

ACT OF 1934

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2005

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)

SECURITIES REGISTERED PURSUANT TO SECTION 12(B) OF THE ACT:

NOT APPLICABLE

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT:

COMMON STOCK, \$.01 PAR VALUE (COMMON STOCK)

(TITLE OF CLASS)

**SERIES I \$6.00 CONVERTIBLE, VOTING, CUMULATIVE 11% PREFERRED STOCK, \$.01 PAR VALUE
(SERIES I PREFERRED STOCK)**

(TITLE OF CLASS)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

As of June 30, 2005, the aggregate market value of the Common Stock outstanding and held by nonaffiliates (without admitting that any person whose shares are not included in such calculation is an affiliate) was approximately \$6.7 million and the aggregate market value of the Series I Preferred Stock outstanding and held by nonaffiliates (without admitting that any person whose shares are not included in such calculation is an affiliate) was approximately \$7.6 million. In each case, the market value of outstanding securities was based on the closing price of such securities as reported by the NASDAQ Capital Market.

As of March 24, 2006, 17,256,296 shares of Common Stock, 1,100,122 shares of Series I Preferred Stock and 10,984,971 shares of Series J Preferred Stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

The Exhibit index is located on page 53 of this filing.

Part III incorporates certain information by reference to registrant's Proxy Statement for its 2006 Annual Meeting of Stockholders.

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PART I

ITEM 1. BUSINESS

COMPANY OVERVIEW

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.

Prior to June 17, 2002, Aristotle was a holding company which, through its subsidiaries, Simulaids, Inc. (Simulaids) and Safe Passage International, Inc. (Safe Passage), conducted business in two segments, the medical education and training products market and the computer-based training market. On June 17, 2002, Aristotle merged (the Merger) with Nasco International, Inc. (Nasco), an indirect subsidiary of Geneve Corporation (Geneve), a privately-held diversified financial holding company. Pursuant to the Merger, the separate corporate existence of Nasco ceased and Aristotle was the surviving entity. Immediately following the Merger, Aristotle s business was comprised of the operations of the Nasco group of companies, Simulaids and Safe Passage. Due to the relative sizes of the parties and conditions to the Merger, the transaction was accounted for as a reverse acquisition using the purchase method of accounting under U.S. generally accepted accounting principles (GAAP). Accordingly, for accounting and reporting purposes, Nasco was deemed to be the acquiring company, and financial information reported for periods prior to the Merger is that of Nasco. In applying purchase accounting to the Merger, the assets and liabilities of Aristotle were adjusted to their fair market values at June 17, 2002. This accounting method included recognition of a significant deferred tax asset of approximately \$30.7 million, which was principally attributable to Aristotle s Federal net operating tax loss carryforwards. As a result of such recognition, Aristotle s pre-merger goodwill and long-term assets of \$8.3 million were reduced to zero and negative goodwill of \$20.2 million was recognized as an extraordinary gain at the Merger date.

ACQUISITIONS AND DIVESTITURES

On September 17, 2004, Aristotle purchased certain assets of the science product line of Ginsberg Scientific Company and GSC International, Inc. (collectively referred to as Ginsberg) for \$1.8 million. Ginsberg is a manufacturer and distributor of products and kits designed to demonstrate certain science concepts for students in grades 5-12. The Ginsberg offerings complement the science product lines manufactured and distributed by the Company in the educational segment. The results of Ginsberg s operations have been included in the Company s consolidated financial statements since the date of such acquisition. The purchase price allocation resulted in goodwill of \$1.0 million attributable to the educational segment.

On August 11, 2004, Aristotle purchased certain assets of the CPR Prompt product line for \$1.9 million. The CPR Prompt product line is comprised of a number of products, primarily training manikins, used in the instruction of cardiopulmonary resuscitation. The CPR Prompt product line complements product lines manufactured and distributed by the Company in the educational segment. The results of CPR Prompt s operations have been included in the Company s consolidated financial statements since the date of such acquisition. The purchase price allocation resulted in goodwill of \$1.0 million attributable to the educational segment.

On May 31, 2003, Aristotle purchased 100% of the outstanding capital stock of Haan Crafts Corporation (Haan). Haan is a manufacturer and catalog distributor of sewing kits used in middle school and junior high school family and consumer science classrooms. The acquisition complemented the Company s existing product lines in the educational segment. The results of Haan s operations have been included in the Company s consolidated financial statements since the date of such acquisition. The aggregate purchase price, net of cash acquired, was \$5.3 million, including \$3.5 million of cash and \$1.8 million in seller financing, which was subsequently retired by the Company. The purchase price allocation resulted in goodwill of \$3.9 million attributable to the educational segment. In connection with the acquisition of Haan, Aristotle entered into a \$1.2 million capital lease with the seller on a building facility (Haan Building Facility). On February 12, 2004, the Company settled the capital lease on the Haan Building Facility for \$1.1 million.

