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

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**FORM 10-Q**

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(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, 2013**

**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**

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**CARRIAGE SERVICES, INC.**

**(Exact name of registrant as specified in its charter)**

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**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)**

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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 3, 2013 was 18,208,541.

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**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, 2012	(unaudited) March 31, 2013
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 1,698	\$ 1,290
Accounts receivable, net of allowance for bad debts of \$1,177 in 2012 and \$1,016 in 2013	17,812	18,142
Assets held for sale	1,466	3,183
Inventories	5,133	5,010
Prepaid expenses	5,107	4,138
Other current assets	1,923	4,107
Total current assets	33,139	35,870
Preneed cemetery trust investments	70,960	73,067
Preneed funeral trust investments	82,896	85,224
Preneed receivables, net of allowance for bad debts of \$2,059 in 2012 and \$1,851 in 2013	23,222	24,181
Receivables from preneed trusts	25,871	26,938
Property, plant and equipment, net of accumulated depreciation of \$84,291 in 2012 and \$85,361 in 2013	152,433	155,677
Cemetery property	75,156	75,030
Goodwill	218,442	217,243
Deferred charges and other non-current assets	9,424	7,156
Cemetery perpetual care trust investments	46,542	47,165
Total assets	\$ 738,085	\$ 747,551
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Current portion of senior long-term debt and capital lease obligations	\$ 11,218	\$ 11,629
Accounts payable	5,243	4,359
Other liabilities	13,067	14,346
Accrued liabilities	12,278	11,671
Liabilities associated with assets held for sale	369	578
Total current liabilities	42,175	42,583
Long-term debt, net of current portion	118,841	115,718
Line of credit	44,700	43,000
Convertible junior subordinated debentures due in 2029 to an affiliate	89,770	89,770
Obligations under capital leases, net of current portion	4,013	3,943
Deferred preneed cemetery revenue	63,998	64,627
Deferred preneed funeral revenue	39,794	41,846
Deferred preneed cemetery receipts held in trust	70,960	73,067
Deferred preneed funeral receipts held in trust	82,896	85,224
Care trusts' corpus	45,920	47,083
Total liabilities	603,067	606,861
Commitments and contingencies:		
Redeemable preferred stock	200	200
Stockholders' equity:		
Common stock, \$.01 par value; 80,000,000 shares authorized; 22,078,000 and 22,053,000 shares issued at December 31, 2012 and March 31, 2013, respectively	221	221
Additional paid-in capital	202,462	202,880
Accumulated deficit	(52,598)	(47,344)
Treasury stock, at cost; 3,922,000 shares at December 31, 2012 and March 31, 2013	(15,267)	(15,267)
Total stockholders' equity	134,818	140,490
Total liabilities and stockholders' equity	\$ 738,085	\$ 747,551

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,	
	2012	2013
Revenues:		
Funeral	\$ 40,035	\$ 45,157
Cemetery	11,288	12,930
	<u>51,323</u>	<u>58,087</u>
Field costs and expenses:		
Funeral	22,959	26,421
Cemetery	7,182	7,228
Depreciation and amortization	2,158	2,496
Regional and unallocated funeral and cemetery costs	2,333	3,264
	<u>34,632</u>	<u>39,409</u>
Gross profit	16,691	18,678
Corporate costs and expenses:		
General and administrative costs and expenses	5,242	5,775
Home office depreciation and amortization	253	343
	<u>5,495</u>	<u>6,118</u>
Operating income	11,196	12,560
Interest expense, net of other income	(4,552)	(2,595)
Income from continuing operations before income taxes	6,644	9,965
Provision for income taxes	(2,574)	(4,384)
Net income from continuing operations	4,070	5,581
Income (loss) from discontinued operations, net of tax	389	(323)
Net income	4,459	5,258
Preferred stock dividend	(4)	(4)
Net income available to common stockholders	<u>\$ 4,455</u>	<u>\$ 5,254</u>
Basic earnings per common share:		
Continuing operations	\$ 0.22	\$ 0.31
Discontinued operations	0.02	(0.02)
Basic earnings per common share	<u>\$ 0.24</u>	<u>\$ 0.29</u>
Diluted earnings per common share:		
Continuing operations	\$ 0.22	\$ 0.27
Discontinued operations	0.02	(0.02)
Diluted earnings per common share	<u>\$ 0.24</u>	<u>\$ 0.25</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>18,265</u>	<u>18,139</u>
Diluted	<u>18,320</u>	<u>22,728</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)

	<b>For the three months ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
<b>Cash flows from operating activities:</b>		
Net income	\$ 4,459	\$ 5,258
<b>Adjustments to reconcile net income to net cash provided (used) by operating activities:</b>		
(Income) loss from discontinued operations	(389)	323
Depreciation and amortization	2,412	2,839
Amortization of deferred financing costs	174	(638)
Provision for losses on accounts receivable	486	440
Stock-based compensation expense	403	646
Deferred income taxes	2,104	1,354
Other	(10)	—
<b>Changes in operating assets and liabilities that provided (required) cash:</b>		
Accounts and preneed receivables	(1,240)	(1,966)
Inventories and other current assets	(118)	501
Deferred charges and other	(38)	—
Preneed funeral and cemetery trust investments	2,305	1,411
Accounts payable and accrued liabilities	(5,310)	(48)
Deferred preneed funeral and cemetery revenue	182	2,678
Deferred preneed funeral and cemetery receipts held in trust	(2,270)	(1,935)
Net cash provided by continuing operating activities	3,150	10,863
Net cash provided by discontinued operating activities	373	122
Net cash provided by operating activities	3,523	10,985
<b>Cash flows from investing activities:</b>		
Acquisitions	(11,589)	—
Capital expenditures	(3,090)	(8,711)
Net cash used in continuing investing activities	(14,679)	(8,711)
Net cash provided by discontinued investing activities	9	1,928
Net cash used in investing activities	(14,670)	(6,783)
<b>Cash flows from financing activities:</b>		
Net borrowings from (payments against) the bank credit facility	13,900	(4,200)
Payments on long-term debt and obligations under capital leases	(164)	(160)
Proceeds from the exercise of stock options and employee stock purchase plan	318	318
Stock option benefit	21	—
Dividends on common stock	(454)	(452)
Dividend on redeemable preferred stock	(4)	(4)
Payment of loan origination costs	—	(98)
Purchase of treasury stock	(2,731)	—
Net cash provided by (used in) continuing financing activities	10,886	(4,596)
Net cash used in discontinued financing activities	(7)	(14)
Net cash provided by (used in) financing activities	10,879	(4,610)
Net decrease in cash and cash equivalents	(268)	(408)
Cash and cash equivalents at beginning of period	1,137	1,698
Cash and cash equivalents at end of period	\$ 869	\$ 1,290

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, 2013, we owned and operated 167 funeral homes in 26 states and 33 cemeteries in 11 states.

*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, 2012 and 2013 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, 2012 and should be read in conjunction therewith. Certain reclassifications have been made to prior period amounts to conform to the current period financial statement presentation with no effect on our previously reported results of operations, consolidated financial position, or cash flows.

*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 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 our estimates and judgments, including those related to revenue recognition, realization of accounts receivable, goodwill, intangible assets, property and equipment and deferred tax assets. 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 and \$8.7 million of funeral receivables at December 31, 2012 and March 31, 2013, respectively, and \$9.2 million and \$8.9 million of cemetery receivables at December 31, 2012 and March 31, 2013, 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 \$7.3 million and \$7.5 million of funeral receivables and \$15.9 million and \$16.7 million of cemetery receivables at December 31, 2012 and March 31, 2013, respectively. Accounts receivable also include minor amounts of other receivables. Bad debt expense totaled \$0.5 million and \$0.4 million for three months ended March 31, 2012 and 2013, respectively.

#### *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. A marketing plan is then developed for those locations which are identified as held for sale. 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 the Consolidated Balance Sheet and the operating results, as well as impairments, if any, are presented on a comparative basis in the discontinued operations section of the Consolidated Statements of Operations, along with the income tax effect. During the first quarter of 2013, we sold funeral homes in Texas which were reported as held for sale at December 31, 2012. We currently have new letters of intent outstanding on funeral homes in Kansas and California; as such, these businesses are no longer reported within our continuing operations. The assets and liabilities associated with the locations are reclassified as held for sale on the Consolidated Balance Sheet and the operating results are presented on a comparative basis in the discontinued operations section of the Consolidated Statements of Operations. See Note 4 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. During the first quarter of 2012, we completed two acquisitions. There were no acquisitions during the first quarter of 2013. See Note 3 to the Consolidated Financial Statements herein for more information.

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 5 to the Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2012.

#### *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 employee stock purchase plans, 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, 2012. 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 14 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 and convertible junior subordinated debentures.

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 to include outstanding unvested restricted stock awards in both the basic and diluted weighted average shares outstanding calculation. See Note 19 to this Consolidated Financial Statements herein for the computations of per share earnings for the three month periods ended March 31, 2012 and 2013.

The fully diluted weighted average shares outstanding for the three months ended March 31, 2013, and the corresponding calculation of GAAP 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, 2012, the conversion of our convertible junior subordinated debentures is excluded from fully diluted earnings per share calculations and the fully diluted weighted average share count 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* in 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 for 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 certain 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, 2013, CSV RIA provides these services to one institution, which has custody of 68% 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 herein in Notes 6, 10 and 11 to the Consolidated Financial Statements. 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 month period ended March 31, 2013, 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, 2013, 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 appropriate 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 the fixed rate of 7% and are carried on our Consolidated Balance Sheets at a cost of approximately \$89.8 million. The fair value of these securities is estimated to be approximately \$95.2 million at March 31, 2013, based on available broker quotes of the corresponding preferred securities issued by the Trust.

### *Income Taxes*

We and our subsidiaries file a consolidated U.S. Federal income tax return, separate income tax returns in 16 states 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 our unrecognized tax benefits during the next twelve months.

### *Subsequent Events*

Management evaluated events and transactions during the period subsequent to March 31, 2013 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 20 to the Consolidated Financial Statements herein.

## **2. RECENTLY ISSUED ACCOUNTING STANDARDS**

### *Comprehensive Income*

In February 2013, the FASB amended the Comprehensive Income Topic of the ASC to require reporting of amounts reclassified out of accumulated other comprehensive income (AOCI) by component. In addition, we are required to present significant amounts reclassified out of AOCI to net income in its entirety by the respective line items and to cross reference any disclosure elsewhere in the notes for amounts reclassified in less than their entirety. This amendment is effective prospectively for public companies for reporting periods after December 15, 2012 which we adopted effective January 1, 2013. See Note 15 to the Consolidated Financial Statements herein for the appropriate disclosures.

### 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.

During the first quarter of 2012, we completed two acquisitions consisting of two funeral homes. We paid \$11.6 million in cash as consideration for these acquisitions. We acquired substantially all of the assets and assumed certain operating liabilities, including obligations associated with existing preneed contracts. The assets and liabilities were recorded at fair value and included goodwill of \$6.3 million. There were no acquisitions during the first quarter of 2013. The pro forma impact of the acquisition on the prior periods is not presented as the impact is not material to reported results. Thus, the results of the acquired businesses are included in our results from the date of acquisition.

### 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 Acquisition 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 2012, we ended a management agreement with a cemetery in Ohio. We currently have new letters of intent outstanding on funeral homes in Kansas and California; as such, these businesses are no longer reported within our continuing operations and are presented as held for sale on our Consolidated Balance Sheet at March 31, 2013.

Assets and liabilities associated with the businesses held for sale in our Consolidated Balance Sheets at December 31, 2012 and March 31, 2013 consisted of the following (in thousands):

	<u>December 31, 2012</u>	<u>March 31, 2013</u>
<b>Assets:</b>		
Current assets	\$ 238	\$ 309
Preneed funeral trust investments	—	70
Receivables from preneed trusts	293	289
Property, plant and equipment, net	504	1,418
Goodwill	85	1,097
Deferred charges and other non-current assets	346	—
<b>Total</b>	<u>\$ 1,466</u>	<u>\$ 3,183</u>
<b>Liabilities:</b>		
Current liabilities	\$ 75	\$ 106
Current portion of long-term debt and capital lease obligations	—	28
Long-term debt, net of current portion	—	85
Deferred preneed funeral revenue	294	289
Deferred preneed funeral receipts held in trust	—	70
<b>Total</b>	<u>\$ 369</u>	<u>\$ 578</u>

The operating results of the discontinued businesses during the periods presented, as well as the gain on the disposal, are 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,	
	2012	2013
Revenues	\$ 977	\$ 658
Operating income	\$ 226	\$ 62
Gain (loss) on disposition	428	(583)
(Provision) benefit for income taxes	(265)	198
Income (loss) from discontinued operations	<u>\$ 389</u>	<u>\$ (323)</u>

## 5. GOODWILL

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

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

	March 31, 2013
Goodwill as of December 31, 2012	\$ 218,442
Impairments and changes in previous estimates	(102)
Reclassification of assets held for sale	(1,097)
Goodwill as of March 31, 2013	<u>\$ 217,243</u>

Changes in previous estimates are related to minor adjustments to inventory. The impairment of \$0.1 million is related to businesses discontinued in the first quarter of 2013 as the carrying value exceeded fair value.

## 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* in our Consolidated Balance Sheets at December 31, 2012 and March 31, 2013 are as follows (in thousands):

	December 31, 2012	March 31, 2013
Preneed cemetery trust investments, at fair value	\$ 73,126	\$ 75,213
Less: allowance for contract cancellation	(2,166)	(2,146)
Preneed cemetery trust investments, net	<u>\$ 70,960</u>	<u>\$ 73,067</u>

Upon cancellation of a preneed cemetery 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 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, common stock, U.S. treasury debt, U.S. agency obligations 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 corporate debt, preferred stocks, foreign debt, mortgage backed securities and fixed income securities, all of which are classified within Level 2 of the valuation hierarchy. There were no significant transfers between Levels 1 and 2 for the three months ended March 31, 2013. 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, 2013 are detailed below (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 922	\$ —	\$ —	\$ 922
Fixed income securities:					
Foreign	2	2,458	459	—	2,917
Corporate debt	2	39,164	1,453	(551)	40,066
Preferred stock	2	19,142	1,394	—	20,536
Mortgage backed securities	2	1	—	—	1
Common stock	1	9,828	507	(907)	9,428
Trust securities		\$ 71,515	\$ 3,813	\$ (1,458)	\$ 73,870
Accrued investment income		\$ 1,343			\$ 1,343
Preneed cemetery trust investments					\$ 75,213
Fair market value as a percentage of cost					103.3%

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	9,949
Due in five to ten years	18,351
Thereafter	35,220
Total	\$ 63,520

The cost and fair market values associated with preneed cemetery trust investments at December 31, 2012 are detailed below (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 758	\$ —	\$ —	\$ 758
Fixed income securities:					
Foreign	2	2,008	450	—	2,458
Corporate debt	2	38,299	863	(507)	38,655
Preferred stock	2	22,362	824	(294)	22,892
Mortgage backed securities	2	1	—	—	1
Common stock	1	8,759	34	(1,526)	7,267
Trust securities		\$ 72,187	\$ 2,171	\$ (2,327)	\$ 72,031
Accrued investment income		\$ 1,095			\$ 1,095
Preneed cemetery trust investments					\$ 73,126
Market value as a percentage of cost					99.8%

We determine whether or not the assets in the preneed cemetery 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 of the investment due to an other-than-temporary impairment is likewise recorded as a reduction in *Deferred preneed*

*cemetery receipts held in trust*. 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 cemetery merchandise and service 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. Our cemetery merchandise and service trust investment unrealized losses, their associated fair market values, and the duration of unrealized losses as of March 31, 2013 and December 31, 2012, respectively, are shown in the following tables (in thousands):

	March 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:						
Corporate debt	\$ 6,975	\$ (240)	\$ 528	\$ (311)	\$ 7,503	\$ (551)
Common stock	2,687	(738)	920	(169)	3,607	(907)
Total temporary impaired securities	\$ 9,662	\$ (978)	\$ 1,448	\$ (480)	\$ 11,110	\$ (1,458)

	December 31, 2012					
	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:						
Corporate debt	11,363	(325)	622	(182)	11,985	(507)
Preferred stock	1,040	(54)	2,284	(240)	3,324	(294)
Common stock	5,088	(934)	957	(592)	6,045	(1,526)
Total temporary impaired securities	\$ 17,491	\$ (1,313)	\$ 3,863	\$ (1,014)	\$ 21,354	\$ (2,327)

Preneed cemetery trust investment security transactions recorded in *Interest income and other, net* in the Consolidated Statements of Operations for the three months ended March 31, 2012 and 2013 are as follows (in thousands):

	For the three months ended March 31,	
	2012	2013
Investment income	\$ 762	\$ 693
Realized gains	2,373	38
Realized losses	(115)	(430)
Expenses and taxes	(131)	(381)
Increase (decrease) in deferred preneed cemetery receipts held in trust	(2,889)	80
	\$ —	\$ —

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

	For the three months ended March 31,	
	2012	2013
Purchases	\$ (24,039)	\$ (4,161)
Sales	24,088	5,009

### *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* in our Consolidated Balance Sheets at December 31, 2012 and March 31, 2013 are as follows (in thousands):

