
**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 March 31, 2014

OR

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: 1-11961

CARRIAGE SERVICES, INC.

(Exact name of registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of
incorporation or organization)

76-0423828
(I.R.S. Employer
Identification No.)

3040 Post Oak Boulevard, Suite 300
Houston, Texas, 77056
(Address of principal executive offices)
(713) 332-8400
(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Securities Exchange Act of 1934.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company	<input type="checkbox"/>

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

The number of shares of the registrant's Common Stock, \$.01 par value per share, outstanding as of May 5, 2014 was 18,480,253.

CARRIAGE SERVICES, INC.

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PART I – FINANCIAL INFORMATION
Item 1. Financial Statements

CARRIAGE SERVICES, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

	December 31, 2013	(unaudited) March 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 1,377	\$ 21,958
Accounts receivable, net of allowance for bad debts of \$847 in 2013 and \$917 in 2014	17,950	17,715
Assets held for sale	3,544	—
Inventories	5,300	5,348
Prepaid expenses	4,421	4,387
Other current assets	3,525	1,754
Total current assets	36,117	51,162
Preneed cemetery trust investments	68,341	69,475
Preneed funeral trust investments	97,144	100,204
Preneed receivables, net of allowance for bad debts of \$1,825 in 2013 and \$1,887 in 2014	24,521	24,282
Receivables from preneed trusts	11,166	11,738
Property, plant and equipment, net of accumulated depreciation of \$88,627 in 2013 and \$90,250 in 2014	160,690	161,829
Cemetery property	72,911	72,852
Goodwill	221,087	220,945
Deferred charges and other non-current assets	12,280	13,416
Cemetery perpetual care trust investments	42,342	43,529
Total assets	\$ 746,599	\$ 769,432
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of senior long-term debt and capital lease obligations	\$ 13,424	\$ 14,078
Accounts payable	7,046	5,231
Other liabilities	9,939	9,350
Accrued liabilities	12,854	12,558
Liabilities associated with assets held for sale	4,357	—
Total current liabilities	47,620	41,217
Long-term debt, net of current portion	105,642	101,783
Revolving credit facility	36,900	—
Convertible junior subordinated debentures due in 2029 to an affiliate	89,770	27,860
Convertible subordinated notes due 2021	—	112,261
Obligations under capital leases, net of current portion	3,786	1,343
Deferred preneed cemetery revenue	55,479	55,019
Deferred preneed funeral revenue	30,588	31,102
Deferred tax liability	11,915	18,290
Other long-term liabilities	1,548	1,612
Deferred preneed cemetery receipts held in trust	68,341	69,475
Deferred preneed funeral receipts held in trust	97,144	100,204
Care trusts' corpus	41,893	43,566
Total liabilities	590,626	603,732
Commitments and contingencies:		
Stockholders' equity:		
Common stock, \$.01 par value; 80,000,000 shares authorized; 22,183,000 and 22,408,000 shares issued at December 31, 2013 and March 31, 2014, respectively	222	224
Additional paid-in capital	204,324	211,831
Accumulated deficit	(33,306)	(31,088)
Treasury stock, at cost; 3,922,000 shares at December 31, 2013 and March 31, 2014	(15,267)	(15,267)
Total stockholders' equity	155,973	165,700
Total liabilities and stockholders' equity	\$ 746,599	\$ 769,432

The accompanying condensed notes are an integral part of these Consolidated Financial Statements.

CARRIAGE SERVICES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited and in thousands, except per share data)

	For the Three Months Ended March 31,	
	2013	2014
Revenues:		
Funeral	\$ 45,051	\$ 44,159
Cemetery	12,264	11,688
	<u>57,315</u>	<u>55,847</u>
Field costs and expenses:		
Funeral	26,352	26,039
Cemetery	6,815	6,960
Depreciation and amortization	2,476	2,422
Regional and unallocated funeral and cemetery costs	2,759	2,379
	<u>38,402</u>	<u>37,800</u>
Gross profit	18,913	18,047
Corporate costs and expenses:		
General and administrative costs and expenses	6,282	9,335
Home office depreciation and amortization	347	342
	<u>6,629</u>	<u>9,677</u>
Operating income	12,284	8,370
Interest expense	(2,595)	(2,845)
Accretion of discount on convertible subordinated notes	—	(171)
Loss on redemption of convertible junior subordinated debentures	—	(3,778)
Other income	—	1,130
Income from continuing operations before income taxes	9,689	2,706
Provision for income taxes	(4,280)	(1,055)
Net income from continuing operations	5,409	1,651
Income (loss) from discontinued operations, net of tax	(151)	567
Net income	5,258	2,218
Preferred stock dividend	(4)	—
Net income available to common stockholders	<u>\$ 5,254</u>	<u>\$ 2,218</u>
Basic earnings (loss) per common share:		
Continuing operations	\$ 0.30	\$ 0.09
Discontinued operations	(0.01)	0.03
Basic earnings per common share	<u>\$ 0.29</u>	<u>\$ 0.12</u>
Diluted earnings (loss) per common share:		
Continuing operations	\$ 0.26	\$ 0.09
Discontinued operations	(0.01)	0.03
Diluted earnings per common share	<u>\$ 0.25</u>	<u>\$ 0.12</u>
Dividends declared per common share	<u>\$ 0.025</u>	<u>\$ 0.025</u>
Weighted average number of common and common equivalent shares outstanding:		
Basic	<u>17,657</u>	<u>17,984</u>
Diluted	<u>22,246</u>	<u>18,143</u>

The accompanying condensed notes are an integral part of these Consolidated Financial Statements.

CARRIAGE SERVICES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited and in thousands)

	For the Three Months Ended March	
	31,	
	2013	2014
Cash flows from operating activities:		
Net income	\$ 5,258	\$ 2,218
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Loss (gain) on sale / purchase of businesses and other assets	389	(2,039)
Impairment of goodwill	100	—
Depreciation and amortization	2,848	2,764
Amortization of deferred financing costs	(638)	232
Accretion of debt discount on convertible subordinated notes	—	171
Provision for losses on accounts receivable	456	700
Stock-based compensation expense	646	1,491
Deferred income taxes	1,354	(4,780)
Loss on redemption of convertible junior subordinated debentures	—	2,932
Other	(34)	(3)
Changes in operating assets and liabilities that provided (required) cash:		
Accounts and preneed receivables	(1,904)	(245)
Inventories and other current assets	478	299
Deferred charges and other	21	(318)
Preneed funeral and cemetery trust investments	1,410	(5,258)
Accounts payable	(874)	(2,566)
Accrued and other liabilities	(280)	(2,387)
Deferred preneed funeral and cemetery revenue	2,617	(37)
Deferred preneed funeral and cemetery receipts held in trust	(1,934)	5,208
Net cash provided by (used in) operating activities	9,913	(1,618)
Cash flows from investing activities:		
Acquisitions and new construction	(6,051)	—
Net proceeds from the sale of businesses and other assets	2,011	200
Capital expenditures	(2,602)	(5,048)
Net cash used in investing activities	(6,642)	(4,848)
Cash flows from financing activities:		
Net payments on the revolving credit facility	(1,700)	(36,900)
Payments on term loan	(2,500)	(3,000)
Proceeds from the issuance of convertible subordinated notes	—	143,750
Payment of debt issuance costs related to the convertible subordinated notes	—	(4,355)
Payments on other long-term debt and obligations under capital leases	(168)	(185)
Redemption of convertible junior subordinated debentures	—	(61,905)
Payments for performance-based stock awards	—	(16,150)
Proceeds from the exercise of stock options and employee stock purchase plan contributions	318	652
Dividends on common stock	(452)	(456)
Dividend on redeemable preferred stock	(4)	—
Payment of loan origination costs	(98)	—
Excess tax benefit of equity compensation	925	5,596
Net cash provided by (used in) financing activities	(3,679)	27,047
Net increase (decrease) in cash and cash equivalents	(408)	20,581
Cash and cash equivalents at beginning of period	1,698	1,377
Cash and cash equivalents at end of period	\$ 1,290	\$ 21,958

The accompanying condensed notes are an integral part of these Consolidated Financial Statements.

CARRIAGE SERVICES, INC.

**CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)**

1. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company

Carriage Services, Inc. (“Carriage”, the “Company”, “we”, “us” or “our”) is a leading provider of deathcare services and merchandise in the United States. As of March 31, 2014, we operated 161 funeral homes in 26 states and 31 cemeteries in 10 states.

Our operations are reported in two business segments: Funeral Home Operations and Cemetery Operations. Funeral homes are principally service businesses that provide funeral services (traditional burial and cremation) and sell related merchandise, such as caskets and urns. Cemeteries are primarily sales businesses providing interment rights (grave sites and mausoleums) and related merchandise, such as markers and memorials.

Principles of Consolidation

The accompanying Consolidated Financial Statements include us and our subsidiaries. All significant intercompany balances and transactions have been eliminated.

Interim Condensed Disclosures

The information for the three month periods ended March 31, 2013 and 2014 is unaudited, but in the opinion of management, reflects all adjustments which are normal, recurring and necessary for a fair presentation of our financial position and results of operations as of and for the interim periods presented. Certain information and footnote disclosures normally included in annual financial statements have been condensed or omitted. The accompanying Consolidated Financial Statements have been prepared consistent with the accounting policies described in our Annual Report on Form 10-K for the year ended December 31, 2013 and should be read in conjunction therewith.

Cash and Cash Equivalents

We consider all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Use of Estimates

The preparation of our Consolidated Financial Statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an ongoing basis, we evaluate our estimates and judgments, including those related to revenue recognition, realization of accounts receivable, goodwill, intangible assets, property and equipment and deferred tax assets and liabilities. We base our estimates on historical experience, third party data and assumptions that we believe to be reasonable under the circumstances. The results of these considerations form the basis for making judgments about the amount and timing of revenues and expenses, the carrying value of assets and the recorded amounts of liabilities. Actual results may differ from these estimates and such estimates may change if the underlying conditions or assumptions change. Historical performance should not be viewed as indicative of future performance, as there can be no assurance that our results of operations will be consistent from year to year.

Funeral and Cemetery Operations

We record the revenue from sales of funeral and cemetery merchandise and services when the merchandise is delivered or the service is performed. Sales of cemetery interment rights are recorded as revenue in accordance with the retail land sales provisions for accounting for sales of real estate. This method provides for the recognition of revenue in the period in which the customer’s cumulative payments exceed 10% of the contract price related to the interment right. Costs related to the sales of interment rights, which include real property and other costs related to cemetery development activities, are charged to operations using the specific identification method in the period in which the sale of the interment right is recognized as revenue. Revenues to be recognized from the delivery of merchandise and performance of services related to contracts that were acquired in acquisitions are typically lower than those originated by the Company. Sales taxes collected are recognized on a net basis in our Consolidated Financial Statements.

Allowances for bad debts and customer cancellations are provided at the date that the sale is recognized as revenue and are based on our historical experience and the current economic environment. We also monitor changes in delinquency rates

and provide additional bad debt and cancellation reserves when warranted. When preneed sales of funeral services and merchandise are funded through third-party insurance policies, we earn a commission on the sale of the policies. Insurance commissions are recognized as revenues at the point at which the commission is no longer subject to refund, which is typically one year after the policy is issued.

Accounts receivable included approximately \$8.4 million of funeral receivables at December 31, 2013 and March 31, 2014 and \$8.3 million and \$9.1 million of cemetery receivables at December 31, 2013 and March 31, 2014, respectively. Non-current preneed receivables represent the payments expected to be received beyond one year from the balance sheet date. Non-current preneed receivables consisted of approximately \$8.1 million of funeral receivables at December 31, 2013 and March 31, 2014 and \$16.5 million and \$16.2 million of cemetery receivables at December 31, 2013 and March 31, 2014, respectively. Accounts receivable also include minor amounts of other receivables. Bad debt expense totaled \$0.5 million and \$0.7 million for the three months ended March 31, 2013 and 2014, respectively.

Property, Plant and Equipment

Property, plant and equipment (including equipment under capital leases) are stated at cost. The costs of ordinary maintenance and repairs are charged to operations as incurred, while renewals and betterments are capitalized. Depreciation of property, plant and equipment (including equipment under capital leases) is computed based on the straight-line method.

Property, plant and equipment was comprised of the following at December 31, 2013 and March 31, 2014:

	December 31, 2013	March 31, 2014
	(in thousands)	
Land	\$ 55,639	\$ 56,890
Buildings and improvements	132,172	133,196
Furniture, equipment and automobiles	61,506	61,993
Property, plant and equipment, at cost	249,317	252,079
Less: accumulated depreciation	(88,627)	(90,250)
Property, plant and equipment, net	<u>\$ 160,690</u>	<u>\$ 161,829</u>

During the three months ended March 31, 2014, we purchased two buildings which we had previously leased. We recognized a gain of approximately \$1.1 million on the purchase of one of these buildings that we had originally acquired under a capital lease. We recorded approximately \$2.2 million of depreciation expense against operating income for the three months ended March 31, 2013 and 2014.

Discontinued Operations

In accordance with our Strategic Acquisition Model, non-strategic businesses are reviewed to determine whether such businesses should be sold and the proceeds redeployed elsewhere. When we receive a letter of intent and financing commitment from a buyer and the sale is expected to occur within one year, the location is no longer reported within our continuing operations. The assets and liabilities associated with the location are reclassified as held-for-sale on our Consolidated Balance Sheets, and the operating results are presented on a comparative basis in the discontinued operations section of our Consolidated Statements of Operations. During the first quarter of 2014, we sold a cemetery in Florida which was reported as held-for-sale at December 31, 2013. As of March 31, 2014, we had no businesses classified as held-for-sale. See Note 4 and Note 22 to the Consolidated Financial Statements herein for more information.

Business Combinations

Tangible and intangible assets acquired and liabilities assumed are recorded at fair value and goodwill is recognized for any difference between the price of the acquisition and fair value. We customarily estimate related transaction costs known at closing. To the extent that information not available to us at the closing date of an acquisition subsequently becomes available during the allocation period, we may adjust goodwill, assets or liabilities associated with such acquisition. Acquisition related costs are recognized separately from acquisitions and are expensed as incurred. There were no acquisitions of businesses in the first quarter of 2014. See Note 3 to the Consolidated Financial Statements herein for more information.

Goodwill

The excess of the purchase price over the fair value of identifiable net assets of funeral home businesses acquired is recorded as goodwill. Goodwill has primarily been recorded in connection with the acquisition of funeral businesses. Goodwill is tested for impairment by assessing the fair value of each of our reporting units. The funeral segment reporting units consist of

our East, Central and West regions in the United States, and we perform our annual impairment test of goodwill using information as of August 31 of each year. In addition, we assess the impairment of goodwill whenever events or changes in circumstances indicate that the carrying value may be greater than fair value. Factors that could trigger an interim impairment review include, but are not limited to, significant adverse changes in the business climate which may be indicated by a decline in our market capitalization or decline in operating results.

Our methodology for goodwill impairment testing is described in more detail in Notes 1 and 4 to the Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2013 and further discussion of current period activity in Note 5 to the Consolidated Financial Statements herein.

Intangible Assets

Our intangible assets include tradenames primarily resulting from acquisitions. Our tradenames are included in *Deferred charges and other non-current assets* on our Consolidated Balance Sheets. Our tradenames are considered to have an indefinite life and are not subject to amortization. We test for impairment of intangible assets annually at year end in accordance with the Intangibles Topic of the Accounting Standards Codification (“ASC”) 350.

In addition to our annual review, we assess the impairment of intangible assets whenever events or changes in circumstances indicate that the carrying value may be greater than the fair value. Factors that could trigger an interim impairment review include, but are not limited to, significant under performance relative to historical results and significant negative industry or economic trends.

Stock Plans and Stock-Based Compensation

We have stock-based employee and director compensation plans under which we may grant restricted stock, stock options, performance awards and stock from our employee stock purchase plan, which are described in more detail in Note 17 to the Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2013. We recognize compensation expense in an amount equal to the fair value of the share-based awards expected to vest over the requisite service period. Fair value is determined on the date of the grant. The fair value of options or awards containing options is determined using the Black-Scholes valuation model. The fair value of the performance awards is determined using a Monte-Carlo simulation pricing model. See Note 17 to the Consolidated Financial Statements herein for additional information on our stock-based compensation plans.

Computation of Earnings Per Common Share

Basic earnings per share is computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common and dilutive common equivalent shares outstanding during the period. Dilutive common equivalent shares consist of stock options, convertible junior subordinated debentures and convertible subordinated notes.

Share-based awards that contain nonforfeitable rights to dividends or dividend equivalents, whether paid or unpaid, are recognized as participating securities and included in the computation of both basic and diluted earnings per share. Our grants of restricted stock awards to our employees and directors are considered participating securities, and we have prepared our earnings per share calculations attributable to common stockholders to exclude outstanding unvested restricted stock awards, using the two-class method, in both the basic and diluted weighted average shares outstanding calculation.

The fully diluted weighted average shares outstanding for the three months ended March 31, 2013, and the corresponding calculation of fully diluted earnings per share, include approximately 4.4 million shares that would be issued upon conversion of our convertible junior subordinated debentures as a result of the application of the if-converted method prescribed by the Financial Accounting Standards Board (“FASB”) ASC 260-10-45. For the three months ended March 31, 2014, shares from the conversion of our convertible junior subordinated debentures and our convertible subordinated notes are excluded from the fully diluted earnings per share calculation because the inclusion of such converted shares would result in an antidilutive impact.

Preneed Funeral and Cemetery Trust Funds

Our preneed and perpetual care trust funds are reported in accordance with the principles of consolidating Variable Interest Entities (“VIEs”). In the case of preneed trusts, the customers are the legal beneficiaries. In the case of perpetual care trusts, we do not have a right to access the corpus in the perpetual care trusts. For these reasons, we have recognized financial interests of third parties in the trust funds in our financial statements as *Deferred preneed funeral and cemetery receipts held in trust* and *Care trusts’ corpus*. The investments of such trust funds are classified as available-for-sale and are reported at fair market value; therefore, the unrealized gains and losses, as well as accumulated and undistributed income and realized gains

and losses are recorded to *Deferred preneed funeral and cemetery receipts held in trust* and *Care trusts' corpus* on our Consolidated Balance Sheets. Our future obligations to deliver merchandise and services are reported at estimated settlement amounts. Preneed funeral and cemetery trust investments are reduced by the trust investment earnings that we have been allowed to withdraw in certain states prior to maturity. These earnings, along with preneed contract collections not required to be placed in trust, are recorded in *Deferred preneed funeral revenue* and *Deferred preneed cemetery revenue* until the service is performed or the merchandise is delivered.

In accordance with respective state laws, we are required to deposit a specified amount into perpetual and memorial care trust funds for each interment/entombment right and certain memorials sold. Income from the trust funds is distributed to us and used to provide care and maintenance of the cemeteries and mausoleums. Such trust fund income is recognized as revenue when realized by the trust and distributable to us. We are restricted from withdrawing any of the principal balances of these funds.

An enterprise is required to perform an analysis to determine whether the enterprise's variable interest(s) give it a controlling financial interest in a VIE. This analysis identifies the primary beneficiary of a VIE as the enterprise that has both the power to direct the activities of a VIE that most significantly impact the entity's economic performance and the obligation to absorb losses of the entity that could potentially be significant to the VIE, or the right to receive benefits from the entity that could potentially be significant to the VIE. Our analysis continues to support our position as the primary beneficiary in the majority of our funeral and cemetery trust funds.

Trust management fees are earned by us for investment management and advisory services that are provided by our wholly-owned registered investment advisor ("CSV RIA"). As of March 31, 2014, CSV RIA provided these services to two institutions, which have custody of 76% of our trust assets, for a fee based on the market value of trust assets. Under state trust laws, we are allowed to charge the trust a fee for advising on the investment of the trust assets and these fees are recognized as income in the period in which services are provided.

Fair Value Measurements

We define fair value as the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). We disclose the extent to which fair value is used to measure financial assets and liabilities, the inputs utilized in calculating valuation measurements, and the effect of the measurement of significant unobservable inputs on earnings, or changes in net assets, as of the measurement date. Additional required disclosures are provided in Notes 6, 10 and 11 to the Consolidated Financial Statements herein. We currently do not have any assets that have fair values determined by Level 3 inputs and no liabilities measured at fair value. We have not elected to measure any additional financial instruments and certain other items at fair value that are not currently required to be measured at fair value.

To determine the fair value of assets and liabilities in an environment where the volume and level of activity for the asset or liability have significantly decreased, the exit price is used as the fair value measurement. For the three months ended March 31, 2014, we did not incur significant decreases in the volume or level of activity of any asset or liability. We consider an impairment of debt and equity securities other-than-temporary unless (a) the investor has the ability and intent to hold an investment and (b) evidence indicating the cost of the investment is recoverable before we are more likely than not required to sell the investment. If impairment is indicated, then an adjustment is made to reduce the carrying amount to fair value. As of March 31, 2014, no impairments have been identified.

In the ordinary course of business, we are typically exposed to a variety of market risks. Currently, these are primarily related to changes in fair market values related to outstanding debts and changes in the values of securities associated with the preneed and perpetual care trusts. Management is actively involved in monitoring exposure to market risk and developing and utilizing risk management techniques when appropriate and when available for a reasonable price.

Our convertible junior subordinated debentures, payable to Carriage Services Capital Trust (the "Trust"), pay interest at a fixed rate of 7% and are carried on our Consolidated Balance Sheets at a cost of approximately \$27.9 million. The fair value of these securities is estimated to be approximately \$28.0 million at March 31, 2014, based on Bloomberg Finance L.P.'s quotes for the corresponding preferred securities issued by the Trust. Our convertible subordinated notes due 2021, issued in March 2014, pay interest at a fixed rate of 2.75% and are carried on our Consolidated Balance Sheet at a carrying value of approximately \$112.3 million. The fair value of these securities is estimated to be approximately \$151.7 million based on the last traded or broker quoted price.

Income Taxes

We and our subsidiaries file a consolidated U.S. Federal income tax return, separate income tax returns in 16 states in which we operate and combined or unitary income tax returns in 11 states in which we operate. We record deferred taxes for temporary differences between the tax basis and financial reporting basis of assets and liabilities. We record a valuation allowance to reflect the estimated amount of deferred tax assets for which realization is uncertain. Management reviews the valuation allowance at the end of each quarter and makes adjustments if it is determined that it is more likely than not that the tax benefits will be realized.

We analyze tax benefits for uncertain tax positions and how they are to be recognized, measured, and derecognized in financial statements; provide certain disclosures of uncertain tax matters; and specify how reserves for uncertain tax positions should be classified on our Consolidated Balance Sheets. We have reviewed our income tax positions and identified certain tax deductions, primarily related to business acquisitions that are not certain. Our policy with respect to potential penalties and interest is to record them as "Other" expense and "Interest" expense, respectively. The entire balance of unrecognized tax benefits, if recognized, would affect our effective tax rate.

We do not anticipate a significant increase or decrease in unrecognized tax benefits during the next twelve months.

In September 2013, the U.S. Department of the Treasury and the Internal Revenue Service released final regulations relating to guidance on applying tax rules to amounts paid to acquire, produce or improve tangible personal property as well as rules for materials and supplies. The new guidance is required to be applied no later than our tax year beginning January 1, 2014. These regulations are not expected to have a material impact on our financial statements.

Subsequent Events

Management evaluated events and transactions during the period subsequent to March 31, 2014 through the date the financial statements were issued for potential recognition or disclosure in the accompanying financial statements covered by this report. For more information regarding subsequent events, see Note 22 to the Consolidated Financial Statements herein.

2. RECENTLY ISSUED ACCOUNTING STANDARDS

Discontinued Operations and Disclosure of Disposals of Components of an Entity

In April 2014, the FASB modified the requirements for reporting a discontinued operation. The amended definition of "discontinued operations" includes only disposals or held-for-sale classifications for components or groups of components of an entity that represent a strategic shift that either has or will have a major effect on the entity's operations or financial results. Examples of a strategic shift that has or will have a major effect on an entity's operations and financial results include a disposal of a major geographical area, line of business, equity method of investment or other parts of an entity. The new definition of discontinued operations will significantly reduce the volume of transactions requiring discontinued operations presentation and disclosure. However, the new guidance also expands the disclosures required when an entity reports a discontinued operation or when it disposes of or classifies as held-for-sale an individually significant component that does not meet the definition of a discontinued operation. The new guidance is effective for all disposals or classifications as held-for-sale that occur in annual periods, and interim periods within those annual periods, beginning after December 15, 2014. An entity cannot apply the amended guidance to a component or to a business that is classified as held-for-sale before the effective date, even if the component or business is disposed of after the effective date. Early adoption is permitted, but only for disposals or classifications as held-for-sale that have not been reported in previously issued financial statements. We are currently evaluating the impact the adoption of this new guidance will have on our Consolidated Financial Statements.

Income Taxes

In July 2013, the FASB amended the Income Tax Topic of the ASC to eliminate the diversity in practice in the presentation of unrecognized tax benefits. The guidance requires an entity to net its liability for unrecognized tax benefits against the deferred tax assets for all same jurisdiction net operating losses or similar tax loss carryforwards or tax credit carryforwards. A gross presentation will be required only if such carryforwards are not available to settle any additional income taxes resulting from disallowance of the uncertain tax position or the entity does not intend to use these carryforwards for this purpose. This guidance is effective for the first annual or interim period beginning after December 15, 2013, thus effective for us beginning January 1, 2014. Our adoption of this new guidance effective January 1, 2014 did not have a material impact on our financial position or results of operations.

3. ACQUISITIONS

Our growth strategy includes the execution of our Strategic Acquisition Model. We assess acquisition candidates using six strategic ranking criteria to differentiate the price we are willing to pay under a discounted cash flow methodology. Those criteria are:

- size of business;
- size of market;
- competitive standing;
- local market demographics;
- strength of brand; and
- barriers to entry.

There were no business acquisitions during the first quarter of 2014. We acquired land for approximately \$6.0 million during the first quarter of 2013 for funeral home expansion projects.

On March 3, 2014, certain of our subsidiaries entered into an Asset Sale Agreement with certain subsidiaries of Service Corporation International (“SCI”) to acquire four funeral businesses and one cemetery business in the New Orleans, Louisiana region and two funeral businesses in the Northern Virginia region for an aggregate purchase price of approximately \$54.9 million (the “SCI Acquisition”). Under the Asset Sale Agreement, we will acquire the properties, leasehold interests, assets and rights and assume certain liabilities of the businesses being acquired. The closing of the SCI Acquisition is subject to certain customary closing conditions, including, but not limited to, approval by the Federal Trade Commission. We currently anticipate that the SCI Acquisition will close in the second quarter of 2014.

4. ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS

We continually review locations to optimize the sustainable earning power and return on our invested capital. Our strategy, the Strategic Portfolio Optimization Model, also uses strategic ranking criteria to assess potential disposition candidates. The execution of this strategy entails selling generally non-strategic businesses.

During the first quarter of 2014, we sold a cemetery in Florida which was reported as held-for-sale at December 31, 2013 for approximately \$0.2 million in cash.

As of March 31, 2014, we had no assets classified as held-for-sale. Assets and liabilities associated with the businesses held-for-sale on our Consolidated Balance Sheets at December 31, 2013 consisted of the following (in thousands):

	December 31, 2013
Assets:	
Current assets	\$ 30
Preneed cemetery trust investments	2,477
Preneed receivables	31
Property, plant and equipment, net	311
Cemetery perpetual care trust investments	695
Total	\$ 3,544
Liabilities:	
Current liabilities	\$ 10
Deferred preneed cemetery revenue	1,185
Deferred preneed cemetery receipts held in trust	2,477
Care trusts corpus	685
Total	\$ 4,357

The operating results of the discontinued businesses for the three months ended March 31, 2013 and 2014, as well as the gain or loss on the disposal, is presented in the discontinued operations section of the Consolidated Statements of Operations, along with the income tax effect, as follows (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Revenues	\$ 1,432	\$ 51
Operating income	\$ 338	\$ 20
Gain (loss) on disposition	(583)	909
Income tax benefit (provision)	94	(362)
Income (loss) from discontinued operations	<u>\$ (151)</u>	<u>\$ 567</u>

5. GOODWILL

Many of the former owners and staff of acquired funeral homes and certain cemeteries have provided high quality service to families for generations. The resulting loyalty often represents a substantial portion of the value of a business. The excess of the purchase price over the fair value of net identifiable assets acquired and liabilities assumed, as determined by management in business acquisition transactions accounted for as purchases, is recorded as goodwill.

The following table presents the changes in goodwill on our Consolidated Balance Sheets (in thousands):

Goodwill as of December 31, 2013	\$ 221,087
Adjustments	(142)
Reclassification of assets held-for-sale	—
Goodwill as of March 31, 2014	<u>\$ 220,945</u>

The adjustment to goodwill in the three months ended March 31, 2014 represents a purchase price allocation adjustment related to a funeral home business acquisition completed in November 2013. Our purchase price allocation for this acquisition is dependent upon certain valuations, which have not progressed to a stage where there is sufficient information to make a definitive measure and allocation of goodwill and other intangible assets. Material revisions to the ongoing current estimates may be necessary when the valuation process is completed, within a year after the closing date of the acquisition.