On May 31, 2003, Aristotle acquired 100% of the outstanding ownership interests in NHI, LLC (NHI) from Nasco Holdings, Inc. (Holdings), a subsidiary of Geneve. The sole purpose of NHI is the ownership and management of warehouse and office facilities, which had previously been leased to Aristotle. In connection with the purchase of NHI, Aristotle paid to Holdings an amount equal to the book value of NHI, which included a \$3.6 million mortgage related to the properties held by NHI. On August 6, 2004, the Company paid \$3.4 million, including interest, in full settlement of this mortgage.

On December 31, 2002, Aristotle sold its 80% ownership interest in Safe Passage in exchange for certain contingent payments. It is unlikely that contingent payments, if any, which are payable through 2008 and based upon the financial performance of Safe Passage, will be material to the financial statements.

In April 2001, Nasco acquired 100% of the stock ownership of Spectrum Educational Supplies, Ltd. (Spectrum), a Canadian provider of educational products, for \$5.2 million in cash. In March 2001, Nasco completed the stock acquisition for \$5.3 million in cash of that portion of American Educational Products, Inc. (AMEP), a manufacturer and distributor of math and science products, which it did not already own.

DESCRIPTION AND FINANCIAL INFORMATION OF BUSINESS SEGMENTS

The Company operates in two business segments: educational and commercial. The contribution of each business segment to net sales and gross profit, and the identifiable assets attributable to each business segment are set forth in Note 15 of the Notes to the Consolidated Financial Statements included in Item 8 of this Form 10-K.

Educational Segment

The Company's educational segment consists primarily of the sale of supplemental educational supplies and equipment to school districts, individual schools, teachers and curriculum specialists, who purchase products primarily for classroom use.

In addition to its business in the school supply market, the Company, through its Nasco Life/Form, Simulaids and CPR Prompt product lines, sells medical technology training products including manikins and medical simulators used for training in cardiopulmonary resuscitation and the emergency rescue and patient care fields. The Company's primary users of its health care training products are fire and emergency medical departments, and nursing and medical schools.

Commercial Segment

The Company markets agricultural supplies, including small hand tools and equipment, to farmers and ranchers to assist in livestock and crop production.

In addition, the Company provides sterile sampling bags and containers worldwide under the Whirl-Pak trademark. The product line is primarily sold in the food and water treatment industries. The product line provides a stable vehicle for the containment and transporting of food and water samples to laboratories without threat of sample contamination.

In the senior care industry, the Company offers a broad selection of products used by nursing home and senior care facilities to support therapy programs.

INDUSTRY OVERVIEW

Educational Segment

According to the U.S. Department of Education, over \$500 billion is estimated to be spent nationwide on education at the elementary and secondary levels. As the market is affected by prevailing political and social trends, the attitude of the government towards education determines, to some extent, total expenditures on education. In 2002, President Bush signed into law the No Child Left Behind Act of 2001, designed to improve student achievement and change the culture of America's schools. States and local school districts are now receiving more Federal funding, approximately \$56 billion, than ever before for all programs under the No Child Left Behind Act of 2001. Notwithstanding the Federal funding available to support education, state governments are the major source of funding for the educational segment. State governments have been affected by the weak U.S. economy of recent years, resulting in significant state budget deficits in fiscal years 2003-2004. However, improvements in state tax collections and other revenue sources during fiscal year 2005 have led to a reduction in the size of state budget deficits. While state budget deficits have decreased, the National Conference of State Legislatures does not anticipate that current improvements in state revenues will relieve educational funding pressures for fiscal year 2006 due to spending demands in areas such as healthcare, education and energy assistance. However, management believes that, as the U.S. economy continues to improve, these shortfalls in state budgets will be reduced, eventually resulting in increased expenditures on education. Although very few companies or industries are recession-proof, management believes that the Company's educational segment is essentially recession-resistant.

Factors that contribute to the expansion of the education sector include:

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increases in elementary and secondary school enrollment which, according to the U.S. Department of Education, is projected to grow to 56 million students by the year 2013;

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consistent growth in the supplemental education market; and

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a national political and social climate that promotes increasing Federal and state education funding.

The traditional school model of lectures, workbooks, written assignments and text memorization has been criticized for failing to engage students, as opposed to methods that emphasize active learning techniques. The prevailing inclination among educators to use manipulatives, models, or other hands-on tools places the Company within a particularly favorable segment of the already well-positioned education industry.

According to the U.S. Department of Education, there are approximately 15,000 public school districts, 123,000 elementary and secondary schools, 4 million teachers and 55 million students in the United States. The Company believes that American school systems have shown a clear trend toward decentralization, which enables school teachers and administrators at the school to make many of the key decisions regarding instruction methods and school purchases. Administrators for both school districts and individual schools usually make the decision to purchase the general school supplies needed to operate the school. Teachers and curriculum specialists generally decide on curriculum-specific products for use in their classrooms and individual disciplines. Increasingly, teachers and curriculum specialists have the ability to choose the curricular materials that the teachers need to teach effectively. Site-based management is forcing the industry to rethink its sales and marketing strategies in order to address the added challenge and added cost of delivering goods and services to an increasingly decentralized marketplace. In terms of purchasing methods, direct mail ordering by catalog, as well as the internet, are on the rise as purchasing mechanisms among administrators in charge of budgets.