	December 31, 2012	March 31, 2013
Preneed funeral trust investments, at fair value	\$ 85,415	\$ 87,728
Less: allowance for contract cancellation	(2,519)	(2,504)
Preneed funeral trust investments, net	\$ 82,896	\$ 85,224

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. Government, agencies and municipalities, common stocks 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 corporate debt, preferred stocks, foreign debt, mortgage backed securities and fixed income securities, all of which are classified within Level 2 of the valuation hierarchy. There were no significant transfers between Levels 1 and 2 for the three months ended March 31, 2013. 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, 2013 are detailed below (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 13,613	\$ —	\$ —	\$ 13,613
Fixed income securities:					
U.S. treasury debt	1	2,923	86	—	3,009
U.S. agency obligations	1	636	18	(36)	618
Foreign	2	1,477	276	—	1,753
Corporate debt	2	25,292	1,039	(360)	25,971
Preferred stock	2	12,985	1,100	—	14,085
Mortgage backed securities	2	1	—	—	1
Common stock	1	6,566	358	(588)	6,336
Mutual funds:					
Equity	1	11,559	1,474	(23)	13,010
Fixed income	2	6,170	170	(68)	6,272
Other investments	2	2,255	—	(14)	2,241
Trust securities		\$ 83,477	\$ 4,521	\$ (1,089)	\$ 86,909
Accrued investment income		\$ 819			\$ 819
Preneed funeral trust investments					\$ 87,728
Fair market value as a percentage of cost					104.1%

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

Due in one year or less	\$ 639
Due in one to five years	8,164
Due in five to ten years	12,712
Thereafter	23,922
Total	\$ 45,437

The cost and fair market values associated with preneed funeral trust investments at December 31, 2012 are detailed below (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 13,448	\$ —	\$ —	\$ 13,448
Fixed income securities:					
U.S. treasury debt	1	3,001	75	—	3,076
U.S. agency obligations	1	142	4	—	146
Foreign	2	1,217	273	—	1,490
Corporate debt	2	25,060	661	(331)	25,390
Preferred stock	2	15,228	715	(193)	15,750
Common stock	1	5,770	27	(996)	4,801
Mutual funds:					
Equity		11,843	487	(78)	12,252
Fixed income	1	6,105	181	(40)	6,246
Other investments	2	2,143	—	(15)	2,128
Trust securities	2	\$ 83,957	\$ 2,423	\$ (1,653)	\$ 84,727
Accrued investment income		\$ 688			\$ 688
Preneed funeral trust investments					\$ 85,415
Market value as a percentage of cost					100.9%

We determine whether or not the assets in the preneed funeral trusts 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*. 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. Our preneed funeral trust investment unrealized losses, their associated fair market values, and the duration of unrealized losses as of March 31, 2013 and December 31, 2012, respectively, are shown in the following tables (in thousands):

	March 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. agency obligations	\$ 12	\$ —	\$ 231	\$ (36)	\$ 243	\$ (36)
Corporate debt	4,551	(157)	344	(203)	4,895	(360)
Common stock	1,742	(479)	597	(109)	2,339	(588)
Mutual funds:						
Equity	17	—	570	(23)	587	(23)
Fixed income	2,909	(68)	—	—	2,909	(68)
Other investments	—	—	31	(14)	31	(14)
Total temporary impaired securities	\$ 9,231	\$ (704)	\$ 1,773	\$ (385)	\$ 11,004	\$ (1,089)



	December 31, 2012					
	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:						
Corporate debt	7,419	(212)	406	(119)	7,825	(331)
Preferred stock	685	(35)	1,504	(158)	2,189	(193)
Common stock	3,323	(609)	625	(387)	3,948	(996)
Mutual funds:						
Equity	1,613	(25)	632	(53)	2,245	(78)
Fixed income	3,085	(40)	—	—	3,085	(40)
Other investments	—	—	30	(15)	30	(15)
Total temporary impaired securities	<u>\$ 16,125</u>	<u>\$ (921)</u>	<u>\$ 3,197</u>	<u>\$ (732)</u>	<u>\$ 19,322</u>	<u>\$ (1,653)</u>

Preneed funeral trust investment security transactions recorded in *Interest income and other, net* in the Consolidated Statements of Operations for the three months ended March 31, 2012 and 2013 are as follows (in thousands):

	For the three months ended March 31,	
	2012	2013
Investment income	\$ 861	\$ 606
Realized gains	735	5,127
Realized losses	(449)	(5,332)
Expenses and taxes	(210)	(248)
Decrease in deferred preneed funeral receipts held in trust	(937)	(153)
	<u>\$ —</u>	<u>\$ —</u>

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

	For the three months ended March 31,	
	2012	2013
Purchases	\$ (17,873)	\$ (3,186)
Sales	18,174	3,915

## 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. Occasionally, we offer zero percent interest financing to promote sales as limited-time offers. At March 31, 2013, the balances of preneed receivables for cemetery interment rights and for merchandise and services were \$21.3 million and \$8.7 million, respectively, of which \$10.3 million is presented in *Accounts receivable* and \$19.7 million is presented in *Preneed receivables*. The unearned finance charges associated with these receivables were \$3.3 million and \$3.6 million at December 31, 2012 and March 31, 2013, 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 5.3% of the total receivables on recognized sales at March 31, 2013. 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, 2013, changes in the allowance for contract cancellations were as follows (in thousands):

	<b>March 31, 2013</b>
Beginning balance	\$ 1,903
Write-offs and cancellations	(591)
Provision	193
Ending balance	<u>\$ 1,505</u>

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

	<b>31-60 Past Due</b>	<b>61-90 Past Due</b>	<b>91-120 Past Due</b>	<b>&gt;120 Past Due</b>	<b>Total Past Due</b>	<b>Current</b>	<b>Total Financing Receivables</b>
Recognized revenue	\$ 556	\$ 268	\$ 177	\$ 930	\$ 1,931	\$ 19,047	\$ 20,978
Deferred revenue	169	113	84	453	819	8,258	9,077
Total contracts	<u>\$ 725</u>	<u>\$ 381</u>	<u>\$ 261</u>	<u>\$ 1,383</u>	<u>\$ 2,750</u>	<u>\$ 27,305</u>	<u>\$ 30,055</u>

#### 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, 2012 and March 31, 2013, receivables from preneed trusts are as follows (in thousands):

	<b>December 31, 2012</b>	<b>March 31, 2013</b>
Preneed trust funds, at cost	\$ 26,671	\$ 27,772
Less: allowance for contract cancellation	(800)	(834)
Receivables from preneed trusts, net	<u>\$ 25,871</u>	<u>\$ 26,938</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 \$237.4 million and \$272.6 million at December 31, 2012 and March 31, 2013, respectively, and are not included in 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, 2012 and March 31, 2013 are as follows (in thousands):

	<b>December 31, 2012</b>	<b>March 31, 2013</b>
Trust assets, at fair value	\$ 46,542	\$ 47,165
Obligations due to trust	(622)	(82)
Care trusts' corpus	<u>\$ 45,920</u>	<u>\$ 47,083</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, common stock, U.S. treasury debt, U.S. agency obligations 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 corporate debt, preferred stocks, foreign debt, mortgage backed securities and fixed income securities, all of which are classified within Level 2 of the valuation hierarchy. There were no significant transfers between Levels 1 and 2 for the three months ended March 31, 2013. 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, 2013 (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 683	\$ —	\$ —	\$ 683
Fixed income securities:					
Foreign	2	1,527	286	—	1,813
Corporate debt	2	24,493	917	(346)	25,064
Preferred stock	2	11,984	874	—	12,858
Mortgage backed securities	2	1	—	—	1
Common stock	1	6,143	317	(569)	5,891
Trust securities		\$ 44,831	\$ 2,394	\$ (915)	\$ 46,310
Accrued investment income		\$ 855			\$ 855
Cemetery perpetual care trust investments					\$ 47,165
Fair market value as a percentage of cost					103.3%

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	6,233
Due in five to ten years	11,459
Thereafter	22,044
	\$ 39,736

The following table reflects the cost and fair market values associated with the trust investments held in perpetual care trust funds at December 31, 2012 (in thousands):

	Fair Value Hierarchy Level	Cost	Unrealized Gains	Unrealized Losses	Fair Market Value
Cash and money market accounts	1	\$ 545	\$ —	\$ —	\$ 545
Fixed income securities:					
Foreign	2	1,267	284	—	1,551
Corporate debt	2	24,324	556	(323)	24,557
Preferred stock	2	14,225	525	(187)	14,563
Mortgage backed securities	2	1	—	—	1
Common stock	1	5,563	22	(969)	4,616
Trust securities		\$ 45,925	\$ 1,387	\$ (1,479)	\$ 45,833
Accrued investment income		\$ 709			\$ 709
Cemetery perpetual care investments					\$ 46,542
Market value as a percentage of cost					99.8%

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. Our perpetual care trust investment unrealized losses, their associated fair market values, and the duration of unrealized losses for the period as of March 31, 2013 and December 31, 2012, respectively, are shown in the following tables (in thousands):

	March 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:						
Corporate debt	\$ 4,382	\$ (151)	\$ 332	\$ (195)	\$ 4,714	\$ (346)
Common stock	1,684	(463)	577	(106)	2,261	(569)
Total temporary impaired securities	<u>\$ 6,066</u>	<u>\$ (614)</u>	<u>\$ 909</u>	<u>\$ (301)</u>	<u>\$ 6,975</u>	<u>\$ (915)</u>
	December 31, 2012					
	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:						
Corporate debt	7,236	(207)	396	(116)	7,632	(323)
Preferred stock	664	(34)	1,459	(153)	2,123	(187)
Common stock	3,231	(593)	608	(376)	3,839	(969)
Total temporary impaired securities	<u>\$ 11,131</u>	<u>\$ (834)</u>	<u>\$ 2,463</u>	<u>\$ (645)</u>	<u>\$ 13,594</u>	<u>\$ (1,479)</u>

Perpetual care trust investment security transactions recorded in *Interest income and other, net* in the Consolidated Statements of Operations for the three months ended March 31, 2012 and 2013 are as follows (in thousands):

	For the three months ended March 31,	
	2012	2013
Undistributable realized gains	\$ 1,131	\$ 24
Undistributable realized losses	(52)	(295)
Increase in care trusts' corpus	(1,079)	271
	<u>\$ —</u>	<u>\$ —</u>

Perpetual care trust investment security transactions recorded in *Cemetery revenue* for the three months ended March 31, 2012 and 2013 are as follows (in thousands):

	For the three months ended March 31,	
	2012	2013
Interest and dividends	\$ 1,164	\$ 1,411
Realized gains	—	561
Expenses	(14)	(163)
Total	<u>\$ 1,150</u>	<u>\$ 1,809</u>

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

	For the three months ended March 31,	
	2012	2013
Purchases	\$ (16,217)	\$ (2,587)
Sales	16,621	3,121

## 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. The long-term debt and line of credit are classified within Level 2 of the Fair Value Measurements hierarchy. The fair values of the long-term debt and line of credit 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 junior subordinated debentures is approximately \$95.2 million at March 31, 2013, based on available broker quotes of 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 investments categories on our Consolidated Balance Sheets as having met such criteria. See Notes 6 and 10 to this 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, U.S. agency obligations 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 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, 2013, 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. LONG-TERM DEBT**

The Company's senior long-term debt consisted of the following at December 31, 2012 and March 31, 2013 (in thousands):

	<b>December 31, 2012</b>	<b>March 31, 2013</b>
Revolving credit facility, secured, floating rate	\$ 44,700	\$ 43,000
Term loan, secured, floating rate	127,500	125,000
Acquisition debt	2,427	2,187
Less: current portion	(11,086)	(11,469)
<b>Total long-term debt</b>	<b>\$ 163,541</b>	<b>\$ 158,718</b>

As of March 31, 2013, we had a \$235 million secured bank credit facility (the "Credit Facility") with Bank of America, N.A. as Administrative Agent comprised of a \$105 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. Interest under the new Credit Facility is payable at prime or LIBOR options. As of March 31, 2013, \$43 million was drawn under the revolving credit facility and \$125 million was outstanding on the term loan. No letters of credit were issued and outstanding under the Credit Facility at March 31, 2013. See Subsequent Events, Note 20, herein for further information on 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, 2013. 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, 2013, the leverage ratio was 3.03 to 1.00 and the fixed charge coverage ratio was 2.41 to 1.00.

Acquisition debt consists of deferred purchase price and promissory notes payable to sellers. These notes bear interest at 0%, discounted at imputed interest rates ranging from 8.50% to 9.50%, with original maturities from one to ten years.

**13. 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 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 the Defendants’ motion to disqualify Plaintiffs’ counsel. In that order, the Court gave Plaintiffs 60 days within which to retain new 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 the trial court granted the newly retained Plaintiffs’ counsel 90 days to review the case and advise the Court whether or not Plaintiffs would seek leave to amend their complaint to add and/or change the allegations as are currently stated therein and whether or not they would seek leave to amend the proposed class representatives for class certification. Plaintiffs 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. Discovery in this matter will now proceed. We intend to defend this action vigorously. Because the lawsuit is in its preliminary stages, we are unable to evaluate the likelihood of an unfavorable outcome to us or to estimate the amount or range of any potential loss, if any, at this time.

**14. STOCK-BASED COMPENSATION**

*Stock Options and Employee Stock Purchase Plan*

No stock options were awarded during the first quarter of 2013. As of March 31, 2013, there were 283,258 stock options outstanding and 110,124 stock options which remain unvested.

During the first quarter of 2013, employees purchased a total of 22,027 shares of common stock through the employee stock purchase plan (“ESPP”) at a weighted average price of \$11.43 per share. We recorded pre-tax stock-based compensation expense for the ESPP and for stock options totaling \$97,000 and \$146,000 for the three months ended March 31, 2012 and 2013, respectively.

The fair value of the right (option) to purchase shares under the ESPP is estimated on the date of grant (January 1, 2013) associated with the four quarterly purchase dates using the following assumptions:

	2012	2013
Dividend yield	1.7%	0.6%
Expected volatility	32%	31%
Risk-free interest rate	0.02%, 0.06%, 0.09%, 0.12%	0.08%, 0.12%, 0.135%, 0.15%
Expected life (years)	0.25, 0.50, 0.75, 1.00	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 grant (January 1). The expected life of the ESPP grants represents the calendar quarters from the grant date (January 1) to the purchase date (end of each quarter).

*Common Stock Grants to Officers and Key Employees*

We, from time to time, issue shares of restricted common stock to certain officers and key employees from our stock benefit plans. The restricted stock shares issued to officers and key employees vest in 33.33% increments over three year periods. Related to the vesting of restricted stock awards previously awarded to our officers and employees, we recorded \$240,000 and \$313,000 in pre-tax compensation expense, included in general, administrative and other expenses, for the three months ended March 31, 2012 and 2013, respectively.

As of March 31, 2013, we had \$2.3 million of unrecognized compensation costs related to unvested restricted stock awards, which are expected to be recognized over a weighted average period of approximately 1.7 years.

### *Performance-based Stock Awards*

During the third quarter of 2012, the Compensation Committee of our Board of Directors (our “Board”) approved the grant of performance awards with both market and service vesting conditions to certain officers, employees and outside directors. The awards vest and become exercisable only in the event the closing price of our common stock is greater than or equal to \$21.50 on any three days, whether or not consecutive, within a period of 30 consecutive calendar days, and the grantee remains continuously employed by us from the grant date through such date, which can be no earlier than the first anniversary of the grant date. If the market condition is met prior to the first anniversary of the grant date, then such award will not become vested until the first anniversary of the grant date, provided that the grantee remains continuously employed by us from the grant date through the first anniversary of the grant date. Promptly following the date a grantee’s award becomes vested (but no later than March 15th of the year following the year in which the award becomes vested) and subject to the grantee’s payment of the purchase price, we will issue and deliver to the grantee the number of shares of our common stock subject to the award. The purchase price is equal to the greater of (a) the fair market value of a share of our common stock on the grant date plus \$0.50 or (b) \$9.00. A grantee’s award will automatically terminate without payment of any consideration if (i) the grantee’s employment with us terminates for any reason (other than due to death or disability) prior to the vesting or (ii) the vesting does not occur on or before the fifth anniversary of the grant date. No performance awards were granted during the first quarter of 2013. The pre-tax compensation expense associated with these awards for the three months ended March 31, 2013 was approximately \$169,000.

### *Director Compensation Policy*

On March 5, 2012, our Board approved a new Director Compensation Policy, which 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 for this year will be held on May 22, 2013.

We recorded \$161,000 and \$133,000 in pre-tax compensation expense, included in general, administrative and other expenses, for the three months ended March 31, 2012 and 2013, respectively, related to the director fees, annual retainers and deferred compensation amortization.

## **15. STOCKHOLDERS' EQUITY**

### *Share Repurchase Program*

During May 2012, our Board approved an increase to the share repurchase program authorizing us to purchase an additional \$3 million of our common stock up to a total of \$8 million. The repurchases are executed in the open market and through privately negotiated transactions subject to market conditions, normal trading restrictions and other relevant factors. During 2012, we repurchased 686,208 shares of common stock at an aggregate cost of \$4.5 million and an average cost per share of \$6.60. No repurchases were made in the first quarter of 2013. The repurchased shares are held as treasury stock. Since the beginning of this program, we have spent \$5.3 million buying back our common stock under this plan.