6. PRENEED TRUST INVESTMENT

Preneed Cemetery Trust Investments

Preneed cemetery trust investments represent trust fund assets that we are generally permitted to withdraw when the merchandise or services are provided. The components of *Preneed cemetery trust investments* on our Consolidated Balance Sheets at December 31, 2013 and March 31, 2014 are as follows (in thousands):

	December 31, 2013	March 31, 2014
Preneed cemetery trust investments, at fair value	\$ 70,386	\$ 71,510
Less: allowance for contract cancellation	(2,045)	(2,035)
Preneed cemetery trust investments, net	<u>\$ 68,341</u>	<u>\$ 69,475</u>

Upon cancellation of a preneed cemetery contract, a customer is generally entitled to receive a refund of the corpus, and in some cases, some or all of the earnings held in trust. In certain jurisdictions, we are obligated to fund any shortfall if the amounts deposited by the customer exceed the funds in trust, including some or all investment income. As a result, when realized or unrealized losses of a trust result in the trust being under-funded, we assess whether we are responsible for replenishing the corpus of the trust, in which case a loss provision is recorded.

Earnings from our preneed cemetery trust investments are recognized in revenue when a service is performed or merchandise is delivered. Trust management fees charged by our wholly-owned registered investment advisor are included in revenue in the period in which they are earned.

Where quoted prices are available in an active market, investments held by the trusts are classified as Level 1 investments pursuant to the three-level valuation hierarchy. Our Level 1 investments include cash and common stock. Where quoted market prices are not available for the specific security, fair values are estimated by using quoted prices of similar securities in active markets or other inputs other than quoted prices that can corroborate observable market data. These investments are fixed income securities including foreign debt, corporate debt, preferred stocks and mortgage backed securities, all of which are classified within Level 2 of the valuation hierarchy. We review and update our fair value hierarchy classifications quarterly. There were no transfers between Levels 1 and 2 for the three months ended March 31, 2014. There are no Level 3 investments in the preneed cemetery trust investment portfolio. See Note 11 for further information of the fair value measurement and the three-level valuation hierarchy.

The cost and fair market values associated with preneed cemetery trust investments at March 31, 2014 are detailed below (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 910	\$ —	\$ —	\$ 910
Fixed income securities:					
Foreign debt	2	3,938	247	(5)	4,180
Corporate debt	2	30,699	524	(1,385)	29,838
Preferred stock	2	18,475	612	(142)	18,945
Mortgage backed securities	2	1	—	—	1
Common stock	1	13,810	3,378	(585)	16,603
Trust securities		\$ 67,833	\$ 4,761	\$ (2,117)	\$ 70,477
Accrued investment income		\$ 1,033			\$ 1,033
Preneed cemetery trust investments					\$ 71,510
Fair market value as a percentage of cost					103.9%

The estimated maturities of the fixed income securities included above are as follows (in thousands):

Due in one year or less	\$ —
Due in one to five years	6,364
Due in five to ten years	9,873
Thereafter	36,727
Total	\$ 52,964

The cost and fair market values associated with preneed cemetery trust investments at December 31, 2013 are detailed below (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 1,541	\$ —	\$ —	\$ 1,541
Fixed income securities:					
Foreign debt	2	3,460	146	(3)	3,603
Corporate debt	2	32,958	386	(1,150)	32,194
Preferred stock	2	17,754	178	(273)	17,659
Mortgage backed securities	2	1	—	—	1
Common stock	1	12,431	2,362	(267)	14,526
Trust securities		\$ 68,145	\$ 3,072	\$ (1,693)	\$ 69,524
Accrued investment income		\$ 862			\$ 862
Preneed cemetery trust investments					\$ 70,386
Market value as a percentage of cost					102.0%

We determine whether or not the assets in the preneed cemetery trust investments have an other-than-temporary impairment on a security-by-security basis. This assessment is made based upon a number of criteria including the length of

time a security has been in a loss position, changes in market conditions and concerns related to the specific issuer. If a loss is considered to be other-than-temporary, the cost basis of the security is adjusted downward to its fair market value. Any reduction in the cost basis of the investment due to an other-than-temporary impairment is likewise recorded as a reduction in *Deferred preneed cemetery receipts held in trust* on our Consolidated Balance Sheets. There will be no impact on earnings unless and until such time as the investment is withdrawn from the trust in accordance with state regulations at an amount that is less than its original basis.

We have determined that the unrealized losses in our preneed cemetery trust investments are considered temporary in nature, as the unrealized losses were due to temporary fluctuations in interest rates and equity prices. The investments are diversified across multiple industry segments using a balanced allocation strategy to minimize long-term risk. At March 31, 2014, we had corporate debt and equity investments within our preneed cemetery trust investments that had tax lots in loss positions for more than one year. Based on our analyses of these securities, the companies' businesses and current market conditions, we determined that these investment losses were temporary in nature. Our cemetery merchandise and service trust investment unrealized losses, their associated fair market values, and the duration of unrealized losses as of March 31, 2014 and December 31, 2013, are shown in the following tables (in thousands):

	March 31, 2014					
	In Loss Position Less than 12 months		In Loss Position Greater than 12 months		Total	
	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses
Fixed income securities:						
Foreign debt	\$ 433	\$ (5)	\$ —	\$ —	\$ 433	\$ (5)
Corporate debt	5,994	(598)	2,860	(787)	8,854	(1,385)
Preferred stock	4,959	(142)	—	—	4,959	(142)
Common stock	2,850	(570)	98	(15)	2,948	(585)
Total temporary impaired securities	\$ 14,236	\$ (1,315)	\$ 2,958	\$ (802)	\$ 17,194	\$ (2,117)

	December 31, 2013					
	In Loss Position Less than 12 months		In Loss Position Greater than 12 months		Total	
	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses
Fixed income securities:						
Foreign debt	\$ 802	\$ (3)	\$ —	\$ —	\$ 802	\$ (3)
Corporate debt	11,561	(553)	769	(597)	12,330	(1,150)
Preferred stock	9,601	(273)	—	—	9,601	(273)
Common stock	1,077	(171)	705	(96)	1,782	(267)
Total temporary impaired securities	\$ 23,041	\$ (1,000)	\$ 1,474	\$ (693)	\$ 24,515	\$ (1,693)

Preneed cemetery trust investment security transactions recorded in *Interest expense* in our Consolidated Statements of Operations for the three months ended March 31, 2013 and 2014 were as follows (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Investment income	\$ 693	\$ 543
Realized gains	38	539
Realized losses	(430)	(188)
Expenses and taxes	(381)	(558)
Increase (decrease) in deferred preneed cemetery receipts held in trust	80	(336)
	\$ —	\$ —

Purchases and sales of investments in the preneed cemetery trusts were as follows (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Purchases	\$ (4,161)	\$ (8,160)
Sales	5,009	8,537

Preneed Funeral Trust Investments

Preneed funeral trust investments represent trust fund assets that we are permitted to withdraw as services and merchandise are provided to customers. Preneed funeral contracts are secured by funds paid by the customer to us. Preneed funeral trust investments are reduced by the trust earnings we have been allowed to withdraw prior to our performance and amounts received from customers that are not required to be deposited into trust, pursuant to various state laws. The components of *Preneed funeral trust investments* on our Consolidated Balance Sheets at December 31, 2013 and March 31, 2014 were as follows (in thousands):

	December 31, 2013	March 31, 2014
Preneed funeral trust investments, at market value	\$ 100,005	\$ 103,104
Less: allowance for contract cancellation	(2,861)	(2,900)
Preneed funeral trust investments, net	<u>\$ 97,144</u>	<u>\$ 100,204</u>

Upon cancellation of a preneed funeral contract, a customer is generally entitled to receive a refund of the corpus and some or all of the earnings held in trust. In certain jurisdictions, we are obligated to fund any shortfall if the amounts deposited by the customer exceed the funds in trust, including some or all investment income. As a result, when realized or unrealized losses of a trust result in the trust being under-funded, we assess whether we are responsible for replenishing the corpus of the trust, in which case a loss provision is recorded.

Earnings from our preneed funeral trust investments are recognized in revenue when a service is performed or merchandise is delivered. Trust management fees charged by our wholly-owned registered investment advisor are included in revenue in the period in which they are earned.

Where quoted prices are available in an active market, investments held by the trusts are classified as Level 1 investments pursuant to the three-level valuation hierarchy. Our Level 1 investments include cash, U. S. treasury debt, common stock and equity mutual funds. Where quoted market prices are not available for the specific security, then fair values are estimated by using quoted prices of similar securities in active markets or other inputs other than quoted prices that can corroborate observable market data. These investments are fixed income securities including U.S. agency obligations, foreign debt, corporate debt, preferred stocks, mortgage backed securities and fixed income mutual funds and other investments, all of which are classified within Level 2 of the valuation hierarchy. We review and update our fair value hierarchy classifications quarterly. During the three months ended March 31, 2014, we reclassified \$0.4 million of U.S. Agency obligations from Level 1 investments to Level 2 investments due to reduced trading activity of these securities which caused the fair market price to be determined by other inputs other than quoted prices. There are no Level 3 investments in the preneed funeral trust investment portfolio. See Note 11 for further information of the fair value measurement and the three-level valuation hierarchy.

The cost and fair market values associated with preneed funeral trust investments at March 31, 2014 are detailed below (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 14,531	\$ —	\$ —	\$ 14,531
Fixed income securities:					
U.S. treasury debt	1	2,210	41	(41)	2,210
U.S. agency obligations	2	388	9	(5)	392
Foreign debt	2	3,146	198	(4)	3,340
Corporate debt	2	26,183	597	(1,120)	25,660
Preferred stock	2	16,712	678	(113)	17,277
Mortgage backed securities	2	1	—	—	1
Common stock	1	11,997	3,015	(543)	14,469
Mutual funds:					
Equity	1	11,710	2,902	(5)	14,607
Fixed income	2	5,399	144	(113)	5,430
Other investments	2	4,379	—	(26)	4,353
Trust securities		\$ 96,656	\$ 7,584	\$ (1,970)	\$ 102,270
Accrued investment income		\$ 834			\$ 834
Preneed funeral trust investments					\$ 103,104
Fair market value as a percentage of cost					105.8%

The estimated maturities of the fixed income securities included above are as follows (in thousands):

Due in one year or less	\$ 676
Due in one to five years	6,153
Due in five to ten years	9,021
Thereafter	33,030
Total	\$ 48,880

The cost and fair market values associated with preneed funeral trust investments at December 31, 2013 are detailed below (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 14,631	\$ —	\$ —	\$ 14,631
Fixed income securities:					
U.S. treasury debt	1	2,212	47	(54)	2,205
U.S. agency obligations	1	401	8	(7)	402
Foreign debt	2	2,726	115	(2)	2,839
Corporate debt	2	27,993	375	(957)	27,411
Preferred stock	2	15,949	292	(282)	15,959
Mortgage back securities	2	1	—	—	1
Common stock	1	10,681	2,092	(237)	12,536
Mutual funds:					
Equity	1	11,632	2,708	(22)	14,318
Fixed income	2	5,455	88	(179)	5,364
Other investments	2	3,686	—	(26)	3,660
Trust securities		\$ 95,367	\$ 5,725	\$ (1,766)	\$ 99,326
Accrued investment income		\$ 679			\$ 679
Preneed funeral trust investments					\$ 100,005
Market value as a percentage of cost					104.2%

We determine whether or not the assets in the preneed funeral trust investments have other-than-temporary impairments on a security-by-security basis. This assessment is made based upon a number of criteria including the length of time a security has been in a loss position, changes in market conditions and concerns related to the specific issuer. If a loss is considered to be other-than-temporary, the cost basis of the security is adjusted downward to its fair market value. Any reduction in the cost basis of the investment due to an other-than-temporary impairment is likewise recorded as a reduction to *Deferred preneed funeral receipts held in trust* on our Consolidated Balance Sheets. There will be no impact on earnings unless and until such time as the investment is withdrawn from the trust in accordance with state regulations at an amount that is less than its original basis.

We have determined that the unrealized losses in our preneed funeral trust investments are considered temporary in nature, as the unrealized losses were due to temporary fluctuations in interest rates and equity prices. The investments are diversified across multiple industry segments using a balanced allocation strategy to minimize long-term risk. We believe that none of the securities are other-than-temporarily impaired based on our analysis of the investments. At March 31, 2014, we had corporate debt and equity investments within our preneed funeral trust investments that had tax lots in loss positions for more than one year. Based on our analyses of these securities, the companies' businesses and current market conditions, we determined that these investment losses were temporary in nature.

Our preneed funeral trust investment unrealized losses, their associated fair market values, and the duration of unrealized losses as of March 31, 2014 and December 31, 2013, are shown in the following tables (in thousands):

	March 31, 2014					
	In Loss Position Less than 12 months		In Loss Position Greater than 12 months		Total	
	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses
Fixed income securities:						
U.S. debt	\$ —	\$ —	\$ 828	\$ (41)	\$ 828	\$ (41)
U.S. agency obligations	—	—	152	(5)	152	(5)
Foreign debt	346	(4)	—	—	346	(4)
Corporate debt	4,845	(484)	2,312	(636)	7,157	(1,120)
Preferred stock	3,961	(113)	—	—	3,961	(113)
Mutual funds:						
Equity	2,645	(528)	91	(14)	2,736	(542)
Equity and other	74	(2)	62	(4)	136	(6)
Fixed income	474	(17)	1,593	(96)	2,067	(113)
Other investments	—	—	44	(26)	44	(26)
Total temporary impaired securities	<u>\$ 12,345</u>	<u>\$ (1,148)</u>	<u>\$ 5,082</u>	<u>\$ (822)</u>	<u>\$ 17,427</u>	<u>\$ (1,970)</u>

	December 31, 2013					
	In Loss Position Less than 12 months		In Loss Position Greater than 12 months		Total	
	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses
Fixed income securities:						
U.S. debt	\$ —	\$ —	\$ 816	\$ (54)	\$ 816	\$ (54)
U.S. agency obligations	—	—	211	(7)	211	(7)
Foreign debt	632	(2)	—	—	632	(2)
Corporate debt	9,620	(460)	640	(497)	10,260	(957)
Preferred stock	9,918	(282)	—	—	9,918	(282)
Mutual funds:						
Equity	954	(152)	626	(85)	1,580	(237)
Equity and other	314	(13)	195	(9)	509	(22)
Fixed income	865	(43)	1,420	(136)	2,285	(179)
Other investments	—	—	44	(26)	44	(26)
Total temporary impaired securities	<u>\$ 22,303</u>	<u>\$ (952)</u>	<u>\$ 3,952</u>	<u>\$ (814)</u>	<u>\$ 26,255</u>	<u>\$ (1,766)</u>

Preneed funeral trust investment security transactions recorded in *Interest expense* in the Consolidated Statements of Operations for the three months ended March 31, 2013 and 2014 were as follows (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Investment income	\$ 606	\$ 645
Realized gains	5,127	494
Realized losses	(5,332)	(198)
Expenses and taxes	(248)	(405)
Decrease in deferred preneed funeral receipts held in trust	(153)	(536)
	<u>\$ —</u>	<u>\$ —</u>

Purchases and sales of investments in the preneed funeral trusts were as follows (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Purchases	\$ (3,186)	\$ (6,990)
Sales	3,915	7,537

7. PRENEED CEMETERY RECEIVABLES

Preneed sales of cemetery interment rights and related products and services are usually financed through interest-bearing installment sales contracts, generally with terms of up to five years with such interest income reflected as *Preneed cemetery finance charges*. In substantially all cases, we receive an initial down payment at the time the contract is signed. At March 31, 2014, the balances of preneed receivables for cemetery interment rights and for merchandise and services were \$20.8 million and \$8.3 million, respectively, of which \$9.5 million is presented in *Accounts receivable* and \$19.6 million is presented in *Preneed receivables*. The unearned finance charges associated with these receivables were \$3.8 million and \$3.9 million at December 31, 2013 and March 31, 2014, respectively.

We determine an allowance for customer cancellations and refunds on contracts in which revenue has been recognized on sales of cemetery interment rights. We have a collections policy where past due notifications are sent to the customer beginning at 15 days past due and periodically thereafter until the contract is cancelled or payment is received. We reserve 100% of the receivables on contracts in which the revenue has been recognized and payments are 90 days past due or more, which was approximately 5.0% of the total receivables on recognized sales at March 31, 2014. An allowance is recorded at the date that the contract is executed and periodically adjusted thereafter based upon actual collection experience at the business level. For the three months ended March 31, 2014, the change in the allowance for contract cancellations was as follows (in thousands):

	March 31, 2014
Beginning balance	\$ 1,347
Write-offs and cancellations	(365)
Provision	442
Ending balance	\$ 1,424

The aging of past due financing receivables as of March 31, 2014 is as follows (in thousands):

	31-60 Past Due	61-90 Past Due	91-120 Past Due	>120 Past Due	Total Past Due	Current	Total Financing Receivables
Recognized revenue	\$ 626	\$ 265	\$ 192	\$ 841	\$ 1,924	\$ 18,675	\$ 20,599
Deferred revenue	255	104	110	344	813	7,736	8,549
Total contracts	\$ 881	\$ 369	\$ 302	\$ 1,185	\$ 2,737	\$ 26,411	\$ 29,148

The aging of past due financing receivables as of December 31, 2013 is as follows (in thousands):

	31-60 Past Due	61-90 Past Due	91-120 Past Due	>120 Past Due	Total Past Due	Current	Total Financing Receivables
Recognized revenue	\$ 895	\$ 372	\$ 266	\$ 683	\$ 2,216	\$ 18,628	\$ 20,844
Deferred revenue	355	191	85	271	902	7,890	8,792
Total contracts	\$ 1,250	\$ 563	\$ 351	\$ 954	\$ 3,118	\$ 26,518	\$ 29,636

8. RECEIVABLES FROM PRENEED TRUSTS

The receivables from preneed trusts represent assets in trusts which are controlled and operated by third parties in which we do not have a controlling financial interest (less than 50%) in the trust assets. We account for these investments at cost. As of December 31, 2013 and March 31, 2014, receivables from preneed trusts were as follows (in thousands):

	December 31, 2013	March 31, 2014
Preneed trust funds, at cost	\$ 11,511	\$ 12,101
Less: allowance for contract cancellation	(345)	(363)
Receivables from preneed trusts, net	<u>\$ 11,166</u>	<u>\$ 11,738</u>

The following summary reflects the composition of the assets held in trust and controlled by third parties to satisfy our future obligations under preneed arrangements related to the preceding contracts at March 31, 2014 and December 31, 2013. The cost basis includes reinvested interest and dividends that have been earned on the trust assets. Fair value includes the unrealized gains and losses on trust assets.

	Historical Cost Basis	Fair Value
(in thousands)		
As of March 31, 2014		
Cash and cash equivalents	\$ 2,839	\$ 2,839
Fixed income investments	6,752	6,764
Mutual funds and common stocks	2,495	2,576
Annuities	15	15
Total	<u>\$ 12,101</u>	<u>\$ 12,194</u>

	Historical Cost Basis	Fair Value
(in thousands)		
As of December 31, 2013		
Cash and cash equivalents	\$ 2,657	\$ 2,657
Fixed income investments	6,344	6,355
Mutual funds and common stocks	2,484	2,561
Annuities	26	26
Total	<u>\$ 11,511</u>	<u>\$ 11,599</u>

9. CONTRACTS SECURED BY INSURANCE

Certain preneed funeral contracts are secured by life insurance contracts. Generally, the proceeds of the life insurance policies have been assigned to us and will be paid upon the death of the insured. The proceeds will be used to satisfy the beneficiary's obligations under the preneed contract for services and merchandise. Preneed funeral contracts secured by insurance totaled \$289.9 million and \$294.7 million at December 31, 2013 and March 31, 2014, respectively, and are not included on our Consolidated Balance Sheets.

10. CEMETERY PERPETUAL CARE TRUST INVESTMENTS

Care trusts' corpus on our Consolidated Balance Sheets represent the corpus of those trusts plus undistributed income. The components of *Care trusts' corpus* as of December 31, 2013 and March 31, 2014 were as follows (in thousands):

	December 31, 2013	March 31, 2014
Trust assets, at fair value	\$ 42,342	\$ 43,529
Obligations due to (from) trust	(449)	37
Care trusts' corpus	<u>\$ 41,893</u>	<u>\$ 43,566</u>

The income from these perpetual care trusts provides funds necessary to maintain cemetery property and memorials in perpetuity. This trust fund income is recognized, as earned, in *Cemetery revenues*. Trust management fees charged by our wholly-owned registered investment advisor are included in revenue in the period in which they are earned.

Where quoted prices are available in an active market, investments held by the trusts are classified as Level 1 investments pursuant to the three-level valuation hierarchy. Our Level 1 investments include cash and common stock. Where quoted market prices are not available for the specific security, then fair values are estimated by using quoted prices of similar securities in active markets or other inputs other than quoted prices that can corroborate observable market data. These investments are foreign debt, corporate debt, preferred stocks and mortgage backed securities, all of which are classified within Level 2 of the valuation hierarchy. We review and update our fair value hierarchy classifications quarterly. There were no transfers between Levels 1 and 2 for the three months ended March 31, 2014. There are no Level 3 investments in the cemetery perpetual care trust investment portfolio. See Note 11 for further information of the fair value measurement and the three-level valuation hierarchy.

The following table reflects the cost and fair market values associated with the trust investments held in perpetual care trust funds at March 31, 2014 (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 602	\$ —	\$ —	\$ 602
Fixed income securities:					
Foreign debt	2	2,378	149	(3)	2,524
Corporate debt	2	18,641	323	(839)	18,125
Preferred stock	2	11,244	376	(86)	11,534
Mortgage back securities	2	1	—	—	1
Common stock	1	8,478	2,052	(414)	10,116
Trust securities		\$ 41,344	\$ 2,900	\$ (1,342)	\$ 42,902
Accrued investment income		\$ 627			\$ 627
Cemetery perpetual care trust investments					\$ 43,529
Fair market value as a percentage of cost					103.8%

The estimated maturities of the fixed income securities included above are as follows (in thousands):

Due in one year or less	\$ —
Due in one to five years	3,871
Due in five to ten years	5,969
Thereafter	22,344
	\$ 32,184

The following table reflects the cost and fair market values associated with the trust investments held in perpetual care trust funds at December 31, 2013 (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 973	\$ —	\$ —	\$ 973
Fixed income securities:					
Foreign debt	2	2,062	87	(2)	2,147
Corporate debt	2	19,773	236	(691)	19,318
Preferred stock	2	10,668	110	(165)	10,613
Common stock	1	7,539	1,417	(178)	8,778
Trust securities		\$ 41,015	\$ 1,850	\$ (1,036)	\$ 41,829
Accrued investment income		\$ 513			\$ 513
Cemetery perpetual care investments					\$ 42,342
Market value as a percentage of cost					102.0%

We are required by various state laws to pay a portion of the proceeds from the sale of cemetery property interment rights into perpetual care trust funds. We determine whether or not the assets in the cemetery perpetual care trusts have an other-than-temporary impairment on a security-by-security basis. This assessment is made based upon a number of criteria including the length of time a security has been in a loss position, changes in market conditions and concerns related to the specific issuer. If a loss is considered to be other-than-temporary, the cost basis of the security is adjusted downward to its fair market value. Any reduction in the cost basis due to an other-than-temporary impairment is also recorded as a reduction to *Care trusts' corpus*.

We have determined that the unrealized losses in our perpetual care trust investments are considered temporary in nature, as the unrealized losses were due to temporary fluctuations in interest rates and equity prices. The investments are diversified across multiple industry segments using a balanced allocation strategy to minimize long-term risk. We believe that none of the securities are other-than-temporarily impaired based on our analysis of the investments. At March 31, 2014, we had corporate debt and equity investments within our perpetual care trust investments that had tax lots in loss positions for more than one year. Based on our analyses of these securities, the companies' businesses and current market conditions, we determined that these investment losses were temporary in nature. Our perpetual care trust investment unrealized losses, their associated fair market values, and the duration of unrealized losses for the periods ended March 31, 2014 and December 31, 2013, respectively, are shown in the following tables (in thousands):

	March 31, 2014					
	In Loss Position Less than 12 months		In Loss Position Greater than 12 months		Total	
	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses
Fixed income securities:						
Foreign debt	\$ 261	\$ (3)	\$ —	\$ —	\$ 261	\$ (3)
Corporate debt	3,630	(362)	1,732	(477)	5,362	(839)
Preferred stock	2,995	(86)	—	—	2,995	(86)
Common stock	2,019	(403)	69	(11)	2,088	(414)
Total temporary impaired securities	<u>\$ 8,905</u>	<u>\$ (854)</u>	<u>\$ 1,801</u>	<u>\$ (488)</u>	<u>\$ 10,706</u>	<u>\$ (1,342)</u>

	December 31, 2013					
	In Loss Position Less than 12 months		In Loss Position Greater than 12 months		Total	
	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses	Fair Market Value	Unrealized Losses
Fixed income securities:						
Foreign debt	\$ 478	\$ (2)	\$ —	\$ —	\$ 478	\$ (2)
Corporate debt	6,948	(332)	462	(359)	7,410	(691)
Preferred stock	5,811	(165)	—	—	5,811	(165)
Common stock	716	(114)	470	(64)	1,186	(178)
Total temporary impaired securities	<u>\$ 13,953</u>	<u>\$ (613)</u>	<u>\$ 932</u>	<u>\$ (423)</u>	<u>\$ 14,885</u>	<u>\$ (1,036)</u>

Perpetual care trust investment security transactions recorded in *Interest expense* in our Consolidated Statements of Operations for the three months ended March 31, 2013 and 2014 were as follows (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Undistributable realized gains	\$ 24	\$ 417
Undistributable realized losses	(295)	(149)
Increase (decrease) in Care trusts' corpus	271	(268)
Total	<u>\$ —</u>	<u>\$ —</u>

Perpetual care trust investment security transactions recorded in *Cemetery revenues* for the three months ended March 31, 2013 and 2014 were as follows (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Investment income	\$ 1,411	\$ 1,281
Realized gains (losses), net	398	(242)
Total	<u>\$ 1,809</u>	<u>\$ 1,039</u>

Purchases and sales of investments in the perpetual care trusts were as follows (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Purchases	\$ (2,587)	\$ (4,935)
Sales	3,121	5,181

11. FAIR VALUE MEASUREMENTS

Fair value is defined as the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date applicable for items that are recognized or disclosed at fair value in the financial statements on a recurring basis. We disclose the extent to which fair value is used to measure financial assets and liabilities, the inputs utilized in calculating valuation measurements, and the effect of the measurement of significant unobservable inputs on earnings, or changes in net assets, as of the measurement date.

We evaluated our financial assets and liabilities for those financial assets and liabilities that met the criteria of the disclosure requirements and fair value framework. The carrying values of cash and cash equivalents, trade receivables and trade payables approximate the fair values of those instruments due to the short-term nature of the instruments. The fair values of receivables on preneed funeral and cemetery contracts are impracticable to estimate because of the lack of a trading market and the diverse number of individual contracts with varying terms. Our long-term debt and Credit Facility (as defined in Note 13) are classified within Level 2 of the Fair Value Measurement hierarchy. The fair values of our long-term debt and Credit Facility approximate the carrying values of these instruments based on the index yields of similar securities compared to U.S. Treasury yield curves. The fair value of the convertible subordinated notes due 2021, issued in March 2014, is approximately \$151.7 million based on the last traded or broker quoted price. The fair value of the convertible junior subordinated debentures outstanding at March 31, 2014 was approximately \$28.0 million, based on Bloomberg Finance L.P.'s quotes for the corresponding preferred securities issued by the Trust. We identified investments in fixed income securities, common stock and mutual funds presented within the preneed and perpetual care trust investment categories on our Consolidated Balance Sheets as having met such criteria. See Notes 6 and 10 to our Consolidated Financial Statements herein for the fair value hierarchy levels of our trust investments.

The following three-level valuation hierarchy based upon the transparency of inputs is utilized in the measurement and valuation of financial assets or liabilities as of the measurement date:

- Level 1 – Fair value of securities based on unadjusted quoted prices for identical assets or liabilities in active markets. Our investments classified as Level 1 securities include cash, common stock, U.S. treasury debt and equity mutual funds.
- Level 2 – Fair value of securities estimated based on quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and inputs other than quoted market prices that are observable or that can be corroborated by observable market data by correlation. These inputs include interest rates, yield curves, credit risk, prepayment speeds, rating and tax-exempt status. Our investments classified as Level 2 securities include U.S. agency obligations, corporate debt, preferred stocks, foreign debt, mortgage backed securities, certain fixed income securities and fixed income mutual funds.
- Level 3 – Unobservable inputs based upon the reporting entity's internally developed assumptions, which market participants would use in pricing the asset or liability. As of March 31, 2014, we did not have any assets that had fair values determined by Level 3 inputs and no liabilities measured at fair value.

We account for our investments as available-for-sale and measure them at fair value under standards of financial accounting and reporting for investments in equity instruments that have readily determinable fair values and for all investments in debt securities.

12. DEFERRED CHARGES AND OTHER NON-CURRENT ASSETS

Deferred charges and other non-current assets at December 31, 2013 and March 31, 2014 were as follows (in thousands):

	December 31, 2013	March 31, 2014
Prepaid agreements not to compete, net of accumulated amortization of \$4,807 and \$4,947, respectively	\$ 1,299	\$ 1,354
Deferred loan costs, net of accumulated amortization of \$1,252 and \$1,423, respectively	2,602	2,431
Convertible junior subordinated debenture origination costs, net of accumulated amortization of \$1,095	2,949	—
Convertible subordinated notes issuance costs, net of accumulated amortization of \$44	—	3,940
Tradenames	5,430	5,411
Other	—	280
Deferred charges and other non-current assets	<u>\$ 12,280</u>	<u>\$ 13,416</u>

Agreements not to compete are amortized over the term of the respective agreements, ranging generally from one to ten years. Amortization expense was \$19,800 and \$140,000 for the three months ended March 31, 2013 and 2014, respectively. Deferred loan costs are being amortized over the term of the related debt using the effective interest method. In connection with the redemption of our convertible junior subordinated debentures, we wrote-off the related unamortized origination costs of approximately \$2.9 million in March 2014. The debt issuance costs related to our convertible subordinated notes issued in March 2014 are being amortized using the effective interest method over the seven year term of the notes. Our tradenames have indefinite lives and therefore are not amortized.