The industry is also highly fragmented with a substantial number of direct marketers of supplemental educational supplies, many of which are family- or employee-owned businesses that operate in a single geographic region. The Company believes the increasing demand for single-source suppliers, prompt order fulfillment and competitive pricing, along with the related need for suppliers to invest in automated inventory and electronic ordering systems are fostering consolidation within the industry. Increased purchasing at the school and classroom levels, which increases individual schools' and teachers' roles in educational supply procurement decisions, is also driving this trend. The Company's selection of products and vendors allows it to offer an extensive selection of products for each product line. The Company believes that by having available to school teachers and administrators all of the items they need in one place, the inclination to search other sources is reduced. This one stop shopping approach is the Company's hallmark.

Moreover, the Company seeks to be competitive with its catalog prices rather than offering large discounts to single customers. With many products, two or more choices are offered in order to give customers a lower price point with a product that will meet their budget yet perform to required standards.

In the Canadian educational market, the provincial government is responsible for the funding, curriculum and other standards of elementary and secondary educational programs. In addition, the Canadian economy is generally impacted by the overall conditions of the U.S. economy.

The health and medical education teaching aids industry is highly competitive. The Company competes for customers with numerous manufacturers of well-known brands of teaching products. The principal competitive factors in the health and medical education teaching aids market are quality, price, design of products and customer service. Although some of the Company's competitors have greater financial and other resources, and are, therefore, able to expend more resources than the Company in areas such as marketing and business development, the Company believes that it is aggressively marketing its products and competing in an effective manner.

Commercial Segment

The United States Department of Agriculture indicates that there are approximately two million farms in the U.S. The Company not only markets to various groups within this total but its catalog is also directed to the hobby farmer as well. As the number of farms declines, which is a national trend, the remaining farms are becoming larger. With its extensive offerings in the farm catalog, the Company is well positioned to supply the market with the types of supplies and small hand tools and equipment needed.

Commercial distribution of sterile sampling bags and containers experienced growth in recent years as food and water quality standards gained emphasis in global markets. Product lines offered by the Company in this segment are key tools in measuring and enforcing government standards for food and water quality, and have gained a role in meat and other food-related industries. International sales growth for these product lines is driven by a developing consciousness of food and water quality standards in third-world countries. Domestically, the food industry is challenged with additional testing requirements for meat, poultry and fruit products in reaction to biosecurity risks. These increasing government regulations and growing product liability exposures should continue expansion in the amount and frequency of product sampling.

In the senior care market, the expectations of government funding cuts in the upcoming Medicare and Medicaid budgets for nursing home payments are again a cause of concern for the Company. Recognizing that governmental funding for the senior care market may be limited for the next several years, the Company has targeted its product

offering to service the more basic fundamental activity needs for these customers.

GROWTH STRATEGY

Key members of the Company's management team develop and execute multiple action plans in an effort to continue the Company's historically steady growth in sales and earnings. These action plans are continuously monitored by senior management to assess the progress in achieving the planned goals. The principal action plans are as follows:

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Continue strategic evaluation and execution of complementary acquisitions in existing market segments.

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Consistently dedicate resources to the discovery of new product lines to meet the ever-changing needs of customers, including closely observing the evolution in classroom curricula and continuously updating product selection to meet these changing needs.

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Commit resources to the internal development of new products with features that meet changing customer demands, as proprietary items generally carry the added benefits of higher profit margins and exclusive availability. Research and development staffs maintain a constant flow of proprietary items to the catalog offerings.

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Exploit the revenue and earnings potential of acquisitions, including:

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continued expansion into the Canadian educational markets through Spectrum by supplementing existing Canadian catalogs with Nasco product lines; and

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energizing the research and development efforts of acquired businesses to develop and market competitive proprietary products.

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Through senior management evaluation of the relative profitability of catalog performance and operational efficiencies, pursue options for consolidation of overhead costs. Particularly with acquisitions of new businesses, all appropriate opportunities to consolidate overhead and service support functions will be pursued to maximize earnings benefits.

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With minimal investment of capital and manpower, penetrate international markets outside of North America in the health care, sterile sampling bags and containers and agricultural product lines.

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Continue the promotional efforts of the Company's e-commerce website to encourage customer awareness and use of the website.

PRODUCT LINES

The Company markets the following product lines through its various catalogs and websites, including www.eNasco.com, www.summitlearning.com, www.to-sew.com, www.triarcoarts.com, www.bentonkirby.com, www.goodtimeattractions.com, www.shnta.com, www.spectrumed.com, www.haan.com, www.simulaid.com and www.cprprompt.com.