### *Cash Dividends*

Our Board declared a quarterly dividend of \$0.025 per share, totaling \$452,000, which was paid on March 1, 2013 to record holders of our common stock as of February 13, 2013. 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:

	<b>Accumulated Other Comprehensive Income</b>
Balance at December 31, 2012	\$ —
Increased in net unrealized gains associated with available-for-sale securities of the trusts	7,266
Reclassification of net unrealized gain activity attributable to the <i>Deferred preneed funeral and cemetery receipts held in trust and Care trusts' corpus'</i>	(7,266)
Balance at March 31, 2013	\$ —

## 16. 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):

	<b>Funeral</b>	<b>Cemetery</b>	<b>Corporate</b>	<b>Consolidated</b>
<b>Revenues from continuing operations:</b>				
Three months ended March 31, 2013	\$ 45,157	\$ 12,930	\$ —	\$ 58,087
Three months ended March 31, 2012	\$ 40,035	\$ 11,288	\$ —	\$ 51,323
<b>Income (loss) from continuing operations before income taxes:</b>				
Three months ended March 31, 2013	\$ 14,921	\$ 3,915	\$ (8,871)	\$ 9,965
Three months ended March 31, 2012	\$ 13,788	\$ 2,384	\$ (9,528)	\$ 6,644
<b>Total assets:</b>				
March 31, 2013	\$ 490,258	\$ 241,081	\$ 16,212	\$ 747,551
December 31, 2012	\$ 481,356	\$ 237,897	\$ 18,832	\$ 738,085

**17. SUPPLEMENTAL DISCLOSURE OF STATEMENT OF OPERATIONS INFORMATION**

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

	<b>For the three months ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
<b>Revenues</b>		
Goods		
Funeral	\$ 15,753	\$ 18,017
Cemetery	7,003	7,416
Total goods	\$ 22,756	\$ 25,433
Services		
Funeral	\$ 22,158	\$ 24,909
Cemetery	2,400	2,793
Total services	\$ 24,558	\$ 27,702
Financial revenue		
Preneed funeral commission income	\$ 451	\$ 508
Preneed funeral trust earnings	1,673	1,723
Cemetery trust earnings	1,516	2,403
Cemetery finance charges	369	318
Total financial revenue	\$ 4,009	\$ 4,952
<b>Total revenues</b>	<b>\$ 51,323</b>	<b>\$ 58,087</b>
<b>Cost of revenues</b>		
Goods		
Funeral	\$ 12,203	\$ 14,070
Cemetery	5,508	5,402
Total goods	\$ 17,711	\$ 19,472
Services		
Funeral	\$ 10,406	\$ 11,938
Cemetery	1,674	1,779
Total services	\$ 12,080	\$ 13,717
Financial expenses		
Preneed funeral commissions	\$ 350	\$ 397
Trust administration fees	—	63
Total financial expenses	\$ 350	\$ 460
<b>Total cost of revenues</b>	<b>\$ 30,141</b>	<b>\$ 33,649</b>

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.

**18. SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION**

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

	<b>For the three months ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
Cash paid for interest and financing costs	\$ 7,017	\$ 3,269
Cash paid (refunded) for income taxes	50	(77)
Fair value of stock, stock options and performance awards issued to directors, officers and certain employees	1,942	—
Restricted common stock withheld for payroll taxes	210	1,020
Net withdrawals from preneed funeral trusts	1,131	727
Net withdrawals from preneed cemetery trusts	959	375
Net withdrawals from perpetual care trusts	167	1,373
Net (increase)/decrease in preneed funeral receivables	30	(227)
Net increase in preneed cemetery receivables	(124)	(732)
Net (deposits)/withdrawals of receivables into/from preneed trusts	47	(1,063)
Net change in preneed funeral receivables increasing/(decreasing) deferred revenue	(182)	2,049
Net change in preneed cemetery receivables increasing deferred revenue	363	629
Net withdrawals from preneed funeral trust accounts decreasing deferred preneed funeral receipts	(1,131)	(727)
Net withdrawals in cemetery trust accounts decreasing deferred cemetery receipts	(959)	(375)
Net withdrawals in perpetual care trust accounts decreasing perpetual care trusts' corpus	(180)	(834)

## 19. EARNINGS PER SHARE

Earnings per share for the three months ended March 31, 2012 and March 31, 2013 is calculated based on the weighted average number of common and common equivalent shares outstanding during the periods. The following table sets forth the computation of the basic and diluted earnings per share for the three months ended March 31, 2012 and March 31, 2013:

	For the three months ended March 31,	
	2012	2013
Net income	\$ 4,459	\$ 5,258
Net income allocated to non-vested share awards	(110)	(118)
Preferred stock dividend	(4)	(4)
Undistributed earnings available to common stockholders	\$ 4,345	\$ 5,136
Income (loss) from discontinued operations	389	(323)
Undistributed earnings from continuing operations available to common stockholders	3,956	5,459
Weighted average number of common shares outstanding for basic EPS computation	18,265	18,139
Effect of dilutive securities:		
Stock options	55	197
Convertible junior subordinated debentures	—	4,392
Weighted average number of common and common equivalent shares outstanding for diluted EPS computation	18,320	22,728
Basic earnings per common share:		
Undistributed earnings	\$ 0.22	\$ 0.30
Allocation of earnings to non-vested share awards	—	0.01
Basic earnings per share from continuing operations	0.22	0.31
Discontinued operations	0.02	(0.02)
Basic earnings per common share	\$ 0.24	\$ 0.29
Diluted earnings per common share:		
Undistributed earnings	\$ 0.22	\$ 0.26
Allocation of earnings to non-vested share awards	—	0.01
Diluted earnings per share from continuing operations	0.22	0.27
Discontinued operations	0.02	(0.02)
Diluted earnings per common share	\$ 0.24	\$ 0.25

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 include outstanding unvested restricted stock awards in 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 GAAP 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, 2012, the conversion of our convertible junior subordinated debentures is excluded from fully diluted earnings per share calculation and the fully diluted weighted average share count because the inclusion of such converted shares would result in an antidilutive impact.

The following table sets forth the reconciliation of the numerators and denominators of the basic and diluted earnings per share computations for the three months ended March 31, 2013:

	For the three months ended March 31, 2013		
	Income (Numerator)	Shares (Denominator)	Per-Share Amount
Net income	\$ 5,258		
Less: Preferred Stock dividends	(4)		
<b>Basic earnings per share</b>			
Net income available to common stockholders	5,254	18,139	\$ 0.29
<b>Effect of dilutive securities</b>			
Stock options	—	197	
Convertible junior subordinated debentures	484	4,392	
<b>Diluted earnings per share</b>			
Net income available to common stockholders and assumed conversions	\$ 5,738	22,728	\$ 0.25

## 20. SUBSEQUENT EVENTS

### *Conversion of Preferred Stock*

The Company has 40,000,000 authorized shares of preferred stock. In 2008, we issued 20,000 shares of mandatorily redeemable convertible preferred stock to a key employee in exchange for certain intellectual property rights. The preferred stock has a liquidation value of \$10 per share and is convertible at any time prior April 13, 2013 into the Company's common stock on a one-for-one basis. On April 1, 2013, our key employee converted his 20,000 shares of mandatorily redeemable convertible preferred stock into common stock.

### *Amendment to the Credit Facility*

On April 24, 2013, the Company entered into a third amendment to the Credit Facility (the "Third Amendment") which provides for an increase in the revolving credit commitments under the Credit Facility from \$105 million to \$125 million and a decrease in the interest rate margin. 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. The Third Amendment decreases the applicable margin for the Company's outstanding borrowings (for both prime rate and LIBOR base rates) by 50 basis points at each leverage ratio threshold.

The Third Amendment also contains amendments which (a) allow the Company to issue subordinated debt or convertible subordinated debt in an amount not to exceed \$100 million, (b) provide the Company with the ability to repurchase up to \$15 million worth of stock-based employee awards, and (c) allow for the Company to refinance its existing convertible junior subordinated debentures with the proceeds of certain issuances of subordinated debt or convertible subordinated debt.

## 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 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; 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, 2012.

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, 2013, we operated 167 funeral homes in 26 states and 33 cemeteries in 11 states within the United 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 rewards 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 death care 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* – We believe 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 24,510 in 2008 to 28,356 in 2012 (compounded annual increase of 3.7%). Our funeral operating revenue has increased from \$124.1 million in 2008 to \$146.4 million in 2012 (compounded annual increase of 4.2%). The increases are primarily because of businesses we acquired in the last five years and our ability to increase the average revenue per funeral through expanded service offerings and packages. We experienced an increase of 13.3% in

volumes and 13.2% in funeral operating revenues in the first three months of 2013 compared to the first three months of 2012, primarily as a result of the acquisitions completed during the trailing twelve months.

The percentage of funeral services involving cremations has increased from 38.2% for the year ended 2008 to 46.0% for the year ended 2012, and was 46.4% for the first three months of 2013. On a same store basis, the cremation rate has risen to 45.6% for the first three months of 2013, up from 44.5% for the year ended December 31, 2012, and 44.5% for the comparable three month period in 2012.

Cemetery operating results are affected by the size and success of our sales organization. Approximately 47% of our cemetery revenues for the year ended December 31, 2012 related to preneed sales of interment rights and the delivery of related merchandise and services. For the three months ended March 31, 2013, those preneed sales were approximately 46.2% of cemetery revenues. We believe that changes in the level of consumer confidence (a measure of whether consumers will spend for discretionary items) also affect the amount of cemetery revenues. Currently, approximately 20% of our cemetery revenues are attributable to investment earnings on trust funds and finance charges on preneed installment contracts. Changes in the capital markets and interest rates affect this component of our cemetery revenues.

Our cemetery financial performance from 2008 through 2012 was characterized by fluctuating operating revenues yet increasing field level profit margins. Cemetery operating revenue increased from \$38.0 million in 2008 to \$40.1 million in 2012. Our goal is to build stronger teams of sales leaders and counselors in our larger and more strategically located cemeteries in order to focus on growth of our preneed property sales. Additionally, a portion of our capital expenditures in 2013 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 death care 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*. 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*. In substantially all cases, we receive an initial down payment at the time the contract is signed. Occasionally, we offer zero percent interest financing to promote sales as limited-time offers. 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, 2013, CSV RIA provides these services to one institution, which has custody of 68% 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 toward generating long-term investment returns without assuming undue risk, while ensuring the management of 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 *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 2012, we acquired seven funeral home businesses and one cemetery business. The consideration paid for the 2012 acquisitions was \$42.7 million. We did not acquire any businesses during the first three months of 2013.

### *Financial Highlights*

Net income from continuing operations for the three months ended March 31, 2013 totaled \$5.6 million, equal to \$0.27 per diluted share, compared to net income for the three months ended March 31, 2012, which totaled \$4.1 million, equal to \$0.22 per diluted share. Total revenue for the three months ended March 31, 2013 was \$58.1 million, an increase of 13.2%, compared to \$51.3 million for the comparable period in 2012. Our funeral segment experienced increases in revenue and gross profit primarily as a result of our acquisitions and increased number of contracts from our existing locations. The cemetery segment experienced increases in revenue during the three month period ended March 31, 2013 due to higher preneed property sales, increased volume of atneed contracts and higher trust fund earnings. Gross profit in these segments was higher for the three months ended March 31, 2013 primarily as a result of higher revenue. We experienced increases in general and administrative expenses due to increases in incentive compensation and increases in salaries and benefits for additional support staff at the corporate office.

We are providing below a reconciliation 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, then adjusted for special items, including Withdrawable trust income, acquisition expenses and the other items in the table below. Non-GAAP net income is used as a supplemental financial measurement by management and investors to compare our current financial performance with our previous results and with the performance of other deathcare companies. 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. 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.

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 totaled \$0.7 million for the three month period ended March 31, 2012, and \$0.5 million for the three month period ended March 31, 2013. The year over year decline was attributable to substantial gains realized in the trust funds throughout 2012 that were not repeated in 2013. 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>	Three Months Ended March 31,	
	2012	2013
Net income from continuing operations, as reported	\$ 4.1	\$ 5.6
After-tax special items:		
Withdrawable trust income	0.5	0.3
Acquisition expenses	0.2	—
Severance costs	0.3	0.1
Other special items	0.1	0.1
Non-GAAP net income	\$ 5.2	\$ 6.1

## 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. 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, 2012. 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, 2012.

## RESULTS OF OPERATIONS

The following is a discussion of our results of continuing operations for the three month periods ended March 31, 2012 and 2013. The term "same store" or "existing operations" refers to funeral homes and cemeteries acquired prior to January 1, 2008 and owned and operated for the entirety of each period being presented. Funeral homes and cemeteries purchased after December 31, 2007 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, 2012 compared to the three months ended March 31, 2013.

Three months ended March 31, 2012 compared to three months ended March 31, 2013 (dollars in thousands):

	Three Months Ended March 31,		Change	
	2012	2013	Amount	%
<b>Revenues:</b>				
Same store operating revenue	\$ 31,517	\$ 33,172	\$ 1,655	5.3%
Acquired operating revenue	6,394	9,754	3,360	52.5%
Preneed funeral insurance commissions	451	508	57	12.6%
Preneed funeral trust earnings	1,673	1,723	50	3.0%
<b>Total</b>	<b>\$ 40,035</b>	<b>\$ 45,157</b>	<b>\$ 5,122</b>	<b>12.8%</b>
<b>Operating profit:</b>				
Same store operating profit	\$ 12,833	\$ 13,552	\$ 719	5.6%
Acquired operating profit	2,470	3,365	895	36.2%
Preneed funeral insurance commissions	100	110	10	10.0%
Preneed funeral trust earnings	1,673	1,709	36	2.2%
<b>Total</b>	<b>\$ 17,076</b>	<b>\$ 18,736</b>	<b>\$ 1,660</b>	<b>9.7%</b>

Funeral home same store operating revenues for the three months ended March 31, 2013 increased \$1.7 million, or 5.3%, when compared to the three months ended March 31, 2012, as we experienced a 7.0% increase in the number of contracts, while the average revenue per contract decreased 2.1%, or \$119 per contract, to \$5,472 for those existing operations. 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 1.6% to \$5,239. The number of traditional burial contracts increased 5.4% while the average revenue per burial contract decreased 1.3% to \$8,280. The cremation rate for the same store businesses increased from 44.5% to 45.6%. The average revenue per same store cremation contract decreased 2.7% to \$3,048 and the number of cremation contracts increased 9.4%. Cremations with services declined from 37.1% of total cremation contracts in the first quarter of 2012 to 33.4% in the first quarter of 2013. The average revenue for "other" contracts, which are charges for merchandise or services for which we do not perform a funeral service and which make up approximately 6.9% of the total number of contracts, increased 3.6% to \$2,137.

Same store operating profit for the three months ended March 31, 2013 increased \$0.7 million, or 5.6%, from the comparable three months of 2012, and as a percentage of funeral same store operating revenue, increased to 40.9% from 40.7%. The increase in profit is primarily the result of the increase in revenue per the discussion above.

Funeral home acquired revenues for the three months ended March 31, 2013 increased \$3.4 million, or 52.5%, when compared to the three months ended March 31, 2012, as we experienced a 39.7% increase in the number of contracts, and an increase of 9.4%, to \$5,021, in the average revenue per contract for those acquired operations. Excluding funeral trust earnings, the average revenue per contract increased 9.2% to \$4,938. The cremation rate for the acquired businesses was 49.1% for the first quarter of 2013, down 440 basis points from the prior-year period. The average revenue per cremation contract decreased 1.2% to \$3,056 for the first quarter of 2013 and the number of cremation contracts increased 28.3% compared to the same period of 2012. The reason for the large increase in the average revenue per contract for acquired operations and the significant decline in the cremation rate is because the businesses acquired during 2012 serve primarily traditional burial families.

Acquired operating profit for the three months ended March 31, 2013 increased \$0.9 million from the comparable three months of 2012 and, as a percentage of revenue from acquired businesses, was 34.5% for the first quarter of 2013 compared to 38.6% for the first quarter of 2012. 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 5.0% in revenue and 2.6% in operating profit, compared to the three months ended March 31, 2012 as a result of slightly 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, 2012 compared to the three months ended March 31, 2013.

*Three months ended March 31, 2012 compared to three months ended March 31, 2013 (dollars in thousands):*

	Three Months Ended March 31,		Change	
	2012	2013	Amount	%
<b>Revenues:</b>				
Same store operating revenue	\$ 9,403	\$ 10,140	\$ 737	7.8 %
Acquired operating revenue	—	69	69	—
Cemetery trust earnings	1,516	2,403	887	58.5 %
Preneed cemetery finance charges	369	318	(51)	(13.8)%
<b>Total</b>	<b>\$ 11,288</b>	<b>\$ 12,930</b>	<b>\$ 1,642</b>	<b>14.5 %</b>
<b>Operating profit:</b>				
Same store operating profit	\$ 2,222	\$ 3,055	\$ 833	37.5 %
Acquired operating loss	—	(26)	(26)	—
Cemetery trust earnings	1,516	2,355	839	55.3 %
Preneed cemetery finance charges	368	318	(50)	(13.6)%
<b>Total</b>	<b>\$ 4,106</b>	<b>\$ 5,702</b>	<b>\$ 1,596</b>	<b>38.9 %</b>

Cemetery same store operating revenues for the three months ended March 31, 2013 increased \$0.7 million, or 7.8%, compared to the three months ended March 31, 2012. The increase in operating revenue was primarily attributable to preneed property sales which increased \$0.4 million, or 8.7%. We experienced a 4.2% decrease in the number of interment rights (property) sold, yet a 12.3% increase in the average price per interment compared to the first quarter of 2012. 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 92.6% to 91.8%. Same store at-need revenue increased \$0.5 million, or 12.4%, as at-need contracts increased 5.6% while revenue from deliveries of preneed merchandise and services remained flat.