13. LONG-TERM DEBT

Our senior long-term debt consisted of the following at December 31, 2013 and March 31, 2014 (in thousands):

	December 31, 2013	March 31, 2014
Revolving credit facility, secured, floating rate	\$ 36,900	\$ —
Term loan, secured, floating rate	117,000	114,000
Acquisition debt	1,866	1,695
Less: current portion	(13,224)	(13,912)
Total long-term debt	<u>\$ 142,542</u>	<u>\$ 101,783</u>

As of March 31, 2014, we had a \$255 million secured bank credit facility (the "Credit Facility") with Bank of America, N.A. as Administrative Agent comprised of a \$125 million revolving credit facility and a \$130 million term loan. The Credit Facility also contains an accordion provision to borrow up to an additional \$40 million in revolving loans, subject to certain conditions. The Credit Facility matures on September 30, 2017 and is collateralized by all personal property and funeral home real property in certain states. As of March 31, 2014, we had no outstanding borrowings under the revolving credit facility and \$114.0 million was outstanding on the term loan. No letters of credit were issued and outstanding under the Credit Facility at March 31, 2014. Under the Credit Facility, outstanding borrowings bear interest at either a prime rate or a LIBOR rate, plus an applicable margin based upon the Company's leverage ratio. At March 31, 2014, the prime rate margin was equivalent to 1.50% and the LIBOR margin was 2.50%. The weighted average interest rate on the Credit Facility for the three months ended March 31, 2014 was 2.7%.

On February 27, 2014, we entered into a fourth amendment to the Credit Facility which (a) allows us to issue senior unsecured debt in an amount not to exceed \$150 million when aggregated with any subordinated debt or convertible subordinated debt issued by us and (b) allows us to refinance our existing convertible junior subordinated debentures with the proceeds of certain of senior unsecured debt, subordinated debt or convertible subordinated debt.

Refer to Note 22 for additional information concerning our Credit Facility.

We have no material assets or operations independent of our subsidiaries. All assets and operations are held and conducted by subsidiaries, each of which (except for the Trust, which is a single purpose entity that holds our 7% debentures issued in connection with the issuance of the Trust's term income deferrable equity securities (TIDES) 7% convertible preferred securities) have fully and unconditionally guaranteed our obligations under the Credit Facility. Additionally, we do not currently have any significant restrictions on our ability to receive dividends or loans from any subsidiary guarantor under the Credit Facility.

We were in compliance with the covenants contained in the Credit Facility as of March 31, 2014. The Credit Facility calls for key ratios that we must comply with including a requirement to maintain a leverage ratio of no more than 3.75 to 1.00 through June 29, 2014 and no more than 3.50 to 1.00 thereafter, and a covenant to maintain a fixed charge coverage ratio of no less than 1.20 to 1.00. As of March 31, 2014, the leverage ratio was 2.18 to 1.00 and the fixed charge coverage ratio was 1.83 to 1.00.

Acquisition debt consists of deferred purchase price and promissory notes payable to sellers. A majority of the notes bear interest ranging from 7.0% to 11.0%. A few notes bear interest at 0% and are discounted at imputed interest rates ranging from 9.5% to 10.0%. Original maturities range from five to twenty years.

14. CONVERTIBLE SUBORDINATED NOTES

On March 19, 2014, we issued \$143.75 million aggregate principal amount of 2.75% Convertible Subordinated Notes due 2021 (the "Notes"). The Notes have not been registered under the Securities Act of 1933, as amended (the "Securities Act"), and were offered only to "qualified institutional buyers" in compliance with Rule 144A under the Securities Act. The Notes are governed by an indenture dated as of March 19, 2014 between Wilmington Trust, National Association, as Trustee, and us (the "Indenture"). The Notes bear interest at 2.75%. Interest on the Notes accrue from March 19, 2014 and is payable semi-annually in arrears on March 15 and September 15 of each year, beginning September 15, 2014.

The Notes are general unsecured obligations and will be subordinated in the right of payment to all of our existing and future senior indebtedness and equal in right of payment with our other existing and future subordinated indebtedness. The initial conversion rate of the Notes is 44.3169 shares of our common stock per \$1,000 principal amount of the Notes, equivalent to an initial conversion price of approximately \$22.56 per share of common stock. The conversion rate is subject to adjustment upon the occurrence of certain events as described in the Indenture.

The Notes mature on March 15, 2021, unless earlier converted or purchased by us. Holders of the Notes may convert their Notes at their option at any time prior to December 15, 2020, if certain conditions are met. We may not redeem the Notes prior to maturity. However, in the event of a fundamental change (as defined in the Indenture), subject to certain conditions, a holder of the Notes will have the option to require us to purchase all or a portion of its Notes for cash. The fundamental change purchase price will equal 100% of the principal amount of the Notes to be purchased, plus any accrued and unpaid interest, if any, to, but excluding, the fundamental change purchase date.

The conversion option of the Notes is not an embedded derivative. In order to be a derivative, the conversion feature would need to be able to be settled in cash, or an instrument readily convertible to cash. We do not intend to issue a registration statement for the resale of the common stock issuable upon conversion. Thus, the shares that the holder will receive upon conversion are not readily convertible to cash.

We have recorded the issuance of the Notes per the guidance provided under ASC 470, Topic 20, *Debt with Conversion and Other Options*, which requires that we separate the Notes into a liability component and an equity component. The carrying amount of the liability is calculated by measuring the fair value of a similar liability (including any embedded features other than the conversion option) that does not have an associated equity component. The carrying amount of the liability component was determined based on a bond discount rate of 6.75%. The carrying amount of the equity component representing the embedded conversion option was determined by deducting the fair value of the liability component from the initial proceeds of the Notes and is recorded in Additional Paid in Capital ("APIC") on our Consolidated Balance Sheet. The excess of the principal amount of the liability over its carrying amount is amortized to interest expense using the effective interest method. The expected life of the liability component will not be reassessed in subsequent periods unless the terms are modified.

Subsequent to the issuance of the Notes, we accrued for additional transaction costs of \$0.8 million. Total transaction costs of \$5.1 million were allocated to the liability and equity components in proportion to the allocation of the initial proceeds and accounted for as debt issuance costs and equity issuance costs, respectively. Debt issuance costs are included in *Deferred charges and other non-current assets* on our Consolidated Balance Sheets and are being amortized using the effective interest method over the seven year term of the Notes. Equity issuance costs are included in APIC on our Consolidated Balance Sheets and are not amortized. Additionally, the recognition of the Notes as two separate components results in a basis difference associated with the liability component which represents a temporary difference. As a result, we recognized a deferred tax liability of \$12.7 million related to this temporary difference which was recorded as a reduction to APIC and an increase to our deferred tax liability. The deferred tax liability is being amortized over the seven year term of the Notes.

The carrying values of the liability and equity components of the Notes at March 31, 2014 are reflected in our consolidated balance sheets as follows (in thousands):

	March 31, 2014
Long-term liabilities:	
Principal amount	\$ 143,750
Unamortized discount of liability component	(31,489)
Carrying value of the liability component	<u>\$ 112,261</u>
Equity component carrying value	<u>\$ 31,660</u>

The fair value of the Notes, which are Level 2 measurements, was \$151.7 million at March 31, 2014.

Interest expense for the three months ended March 31, 2014 included contractual coupon interest expense of \$0.1 million and amortization of debt issuance costs of \$44,000. Accretion of the discount on the convertible subordinated notes was \$0.2 million for the three months ended March 31, 2014.

The unamortized discount is being amortized over the remaining term of seven years. The effective interest rate on the liability component for the three months ended March 31, 2014 was 6.75%.

We received proceeds of approximately \$143.75 million and paid transactions costs of approximately \$4.3 million. We used a portion of the proceeds to repay our outstanding balance on our revolving credit facility and to redeem our existing convertible junior subordinated debentures. For further discussion of the redemption of the convertible junior subordinated debentures, refer to Note 15 herein.

15. CONVERTIBLE JUNIOR SUBORDINATED DEBENTURES PAYABLE TO AFFILIATE AND COMPANY OBLIGATED MANDATORILY REDEEMABLE CONVERTIBLE PREFERRED SECURITIES OF CARRIAGE SERVICES CAPITAL TRUST

Carriage's wholly-owned subsidiary, Carriage Services Capital Trust, issued 1,875,000 units of 7% convertible preferred securities (TIDES) in June 1999, resulting in approximately \$90.0 million in net proceeds, and the Company issued a 7% convertible junior subordinated debenture to the Trust in the amount of \$93.75 million. The convertible preferred securities have a liquidation amount of \$50 per unit and are convertible into Carriage's common stock at the equivalent conversion price of \$20.4375 per share of common stock. The convertible junior subordinated debentures and the TIDES mature in 2029, and the TIDES are guaranteed on a subordinated basis by the Company. Both the convertible junior subordinated debentures and the TIDES contain a provision for the deferral of distributions for up to 20 consecutive quarters. During the period in which distribution payments are deferred, distributions will continue to accumulate at the 7% annual rate. Also, the deferred distributions will themselves accumulate distributions at the annual rate of 7%. During the period in which distributions are deferred, Carriage is prohibited from paying dividends on its common stock or repurchasing its common stock, with limited exceptions. There are no deferred distributions at March 31, 2014.

On March 17, 2014, we called for the redemption of all our outstanding convertible junior subordinated debentures due 2029 held by Carriage Services Capital Trust and the corresponding TIDES at a price \$50 per \$50 principal amount of the convertible junior subordinated debentures being redeemed, plus accrued and unpaid interest to the redemption dated. Redemption period for the TIDES ended April 16, 2014. In March 2014, we used a portion of the net proceeds from the issuance of the Notes to redeem the convertible junior subordinated debentures for approximately \$61.9 million in principal amount of our existing convertible junior subordinated debentures and approximately \$0.9 million associated with the call premium. At December 31, 2013 and March 31, 2014, amounts outstanding under the convertible junior subordinated debentures totaled \$89.8 million and \$27.9 million, respectively.

16. COMMITMENTS AND CONTINGENCIES

Litigation

We are a party to various litigation matters and proceedings. For each of our outstanding legal matters, we evaluate the merits of the case, our exposure to the matter, possible legal or settlement strategies, and the likelihood of an unfavorable outcome. We intend to defend ourselves in the lawsuits described herein. If we determine that an unfavorable outcome is probable and can be reasonably estimated, we establish the necessary accruals. We hold certain insurance policies that may reduce cash outflows with respect to an adverse outcome of certain of these litigation matters.

Leathermon, et al. v. Grandview Memorial Gardens, Inc., et al., United States District Court, Southern District of Indiana, Case No. 4:07-cv-137. On August 17, 2007, five plaintiffs filed a putative class action against the current and past owners of Grandview Cemetery in Madison, Indiana, including our subsidiaries that owned the cemetery from January 1997 until February 2001, on behalf of all individuals who purchased cemetery and burial goods and services at Grandview Cemetery. Plaintiffs are seeking monetary damages and claim that the cemetery owners performed burials negligently, breached Plaintiffs' contracts and made misrepresentations regarding the cemetery. The Plaintiffs also allege that the claims occurred prior, during and after we owned the cemetery. On October 15, 2007, the case was removed from Jefferson County Circuit Court, Indiana to the Southern District of Indiana. On April 24, 2009, shortly before the Defendants had been scheduled to file their briefs in opposition to Plaintiffs' motion for class certification, Plaintiffs moved to amend their complaint to add new class representatives and claims, while also seeking to abandon other claims. We, as well as several other Defendants, opposed Plaintiffs' motion to amend their complaint and add parties. In April 2009, two Defendants moved to disqualify Plaintiffs' counsel from further representing Plaintiffs in this action. On June 30, 2010, the Court granted Defendants' motion to disqualify Plaintiffs' counsel. On May 6, 2010, Plaintiffs filed a petition for writ of mandamus with the Seventh Circuit Court of Appeals seeking relief from the trial court's order of disqualification of counsel. On May 19, 2010, the Defendants responded to the petition of mandamus. On July 8, 2010, the Seventh Circuit denied Plaintiffs' petition for writ of mandamus. Thus, pursuant to the trial court's order, Plaintiffs were given 60 days from July 8, 2010 in which to retain new counsel to prosecute this action on their behalf. Plaintiffs retained new counsel and Plaintiffs' counsel moved for leave to amend both the class representatives and the allegations stated within the complaint. Defendants filed oppositions to such amendments. The Court issued an order permitting the Plaintiffs to proceed with amending the class representatives and a portion of their claims; however, certain of Plaintiffs' claims have been dismissed. The parties have now reached a proposed class settlement and the Court has granted its preliminary approval of such settlement by order dated March 19, 2014. As such, notice of the class settlement shall be provided pursuant to the Preliminary Order Approving Class Action Settlement. The final approval hearing is scheduled to take place on June 23, 2014. Except for those actions necessary to carry out the parties' contemplated settlement, the lawsuit has been stayed pending determination of the final approval of the settlement.

17. STOCKHOLDERS' EQUITY

Stock Options

As of March 31, 2014, there were 1,414,421 stock options outstanding and 1,243,521 stock options which remain unvested. On February 25, 2014, we granted 457,700 options to certain employees at a grant price of \$20.26. On March 3, 2014, we granted 300,000 options to three executives at a grant price of \$20.49. These options will vest in 33.33% increments over a three year period and have a five year term. The value of these stock options is approximately \$3.9 million.

The fair value of the option grants are estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions, as indicated by grant date:

	February 25, 2014	March 3, 2014
Dividend yield	0.494%	0.488%
Expected volatility	33.37%	33.28%
Risk-free interest rate	0.995%	0.949%
Expected life (years)	3.71	3.73
Black-Scholes value	\$ 5.15	\$ 5.20

We recorded pre-tax stock-based compensation expense for stock options totaling \$47,000 and \$265,000 for the three months ended March 31, 2013 and 2014, respectively. The significant increase in expense for the three months ended March 31, 2014 was due to the large number of stock option grants in the first quarter of 2014 at a significantly higher grant price compared to prior grants.

Employee Stock Purchase Plan

During the first quarter of 2014, employees purchased a total of 18,471 shares of common stock through the employee stock purchase plan ("ESPP") at a weighted average price of \$15.50 per share. We recorded pre-tax stock-based compensation expense for the ESPP totaling approximately \$99,000 and \$116,000 for the three months ended March 31, 2013 and 2014, respectively.

The fair value of the right (option) to purchase shares under the ESPP is estimated on the date of grant (January 1, 2014) associated with the four quarterly purchase dates using the following assumptions:

	2014
Dividend yield	0.6%
Expected volatility	33.37%
Risk-free interest rate	0.07%, 0.09%, 0.11%, 0.13%
Expected life (years)	0.25, 0.50, 0.75, 1.00

Expected volatilities are based on the historical volatility during the previous twelve months of the underlying common stock. The risk-free rate for the quarterly purchase periods is based on the U.S. Treasury yields in effect at the time of the purchase. The expected life of the ESPP grants represents the calendar quarters from the beginning of the year to the purchase date (end of each quarter).

Restricted Stock Grants

From time to time, we issue shares of restricted common stock to certain officers, directors and key employees of the Company from our stock benefit plans. The restricted stock shares issued to officers and key employees vest in either 25% or 33.33% increments over four or three year terms, respectively. During the first quarter of 2014, we awarded a grant of 200,000 shares of restricted stock to three officers. These shares vest in 25% increments over a four year period and have an aggregate grant date market value of \$4.1 million.

Related to the vesting of restricted stock awards awarded to our officers, employees and directors, we recorded \$313,000 and \$349,000 of pre-tax compensation expense, which is included in general, administrative and other expenses for the three months ended March 31, 2013 and 2014, respectively.

As of March 31, 2014, we had \$6.0 million of total unrecognized compensation costs related to unvested restricted stock awards, which are expected to be recognized over a weighted average period of approximately 2.8 years.

Performance-Based Stock Awards

During the third quarter of 2012, the Compensation Committee of our Board of Directors (our "Board") granted performance-based awards (the "PBS Awards") with both market and service vesting conditions to certain officers, employees and outside directors. No PBS Awards were granted during fiscal year 2013. To the extent vested, each PBS Award represented the right to receive a specified number of shares of our common stock, subject to the grantee's payment, with respect to each share of common stock subject to such PBS Award, of an amount equal to the greater of (a) the then-current market price per share of our common stock on the date such PBS Award was granted plus \$0.50 or (b) \$9.00. Each PBS Award would have vested if on or before the fifth anniversary of the applicable grant date, the closing price of our common stock was greater than or equal to \$21.50 on any three days, whether or not consecutive, within a period of 30 consecutive calendar days, subject to the applicable grantee's continuous employment or service relationship with us through such date (the "Price Vesting Date"). However, if the Price Vesting Date occurred prior to the first anniversary of the grant date, then each PBS Award would not vest until the first anniversary of such grant date, subject to the applicable grantee's continued employment or service relationship with us through the first anniversary of the grant date.

On January 3, 2014, we offered all grantees who held outstanding PBS Awards an opportunity to surrender their PBS Awards to us in exchange for cash payments equal to the product of (i) the difference between (x) \$19.00 and (y) the applicable purchase price under their respective PBS Awards and (ii) the number of shares of our common stock subject to their PBS Awards (the "Cash Out Payments"). All outstanding PBS Awards were surrendered to us and canceled in exchange for Cash Out Payments of approximately \$16.1 million.

Director Compensation Policy

Our Director Compensation Policy provides for the following: (a) the chairman of our Audit Committee receives an annual cash retainer of \$17,500, the chairman of our Compensation and our Corporate Governance Committees receives an annual cash retainer of \$15,000 and the Lead Director of our Board receives an annual cash retainer of \$115,000, payable in quarterly installments; (b) each independent director of our Board receives an annual cash retainer of \$40,000 paid on a quarterly basis and an annual equity retainer of \$75,000 in shares of our common stock issued at our annual meeting of stockholders. Additionally, each independent director receives \$2,000 for each regular or special meeting of the full Board, our Audit Committee and our Executive Committee attended in person or by phone. Members of the other committees and their chairmen receive \$1,600 for each committee meeting held in person or by phone that such director attends. Under our Director

Compensation Policy, the annual cash retainers for each committee chairman and the annual equity retainer are paid on the date of our annual meeting of stockholders, which will be held on May 21, 2014.

We recorded \$133,000 and \$175,000 of pre-tax compensation expense, which is included in general, administrative and other expenses, for the three months ended March 31, 2013 and 2014, respectively, related to the director fees, annual retainers and deferred compensation amortization.

Cash Dividends

Our Board declared a quarterly dividend of \$0.025 per share, totaling approximately \$0.5 million, which was paid on March 3, 2014 to record holders of our common stock as of February 13, 2014. We have a dividend reinvestment program so that stockholders may elect to reinvest their dividends into additional shares of our common stock.

Accumulated other comprehensive income

Our components of Accumulated other comprehensive income are as follows:

	Accumulated Other Comprehensive Income
Balance at December 31, 2013	\$ —
Increase in net unrealized gains associated with available-for-sale securities of the trusts	9,816
Reclassification of net unrealized gain activity attributable to the <i>Deferred preneed funeral and cemetery receipts held in trust and Care trusts' corpus</i>	(9,816)
Balance at March 31, 2014	\$ —

18. MAJOR SEGMENTS OF BUSINESS

We conduct funeral and cemetery operations only in the United States. The following table presents revenue, pre-tax income and total assets by segment (in thousands):

	<u>Funeral</u>	<u>Cemetery</u>	<u>Corporate</u>	<u>Consolidated</u>
Revenues from continuing operations:				
Three months ended March 31, 2014	\$ 44,159	\$ 11,688	\$ —	\$ 55,847
Three months ended March 31, 2013	\$ 45,051	\$ 12,264	\$ —	\$ 57,315
Income (loss) from continuing operations before income taxes:				
Three months ended March 31, 2014	\$ 14,355	\$ 3,303	\$ (14,952)	\$ 2,706
Three months ended March 31, 2013	\$ 14,694	\$ 3,891	\$ (8,896)	\$ 9,689
Total assets:				
March 31, 2014	\$ 507,499	\$ 226,282	\$ 35,651	\$ 769,432
December 31, 2013	\$ 502,525	\$ 227,520	\$ 16,554	\$ 746,599

19. SUPPLEMENTAL DISCLOSURE OF STATEMENT OF OPERATIONS INFORMATION

The following information is supplemental disclosure for the Consolidated Statements of Operations (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Revenues		
Goods		
Funeral	\$ 17,962	\$ 17,418
Cemetery	7,149	7,115
Total goods	\$ 25,111	\$ 24,533
Services		
Funeral	\$ 24,855	\$ 24,242
Cemetery	2,611	2,652
Total services	\$ 27,466	\$ 26,894
Financial revenue		
Preneed funeral commission income	\$ 508	\$ 564
Preneed funeral trust earnings	1,726	1,935
Cemetery trust earnings	2,194	1,584
Cemetery finance charges	310	337
Total financial revenue	\$ 4,738	\$ 4,420
Total revenues	\$ 57,315	\$ 55,847
Cost of revenues		
Goods		
Funeral	\$ 14,028	\$ 13,866
Cemetery	5,124	5,213
Total goods	\$ 19,152	\$ 19,079
Services		
Funeral	\$ 11,912	\$ 11,919
Cemetery	1,643	1,724
Total services	\$ 13,555	\$ 13,643
Financial expenses		
Preneed funeral commissions	\$ 397	\$ 247
Trust administration fees	63	30
Total financial expenses	\$ 460	\$ 277
Total cost of revenues	\$ 33,167	\$ 32,999

The costs of revenues, for purposes of this supplemental disclosure, include only field costs and expenses that are directly allocable between the goods, services and financial categories in the funeral and cemetery segments. Depreciation and amortization and regional and unallocated funeral and cemetery costs are not included in this disclosure.

20. SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

The following information is supplemental disclosure for the Consolidated Statements of Cash Flows (in thousands):

	For the Three Months Ended March 31,	
	2013	2014
Cash paid for interest	\$ 3,269	\$ 2,801
Cash paid (refunded) for income taxes	(77)	296
Fair value of stock, stock options and performance awards issued to directors, officers and certain employees	—	8,002
Restricted common stock withheld for payroll taxes	1,020	1,079
Net (deposits) withdrawals from preneed funeral trusts	726	(3,060)
Net (deposits) withdrawals from preneed cemetery trusts	375	(1,134)
Net (deposits) withdrawals from perpetual care trusts	1,372	(493)
Net (increase) decrease in preneed receivables	(959)	271
Net deposits of receivables from preneed trusts	(1,063)	(571)
Net change in preneed funeral receivables increasing deferred revenue	2,049	513
Net change in preneed cemetery receivables increasing (decreasing) deferred revenue	568	(550)
Net deposits (withdrawals) into/from preneed funeral trust accounts increasing (decreasing) deferred preneed funeral receipts held in trust	(726)	3,060
Net deposits (withdrawals) into/from cemetery trust accounts increasing (decreasing) deferred cemetery receipts held in trust	(375)	1,134
Net deposits (withdrawals) from perpetual care trust accounts increasing (decreasing) perpetual care trusts' corpus	(833)	1,014

21. EARNINGS PER SHARE

Share-based awards that contain non-forfeitable rights to dividends or dividend equivalents, whether paid or unpaid, are participating securities and included in the computation of both basic and diluted earnings per share. Our grants of restricted stock awards to our employees and directors are considered participating securities and we have prepared our earnings per share calculations to exclude outstanding unvested restricted stock awards, using the two-class method, in the basic and diluted weighted average shares outstanding calculation.

The following table sets forth the computation of the basic and diluted earnings per share for the three months ended March 31, 2013 and 2014:

	For the Three Months Ended March 31,	
	2013	2014
Numerator for basic earnings per share:		
Numerator from continuing operations		
Income from continuing operations	\$ 5,409	\$ 1,651
Less: Earnings allocated to unvested restricted stock	(139)	(37)
Income attributable to continuing operations	<u>\$ 5,270</u>	<u>\$ 1,614</u>
Numerator from discontinued operations		
Income (loss) from discontinued operations	\$ (151)	\$ 567
Less: Earnings allocated to unvested restricted stock	3	(13)
Income (loss) attributable to discontinued operations	<u>\$ (148)</u>	<u>\$ 554</u>
Numerator for diluted earnings per share:		
Adjustment for diluted earnings per share:		
Interest on convertible junior subordinated debentures, net of tax	485	—
	<u>\$ 485</u>	<u>\$ —</u>
Income attributable to continuing operations	\$ 5,756	\$ 1,614
Income (loss) attributable to discontinued operations	\$ (148)	\$ 554
Denominator		
Denominator for basic earnings per common share - weighted average shares outstanding	17,657	17,984
Effect of dilutive securities:		
Stock options	197	159
Convertible junior subordinated debentures	4,392	—
Denominator for diluted earnings per common share - weighted average shares outstanding	<u>22,246</u>	<u>18,143</u>
Basic earnings (loss) per common share:		
Continuing operations	\$ 0.30	\$ 0.09
Discontinued operations	\$ (0.01)	\$ 0.03
Basic earnings per common share	<u>\$ 0.29</u>	<u>\$ 0.12</u>
Diluted earnings (loss) per common share:		
Continuing operations	\$ 0.26	\$ 0.09
Discontinued operations	\$ (0.01)	\$ 0.03
Diluted earnings per common share	<u>\$ 0.25</u>	<u>\$ 0.12</u>

The fully diluted weighted average shares outstanding for the three months ended March 31, 2013, and the corresponding calculation of fully diluted earnings per share include approximately 4.4 million shares that would be issued upon conversion of our convertible junior subordinated debentures as a result of the application of the if-converted method prescribed by FASB ASC 260-10-45. For the three months ended March 31, 2014, shares from the conversion of our convertible junior subordinated debentures and our convertible subordinated notes are excluded from the fully diluted earnings per share calculation because the inclusion of such converted shares would result in an antidilutive impact.

22. SUBSEQUENT EVENTS

On April 14, 2014, we entered into a fifth amendment to our Credit Facility (the “Fifth Amendment”), which provides for an increase in our revolving credit facility from \$125 million to \$200 million and new funding under our term loan so that \$125 million will be outstanding upon effectiveness of the Fifth Amendment. The Fifth Amendment becomes effective upon the consummation of the SCI Acquisition. We currently anticipate that the SCI Acquisition will close in the second quarter of 2014. Borrowings under the term loan facility are subject to amortization payments of 7.5% of the principal amount in the first two years following the Fifth Amendment effective date, 10.0% for the third and fourth years following the effective date and 12.5% per year thereafter. Obligations under the Fifth Amendment mature on March 31, 2019. The Fifth Amendment also modifies the financial covenants so that we must maintain a leverage ratio of 3.75 to 1.00 through March 30, 2015 and 3.50 to 1.00 thereafter.

As of April 16, 2014, we completed the redemption of our convertible junior subordinated debentures.

CAUTIONARY STATEMENT ON FORWARD-LOOKING STATEMENTS

In addition to historical information, this Form 10-Q contains certain statements and information that may constitute forward-looking statements within the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements include statements regarding the consummation of the SCI Acquisition, any projections of earnings, revenues, asset sales, cash flow, debt levels or other financial items; any statements of the plans, strategies and objectives of management for future operations; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing and are based on our current expectations and beliefs concerning future developments and their potential effect on us. The words “may”, “will”, “estimate”, “intend”, “believe”, “expect”, “project”, “forecast”, “foresee”, “should”, “would”, “could”, “plan”, “anticipate” and other similar words or expressions are intended to identify forward-looking statements, which are generally not historical in nature. While management believes that these forward-looking statements are reasonable as and when made, there can be no assurance that future developments affecting us will be those that we anticipate. All comments concerning our expectations for future revenues and operating results are based on our forecasts for our existing operations and do not include the potential impact of any future acquisitions. Our forward-looking statements involve significant risks and uncertainties (some of which are beyond our control) and assumptions that could cause actual results to differ materially from our historical experience and our present expectations or projections. Important factors that could cause actual results to differ materially from those in the forward-looking statements include, but are not limited to, those summarized below:

- the execution of our Standards Operating Model;
- changes in the number of deaths in our markets;
- changes in consumer preferences;
- ability to find and retain skilled personnel;
- the effects of competition;
- the investment performance of our funeral and cemetery trust funds;
- fluctuations in interest rates;
- our ability to obtain debt or equity financing on satisfactory terms to fund additional acquisitions, expansion projects, working capital requirements and the repayment or refinancing of indebtedness;
- death benefits related to preneed funeral contracts funded through life insurance contracts;
- our ability to generate preneed sales;
- the financial condition of third-party insurance companies that fund our preneed funeral contracts;
- increased or unanticipated costs, such as insurance or taxes;
- effects of the application of applicable laws and regulations, including changes in such regulations or the interpretation thereof;
- consolidation of the deathcare industry;
- our ability to consummate the SCI Acquisition; and
- other factors and uncertainties inherent in the deathcare industry.

For additional information regarding known material factors that could cause our actual results to differ from our projected results, please see (i) Part II, Item 1A “Risk Factors” in this Form 10-Q and (ii) Part I, Item 1A “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2013.

Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof. We undertake no obligation to publicly update or revise any forward-looking statements after the date they are made, whether as a result of new information, future events or otherwise.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

OVERVIEW

General

We operate two types of businesses: funeral homes, which account for approximately 75% of our revenues, and cemeteries, which account for approximately 25% of our revenues. Funeral homes are principally service businesses that provide funeral services (traditional burial and cremation) and sell related merchandise, such as caskets and urns. Cemeteries are primarily a sales business that sells interment rights (grave sites and mausoleum spaces) and related merchandise, such as markers and outer burial containers. As of March 31, 2014, we operated 161 funeral homes in 26 states and 31 cemeteries in 10 states. Substantially all administrative activities are conducted in our home office in Houston, Texas.

We have implemented a long-term strategy in our operations designed to improve operating and financial results by growing market share and increasing profitability. We have a decentralized, entrepreneurial and local operating model that includes operating and financial standards developed from our best operations, along with an incentive compensation plan to reward Managing Partners for successfully meeting or exceeding the standards. The model essentially eliminated the use of line-item financial budgets at the location level in favor of the standards. The operating model and its standards, which we refer to as the "Standards Operating Model," focus on the key drivers of a successful operation, organized around three primary areas - market share, people and operating financial metrics. The model and standards are the measures by which we judge the success of each business. In 2012, we began a five year incentive plan, called "Good to Great," which reward business managers, known as "Managing Partners," with a bonus at the end of five years, equal to a ratio of 4 to 6 times their average annual bonus, if they are able to achieve an annual compound growth rate of 2% over a five year period. To date, the Standards Operating Model has driven significant changes in our organization, leadership and operating practices. Most importantly, the Standards Operating Model has allowed us to measure the sustainable revenue growth and earning power of our portfolio businesses. The Standards Operating Model led to the development of our Strategic Acquisition Model, described below under "Acquisitions," which guides our acquisition and disposition strategy. We expect both models to drive long-term, sustainable increases in market share, revenue, earnings and cash flow. The standards are not designed to produce maximum short-term earnings because we do not believe such performance is sustainable without ultimately stressing the business, which often leads to declining market share, revenues and earnings. Important elements of the Standards Operating Model include:

- *Balanced Operating Model* – We believe a decentralized structure works best in the deathcare industry. Successful execution of the Standards Operating Model is highly dependent on strong local leadership, intelligent risk taking, entrepreneurial drive and corporate support aligned with the key drivers of a successful operation organized around three primary areas - market share, people and operating financial metrics.
- *Incentives Aligned with Standards* – Empowering Managing Partners to do the right things in their operations and local communities, and providing appropriate support with operating and financial practices, will enable long-term growth and sustainable profitability. Each Managing Partner participates in a variable bonus plan whereby he or she earns a percentage of his or her respective business' earnings based upon the actual standards achieved as long as the performance exceeds our minimum standards.
- *The Right Local Leadership* – Successful execution of our operating model is highly dependent on strong local leadership as defined by our 4E Leadership Model, intelligent risk taking and entrepreneurial empowerment. A Managing Partner's performance is judged according to achievement of the standards for that business.

Funeral and Cemetery Operations

Factors affecting our funeral operating results include: demographic trends relating to population growth and average age, which impact death rates and number of deaths; establishing and maintaining leading market share positions supported by strong local heritage and relationships; effectively responding to increasing cremation trends by selling complementary services and merchandise; controlling salary and merchandise costs; and exercising pricing leverage related to our at-need business to increase average revenue per contract. In simple terms, volume and price are the two variables that affect funeral revenues. The average revenue per contract is influenced by the mix of traditional burial and cremation services because our average cremation service revenue is approximately one-third of the average revenue earned from a traditional burial service. Funeral homes have a relatively fixed cost structure. Thus, small changes in revenues, up or down, normally cause significant changes to our profitability.

Our funeral volumes have increased from 23,010 in 2009 to 29,996 in 2013 (compounded annual increase of 6.9%). Our funeral operating revenue, excluding financial revenue, has increased from \$120.6 million in 2009 to \$154.7 million in 2013 (compounded annual increase of 6.4%). The increases are primarily a result of businesses we have acquired in the last five years and our ability to increase the average revenue per funeral through expanded service offerings and packages. Additional funeral revenue from preneed commissions and preneed funeral trust earnings has increased from \$5.8 million in 2009 to \$9.3

million in 2013. We experienced a decrease of 3.4% in volumes and 2.7% in funeral operating revenues in the first three months of 2014 compared to the first three months of 2013, primarily due to a decrease in same store volumes and revenues.

The percentage of funeral services involving cremations has increased from 40.6% for the year ended 2009 to 46.8% for the year ended 2013, and was 46.4% for the first three months of 2014. On a same store basis, the cremation rate has risen to 46.6% for the first three months of 2014, up from 46.1% for the year ended December 31, 2013, and 45.8% for the comparable three month period in 2013. The cremation rate for our acquired funeral home businesses was 46.1% for the first three months of 2014 compared to 48.7% for the comparable three month period in 2013.

Cemetery operating results are affected by the size and success of our sales organization. Approximately 48.0% of our cemetery revenues for the year ended December 31, 2013 related to preneed sales of interment rights and related merchandise and services. For the three months ended March 31, 2014, those preneed sales were approximately 46.0% of total cemetery revenues. We believe that changes in the economy and consumer confidence affect the amount of preneed cemetery revenues. Cemetery revenues from investment earnings on trust funds were approximately \$1.9 million, or 16.4% of total cemetery revenues, for the three months ended March 31, 2014, down from \$2.5 million, or 20.4% of total cemetery revenues for the three months ended March 31, 2013. Changes in the capital markets and interest rates affect this component of our cemetery revenues.

Our cemetery financial performance from 2009 through 2013 was characterized by varying levels of operating revenues yet increasing field-level profit margins. Cemetery operating revenue increased from \$39.3 million in 2009 to \$40.5 million in 2013. Our goal is to build broader and deeper teams of sales leaders and counselors in our larger and more strategically located cemeteries in order to focus on the growth of our preneed property sales. Additionally, a portion of our capital expenditures in 2014 is designated to expand our cemetery product offerings.

Financial Revenue

We market funeral and cemetery services and products on a preneed basis. Preneed funeral or cemetery contracts enable families to establish, in advance, the type of service to be performed, the products to be used and the cost of such products and services. Preneed contracts permit families to eliminate issues of making deathcare plans at the time of need and allow input from other family members before the death occurs. We guarantee the price and performance of the preneed contracts to the customer.

Preneed funeral contracts are usually paid on an installment basis. The performance of preneed funeral contracts is usually secured by placing the funds collected in trust for the benefit of the customer or by the purchase of a life insurance policy, the proceeds of which will pay for such services at the time of need. Insurance policies, intended to fund preneed funeral contracts, cover the original contract price and generally include an element of growth (earnings) designed to offset future inflationary cost increases. Revenue from preneed funeral contracts, along with accumulated earnings, is not recognized until the time the funeral service is performed. The accumulated earnings from the trust investments and insurance policies are intended to offset the inflation in funeral prices. Additionally, we generally earn a commission from the insurance company from the sale of insurance-funded policies reflected as *Preneed Insurance Commission* within *Funeral Revenue*. The commission income is recognized as revenue when the period of refund expires (generally one year), which helps us defray the costs we incur to originate the preneed contract (primarily commissions we pay to our sales counselors).

Preneed sales of cemetery interment rights are usually financed through interest-bearing installment sales contracts, generally with terms of up to five years with such earnings reflected as *Preneed Cemetery Finance Charges* within *Cemetery Revenue*. In substantially all cases, we receive an initial down payment at the time the contract is signed. In most states, regulations require a portion (generally 10%) of the sale amount of cemetery property and memorials to be placed in a perpetual care trust.

We have established a variety of trusts in connection with funeral home and cemetery operations as required under applicable state laws. Such trusts include (i) preneed funeral trusts; (ii) preneed cemetery merchandise and service trusts; and (iii) perpetual care trusts. These trusts are typically administered by independent financial institutions selected by us. Investment management and advisory services are provided either by our wholly-owned registered investment advisor (CSV RIA) or independent financial advisors. As of March 31, 2014, CSV RIA provided these services to two institutions, which have custody of 76% of our trust assets, for a fee based on the market value of trust assets. Under state trust laws, we are allowed to charge the trust a fee for advising on the investment of the trust assets and these fees are recognized as income as the advisory services are provided. The investment advisors establish an investment policy that gives guidance on asset allocation, investment requirements, investment manager selection and performance monitoring. The investment objectives are tailored to generate long-term investment returns without assuming undue risk, while ensuring the management of the assets is in compliance with applicable laws.

Preneed funeral trust fund income earned, along with the receipt and recognition of any insurance benefits, are deferred until the service is performed. Applicable state laws generally require us to deposit a specified amount (which varies from state to state, generally 50% to 100% of selling price) into a merchandise and service trust fund for preneed cemetery merchandise and service sales. The related trust fund income earned is recognized when the related merchandise and services are delivered. In most states, regulations require a portion (generally 10%) of the sale amount of cemetery property and memorials to be placed in a perpetual care trust. The income from perpetual care trusts provides a portion of the funds necessary to maintain cemetery property and memorials in perpetuity. Perpetual care trust fund income is recognized, as earned, in our cemetery revenues.

Acquisitions

Our growth strategy includes the execution of our Strategic Acquisition Model. We use six strategic ranking criteria to assess acquisition candidates and to differentiate the price we are willing to pay under a discounted cash flow methodology. Those criteria are:

- size of business;
- size of market;
- competitive standing;
- local market demographics;
- strength of brand; and
- barriers to entry.

In general terms, should a target business be acceptable per the criteria above, we will then determine the value of the target using a discounted cash flow methodology. During 2013, we acquired two funeral homes, one in Tennessee and one in Georgia. The consideration paid for the 2013 acquisitions was \$13.7 million. Additionally, we purchased land for approximately \$6.0 million in 2013 to be used for future funeral expansions. We have not acquired any businesses to date in 2014.

Financial Highlights

Net income from continuing operations for the three months ended March 31, 2014 totaled \$1.7 million, equal to \$0.09 per diluted share, compared to net income from continuing operations for the three months ended March 31, 2013, which totaled \$5.4 million, equal to \$0.26 per diluted share. Net income from continuing operations for the three months ended March 31, 2014 included a loss of approximately \$3.8 million on the redemption of our convertible junior subordinated debentures. Total revenue for the three months ended March 31, 2014 was \$55.8 million, a decrease of 2.6% for the comparable period in 2013. Our funeral segment experienced a decrease in revenue and gross profit during the three months ended March 31, 2014 primarily as a result of a decrease in same store contracts compared to the same period of 2013. The cemetery segment experienced decreases in revenue during the three months ended March 31, 2014 due to lower preneed property sales and lower trust earnings offset, in part, by increased at-need revenue and margin. Gross profit for these segments decreased as a result of lower revenues in the three months ended March 31, 2014 as compared to the same period in 2013. We experienced increases in general and administrative expenses due to increases in severance costs, incentive and stock-based compensation, acquisition and divestiture expenses and consulting costs.

We also present our financial performance in our “Operating and Financial Trend Report” (“Trend Report”) as reported in our earnings release and discussed on our earnings call for the quarter ending March 31, 2014. This Trend Report is used as a supplemental financial measurement statement by management and investors to compare our current financial performance with our previous results and with the performance of other deathcare companies. The Trend Report is a Non-GAAP statement from continuing operations that also provides insight into underlying trends in our business. We do not intend for this information to be considered in isolation or as a substitute for other measures of performance prepared in accordance with GAAP.

The Non-GAAP financial measures in the Trend Report include “Adjusted Net Income,” “Adjusted Basic Earnings Per Share,” “Adjusted Diluted Earnings Per Share,” “Consolidated EBITDA,” “Adjusted Consolidated EBITDA,” “Free Cash Flow,” “Funeral, Cemetery and Financial EBITDA,” “Total Field EBITDA” and “Special Items.” These financial measurements are defined as similar GAAP items adjusted for Special Items and are reconciled to GAAP in our earnings release and on the Trend Reports posted on our website (www.carriageservices.com). In addition, our presentation of these measures may not be comparable to similarly titled measures in other companies’ reports. We are providing below a reconciliation after tax of net income from continuing operations (a GAAP measure) to Non-GAAP net income (a non-GAAP measure). Non-GAAP net income is defined as net income from continuing operations adjusted for Special Items, including

Withdrawable trust income, acquisition expenses, severance costs and other items in the table below. The adjustment of Special Items in Non-GAAP income allows management to focus on the evaluation of operating performance as it primarily relates to our operating expenses.

In certain states, we are allowed to withdraw realized trust earnings prior to delivery from cemetery merchandise and services trusts, which management describes as “Withdrawable trust income.” The Withdrawable trust income, pre-tax, totaled \$0.5 million and \$0.2 million for the three months ended March 31, 2013 and 2014, respectively. While the Withdrawable trust income is not recognized as revenue in our Consolidated Statements of Operations, it increases cash flow from operations. The Withdrawable trust income is treated as a special item in our Non-GAAP net income calculation.

<i>(In millions)</i>	For the Three Months Ended March 31,			
	2013		2014	
Net income from continuing operations, as reported	\$	5.4	\$	1.7
After-tax special items:				
Withdrawable trust income		0.3		0.1
Acquisition and divestiture expenses		—		0.5
Severance costs		0.1		0.2
Other incentive compensation		—		0.6
Consulting fees		—		0.1
Loss on redemption of convertible junior subordinated debentures		—		2.3
Accretion of discount on convertible subordinated notes		—		0.1
Other		0.2		(0.2)
Non-GAAP net income	\$	6.0	\$	5.4

OVERVIEW OF CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of the Consolidated Financial Statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an ongoing basis, we evaluate estimates and judgments, including those related to revenue recognition, realization of accounts receivable, inventories, goodwill, other intangible assets, property and equipment and deferred tax assets and liabilities. We base our estimates on historical experience, third party data and assumptions that we believe to be reasonable under the circumstances. The results of these considerations form the basis for making judgments about the amount and timing of revenues and expenses, the carrying value of assets and the recorded amounts of liabilities. Actual results may differ from these estimates and such estimates may change if the underlying conditions or assumptions change. Historical performance should not be viewed as indicative of future performance because there can be no assurance that our results of operations will be consistent from year to year.

Management’s discussion and analysis of financial condition and results of operations (“MD&A”) is based upon our Consolidated Financial Statements presented herewith, which have been prepared in accordance with accounting principles generally accepted in the United States. Our significant accounting policies are more fully described in Note 1 to our Consolidated Financial Statements included in this Form 10-Q. Our critical accounting policies are those that are both important to the portrayal of our financial condition and results of operations and require management’s most difficult, subjective and complex judgment. These critical accounting policies are discussed in MD&A in our Annual Report on Form 10-K for the year ended December 31, 2013. There have been no significant changes to our critical accounting policies since the filing of our Annual Report on Form 10-K for the year ended December 31, 2013.

RECENT DEVELOPMENTS

On January 3, 2014, we cancelled all the outstanding Performance-Based Stock Awards (the “PBS Awards”). All holders of the PBS Awards surrendered their outstanding shares in exchange for a cash payout of approximately \$16.1 million. See Item 1, Notes to the Consolidated Financial Statements, Note 17 for additional information.

On January 16, 2014, we sold a cemetery business in Florida that was held for sale at December 31, 2013 for approximately \$0.2 million in cash. See Item 1, Notes to the Consolidated Financial Statements, Note 4 for additional information.

On February 27, 2014, we entered into a fourth amendment to our Credit Facility which (a) allows us to issue senior unsecured debt in an amount not to exceed \$150 million when aggregated with any subordinated debt or convertible subordinated debt issued by us and (b) allows us to refinance our existing convertible junior subordinated debentures with the proceeds of certain of senior unsecured debt, subordinated debt or convertible subordinated debt.

On March 3, 2014, certain of our subsidiaries entered into an Asset Sale Agreement with SCI to acquire four funeral businesses and one cemetery business in the New Orleans, Louisiana region and two funeral businesses in the Northern Virginia region for an aggregate purchase price of \$54.9 million. Under the Asset Sale Agreement, we will acquire the properties, leasehold interests, assets and rights and assume certain liabilities of the businesses being acquired. The closing of the SCI Acquisition is subject to certain closing conditions, including, but not limited to, approval by the Federal Trade Commission. We currently anticipate that the SCI Acquisition will close in the second quarter of 2014.

On March 3, 2014, David J. DeCarlo joined our executive leadership team as President and Vice Chairman of the Board. Mr. DeCarlo will lead our Strategic and Corporate Development, Supply and Project Development and Operations Support including Information Technology and Human Resources. Bill Heiligbrodt is now our Executive Vice President and Secretary and has resigned from the Board. Mr. Heiligbrodt will lead our Treasury and Finance, Accounting and Reporting, Legal and Investor Relations.

On March 19, 2014, we issued \$143.75 million aggregate principal amount of 2.75% Convertible Subordinated Notes due 2021 (the "Notes"). The Notes have not been registered under the Securities Act of 1933, as amended, and were offered only to "qualified institutional buyers" in compliance with Rule 144A under the Securities Act. The Notes bear interest at 2.75%. We used a portion of the proceeds to repay our outstanding balance on our revolving credit facility and to redeem our existing convertible junior subordinated debentures. See Item 1, Notes to the Consolidated Financial Statements, Notes 14 and 15 and Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources for additional information.

On April 14, 2014, we entered into a fifth amendment to our Credit Facility (the "Fifth Amendment"), which provides for an increase in our revolving credit facility from \$125 million to \$200 million and new funding under our term loan so that \$125 million will be outstanding upon effectiveness of the Fifth Amendment. The Fifth Amendment becomes effective upon the consummation of the SCI Acquisition. We currently anticipate that the SCI Acquisition will close in the second quarter of 2014. Borrowings under the term loan facility are subject to amortization payments of 7.5% of the principal amount in the first two years following the Fifth Amendment effective date, 10.0% for the third and fourth years following the effective date and 12.5% per year thereafter. Obligations under the Fifth Amendment mature on March 31, 2019. The Fifth Amendment also modifies the financial covenants so that we must maintain a leverage ratio of 3.75 to 1.00 through March 30, 2015 and 3.50 to 1.00 thereafter.

RESULTS OF OPERATIONS

The following is a discussion of our results of continuing operations for the three months ended March 31, 2013 and 2014. The term "same store" or "existing operations" refers to funeral homes and cemeteries acquired prior to January 1, 2009 and operated for the entirety of each period being presented. Funeral homes and cemeteries purchased after December 31, 2008 are referred to as "acquired." This classification of acquisitions has been important to management and investors in monitoring the results of these businesses and to gauge the leveraging performance contribution that a selective acquisition program can have on total company performance. Depreciation and amortization and regional and unallocated funeral and cemetery costs are not included in operating profit.

Funeral Home Segment. The following tables set forth certain information regarding the revenues and operating profit from the funeral home operations for the three months ended March 31, 2013 compared to the three months ended March 31, 2014.

Three months ended March 31, 2013 compared to three months ended March 31, 2014 (dollars in thousands):

	Three Months Ended March 31,		Change	
	2013	2014	Amount	%
Revenues:				
Same store operating revenue	\$ 33,671	\$ 31,482	\$ (2,189)	(6.5)%
Acquired operating revenue	9,146	10,178	1,032	11.3 %
Preneed funeral insurance commissions	508	564	56	11.0 %
Preneed funeral trust earnings	1,726	1,935	209	12.1 %
Total	\$ 45,051	\$ 44,159	\$ (892)	(2.0)%
Operating profit:				
Same store operating profit	\$ 13,664	\$ 12,103	\$ (1,561)	(11.4)%
Acquired operating profit	3,213	3,772	559	17.4 %
Preneed funeral insurance commissions	110	317	207	188.2 %
Preneed funeral trust earnings	1,712	1,928	216	12.6 %
Total	\$ 18,699	\$ 18,120	\$ (579)	(3.1)%

Funeral home same store operating revenues for the three months ended March 31, 2014 decreased \$2.2 million, or 6.5%, when compared to the three months ended March 31, 2013. Same store operating contracts decreased from 6,435 in the first quarter of 2013 to 6,049 in the first quarter of 2014, while the average revenue per contract remained flat at \$5,469 for the three months ended March 31, 2014. The average revenue per contract includes the impact of the funeral trust fund earnings recognized at the time that we provide the services pursuant to the preneed contract. Excluding funeral trust earnings, the average revenue per contract decreased \$29 from \$5,233 for the three months ended March 31, 2013 to \$5,204 for the three months ended March 31, 2014. The number of traditional burial contracts decreased 8.7%, while the average revenue per burial contract increased 2.6% from \$8,280 in 2013 to \$8,496 in 2014. The cremation rate for same store businesses increased from 45.8% in 2013 to 46.6% in 2014, while the number of cremation contracts decreased 4.5%. The average revenue per same store cremation contract decreased 2.6% to \$3,010. Cremations with services declined from 33.5% of total cremation contracts in the first quarter of 2013 to 31.3% in the first quarter of 2014. The average revenue for "other" contracts, which are charges for merchandise or services for which we do not perform a funeral service and which made up approximately 7.5% of the total number of contracts in the first quarter of 2014, decreased slightly to \$2,174.

Same store operating profit for the three months ended March 31, 2014 decreased \$1.6 million, or 11.4%, from the comparable three months of 2013, and as a percentage of funeral same store operating revenue, decreased to 38.4% from 40.5%. The decrease in operating profit is primarily the result of the decrease in revenue, offset in part, by better management of costs including salaries and benefits and field insurance expenses.

Funeral home acquired revenues for the three months ended March 31, 2014 increased \$1.0 million, or 11.3%, when compared to the three months ended March 31, 2013, as we experienced a 5.7% increase in the number of contracts, and an increase of 6.1%, to \$5,299, in the average revenue per contract for those acquired operations. Excluding funeral trust earnings, the average revenue per contract increased 5.3% to \$5,185. The number of traditional burial contracts increased 11.0%, and the average revenue per burial contract increased 6.5% to \$8,113. The cremation rate for the acquired businesses was 46.1% for the first quarter of 2014 compared to 48.7% in the first quarter of 2013. The average revenue per cremation contract increased 1.8% to \$3,102 for the first quarter of 2014, while the number of cremation contracts remained flat at 904 for the three months ended March 31, 2014. Cremations with services decreased from 35.1% in the three months ended March 31, 2013 to 33.3% for the three months ended March 31, 2014. The increase in the average revenue per contract for acquired operations and the decline in the cremation rate is because the acquired businesses serve primarily traditional burial families.

Acquired operating profit for the three months ended March 31, 2014 increased \$0.6 million, or 17.4%, from the comparable three months of 2013 and, as a percentage of revenue from acquired businesses, was 37.1% for the first quarter of 2014 compared to 35.1% for the first quarter of 2013. Salaries and benefits of acquired operations, as a percentage of revenue, are generally higher as a percentage of revenue than existing locations. As these acquired businesses transition into our Standards Operating Model, we expect to see operating profit margins rise toward those on a same store basis.

The two categories of financial revenue (insurance commissions and trust earnings on matured preneed contracts) on a combined basis increased 11.9% in revenue and 23.2% in operating profit in the three months ended March 31, 2014 as compared to the three months ended March 31, 2013 as a result of higher earnings on trust contracts. Trust earnings also include trust management fees charged by our wholly-owned registered investment advisor based on the fair market value of the trust assets.

Cemetery Segment. The following tables set forth certain information regarding the revenues and operating profit from the cemetery operations for the three months ended March 31, 2013 compared to the three months ended March 31, 2014.

Three months ended March 31, 2013 compared to three months ended March 31, 2014 (dollars in thousands):

	Three Months Ended March 31,		Change	
	2013	2014	Amount	%
Revenues:				
Same store operating revenue	\$ 9,691	\$ 9,712	\$ 21	0.2 %
Acquired operating revenue	69	55	(14)	n/a
Cemetery trust earnings	2,194	1,584	(610)	(27.8)%
Preneed cemetery finance charges	310	337	27	8.7 %
Total	\$ 12,264	\$ 11,688	\$ (576)	(4.7)%
Operating profit:				
Same store operating profit	\$ 3,020	\$ 2,839	\$ (181)	(6.0)%
Acquired operating loss	(27)	(9)	18	n/a
Cemetery trust earnings	2,146	1,561	(585)	(27.3)%
Preneed cemetery finance charges	310	337	27	8.7 %
Total	\$ 5,449	\$ 4,728	\$ (721)	(13.2)%

Cemetery same store operating revenues for the three months ended March 31, 2014 increased slightly to \$9,712, or 0.2%, from \$9,691 for the three months ended March 31, 2013. Preneed property sales decreased \$0.3 million, or 5.7%. We experienced a 6.0% decrease in the number of preneed interment rights (property) sold, while the average price per interment remained flat. The percentage of those interment rights sold that we were able to recognize as revenue, because we received at least 10% of the sales price from the customer, decreased from 92.1% in the three months ended March 31, 2013 to 91.0% in the three months ended March 31, 2014. Same store at-need revenue increased \$0.4 million, or 9.4%, while the number of at-need contracts decreased 2.9%. Revenue from deliveries of preneed merchandise and services declined \$0.2 million, or 13.5%.

Cemetery same store operating profit for the three months ended March 31, 2014 decreased \$0.2 million, or 6.0%. As a percentage of revenues, cemetery same store operating profit decreased from 31.2% to 29.2%. The decrease in cemetery same store operating profit is primarily a result of an increase in bad debt expense, offset by a decrease in insurance costs.

We acquired one cemetery in the second quarter of 2012 which primarily operates as an at-need business. This is the only cemetery business in this category.

The two categories of financial revenue consist of trust earnings and finance charges on preneed receivables. Total trust earnings for the three months ended March 31, 2014 decreased 27.8% when compared to the three months ended March 31, 2013. Earnings from perpetual care trust funds totaled \$1.0 million for the three months ended March 31, 2014 compared to \$1.6 million for the three months ended March 31, 2013, a decrease of \$0.6 million, or 34.4%. Trust earnings recognized upon the delivery of merchandise and service contracts decreased 13.4% from the same period in 2013. Trust earnings also include trust management fees charged by our wholly-owned registered investment advisor based on the fair market value of the trust assets. Finance charges on the preneed contracts increased 8.7%.

Regional and Unallocated Funeral and Cemetery Costs. Regional and unallocated funeral and cemetery costs for the three months ended March 31, 2014 decreased \$0.4 million, or 13.8%, compared to the three months ended March 31, 2013 primarily due to a \$0.2 million decrease in regional management salaries and benefits and a \$0.2 million decrease in termination expenses.

General and Administrative. General and administrative expenses totaled \$9.3 million for the three months ended March 31, 2014, an increase of \$3.1 million, or 48.6%, compared to the three months ended March 31, 2013 primarily due to a \$0.7 million increase in incentive compensation, \$0.8 million increase in stock-based compensation, \$0.7 million increase in

acquisition and divestiture expenses, \$0.6 million increase in termination and consulting expenses, \$0.2 million increase in 401(k) matching and \$0.1 million increase in public company costs.

Interest Expense. Interest expense, net was \$2.6 million and \$2.8 million for the three months ended March 31, 2013 and 2014, respectively. Interest expense increased year over year as 2014 includes approximately \$0.2 million of additional cash interest paid and debt issuance cost amortization on the Notes which did not occur in 2013.

Loss on redemption of convertible subordinated debentures. On March 17, 2014, we called for the redemption of all our outstanding convertible junior subordinated debentures due 2029 held by Carriage Services Capital Trust and the corresponding TIDES at a price \$50 per \$50 principal amount of the convertible junior subordinated debentures being redeemed, plus accrued and unpaid interest to the redemption dated. Redemption period for the TIDES ended April 16, 2014. During the first quarter of 2014, approximately \$61.9 million in principal amount of the convertible junior subordinated debentures were redeemed. We recognized a total loss of \$3.8 million in the three months ended March 31, 2014 as a result of the write-off of the related unamortized debt issuance costs of \$2.9 million and \$0.9 million for the premium paid on the convertible junior subordinated debentures redeemed.

Other Income. For the three months ended March 31, 2014, we recognized a gain of \$1.1 million in connection with the purchase of funeral home building previously under a capital lease.

Income Taxes. We recorded income taxes at the estimated effective rate of 37.9% for the year ended December 31, 2013 and 39.0% for the three months ended March 31, 2014. We have approximately \$47.3 million of state net operating loss carry forwards that will expire between 2015 and 2035, if not utilized. Based on management's assessment of the various state net operating losses, it has been determined that it is more likely than not that we will not be able to realize the tax benefits of certain portions of the state losses. Accordingly, a valuation allowance has been established and is reviewed every quarter related to the deferred tax asset for the state operating losses. At March 31, 2014 the valuation allowance totaled \$0.3 million.

LIQUIDITY AND CAPITAL RESOURCES

Overview

Our primary sources of liquidity and capital resources are internally generated cash flows from operating activities and availability under our Credit Facility (as defined below under *Debt Obligations*). We generate cash in our operations primarily from at-need sales and delivery of preneed sales. We also generate cash from earnings on our cemetery perpetual care trusts. We believe that existing cash balances, future cash flows from operations and borrowings under our Credit Facility will be sufficient to meet our anticipated working capital requirements, capital expenditures, scheduled debt payments, commitments, dividend payments and acquisitions for the foreseeable future. Based on our recent operating results, current cash position, anticipated future cash flows and sources of financing that we expect to have available, we do not anticipate any significant liquidity constraints in the foreseeable future. However, if our capital expenditures or acquisition plans for 2014 change, we may need to access the capital markets to obtain additional funding. Further, to the extent operating cash flow or access to and cost of financing sources are materially different than expected, future liquidity may be adversely affected. Please read Part I, Item IA "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2013.