Educational Offerings

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Arts and Crafts - Complete offering of supplies to nurture the creative artistic spirit of all ages and skill levels. A source for the specialty art teacher as well as anyone interested in this discipline. Target - grades kindergarten to twelve, camps and recreation centers.

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Science - Complete catalog of equipment and supplies for general science, biology, chemistry, physical science, earth science and technology education. Also, offers live and preserved specimens as well as alternatives to dissection. Target - science teachers in grades three to twelve and specimens for the college instructor.

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Math - Provide teaching aids for the primary grades through pre-algebra and geometry. Includes manipulatives, calculators, games, overhead math items, software and other math products. Target - grades kindergarten to twelve.

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Health Care - Features the proprietary Nasco Life/Form, Simulaids and CPR Prompt product lines, anatomical replicas and medical procedure simulators to aid in the training of the medical profession. Includes videos, software, games, charts and replicas. Also includes hands-on teaching aids developed to make learning about health fun and interesting for kindergarten through twelfth grade students. Target - nursing and medical schools, emergency training professionals and health teachers.

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Family and Consumer Sciences - A broad listing of products, including products to teach life skills, cooking, sewing and teaching resources for the entire family and consumer science teaching profession. Also features teaching aids for dietitians in hospitals, schools and diabetes education. Target - family and consumer science teachers, dietitians and nutrition instructors.

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Early Learning - Features a carefully chosen selection of teaching materials, learning toys and games developed for the early childhood market to make learning fun. Target - grades pre-kindergarten to three.

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Physical Education - An extensive listing of items specifically for physical education professionals. Target - physical education teachers in grades kindergarten to twelve.

Commercial Offerings

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Farm and Ranch - Includes products for animal identification, showing, grooming, veterinarian supplies, artificial insemination, animal health, crops and soils and equine supplies. Target - farmers and ranchers.

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Senior Activities - Products developed to assist the activity therapist in providing the best activity programs in the nursing home and assisted living industries. Includes products for sensory, memory and musical activities plus games and arts and crafts. Target - activity therapists in nursing homes and assisted living homes.

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Whirl-Pak Sampling Products - Features sterile Whirl-Pak sampling bags, the industry leader in sampling containers for over 40 years. This laboratory product is sold in the U.S. and throughout the world. Target - food and microbiology laboratories throughout the world.

SALES AND MARKETING

The Company offers a wide variety of products, both proprietary products and products manufactured by others, primarily through catalogs distributed to customers throughout the United States and internationally. The Company also sells products through distributors. Additionally, the Company's products are available for sale on its websites. Within the Company's current markets served, research is conducted by sales and marketing personnel to identify needed products. The Company often hires consultants or sales directors from the niche served. The Company's catalog teams continually search for new, improved and unique products. Catalog teams pursue sales growth goals through efforts to present more than 7,000 catalog pages with broad selections of popular and new products at competitive catalog prices, and with choices of similar types of products with different price points, qualities, or features. If the Company is unable to find products to meet a specified demand, it has the option of attempting to manufacture the product in its own plants or contract manufacturing under a private label.

The Company attempts to time the distribution of catalogs to meet the peak buying periods and mails the catalogs to the individuals whom the Company believes make the buying decision. The Company's experience indicates that the actual user of the materials usually makes the buying decision, except for those items that are a part of school bid requests. The Company's mailings concentrate on putting the catalogs in the hands of these decision makers. All catalogs are annually reviewed for revision. The Company's bid request goal is to be competitively priced. The Company issues most major catalogs annually to over three million potential customers. The Company relies mainly on its more than 45 separate catalogs as its sales staff, which relieves the need for expensive sales calls on customers.

In recent years, the Company has expanded its efforts in international markets outside of North America, primarily in the health care, sterile sampling bags and containers and agricultural product lines. While international sales represent less than 10% of 2005 total net sales, the acceptance of product lines by international markets has been a significant growth contributor for these particular product lines.

Orders are received via mail, phone, facsimile, or internet. The Company aims to exceed customer expectations based on customers' directions. The Company's business is transacted by open order and purchase orders. The Company ships many orders the same day received and most orders are shipped within three days. Sale terms are typically net 30 days.

The Company is not dependent upon a single customer, or a few customers. Therefore, the loss thereof would not have a material adverse effect on the Company or either of its business segments.

PURCHASING

Substantial portions of the products distributed by the Company are purchased from manufacturers and distributors worldwide. The Company's purchasing staff is in contact with vendors to insure awareness of new products, timely delivery and competitive pricing. With its broad range of vendors, including alternative product sources, the Company does not generally maintain contractual fulfillment agreements for purchase quantity commitments. Vendors often review catalog pages and make suggestions for the following year's offering. Alternate vendors are reviewed on a continuous basis. To broaden its product mix to meet specific customer needs, the Company operates manufacturing facilities that produce proprietary items. Sales of proprietary products generally result in a higher profit margin and enable the Company to sell such products at wholesale in the U.S. and foreign markets where the Company often develops distribution relationships. The Company has historically been able to obtain sufficient quantities of the raw materials necessary for the manufacture of proprietary products.