Cemetery same store operating profit for the three months ended March 31, 2013 increased \$0.8 million, or 37.5%. As a percentage of revenues, cemetery same store operating profit increased from 23.6% to 30.1%. The increase in operating profit is primarily a result of the increase in revenue and lower promotional expenses and bad debt.

We acquired one cemetery in the second quarter of 2012 which primarily operates as an at-need business. This is the only 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, 2013 increased 58.5%, when compared to the three months ended March 31, 2012. Earnings from perpetual care trust funds totaled \$1.7 million for the three months ended March 31, 2013 compared to \$1.1 million for the three months ended March 31, 2012, an increase of \$0.6 million, or 49.8%. Trust earnings recognized upon the delivery of merchandise and service contracts increased 25.4% from the same period in 2012. Trust earnings also include trust management fees charged by the company's wholly-owned registered investment advisor based on the fair market value of the trust assets. Finance charges on the preneed contracts decreased 13.8% because of the decrease in the total receivables outstanding.

*Other.* General and administrative expenses totaled \$5.8 million for the three months ended March 31, 2013, an increase of \$0.5 million, or 10.2%, compared to the three months ended March 31, 2012, primarily due to increases in costs of approximately \$0.2 million for incentive compensation and \$0.6 million of additional costs for talent in our corporate office offset by \$0.3 million in expenses in 2012 related to termination expenses and acquisition expenses that were not as significant in the current period.

*Income Taxes.* We recorded income taxes at the estimated effective rate of 39.7% for the year ended December 31, 2012 and 38.0% for the first three months of 2013 before discrete items. Discrete items added an additional \$0.6 million or 6.0% of our first quarter revenues for a total stated rate of 44.0%. We have approximately \$36.8 million of state net operating loss carryforwards that will expire between 2013 and 2033, 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, 2013, the valuation allowance was approximately \$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). 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 borrowing under our Credit Facility (as defined below) 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 2013 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, 2012.

### Cash Flows

We began 2013 with \$1.7 million in cash and other liquid investments and ended the first quarter with \$1.3 million in cash and \$43.0 million drawn on our revolving credit facility.

The following table sets forth the elements of cash flow for the three months ended March 31, 2012 and March 31, 2013 (in millions):

	Three Months Ended March 31,	
	2012	2013
Cash at January 1st	\$ 1.1	\$ 1.7
Cash flow from continuing operating activities	3.1	10.9
Acquisitions	(11.6)	—
Borrowings (payments) on our Credit Facility	13.9	(4.2)
Maintenance capital expenditures	(0.9)	(1.8)
Dividends on common stock	(0.4)	(0.4)
Repurchase of common stock	(2.7)	—
Growth capital expenditures – funeral homes	(1.3)	(6.6)
Growth capital expenditures – cemeteries	(0.9)	(0.3)
Cash provided by discontinued operations	0.4	2.0
Other financing costs	0.2	—
Cash at March 31st	<u>\$ 0.9</u>	<u>\$ 1.3</u>

For the three months ended March 31, 2013 cash provided by continuing operating activities was \$10.9 million as compared to \$3.1 million for the three months ended March 31, 2012. The increase was due to an increase in revenue and cash earned on delivered contracts.

Our investing activities resulted in a net cash outflow of \$6.8 million for the three months ended March 31, 2013, compared to a net cash outflow of \$14.7 million for the three months ended March 31, 2012. The decrease in cash outflows from investing activities was due to the lack of acquisition activity in the first three months of 2013. For the three months ended March 31, 2013, capital expenditures totaled \$8.7 million, compared to \$3.1 million for the three months ended March 31, 2012. Capital expenditures during the first three months of 2013 included \$6.0 million for funeral home expansion projects.

Our financing activities resulted in net cash outflow of \$4.6 million for the three months ended March 31, 2013, compared to a net cash inflow of \$10.9 million for the three months ended March 31, 2012. The decrease in cash flows from financing activities is primarily due to scheduled payments under our Credit Facility and long-term debt during the first quarter of 2013. During the first quarter of 2012, we borrowed \$13.9 million under the Credit Facility whereas we repaid \$4.2 million under our Credit Facility in the first quarter of 2013. The cash flows from financing activities during the first three months of 2012 was partially offset by the purchase of \$2.7 million in treasury stock, which did not occur during the first three months of 2013.

#### *Dividends*

Our Board declared a quarterly cash dividend of \$0.025 per share, totaling \$0.4 million, which was paid on March 1, 2013 to record holders of our common stock as of February 13, 2013.

#### *Debt Obligations*

The outstanding principal of long-term debt at March 31, 2013 totaled \$174.3 million and consisted of \$125.0 million under our term loan, \$43.0 million outstanding under our revolving credit facility and \$6.3 million in acquisition indebtedness and capital lease obligations.

As of March 31, 2013, we had a \$235 million secured bank credit facility (the "Credit Facility") with Bank of America, N.A. as the Administrative Agent comprised of a \$105 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. Interest under the new Credit Facility is payable at prime or LIBOR options. As of March 31, 2013, \$43 million was drawn under the revolving credit facility and \$125 million was outstanding under the term loan. No letters of credit were issued and outstanding under the Credit Facility at March 31, 2013.

We have the option to pay interest under the Credit Facility at either prime rate or LIBOR rate plus a margin. At March 31, 2013, the prime rate margin was equivalent to 2.50% and the LIBOR margin was 3.50%. The weighted average interest rate on the Credit Facility at March 31, 2013 was 3.7%.

On April 24, 2013, the Company entered into a third amendment to the Credit Facility (the "Third Amendment") which provides for an increase in the revolving credit commitments under the Credit Facility from \$105 million to \$125 million and a decrease in the interest rate margin. 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. The Third Amendment decreases the applicable margin for the Company's outstanding borrowings (for both prime rate and LIBOR base rates) by 50 basis points at each leverage ratio threshold.

The Third Amendment also contains amendments which (a) allow the Company to issue subordinated debt or convertible subordinated debt in an amount not to exceed \$100 million, (b) provide the Company with the ability to repurchase up to \$15 million worth of stock-based employee awards, and (c) allow for the Company to refinance its existing convertible junior subordinated debentures with the proceeds of certain issuances of subordinated debt or convertible subordinated debt.

A total of \$89.8 million was outstanding at March 31, 2013 under the convertible junior subordinated debenture. Amounts outstanding under the debentures are payable to our affiliate trust, Carriage Services Capital Trust (the "Trust"), bear interest at 7.0% and mature in 2029. Substantially all the assets of the Trust consist of the convertible junior subordinated debentures. In 1999, the Trust issued 1.875 million shares of 7% convertible preferred securities, termed "TIDES." The rights under the debentures are functionally equivalent to those of the TIDES.

The convertible junior subordinated debentures payable to the affiliated Trust, and the TIDES, each contain a provision for the deferral of interest payments and distributions for up to 20 consecutive quarters. During any period in which distribution payments are deferred, distributions will continue to accumulate at the 7% annual rate. Also, the deferred distributions themselves accumulate distributions at the annual rate of 7%. During any deferral period, we are prohibited from paying dividends on common stock or repurchasing common stock, subject to limited exceptions. We currently expect to continue paying the distributions as due.

We were in compliance with the covenants contained in the Credit Facility as of March 31, 2013. 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 June 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, 2013, the leverage ratio was 3.03 to 1.00 and the fixed charge coverage ratio was 2.41 to 1.00.

In May 2012, our Board approved an increase to the share repurchase program authorizing the Company to purchase an additional \$3 million of our common stock up to an aggregate of \$8 million. Through March 31, 2013, we spent \$5.3 million buying back our common stock under this plan.

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, 2013, 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, 2013 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 1.48% 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, 2013, we had \$43.0 million outstanding under our \$105.0 million revolving credit facility and \$125.0 million 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, 2013, the prime rate margin was equivalent to 2.50% and the LIBOR margin was 3.50%. 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 \$1.7 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 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 \$89.8 million. The estimated fair value of these securities is estimated to be approximately \$95.2 million at March 31, 2013, based on available broker quotes of the corresponding preferred securities issued by the Trust.

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) or 15d-15(e) under 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, 2013 (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, 2013, 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 13 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, 2012. 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, 2012, 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, 2012 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>
*10.1	Employment Agreement with Mark R. Bruce dated January 4, 2011.
*10.2	Employment Letter with Mark R. Bruce dated March 14, 2012.
*10.3	Employment Agreement with Shawn R. Phillips dated January 4, 2011.
*10.4	Employment Letter with Shawn R. Phillips dated March 14, 2012.
*10.5	Employment Agreement with Paul D. Elliott dated August 31, 2012.
10.6	Third Amendment and Commitment Increase dated April 23, 2013 among Carriage Services, Inc., the Lenders and Bank of America, N.A. Incorporated by reference to Exhibit 10.1 to the Company’s Current Report on Form 8-K filed April 25, 2013.
*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, 2013

CARRIAGE SERVICES, INC.

/s/ L. William Heiligbrodt

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L. William Heiligbrodt

Vice Chairman of the Board, Executive

Vice President, Secretary and Director

(Principal Financial Officer and Duly Authorized Officer)

**CARRIAGE SERVICES, INC.**

**INDEX OF EXHIBITS**

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## EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (the "Agreement"), dated January 4, 2011 (the "Effective Date"), is entered into between CARRIAGE SERVICES, INC., a Delaware corporation (the "Company"), and Mark R. Bruce, a resident of Missouri City, TX (the "Employee").

1. Employment Term. The Company hereby continues the employment of the Employee for an initial term commencing as of the Effective Date and continuing until the third anniversary of the Effective Date (the "Initial Term"). On the third anniversary of the Effective Date and on each subsequent anniversary thereafter, this Agreement shall automatically renew and extend for a period of 12 months (each such 12-month period being a "Renewal Term") unless written notice of non-renewal is delivered from either party to the other not less than sixty (60) days prior to the expiration of the then-existing Initial Term or Renewal Term, as applicable. Notwithstanding the foregoing, the Employee's employment pursuant to this Agreement may be terminated prior to the expiration of the then-existing Initial Term or Renewal Term as provided in Section 7 hereof. The Employee agrees to accept such employment and to perform the services specified herein, all upon the terms and conditions hereinafter stated.

2. Duties. The Employee shall serve the Company and shall report to, and be subject to the general direction and control, of the Chief Executive Officer of the Company or any other Executive Officer designated by him. The Employee shall faithfully, diligently, competently, and to the best of Employee's ability, perform the management and administrative duties of Regional Managing Partner and Regional Vice President of Operations of the Company. The Employee shall also serve as Regional Managing Partner and Regional Vice President of Operations of any subsidiary of the Company as requested by the Company, and the Employee shall perform such other duties as are from time to time assigned to him by the Chief Executive Officer or any other Executive Officer designated by him as are not inconsistent with the provisions hereof. The Employee represents and warrants to the Company that Employee is not subject to any obligation to any third party that would restrict or interfere with Employee's ability to perform hereunder.

3. Extent of Service. The Employee shall devote his full business time and attention to the business of the Company and, except as may be specifically permitted by the Company, shall not be engaged in any other business activity during the term of this Agreement. The foregoing shall not be construed as preventing the Employee (i) from making passive investments in other businesses or enterprises, and (ii) from engaging in other civic, charitable and business activities, provided, however, that such investments and activities will not require services on the part of the Employee which would in any way impair the performance of his duties under this Agreement.

4. Compensation. During the term of this Agreement, the Company shall pay the Employee an annual salary at a rate of not less than \$200,000 per full calendar year of service completed (“Base Salary”), appropriately prorated for partial years at the commencement and end of the term of this Agreement. The Employee's salary and benefits will be reviewed annually, and any increase therein shall remain in the sole discretion of the Company, acting through the Compensation Committee of the Board (the “Compensation Committee”). The salary set forth herein shall not be subject to reduction and shall be payable in bi-weekly installments in accordance with the payroll policies of the Company in effect from time to time during the term of this Agreement. The Company shall have the right to deduct from payment of all compensation to the Employee hereunder (i) any federal, state or local taxes required by law to be withheld with respect to such payments, and (ii) any other amounts specifically authorized to be withheld or deducted by the Employee.

5. Benefits. In addition to the Base Salary, the Employee shall be entitled to participate in the following benefits during the term of this Agreement:

(a) Employee shall be eligible for an annual, discretionary incentive award (the “Incentive Award”) for each full calendar year that he is employed hereunder, based on achievement of specified corporate and individual performance goals established at the beginning of the year by the Compensation Committee of the Board at its first meeting of the fiscal year. The goals 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 Target level the Incentive Award will be 40% of Base Salary, (ii) at the Threshold level the Incentive Award will be 20 % of Base Salary and (iii) at the Maximum level the Incentive Award will be 80% of Base Salary. In the discretion of the Compensation Committee, awards for performance falling between Threshold, Target and Maximum goals may be ratably scaled above and below the goal levels. The Incentive Award shall be payable before March 15 of the year following the calendar year to which the Incentive Award 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 Incentive Award.

(b) Employee shall be eligible for consideration of awards of restricted stock or other incentive-based compensation under the terms of the Company's 2006 Long Term Incentive Plan or one or more of the Company's other incentive plans, as may be recommended by the Chief Executive Officer and approved by the Compensation Committee.

(c) Four weeks of paid vacation in each calendar year, subject to the Company's personnel policies respecting such matters.

(d) Participation in the Company's group health and hospitalization program, and inclusion in such other employee benefits, as are available generally to executive-level employees of the Company.

(e) Reimbursement for travel, lodging and other out-of-pocket expenses reasonably incurred by Employee in the exercise of Employee's duties under this Agreement which are approved by the Company in advance and are duly substantiated in accordance with the Company's policies as to reimbursement. In order to assure compliance with Section 409A of

the Internal Revenue Code of 1986, as amended (the "Code"), (i) such reimbursements shall be made as soon as practicable, but in no event later than the last day of the calendar year following the calendar year in which the expense was incurred, (ii) Employee is not permitted to receive a payment or other benefit in lieu of reimbursement under this Section 5(e), and (iii) the amount of expenses for which Employee is eligible to receive reimbursement during any calendar year shall not affect the amount of expenses for which Employee is eligible to receive reimbursement during any other calendar year within the term of the Agreement.

6. Certain Additional Matters. The Employee agrees that at all times during the term of this Agreement and for a period of two years following any cessation of employment with the Company:

(a) The Employee will not knowingly or intentionally do or say any act or thing which will or may impair, damage or destroy the goodwill and esteem for the Company held by its suppliers, employees, patrons, customers and others who may at any time have or have had business relations with the Company.

(b) The Employee will not knowingly or intentionally do any act or thing detrimental to the Company or its business.

Nothing herein shall be construed to prevent the Employee from complying with any requirements of law or legal process or taking such actions as the Company may consent to in writing.

7. Termination.

(a) Death. If the Employee dies during the Initial Term or any then-existing Renewal Term and while in the employ of the Company, this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate except that the Company shall pay the Employee's estate (i) that portion of the Employee's Base Salary accrued through the date on which the Employee's death occurred, (ii) a pro rata amount of the annual Incentive Award for the year in which the death occurred at the Target goal level described in Section 5(a) above, based on the number of days the Employee was employed in the year in comparison to 365, and (iii) all benefits payable under the governing provisions of any benefit plan or program of the Company (including as provided in Section 5(f) above). Such payment of Base Salary and Annual Incentive Award to the Employee's estate shall be made in the same manner and at the same times as they would have been paid to the Employee had he not died.

(b) Disability. If during the Initial Term or any then-existing Renewal Term, the Employee shall be prevented from performing his duties hereunder by reason of disability, and such disability shall continue for a period of six months, then the Company may terminate this Agreement at any time after the expiration of such six-month period. For purposes of this Agreement, the Employee shall be deemed to have become disabled when the Company, upon the advice of a qualified physician, shall have determined that the Employee is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous

period of not less than 12 months. In the event of a termination pursuant to this paragraph (b), the Company shall be relieved of all its obligations under this Agreement, except that the Company shall pay to the Employee (or his estate in the event of his subsequent death): (i) the Employee's Base Salary through the date on which such termination shall have occurred, reduced during such period by the amount of any benefits received under any disability policy maintained by the Company, as applicable; (ii) subject to the provisions of Section 20 below, a pro rata amount of the annual Incentive Award for the year in which Employee's employment was terminated at the Target goal level described in Section 5(a) above, based on the number of days the Employee was employed in the year in comparison to 365, which such pro rata Incentive Award payment shall be provided on the later of the first business day after the Release (as defined in Section 20 below) is no longer revocable or the payment date that an Incentive Award for the year of termination otherwise would have been payable pursuant to Section 5(a) 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)); and (iii) all benefits payable under the governing provisions of any benefit plan or program of the Company (including as provided in Section 5(f) above). Unless otherwise provided above, all such payments to the Employee or his estate shall be made in the same manner and at the same times as they would have been paid to the Employee had he remained employed by the Company. No such termination pursuant to this paragraph (b) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder.