Cash Flows

We began 2014 with \$1.4 million in cash and other liquid investments and ended the first quarter with \$22.0 million in cash. As of March 31, 2014, we had no outstanding borrowings on our revolving credit facility.

The following table sets forth the elements of cash flow for the three months ended March 31, 2013 and March 31, 2014 (in millions):

	For the Three Months Ended March 31,	
	2013	2014
Cash at January 1st	\$ 1.7	\$ 1.4
Cash flow from operating activities	9.9	(1.6)
Acquisitions and new construction	(6.0)	—
Proceeds from the sale of businesses and other assets	2.0	0.2
Net payments on our revolving credit facility, term loan and long-term debt obligations	(4.4)	(40.1)
Proceeds from issuance of convertible subordinated notes	—	143.7
Payment of issuance costs related the convertible subordinated notes	—	(4.4)
Redemption of convertible junior subordinated debentures	—	(61.9)
Payments for performance awards	—	(16.2)
Maintenance capital expenditures	(1.8)	(0.9)
Growth capital expenditures	(0.8)	(4.1)
Dividends on common stock	(0.4)	(0.4)
Excess tax benefit of equity compensation	0.9	5.6
Other financing costs	0.2	0.6
Cash at March 31st	<u>\$ 1.3</u>	<u>\$ 21.9</u>

For the three months ended March 31, 2014 cash used in operating activities was \$1.6 million compared to cash provided by operating activities of \$9.9 million for the three months ended March 31, 2013. The decrease in cash was primarily due to non-cash adjustments to operating activities of \$3.0 million decrease in net income, a \$4.9 million deferred tax benefit related to the cash out payments of the performance-based stock awards and a \$2.0 million gain recognized on the sale of a cemetery and the purchase of a building previously held as a capital lease offset, in part, by a \$2.9 million write-off of unamortized deferred loan costs related to the redemption of the convertible junior subordinated debentures and a \$0.8 million increase in stock-based compensation expense as a result of the write-off of unamortized stock-based compensation expense related to the cancellation of our performance-based stock awards. The decrease in cash due to working capital changes was due to a \$4.9 million decrease in accounts payable and accrued liabilities as a result of reduction in accruals related to income and property taxes and interest related to the convertible junior subordinated debentures.

Our investing activities resulted in a net cash outflow of \$4.8 million for the three months ended March 31, 2014 compared to \$6.6 million for the three months ended March 31, 2013. The decrease was due to lower new construction expenditures and lower proceeds from the sale of businesses and other assets, offset by an increase in capital expenditures. We acquired land for approximately \$6.0 million in the three months ended March 31, 2013 for funeral home expansion projects. For the three months ended March 31, 2014, we sold a business for approximately \$0.2 million compared to net proceeds of \$2.0 million for businesses sold in the three months ended March 31, 2013.

For the three months ended March 31, 2014, capital expenditures totaled \$5.0 million compared to \$2.6 million for the three months ended March 31, 2013. For the three months ended March 31, 2014, we purchased two buildings which we previously leased for approximately \$3.1 million. Maintenance capital expenditures were \$0.9 million in the three months ended March 31, 2014 compared to \$1.8 million in the three months ended March 31, 2013. The decrease in maintenance capital expenditures of \$0.9 million was primarily due to decreases in expenditures for information technology and infrastructure improvements of \$0.4 million and other funeral and cemetery major repair projects of \$0.4 million. Additionally, we had a decrease of \$0.1 million in vehicles purchased in 2014 as compared to 2013.

Our financing activities resulted in a net cash inflow of \$27.0 million for the three months ended March 31, 2014 compared to a net cash outflow of \$3.7 million for the three months ended March 31, 2013. During the three months ended March 31, 2014, we received proceeds of approximately \$143.75 million from the issuance of convertible subordinated notes in March 2014. We paid transaction costs of approximately \$4.3 million related to the issuance of these notes. In connection of with issuance of the notes, we paid \$61.9 million in principal to redeem our outstanding convertible junior subordinated debentures and paid down our revolving credit facility. During the three months ended March 31, 2014, we repaid \$3.0 million on our term loan. During the three months ended March 31, 2013, we had net payments of \$1.7 million on our Credit Facility and repaid \$2.5 million on our term loan. Additionally, during the three months ended March 31, 2014, we paid approximately

\$16.1 million related to performance-based stock awards. During the three months ended March 31, 2014, we recognized \$5.6 million related to the excess tax benefit of equity compensation.

Dividends

Our Board declared a quarterly dividend of \$0.025 per share, totaling approximately \$0.5 million, which was paid on March 3, 2014 to record holders of our common stock as of February 13, 2014. We have a dividend reinvestment program so that stockholders may elect to reinvest their dividends into additional shares of our common stock.

Debt Obligations

As of March 31, 2014, we had a \$255 million credit facility with Bank of America, N.A. as the Administrative Agent comprised of a \$125 million revolving credit facility and a \$130 million term loan. The Credit Facility also contains an accordion provision to borrow up to an additional \$40 million in revolving loans, subject to certain conditions. The Credit Facility is set to mature on September 30, 2017 and is collateralized by all personal property and funeral home real property in certain states. As of March 31, 2014, we had nothing drawn under the revolving credit facility and \$114.0 million was outstanding under the term loan. No letters of credit were issued and outstanding under the Credit Facility at March 31, 2014. Under the Credit Facility, outstanding borrowings bear interest at either a prime rate or a LIBOR rate, plus an applicable margin based upon the Company's leverage ratio. At March 31, 2014, the prime rate margin was equivalent to 1.50% and the LIBOR margin was 2.50%. The weighted average interest rate on the Credit Facility for the three months ended March 31, 2014 was 2.7% .

The outstanding principal of long-term debt and capital lease obligations at March 31, 2014 totaled \$117.2 million and consisted of \$114.0 million under our term loan and \$3.2 million in acquisition indebtedness and capital lease obligations.

On February 27, 2014, we entered into a fourth amendment to our Credit Facility which (a) allows us to issue senior unsecured debt in an amount not to exceed \$150 million when aggregated with any subordinated debt or convertible subordinated debt issued by us and (b) allows us to refinance our existing convertible junior subordinated debentures with the proceeds of certain of senior unsecured debt, subordinated debt or convertible subordinated debt.

We were in compliance with the covenants contained in the Credit Facility as of March 31, 2014. Key ratios that we must comply with include a Total Debt to EBITDA ratio that as of the last day of each quarter must not be greater than 3.75 to 1.00 through September 30, 2014 and no more than 3.50 to 1.00 thereafter and a fixed charge coverage ratio that must not be less than 1.20 to 1.00. As of March 31, 2014, the leverage ratio was 2.18 to 1.00 and the fixed charge coverage ratio was 1.83 to 1.00. The leverage ratio decline to below 3.00 to 1.00 at June 30, 2013 automatically triggered a 50 basis point rate decline on all our term loan and revolving credit facility during the third quarter of 2013.

On April 14, 2014, we entered into a Fifth Amendment which provides, among other things, for an increase in our revolving credit facility from \$125 million to \$200 million and new funding under our term loan so that \$125 million will be outstanding upon effectiveness of the Fifth Amendment. The Fifth Amendment becomes effective upon the consummation of the SCI Acquisition. We currently anticipate that the SCI Acquisition will close in the second quarter of 2014. Borrowings under the term loan facility are subject to amortization payments of 7.5% of the principal amount in the first two years following the Fifth Amendment effective date, 10.0% for the third and fourth years following the effective date and 12.5% per year thereafter. Obligations under the Fifth Amendment mature on March 31, 2019. The Fifth Amendment also modifies the financial covenants so that we must maintain a leverage ratio of 3.75 to 1.00 through March 30, 2015 and 3.50 to 1.00 thereafter.

Convertible Subordinated Notes due 2021

On March 19, 2014, we issued \$143.75 million aggregate principal amount of Notes. The Notes have not been registered under the Securities Act of 1933, as amended (the "Securities Act"), and were offered only to "qualified institutional buyers" in compliance with Rule 144A under the Securities Act. The Notes are governed by an indenture dated as of March 19, 2014 between Wilmington Trust, National Association, as Trustee, and us (the "Indenture"). The Notes bear interest at 2.75%. Interest on the Notes accrues from March 19, 2014 and is payable semi-annually in arrears on March 15 and September 15 of each year, beginning September 15, 2014.

The Notes are general unsecured obligations and will be subordinated in the right of payment to all of our existing and future senior indebtedness and equal in right of payment with our other existing and future subordinated indebtedness. The initial conversion rate of the Notes is 44.3169 shares of our common stock per \$1,000 principal amount of the Notes, equivalent to an initial conversion price of approximately \$22.56 per share of common stock. The conversion rate is subject to adjustment upon the occurrence of certain events as described in the Indenture.

The Notes mature on March 15, 2021, unless earlier converted or purchased by us. Holders of the Notes may convert their Notes at their option at any time prior to December 15, 2020, if one or more of the following conditions has been satisfied: (1) during any fiscal quarter (and only during such fiscal quarter) commencing after March 31, 2014, if, for a least 20 trading days, (whether or not consecutive) during the 30 consecutive trading day period ending on the last trading day of the immediately preceding fiscal quarter, the last reported sales price of our common stock for such trading day is greater than or equal to 130% of the applicable conversion price on such trading day; (2) during the five consecutive business day period immediately following any five consecutive trading day period (the "Measurement Period"), in which, for each trading day of the Measurement Period, the trading price (as defined in the Indenture) per \$1,000 principal amount of the Notes for such trading day was less than 98% of the product of last reported sale price of our common stock for such trading day and the applicable conversion rate on such trading day; or (3) upon the occurrence of specified corporate transactions described in the Indenture. Holders may also convert their Notes at their option at any time beginning on December 15, 2020, and ending on the close of business on the business day immediately preceding the maturity date.

We may not redeem the Notes prior to maturity. However, in the event of a fundamental change (as defined in the Indenture), subject to certain conditions, a holder of the Notes will have the option to require us to purchase all or a portion of its Notes for cash. The fundamental change purchase price will equal 100% of the principal amount of the Notes to be purchased, plus any accrued and unpaid interest, if any, to, but excluding, the fundamental change purchase date.

The conversion option of the Notes is not an embedded derivative. In order to be a derivative, the conversion feature would need to be able to be settled in cash, or an instrument readily convertible to cash. We do not intend to issue a registration statement for the resale of the common stock issuable upon conversion. Thus, the shares that the holder will receive upon conversion are not readily convertible to cash.

We have recorded the issuance of the Notes per the guidance provided under ASC 470, Topic 20, *Debt with Conversion and Other Options*, which requires that we separate the Notes into a liability component and an equity component. The carrying amount of the liability is calculated by measuring the fair value of a similar liability (including any embedded features other than the conversion option) that does not have an associated equity component. The carrying amount of the liability component was determined based on a bond discount rate of 6.75%. The carrying amount of the equity component representing the embedded conversion option was determined by deducting the fair value of the liability component from the initial proceeds of the Notes and is recorded in Additional Paid in Capital ("APIC") on our Consolidated Balance Sheet. The excess of the principal amount of the liability over its carrying amount is amortized to interest expense using the effective interest method. The expected life of the liability component will not be reassessed in subsequent periods unless the terms are modified.

We received proceeds of approximately \$143.75 million and paid transactions costs of approximately \$4.3 million. We used a portion of the proceeds to repay our outstanding balance on our revolving credit facility and to redeem our existing convertible junior subordinated debentures.

Subsequent to the issuance of the Notes, we accrued additional transaction costs of \$0.8 million. Total transaction costs of \$5.1 million were allocated to the liability and equity components in proportion to the allocation of the initial proceeds and accounted for as debt issuance costs and equity issuance costs, respectively. Debt issuance costs are included in Deferred charges and other non-current assets on our Consolidated Balance Sheet and are being amortized using the effective interest method over the seven year term of the Notes. Equity issuance costs are included in Additional Paid in Capital ("APIC") on our Consolidated Balance Sheet and are not amortized. Additionally, the recognition of the Notes as two separate components results in a basis difference associated with liability component which represents a temporary difference. As a result, we recognized a deferred tax liability of \$12.7 million related to this temporary difference which was recorded as a reduction to APIC and an increase to our deferred tax liability.

At March 31, 2014, the carrying amount of the equity component was \$31.7 million. At March 31, 2014, the principal amount of the liability component was \$143.75 million and the net carrying amount was \$112.3 million. The unamortized discount of \$31.5 million as of March 31, 2014 will be amortized over the remaining term of seven years.

For the three months ended March 31, 2014, we recognized contractual coupon interest expense of \$0.1 million and interest expense of \$0.2 million related to the accretion of the debt discount. The effective interest rate on the liability component for the three months ended March 31, 2014 was 6.75%. Additionally, we recognized amortization expense of \$44,000 related to the debt issuance costs.

Convertible Junior Subordinated Debentures Payable To Affiliate And Company Obligated Mandatorily Redeemable Convertible Preferred Securities of Carriage Services Capital Trust

On March 17, 2014, we called for the redemption of all our outstanding convertible junior subordinated debentures due 2029 held by Carriage Services Capital Trust for redemption on April 16, 2014 at a price \$50 per \$50 principal amount of the convertible junior subordinated debentures being redeemed, plus accrued and unpaid interest to the redemption dated. In March 2014, we used a portion of the net proceeds from the issuance of the Notes to repurchase approximately \$61.9 million in principal amount of the convertible junior subordinated debentures and \$0.9 million associated with the call premium. At December 31, 2013 and March 31, 2014, amounts outstanding under the convertible junior subordinated debentures totaled \$89.8 million and \$27.9 million, respectively.

We intend to use cash on hand and borrowing under our Credit Facility primarily to acquire funeral home and cemetery businesses and for internal growth projects, such as cemetery inventory development and funeral home expansion projects. We have the ability to draw on our revolving credit facility, subject to customary terms and conditions of the credit agreement. We believe that existing cash balances, future cash flows from operations and the borrowing under our Credit Facility described above will be sufficient to meet our anticipated working capital requirements, capital expenditures, scheduled debt payments, commitments, dividends and acquisitions for the foreseeable future.

SEASONALITY

Our business can be affected by seasonal fluctuations in the death rate. Generally, the death rate is higher during the winter months because the incidences of death from influenza and pneumonia are higher during this period than other periods of the year.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

In the ordinary course of business, we are typically exposed to a variety of market risks. Currently, these are primarily related to interest rate risk and changes in the values of securities associated with the preneed and perpetual care trusts. Management is actively involved in monitoring exposure to market risk and developing and utilizing appropriate risk management techniques when appropriate and when available for a reasonable price. We are not exposed to any other significant market risks.

The following quantitative and qualitative information is provided about financial instruments to which we are a party at March 31, 2014 and from which we may incur future gains or losses from changes in market conditions. We do not enter into derivative or other financial instruments for speculative or trading purposes.

Hypothetical changes in interest rates and the values of securities associated with the preneed and perpetual care trusts chosen for the following estimated sensitivity analysis are considered to be reasonable near-term changes generally based on consideration of past fluctuations for each risk category. However, since it is not possible to accurately predict future changes in interest rates, these hypothetical changes may not necessarily be an indicator of probable future fluctuations.

The following information about our market-sensitive financial instruments constitutes a “forward-looking statement.”

In connection with our preneed funeral operations and preneed cemetery merchandise and service sales, the related funeral and cemetery trust funds own investments in equity and debt securities and mutual funds, which are sensitive to current market prices. Cost and market values of such investments as of March 31, 2014 are presented in Item I, Notes to the Consolidated Financial Statements, Notes 6, 8 and 10 to our Consolidated Financial Statements in this Form 10-Q. See also Item 2, Management’s Discussion and Analysis of Financial Condition and Results of Operations in this Form 10-Q. The sensitivity of the fixed income securities is such that a 0.25% change in interest rates causes an approximate 1.5% change in the value of the fixed income securities.

We monitor current and forecasted interest rate risk in the ordinary course of business and seek to maintain optimal financial flexibility, quality and solvency. As of March 31, 2014, we had no outstanding borrowings under our \$125 million revolving credit facility and \$114.0 million outstanding on our term loan. Any further borrowings or voluntary prepayments against the revolving credit facility or any change in the floating rate would cause a change in interest expense. We have the option to pay interest under the Credit Facility at either prime rate or LIBOR rate plus a margin. At March 31, 2014, the prime rate margin was equivalent to 1.50% and the LIBOR margin was 2.50%. Assuming the outstanding balance remains unchanged, a change of 100 basis points in our borrowing rate would result in a change in income before taxes of \$1.1 million. We have not entered into interest rate hedging arrangements in the past. Management continually evaluates the cost and potential benefits of interest rate hedging arrangements.

The remaining unredeemed convertible junior subordinated debentures, payable to the Trust, pay interest at the fixed rate of 7% and are carried on our Consolidated Balance Sheet at a cost of approximately \$27.9 million. The estimated fair value of these securities is estimated to be approximately \$28.0 million at March 31, 2014, based on available broker quotes of the corresponding preferred securities issued by the Trust.

The fair value of the Notes due 2021 issued in March 2014 is approximately \$151.7 million based on the last traded or broker quoted price.

Increases in market interest rates may cause the value of these debt instruments to decrease but such changes will not affect our interest costs. The remainder of our long-term debt and leases consist of non-interest bearing notes and fixed rate instruments that do not trade in a market and do not have a quoted market value. Any increase in market interest rates causes the fair value of those liabilities to decrease.

Item 4. Controls and Procedures

Management's Evaluation of Disclosure Controls and Procedures

Our management, including our principal executive and financial officers, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of the end of the period covered by this Form 10-Q. Our disclosure controls and procedures are designed to ensure that the information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and to ensure that such information is accumulated and communicated to management, including our principal executive and financial officers, as appropriate, to allow timely decisions regarding required disclosure. Based on such evaluation, our principal executive and financial officers have concluded that our disclosure controls and procedures were effective as of March 31, 2014 (the end of the period covered by this Form 10-Q) at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

During the three months ended March 31, 2014, there was no change in our system of internal control over financial reporting (defined in Rules 13a-15(f) or 15d-15(f) under the Exchange Act) that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION**Item 1. Legal Proceedings**

In addition to the matters in Note 16 to our Consolidated Financial Statements, we and our subsidiaries are parties to a number of legal proceedings that arise from time to time in the ordinary course of our business. While the outcome of these proceedings cannot be predicted with certainty, we do not expect these matters to have a material adverse effect on our financial statements. We self-insure against certain risks and carry insurance with coverage and coverage limits for risk in excess of the coverage amounts consistent with our assessment of risks in our business and of an acceptable level of financial exposure. Although there can be no assurance that self-insurance reserves and insurance will be sufficient to mitigate all damages, claims, or contingencies, we believe that the reserves and our insurance provides reasonable coverage for known asserted and unasserted claims. In the event we sustain a loss from a claim, and the insurance carrier disputes coverage or coverage limits, we may record a charge in a different period than the recovery, if any, from the insurance carrier.

Item 1A. Risk Factors

There have been no material changes in our risk factors as previously disclosed in “Part I, Item 1A. Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2013. Readers should carefully consider the factors discussed in Part 1, Item 1A “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2013, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K for the year ended December 31, 2013 are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition or future results.

Item 6. Exhibits

<u>Exhibit No.</u>	<u>Description</u>
2.1	Asset Sale Agreement dated as of March 3, 2014, by and among Carriage Services of Louisiana, Inc., Carriage Funeral Holdings, Inc., SCI Louisiana Funeral Services, Inc., S.E. Funeral Homes of Louisiana, LLC and S.E. Funeral Homes of Virginia, LLC. Incorporated herein by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed March 5, 2014.
4.1	Indenture, dated as of March 19, 2014, by and among Carriage Services, Inc. and Wilmington Trust, National Association, as Trustee. Incorporated herein by reference to Exhibit 4.1 on the Company's Current Report on Form 8-K filed March 19, 2014.
10.1	Fifth Amendment to Credit Agreement dated as of April 14, 2014, by and among Carriage Services, Inc., the banks listed on the signature page thereto and Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer. Incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on April 16, 2014.
10.2	Fourth Amendment to Credit Agreement dated as of February 27, 2014, by and among Carriage Services, Inc., the banks listed on the signature page thereto and Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer. Incorporated herein by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed March 5, 2014.
10.3	Purchase Agreement dated as of March 13, 2014 by and among Carriage Services, Inc. and Merrill Lynch, Pierce, Fenner & Smith Incorporated, as representative of the Initial Purchasers named in Schedule A thereto. Incorporated herein by reference to the Company's Current Report on Form 8-K filed March 19, 2014.
*10.4	First Amendment to Second Amended and Restated Employment Agreement by and between Carriage Services, Inc. and Melvin C. Payne dated March 3, 2014.
*10.5	Second Amended and Restated Employment Agreement by and between Carriage Services, Inc. and L. William Heiligbrodt dated March 3, 2014.

*10.6	Employment Agreement by and between Carriage Services, Inc. and David J. DeCarlo dated March 3, 2014.
*31.1	Certification of Periodic Financial Reports by Melvin C. Payne in satisfaction of Section 302 of the Sarbanes-Oxley Act of 2002.
*31.2	Certification of Periodic Financial Reports by L. William Heiligbrodt in satisfaction of Section 302 of the Sarbanes-Oxley Act of 2002.
*32	Certification of Periodic Financial Reports by Melvin C. Payne and L. William Heiligbrodt in satisfaction of Section 906 of the Sarbanes-Oxley Act of 2002 and 18 U.S.C. Section 1350.
**101	Interactive Data Files.

* Filed or furnished herewith, as applicable.

** Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, or Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability.

SIGNATURE

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: May 7, 2014

CARRIAGE SERVICES, INC.

/s/ L. William Heiligbrodt

L. William Heiligbrodt

Executive Vice President and Secretary

(Principal Financial Officer)

CARRIAGE SERVICES, INC.

INDEX OF EXHIBITS

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**FIRST AMENDMENT TO
SECOND AMENDED AND RESTATED
EMPLOYMENT AGREEMENT**

THIS FIRST AMENDMENT TO SECOND AMENDED AND RESTATED EMPLOYMENT AGREEMENT (this "**First Amendment**") is executed and agreed to by and between Carriage Services, Inc., a Delaware corporation (the "**Company**"), and Melvin C. Payne ("**Employee**"), effective as of March 3, 2014 (the "**Amendment Effective Date**").

WHEREAS, the Company and Employee have heretofore entered into that certain Second Amended and Restated Employment Agreement effective as of March 14, 2012 (the "**Agreement**"); and

WHEREAS, the Company and Employee desire to amend the Agreement in certain respects.

NOW, THEREFORE, in consideration of the premises set forth above and the mutual agreements set forth herein, the Company and Employee hereby agree that the Agreement shall be amended as hereafter provided, effective as of the Amendment Effective Date:

1. Section 2.1 of the Agreement shall be deleted and the following shall be substituted therefor:

"2.1 Term. Unless sooner terminated pursuant to other provisions hereof, the Company agrees to employ Employee for the period beginning on March 3, 2014 and ending on March 3, 2018 (the "**Employment Period**"); provided, however, that on each anniversary of March 3, 2014 (the "**Anniversary Date**"), so long as this Agreement has not been earlier terminated, the Employment Period shall be extended for another year so that, absent a termination of this Agreement or the provision of a notice of non-extension pursuant to the next sentence, there shall be between three and four years remaining in the then-existing Employment Period. Notwithstanding the foregoing, at least sixty (60) days prior to each anniversary of the Anniversary Date, either the Company or Employee may provide the other Party with notice that it does not intend for the automatic extension referenced in the previous sentence to occur. In the event that such a notice of non-extension is provided, no future extensions of the Employment Period shall occur and, unless Employee's employment hereunder is sooner terminated pursuant to the other provisions hereof, the Employment Period shall terminate as of the expiration of the Employment Period that existed on the date that such notice of non-extension is provided."

2. Section 3.1 of the Agreement shall be deleted and the following shall be substituted therefor:

"3.1 Base Salary. During the period that he is employed hereunder, Employee shall receive an annualized base salary of \$625,000 (the "**Base**

Salary”). Employee’s Base Salary will be reviewed annually, and any increase thereof shall remain in the sole discretion of the Board, acting through its Compensation Committee (the “**Compensation Committee**”). Employee’s Base Salary shall be paid in equal installments in accordance with Company’s standard policy regarding payment of compensation to similarly situated employees, but no less frequently than monthly.”

3. Except as expressly modified by this First Amendment, the terms of the Agreement shall remain in full force and effect and are hereby confirmed and ratified.

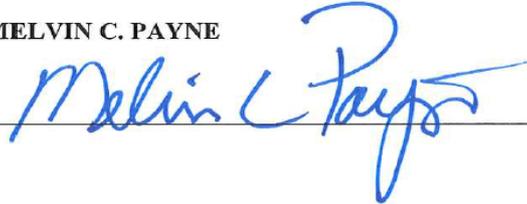
[Remainder of Page Intentionally Blank;
Signature Page Follows]

IN WITNESS WHEREOF, the parties hereto have executed and delivered this First Amendment as of the date first set forth above.

CARRIAGE SERVICES, INC.

By: 
L. William Heiligbrodt
Executive Vice President and Secretary

MELVIN C. PAYNE



SIGNATURE PAGE TO
FIRST AMENDMENT TO
SECOND AMENDED AND RESTATED
EMPLOYMENT AGREEMENT

SECOND AMENDED AND RESTATED EMPLOYMENT AGREEMENT

THIS SECOND AMENDED AND RESTATED EMPLOYMENT AGREEMENT (this “*Agreement*”) is made by and between Carriage Services, Inc., a Delaware corporation (the “*Company*”) and L. William Heiligbrodt, a resident of Harris County, Texas (“*Employee*”). Employee and the Company are referred to individually herein as a “*Party*” and collectively as the “*Parties.*”

WITNESSETH:

WHEREAS, Employee is employed by the Company pursuant to that certain First Amended and Restated Employment Agreement dated March 14, 2012 (the “*Prior Agreement*”);

WHEREAS, the Parties wish to amend and restate the terms of Employee’s employment with the Company and enter into this Agreement, which shall supersede and replace the Prior Agreement in its entirety; and

WHEREAS the Company desires to continue to employ Employee, and Employee desires to continue to be employed by the Company, on the terms and conditions, and for the consideration, set forth herein.

NOW, THEREFORE, for and in consideration of the mutual promises, covenants and obligations contained herein, the Company and Employee agree as follows:

**ARTICLE I
EMPLOYMENT AND DUTIES**

1.1 Employment; Effective Date. The Company agrees to employ Employee and Employee agrees to be employed by the Company, on the terms herein, beginning as of March 3, 2014 (the “*Effective Date*”) and continuing for the period of time set forth in Article II of this Agreement, subject to the terms and conditions of this Agreement.

1.2 Positions. From and after the Effective Date, Employee shall be employed in the position of Executive Vice President and Secretary or in such other position or positions as the Parties mutually may agree, and Employee shall report to the Company’s Chief Executive Officer.

1.3 Duties and Services. Employee agrees to serve in the position(s) referred to in Section 1.2 and to perform diligently and to the best of Employee’s abilities the duties and services appertaining to such positions, as well as such additional duties and services appropriate to such positions which the Parties mutually may agree upon from time to time. Employee’s employment shall also be subject to the policies maintained and established by the Company, as such policies may be amended from time to time.

1.4 Other Interests. Employee agrees, during the period of his employment by the Company, to devote his full business time, energy and attention to the business and affairs of the Company and its Affiliates, if applicable. Employee may serve on corporate, industry, civic, religious or charitable boards or committees without violating this Section 1.4 so long as such

activities do not violate the terms of Articles IV or VI of this Agreement, present a conflict of interest, or interfere in any material respect with the performance of Employee's duties and responsibilities pursuant to this Agreement; *provided, further* that any service by Employee on a board or committee of a for-profit entity shall be subject to the prior approval of the Board of Directors of the Company (the "**Board**").

1.5 Duty of Loyalty. Employee acknowledges that Employee owes a fiduciary duty of loyalty, fidelity and allegiance to act in the best interests of the Company and to do no act that would injure the business, interests, or reputation of the Company or its Affiliates. Consistent with those duties, Employee agrees to disclose to the Company all business opportunities pertaining to the Company's business and shall not appropriate (directly or indirectly) for Employee's own benefit business opportunities concerning the Company's business. If Employee's other business interests present a conflict of interest with the Company's business, Employee shall fully disclose the conflict.

ARTICLE II TERM AND TERMINATION OF EMPLOYMENT

2.1 Term. Unless sooner terminated pursuant to other provisions hereof, the Company agrees to employ Employee for the period beginning on the Effective Date and ending on the fourth anniversary of the Effective Date (the "**Employment Period**"); *provided, however*, that on each anniversary of the Effective Date, so long as this Agreement has not been earlier terminated, the Employment Period shall be extended for another year so that, so long as this Agreement has not been terminated or a notice of non-extension has not been given pursuant to the following sentence, there shall be between three and four years remaining in the then-existing Employment Period. Notwithstanding the foregoing, at least sixty (60) days prior to each anniversary of the Effective Date, either the Company or Employee may provide the other party notice that it does not intend for the automatic extension referenced in the previous sentence to occur. In the event that such a notice of non-extension is provided, no future extensions shall occur and, unless Employee's employment hereunder is sooner terminated pursuant to the other provisions hereof, the Employment Period shall terminate as of the expiration of the Employment Period that existed on the date that such notice of non-extension was provided.