INTELLECTUAL PROPERTY

The Company has a number of trademarks and trade names that it applies to various product lines such as Nasco, Life/Form, Whirl-Pak and CPR Prompt. Except for the Nasco trademark, the various trademarks and trade names are not considered material or vital to on-going business operations. To protect the unique product lines developed, the Company has applied for and received patents for various products in the U.S. and Canada. None of these issued or pending patents are considered vital or material to on-going business operations.

COMPETITION

Although there are several large general school suppliers and wholesale and retail stores which compete with the Company, the Company believes that it offers more specialty items in more disciplines in the educational, health, medical technology and agricultural markets than any competitor. Although the Company faces competition with regard to each of its catalogs from businesses that specialize in limited numbers of curriculum subjects or markets, few, if any, of the Company's competitors have as broad a range of products that serve as many market areas.

BACKLOG

The Company's customers typically purchase products on an as-needed basis. The Company believes that, as of December 31, 2005, backlog was not a meaningful indicator of future business prospects due to the large volume of products delivered from inventories on hand.

INFORMATION SYSTEMS

The Company's main computer system, housed in Fort Atkinson, Wisconsin, is an IBM AS 400 computer. The Company's business is highly computerized, with almost all functions including accounting, order processing, purchasing, quotes, phone orders, billing, receivables, payables and warehousing running on this system. The system is routinely upgraded, increasing capacity to handle the Company's needs. To facilitate and continuously improve the software system, a staff of programmers responds to suggestions from all departments and management.

CATALOG PREPARATION

Catalog preparation is primarily handled in Fort Atkinson. A staff of graphic artists and editors works with Macintosh desktop publishing systems to complete all production work in-house, with the exception of printing.

EMPLOYEES

At December 31, 2005, the Company had approximately 850 employees. In addition, the Company engages approximately 200 temporary employees to accommodate the peak business season during the summer months. All employees at all locations are employed at-will and none are represented by a labor union.

ITEM 1A. RISK FACTORS

FORWARD-LOOKING STATEMENTS

The Company believes that this Annual Report on Form 10-K 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 risk factors set forth below. 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 Securities and Exchange Commission ("SEC"), including its Forms 10-K, 10-Q and 8-K.

RISK FACTORS

If the Company's competitors are successful in developing, manufacturing and selling competitive products, the Company's operating results could suffer.

The Company operates in highly competitive and fragmented markets. Businesses that compete with the Company are likely to continue expansion of their product offerings that may erode the Company's gross margins. The broad range of product lines offered by the Company is unique to the market as few competitors offer the depth of subject matter in their product mix. However, each of the Company's catalogs competes against a unique list of businesses that specialize in limited numbers of curriculum subjects or markets. Some competitors may be able to commit greater resources to product development, invest greater amounts on capital equipment and marketing plans, or offer more aggressive discounts for its products or services. In fragmented markets, competitors may further merge and consolidate, increasing market competition. Any of these competitive pressures could have a negative effect on the Company's operating results.

If the Company is unable, for technical, legal, financial or other reasons, to adapt in a timely manner in response to changing market conditions or customer requirements, the Company's business, prospects, financial condition and results of operations would be materially adversely affected.

The Company's success depends on its ability to enhance existing products and services, develop new products, services and technologies that address the increasingly sophisticated and varied needs of customers and its ability to respond to technological advances and emerging industry standards and practices on a cost-effective and timely basis.

If the Company is unable, for technical, legal, financial or other reasons, to adapt in a timely manner in response to changing market conditions or customer requirements, the Company's business, prospects, financial condition and results of operations could be negatively affected.

The Company is dependent upon the levels of student enrollment in elementary and secondary schools and expenditures per student.

The Company's ability to grow the business depends in part on the levels of student enrollment in elementary and secondary schools and expenditures per student. The level of student enrollment in elementary and secondary schools is largely a function of demographics. Expenditures per student are a function of prevailing political and social attitudes toward education, as well as government budgets. Any significant and sustained decline in the size of the levels of student enrollment and/or expenditures per student could have an adverse effect on the Company's business, prospects, financial condition and results of operations.

If the Company fails to retain key personnel and hire, train and retain qualified employees, the Company may not be able to compete effectively, which could result in reduced sales.

The performance of the Company is substantially dependent on the services and performance of its senior management and other key personnel. The loss of the services of, and the failure to promptly replace, any of the Company's executive officers or other key personnel, as well as the Company's inability to attract and retain qualified personnel, could have a negative effect on the business, prospects, financial condition and results of operations of the Company. Competition for qualified personnel is intense, and there can be no assurance that the Company will be able to successfully attract, integrate or retain sufficiently qualified personnel.

The Company expects its results of operations to fluctuate from quarter to quarter and the price of its Common Stock and Series I Preferred Stock could fall if quarterly results are lower than the expectations of the market.