(c) Discharge for Cause. The Company may discharge the Employee for Cause and terminate this Agreement prior to the end of the Initial Term or any then-existing Renewal Term. In such case, this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate other than to pay to the Employee (or his estate in the event of his subsequent death) that portion of the Employee's salary accrued through the date of termination.

For purposes of this Agreement, the Company shall have "Cause" to discharge the Employee or terminate the Employee's employment hereunder upon (i) the Employee's conviction of any felony or any other crime involving moral turpitude, (ii) the 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 Chief Executive Officer of the Company, (iii) the Employee's commission of acts amounting to gross negligence or willful misconduct to the material detriment of the Company, or (iv) the Employee's material breach of any provision of this Agreement or uniformly applied provisions 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 Chief Executive Officer of the Company.

Any such termination by virtue of this paragraph (c) shall not prejudice any remedy that the Company may have at law, in equity, or under this Agreement, for breach hereof by Employee. No such termination pursuant to this paragraph (c) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder.



(d) Discharge Without Cause. Prior to the end of the Initial Term or any then-existing Renewal Term, the Company may discharge the Employee without Cause (as defined in paragraph (c) above) and terminate this Agreement. In such case this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate, except that, subject to the provisions of Section 20 below, the Company shall continue to pay to the Employee (or his estate in the event of his subsequent death): (i) the Employee's monthly Base Salary, in arrears, for a period of 18 months following the date of discharge; *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, that would have otherwise been made pursuant to this Section 7(d)(i) between the date of Employee's termination of employment and the First Payment Date; (ii) a pro rata amount of the annual Incentive Award at the Target goal level described in Section 5(a) above, based on the number of days the Employee was employed in the year in comparison to 365, for the year of termination, which such pro rata Incentive Award payment shall be provided on the later of the first business day after the Release is no longer revocable or the payment date that an Incentive Award for the year of termination otherwise would have been payable pursuant to Section 5(a) 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)); and (iii) if following the date of such discharge, the Employee becomes eligible to elect continuation coverage under the Consolidated Omnibus Budget Reconciliation Act ("COBRA") and properly elects such coverage, the Company shall reimburse the Employee or pay on the Employee's behalf 100% of applicable medical continuation premiums for the benefit of the Employee (and his covered dependents as of the date of his termination, if any) under the Employee's then-current plan election, with such coverage to be provided under the closest comparable plan as offered by the Company from time to time, for so long during the 18-month period following termination as he remains eligible for and elects COBRA coverage; provided that such reimbursement shall not be applicable until the Release becomes irrevocable and the first such reimbursement payment shall include, if applicable, all reimbursement payments that would have otherwise been made pursuant to this Section 7(d)(iii) between the date of Employee's termination of employment and the date that the Release became irrevocable. The Company will also provide all salary earned by Employee through the date of termination and any applicable benefits payable under the governing provisions of any benefit plan or program of the Company. No such termination pursuant to this paragraph (d) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder. Notwithstanding anything to the contrary in this Section 7(d) or Section 20, 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 7(d)(i) will not commence and the First Payment Date shall not occur until the second taxable year, irrespective of when the Release actually becomes irrevocable.

(e) Corporate Change. If following a Corporate Change (as defined in the Company's 2006 Long-Term Incentive Plan), the Employee terminates his employment for Good Reason (as defined below) or the Employee is discharged without Cause, in either case within 24 months following the Corporate Change, then this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate, except that, subject to the provisions of Section 20 below, the Company shall pay to the Employee (or his estate in the event of his subsequent death): (i) a lump sum payment payable following such termination equal to one and one-half times the Employee's Base Salary, which such payment shall be made within ten (10) business days after the Release is no longer revocable; (ii) 100% of the annual Incentive Award at the Target goal level described in Section 5(a) above for the year of termination, which such Incentive Award payment shall be provided on the later of the first business day after the Release is no longer revocable or the payment date that an Incentive Award for the year of termination otherwise would have been payable pursuant to Section 5(a) 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)); and (iii) if following the date of such discharge, the Employee becomes eligible to elect continuation coverage under COBRA and properly elects such coverage, the Company shall reimburse the Employee or pay on the Employee's behalf 100% of applicable medical continuation premiums for the benefit of the Employee (and his covered dependents as of the date of his termination, if any) under the Employee's then-current plan election, with such coverage to be provided under the closest comparable plan as offered by the Company from time to time, for so long during the 36-month period following termination as he remains eligible for and elects COBRA coverage; provided that such reimbursement shall not be applicable until the Release becomes irrevocable and the first such reimbursement payment shall include, if applicable, all reimbursement payments that would have otherwise been made pursuant to this Section 7(e)(iii) between the date of Employee's termination of employment and the date that the Release became irrevocable. The Company will also provide all salary earned by Employee through the date of termination and any applicable. The Company will also provide any applicable benefits payable under the governing provisions of any benefit plan or program of the Company. No such termination pursuant to this paragraph (e) will relieve the Employee of his obligations under Sections 6 and 9 hereunder.

"Good Reason" means any of the following actions if taken without the Employee's prior written consent: (A) any material breach by the Company to comply with its obligations under the terms of the Agreement; (B) any material diminution in the Employee's responsibilities, authority or duties, (C) a material diminution in the Employee's Base Salary; or (D) any change greater than 50 miles in the permanent location at which the Employee performs services for the Company. The Employee shall give written notice to the Board specifying such actions within 90 days of the initial existence of such action and providing a period of 30 days in which the Company shall be allowed to cure such circumstances. Provided that the condition purporting to give rise to the Good Reason event is not cured within the 30-day cure period, Employee must exercise his right to terminate this Agreement for Good Reason within 120 days after the initial existence of the Good Reason event.

(f) Notice. Prior to the end of the term of this Agreement, the Employee may terminate this Agreement upon ninety (90) days written notice. This Agreement shall automatically terminate at the end of the notice period, and the Company shall have no further obligation to the Employee other than to pay to the Employee that portion of the Employee's salary accrued through the date of termination. No such termination pursuant to this paragraph (f) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder

(g) Equity Award Termination Provision. The impact of 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 Employee's termination from employment on: (i) the vesting of Employee's stock option, restricted stock and other share-based awards; or (ii) Employee's repurchase rights and obligations following such termination of employment, 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 for Cause (as defined in Section 7(c) above)	Forfeit all unvested awards	Forfeit all unvested awards	Forfeit all unvested awards
Involuntary Termination without Cause (as defined in Section 7(c) above) or for Good Reason (as defined in Section 7(e) above)	Forfeit all unvested awards; Employee has 12 months from the date of termination to exercise all vested awards	Forfeit all unvested awards	Forfeit all unvested awards
Voluntary Termination	Forfeit all unvested awards; Employee has 90 days from the date of termination to exercise all vested awards	Forfeit all unvested awards	Forfeit all unvested awards
Death	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

Disability	Forfeit 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 90 days 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

8. Restrictive Covenants. The Company has provided and shall provide in the future to the Employee, confidential and proprietary information as that term is defined in Section 9 of this Agreement (“Confidential Information”). The 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 shall be given possession of and access to Confidential Information of the Company and its Affiliates (as defined on Schedule I hereto), and will develop through such employment business systems, methods of doing business, and contacts within the death care industry, all of which will help to identify him 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 the Employee in the future, the sufficiency of which is hereby acknowledged by the Employee, the Employee agrees to enter into the covenants contained in this Agreement. 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 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, if the Employee had management responsibilities either directly or indirectly, over that funeral home, cemetery, or other death care business at any time during the previous 12 months;

(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, if the Employee had management responsibilities either directly or indirectly, over that funeral home, cemetery, or other death care business at any time during the previous 12 months.

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.

9. Confidential Information; Copyrightable Material. The Employee acknowledges that in the course of his employment by the Company he shall receive and access certain trade secrets, management methods, financial and accounting data (including, but not limited to, reports, studies, analyses, spreadsheets and other materials and information), operating techniques, prospective acquisitions, employee lists, training manuals and procedures, personnel evaluation procedures, and other confidential information and knowledge concerning the business of the Company and its Affiliates (hereinafter collectively referred to as "Confidential Information") which the Company desires to protect. The Employee understands that the Confidential Information is confidential and he agrees not to reveal the Confidential Information to anyone outside the Company so long as the confidential or secret nature of the Confidential Information shall continue, except as required by law or legal process. The Employee further agrees that he will at no time use the Confidential Information in competing with the Company. Upon termination of this Agreement, the Employee shall surrender to the Company all papers, documents, writings and other property produced by him or coming into his possession by or through his employment or relating to the Confidential Information and the Employee agrees that all such materials will at all times remain the property of the Company. The Employee acknowledges that all materials and other copyrightable works and subject matter (regardless of whether or not constituting "Confidential Information") produced by the Employee within the scope of his employment (regardless of whether or not denoted as copyrighted material) shall be deemed "works made for hire" and shall be owned by and proprietary to the Company and may not be used or reproduced in whole or in part without the Company's prior written consent.

10. Remedies. The parties recognize that the services to be rendered under this Agreement by the Employee are special, unique, and of extraordinary character, and that in the event of the breach by the Employee of the covenants contained in Section 8 or Section 9 hereof, the Company may suffer irreparable harm as a result. The parties therefore agree that, in the event of any breach or threatened breach of any of such covenants, the Company shall be entitled to specific performance or injunctive relief, or both, and may, in addition to and not in lieu of any claim or proceeding for damages, institute and prosecute proceedings in any court of competent jurisdiction to enforce through injunctive relief such covenants. In addition, the Company may, if it so elects, suspend (if applicable) any payments due under this Agreement pending any such breach and offset against any future payments the amount of the Company's damages arising from any such breach. The Employee agrees to waive and hereby waives any requirement for the Company to secure any bond in connection with the obtaining of such injunction or other equitable relief.

11. Notices. All notices, requests, consents and other communications under this Agreement shall be in writing and shall be deemed to have been delivered on the date personally delivered or three business days after the date mailed, postage prepaid, by certified mail, return receipt requested, or when sent by electronic means or facsimile and receipt is confirmed, if addressed to the respective parties as follows:

If to the Employee:     Mark R. Bruce  
                                  3811 Carnden Lane  
                                  Missouri City, TX 77459

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

Either party hereto may designate a different address by providing written notice of such new address to the other party hereto.

12. Severability. Whenever possible, each provision of this Agreement shall be interpreted in such manner as to be effective and valid under applicable law but if any provision of this Agreement shall be prohibited by or invalid under applicable law, such provision shall be ineffective to the extent of such provision or invalidity, without invalidating the remainder of such provision or the remaining provisions of this Agreement.

13. Assignment. This Agreement may not be assigned by the Employee. Neither the Employee nor his estate shall have any right to commute, encumber or dispose of any right to receive payments hereunder, it being agreed that such payments and the right thereto are nonassignable and nontransferable.

14. Binding Effect. Subject to the provisions of Section 13 of this Agreement, this Agreement shall be binding upon and inure to the benefit of the parties hereto, the Employee's heirs and personal representatives, and the successors and as-signs of the Company.

15. Captions. The section and paragraph headings in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement.

16. Complete Agreement. This Agreement represents the entire agreement between the parties concerning the subject hereof and supersedes all prior agreements and arrangements between the parties concerning the subject thereof.

17. Governing Law; Venue. A substantial portion of the Employee's duties under this Agreement shall be performed at the Company's corporate headquarters in Houston, Texas, and this Agreement has been substantially negotiated and is being executed and delivered in the State of Texas. This Agreement shall be construed and enforced in accordance with and governed by the laws of the State of Texas. Any suit, claim or proceeding arising under or in connection with this Agreement or the employment relationship evidenced hereby must be brought, if at all, in a state district court in Harris County, Texas or federal district court in the Southern District of Texas, Houston Division. Each party submits to the jurisdiction of such courts and agrees not to raise any objection to such jurisdiction.

18. Survival. The provisions of Sections 6, 8 and 9 shall survive any termination of this Agreement or the employment relationship of the Company and Employee; provided, however, if such termination is the result of Corporate Change as provided in Section 7(e) hereof, Employee shall not thereafter be bound by the provisions of Section 8 hereof.

19. Counterparts. This Agreement may be executed in multiple original counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

20. Severance Payments Conditioned on Release; Time of Payments. The amounts payable to Employee under Sections 7(b)(ii), 7(d)(i)-(iii) and 7(e)(i)-(iii) shall not become payable unless Employee executes (and does not revoke within seven days of its execution) a release of claims in a form satisfactory to the Company (the "Release") within the time period prescribed by the Company, which such time period shall be no later than fifty (50) days from the date of Employee's termination of employment. Notwithstanding anything contained in this Agreement to the contrary, to the maximum extent permitted by applicable law, amounts payable to Employee pursuant to Section 7 are intended to be made in reliance upon Treas. Reg. § 1.409A-1(b)(9) (separation pay plans) or Treas. Reg. § 1.409A-1(b)(4) (short-term deferrals). No amounts payable under Section 7 of this Agreement upon Employee's termination of employment shall be payable unless Employee's termination of employment constitutes a "separation from service" within the meaning of Treas. Reg. § 1.409A-1(h). The Company and Employee intend that their exercise of authority or discretion under this Agreement shall comply with Section 409A of the Code. If any provision of this Agreement does not satisfy the requirements of Section 409A, 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. Notwithstanding the foregoing, no particular tax result for Employee with respect to any income recognized by Employee in connection with this Agreement is guaranteed. Neither the Company nor any of its affiliates shall have any obligation to indemnify or otherwise hold Employee harmless from any or all such taxes, interest, penalties, or liability for any damages related

thereto. Each payment under this Agreement is intended to be a “separate payment” and not a series of payments for purposes of Section 409A. References in this Agreement to Section 409A of the Code includes rules, regulations and guidance of general applicability issued by the Department of the Treasury under Code Section 409A. If the Employee is a “specified employee,” as such term is defined in Section 409A of the Code and related regulations and Treasury pronouncements (“Section 409A”) and determined as described below in this Section 20, any payments payable as a result of the Employee's termination (other than death) that are required to be delayed in accordance with Section 409A of the Code as a result of Employee's status as a “specified employee” shall not be payable before the earliest of (i) the date that is six months after the Employee's termination, (ii) the date of the Employee's death, or (iii) the date that otherwise complies with the requirements of Section 409A. This Section 20 shall be applied by accumulating all payments that otherwise would have been paid within six months of the Employee's termination and paying such accumulated amounts without interest at the earliest date which complies with the requirements of Section 409A. The Employee shall be a “specified employee” for the twelve-month period beginning on April 1 of a year if the Employee is a “key employee” as defined in Section 416(i) of the Code (without regard to Section 416(i)(5)) as of December 31 of the preceding year or using such dates as designated by the Company in accordance with Section 409A and in a manner that is consistent with respect to all of the Company's nonqualified deferred compensation plans. For purposes of determining the identity of specified employees, the Company may establish procedures as it deems appropriate in accordance with Section 409A.

21. Income, Excise or Other Tax Liability. 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 normal employee deductions made with respect to the Company's employees generally.

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



IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date and year first above written.

CARRIAGE SERVICES, INC.

By: /s/ L. William Heiligbrodt

L. William Heiligbrodt  
Chairman, Compensation Committee

By: /s/ Mark R. Bruce

Mark R. Bruce  
Individually

SCHEDULE I

TO

EMPLOYMENT AGREEMENT

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

Service Corporation International  
Alderwoods Group, Inc.  
Stewart Enterprises, Inc.  
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

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

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

**CARRIAGE SERVICES, INC.  
3040 POST OAK BLVD., SUITE 300  
HOUSTON, TEXAS 77056**

March 14, 2012

Mark R. Bruce  
3811 Carnden Lane  
Missouri City, Texas 77459

Dear Mark:

Carriage Services, Inc. (the “**Company**”) and you previously entered into that certain Employment Agreement, dated January 4, 2011 (the “**Agreement**”), pursuant to which you serve as a Regional Managing Partner of the Company. The Company and you now enter into this agreement (this “**Amendment**”) in order to amend certain provisions of the Agreement as set forth herein. As used in this Amendment, terms that begin with an initial capital letter have the same meanings as such terms have in the Agreement unless a contrary meaning is specified in this Amendment.

For good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Company and you agree to amend the Agreement pursuant to this Amendment, effective as of the date hereof, as follows:

1. The annual Base Salary rate stated in Section 4 of the Agreement shall be modified to be not less than \$240,000.00 for the remaining term of the Agreement.

2. Section 5(a) of the Agreement shall be deleted in its entirety and shall be replaced with the following:

(a) Employee shall be eligible for an annual, discretionary incentive award (the “Incentive Award”) for each full calendar year that he is employed hereunder, as determined in the sole discretion of the Chief Executive Officer of the Company upon consideration of, among other things, regional corporate and individual performance for the year. The Incentive Award shall be payable before March 15 of the year following the calendar year to which the Incentive Award 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 Incentive Award.

