ST. BERNARD SOFTWARE, INC.
Form 8-K
October 19, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 8-K

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the

Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): October 15, 2007

ST. BERNARD SOFTWARE, INC.

(Exact name of registrant as specified in its charter)

Delaware	**0-50813**	**20-0996152**
(State or other jurisdiction of incorporation)	**(Commission File Number)**	**(I.R.S. Employer Identification No.)**

15015 Avenue of Science

San Diego, CA 92128

(Address of principal executive offices and zip code)

Registrant s telephone number, including area code: (858) 676-2277

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

¨ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

¨ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

¨ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

¨ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 4.01 Changes in Registrant s Certifying Accountant.
On October 15, 2007, Mayer Hoffman McCann P.C. (***Mayer Hoffman***) resigned as the independent registered public accounting firm of St. Bernard Software, Inc., a Delaware corporation (***St. Bernard***). The resignation will be effective on the earlier to occur of (i) the date that St. Bernard files its Form 10-QSB for the period ending September 30, 2007 or (ii) November 20, 2007.

Mayer Hoffman s report on St. Bernard s consolidated financial statements for the fiscal years ending December 31, 2005 and December 31, 2006 did not contain an adverse opinion or a disclaimer of opinion and was not qualified or modified as to uncertainty, audit scope, or accounting principles.

From October 17, 2005, the date on which St. Bernard initially engaged Mayer Hoffman, through October 15, 2007, the resignation date, there were no disagreements between St. Bernard and Mayer Hoffman on any matters of accounting principles or practices, financial statement disclosures, or auditing scope or procedure which, if not resolved to Mayer Hoffman s satisfaction, would have caused Mayer Hoffman to make reference to the subject matter of the disagreement in connection with its reports on the financial statements of St. Bernard.

St. Bernard has furnished a copy of the above disclosures to Mayer Hoffman and has requested that Mayer Hoffman furnish St. Bernard with a letter addressed to the Securities and Exchange Commission stating whether or not it agrees with the above statements. A copy of such a letter is attached to this Current Report on Form 8-K as Exhibit 16.1.

On October 15, 2007, St. Bernard undertook an independent audit investigation which was initiated to review St. Bernard s internal control over its information technology systems. The independent audit investigation is ongoing, and at the time of the filing of this Current Report, St. Bernard is unable to predict the findings that may result.

Item 9.01 Financial Statements and Exhibits.
(d) *Exhibits.*

Exhibit Number	Description
16.1	Letter from Mayer Hoffman McCann P.C. to the Securities and Exchange Commission, dated October 19, 2007.

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.

	St. Bernard Software, Inc.
Dated: October 19, 2007	By: /s/ Alfred F. Riedler Alfred F. Riedler Chief Financial Officer

EXHIBIT INDEX

Exhibit Number	**Description**
16.1	Letter from Mayer Hoffman McCann P.C. to the Securities and Exchange Commission, dated October 19, 2007.

M: 0in; BORDER-LEFT-STYLE: none; PADDING-LEFT: 0in; PADDING-RIGHT: 0in; BORDER-TOP-STYLE: none; BACKGROUND: white; HEIGHT: 13.5pt; BORDER-RIGHT: black 1pt; PADDING-TOP: 0in" vAlign=bottom width="1%">

	$	31,069
	$	34,893
Non-cash investing activity		
Accrued plant and equipment	**$**	**4,315**
	$	2,819
	$	-

See notes to consolidated financial statements.

34

THE CATO CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Class A Common Stock	Convertible Class B Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Stockholders' Equity
			(Dollars in thousands)			
Balance — January 29, 2011	$ 925	$ 58	$ 68,537	$ 264,217	$ 276	334,013
Comprehensive income:						
Net income	-	-	-	64,834	-	64,834
Unrealized losses on available-for-sale securities, net of deferred income tax liability of $406	-	-	-		660	660
Dividends paid ($0.875 per share)	-	-	-	(25,715)	-	(25,715)
Class A common stock sold through employee stock purchase plan — 23,975 shares	1	-	571	-	-	572
Class A common stock sold through stock option plans — 4,875 shares	-	-	290	-	-	290
Class A common stock issued through restricted stock grant plans 85,556 shares	3	-	2,459	12	-	2,474
Windfall tax benefit from equity compensation plans		-	173	-	-	173
Repurchase and retirement of treasury shares – 453,655 shares	(15)	-	-	(10,607)	-	(10,622)
Balance — January 28, 2012	$ 914	$ 58	$ 72,030	$ 292,741	$ 936	366,679
Comprehensive income:						
Net income	-	-	-	61,668	-	61,668
Unrealized gains on available-for-sale securities, net of deferred income tax benefit of ($69)	-	-	-	-	(115)	(115)
Dividends paid ($2.98 per share)	-	-	-	(87,222)	-	(87,222)
Class A common stock sold through employee stock purchase plan — 32,995 shares	1	-	849	-	-	850