The Company's results of operations have fluctuated in the past, and the Company's results of operations may vary from quarter to quarter in the future. If quarterly results fall below market expectations, the price of the Company's Common Stock and/or Series I Preferred Stock could fall. A number of factors, many of which are outside of the Company's control, may cause variations in its results of operations including:

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fluctuations in the demand for educational, health, medical technology and agricultural products;

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seasonality of sales typically experienced by educational supply retailers with peak levels of sales occurring in the second and third quarters of the calendar year primarily due to increased educational shipments coinciding with the Fall start of new school years; and

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fluctuations in sales and marketing expenses and technology infrastructure costs.

A substantial portion of the Company's operating expenses are and will be related to sales and marketing, product development, technology and infrastructure, which expenses cannot be adjusted quickly and are therefore relatively fixed in the short term. The Company's operating expense levels are based in significant part on its expectations of future sales on a quarterly basis. As a result, if sales for a particular quarter are below expectations, the Company may not be able to reduce operating expenses proportionately for that quarter; this sales shortfall would have a negative effect on the Company's operating results and cash flow for that quarter, which would likely have a negative impact on the price of the Company's Common Stock and/or Series I Preferred Stock.

The Company's stock price may fluctuate based on factors beyond its control.

Market prices for securities of companies comparable to the Company are highly volatile. The market for the Company's Common Stock and Series I Preferred Stock has from time to time experienced significant price and volume fluctuations that are unrelated to the Company's operating performance.

Geneve beneficially owns approximately 90% of the aggregate voting power of the Company.

Geneve currently owns approximately 90% of the aggregate voting power of the Company. Accordingly, in many circumstances, stockholders of the Company other than Geneve have no ability to determine the outcome of corporate actions requiring stockholder approval, including the election of directors and certain amendments to the Company's amended and restated certificate of incorporation.

Concentration of common share ownership and limited number of shares outstanding could prevent an active market for the Company's Common Stock and Series I Preferred Stock.

Although the Company's Common Stock and Series I Preferred Stock are publicly traded on the NASDAQ Capital Market, the concentration of common share ownership amongst Geneve and the Company's management and directors and the small number of its outstanding Common Stock and Series I Preferred Stock that is publicly traded could prevent an active market for the Company's Common Stock and Series I Preferred Stock. If there is not an active market for the Common Stock and Series I Preferred Stock, it may be difficult to sell shares of Common Stock and Series I Preferred Stock, which could lower the price of the shares.

The Company may not pay dividends on the Series I preferred stock.

Each share of Series I Preferred Stock accrues cumulative dividends at the rate of 11% per share, based on the \$6.00 stated value of the Series I Preferred Stock, and it is the current intent of the Company's board of directors to declare such dividends. However, the payment of this dividend will be subject to the discretion of the board of directors of the Company, which has no obligation to declare or pay the dividend. While no dividends may be paid with respect to the Company's Common Stock or Series J Preferred Stock until dividends are paid with respect to the Series I Preferred Stock, there can be no assurance that any cash dividend payments will be made to holders of Series I Preferred Stock.

Conversion of the Series I Preferred Stock to Common Stock may not compensate for non-payment of dividends or lack of liquidity.

Although each share of Series I Preferred Stock and any accrued but unpaid dividends may be converted into shares of the Company's Common Stock during the 90-day period beginning on June 17, 2007, the market price of the Company's Common Stock when the Series I Preferred Stock becomes convertible may not be sufficient for such

conversion to adequately compensate for the Company's failure to pay accrued dividends on its Series I Preferred Stock. Moreover, there can be no assurance that the market for the Company's Common Stock at the time of conversion will have sufficient trading volume so as to provide liquidity for holders of Series I Preferred Stock.

Certain factors may affect the Company's ability to fully utilize its Federal net operating tax loss carryforwards.

The Company believes that its Federal net operating tax loss carryforwards will be available to offset future taxable income through 2006, and that the Company's stockholders will continue to benefit from the Company's Federal net operating tax loss carryforwards. The realizability of the Federal net operating tax loss carryforwards is dependent upon the Company's generation of sufficient levels of future taxable income and the ability to retain its Federal net operating tax loss carryforward position. However, events may limit the use of all or a portion of these Federal net operating tax loss carryforwards, thus potentially resulting in a higher tax liability for the Company in the future.

The Company may not be able to obtain financing and additional capital to fund its business strategy on acceptable terms.

From time to time the Company accesses the capital markets to obtain financing. Although the Company believes that it can continue to access the capital markets in the future on acceptable terms and conditions, the Company's flexibility could be limited by the Company's operating results and financial position, including such factors as current levels of outstanding debt and working capital. In addition, many of the factors that affect our ability to access the capital markets, such as the current state of the economy, are outside of the Company's control. There can be no assurances that the Company will continue to have access to the capital markets on acceptable terms.

The Company views its existing \$45.0 million Revolving Credit Facility as a source of available liquidity. This facility contains various covenants with which the Company must be in compliance in order to borrow funds. If the Company wishes to borrow under this facility in the future, there can be no assurance that the Company will be in compliance with these covenants. By its terms, the Revolving Credit Facility expires in October 2008. The Company anticipates renewing the facility on terms at least as favorable as the existing facility, but there can be no assurances of renewal or the terms on which the Company renews.