3. The chart included in Section 7(g) of the Agreement shall be deleted in its entirety and replaced with the chart set forth in Exhibit A attached to this Amendment, which chart set forth in Exhibit A shall govern 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 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 of employment on the vesting of such awards.

4. A new Section 7(h) shall be added to the Agreement and shall read as follows:

(h) 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 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 7(h) 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.

5. In all other respects, the Agreement remains unchanged and in full force and effect and, in signing below, you recognize the continuing effect and enforceability of the Agreement, as amended by this Amendment.

If the foregoing correctly sets forth our understanding, please sign, date and return the original copy of this Amendment to the undersigned. After this Amendment has been executed by both parties, it shall constitute a binding Amendment to the Agreement.

Sincerely,

/s/ Melvin C. Payne

Melvin C. Payne

Chief Executive Officer

ACCEPTED AND AGREED:

/s/ Mark R. Bruce

Mark R. Bruce

**EXHIBIT A**

<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 (as defined in Section 7(c) above)	Forfeit all unvested awards	Forfeit all unvested awards	Forfeit all unvested awards
Involuntary Termination by the Company without Cause (as defined in Section 7(c) above) or by Employee for Good Reason (as defined in Section 7(e) above) other than during the 24 month period following a Corporate Change	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 (not for Good Reason)	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
Termination during the 24 month period following a Corporate Change for one of the reasons specified in Section 7(e) 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
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.

## FIRST AMENDED AND RESTATED EMPLOYMENT AGREEMENT

THIS FIRST AMENDED AND RESTATED EMPLOYMENT AGREEMENT (the "Agreement"), dated January 4, 2011 (the "Effective Date"), is entered into between CARRIAGE SERVICES, INC., a Delaware corporation (the "Company"), and Shawn R. Phillips, a resident of Lebanon, Ohio (the "Employee").

1. Employment Term. The Company hereby continues the employment of the Employee for an initial term commencing as of the Effective Date and continuing until the third anniversary of the Effective Date (the "Initial Term"). On the third anniversary of the Effective Date and on each subsequent anniversary thereafter, this Agreement shall automatically renew and extend for a period of 12 months (each such 12-month period being a "Renewal Term") unless written notice of non-renewal is delivered from either party to the other not less than sixty (60) days prior to the expiration of the then-existing Initial Term or Renewal Term, as applicable. Notwithstanding the foregoing, the Employee's employment pursuant to this Agreement may be terminated prior to the expiration of the then-existing Initial Term or Renewal Term as provided in Section 7 hereof. The Employee agrees to accept such employment and to perform the services specified herein, all upon the terms and conditions hereinafter stated.

2. Duties. The Employee shall serve the Company and shall report to, and be subject to the general direction and control, of the Chief Executive Officer of the Company or any other Executive Officer designated by him. The Employee shall faithfully, diligently, competently, and to the best of Employee's ability, perform the management and administrative duties of Regional Managing Partner and Regional Vice President of Operations of the Company. The Employee shall also serve as Regional Managing Partner and Regional Vice President of Operations of any subsidiary of the Company as requested by the Company, and the Employee shall perform such other duties as are from time to time assigned to him by the Chief Executive Officer or any other Executive Officer designated by him as are not inconsistent with the provisions hereof. The Employee represents and warrants to the Company that Employee is not subject to any obligation to any third party that would restrict or interfere with Employee's ability to perform hereunder.

3. Extent of Service. The Employee shall devote his full business time and attention to the business of the Company and, except as may be specifically permitted by the Company, shall not be engaged in any other business activity during the term of this Agreement. The foregoing shall not be construed as preventing the Employee (i) from making passive investments in other businesses or enterprises, and (ii) from engaging in other civic, charitable and business activities, provided, however, that such investments and activities will not require services on the part of the Employee which would in any way impair the performance of his duties under this Agreement.

4. Compensation. During the term of this Agreement, the Company shall pay the Employee an annual salary at a rate of not less than \$220,000 per full calendar year of service



completed (“Base Salary”), appropriately prorated for partial years at the commencement and end of the term of this Agreement. The Employee's salary and benefits will be reviewed annually, and any increase therein shall remain in the sole discretion of the Company, acting through the Compensation Committee of the Board (the “Compensation Committee”). The salary set forth herein shall not be subject to reduction and shall be payable in bi-weekly installments in accordance with the payroll policies of the Company in effect from time to time during the term of this Agreement. The Company shall have the right to deduct from payment of all compensation to the Employee hereunder (i) any federal, state or local taxes required by law to be withheld with respect to such payments, and (ii) any other amounts specifically authorized to be withheld or deducted by the Employee.

5. Benefits. In addition to the Base Salary, the Employee shall be entitled to participate in the following benefits during the term of this Agreement:

(a) Employee shall be eligible for an annual, discretionary incentive award (the “Incentive Award”) for each full calendar year that he is employed hereunder, based on achievement of specified corporate and individual performance goals established at the beginning of the year by the Compensation Committee of the Board at its first meeting of the fiscal year. The goals 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 Target level the Incentive Award will be 40% of Base Salary, (ii) at the Threshold level the Incentive Award will be 20 % of Base Salary and (iii) at the Maximum level the Incentive Award will be 80% of Base Salary. In the discretion of the Compensation Committee, awards for performance falling between Threshold, Target and Maximum goals may be ratably scaled above and below the goal levels. The Incentive Award shall be payable before March 15 of the year following the calendar year to which the Incentive Award 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 Incentive Award.

(b) Employee shall be eligible for consideration of awards of restricted stock or other incentive-based compensation under the terms of the Company's 2006 Long Term Incentive Plan or one or more of the Company's other incentive plans, as may be recommended by the Chief Executive Officer and approved by the Compensation Committee.

(c) Four weeks of paid vacation in each calendar year, subject to the Company's personnel policies respecting such matters.

(d) Participation in the Company's group health and hospitalization program, and inclusion in such other employee benefits, as are available generally to executive-level employees of the Company.

(e) Reimbursement for travel, lodging and other out-of-pocket expenses reasonably incurred by Employee in the exercise of Employee's duties under this Agreement which are approved by the Company in advance and are duly substantiated in accordance with the Company's policies as to reimbursement. In order to assure

compliance with Section 409A of the Internal Revenue Code of 1986, as amended (the "Code"), (i) such reimbursements shall be made as soon as practicable, but in no event later than the last day of the calendar year following the calendar year in which the expense was incurred, (ii) Employee is not permitted to receive a payment or other benefit in lieu of reimbursement under this Section 5(e), and (iii) the amount of expenses for which Employee is eligible to receive reimbursement during any calendar year shall not affect the amount of expenses for which Employee is eligible to receive reimbursement during any other calendar year within the term of the Agreement.

6. Certain Additional Matters. The Employee agrees that at all times during the term of this Agreement and for a period of two years following any cessation of employment with the Company:

(a) The Employee will not knowingly or intentionally do or say any act or thing which will or may impair, damage or destroy the goodwill and esteem for the Company held by its suppliers, employees, patrons, customers and others who may at any time have or have had business relations with the Company.

(b) The Employee will not knowingly or intentionally do any act or thing detrimental to the Company or its business.

Nothing herein shall be construed to prevent the Employee from complying with any requirements of law or legal process or taking such actions as the Company may consent to in writing.

7. Termination.

(a) Death. If the Employee dies during the Initial Term or any then-existing Renewal Term and while in the employ of the Company, this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate except that the Company shall pay the Employee's estate (i) that portion of the Employee's Base Salary accrued through the date on which the Employee's death occurred, (ii) a pro rata amount of the annual Incentive Award for the year in which the death occurred at the Target goal level described in Section 5(a) above, based on the number of days the Employee was employed in the year in comparison to 365, and (iii) all benefits payable under the governing provisions of any benefit plan or program of the Company (including as provided in Section 5(f) above). Such payment of Base Salary and Annual Incentive Award to the Employee's estate shall be made in the same manner and at the same times as they would have been paid to the Employee had he not died.

(b) Disability. If during the Initial Term or any then-existing Renewal Term, the Employee shall be prevented from performing his duties hereunder by reason of disability, and such disability shall continue for a period of six months, then the Company may terminate this Agreement at any time after the expiration of such six-month period. For purposes of this Agreement, the Employee shall be deemed to have become disabled when the Company, upon the advice of a qualified physician, shall have determined that the Employee is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous

period of not less than 12 months. In the event of a termination pursuant to this paragraph (b), the Company shall be relieved of all its obligations under this Agreement, except that the Company shall pay to the Employee (or his estate in the event of his subsequent death): (i) the Employee's Base Salary through the date on which such termination shall have occurred, reduced during such period by the amount of any benefits received under any disability policy maintained by the Company, as applicable; (ii) subject to the provisions of Section 20 below, a pro rata amount of the annual Incentive Award for the year in which Employee's employment was terminated at the Target goal level described in Section 5(a) above, based on the number of days the Employee was employed in the year in comparison to 365, which such pro rata Incentive Award payment shall be provided on the later of the first business day after the Release (as defined in Section 20 below) is no longer revocable or the payment date that an Incentive Award for the year of termination otherwise would have been payable pursuant to Section 5(a) 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)); and (iii) all benefits payable under the governing provisions of any benefit plan or program of the Company (including as provided in Section 5(f) above). Unless otherwise provided above, all such payments to the Employee or his estate shall be made in the same manner and at the same times as they would have been paid to the Employee had he remained employed by the Company. No such termination pursuant to this paragraph (b) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder.

(c) Discharge for Cause. The Company may discharge the Employee for Cause and terminate this Agreement prior to the end of the Initial Term or any then-existing Renewal Term. In such case, this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate other than to pay to the Employee (or his estate in the event of his subsequent death) that portion of the Employee's salary accrued through the date of termination.

For purposes of this Agreement, the Company shall have "Cause" to discharge the Employee or terminate the Employee's employment hereunder upon (i) the Employee's conviction of any felony or any other crime involving moral turpitude, (ii) the 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 Chief Executive Officer of the Company, (iii) the Employee's commission of acts amounting to gross negligence or willful misconduct to the material detriment of the Company, or (iv) the Employee's material breach of any provision of this Agreement or uniformly applied provisions 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 Chief Executive Officer of the Company.

Any such termination by virtue of this paragraph (c) shall not prejudice any remedy that the Company may have at law, in equity, or under this Agreement, for breach hereof by Employee. No such termination pursuant to this paragraph (c) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder.

(d) Discharge Without Cause. Prior to the end of the Initial Term or any then-existing Renewal Term, the Company may discharge the Employee without Cause (as defined in paragraph (c) above) and terminate this Agreement. In such case this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate, except that, subject to the provisions of Section 20 below, the Company shall continue to pay to the Employee (or his estate in the event of his subsequent death): (i) the Employee's monthly Base Salary, in arrears, for a period of 18 months following the date of discharge; *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, that would have otherwise been made pursuant to this Section 7(d)(i) between the date of Employee's termination of employment and the First Payment Date; (ii) a pro rata amount of the annual Incentive Award at the Target goal level described in Section 5(a) above, based on the number of days the Employee was employed in the year in comparison to 365, for the year of termination, which such pro rata Incentive Award payment shall be provided on the later of the first business day after the Release is no longer revocable or the payment date that an Incentive Award for the year of termination otherwise would have been payable pursuant to Section 5(a) 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)); and (iii) if following the date of such discharge, the Employee becomes eligible to elect continuation coverage under the Consolidated Omnibus Budget Reconciliation Act ("COBRA") and properly elects such coverage, the Company shall reimburse the Employee or pay on the Employee's behalf 100% of applicable medical continuation premiums for the benefit of the Employee (and his covered dependents as of the date of his termination, if any) under the Employee's then-current plan election, with such coverage to be provided under the closest comparable plan as offered by the Company from time to time, for so long during the 18-month period following termination as he remains eligible for and elects COBRA coverage; provided that such reimbursement shall not be applicable until the Release becomes irrevocable and the first such reimbursement payment shall include, if applicable, all reimbursement payments that would have otherwise been made pursuant to this Section 7(d)(iii) between the date of Employee's termination of employment and the date that the Release became irrevocable. The Company will also provide all salary earned by Employee through the date of termination and any applicable benefits payable under the governing provisions of any benefit plan or program of the Company. No such termination pursuant to this paragraph (d) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder. Notwithstanding anything to the contrary in this Section 7(d) or Section 20, 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 7(d)(i) will not commence and the First Payment Date shall not occur until the second taxable year, irrespective of when the Release actually becomes irrevocable.

(e) Corporate Change. If following a Corporate Change (as defined in the Company's 2006 Long-Term Incentive Plan), the Employee terminates his employment for Good Reason (as defined below) or the Employee is discharged without Cause, in either case within 24 months following the Corporate Change, then this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate, except that, subject to the provisions of Section 20 below, the Company shall pay to the Employee (or his estate in the event of his subsequent death): (i) a lump sum payment payable following such termination equal to one and one-half times the Employee's Base Salary, which such payment shall be made within ten (10) business days after the Release is no longer revocable; (ii) 100% of the annual Incentive Award at the Target goal level described in Section 5(a) above for the year of termination, which such Incentive Award payment shall be provided on the later of the first business day after the Release is no longer revocable or the payment date that an Incentive Award for the year of termination otherwise would have been payable pursuant to Section 5(a) 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)); and (iii) if following the date of such discharge, the Employee becomes eligible to elect continuation coverage under COBRA and properly elects such coverage, the Company shall reimburse the Employee or pay on the Employee's behalf 100% of applicable medical continuation premiums for the benefit of the Employee (and his covered dependents as of the date of his termination, if any) under the Employee's then-current plan election, with such coverage to be provided under the closest comparable plan as offered by the Company from time to time, for so long during the 36-month period following termination as he remains eligible for and elects COBRA coverage; provided that such reimbursement shall not be applicable until the Release becomes irrevocable and the first such reimbursement payment shall include, if applicable, all reimbursement payments that would have otherwise been made pursuant to this Section 7(e)(iii) between the date of Employee's termination of employment and the date that the Release became irrevocable. The Company will also provide all salary earned by Employee through the date of termination and any applicable. The Company will also provide any applicable benefits payable under the governing provisions of any benefit plan or program of the Company. No such termination pursuant to this paragraph (e) will relieve the Employee of his obligations under Sections 6 and 9 hereunder.

"Good Reason" means any of the following actions if taken without the Employee's prior written consent: (A) any material breach by the Company to comply with its obligations under the terms of the Agreement; (B) any material diminution in the Employee's responsibilities, authority or duties, (C) a material diminution in the Employee's Base Salary; or (D) any change greater than 50 miles in the permanent location at which the Employee performs services for the Company. The Employee shall give written notice to the Board specifying such actions within 90 days of the initial existence of such action and providing a period of 30 days in which the Company shall be allowed to cure such circumstances. Provided that the condition purporting to give rise to the Good Reason event is not cured within the 30-day cure period, Employee must exercise his right to terminate this Agreement for Good Reason within 120 days after the initial existence of the Good Reason event.

(f) Notice. Prior to the end of the term of this Agreement, the Employee may terminate this Agreement upon ninety (90) days written notice. This Agreement shall automatically terminate at the end of the notice period, and the Company shall have no further obligation to the Employee other than to pay to the Employee that portion of the Employee's salary accrued through the date of termination. No such termination pursuant to this paragraph (f) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder

(g) Equity Award Termination Provision. The impact of 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 Employee's termination from employment on: (i) the vesting of Employee's stock option, restricted stock and other share-based awards; or (ii) Employee's repurchase rights and obligations following such termination of employment, 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 for Cause (as defined in Section 7(c) above)	Forfeit all unvested awards	Forfeit all unvested awards	Forfeit all unvested awards
Involuntary Termination without Cause (as defined in Section 7(c) above) or for Good Reason (as defined in Section 7(e) above)	Forfeit all unvested awards; Employee has 12 months from the date of termination to exercise all vested awards	Forfeit all unvested awards	Forfeit all unvested awards
Voluntary Termination	Forfeit all unvested awards; Employee has 90 days from the date of termination to exercise all vested awards	Forfeit all unvested awards	Forfeit all unvested awards
Death	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

Disability	Forfeit 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 90 days 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

8. Restrictive Covenants. The Company has provided and shall provide in the future to the Employee, confidential and proprietary information as that term is defined in Section 9 of this Agreement (“Confidential Information”). The 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 shall be given possession of and access to Confidential Information of the Company and its Affiliates (as defined on Schedule I hereto), and will develop through such employment business systems, methods of doing business, and contacts within the death care industry, all of which will help to identify him 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 the Employee in the future, the sufficiency of which is hereby acknowledged by the Employee, the Employee agrees to enter into the covenants contained in this Agreement. 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 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, if the Employee had management

responsibilities either directly or indirectly, over that funeral home, cemetery, or other death care business at any time during the previous 12 months;

(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, if the Employee had management responsibilities either directly or indirectly, over that funeral home, cemetery, or other death care business at any time during the previous 12 months.

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.