Class A common stock sold through stock option plans — 5,750 shares	-	-	562	-	-	562
Class A common stock issued through restricted stock grant plans 98,743 shares	3	-	2,644	23	-	2,670
Windfall tax benefit from equity compensation plans	-	-	509		-	509
Repurchase and retirement of treasury shares – 12,997 shares	-	-	-	(367)	-	(367)
Balance — February 2, 2013	$ 918	$ 58	$ 76,594	$ 266,843	$ 821	$ 345,234
Comprehensive income:						
Net income	-	-	-	54,322	-	54,322
Unrealized gains on available-for-sale securities, net of deferred income tax benefit of ($26)	-	-	-	-	(43)	(43)
Dividends paid ($0.20 per share)	-	-	-	(5,853)	-	(5,853)
Class A common stock sold through employee stock purchase plan — 19,070 shares	1	-	463	-	-	464
Class A common stock sold through stock option plans — 9,050 shares	-	-	145	-	-	145
Class A common stock issued through restricted stock grant plans 198,017 shares	7	-	2,915	1	-	2,923
Windfall tax benefit from equity compensation plans	-	-	346	-	-	346
Repurchase and retirement of treasury shares – 271,296 shares	(9)	-	-	(6,420)	-	(6,429)
Balance — February 1, 2014	$ 917	$ 58	$ 80,463	$ 308,893	$ 778	$ 391,109

See notes to consolidated financial statements.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies:

Principles of Consolidation: The consolidated financial statements include the accounts of The Cato Corporation and its wholly-owned subsidiaries (the "Company"). All significant intercompany accounts and transactions have been eliminated.

Correction of Prior Period Error: In connection with the preparation of our consolidated financial statements for the year ended February 2, 2013, the Company recorded the following out of period adjustments: (1) corrected its accounting for accrued landlord insurance by recording additional pre-tax expense of $1.2 million in 2012 which originated prior to fiscal year 2008; (2) corrected fiscal year 2011 federal income tax expense by recording an additional $1.1 million of income tax expense in 2012; and (3) corrected prior period state income tax expense of $0.6 million in 2012, of which $0.5 million originated in fiscal year 2011 and $0.1 million in fiscal year 2010. The Company has assessed the materiality of these errors and concluded that the errors were not material to any of the current or previously issued financial statements.

Description of Business and Fiscal Year: The Company has two reportable segments — the operation of a fashion specialty stores segment ("Retail Segment") and a credit card segment ("Credit Segment"). The apparel specialty stores operate under the names "Cato," "Cato Fashions," "Cato Plus," "It's Fashion," "It's Fashion Metro" and "Versona Accessories are located primarily in strip shopping centers principally in the southeastern United States. The Company's fiscal year ends on the Saturday nearest January 31.

Use of Estimates: The preparation of the Company's financial statements in conformity with accounting principles generally accepted in the United States ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant accounting estimates reflected in the Company's financial statements include the allowance for doubtful accounts, inventory shrinkage, the calculation of potential asset impairment, workers' compensation, general and auto insurance liabilities, reserves relating to self-insured health insurance, and uncertain tax positions.

Cash and Cash Equivalents: Cash equivalents consist of highly liquid investments with original maturities of three months or less.

Short-Term Investments: Investments with original maturities beyond three months are classified as short-term investments. See Note 3 for the Company's estimated fair value of, and other information regarding, its short-term investments. The Company's short-term investments are all classified as available-for-sale. As they are available for current operations, they are classified on the Consolidated Balance Sheets as Current Assets. Available-for-sale securities are carried at fair value, with unrealized gains and temporary losses, net of income taxes, reported as a component of Accumulated other comprehensive income. Other than temporary declines in the fair value of investments are recorded as a reduction in the cost of the investments in the accompanying Consolidated Balance Sheets and a reduction of Interest and other income in the accompanying Consolidated Statements of Income. The cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. The amortization of premiums, accretion of discounts and realized gains and losses are included in Interest and other income.

During the fourth quarter of 2013, we discovered that we had improperly netted our purchases and sales activity for our investments within cash flows related to investing activities in prior periods. In addition, we had also improperly classified the premiums and amortization of premiums on those investments in cash flows related to investing activities when they should have been in cash flows related to operating activities. The presentation of these amounts was corrected in the current period financial statements and was immaterial to all prior periods presented

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Restricted Cash and Investments: The Company has $4.7 million in escrow at February 1, 2014 as security and collateral for administration of the Company's self-insured workers' compensation and general liability coverage which is reported as Restricted cash and investments on the Consolidated Balance Sheets.