The Company may expand its business through acquisitions.

The Company reviews many acquisition candidates and, in addition to acquisitions which the Company has already made, the Company is continually evaluating new acquisition opportunities. Factors which may affect our ability to grow successfully through acquisitions include:

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ability of the Company on a timely basis to find, prudently negotiate and consummate additional acquisitions;

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difficulties and expenses in connection with integrating the acquired companies and achieving the expected benefits;

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diversion of management's attention from current operations;

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the possibility that the Company may be adversely affected by risk factors facing the acquired companies;

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acquisitions could be dilutive to earnings, or in the event of acquisitions made through the issuance of the Company's Common Stock to the stockholders of the acquired company, dilutive to the percentage ownership of our existing

capital stock;

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potential losses resulting from undiscovered liabilities of acquired companies not covered by the indemnification we may obtain from the seller; and

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loss of key employees of the acquired companies.

The Company may be required to expend significant resources to comply with Section 404 of the Sarbanes-Oxley Act and may not be able to comply on a timely basis, if at all.

The Company is not an accelerated filer as defined under relevant SEC regulations, and therefore is not required to comply with Section 404 of the Sarbanes-Oxley Act until its 2007 Annual Report, which will be filed by the Company in 2008. Complying with Section 404 of the Sarbanes-Oxley Act may require the Company to expend significant resources, which could increase selling and administrative expenses and divert management time and attention from sales-generating activities.

ITEM 2. PROPERTIES

The Company leases approximately 1,000 square feet of executive office space in Stamford, Connecticut from Geneve, the Company's majority stockholder.

The Company's primary distribution center is located in Fort Atkinson, Wisconsin. The approximately 220,000 square foot owned distribution center is the headquarters for all Nasco marketing efforts. The Company also leases approximately 45,000 square feet of manufacturing space to support the catalog product lines. The Company owns approximately 300,000 square feet of adjacent warehouse space and 40,000 square feet of adjacent office space. The Company currently occupies approximately 230,000 square feet of the warehouse space, and leases the office space and remaining warehouse space to third parties under lease agreements expiring on various dates over the next two years. These facilities afford the Company the necessary expansion capacity for the foreseeable future. In 2003, the Company became the owner of these facilities as a result of the acquisition of 100% of the outstanding interest in NHI from Holdings. For more information regarding this and other acquisitions of the Company, please refer to the Acquisitions and Divestitures section above.

To service the western United States, the Company owns and operates an approximately 68,000 square foot distribution center in Modesto, California. This distribution center services all Nasco catalogs for customers in the 12 western states.

The Company operates its Triarco arts and crafts catalog operation, along with three other independent catalogs, from an approximately 4,000 square foot leased office facility in Plymouth, Minnesota. The distribution center in Fort Atkinson, Wisconsin services these catalogs.

The Company also maintains an educational materials catalog distribution center in Fort Collins, Colorado from an approximately 18,000 square foot owned facility. From this location and approximately 39,000 square feet of leased facilities in Chippewa Falls, Wisconsin, the Company's AMEP and Ginsberg product lines service math and science teachers and distributors worldwide. Light manufacturing operations are situated at both of these locations, producing mainly proprietary items.

An approximately 83,000 square foot owned facility located in Newmarket, Ontario, Canada, currently operates as a distribution center of educational and commercial supplies sold by Spectrum via catalog mailings to schools and businesses throughout Canada.

The Company owns two buildings comprising approximately 50,000 square feet of office and manufacturing space in Woodstock, New York. The Company also leased approximately 8,000 square feet of nearby warehouse space through January 2006. In the first quarter of 2006, the Company began operations in a new approximately 80,000 square foot office and manufacturing facility in Saugerties, New York, which it finished constructing at the end of 2005. The final construction costs will be approximately \$5.0 million. The Company produces manikins and medical simulators used for training in the health care field at this location for its Simulaids operations. The Company intends to sell the old Simulaids facilities.

The Company owns an approximately 43,000 square foot light manufacturing and distribution facility in Otterbein, Indiana. The Company produces sewing kits used in middle school and junior high school family and consumer science classrooms at this location for its Haan operations.

The locations in Fort Atkinson, Wisconsin; Modesto, California; Plymouth, Minnesota; and Newmarket, Ontario, Canada service both of the Company's business segments. The locations in Fort Collins, Colorado; Chippewa Falls, Wisconsin; Woodstock, New York; and Otterbein, Indiana service the Company's educational segment.

Certain of the Company's owned properties, including the primary distribution center in Fort Atkinson, Wisconsin and owned properties located in Modesto, California; Fort Collins, Colorado; and Otterbein, Indiana, are each subject to a mortgage in favor of the Company's principal lender, JPMorgan Chase Bank, N.A. (formerly Bank One, NA), as additional security pursuant to a Revolving Credit Facility entered into by the Company on October 15, 2003. For more information regarding this Revolving Credit Facility, please refer to Note 8 of the Notes to the Consolidated Financial Statements included in Item 8 of this Form 10-K.