9. Confidential Information; Copyrightable Material. The Employee acknowledges that in the course of his employment by the Company he shall receive and access certain trade secrets, management methods, financial and accounting data (including, but not limited to, reports, studies, analyses, spreadsheets and other materials and information), operating techniques, prospective acquisitions, employee lists, training manuals and procedures, personnel evaluation procedures, and other confidential information and knowledge concerning the business of the Company and its Affiliates (hereinafter collectively referred to as "Confidential Information") which the Company desires to protect. The Employee understands that the Confidential Information is confidential and he agrees not to reveal the Confidential Information to anyone outside the Company so long as the confidential or secret nature of the Confidential Information shall continue, except as required by law or legal process. The Employee further agrees that he will at no time use the Confidential Information in competing with the Company. Upon termination of this Agreement, the Employee shall surrender to the Company all papers, documents, writings and other property produced by him or coming into his possession by or through his employment or relating to the Confidential Information and the Employee agrees that all such materials will at all times remain the property of the Company. The Employee acknowledges that all materials and other copyrightable works and subject matter (regardless of whether or not constituting "Confidential Information") produced by the Employee within the scope of his employment (regardless of whether or not denoted as copyrighted material) shall be deemed "works made for hire" and shall be owned by and proprietary to the Company and may not be used or reproduced in whole or in part without the Company's prior written consent.



10. Remedies. The parties recognize that the services to be rendered under this Agreement by the Employee are special, unique, and of extraordinary character, and that in the event of the breach by the Employee of the covenants contained in Section 8 or Section 9 hereof, the Company may suffer irreparable harm as a result. The parties therefore agree that, in the event of any breach or threatened breach of any of such covenants, the Company shall be entitled to specific performance or injunctive relief, or both, and may, in addition to and not in lieu of any claim or proceeding for damages, institute and prosecute proceedings in any court of competent jurisdiction to enforce through injunctive relief such covenants. In addition, the Company may, if it so elects, suspend (if applicable) any payments due under this Agreement pending any such breach and offset against any future payments the amount of the Company's damages arising from any such breach. The Employee agrees to waive and hereby waives any requirement for the Company to secure any bond in connection with the obtaining of such injunction or other equitable relief.

11. Notices. All notices, requests, consents and other communications under this Agreement shall be in writing and shall be deemed to have been delivered on the date personally delivered or three business days after the date mailed, postage prepaid, by certified mail, return receipt requested, or when sent by electronic means or facsimile and receipt is confirmed, if addressed to the respective parties as follows:

If to the Employee:     Shawn R. Phillips  
                              629 Red Deer Road  
                              Lebanon, Ohio 45036

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

Either party hereto may designate a different address by providing written notice of such new address to the other party hereto.

12. Severability. Whenever possible, each provision of this Agreement shall be interpreted in such manner as to be effective and valid under applicable law but if any provision of this Agreement shall be prohibited by or invalid under applicable law, such provision shall be ineffective to the extent of such provision or invalidity, without invalidating the remainder of such provision or the remaining provisions of this Agreement.

13. Assignment. This Agreement may not be assigned by the Employee. Neither the Employee nor his estate shall have any right to commute, encumber or dispose of any right to receive payments hereunder, it being agreed that such payments and the right thereto are nonassignable and nontransferable.

14. Binding Effect. Subject to the provisions of Section 13 of this Agreement, this Agreement shall be binding upon and inure to the benefit of the parties hereto, the Employee's heirs and personal representatives, and the successors and as-signs of the Company.

15. Captions. The section and paragraph headings in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement.

16. Complete Agreement. This Agreement represents the entire agreement between the parties concerning the subject hereof and supersedes all prior agreements and arrangements between the parties concerning the subject thereof including without limitation that Employment Agreement between the parties dated September 24, 2007.

17. Governing Law; Venue. A substantial portion of the Employee's duties under this Agreement shall be performed at the Company's corporate headquarters in Houston, Texas, and this Agreement has been substantially negotiated and is being executed and delivered in the State of Texas. This Agreement shall be construed and enforced in accordance with and governed by the laws of the State of Texas. Any suit, claim or proceeding arising under or in connection with this Agreement or the employment relationship evidenced hereby must be brought, if at all, in a state district court in Harris County, Texas or federal district court in the Southern District of Texas, Houston Division. Each party submits to the jurisdiction of such courts and agrees not to raise any objection to such jurisdiction.

18. Survival. The provisions of Sections 6, 8 and 9 shall survive any termination of this Agreement or the employment relationship of the Company and Employee; provided, however, if such termination is the result of Corporate Change as provided in Section 7(e) hereof, Employee shall not thereafter be bound by the provisions of Section 8 hereof.

19. Counterparts. This Agreement may be executed in multiple original counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

20. Severance Payments Conditioned on Release; Time of Payments. The amounts payable to Employee under Sections 7(b)(ii), 7(d)(i)-(iii) and 7(e)(i)-(iii) shall not become payable unless Employee executes (and does not revoke within seven days of its execution) a release of claims in a form satisfactory to the Company (the "Release") within the time period prescribed by the Company, which such time period shall be no later than fifty (50) days from the date of Employee's termination of employment. Notwithstanding anything contained in this Agreement to the contrary, to the maximum extent permitted by applicable law, amounts payable to Employee pursuant to Section 7 are intended to be made in reliance upon Treas. Reg. § 1.409A-1(b)(9) (separation pay plans) or Treas. Reg. § 1.409A-1(b)(4) (short-term deferrals). No amounts payable under Section 7 of this Agreement upon Employee's termination of employment shall be payable unless Employee's termination of employment constitutes a "separation from service" within the meaning of Treas. Reg. § 1.409A-1(h). The Company and Employee intend that their exercise of authority or discretion under this Agreement shall comply with Section 409A of the Code. If any provision of this Agreement does not satisfy the requirements of Section 409A, 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. Notwithstanding the foregoing, no particular tax result for Employee with respect to any income recognized by Employee in connection with this Agreement is guaranteed. Neither the Company nor any of its affiliates shall have any obligation to indemnify or otherwise hold

Employee harmless from any or all such taxes, interest, penalties, or liability for any damages related thereto. Each payment under this Agreement is intended to be a “separate payment” and not a series of payments for purposes of Section 409A. References in this Agreement to Section 409A of the Code includes rules, regulations and guidance of general applicability issued by the Department of the Treasury under Code Section 409A. If the Employee is a “specified employee,” as such term is defined in Section 409A of the Code and related regulations and Treasury pronouncements (“Section 409A”) and determined as described below in this Section 20, any payments payable as a result of the Employee's termination (other than death) that are required to be delayed in accordance with Section 409A of the Code as a result of Employee's status as a “specified employee” shall not be payable before the earliest of (i) the date that is six months after the Employee's termination, (ii) the date of the Employee's death, or (iii) the date that otherwise complies with the requirements of Section 409A. This Section 20 shall be applied by accumulating all payments that otherwise would have been paid within six months of the Employee's termination and paying such accumulated amounts without interest at the earliest date which complies with the requirements of Section 409A. The Employee shall be a “specified employee” for the twelve-month period beginning on April 1 of a year if the Employee is a “key employee” as defined in Section 416(i) of the Code (without regard to Section 416(i)(5)) as of December 31 of the preceding year or using such dates as designated by the Company in accordance with Section 409A and in a manner that is consistent with respect to all of the Company's nonqualified deferred compensation plans. For purposes of determining the identity of specified employees, the Company may establish procedures as it deems appropriate in accordance with Section 409A.

21. Income, Excise or Other Tax Liability. 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 normal employee deductions made with respect to the Company's employees generally.

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

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date and year first above written.

CARRIAGE SERVICES, INC.

By: /s/ L. William Heiligbrodt

L. William Heiligbrodt  
Chairman, Compensation Committee

By: /s/ Shawn R. Phillips

Shawn R. Phillips  
Individually

SCHEDULE I

TO

EMPLOYMENT AGREEMENT

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

Service Corporation International  
Alderwoods Group, Inc.  
Stewart Enterprises, Inc.  
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

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

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

**CARRIAGE SERVICES, INC.**  
**3040 POST OAK BLVD., SUITE 300**  
**HOUSTON, TEXAS 77056**

March 14, 2012

Shawn R. Phillips  
629 Red Deer Road  
Lebanon, Ohio 45036

Dear Shawn:

Carriage Services, Inc. (the “**Company**”) and you previously entered into that certain First Amended and Restated Employment Agreement, dated January 4, 2011 (the “**Agreement**”), pursuant to which you serve as a Regional Managing Partner of the Company. The Company and you now enter into this agreement (this “**Amendment**”) in order to amend certain provisions of the Agreement as set forth herein. As used in this Amendment, terms that begin with an initial capital letter have the same meanings as such terms have in the Agreement unless a contrary meaning is specified in this Amendment.

For good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Company and you agree to amend the Agreement pursuant to this Amendment, effective as of the date hereof, as follows:

1. The annual Base Salary rate stated in Section 4 of the Agreement shall be modified to be not less than \$230,000.00 for the remaining term of the Agreement.
2. Section 5(a) of the Agreement shall be deleted in its entirety and shall be replaced with the following:
  - (a) Employee shall be eligible for an annual, discretionary incentive award (the “Incentive Award”) for each full calendar year that he is employed hereunder, as determined in the sole discretion of the Chief Executive Officer of the Company upon consideration of, among other things, regional corporate and individual performance for the year. The Incentive Award shall be payable before March 15 of the year following the calendar year to which the Incentive Award 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 Incentive Award.
3. The chart included in Section 7(g) of the Agreement shall be deleted in its entirety and replaced with the chart set forth in Exhibit A attached to this Amendment, which chart set forth in Exhibit A shall govern 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 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 of employment on the vesting of such awards.

4. A new Section 7(h) shall be added to the Agreement and shall read as follows:

(h) 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 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 7(h) 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.

5. In all other respects, the Agreement remains unchanged and in full force and effect and, in signing below, you recognize the continuing effect and enforceability of the Agreement, as amended by this Amendment.

If the foregoing correctly sets forth our understanding, please sign, date and return the original copy of this Amendment to the undersigned. After this Amendment has been executed by both parties, it shall constitute a binding Amendment to the Agreement.

Sincerely,

/s/ Melvin C. Payne

Melvin C. Payne

Chief Executive Officer

ACCEPTED AND AGREED:

/s/ Shawn R. Phillips

Shawn R. Phillips



**EXHIBIT A**

<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 (as defined in Section 7(c) above)	Forfeit all unvested awards	Forfeit all unvested awards	Forfeit all unvested awards
Involuntary Termination by the Company without Cause (as defined in Section 7(c) above) or by Employee for Good Reason (as defined in Section 7(e) above) other than during the 24 month period following a Corporate Change	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 (not for Good Reason)	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
Termination during the 24 month period following a Corporate Change for one of the reasons specified in Section 7(e) 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
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.

## EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (the "Agreement"), dated August 31, 2012 at 5:01 p.m. (the "Effective Date"), is entered into between CARRIAGE SERVICES, INC., a Delaware corporation (the "Company"), and Paul D. Elliott, a resident of Harris County, Texas (the "Employee").

1. Employment Term. The Company hereby employs the Employee for an initial term commencing as of the Effective Date and continuing until the third anniversary of the Effective Date (the "Initial Term"). On the third anniversary of the Effective Date and on each subsequent anniversary thereafter, this Agreement shall automatically renew and extend for a period of 12 months (each such 12-month period being a "Renewal Term") unless written notice of non-renewal is delivered from either party to the other not less than sixty (60) days prior to the expiration of the then-existing Initial Term or Renewal Term, as applicable. Notwithstanding the foregoing, the Employee's employment pursuant to this Agreement may be terminated prior to the expiration of the then-existing Initial Term or Renewal Term as provided in Section 7 hereof. The Employee agrees to accept such employment and to perform the services specified herein, all upon the terms and conditions hereinafter stated.

2. Duties. The Employee shall serve the Company and shall report to, and be subject to the general direction and control, of the Chief Executive Officer of the Company or any other Executive Officer designated by him. The Employee shall faithfully, diligently, competently, and to the best of Employee's ability, perform the management and administrative duties of Regional Managing Partner and Regional Vice President of Operations of the Company. The Employee shall also serve as Regional Managing Partner and Regional Vice President of Operations of any subsidiary of the Company as requested by the Company, and the Employee shall perform such other duties as are from time to time assigned to him by the Chief Executive Officer or any other Executive Officer designated by him as are not inconsistent with the provisions hereof. The Employee represents and warrants to the Company that Employee is not subject to any obligation to any third party that would restrict or interfere with Employee's ability to perform hereunder.

3. Extent of Service. The Employee shall devote his full business time and attention to the business of the Company and, except as may be specifically permitted by the Company, shall not be engaged in any other business activity during the term of this Agreement. The foregoing shall not be construed as preventing the Employee (i) from making passive investments in other businesses or enterprises, and (ii) from engaging in other civic, charitable and business activities, provided, however, that such investments and activities will not require services on the part of the Employee which would in any way impair the performance of his duties under this Agreement.

4. Compensation. During the term of this Agreement, the Company shall pay the Employee an annual salary at a rate of not less than \$240,000 per full calendar year of service completed ("Base Salary"), appropriately prorated for partial years at the commencement and end of the term of this Agreement. The Employee's salary and benefits will be reviewed annually, and any increase therein shall remain in the sole discretion of the Company, acting through the Compensation Committee of the Board (the "Compensation Committee"). The salary set forth

herein shall not be subject to reduction and shall be payable in bi-weekly installments in accordance with the payroll policies of the Company in effect from time to time during the term of this Agreement. The Company shall have the right to deduct from payment of all compensation to the Employee hereunder (i) any federal, state or local taxes required by law to be withheld with respect to such payments, and (ii) any other amounts specifically authorized to be withheld or deducted by the Employee.

5. Benefits. In addition to the Base Salary, the Employee shall be entitled to participate in the following benefits during the term of this Agreement:

(a) Employee shall be eligible for an annual, discretionary incentive award (the "Incentive Award") for each full calendar year that he is employed hereunder, as determined in the sole discretion of the Chief Executive Officer of the Company upon consideration of, among other things, regional, corporate, and individual performance for the year. The Incentive Award shall be payable before March 15 of the year following the calendar year to which the Incentive Award 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 Incentive Award.

(b) Employee shall be eligible for consideration of awards of restricted stock or other incentive-based compensation under the terms of the Company's Second Amended & Restated 2006 Long-Term Incentive Plan or one or more of the Company's other incentive plans, as may be recommended by the Chief Executive Officer and approved by the Compensation Committee.

(c) Four weeks of paid vacation in each calendar year, subject to the Company's personnel policies respecting such matters.

(d) Participation in the Company's group health and hospitalization program, and inclusion in such other employee benefits, as are available generally to executive-level employees of the Company.

(e) Reimbursement for travel, lodging and other out-of-pocket expenses reasonably incurred by Employee in the exercise of Employee's duties under this Agreement which are approved by the Company in advance and are duly substantiated in accordance with the Company's policies as to reimbursement. In order to assure compliance with Section 409A of the Internal Revenue Code of 1986, as amended (the "Code"), (i) such reimbursements shall be made as soon as practicable, but in no event later than the last day of the calendar year following the calendar year in which the expense was incurred, (ii) Employee is not permitted to receive a payment or other benefit in lieu of reimbursement under this Section 5(e), and (iii) the amount of expenses for which Employee is eligible to receive reimbursement during any calendar year shall not affect the amount of expenses for which Employee is eligible to receive reimbursement during any other calendar year within the term of the Agreement.

6. Certain Additional Matters. The Employee agrees that at all times during the term of this Agreement and for a period of two years following any cessation of employment with the Company:

(a) The Employee will not knowingly or intentionally do or say any act or thing which will or may impair, damage or destroy the goodwill and esteem for the Company held by its suppliers, employees, patrons, customers and others who may at any time have or have had business relations with the Company.

(b) The Employee will not knowingly or intentionally do any act or thing detrimental to the Company or its business.

Nothing herein shall be construed to prevent the Employee from complying with any requirements of law or legal process or taking such actions as the Company may consent to in writing.

7. Termination.

(a) Death. If the Employee dies during the Initial Term or any then-existing Renewal Term and while in the employ of the Company, this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate except that the Company shall pay the Employee's estate (i) that portion of the Employee's Base Salary accrued through the date on which the Employee's death occurred; (ii) a pro rata amount of the annual Incentive Award described in Section 5(a) above for the year in which the death occurred, if any, based on the number of days the Employee was employed in the year in comparison to 365; and (iii) all benefits payable under the governing provisions of any benefit plan or program of the Company (including as provided in Section 5(d) above). Such payment of Base Salary and annual Incentive Award to the Employee's estate shall be made in the same manner and at the same times as they would have been paid to the Employee had he not died.