Supplemental Cash Flow Information: Income tax payments, net of refunds received, for the fiscal years ended February 1, 2014, February 2, 2013 and January 28, 2012 were $34,238,000, $43,124,000 and $34,290,000, respectively.

Inventories: Merchandise inventories are stated at the lower of cost or market as determined by the weighted-average cost method.

Property and Equipment: Property and equipment are recorded at cost. Maintenance and repairs are expensed to operations as incurred; renewals and betterments are capitalized. Depreciation is determined on the straight-line method over the estimated useful lives of the related assets excluding leasehold improvements. Leasehold improvements are amortized over the shorter of the estimated useful life or lease term. For leases with renewal periods at the Company's option, the Company generally uses the original lease term plus reasonably assured renewal option periods (generally one five year option period) to determine estimated useful lives. Typical estimated useful lives are as follows:

Classification	**Estimated Useful Lives**
Land improvements	10 years
Buildings	30-40 years
Leasehold improvements	5-10 years
Fixtures and equipment	3-10 years
Information technology equipment and software	3-10 years

Impairment of Long-Lived Assets

The Company invests in property and equipment primarily in connection with the opening and remodeling of stores and in computer software and hardware. The Company periodically reviews its store locations and estimates the recoverability of its assets, recording an impairment charge for the amount by which the carrying value exceeds the fair value, if necessary, when the Company decides to close the store or otherwise determines that future estimated undiscounted cash flows associated with those assets will not be sufficient to recover the carrying value. This determination is based on a number of factors, including the store's historical operating results and cash flows, estimated future sales growth, real estate development in the area and perceived local market conditions that can be difficult to predict and may be subject to change. Store asset impairment charges incurred in fiscal 2013 were $2,646,000. Store asset impairment charges incurred in fiscal 2012 were $2,011,000. Store asset impairment charges incurred in fiscal 2011 were de minimis. In addition, the Company regularly evaluates its computer-related and other long-lived assets and may accelerate depreciation over the revised useful life if the asset is expected to be replaced or has limited future value. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation or amortization are removed from the accounts, and any resulting gain or loss is reflected in income for that period.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Leases

The Company determines the classification of leases consistent with ASC 840 - *Leases*. The Company leases all of its retail stores. Most lease agreements contain construction allowances and rent escalations. For purposes of recognizing incentives and minimum rental expenses on a straight-line basis over the terms of the leases, including renewal periods considered reasonably assured, the Company begins amortization as of the initial possession date which is when the Company enters the space and begins to make improvements in preparation for intended use.

For construction allowances, the Company records a deferred rent liability in Other noncurrent liabilities on the Consolidated Balance Sheets and amortizes the deferred rent over the term of the respective lease as a reduction to Cost of goods sold on the Consolidated Statements of Income and Comprehensive Income.

For scheduled rent escalation clauses during the lease terms or for rental payments commencing at a date other than the date of initial occupancy, the Company records minimum rental expenses on a straight-line basis over the terms of the leases.

Revenue Recognition

The Company recognizes sales at the point of purchase when the customer takes possession of the merchandise and pays for the purchase, generally with cash or credit. Sales from purchases made with Cato credit, gift cards and layaway sales from stores are also recorded when the customer takes possession of the merchandise. E-Commerce sales are recorded when the risk of loss is transferred to the customer. Gift cards are recorded as deferred revenue until they are redeemed or forfeited. Layaway sales are recorded as deferred revenue until the customer takes possession or forfeits the merchandise. Gift cards do not have expiration dates. A provision is made for estimated merchandise returns based on sales volumes and the Company’s experience; actual returns have not varied materially from historical amounts.

In fiscal 2013, 2012 and 2011, the Company recognized $370,000, $500,000 and $470,000, respectively, of income on unredeemed gift cards ("gift card breakage") as a component of Other income on the Consolidated Statements of Income and Comprehensive Income. Gift card breakage is determined after 60 months when the likelihood of the remaining balances being redeemed is remote based on our historical redemption data and there is no legal obligation to remit the remaining balances to relevant jurisdictions.

The Company offers its own credit card to customers. All credit activity is performed by the Company's wholly-owned subsidiaries. None of the credit card receivables are secured. Finance income is recognized as earned under the interest method and late charges are recognized in the month in which they are assessed, net of provisions for estimated uncollectible amounts. The Company evaluates the collectability of accounts receivable and records an allowance for doubtful accounts based on the aging of accounts and estimates of actual write-offs. Finance revenue on the Company's private label credit card portfolio is recognized as earned under the interest method. Late fees are recognized as earned, less provisions for estimated uncollectible fees.