2.2 Company's Right to Terminate. Notwithstanding the provisions of Section 2.1, Employee's employment by the Company shall automatically terminate upon the death of Employee, and the Company shall have the right to terminate Employee's employment under this Agreement at any time for any of the following reasons:

(a) upon Employee's becoming incapacitated by accident, sickness or other circumstance which has rendered him mentally or physically incapable of performing the duties and services required of him hereunder on a full-time basis for a period of at least 180 consecutive days (Employee's "**Disability**");

(b) for "**Cause**," which for purposes of this Agreement shall mean: (i) Employee's conviction of, or plea of no contest to, a misdemeanor involving moral turpitude or a felony, (ii) Employee's repeated failure or refusal to perform all of his duties, obligations and agreements herein contained or imposed by law, including his

fiduciary duties, to the reasonable satisfaction of the Board; (iii) Employee's commission of acts amounting to gross negligence or willful misconduct to the material detriment of the Company; or (iv) Employee's material breach of any provision of this Agreement or uniformly applied provision of the Company's employee handbook or other personnel policies, including without limitation, its Code of Business Conduct and Ethics. Such determination of "Cause" shall be made by the Board and, in the event of circumstances described in (ii) or (iv), the Board shall give written notice to Employee specifying such circumstances and providing a period of 30 days in which Employee shall be allowed to cure such circumstances if capable of cure; or

(c) at any time for any other reason whatsoever or for no reason at all, in the sole discretion of the Company.

2.3 Employee's Right to Terminate. Notwithstanding the provisions of Section 2.1, Employee shall have the right to terminate his employment under this Agreement at any time for any reason whatsoever or for no reason at all. If Employee terminates his employment under this Agreement after the second anniversary of the Effective Date, then such termination shall be treated as Employee's "**Retirement**" for purposes of this Agreement so long as Employee provides written notice to the Company of his intent to terminate his employment at least six months prior to the effective date of such termination.

2.4 Notice of Termination and Effective Date of Termination.

(a) *Notice of Termination.* If the Company or Employee desires to terminate Employee's employment hereunder, the Company or Employee shall do so by giving written notice to the other Party that it or he has elected to terminate Employee's employment hereunder and stating the effective date of the termination and reason for such termination; *provided, however,* that in the event that Employee has provided notice to the Company of his termination of employment, the Company may determine, in its sole discretion, that such termination shall be effective on any date prior to the effective date of termination provided in such notice (and, if such earlier date is so required, then it shall not change the basis for Employee's termination of employment nor be construed or interpreted as a termination of employment pursuant to Section 2.2). No action by either Party pursuant to this Section 2.4(a) shall alter or amend any other provisions hereof or rights arising hereunder, including, without limitation, the provisions of Articles IV, V and VI hereof.

(b) *Date of Termination.* The effective date of Employee's termination will be as follows: (i) if Employee's employment is terminated by his death, the date of his death; (ii) if Employee's employment is terminated by the Company for any reason, then the date specified in the notice of termination delivered to Employee by the Company; (iii) if Employee's employment is terminated by Employee pursuant to Section 2.3 above, then, unless the Company exercises its right pursuant to Section 2.4(a) above to specify an earlier date, the date specified in the notice of such termination delivered to the Company by Employee; or (iv) Employee's employment is terminated upon the expiration of the Employment Period after the issuance of a notice of non-extension pursuant to Section 2.1 above, then the date on which the Employment Period expires.

2.5 Deemed Resignations. Unless otherwise agreed to in writing by the Parties prior to the termination of Employee's employment, any termination of Employee's employment shall constitute an automatic resignation of Employee (i) as an officer of the Company and each of the Company's Affiliates (if applicable), (ii) from the Board (if applicable) and from the board of directors (or similar governing body) of each of the Company's Affiliates (if applicable), and (iii) from the board of directors (or similar governing body) of any corporation, limited liability company or other entity in which the Company holds an equity interest and with respect to which board (or similar governing body) Employee serves as a designee or other representative of the Company.

2.6 Separation from Service. For purposes of this Agreement, references to Employee's termination of employment shall mean, and be interpreted in accordance with, Employee's "separation from service" from the Company within the meaning of Treasury Regulation § 1.409A-1(h)(1)(ii).

ARTICLE III COMPENSATION AND BENEFITS

3.1 Base Salary. During the period that he is employed hereunder, Employee shall receive an annualized base salary of \$545,000 (the "**Base Salary**"). Employee's Base Salary will be reviewed annually, and any increase therein shall remain in the sole discretion of the Board, acting through its Compensation Committee (the "**Compensation Committee**"). Employee's Base Salary shall be paid in equal installments in accordance with the Company's standard policy regarding payment of compensation to similarly situated employees, but no less frequently than monthly.

3.2 Annual Bonuses. For each complete calendar year that he is employed hereunder, Employee shall be eligible to receive such annual bonus as may be determined in the Company's discretion (each an "**Annual Bonus**") after considering specified corporate and individual performance goals established by the Compensation Committee at its first meeting of the fiscal year. The goals for the Annual Bonus will be established at three levels: (i) threshold; (ii) target; and (iii) maximum. If the Compensation Committee determines that performance is achieved (i) at the threshold level, the Annual Bonus shall be 40% of the Base Salary; (ii) at the target level, the Annual Bonus shall be 80% of the Base Salary; and (iii) at the maximum level, the Annual Bonus shall be 160% of the Base Salary. In the discretion of the Compensation Committee, Annual Bonuses for performance falling between threshold, target and maximum goals may be ratably scaled above and below the goal levels. The Annual Bonus shall be payable before March 15 of the year following the calendar year to which the Annual Bonus relates, following the certification of applicable year-end financial results. Employee must be employed by the Company on the payment date in order to earn and receive an Annual Bonus.

3.3 Expenses. The Company shall promptly reimburse Employee for all reasonable business expenses incurred by Employee in performing services hereunder, including all expenses of travel and lodging expenses while away from home on business or at the request of the Company; provided, in each case, that such expenses are incurred and accounted for in accordance with the policies and procedures established by the Company from time to time. Any such reimbursement of expenses shall be made by the Company upon or as soon as practicable

following receipt of supporting documentation reasonably satisfactory to the Company (but in any event not later than the close of Employee's taxable year following the taxable year in which the expense is incurred by Employee). In no event shall (i) any reimbursement under this Section 3.3 be made to Employee for such expenses incurred after the date of Employee's termination of employment with the Company, (ii) Employee be permitted to receive a payment or other benefit in lieu of reimbursement, or (iii) the amount of expenses for which Employee is eligible to receive reimbursement during any calendar year effect the amount of expenses for which Employee is eligible to receive reimbursement during any other calendar year within the term of this Agreement.

3.4 Vacation. During Employee's employment hereunder, Employee shall be entitled to four (4) weeks paid vacation each calendar year, subject to the Company's vacation policies as may exist from time to time.

3.5 Special One-Time Bonus. The Company shall pay Employee a one-time special bonus equal to \$1,000,000 on the Company's first regularly scheduled pay date coincident with or next following the Effective Date.

3.6 Equity-Based Compensation. Employee shall be eligible to receive equity-based compensation awards under the terms of the Company's Second Amended and Restated 2006 Long Term Incentive Plan or one or more of the Company's other equity incentive plans in effect from time to time, as determined by the Compensation Committee of the Board in its sole discretion.

3.7 Other Benefits and Perquisites. During Employee's employment hereunder, and subject to the terms and conditions of the applicable plans and programs, Employee and, to the extent applicable, Employee's spouse, dependents and beneficiaries, shall be eligible to participate in all benefit plans and programs of the Company, including improvements or modifications of the same, which are now, or may hereafter be, available to similarly situated employees of the Company. The Company shall not, however, by reason of this Section 3.7, be obligated to institute, maintain, or refrain from changing, amending, or discontinuing, any such plan or program.

ARTICLE IV PROTECTION OF INFORMATION

4.1 Access to Information. The Company shall, during the time that Employee is employed by the Company, (a) disclose or entrust to Employee, and provide Employee access to, or place Employee in a position to create or develop, trade secrets or Confidential Information belonging to the Company, (b) place Employee in a position to develop business goodwill belonging to the Company and (c) disclose or entrust to Employee business opportunities to be developed for the Company.

4.2 Disclosure to and Property of the Company. All information, trade secrets, designs, ideas, concepts, improvements, product developments, discoveries and inventions, whether patentable or not, that are conceived, made, developed or acquired by, or disclosed to, Employee, individually or in conjunction with other employees or agents of the Company during

the term and in the scope of his employment that relate to the Company's business, products or services (including, without limitation, all such information relating to corporate opportunities, research, financial, accounting and sales data, pricing terms, evaluations, opinions, interpretations, analyses, reports, operating techniques, employee lists, training methods and procedures, personnel evaluation procedures, acquisition prospects, the identity of customers or their requirements, the identity of key contacts within the customer's organizations or within the organization of acquisition prospects, or marketing and merchandising techniques, prospective names and marks) and all writings or materials of any type embodying any of such information, ideas, concepts, improvements, discoveries, inventions and other similar forms of expression (collectively, "**Confidential Information**") shall be disclosed to the Company, and are and shall be the sole and exclusive property of the Company. Employee agrees to perform all actions reasonably requested by the Company to establish and confirm such exclusive ownership. Upon termination of Employee's employment by the Company, for any reason, Employee promptly shall deliver such Confidential Information and work product, and all copies thereof, to the Company. "Confidential Information" does not, however, include any information that, at the time of disclosure by Employee, is available to the public other than as a result of any act of Employee in breach of this Agreement.

4.3 No Unauthorized Use or Disclosure. Employee agrees that Employee will preserve and protect the confidentiality of all Confidential Information and work product of the Company, and will not, at any time during or after the termination of Employee's employment with the Company, make any unauthorized disclosure of, and shall not remove from Company premises, and will use his best efforts to prevent the removal from Company premises of, Confidential Information, or make any use thereof, in each case, except in the carrying out of Employee's responsibilities hereunder. Employee shall inform all persons or entities to whom or to which any Confidential Information shall be disclosed by him in accordance with this Agreement about the confidential nature of such Confidential Information, and Employee shall ensure that such Confidential Information is identified as being confidential, and shall call such identifying mark to such recipient's attention. Employee shall have no obligation hereunder to keep confidential any Confidential Information if and to the extent disclosure thereof is specifically required by law; *provided, however*, that in the event disclosure is required by applicable law and Employee is making such disclosure, Employee shall provide the Company with prompt notice of such requirement, and shall use his commercially reasonable efforts to give such notice prior to making any disclosure, so that the Company may seek an appropriate protective order. At the request of the Company, Employee agrees to deliver to the Company, at any time during the term of employment, or thereafter, all Confidential Information that he may possess or control.

4.4 Ownership by the Company. If, during Employee's employment by the Company, Employee creates any original work of authorship fixed in any tangible medium of expression which is the subject matter of copyright relating to the business, products, or services of the Company, whether such work is created solely by Employee or jointly with others (whether during business hours or otherwise and whether on the Company's premises or otherwise), Employee shall disclose such work to the Company. The Company shall be deemed the author of such work if the work is prepared by Employee in the scope of Employee's employment; or, if the work is not prepared by Employee within the scope of Employee's employment but is specially ordered by the Company as a contribution to a collective work, then

the work shall be considered to be work made for hire and the Company shall be the author of the work. If such work is neither prepared by Employee within the scope of Employee's employment nor a work specially ordered and is deemed to be a work made for hire, then Employee hereby agrees to assign, and hereby does assign, to the Company all of Employee's worldwide rights, titles, and interests in and to such work and all rights of copyright therein.

4.5 Assistance by Employee. During the period of Employee's employment by the Company, Employee shall assist the Company and its nominee, at any time, in the protection of the Company's and its nominee's worldwide right, title and interest in and to Confidential Information and shall execute all formal assignment documents and all lawful oaths and applications for patents and registration of copyrights in the United States and foreign countries as requested by the Company or its nominee. After Employee's employment with the Company terminates, at the request and cost of the Company, Employee shall reasonably assist the Company and its nominee, at reasonable times and for reasonable periods and for reasonable compensation, in the protection of the Company's or its nominee's worldwide right, title and interest in and to Confidential Information and the execution of all formal assignment documents requested by the Company or its nominee and the execution of all lawful oaths and applications for patents and registration of copyright in the United States and foreign countries, all as may be requested by the Company from time to time.

4.6 Remedies. Employee acknowledges that money damages would not be sufficient remedy for any breach of this Article IV by Employee, and the Company shall be entitled to enforce the provisions of this Article IV by obtaining specific performance and injunctive relief as remedies for such breach or any threatened breach, which such remedies shall be in addition to all other remedies available to the Company at law and equity. Each affiliate of the Company shall be a third party beneficiary of Employee's obligations under this Article IV and, for purposes of this Article IV, the term "Company" shall be deemed to also include the Company's Affiliates.

ARTICLE V EFFECT OF TERMINATION ON COMPENSATION

5.1 Due to Employee's Death. If Employee's employment hereunder shall terminate due to Employee's death, then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that the Company shall pay to Employee's estate: (a) that portion of Employee's Base Salary accrued through the date on which Employee's death occurred and all benefits payable under the governing provisions of any benefit plan or program of the Company in which Employee participated; (b) a pro rata amount of the Annual Bonus for the year in which the death occurred, which such pro rata bonus shall be at the target level described in Section 3.2 above and based on the number of days Employee was employed in the applicable calendar year in comparison to 365; and (c) all of the consulting fee payments Employee could have received during the term of the Consulting Agreement (as defined below) and all of the non-compete payments Employee could have received under the Consulting Agreement if the Prohibited Period continued for five years following the termination of Employee's employment (collectively, the "**Consulting and Non-Compete Payments**"). All payments pursuant to this

Section 5.1 shall be made in the same manner and at the same times as they would have been paid to Employee.

5.2 Due to Employee's Disability. If Employee's employment hereunder shall terminate due to Employee's Disability as set forth in Section 2.2(a) above, then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that the Company shall pay to Employee: (a) that portion of Employee's Base Salary accrued through the date on which Employee's employment terminated and all benefits payable under the governing provisions of any benefit plan or program of the Company in which Employee participated; and (b) subject to Section 5.7 below, a pro rata amount of the Annual Bonus for the year in which the termination of employment occurred, which such pro rata bonus shall be at the target level described in Section 3.2 above and based on the number of days Employee was employed in the applicable calendar year in comparison to 365, which such pro rata amount of the Annual Bonus shall be provided on the later of the first business day after the Release (as defined in Section 5.7 below) is no longer revocable or the payment date that an Annual Bonus for the year of termination otherwise would have been payable pursuant to Section 3.2 above had Employee's employment not terminated (provided, that, in no event shall such payment occur later than the date necessary to qualify such payment as a "short-term deferral" within the meaning of Treas. Reg. § 1.409A-1(b)(4)).

5.3 Termination by the Company for Cause; Resignation by Employee (other than due to Employee's Retirement) and Not Within a Corporate Change Period. If Employee's employment hereunder is terminated: (i) by the Company for Cause pursuant to Section 2.2(b) above; or (ii) is terminated by Employee pursuant to Section 2.3 above (other than due to Employee's Retirement) and, with respect to the applicable circumstances set forth in part (i) or (ii) of this sentence, the date of such termination occurs at any time other than during a Corporate Change Period (as defined below), then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that the Company shall pay to Employee that portion of Employee's Base Salary accrued through the date on which Employee's employment terminated and all benefits payable under the governing provisions of any benefit plan or program of the Company in which Employee participated.

5.4 Termination by the Company without Cause (other than due to Disability) or due to Employee's Retirement and Not Within a Corporate Change Period. If Employee's employment hereunder is terminated (i) by the Company pursuant to Section 2.2(c) above or (ii) by Employee pursuant to Section 2.3 above due to Employee's Retirement and, with respect to the applicable circumstances set forth in part (i) or (ii) of this sentence, the date of such termination occurs at any time other than during a Corporate Change Period, then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that (A) the Company shall pay to Employee that portion of Employee's Base Salary accrued through the date on which Employee's employment terminated and all benefits payable under the governing provisions of any benefit plan or program of the Company in which Employee participated and (B) Employee and the Company shall enter into a consulting agreement in a form mutually acceptable to Employee and the Company that includes the terms set forth on Exhibit A attached hereto and

such other terms, if any, that are agreed to by Employee and the Company (the “**Consulting Agreement**”); *provided, however*, that the level of consulting services to be performed pursuant to the Consulting Agreement shall not exceed a level equal to 20% of the average level of services performed by Employee in his capacity as an employee of the Company during the 36-month period ending on the termination of his employment, except for any deviations that may be permitted in accordance with the Nonqualified Deferred Compensation Rules and, accordingly, Employee’s transition from an employee of the Company to a consultant of the Company shall give rise to a “separation from service” within the meaning of the Nonqualified Deferred Compensation Rules.

5.5 Termination By the Company Without Cause or Resignation By Employee and Within a Corporate Change Period. If, within the period that begins on the date of a Corporate Change (as defined below) and ends on the date that is 24 months after the date of a Corporate Change (the “**Corporate Change Period**”), Employee’s employment is terminated: (i) by the Company for any reason (other than Cause or Employee’s death or Disability or due to the issuance of a notice of non-renewal by the Company pursuant to Section 2.1); or (ii) by Employee pursuant to Section 2.3 above, then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that the Company shall pay to Employee that portion of Employee’s Base Salary accrued through the date on which Employee’s employment terminated and all benefits payable under the governing provisions of any benefit plan or program of the Company in which Employee participated. In addition, subject to Section 5.7 below, the Company shall provide Employee:

(a) a lump sum payment equal to the sum of (i) three times the sum of (x) Employee’s then-current annual Base Salary, plus (y) Employee’s then-current target Annual Bonus and (ii) the Consulting and Non-Compete Payments (regardless of whether Employee is engaged to provide any post-termination consulting services to the Company, its successor or any of their respective Affiliates), which such payment shall be paid to Employee on the Company’s first regularly scheduled pay date that occurs after the Release is no longer revocable; and

(b) for that period beginning on the date of the termination of Employee’s employment and for so long during the 36-month period following the date of termination that Employee remains eligible to receive, and elects to receive, continuation of coverage under a Company group health plan under the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended (“**COBRA**”), the Company shall provide reimbursement of the premiums paid by Employee, if any, for such continuation coverage; *provided, however*, that to receive such reimbursement, Employee must not be eligible to receive health insurance benefits under any other employer’s group health plan and Employee must provide Company with documentation evidencing his payment of the applicable premiums within thirty (30) days of their payment. The Company’s payments of COBRA reimbursements shall be made within thirty (30) days of its receipt of such documentation; *provided, however*, the Company will provide the first COBRA reimbursement referenced in this Section 5.5(b) after the Release has been executed by Employee and become irrevocable, and the first such reimbursement payment shall include all payments, without interest, that otherwise would have been made pursuant to

this Section 5.5(b) between the date of Employee’s termination of employment and the date that the Release became irrevocable.

As used herein, a “**Corporate Change**” means: (a) the dissolution or liquidation of the Company; (b) a reorganization, merger or consolidation of the Company with one or more corporations (other than a merger or consolidation effecting a reincorporation of the Company in another state or any other merger or consolidation in which the stockholders of the surviving corporation and their proportionate interests therein immediately after the merger or consolidation are substantially identical to the stockholders of the Company and their proportionate interests therein immediately prior to the merger or consolidation) (collectively, a “**Corporate Change Merger**”); (c) the sale of all or substantially all of the assets of the Company; or (d) the occurrence of a Change in Control. A “**Change in Control**” shall be deemed to have occurred if (a) individuals who were directors of the Company immediately prior to a Control Transaction shall cease, within two years of such Control Transaction to constitute a majority of the Board (or of the board of directors of any successor to the Company or to a company which has acquired all or substantially all its assets) other than by reason of an increase in the size of the membership of the applicable board that is approved by at least a majority of the individuals who were directors of the Company immediately prior to such Control Transaction; or (b) any entity, person or Group acquires shares of the Company in a transaction or series of transactions that result in such entity, person or Group directly or indirectly owning beneficially 50% or more of the outstanding shares of Common Stock. As used herein, “**Control Transaction**” means (a) any tender offer for or acquisition of capital stock of the Company pursuant to which any person, entity, or Group directly or indirectly acquires beneficial ownership of 20% or more of the outstanding shares of Common Stock; (b) any Corporate Change Merger of the Company; (c) any contested election of directors of the Company; or (d) any combination of the foregoing, any one of which results in a change in voting power sufficient to elect a majority of the Board. As used herein, “**Group**” means persons who act “in concert” as described in Sections 13(d)(3) and/or 14(d)(2) of the Securities Exchange Act of 1934, as amended. As used herein, “**Common Stock**” means the common stock of the Company, \$.01 par value per share, or any stock or other securities hereafter issued or issuable in substitution or exchange for the Common Stock.

5.6 Consequences to Equity Awards. The impact of a Corporate Change and/or Employee’s termination from employment with the Company on stock option, restricted stock and other share-based awards made pursuant to a Company incentive plan shall be governed by the terms of such plan. Where, in the discretion of the Company, the applicable plan(s) is/are silent about the impact of a Corporate Change and/or Employee’s termination from employment on the vesting of Employee’s stock option, restricted stock and other share-based awards, then the following terms shall apply with respect to the applicable vested and unvested stock options, restricted stock and other share-based awards awarded to Employee:

<u>Reason for Termination</u>	<u>Stock Options</u>	<u>Restricted Stock</u>	<u>Other share-based awards</u>
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<u>Reason for Termination</u>	<u>Stock Options</u>	<u>Restricted Stock</u>	<u>Other share-based awards</u>
Termination by the Company for Cause pursuant to Section 2.2(b) above	Forfeit all unvested awards	Forfeit all unvested awards	Forfeit all unvested awards
Voluntary termination by Employee pursuant to Section 2.3 above (other than due to Employee's Retirement and not during a Corporate Change Period)	Forfeit all unvested awards; Employee has 3 months from the date of termination to exercise all vested awards*	Forfeit all unvested awards	Forfeit all unvested awards
Involuntary termination by the Company without Cause (and not due to death or Disability) pursuant to Section 2.2(c) above (other than during a Corporate Change Period)	Immediate vesting of all unvested awards; Employee has five years from the date of termination to exercise all vested awards*	Immediate vesting of all unvested awards	Immediate vesting of all unvested awards
Voluntary termination by Employee due to his Retirement (other than during a Corporate Change Period)	Immediate vesting of all unvested awards; Employee has five years from the date of termination to exercise all vested awards*	Immediate vesting of all unvested awards granted prior to the Effective Date; forfeit all unvested awards granted on or after the Effective Date	Immediate vesting of all unvested awards granted prior to the Effective Date; forfeit all unvested awards granted on or after the Effective Date
Termination during a Corporate Change Period for one of the reasons specified in Section 5.5 above	Immediate vesting of all unvested awards; Employee has 3 months from the date of termination to exercise all vested awards*	Immediate vesting of all unvested awards	Payouts made within 60 days following the end of the performance period as if Employee had been employed during the entirety of the period, provided that applicable performance targets have been met

<u>Reason for Termination</u>	<u>Stock Options</u>	<u>Restricted Stock</u>	<u>Other share-based awards</u>
Death	Immediate vesting of all unvested awards; Employee's estate has 12 months to exercise all vested awards*	Immediate vesting of all unvested awards	Awards will be prorated based on termination date and prorated payouts will be made within 60 days following the end of the performance period, provided that applicable performance targets have been met
Disability	Immediate vesting of all unvested awards; Employee has 12 months to exercise all vested awards*	Immediate vesting of all unvested awards	Awards will be prorated based on termination date and prorated payouts will be made within 60 days following the end of the performance period, provided that applicable performance targets have been met

* Notwithstanding anything herein to the contrary, in no event will any vested stock options be exercisable after the expiration of the original terms of such options.

5.7 Release and Full Settlement. Anything to the contrary herein notwithstanding, as a condition to the receipt of any payment or benefit under Section 5.2(b) or 5.5(a)-(b), Employee shall first execute (and not revoke within 7 days of execution) a release of all claims in a form acceptable to the Company (the "**Release**"), which such Release shall release the Company, its affiliates and their respective shareholders, members, partners, Board members, officers, directors, employees and agents from any and all claims, including without limitation any and all causes of action arising out of Employee's employment with the Company and the termination of such employment, but excluding (a) all claims to severance payments Employee may have under Sections 5.2(b) or 5.5(a)-(b) above, and (b) all vested benefits to which Employee is entitled under the Company's employee benefit plans. The performance of the Company's obligations hereunder and Employee's receipt of any payments or benefits provided to Employee hereunder shall constitute full settlement of all such claims and causes of action. The Release must be executed by Employee no later than 50 days following the date of termination of his employment (or earlier if requested by the Company and permitted by applicable law). Employee acknowledges Employee's understanding that if the applicable

Release is not timely executed, and the required revocation period has not fully expired, Employee shall not be entitled to any payment under Sections 5.2(b) or 5.5(a)-(b) above. Notwithstanding anything to the contrary in this Section 5, in the event the time period (including any applicable revocation period) prescribed by the Company for Employee's execution of the Release begins in one taxable year and ends in a second taxable year, payments under Section 5.5 will not commence until the second taxable year, irrespective of when the Release actually becomes irrevocable.

5.8 Reduction of Payments. Notwithstanding anything to the contrary in this Agreement, if Employee is a "disqualified individual" (as defined in Section 280G(c) of the Internal Revenue Code of 1986, as amended (the "**Code**")), and the payments and benefits provided for in this Agreement, together with any other payments and benefits which Employee has the right to receive from the Company or any of its affiliates, would constitute a "parachute payment" (as defined in Section 280G(b)(2) of the Code), then the payments and benefits provided for in this Agreement shall be reduced (but not below zero) so that the present value of such total amounts and benefits received by Employee from the Company and its affiliates will be one dollar (\$1.00) less than three times Employee's "base amount" (as defined in Section 280G(b)(3) of the Code) and so that no portion of such amounts and benefits received by Employee shall be subject to the excise tax imposed by Section 4999 of the Code. The reduction of payments and benefits hereunder, if applicable, shall be made by reducing, first, payments or benefits to be paid in cash hereunder in the order in which such payment or benefit would be paid or provided (beginning with such payment or benefit that would be made last in time and continuing, to the extent necessary, through to such payment or benefit that would be made first in time) and, then, reducing any benefit to be provided in-kind hereunder in a similar order. The determination as to the extent of any such reduction in the amount of the payments and benefits provided hereunder shall be made by the Company in good faith. If a reduced payment or benefit is made or provided and through error or otherwise that payment or benefit, when aggregated with other payments and benefits from the Company (or its affiliates) used in determining if a "parachute payment" exists, exceeds one dollar (\$1.00) less than three times Employee's base amount, then Employee shall immediately repay such excess to the Company upon notification that an overpayment has been made. Nothing in this Section 5.8 shall require the Company to be responsible for, or have any liability or obligation with respect to, Employee's excise tax liabilities under Section 4999 of the Code, if any.

ARTICLE VI NON-COMPETITION AGREEMENT

6.1 Restrictive Covenants. The Company has provided and shall provide in the future to Employee, Confidential Information. Employee acknowledges that in the course of his employment with the Company as a member of the Company's senior executive and management team, he has been given, and in the future shall be given, possession of and access to Confidential Information of the Company. Employee further acknowledges that, in the course of his employment with the Company, he has been given contacts within the death care industry, and he has been and shall be identified with the business and goodwill of the Company. Consequently, it is important that the Company protect its interests in regard to such matters from unfair competition. In consideration of the Confidential Information that has been received and that the Company covenants to provide Employee in the future, the sufficiency of which is

hereby acknowledged by Employee, and in order to protect the Company's legitimate business interests, including the preservation of its Confidential Information and goodwill, Employee agrees to enter into the covenants contained in this Article VI. The Parties therefore agree that during the Prohibited Period (as defined below), the Employee shall not, directly or indirectly:

(a) alone or for his own account, or as an officer, director, shareholder, partner, member, trustee, employee, consultant, advisor, agent or any other capacity of any corporation, partnership, joint venture, trust, or other business organization or entity, encourage, support, finance, be engaged in, interested in, or concerned with (i) any of the companies and entities described on Schedule I hereto, except to the extent that any activities in connection therewith are confined exclusively outside the continental United States, or (ii) any other business within the death care industry having an office or being conducted within a radius of fifty (50) miles of any funeral home, cemetery or other death care business owned or operated by the Company or any of its Affiliates at the time of such termination;

(b) induce or assist anyone in inducing in any way any employee of the Company or any of its Affiliates to resign or sever his or her employment or to breach an employment contract with the Company or any Affiliate; or

(c) own, manage, advise, encourage, support, finance, operate, join, control, or participate in the ownership, management, operation, or control of, or be connected in any manner with, any business which is or may be in the funeral, mortuary, crematory, cemetery or burial insurance business or in any business related thereto (i) as part of any of the companies or entities listed on Schedule I, or (ii) otherwise within a radius of fifty (50) miles of any funeral home, cemetery or other death care business owned or operated by the Company or any of its Affiliates at the time of such termination.

Notwithstanding the foregoing, the above covenants shall not prohibit the passive ownership of not more than one percent (1%) of the outstanding voting securities of any entity within the death care industry. The foregoing covenants shall not be held invalid or unenforceable because of the scope of the territory or actions subject hereto or restricted hereby, or the period of time within which such covenants respectively are operative, but the maximum territory, the action subject to such covenants and the period of time they are enforceable are subject to any determination by a final judgment of any court which has jurisdiction over the Parties and subject matter.