(b) Disability. If during the Initial Term or any then-existing Renewal Term, the Employee shall be prevented from performing his duties hereunder by reason of disability, and such disability shall continue for a period of six months, then the Company may terminate this Agreement at any time after the expiration of such six-month period. For purposes of this Agreement, the Employee shall be deemed to have become disabled when the Company, upon the advice of a qualified physician, shall have determined that the Employee is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous period of not less than 12 months. In the event of a termination pursuant to this paragraph (b), the Company shall be relieved of all its obligations under this Agreement, except that the Company shall pay to the Employee (or his estate in the event of his subsequent death): (i) the Employee's Base Salary through the date on which such termination shall have occurred, reduced during such period by the amount of any benefits received under any disability policy maintained by the Company, as applicable; (ii) subject to the provisions of Section 20 below, a pro rata amount of the annual Incentive Award described

in Section 5(a) above for the year in which the termination occurred, if any, based on the number of days the Employee was employed in the year in comparison to 365, which such pro rata Incentive Award payment shall be provided on the later of the first business day after the Release (as defined in Section 20 below) is no longer revocable or the payment date that an Incentive Award for the year of termination otherwise would have been payable pursuant to Section 5(a) 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)); and (iii) all benefits payable under the governing provisions of any benefit plan or program of the Company (including as provided in Section 5(d) above). Unless otherwise provided above, all such payments to the Employee or his estate shall be made in the same manner and at the same times as they would have been paid to the Employee had he remained employed by the Company. No such termination pursuant to this paragraph (b) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder.

(c) Discharge for Cause. The Company may discharge the Employee for Cause and terminate this Agreement prior to the end of the Initial Term or any then-existing Renewal Term. In such case, this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate other than to pay to the Employee (or his estate in the event of his subsequent death) that portion of the Employee's Base Salary accrued through the date of termination.

For purposes of this Agreement, the Company shall have "Cause" to discharge the Employee or terminate the Employee's employment hereunder upon (i) the Employee's conviction of any felony or any other crime involving moral turpitude, (ii) the 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 Chief Executive Officer of the Company, (iii) the Employee's commission of acts amounting to gross negligence or willful misconduct to the material detriment of the Company, or (iv) the Employee's material breach of any provision of this Agreement or uniformly applied provisions 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 Chief Executive Officer of the Company.

Any such termination by virtue of this paragraph (c) shall not prejudice any remedy that the Company may have at law, in equity, or under this Agreement, for breach hereof by Employee. No such termination pursuant to this paragraph (c) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder.

(d) Discharge Without Cause. Prior to the end of the Initial Term or any then-existing Renewal Term, the Company may discharge the Employee without Cause (as defined in paragraph (c) above) and terminate this Agreement. In such case this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate, except that, subject to the provisions of Section 20 below, the Company shall continue to pay to the Employee (or his estate in the event of his subsequent death): (i) the Employee's monthly Base Salary, in arrears, for

a period of 18 months following the date of discharge; *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, that would have otherwise been made pursuant to this Section 7(d)(i) between the date of Employee's termination of employment and the First Payment Date; (ii) a pro rata amount of the annual Incentive Award described in Section 5(a) above for the year in which the discharge occurred, if any, based on the number of days the Employee was employed in the year in comparison to 365, which such pro rata Incentive Award payment shall be provided on the later of the first business day after the Release is no longer revocable or the payment date that an Incentive Award for the year of termination otherwise would have been payable pursuant to Section 5(a) 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)); and (iii) if, following the date of such discharge, the Employee becomes eligible to elect continuation coverage under the Consolidated Omnibus Budget Reconciliation Act ("COBRA") and properly elects such coverage, the Company shall reimburse the Employee or pay on the Employee's behalf 100% of applicable medical continuation premiums for the benefit of the Employee (and his covered dependents as of the date of his termination, if any) under the Employee's then-current plan election, with such coverage to be provided under the closest comparable plan as offered by the Company from time to time, for so long during the 18-month period following termination as he remains eligible for and elects COBRA coverage; provided that such reimbursement shall not be applicable until the Release becomes irrevocable and the first such reimbursement payment shall include, if applicable, all reimbursement payments that would have otherwise been made pursuant to this Section 7(d)(iii) between the date of Employee's termination of employment and the date that the Release became irrevocable. The Company will also provide all salary earned by Employee through the date of termination and any applicable benefits payable under the governing provisions of any benefit plan or program of the Company. No such termination pursuant to this paragraph (d) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder. Notwithstanding anything to the contrary in this Section 7(d) or Section 20, 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 7(d)(i) will not commence and the First Payment Date shall not occur until the second taxable year, irrespective of when the Release actually becomes irrevocable.

(e) Corporate Change. If following a Corporate Change (as defined in the Company's 2006 Long-Term Incentive Plan), the Employee terminates his employment for Good Reason (as defined below) or the Employee is discharged without Cause, in either case within 24 months following the Corporate Change, then this Agreement shall automatically terminate and the Company shall have no further obligation to the Employee or his estate, except that, subject to the provisions of Section 20 below, the Company shall pay to the Employee (or his estate in the event of his subsequent death): (i) a lump sum payment payable following such termination equal to one and a half times the Employee's Base Salary, which such payment shall be made within ten (10) business days after the Release is no longer revocable; (ii) 100% of the annual Incentive Award described in Section 5(a) above for the year of termination, if any, which such Incentive Award payment shall be provided on the later of the first business day after the Release is no longer revocable or the payment date that an Incentive Award for the year of termination otherwise would have been payable pursuant to Section 5(a) 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)); and (iii) if, following the date of such discharge, the Employee becomes eligible to elect continuation coverage under COBRA and properly elects such coverage, the Company shall reimburse the Employee or pay on the Employee's behalf 100% of applicable medical continuation premiums for the benefit of the Employee (and his covered dependents as of the date of his termination, if any) under the Employee's then-current plan election, with such coverage to be provided under the closest comparable plan as offered by the Company from time to time, for so long during the 36-month period following termination as he remains eligible for and elects COBRA coverage; provided that such reimbursement shall not be applicable until the Release becomes irrevocable and the first such reimbursement payment shall include, if applicable, all reimbursement payments that would have otherwise been made pursuant to this Section 7(e)(iii) between the date of Employee's termination of employment and the date that the Release became irrevocable. The Company will also provide all salary earned by Employee through the date of termination and any applicable benefits payable under the governing provisions of any benefit plan or program of the Company. No such termination pursuant to this paragraph (e) will relieve the Employee of his obligations under Sections 6 and 9 hereunder.

“Good Reason” means any of the following actions if taken without the Employee's prior written consent: (A) any material breach by the Company to comply with its obligations under the terms of the Agreement; (B) any material diminution in the Employee's responsibilities, authority or duties, (C) a material diminution in the Employee's Base Salary; or (D) any change greater than 50 miles in the permanent location at which the Employee performs services for the Company. The Employee shall give written notice to the Board specifying such actions within 90 days of the initial existence of such action and providing a period of 30 days in which the Company shall be allowed to cure such circumstances. Provided that the condition purporting to give rise to the Good Reason event is not cured within the 30-day cure period, Employee must exercise his right to terminate this Agreement for Good Reason within 120 days after the initial existence of the Good Reason event.

(f) Notice. Prior to the end of the term of this Agreement, the Employee may terminate this Agreement upon ninety (90) days written notice. This Agreement shall automatically terminate at the end of the notice period, and the Company shall have no further obligation to the Employee other than to pay to the Employee that portion of the Employee's Base Salary accrued through the date of termination. No such termination pursuant to this paragraph (f) will relieve the Employee of his obligations under Sections 6, 8 and 9 hereunder



(g) Equity Award Termination Provision. The impact of a Corporate Change (as defined in Section 7(e) above) 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: (i) the vesting of Employee's stock option, restricted stock and other share-based awards; or (ii) Employee's repurchase rights and obligations following such termination of employment, 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 (as defined in Section 7(c) above)	Forfeit all unvested awards	Forfeit all unvested awards	Forfeit all unvested awards
Involuntary Termination by the Company without Cause (as defined in Section 7(c) above) or by Employee for Good Reason (as defined in Section 7(e) above) other than during the 24 month period following a Corporate Change	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 (not for Good Reason)	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
Termination during the 24 month period following a Corporate Change for one of the reasons specified in Section 7(e) 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
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.

(h) 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 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 7(h) 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.

8. Restrictive Covenants. The Company has provided and shall provide in the future to the Employee, confidential and proprietary information as that term is defined in Section 9 of this Agreement (“Confidential Information”). The 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 shall be given possession of and access to Confidential Information of the Company and its Affiliates (as defined on Schedule I hereto), and will develop through such employment business systems, methods of doing business, and contacts within the death care industry, all of which will help to identify him 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 the Employee in the future, the sufficiency of which is hereby acknowledged by the Employee, the Employee agrees to enter into the covenants contained in this Agreement. 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 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, if the Employee had management responsibilities either directly or indirectly, over that funeral home, cemetery, or other death care business at any time during the previous 12 months;

(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, if the Employee had management responsibilities either directly or indirectly, over that funeral home, cemetery, or other death care business at any time during the previous 12 months.

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.

9. Confidential Information; Copyrightable Material. The Employee acknowledges that in the course of his employment by the Company he shall receive and access certain trade secrets, management methods, financial and accounting data (including, but not limited to, reports, studies, analyses, spreadsheets and other materials and information), operating techniques, prospective acquisitions, employee lists, training manuals and procedures, personnel evaluation procedures, and other confidential information and knowledge concerning the business of the Company and its Affiliates (hereinafter collectively referred to as "Confidential Information") which the Company desires to protect. The Employee understands that the Confidential Information is confidential and he agrees not to reveal the Confidential Information to anyone outside the Company so long as the confidential or secret nature of the Confidential Information shall continue, except as required by law or legal process. The Employee further agrees that he will at no time use the Confidential Information in competing with the Company. Upon termination of this Agreement, the Employee shall surrender to the Company all papers, documents, writings and other property produced by him or coming into his possession by or through his employment or relating to the Confidential Information and the Employee agrees that all such materials will at all times remain the property of the Company. The Employee acknowledges that all materials and other copyrightable works and subject matter (regardless of whether or not constituting "Confidential Information") produced by the Employee within the scope of his employment (regardless of whether or not denoted as copyrighted material) shall be deemed "works made for hire" and shall be owned by and proprietary to the Company and may not be used or reproduced in whole or in part without the Company's prior written consent.

10. Remedies. The parties recognize that the services to be rendered under this Agreement by the Employee are special, unique, and of extraordinary character, and that in the event of the breach by the Employee of the covenants contained in Section 8 or Section 9 hereof, the Company may suffer irreparable harm as a result. The parties therefore agree that, in the event of any breach or threatened breach of any of such covenants, the Company shall be entitled to specific performance or injunctive relief, or both, and may, in addition to and not in lieu of any claim or proceeding for damages, institute and prosecute proceedings in any court of competent jurisdiction to enforce through injunctive relief such covenants. In addition, the Company may, if it so elects, suspend (if applicable) any payments due under this Agreement pending any such breach and offset against any future payments the amount of the Company's damages arising from any

such breach. The Employee agrees to waive and hereby waives any requirement for the Company to secure any bond in connection with the obtaining of such injunction or other equitable relief.

11. Notices. All notices, requests, consents and other communications under this Agreement shall be in writing and shall be deemed to have been delivered on the date personally delivered or three business days after the date mailed, postage prepaid, by certified mail, return receipt requested, or when sent by electronic means or facsimile and receipt is confirmed, if addressed to the respective parties as follows:

If to the Employee: Paul Elliott  
5219 Laurelwood  
Kingwood, Texas 77345

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

Either party hereto may designate a different address by providing written notice of such new address to the other party hereto.

12. Severability. Whenever possible, each provision of this Agreement shall be interpreted in such manner as to be effective and valid under applicable law but if any provision of this Agreement shall be prohibited by or invalid under applicable law, such provision shall be ineffective to the extent of such provision or invalidity, without invalidating the remainder of such provision or the remaining provisions of this Agreement.

13. Assignment. This Agreement may not be assigned by the Employee. Neither the Employee nor his estate shall have any right to commute, encumber or dispose of any right to receive payments hereunder, it being agreed that such payments and the right thereto are nonassignable and nontransferable.

14. Binding Effect. Subject to the provisions of Section 13 of this Agreement, this Agreement shall be binding upon and inure to the benefit of the parties hereto, the Employee's heirs and personal representatives, and the successors and assigns of the Company.

15. Captions. The section and paragraph headings in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement.

16. Complete Agreement. This Agreement represents the entire agreement between the parties concerning the subject hereof and supersedes all prior agreements and arrangements between the parties concerning the subject thereof.

17. Governing Law; Venue. A substantial portion of the Employee's duties under this Agreement shall be performed at the Company's corporate headquarters in Houston, Texas, and this Agreement has been substantially negotiated and is being executed and delivered in the State of

Texas. This Agreement shall be construed and enforced in accordance with and governed by the laws of the State of Texas. Any suit, claim or proceeding arising under or in connection with this Agreement or the employment relationship evidenced hereby must be brought, if at all, in a state district court in Harris County, Texas or federal district court in the Southern District of Texas, Houston Division. Each party submits to the jurisdiction of such courts and agrees not to raise any objection to such jurisdiction.

18. Survival. The provisions of Sections 6, 8 and 9 shall survive any termination of this Agreement or the employment relationship of the Company and Employee; provided, however, if such termination is the result of Corporate Change as provided in Section 7(e) hereof, Employee shall not thereafter be bound by the provisions of Section 8 hereof.

19. Counterparts. This Agreement may be executed in multiple original counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

20. Severance Payments Conditioned on Release; Time of Payments. The amounts payable to Employee under Sections 7(b)(ii), 7(d)(i)-(iii) and 7(e)(i)-(iii) shall not become payable unless Employee executes (and does not revoke within seven days of its execution) a release of claims in a form satisfactory to the Company (the "Release") within the time period prescribed by the Company, which such time period shall be no later than fifty (50) days from the date of Employee's termination of employment. Notwithstanding anything contained in this Agreement to the contrary, to the maximum extent permitted by applicable law, amounts payable to Employee pursuant to Section 7 are intended to be made in reliance upon Treas. Reg. § 1.409A-1(b)(9) (separation pay plans) or Treas. Reg. § 1.409A-1(b)(4) (short-term deferrals). No amounts payable under Section 7 of this Agreement upon Employee's termination of employment shall be payable unless Employee's termination of employment constitutes a "separation from service" within the meaning of Treas. Reg. § 1.409A-1(h). The Company and Employee intend that their exercise of authority or discretion under this Agreement shall comply with Section 409A of the Code. If any provision of this Agreement does not satisfy the requirements of Section 409A, 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. Notwithstanding the foregoing, no particular tax result for Employee with respect to any income recognized by Employee in connection with this Agreement is guaranteed. Neither the Company nor any of its affiliates shall have any obligation to indemnify or otherwise hold Employee harmless from any or all such taxes, interest, penalties, or liability for any damages related thereto. Each payment under this Agreement is intended to be a "separate payment" and not a series of payments for purposes of Section 409A. References in this Agreement to Section 409A of the Code includes rules, regulations and guidance of general applicability issued by the Department of the Treasury under Code Section 409A. If the Employee is a "specified employee," as such term is defined in Section 409A of the Code and related regulations and Treasury pronouncements ("Section 409A") and determined as described below in this Section 20, any payments payable as a result of the Employee's termination (other than death) that are required to be delayed in accordance with Section 409A of the Code as a result of Employee's status as a "specified employee" shall not be payable before the earliest of (i) the date that is six months after the Employee's termination, (ii) the date of the Employee's death, or (iii) the date that otherwise complies with the requirements of Section

409A. This Section 20 shall be applied by accumulating all payments that otherwise would have been paid within six months of the Employee's termination and paying such accumulated amounts without interest at the earliest date which complies with the requirements of Section 409A. The Employee shall be a "specified employee" for the twelve-month period beginning on April 1 of a year if the Employee is a "key employee" as defined in Section 416(i) of the Code (without regard to Section 416(i)(5)) as of December 31 of the preceding year or using such dates as designated by the Company in accordance with Section 409A and in a manner that is consistent with respect to all of the Company's nonqualified deferred compensation plans. For purposes of determining the identity of specified employees, the Company may establish procedures as it deems appropriate in accordance with Section 409A.

21. Income, Excise or Other Tax Liability. 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 normal employee deductions made with respect to the Company's employees generally.

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

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date and year first above written.

CARRIAGE SERVICES, INC.

By: /s/ Melvin C. Payne

Melvin C. Payne,  
Chief Executive Officer

EMPLOYEE

By: /s/ Paul D. Elliott

Paul D. Elliott



SCHEDULE I  
TO  
EMPLOYMENT AGREEMENT

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

Service Corporation International  
Alderwoods Group, Inc.  
Stewart Enterprises, Inc.  
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  
The Signature Group

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

2. Any new entity which may hereafter be established which acquires any combination of ten or more funeral homes and/or cemeteries from any of the entities described in 1 above.
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, 2013

/s/ Melvin C. Payne

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Melvin C. Payne  
Chairman of the Board and  
Chief 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, 2013

/s/ L. William Heiligbrodt

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L. William Heiligbrodt

Vice Chairman of the Board, Executive

Vice President, Secretary and Director

(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, Principal Accounting Officer 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, 2013

/s/ Melvin C. Payne

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Melvin C. Payne

Chairman of the Board and

Chief Executive Officer

(Principal Executive Officer)

/s/ L. William Heiligbrodt

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L. William Heiligbrodt

Vice Chairman of the Board, Executive

Vice President, Secretary and Director

(Principal Financial Officer)