ITEM 3. LEGAL PROCEEDINGS

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

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 fourth quarter of the year ended December 31, 2005.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

MARKET INFORMATION

The Company's Common Stock is quoted on the NASDAQ Capital Market under the symbol ARTL. The high and low sale prices per share of Common Stock on the NASDAQ Capital Market (as reported by NASDAQ) during the fiscal quarters indicated are set forth below.

	MARKET PRICE \$	
	HIGH	LOW
FISCAL YEAR ENDED DECEMBER 31, 2005:		
December 31	8.00	5.80
September 30	8.75	6.25
June 30	7.49	4.50
March 31	7.56	6.30
FISCAL YEAR ENDED DECEMBER 31, 2004:		
December 31	8.00	5.12
September 30	9.90	4.66
June 30	5.17	4.65
March 31	5.35	4.43

The Company's Series I Preferred Stock is quoted on the NASDAQ Capital Market under the symbol ARTLP. The high and low sale prices per share of Series I Preferred Stock (as reported by NASDAQ) during the fiscal quarters indicated are set forth below.

	MARKET PRICE \$	
	HIGH	LOW
FISCAL YEAR ENDED DECEMBER 31, 2005:		
December 31	9.45	7.78
September 30	9.87	8.35
June 30	8.84	7.87
March 31	12.74	7.50
FISCAL YEAR ENDED DECEMBER 31, 2004:		
December 31	8.95	7.60
September 30	8.75	7.68
June 30	8.62	7.66
March 31	9.00	7.62

The Series J \$6.00 non-convertible, non-voting cumulative 12% preferred stock, par value \$.01 per share (Series J Preferred Stock) is privately-held and no trading market exists for such shares.

HOLDERS OF RECORD

As of March 7, 2006, there were approximately 2,067 holders of record of the Company's Common Stock and approximately 1,898 holders of record of the Company's Series I Preferred Stock.

DIVIDENDS

The Company has not paid any cash dividends on its Common Stock since its inception and does not intend to pay any cash dividends on its Common Stock in the foreseeable future.

Dividends on the Company's Series I Preferred Stock and Series J Preferred Stock are payable on March 31 and September 30, if and when declared by the Company's Board of Directors. For each of 2005 and 2004, the Company paid semi-annual dividends of \$.33 and \$.36 per share on its outstanding shares of Series I Preferred Stock and Series J Preferred Stock, respectively.

On March 1, 2006, the Company announced that it had declared a cash dividend of \$.33 and \$.36 per share, respectively, on its outstanding shares of Series I Preferred Stock and Series J Preferred Stock. The dividends are payable on March 31, 2006, to holders of record on March 15, 2006.

EQUITY COMPENSATION PLAN INFORMATION

The following table summarizes the Company's Equity Compensation Plans as of December 31, 2005:

Plan Category	(A) Number Of Securities To Be Issued Upon Exercise Of Outstanding Options, Warrants And Rights	(B) Weighted Average Exercise Price Of Outstanding Options, Warrants And Rights	(C) Number Of Securities Remaining Available For Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected In Column (A))
Equity Compensation Plans			
Approved by Security Holders			
1997 Plan	5,000 (1)	\$ 5.63	-
2002 Plan	809,025 (2)	3.59	523,066
Equity Compensation Plans Not			
Approved by Security Holders	-	-	-
	814,025	\$ 3.60	523,066

(1)

Includes 2,500 shares of the Company's Common Stock and 2,500 shares of the Company's Series I Preferred Stock to be issued upon the exercise of outstanding options granted pursuant to the Company's 1997 Employee and Director Stock Plan (1997 Plan). Options granted under the 1997 Plan are exercisable for one share of Common Stock and one share of Series I Preferred Stock. The Company does not currently intend to grant any additional options under the 1997 Plan.

(2)

Options granted under the 2002 Employee, Director and Consultant Stock Plan are exercisable for one share of the Company's Common Stock.

ITEM 6. SELECTED FINANCIAL DATA

The selected consolidated financial data presented below should be read in conjunction with the Consolidated Financial Statements of the Company, together with the Notes to Consolidated Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this report.

SELECTED CONSOLIDATED FINANCIAL DATA (1) (2)

(AMOUNTS IN MILLIONS, EXCEPT PER SHARE DATA)

	2005	2004	2003	2002	2001
Consolidated Statements of Earnings Data:					
Net sales	\$ 188.8	\$ 175.1	\$ 163.2	\$ 165.9	\$ 162.0
Cost of sales	117.2	109.6	101.9	107.0	105.5
Gross profit	71.6	65.5	61.3	58.9	56.5
Selling and administrative expense	43.6	41.2	39.5	40.6	39.3
Earnings from operations	28.0	24.3	21.8		