As used herein, the "**Prohibited Period**" means the period during which Employee is employed by the Company and continuing through the date that is two (2) years following the date on which Employee is no longer employed by the Company; *provided, however*, that in the event that Employee's employment hereunder is terminated (i) by the Company pursuant to Section 2.2(c) above or (ii) by Employee due to his Retirement, the Prohibited Period shall continue until the date that is five (5) years following such termination.

6.2 Relief. Employee and the Company agree and acknowledge that the limitations as to time, geographic area and scope of activity to be restrained as set forth in Section 6.1 are reasonable and do not impose any greater restraint than is necessary to protect the legitimate

business interests of the Company. Employee and the Company further agree and acknowledge that money damages would not be sufficient remedy for any breach of this Article VI by Employee, and the Company shall be entitled to enforce the provisions of this Article VI by terminating payments then owing to Employee under this Agreement or otherwise and to obtain specific performance and injunctive relief as remedies for such breach or any threatened breach. Such remedies shall not be deemed the exclusive remedies for a breach of this Article VI but shall be in addition to all remedies available, at law or in equity, including the recovery of damages from Employee and his agents.

6.3 Reasonableness; Enforcement. Employee hereby represents to the Company that Employee has read and understands, and agrees to be bound by, the terms of this Article VI. Employee acknowledges that the geographic scope and duration of the covenants contained in this Article VI are the result of arm's-length bargaining and are fair and reasonable in light of (a) the nature and wide geographic scope of the operations of the Business, (b) Employee's level of control over and contact with and association with the goodwill of the Business in all jurisdictions in which it is conducted, (c) the fact that the Business is conducted throughout the restricted area and (d) the Confidential Information that Employee is receiving in connection with the performance of Employee's duties hereunder. It is the desire and intent of the Parties that the provisions of this Article VI be enforced to the fullest extent permitted under applicable law, whether now or hereafter in effect and therefore, to the extent permitted by applicable law, Employee and the Company hereby waive any provision of applicable law that would render any provision of this Article VI invalid or unenforceable.

6.4 Reformation. The Company and Employee agree that the foregoing restrictions are reasonable under the circumstances and that any breach of the covenants contained in this Article VI may cause irreparable injury to the Company. Employee understands that the foregoing restrictions may limit Employee's ability to engage in certain businesses in the restricted area and on behalf of certain entities during the Prohibited Period, but acknowledges that such restrictions will not prevent Employee from earning a living. Nevertheless, if any of the aforesaid restrictions are found by a court of competent jurisdiction to be unreasonable, or overly broad as to geographic area or time, or otherwise unenforceable, the Parties intend for the restrictions therein set forth to be modified by the court making such determination so as to be reasonable and enforceable and, as so modified, to be fully enforced. By agreeing to this contractual modification prospectively at this time, the Company and Employee intend to make this provision enforceable under the law or laws of all applicable States and other applicable jurisdictions so that the entire agreement not to compete or to solicit other employees or customers and this Agreement as prospectively modified shall remain in full force and effect and shall not be rendered void or illegal. Such modification shall not affect the payments made to Employee under this Agreement.

ARTICLE VII DISPUTE RESOLUTION

7.1 Choice of Law. The Parties stipulate that this Agreement has been entered into in the State of Texas and this Agreement shall be construed and interpreted and the rights of the Parties governed by the internal laws of the State of Texas, without regard to the conflict of law principles thereof.

7.2 Venue. The Parties submit to the exclusive jurisdiction of the state and federal courts, as applicable, located in Houston, Texas, and appropriate appellate courts therefrom, over any dispute, controversy or claim between Employee and the Company arising out of or relating to this Agreement or Employee's employment with the Company. Each Party submits to the jurisdiction of such courts and agrees not to raise any objections to such jurisdiction.

**ARTICLE VIII
MISCELLANEOUS**

8.1 Successors; Assigns. This Agreement is personal to Employee, and neither this Agreement nor any rights or obligations hereunder shall be assignable or otherwise transferred by Employee. With Employee's consent, the Company may assign this Agreement to any Affiliate or successor (whether by merger, purchase or otherwise) to all or substantially all of the equity, assets or businesses of the Company. Subject to the foregoing, this Agreement shall be binding upon and inure to the benefit of the Parties and their respective successors and assigns.

8.2 Notices. For purposes of this Agreement, notices and all other communications provided for herein shall be in writing and shall be deemed to have been duly given (a) when received if delivered personally or by courier, (b) on the date receipt is acknowledged if delivered by certified mail, postage prepaid, return receipt requested, as follows:

If to Employee, addressed to: L. William Heiligbrodt
11015 Landon Lane
Houston, TX 77024

If to the Company, addressed to: Carriage Funeral Services, Inc.
3040 Post Oak Blvd., Suite 300
Houston, TX 77056

Attn: Chief Executive Officer

or to such other address as either Party may furnish to the other in writing in accordance herewith, except that notices or changes of address shall be effective only upon receipt.

8.3 No Waiver. No failure by either Party hereto at any time to give notice of any breach by the other Party of, or to require compliance with, any condition or provision of this Agreement shall be deemed a waiver of similar or dissimilar provisions or conditions at the same or at any prior or subsequent time.

8.4 Severability. If a court of competent jurisdiction determines that any provision of this Agreement is invalid or unenforceable, then the invalidity or unenforceability of that provision shall not affect the validity or enforceability of any other provision of this Agreement, and all other provisions shall remain in full force and effect.

8.5 Counterparts. This Agreement may be executed in one or more counterparts, each of which shall be deemed to be an original, but all of which together will constitute one and the same Agreement.

8.6 Withholding of Taxes and Other Employee Deductions. The Company may withhold from any benefits and payments made pursuant to this Agreement all federal, state, city and other taxes as may be required pursuant to any law or governmental regulation or ruling and all other employee deductions made with respect to the Company's employees generally.

8.7 Headings. The Article and Section headings have been inserted for purposes of convenience and shall not be used for interpretive purposes.

8.8 Effect of Termination of Employment or Service Relationship. The provisions of Articles IV, V, VI, VII, and VIII, and those provisions necessary to interpret and apply them, shall survive any termination of this Agreement and any termination of the employment or other service relationship between the Company and Employee.

8.9 Entire Agreement. Except as provided in the written plans and programs referenced in Section 3.6 and 3.7, this Agreement constitutes the entire agreement of the Parties with regard to the subject matter hereof and contains all the covenants, promises, representations, warranties and agreements between the Parties with respect to the employment of Employee by the Company. Without limiting the scope of the preceding sentence, all understandings and agreements preceding the date of execution of this Agreement and relating to the subject matter hereof, including, without limitation, the Prior Agreement, are hereby null and void and of no further force and effect, and this Agreement shall supersede all other agreements, written or oral, that purport to govern the terms of Employee's employment (including Employee's compensation) with the Company or any of its Affiliates. In entering into this Agreement, Employee expressly acknowledges and agrees that Employee has received all sums and compensation that Employee has been owed, is owed, or ever could be owed pursuant to the agreement(s) referenced in the previous sentence. Notwithstanding anything in the preceding provisions of this Section 8.9 to the contrary, the Parties expressly acknowledge and agree that this Agreement does not supersede or replace, but instead complements and is in addition to, all agreements and obligations that Employee has to the Company and its Affiliates (whether contained in a prior written agreement or otherwise) with regard to: (a) confidentiality and the non-use, non-disclosure, return and protection of trade secrets, confidential and proprietary information and materials (including, without limitation, those covenants set forth in Sections 8, 9 and 10 of the Employment Agreement dated September 1, 2011 entered into between Employee and the Company, which survived the termination of such agreement, as memorialized in the Prior Agreement, and Articles IV and VI of the Prior Agreement); (b) non-competition and non-solicitation; and (c) the assignment of intellectual property rights.

8.10 Modification; Waiver. Any modification to or waiver of this Agreement will be effective only if it is in writing and signed by the Party to be charged.

8.11 Advice of Counsel. Employee acknowledges that Employee has been instructed to, and has had adequate opportunity to obtain, the advice of his own counsel in connection with this Agreement.

8.12 Section 409A of the Code. Notwithstanding any provision of this Agreement to the contrary, if Employee is considered a "specified employee" upon his termination from employment under such procedures as established by the Company in accordance with the

limitations and requirements set forth in Section 409A of the Code, the regulations promulgated thereunder, and any additional guidance issued by the Internal Revenue Service related thereto (the “**Nonqualified Deferred Compensation Rules**”), then any portion of a cash payment or benefit distribution made upon such a termination from employment under Section 5.5 or otherwise that would cause the acceleration of, or an addition to, any taxes pursuant to the Nonqualified Deferred Compensation Rules may not commence earlier than six months after the date of such termination from employment; except to the extent any such payments or benefits would be exempt from the Nonqualified Deferred Compensation Rules, which such payments and benefits shall be paid in accordance with the original schedules noted in other sections of this Agreement. Therefore, in the event this Section 8.12 is applicable to Employee, any payment or distribution under Section 5.5 or otherwise that would cause the acceleration of, or an addition to, any taxes pursuant to the Nonqualified Deferred Compensation Rules that would otherwise have been paid to Employee within the first six months following Employee’s termination from employment shall be accumulated and paid to Employee, without interest, in a lump sum on the first day of the seventh month following his termination from employment (except to the extent exempt from the Nonqualified Deferred Compensation Rules). If any provision of this Agreement does not satisfy the requirements of Section 409A of the Code, then such provision shall nevertheless be applied in a manner consistent with those requirements. In no event whatsoever shall the Company be liable for any tax, interest or penalties that may be imposed on Employee under Section 409A of the Code. Each payment under this Agreement is intended to be a “separate payment” and not a series of payments for purposes of Section 409A of the Code. Any payments or reimbursements of any expenses provided for under this Agreement shall be made in accordance with Treas. Reg. §1.409A-3(i)(1)(iv).

8.13 Affiliates. For purposes of this Agreement (including Schedule I hereto), an “**Affiliate**” of an entity is an entity that directly or indirectly controls, is under the control of, or is under common control with, such entity.

[Remainder of Page Intentionally Blank;
Signature Page Follows]

IN WITNESS WHEREOF, the Parties have executed this Agreement as of the 5th
day of MARCH, 2014, effective as of the Effective Date.

CARRIAGE SERVICES, INC.

By: 
Melvin C. Payne
Chief Executive Officer

L. WILLIAM HEILIGBRODT



*Signature Page to
Employment Agreement*

SCHEDULE I

1. The following entities, together with all Affiliates thereof:

Service Corporation International
Keystone North America, Inc.
Meridian Mortuary Group, Inc.
StoneMor Partners LP
Saber Management LLC
Thomas Pierce & Co.
Legacy Funeral Holdings, LLC
Northstar Memorial Group, LLC
Foundation Partners
The Signature Group

2. Any new entity which may hereafter be established which acquires any combination of five or more funeral homes and/or cemeteries.
3. Any funeral home, cemetery or other death care enterprise which is managed by any entity described in 1 or 2 above.

Schedule I

EXHIBIT A

CONSULTING AGREEMENT TERM SHEET

Parties:	A consulting agreement (the " <u>Agreement</u> ") will be entered into by and between Carriage Services, Inc. (the " <u>Company</u> ") and L. William Heiligbrodt (" <u>Consultant</u> ").
Term:	24-month period commencing on the termination of Consultant's employment with the Company without Cause or due to Employee's Retirement (as such capitalized terms are defined in the Employment Agreement to which this Term Sheet is attached) unless extended by mutual written agreement of the parties (the " <u>Term</u> ").
Services:	Consultant shall make himself available to the Company upon the request of the Company's chief executive officer to perform consulting and advisory services on special projects, including, without limitation, capital structure matters (including those relating to the Company's banking group), investor relations, strategic acquisitions, field operations and collaborative development matters.
Consulting Fee:	At the rate of \$25,000 per complete calendar month during the Term
Non-Compete Payments:	At the rate of \$15,000 per complete calendar month during the portion of the Prohibited Period (as defined in the Employment Agreement to which this Term Sheet is attached) following the termination of Consultant's employment with the Company (the "Post-Employment Prohibited Period")
Non-Competition/Non-Solicitation/Confidentiality Covenants:	Consultant will reaffirm his obligation to comply with the non-competition, non-solicitation and confidentiality covenants set forth in his Employment Agreement during the five-year period commencing on the first day of the Term.
Benefits:	<p>For each month during the Post-Employment Prohibited Period, the Company shall pay Consultant a lump sum cash amount equal to the cost of premiums he pays for health care coverage (as a supplement to Medicare benefits) under an individual policy obtained from a third party insurer; provided, however, that the amount of the Company's reimbursement obligation shall not exceed \$800 in any single month.</p> <p>Consultant shall be an independent contractor and not a common-law employee of the Company. Therefore, Consultant shall not, during the Term, be entitled to participate in any of the Company's benefit plans and programs maintained for its employees.</p>
Office/Secretary:	During the Term, the Company will provide Consultant with an office and a secretary whose sole job responsibilities will consist of providing support to Consultant. Such secretary will be Donna Cowart (" <u>Cowart</u> ") for so long as she is employed by the Company. The Company will continue to pay Cowart her base salary in effect at the commencement of the Term, subject to adjustment from time to time in the ordinary course of business. For so long as she remains employed by the Company during the Term, Cowart will be eligible to participate in the Company's benefit plans and programs made available to similarly situated employees of the Company, subject to the terms and conditions of such plans and programs as in effect from time to time; provided, however, that in no event will the Company be required to provide Cowart with any incentive compensation opportunities or long-term incentive plan awards in respect of her employment

	during the term.
Release:	The Agreement will include a release of all claims, in a form acceptable to the Company, that releases the Company, its affiliates and their respective shareholders, members, partners, board members, officers, directors, employees and agents from any and all claims, including, without limitation, any and all causes of action arising out of Consultant's employment with the Company and the termination of such employment.
Governing Law:	The Agreement shall be governed by the laws of the State of Texas, without regard to the conflicts of laws principles thereof.

Exhibit A-2

EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (this “*Agreement*”) is made by and between Carriage Services, Inc., a Delaware corporation (the “*Company*”), and David J. DeCarlo (“*Employee*”). Employee and the Company are referred to individually herein as a “*Party*” and collectively as the “*Parties.*”

WITNESSETH:

WHEREAS the Company desires to employ Employee, and Employee desires to be employed by the Company, on the terms and conditions, and for the consideration, set forth herein.

NOW, THEREFORE, for and in consideration of the mutual promises, covenants and obligations contained herein, the Company and Employee agree as follows:

**ARTICLE I
EMPLOYMENT AND DUTIES**

1.1 Employment; Effective Date. The Company agrees to employ Employee and Employee agrees to be employed by the Company, on the terms herein, beginning as of March 3, 2014 (the “*Effective Date*”) and continuing for the period of time set forth in Article II of this Agreement, subject to the terms and conditions of this Agreement.

1.2 Positions. From and after the Effective Date, Employee shall be employed in the position of President or in such other position or positions as the Parties mutually may agree, and Employee shall report to the Company’s Chief Executive Officer.

1.3 Duties and Services. Employee agrees to serve in the position(s) referred to in Section 1.2 and to perform diligently and to the best of Employee’s abilities the duties and services appertaining to such positions, as well as such additional duties and services appropriate to such positions which the Parties mutually may agree upon from time to time. Employee’s employment shall also be subject to the policies maintained and established by the Company, as such policies may be amended from time to time.

1.4 Other Interests. Employee agrees, during the period of his employment by the Company, to devote his full business time, energy and attention to the business and affairs of the Company and its Affiliates, if applicable. Employee may serve on corporate, industry, civic, religious or charitable boards or committees without violating this Section 1.4 so long as such activities do not violate the terms of Articles IV or VI of this Agreement, present a conflict of interest, or interfere in any material respect with the performance of Employee’s duties and responsibilities pursuant to this Agreement; *provided, further* that any service by Employee on a board or committee of a for-profit entity shall be subject to the prior approval of the Board of Directors of the Company (the “*Board*”).

1.5 Duty of Loyalty. Employee acknowledges that Employee owes a fiduciary duty of loyalty, fidelity and allegiance to act in the best interests of the Company and to do no act that

would injure the business, interests, or reputation of the Company or its Affiliates. Consistent with those duties, Employee agrees to disclose to the Company all business opportunities pertaining to the Company's business and shall not appropriate (directly or indirectly) for Employee's own benefit business opportunities concerning the Company's business. If Employee's other business interests present a conflict of interest with the Company's business, Employee shall fully disclose the conflict.

ARTICLE II TERM AND TERMINATION OF EMPLOYMENT

2.1 Term. Unless sooner terminated pursuant to other provisions hereof, the Company agrees to employ Employee for the period beginning on the Effective Date and ending on the fourth anniversary of the Effective Date (the "**Employment Period**"); *provided, however,* that on each anniversary of the Effective Date, so long as this Agreement has not been earlier terminated, the Employment Period shall be extended for another year so that, so long as this Agreement has not been terminated or a notice of non-extension has not been given pursuant to the following sentence, there shall be between three and four years remaining in the then-existing Employment Period. Notwithstanding the foregoing, at least sixty (60) days prior to each anniversary of the Effective Date, either the Company or Employee may provide the other party notice that it does not intend for the automatic extension referenced in the previous sentence to occur. In the event that such a notice of non-extension is provided, no future extensions shall occur and, unless Employee's employment hereunder is sooner terminated pursuant to the other provisions hereof, the Employment Period shall terminate as of the expiration of the Employment Period that existed on the date that such notice of non-extension was provided.

2.2 Company's Right to Terminate. Notwithstanding the provisions of Section 2.1, Employee's employment by the Company shall automatically terminate upon the death of Employee, and the Company shall have the right to terminate Employee's employment under this Agreement at any time for any of the following reasons:

(a) upon Employee's becoming incapacitated by accident, sickness or other circumstance which has rendered him mentally or physically incapable of performing the duties and services required of him hereunder on a full-time basis for a period of at least 180 consecutive days (Employee's "**Disability**");

(b) for "**Cause**," which for purposes of this Agreement shall mean: (i) Employee's conviction of, or plea of no contest to, a misdemeanor involving moral turpitude or a felony, (ii) Employee's repeated failure or refusal to perform all of his duties, obligations and agreements herein contained or imposed by law, including his fiduciary duties, to the reasonable satisfaction of the Board; (iii) Employee's commission of acts amounting to gross negligence or willful misconduct to the material detriment of the Company; or (iv) Employee's material breach of any provision of this Agreement or uniformly applied provision of the Company's employee handbook or other personnel policies, including without limitation, its Code of Business Conduct and Ethics. Such determination of "Cause" shall be made by the Board and, in the event of circumstances described in (ii) or (iv), the Board shall give written notice to Employee specifying such

circumstances and providing a period of 30 days in which Employee shall be allowed to cure such circumstances if capable of cure; or

(c) at any time for any other reason whatsoever or for no reason at all, in the sole discretion of the Company.

2.3 Employee's Right to Terminate. Notwithstanding the provisions of Section 2.1, Employee shall have the right to terminate his employment under this Agreement for any of the following reasons:

(a) for "**Good Reason**," which for purposes of this Agreement shall mean termination of Employee's employment, within 120 days of, and in connection with or based upon, without Employee's prior written consent, (i) a material breach by the Company of any material provision of this Agreement, (ii) any material diminution of Employee's Base Salary, (iii) any material diminution in Employee's authority, duties or responsibilities; or (iv) the Company requiring Employee to relocate to a primary place of employment that is located more than fifty (50) miles outside of the location at which Employee is primarily based as of the Effective Date; *provided, however*, that, prior to Employee's termination of employment under this Section 2.3(a), Employee must give written notice to the Company of any Good Reason event within 90 days after Employee has actual knowledge of the facts or circumstances giving rise thereto and such breach must remain uncorrected for 30 days following such written notice; or

(b) at any time for any other reason whatsoever or for no reason at all.

2.4 Notice of Termination and Effective Date of Termination.

(a) *Notice of Termination.* If the Company or Employee desires to terminate Employee's employment hereunder, the Company or Employee shall do so by giving written notice to the other Party that it or he has elected to terminate Employee's employment hereunder and stating the effective date of the termination and reason for such termination; *provided, however*, that in the event that Employee has provided notice to the Company of his termination of employment, the Company may determine, in its sole discretion, that such termination shall be effective on any date prior to the effective date of termination provided in such notice (and, if such earlier date is so required, then it shall not change the basis for Employee's termination of employment nor be construed or interpreted as a termination of employment pursuant to Section 2.2). No action by either Party pursuant to this Section 2.4(a) shall alter or amend any other provisions hereof or rights arising hereunder, including, without limitation, the provisions of Articles IV, V and VI hereof.

(b) *Date of Termination.* The effective date of Employee's termination will be as follows: (i) if Employee's employment is terminated by his death, the date of his death; (ii) if Employee's employment is terminated by the Company for any reason, then the date specified in the notice of termination delivered to Employee by the Company; (iii) if Employee's Employment is terminated by Employee pursuant to Section 2.3 above,

then, unless the Company exercises its right pursuant to Section 2.4(a) above to specify an earlier date, the date specified in the notice of such termination delivered to the Company by Employee; or (iv) Employee's employment is terminated upon the expiration of the Employment Period after the issuance of a notice of non-extension pursuant to Section 2.1 above, then the date on which the Employment Period expires.

2.5 Deemed Resignations. Unless otherwise agreed to in writing by the Parties prior to the termination of Employee's employment, any termination of Employee's employment shall constitute an automatic resignation of Employee (i) as an officer of the Company and each of the Company's Affiliates (if applicable), (ii) from the Board (if applicable) and from the board of directors (or similar governing body) of each of the Company's Affiliates (if applicable), and (iii) from the board of directors (or similar governing body) of any corporation, limited liability company or other entity in which the Company holds an equity interest and with respect to which board (or similar governing body) Employee serves as a designee or other representative of the Company.

2.6 Separation from Service. For purposes of this Agreement, references to Employee's termination of employment shall mean, and be interpreted in accordance with, Employee's "separation from service" from the Company within the meaning of Treasury Regulation § 1.409A-1(h)(1)(ii).

ARTICLE III COMPENSATION AND BENEFITS

3.1 Base Salary. During the period that he is employed hereunder, Employee shall receive an annualized base salary of \$545,000 (the "**Base Salary**"). Employee's Base Salary will be reviewed annually, and any increase therein shall remain in the sole discretion of the Board, acting through its Compensation Committee (the "**Compensation Committee**"). Employee's Base Salary shall be paid in equal installments in accordance with the Company's standard policy regarding payment of compensation to similarly situated employees, but no less frequently than monthly.

3.2 Annual Bonuses. For each complete calendar year that he is employed hereunder, Employee shall be eligible to receive such annual bonus as may be determined in the Company's discretion (each an "**Annual Bonus**") after considering specified corporate and individual performance goals established by the Compensation Committee at its first meeting of the fiscal year. The goals for the Annual Bonus will be established at three levels: (i) threshold; (ii) target; and (iii) maximum. If the Compensation Committee determines that performance is achieved (i) at the threshold level, the Annual Bonus shall be 40% of the Base Salary; (ii) at the target level, the Annual Bonus shall be 80% of the Base Salary; and (iii) at the maximum level, the Annual Bonus shall be 160% of the Base Salary. In the discretion of the Compensation Committee, Annual Bonuses for performance falling between threshold, target and maximum goals may be ratably scaled above and below the goal levels. The Annual Bonus shall be payable before March 15 of the year following the calendar year to which the Annual Bonus relates, following the certification of applicable year-end financial results. Employee must be employed by the Company on the payment date in order to earn and receive an Annual Bonus.

3.3 Expenses. The Company shall promptly reimburse Employee for all reasonable business expenses incurred by Employee in performing services hereunder, including all expenses of travel and lodging expenses while away from home on business or at the request of the Company; provided, in each case, that such expenses are incurred and accounted for in accordance with the policies and procedures established by the Company from time to time. Any such reimbursement of expenses shall be made by the Company upon or as soon as practicable following receipt of supporting documentation reasonably satisfactory to the Company (but in any event not later than the close of Employee's taxable year following the taxable year in which the expense is incurred by Employee). In no event shall (i) any reimbursement under this Section 3.3 be made to Employee for such expenses incurred after the date of Employee's termination of employment with the Company, (ii) Employee be permitted to receive a payment or other benefit in lieu of reimbursement, or (iii) the amount of expenses for which Employee is eligible to receive reimbursement during any calendar year effect the amount of expenses for which Employee is eligible to receive reimbursement during any other calendar year within the term of this Agreement.

3.4 Vacation. During Employee's employment hereunder, Employee shall be entitled to four (4) weeks paid vacation each calendar year, subject to the Company's vacation policies as may exist from time to time.

3.5 Equity-Based Compensation. Employee shall be eligible to receive equity-based compensation awards under the terms of the Company's Second Amended and Restated 2006 Long Term Incentive Plan or one or more of the Company's other equity incentive plans in effect from time to time, as determined by the Compensation Committee of the Board in its sole discretion.

3.6 Intentionally left blank.

3.7 Other Benefits and Perquisites. During Employee's employment hereunder, and subject to the terms and conditions of the applicable plans and programs, Employee and, to the extent applicable, Employee's spouse, dependents and beneficiaries, shall be eligible to participate in all benefit plans and programs of the Company, including improvements or modifications of the same, which are now, or may hereafter be, available to similarly situated employees of the Company. The Company shall not, however, by reason of this Section 3.7, be obligated to institute, maintain, or refrain from changing, amending, or discontinuing, any such plan or program.

ARTICLE IV PROTECTION OF INFORMATION

4.1 Access to Information. The Company shall, during the time that Employee is employed by the Company, (a) disclose or entrust to Employee, and provide Employee access to, or place Employee in a position to create or develop, trade secrets or Confidential Information belonging to the Company, (b) place Employee in a position to develop business goodwill belonging to the Company and (c) disclose or entrust to Employee business opportunities to be developed for the Company.

4.2 Disclosure to and Property of the Company. All information, trade secrets, designs, ideas, concepts, improvements, product developments, discoveries and inventions, whether patentable or not, that are conceived, made, developed or acquired by, or disclosed to, Employee, individually or in conjunction with other employees or agents of the Company during the term and in the scope of his employment that relate to the Company's business, products or services (including, without limitation, all such information relating to corporate opportunities, research, financial, accounting and sales data, pricing terms, evaluations, opinions, interpretations, analyses, reports, operating techniques, employee lists, training methods and procedures, personnel evaluation procedures, acquisition prospects, the identity of customers or their requirements, the identity of key contacts within the customer's organizations or within the organization of acquisition prospects, or marketing and merchandising techniques, prospective names and marks) and all writings or materials of any type embodying any of such information, ideas, concepts, improvements, discoveries, inventions and other similar forms of expression (collectively, "**Confidential Information**") shall be disclosed to the Company, and are and shall be the sole and exclusive property of the Company. Employee agrees to perform all actions reasonably requested by the Company to establish and confirm such exclusive ownership. Upon termination of Employee's employment by the Company, for any reason, Employee promptly shall deliver such Confidential Information and work product, and all copies thereof, to the Company. "Confidential Information" does not, however, include any information that, at the time of disclosure by Employee, is available to the public other than as a result of any act of Employee in breach of this Agreement.

4.3 No Unauthorized Use or Disclosure. Employee agrees that Employee will preserve and protect the confidentiality of all Confidential Information and work product of the Company, and will not, at any time during or after the termination of Employee's employment with the Company, make any unauthorized disclosure of, and shall not remove from Company premises, and will use his best efforts to prevent the removal from Company premises of, Confidential Information, or make any use thereof, in each case, except in the carrying out of Employee's responsibilities hereunder. Employee shall inform all persons or entities to whom or to which any Confidential Information shall be disclosed by him in accordance with this Agreement about the confidential nature of such Confidential Information, and Employee shall ensure that such Confidential Information is identified as being confidential, and shall call such identifying mark to such recipient's attention. Employee shall have no obligation hereunder to keep confidential any Confidential Information if and to the extent disclosure thereof is specifically required by law; *provided, however*, that in the event disclosure is required by applicable law and Employee is making such disclosure, Employee shall provide the Company with prompt notice of such requirement, and shall use his commercially reasonable efforts to give such notice prior to making any disclosure, so that the Company may seek an appropriate protective order. At the request of the Company, Employee agrees to deliver to the Company, at any time during the term of employment, or thereafter, all Confidential Information that he may possess or control.

4.4 Ownership by the Company. If, during Employee's employment by the Company, Employee creates any original work of authorship fixed in any tangible medium of expression which is the subject matter of copyright relating to the business, products, or services of the Company, whether such work is created solely by Employee or jointly with others

(whether during business hours or otherwise and whether on the Company's premises or otherwise), Employee shall disclose such work to the Company. The Company shall be deemed the author of such work if the work is prepared by Employee in the scope of Employee's employment; or, if the work is not prepared by Employee within the scope of Employee's employment but is specially ordered by the Company as a contribution to a collective work, then the work shall be considered to be work made for hire and the Company shall be the author of the work. If such work is neither prepared by Employee within the scope of Employee's employment nor a work specially ordered and is deemed to be a work made for hire, then Employee hereby agrees to assign, and hereby does assign, to the Company all of Employee's worldwide rights, titles, and interests in and to such work and all rights of copyright therein.

4.5 Assistance by Employee. During the period of Employee's employment by the Company, Employee shall assist the Company and its nominee, at any time, in the protection of the Company's and its nominee's worldwide right, title and interest in and to Confidential Information and shall execute all formal assignment documents and all lawful oaths and applications for patents and registration of copyrights in the United States and foreign countries as requested by the Company or its nominee. After Employee's employment with the Company terminates, at the request and cost of the Company, Employee shall reasonably assist the Company and its nominee, at reasonable times and for reasonable periods and for reasonable compensation, in the protection of the Company's or its nominee's worldwide right, title and interest in and to Confidential Information and the execution of all formal assignment documents requested by the Company or its nominee and the execution of all lawful oaths and applications for patents and registration of copyright in the United States and foreign countries, all as may be requested by the Company from time to time.

4.6 Remedies. Employee acknowledges that money damages would not be sufficient remedy for any breach of this Article IV by Employee, and the Company shall be entitled to enforce the provisions of this Article IV by obtaining specific performance and injunctive relief as remedies for such breach or any threatened breach, which such remedies shall be in addition to all other remedies available to the Company at law and equity. Each affiliate of the Company shall be a third party beneficiary of Employee's obligations under this Article IV and, for purposes of this Article IV, the term "Company" shall be deemed to also include the Company's Affiliates.

ARTICLE V EFFECT OF TERMINATION ON COMPENSATION

5.1 Due to Employee's Death. If Employee's employment hereunder shall terminate due to Employee's death, then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that the Company shall pay to Employee's estate: (a) that portion of Employee's Base Salary accrued through the date on which Employee's death occurred and all benefits payable under the governing provisions of any benefit plan or program of the Company in which Employee participated; and (b) a pro rata amount of the Annual Bonus for the year in which the death occurred, which such pro rata bonus shall be at the target level described in Section 3.2 above and based on the number of days Employee was employed in the applicable calendar year

in comparison to 365. Such payments pursuant to this Section 5.1 shall be made in the same manner and at the same times as they would have been paid to Employee had he remained employed by the Company.

5.2 Due to Employee's Disability. If Employee's employment hereunder shall terminate due to Employee's Disability as set forth in Section 2.2(a) above, then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that the Company shall pay to Employee: (a) that portion of Employee's Base Salary accrued through the date on which Employee's employment terminated and all benefits payable under the governing provisions of any benefit plan or program of the Company in which Employee participated; and (b) subject to Section 5.7 below, a pro rata amount of the Annual Bonus for the year in which the termination of employment occurred, which such pro rata bonus shall be at the target level described in Section 3.2 above and based on the number of days Employee was employed in the applicable calendar year in comparison to 365, which such pro rata amount of the Annual Bonus shall be provided on the later of the first business day after the Release (as defined in Section 5.7 below) is no longer revocable or the payment date that an Annual Bonus for the year of termination otherwise would have been payable pursuant to Section 3.2 above had Employee's employment not terminated (provided, that, in no event shall such payment occur later than the date necessary to qualify such payment as a "short-term deferral" within the meaning of Treas. Reg. § 1.409A-1(b)(4)).

5.3 Termination for Cause or Resignation By Employee Not Within a Corporate Change Period. If Employee's employment hereunder is terminated: (i) by the Company for Cause at any time pursuant to Section 2.2(b) above; or (ii) is terminated by Employee pursuant to Section 2.3 above and, with respect to the applicable circumstances set forth in part (i) or (ii) of this sentence, the date of such termination occurs at any time other than during a Corporate Change Period (as defined below), then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that the Company shall pay to Employee that portion of Employee's Base Salary accrued through the date on which Employee's employment terminated and all benefits payable under the governing provisions of any benefit plan or program of the Company in which Employee participated.

5.4 Termination By the Company Without Cause. If Employee's employment hereunder is terminated by the Company without Cause (and not due to Employee's death or Disability or due to the issuance of a notice of non-renewal by the Company pursuant to Section 2.1) pursuant to Section 2.2(c) above, and such termination does not occur within a Corporate Change Period, then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that the Company shall pay to Employee that portion of Employee's Base Salary accrued through the date on which Employee's employment terminated and all benefits payable under the governing provisions of any benefit plan or program of the Company in which Employee participated. In addition, subject to Section 5.7 below, the Company shall provide Employee:

(a) an amount equal to 80% of Base Salary, multiplied by a fraction, the numerator of which is the number of days Employee was employed by the Company in the calendar year of Employee's termination, and the denominator of which is 365, which amount shall be paid on the later of the first business day after the Release is no longer revocable or the payment date that an Annual Bonus for the year of termination otherwise would have been payable pursuant to Section 3.2 above had Employee's employment not terminated (provided, that, in no event shall such payment occur later than the date necessary to qualify such payment as a "short-term deferral" within the meaning of Treas. Reg. § 1.409A-1(b)(4));

(b) continued payment of Employee's monthly Base Salary, in arrears, for a period of 18 months following the date of termination; *provided, however*, that the first such payment shall be made on the Company's first regular payroll date that comes after the Release is no longer revocable (the "**First Payment Date**") and shall include all payments, if any, without interest, that would have otherwise been made pursuant to this Section 5.4(b) between the date of Employee's termination of employment and the First Payment Date; and

(c) for that period beginning on the date of the termination of Employee's employment and for so long during the 18-month period following the date of termination that Employee remains eligible to receive, and elects to receive, continuation of coverage under a Company group health plan under the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended ("**COBRA**"), the Company shall provide reimbursement of the premiums paid by Employee, if any, for such continuation coverage; *provided, however*, that to receive such reimbursement, Employee must not be eligible to receive health insurance benefits under any other employer's group health plan and Employee must provide Company with documentation evidencing his payment of the applicable premiums within thirty (30) days of their payment. The Company's payments of COBRA reimbursements shall be made within thirty (30) days of its receipt of such documentation; *provided, however*, the Company will provide the first COBRA reimbursement referenced in this Section 5.4(c) after the Release has been executed by Employee and become irrevocable, and the first such reimbursement payment shall include all payments, without interest, that otherwise would have been made pursuant to this Section 5.4(c) between the date of Employee's termination of employment and the date that the Release became irrevocable.

5.5 Termination By the Company Without Cause or Resignation By Employee Within a Corporate Change Period.

If, within the period that begins on the date of a Corporate Change (as defined below) and ends on the date that is 24 months after the date of a Corporate Change (the "**Corporate Change Period**"), Employee's employment is terminated: (i) by the Company for any reason (other than Cause or Employee's death or Disability or due to the issuance of a notice of non-renewal by the Company pursuant to Section 2.1); or (ii) by Employee pursuant to Section 2.3 above, then all compensation and all benefits to Employee hereunder shall terminate contemporaneously with the effective date of the termination of his employment, except that the Company shall pay to Employee that portion of Employee's Base Salary accrued through the date on which Employee's employment terminated and all benefits

payable under the governing provisions of any benefit plan or program of the Company in which Employee participated. In addition, subject to Section 5.7 below, the Company shall provide Employee:

(a) a lump sum payment equal to three times the sum of (i) Employee's then-current annual Base Salary, plus (ii) Employee's then-current target Annual Bonus, which such payment shall be paid to Employee on the First Payment Date; and

(b) for that period beginning on the date of the termination of Employee's employment and for so long during the 36-month period following the date of termination that Employee remains eligible to receive, and elects to receive, continuation of coverage under a Company group health plan under COBRA, the Company shall provide reimbursement of the premiums paid by Employee, if any, for such continuation coverage; *provided, however*, that to receive such reimbursement, Employee must not be eligible to receive health insurance benefits under any other employer's group health plan and Employee must provide Company with documentation evidencing his payment of the applicable premiums within thirty (30) days of their payment. The Company's payments of COBRA reimbursements shall be made within thirty (30) days of its receipt of such documentation; *provided, however*, the Company will provide the first COBRA reimbursement referenced in this Section 5.5(b) after the Release has been executed by Employee and become irrevocable, and the first such reimbursement payment shall include all payments, without interest, that otherwise would have been made pursuant to this Section 5.5(b) between the date of Employee's termination of employment and the date that the Release became irrevocable.

As used herein, a "**Corporate Change**" means: (a) the dissolution or liquidation of the Company; (b) a reorganization, merger or consolidation of the Company with one or more corporations (other than a merger or consolidation effecting a reincorporation of the Company in another state or any other merger or consolidation in which the stockholders of the surviving corporation and their proportionate interests therein immediately after the merger or consolidation are substantially identical to the stockholders of the Company and their proportionate interests therein immediately prior to the merger or consolidation) (collectively, a "**Corporate Change Merger**"); (c) the sale of all or substantially all of the assets of the Company; or (d) the occurrence of a Change in Control. A "**Change in Control**" shall be deemed to have occurred if (a) individuals who were directors of the Company immediately prior to a Control Transaction shall cease, within two years of such Control Transaction to constitute a majority of the Board (or of the board of directors of any successor to the Company or to a company which has acquired all or substantially all its assets) other than by reason of an increase in the size of the membership of the applicable board that is approved by at least a majority of the individuals who were directors of the Company immediately prior to such Control Transaction; or (b) any entity, person or Group acquires shares of the Company in a transaction or series of transactions that result in such entity, person or Group directly or indirectly owning beneficially 50% or more of the outstanding shares of Common Stock. As used herein, "**Control Transaction**" means (a) any tender offer for or acquisition of capital stock of the Company pursuant to which any person, entity, or Group directly or indirectly acquires beneficial ownership of 20% or more of the outstanding shares of Common Stock; (b) any Corporate Change Merger of the Company; (c)

any contested election of directors of the Company; or (d) any combination of the foregoing, any one of which results in a change in voting power sufficient to elect a majority of the Board. As used herein, “**Group**” means persons who act “in concert” as described in Sections 13(d)(3) and/or 14(d)(2) of the Securities Exchange Act of 1934, as amended. As used herein, “**Common Stock**” means the common stock of the Company, \$.01 par value per share, or any stock or other securities hereafter issued or issuable in substitution or exchange for the Common Stock.

5.6 Consequences to Equity Awards. The impact of a Corporate Change and/or Employee’s termination from employment with the Company on stock option, restricted stock and other share-based awards made pursuant to a Company incentive plan shall be governed by the terms of such plan. Where, in the discretion of the Company, the applicable plan(s) is/are silent about the impact of a Corporate Change and/or Employee’s termination from employment on the vesting of Employee’s stock option, restricted stock and other share-based awards, then the following terms shall apply with respect to the applicable vested and unvested stock options, restricted stock and other share-based awards awarded to Employee:

<u>Reason for Termination</u>	<u>Stock Options</u>	<u>Restricted Stock</u>	<u>Other share-based awards</u>
Termination by the Company for Cause pursuant to Section 2.2(b) above	Forfeit all unvested awards	Forfeit all unvested awards	Forfeit all unvested awards
Involuntary termination by the Company without Cause (and not due to death or Disability) pursuant to Section 2.2(c) above or by Employee for Good Reason pursuant to Section 2.3(a) above (other than during a Corporate Change Period)	Forfeit all unvested awards; Employee has 3 months from the date of termination to exercise all vested awards*	Forfeit all unvested awards	Forfeit all unvested awards
Voluntary termination by Employee (other than for Good Reason) pursuant to Section 2.3(b) above (other than during a Corporate Change Period)	Forfeit all unvested awards; Employee has 3 months from the date of termination to exercise all vested awards*	Forfeit all unvested awards	Forfeit all unvested awards

<u>Reason for Termination</u>	<u>Stock Options</u>	<u>Restricted Stock</u>	<u>Other share-based awards</u>
Termination during a Corporate Change Period for one of the reasons specified in Section 5.5 above	Immediate vesting of all unvested awards; Employee has 3 months from the date of termination to exercise all vested awards*	Immediate vesting of all unvested awards	Payouts made within 60 days following the end of the performance period as if Employee had been employed during the entirety of the period, provided that applicable performance targets have been met
Death	Immediate vesting of all unvested awards; Employee's estate has 12 months to exercise all vested awards*	Immediate vesting of all unvested awards	Awards will be prorated based on termination date and prorated payouts will be made within 60 days following the end of the performance period, provided that applicable performance targets have been met
Disability	Immediate vesting of all unvested awards; Employee has 12 months to exercise all vested awards*	Immediate vesting of all unvested awards	Awards will be prorated based on termination date and prorated payouts will be made within 60 days following the end of the performance period, provided that applicable performance targets have been met
Retirement pursuant to a plan or policy adopted by the Company, if any, or on terms approved by the Board of Directors	Forfeit all unvested awards; Employee has 3 months to exercise all vested awards*	Immediate vesting of all unvested awards	Awards will be prorated based on termination date and prorated payouts will be made within 60 days following the end of the performance period, provided that applicable performance targets have been met.

* Notwithstanding anything herein to the contrary, in no event will any vested stock options be exercisable after the expiration of the original terms of such options.

5.7 Release and Full Settlement. Anything to the contrary herein notwithstanding, as a condition to the receipt of any payment or benefit under Section 5.2(b), 5.4(a)-(c) or 5.5(a)-(b), Employee shall first execute (and not revoke within 7 days of execution) a release of all claims in a form acceptable to the Company (the “**Release**”), which such Release shall release the Company, its affiliates and their respective shareholders, members, partners, Board members, officers, directors, employees and agents from any and all claims, including without limitation any and all causes of action arising out of Employee’s employment with the Company and the termination of such employment, but excluding (a) all claims to severance payments Employee may have under Sections 5.2(b), 5.4(a)-(c) or 5.5(a)-(b) above, and (b) all vested benefits to which Employee is entitled under the Company’s employee benefit plans. The performance of the Company’s obligations hereunder and Employee’s receipt of any payments or benefits provided to Employee hereunder shall constitute full settlement of all such claims and causes of action. The Release must be executed by Employee no later than 50 days following the date of termination of his employment (or earlier if requested by the Company and permitted by applicable law). Employee acknowledges Employee’s understanding that if the applicable Release is not timely executed, and the required revocation period has not fully expired, Employee shall not be entitled to any payment under Sections 5.2(b), 5.4(a)-(c) or 5.5(a)-(b) above. Notwithstanding anything to the contrary in this Section 5, in the event the time period (including any applicable revocation period) prescribed by the Company for Employee’s execution of the Release begins in one taxable year and ends in a second taxable year, payments under Section 5.4 or 5.5 will not commence and the First Payment Date shall not occur until the second taxable year, irrespective of when the Release actually becomes irrevocable.

5.8 Reduction of Payments. Notwithstanding anything to the contrary in this Agreement, if Employee is a “disqualified individual” (as defined in Section 280G(c) of the Internal Revenue Code of 1986, as amended (the “**Code**”)), and the payments and benefits provided for in this Agreement, together with any other payments and benefits which Employee has the right to receive from the Company or any of its affiliates, would constitute a “parachute payment” (as defined in Section 280G(b)(2) of the Code), then the payments and benefits provided for in this Agreement shall be reduced (but not below zero) so that the present value of such total amounts and benefits received by Employee from the Company and its affiliates will be one dollar (\$1.00) less than three times Employee’s “base amount” (as defined in Section 280G(b)(3) of the Code) and so that no portion of such amounts and benefits received by Employee shall be subject to the excise tax imposed by Section 4999 of the Code. The reduction of payments and benefits hereunder, if applicable, shall be made by reducing, first, payments or benefits to be paid in cash hereunder in the order in which such payment or benefit would be paid or provided (beginning with such payment or benefit that would be made last in time and continuing, to the extent necessary, through to such payment or benefit that would be made first in time) and, then, reducing any benefit to be provided in-kind hereunder in a similar order. The determination as to the extent of any such reduction in the amount of the payments and benefits provided hereunder shall be made by the Company in good faith. If a reduced payment or benefit is made or provided and through error or otherwise that payment or benefit, when aggregated with other payments and benefits from the Company (or its affiliates) used in determining if a “parachute payment” exists, exceeds one dollar (\$1.00) less than three times Employee’s base amount, then Employee shall immediately repay such excess to the Company upon notification that an overpayment has been made. Nothing in this Section 5.8 shall require

the Company to be responsible for, or have any liability or obligation with respect to, Employee's excise tax liabilities under Section 4999 of the Code, if any.

ARTICLE VI NON-COMPETITION AGREEMENT

6.1 Restrictive Covenants. The Company has provided and shall provide in the future to Employee, Confidential Information. Employee acknowledges that in the course of his employment with the Company as a member of the Company's senior executive and management team, he has been given, and in the future shall be given, possession of and access to Confidential Information of the Company. Employee further acknowledges that, in the course of his employment with the Company, he has been given contacts within the death care industry, and he has been and shall be identified with the business and goodwill of the Company. Consequently, it is important that the Company protect its interests in regard to such matters from unfair competition. In consideration of the Confidential Information that has been received and that the Company covenants to provide Employee in the future, the sufficiency of which is hereby acknowledged by Employee, and in order to protect the Company's legitimate business interests, including the preservation of its Confidential Information and goodwill, Employee agrees to enter into the covenants contained in this Article VI. The Parties therefore agree that for so long as the Employee shall remain employed by the Company and, if the employment of the Employee ceases for any reason (including voluntary resignation), then for a period of two (2) years thereafter (the "**Prohibited Period**"), the Employee shall not, directly or indirectly:

(a) alone or for his own account, or as an officer, director, shareholder, partner, member, trustee, employee, consultant, advisor, agent or any other capacity of any corporation, partnership, joint venture, trust, or other business organization or entity, encourage, support, finance, be engaged in, interested in, or concerned with (i) any of the companies and entities described on Schedule I hereto, except to the extent that any activities in connection therewith are confined exclusively outside the continental United States, or (ii) any other business within the death care industry having an office or being conducted within a radius of fifty (50) miles of any funeral home, cemetery or other death care business owned or operated by the Company or any of its Affiliates at the time of such termination;

(b) induce or assist anyone in inducing in any way any employee of the Company or any of its Affiliates to resign or sever his or her employment or to breach an employment contract with the Company or any Affiliate; or

(c) own, manage, advise, encourage, support, finance, operate, join, control, or participate in the ownership, management, operation, or control of, or be connected in any manner with, any business which is or may be in the funeral, mortuary, crematory, cemetery or burial insurance business or in any business related thereto (i) as part of any of the companies or entities listed on Schedule I, or (ii) otherwise within a radius of fifty (50) miles of any funeral home, cemetery or other death care business owned or operated by the Company or any of its Affiliates at the time of such termination.

Notwithstanding the foregoing, the above covenants shall not prohibit the passive ownership of not more than one percent (1%) of the outstanding voting securities of any entity within the death care industry. The foregoing covenants shall not be held invalid or unenforceable because of the scope of the territory or actions subject hereto or restricted hereby, or the period of time within which such covenants respectively are operative, but the maximum territory, the action subject to such covenants and the period of time they are enforceable are subject to any determination by a final judgment of any court which has jurisdiction over the Parties and subject matter.

6.2 Relief. Employee and the Company agree and acknowledge that the limitations as to time, geographic area and scope of activity to be restrained as set forth in Section 6.1 are reasonable and do not impose any greater restraint than is necessary to protect the legitimate business interests of the Company. Employee and the Company further agree and acknowledge that money damages would not be sufficient remedy for any breach of this Article VI by Employee, and the Company shall be entitled to enforce the provisions of this Article VI by terminating payments then owing to Employee under this Agreement or otherwise and to obtain specific performance and injunctive relief as remedies for such breach or any threatened breach. Such remedies shall not be deemed the exclusive remedies for a breach of this Article VI but shall be in addition to all remedies available, at law or in equity, including the recovery of damages from Employee and his agents.

6.3 Reasonableness; Enforcement. Employee hereby represents to the Company that Employee has read and understands, and agrees to be bound by, the terms of this Article VI. Employee acknowledges that the geographic scope and duration of the covenants contained in this Article VI are the result of arm's-length bargaining and are fair and reasonable in light of (a) the nature and wide geographic scope of the operations of the Business, (b) Employee's level of control over and contact with and association with the goodwill of the Business in all jurisdictions in which it is conducted, (c) the fact that the Business is conducted throughout the restricted area and (d) the Confidential Information that Employee is receiving in connection with the performance of Employee's duties hereunder. It is the desire and intent of the Parties that the provisions of this Article VI be enforced to the fullest extent permitted under applicable law, whether now or hereafter in effect and therefore, to the extent permitted by applicable law, Employee and the Company hereby waive any provision of applicable law that would render any provision of this Article VI invalid or unenforceable.

6.4 Reformation. The Company and Employee agree that the foregoing restrictions are reasonable under the circumstances and that any breach of the covenants contained in this Article VI may cause irreparable injury to the Company. Employee understands that the foregoing restrictions may limit Employee's ability to engage in certain businesses in the restricted area and on behalf of certain entities during the Prohibited Period, but acknowledges that such restrictions will not prevent Employee from earning a living. Nevertheless, if any of the aforesaid restrictions are found by a court of competent jurisdiction to be unreasonable, or overly broad as to geographic area or time, or otherwise unenforceable, the Parties intend for the restrictions therein set forth to be modified by the court making such determination so as to be reasonable and enforceable and, as so modified, to be fully enforced. By agreeing to this contractual modification prospectively at this time, the Company and Employee intend to make

this provision enforceable under the law or laws of all applicable States and other applicable jurisdictions so that the entire agreement not to compete or to solicit other employees or customers and this Agreement as prospectively modified shall remain in full force and effect and shall not be rendered void or illegal. Such modification shall not affect the payments made to Employee under this Agreement.

ARTICLE VII DISPUTE RESOLUTION

7.1 Choice of Law. The Parties stipulate that this Agreement has been entered into in the State of Texas and this Agreement shall be construed and interpreted and the rights of the Parties governed by the internal laws of the State of Texas, without regard to the conflict of law principles thereof.

7.2 Venue. The Parties submit to the exclusive jurisdiction of the state and federal courts, as applicable, located in Houston, Texas, and appropriate appellate courts therefrom, over any dispute, controversy or claim between Employee and the Company arising out of or relating to this Agreement or Employee's employment with the Company. Each Party submits to the jurisdiction of such courts and agrees not to raise any objections to such jurisdiction.

ARTICLE VIII MISCELLANEOUS

8.1 Successors; Assigns. This Agreement is personal to Employee, and neither this Agreement nor any rights or obligations hereunder shall be assignable or otherwise transferred by Employee. With Employee's consent, the Company may assign this Agreement to any Affiliate or successor (whether by merger, purchase or otherwise) to all or substantially all of the equity, assets or businesses of the Company. Subject to the foregoing, this Agreement shall be binding upon and inure to the benefit of the Parties and their respective successors and assigns.

8.2 Notices. For purposes of this Agreement, notices and all other communications provided for herein shall be in writing and shall be deemed to have been duly given (a) when received if delivered personally or by courier, (b) on the date receipt is acknowledged if delivered by certified mail, postage prepaid, return receipt requested, as follows:

If to Employee, addressed to: David J. DeCarlo
4501 Gulf Shore Blvd N
Unit 1901
Naples, FL 34103

If to the Company, addressed to: Carriage Services, Inc.
3040 Post Oak Blvd., Suite 300
Houston, TX 77056 Attn: Chief Executive Officer

or to such other address as either Party may furnish to the other in writing in accordance herewith, except that notices or changes of address shall be effective only upon receipt.

8.3 No Waiver. No failure by either Party hereto at any time to give notice of any breach by the other Party of, or to require compliance with, any condition or provision of this Agreement shall be deemed a waiver of similar or dissimilar provisions or conditions at the same or at any prior or subsequent time.

8.4 Severability. If a court of competent jurisdiction determines that any provision of this Agreement is invalid or unenforceable, then the invalidity or unenforceability of that provision shall not affect the validity or enforceability of any other provision of this Agreement, and all other provisions shall remain in full force and effect.

8.5 Counterparts. This Agreement may be executed in one or more counterparts, each of which shall be deemed to be an original, but all of which together will constitute one and the same Agreement.

8.6 Withholding of Taxes and Other Employee Deductions. The Company may withhold from any benefits and payments made pursuant to this Agreement all federal, state, city and other taxes as may be required pursuant to any law or governmental regulation or ruling and all other employee deductions made with respect to the Company's employees generally.

8.7 Headings. The Article and Section headings have been inserted for purposes of convenience and shall not be used for interpretive purposes.

8.8 Effect of Termination of Employment Relationship. The provisions of Articles IV, V, VI, VII, and VIII, and those provisions necessary to interpret and apply them, shall survive any termination of this Agreement and any termination of the employment relationship between the Company and Employee.

8.9 Entire Agreement. Except as provided in the written plans and programs referenced in Section 3.5 and 3.7, this Agreement constitutes the entire agreement of the Parties with regard to the subject matter hereof and contains all the covenants, promises, representations, warranties and agreements between the Parties with respect to the employment of Employee by the Company. Without limiting the scope of the preceding sentence, all understandings and agreements preceding the date of execution of this Agreement and relating to the subject matter hereof, are hereby null and void and of no further force and effect, and this Agreement shall supersede all other agreements, written or oral, that purport to govern the terms of Employee's employment (including Employee's compensation) with the Company or any of its Affiliates.

8.10 Modification; Waiver. Any modification to or waiver of this Agreement will be effective only if it is in writing and signed by the Party to be charged.

8.11 Advice of Counsel. Employee acknowledges that Employee has been instructed to, and has had adequate opportunity to obtain, the advice of his own counsel in connection with this Agreement.

8.12 Section 409A of the Code. Notwithstanding any provision of this Agreement to the contrary, if Employee is considered a "specified employee" upon his termination from employment under such procedures as established by the Company in accordance with the

limitations and requirements set forth in Section 409A of the Code, the regulations promulgated thereunder, and any additional guidance issued by the Internal Revenue Service related thereto (the “**Nonqualified Deferred Compensation Rules**”), then any portion of a cash payment or benefit distribution made upon such a termination from employment under Section 5.4 or 5.5 or otherwise that would cause the acceleration of, or an addition to, any taxes pursuant to the Nonqualified Deferred Compensation Rules may not commence earlier than six months after the date of such termination from employment; except to the extent any such payments or benefits would be exempt from the Nonqualified Deferred Compensation Rules, which such payments and benefits shall be paid in accordance with the original schedules noted in other sections of this Agreement. Therefore, in the event this Section 8.12 is applicable to Employee, any payment or distribution under Section 5.4 or 5.5 or otherwise that would cause the acceleration of, or an addition to, any taxes pursuant to the Nonqualified Deferred Compensation Rules that would otherwise have been paid to Employee within the first six months following Employee’s termination from employment shall be accumulated and paid to Employee, without interest, in a lump sum on the first day of the seventh month following his termination from employment (except to the extent exempt from the Nonqualified Deferred Compensation Rules). If any provision of this Agreement does not satisfy the requirements of Section 409A of the Code, then such provision shall nevertheless be applied in a manner consistent with those requirements. In no event whatsoever shall the Company be liable for any tax, interest or penalties that may be imposed on Employee under Section 409A of the Code. Each payment under this Agreement is intended to be a “separate payment” and not a series of payments for purposes of Section 409A of the Code. Any payments or reimbursements of any expenses provided for under this Agreement shall be made in accordance with Treas. Reg. §1.409A-3(i)(1)(iv).

8.13 Affiliates. For purposes of this Agreement (including Schedule I hereto), an “**Affiliate**” of an entity is an entity that directly or indirectly controls, is under the control of, or is under common control with, such entity.

[Remainder of Page Intentionally Blank;
Signature Page Follows]

IN WITNESS WHEREOF, the Parties have executed this Agreement as of the 17th
day of MARCH, 2014, effective as of the Effective Date.

CARRIAGE SERVICES, INC.

By: Melvin C Payne
Melvin C. Payne
Chief Executive Officer

DAVID J. DECARLO

D. J. DeCarlo

*Signature Page to
Employment Agreement*

SCHEDULE I

1. The following entities, together with all Affiliates thereof:

- Service Corporation International
- Keystone North America, Inc.
- Meridian Mortuary Group, Inc.
- StoneMor Partners LP
- Saber Management LLC
- Thomas Pierce & Co.
- Legacy Funeral Holdings, LLC
- Northstar Memorial Group, LLC
- Foundation Partners
- The Signature Group

2. Any new entity which may hereafter be established which acquires any combination of five or more funeral homes and/or cemeteries.
3. Any funeral home, cemetery or other death care enterprise which is managed by any entity described in 1 or 2 above.

I, Melvin C. Payne, certify that:

1. I have reviewed this report on Form 10-Q of Carriage Services, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Dated: May 7, 2014

/s/ Melvin C. Payne

Melvin C. Payne

Chief Executive Officer and Chairman of the Board

(Principal Executive Officer)

I, L. William Heiligbrodt, certify that:

1. I have reviewed this report on Form 10-Q of Carriage Services, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Dated: May 7, 2014

/s/ L. William Heiligbrodt

L. William Heiligbrodt

Executive Vice President and Secretary

(Principal Financial Officer)

**Certification of
Chief Executive Officer and Chief Financial Officer
under Section 906 of the
Sarbanes Oxley Act of 2002, 18 U.S.C. § 1350**

In connection with the Quarterly Report on Form 10-Q of Carriage Services, Inc. (the "Company"), as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Melvin C. Payne, Chief Executive Officer of the Company, and L. William Heiligbrodt, Executive Vice President and Secretary of the Company, each certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to his knowledge:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 7, 2014

/s/ Melvin C. Payne

Melvin C. Payne

Chief Executive Officer and Chairman of the Board

(Principal Executive Officer)

/s/ L. William Heiligbrodt

L. William Heiligbrodt

Executive Vice President and Secretary

(Principal Financial Officer)