Cost of Goods Sold: Cost of goods sold includes merchandise costs, net of discounts and allowances, buying costs, distribution costs, occupancy costs, freight, and inventory shrinkage. Net merchandise costs and in-bound freight are capitalized as inventory costs. Buying and distribution costs include payroll, payroll-related costs and operating expenses for our buying departments and distribution center. Occupancy expenses include rent, real estate taxes, insurance, common area maintenance, utilities and maintenance for stores and distribution facilities. Buying, distribution, occupancy and internal transfer costs are treated as period costs and are not capitalized as part of inventory.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Advertising: Advertising costs are expensed in the period in which they are incurred. Advertising expense was approximately $5,741,000, $6,186,000 and $7,056,000 for the fiscal years ended February 1, 2014, February 2, 2013 and January 28, 2012, respectively.

Stock Repurchase Program: For fiscal year ending February 1, 2014, the Company had 1,704,672 shares remaining in open authorization. There is no specified expiration date for the Company's repurchase program.

Earnings Per Share: ASC 260 - *Earnings Per Share*, requires dual presentation of basic EPS and diluted EPS on the face of all income statements for all entities with complex capital structures. The Company has presented one basic EPS and one diluted EPS amount for all common shares in the accompanying Consolidated Statements of Income. While the Company's certificate of incorporation provides the right for the Board of Directors to declare dividends on Class A shares without declaration of commensurate dividends on Class B shares, the Company has historically paid the same dividends to both Class A and Class B shareholders and the Board of Directors has resolved to continue this practice. Accordingly, the Company's allocation of income for purposes of EPS computation is the same for Class A and Class B shares and the EPS amounts reported herein are applicable to both Class A and Class B shares.

Basic EPS is computed as net income less earnings allocated to non-vested equity awards divided by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issuable through stock options and the Employee Stock Purchase Plan.

				Fiscal Year Ended			
			February 1, 2014		February 2, 2013		January 28, 2012
Numerator					**(Dollars in thousands)**		
	Net earnings	**$**	**54,322**	$	61,668	$	64,834
	Earnings allocated to non-vested equity awards		**(884)**		(894)		(1,016)
	Net earnings available to common stockholders	**$**	**53,438**	$	60,774	$	63,818
Denominator							
	Basic weighted average common shares outstanding		**28,767,615**		28,796,815		28,896,355

Dilutive effect of stock options and restricted stock		**5,063**		3,563		4,930
Diluted weighted average common shares outstanding		**28,772,678**		28,800,378		28,901,285
Net income per common share						
Basic earnings per share	**$**	**1.86**	$	2.11	$	2.21
Diluted earnings per share	**$**	**1.86**	$	2.11	$	2.21

Vendor Allowances: The Company receives certain allowances from vendors primarily related to purchase discounts and markdown and damage allowances. All allowances are reflected in Cost of goods sold as earned when the related products are sold. Cash consideration received from a vendor is presumed to be a reduction of the purchase cost of merchandise and is reflected as a reduction of inventory. The Company does not receive cooperative advertising allowances.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Income Taxes: The Company files a consolidated federal income tax return. Income taxes are provided based on the asset and liability method of accounting, whereby deferred income taxes are provided for temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities.

Unrecognized tax benefits for uncertain tax positions are established in accordance with ASC 740 when, despite the fact that the tax return positions are supportable, the Company believes these positions may be challenged and the results are uncertain. The Company adjusts these liabilities in light of changing facts and circumstances. Potential accrued interest and penalties related to unrecognized tax benefits within operations are recognized as a component of earnings before taxes.

Store Opening Costs: Costs relating to the opening of new stores or the relocating or expanding of existing stores are expensed as incurred. A portion of construction, design, and site selection costs are capitalized to new, relocated and remodeled stores.

Closed Store Lease Obligations: At the time stores are closed, provisions are made for the rentals required to be paid over the remaining lease terms on a discounted cash flow basis, reduced by any expected sublease rentals.

Insurance: The Company is self-insured with respect to employee health care, workers' compensation and general liability. The Company's self-insurance liabilities are based on the total estimated cost of claims filed and estimates of claims incurred but not reported, less amounts paid against such claims, and are not discounted. Management reviews current and historical claims data in developing its estimates. The Company has stop-loss insurance coverage for individual claims in excess of $325,000 for employee healthcare, $350,000 for workers' compensation and $250,000 for general liability.

Fair Value of Financial Instruments: The Company's carrying values of financial instruments, such as cash and cash equivalents, short-term investments, restricted cash and short-term investments, approximate their fair values due to their short terms to maturity and/or their variable interest rates.

Stock Based Compensation: The Company records compensation expense associated with restricted stock and other forms of equity compensation in accordance with ASC 718 - *Compensation – Stock Compensation.* Compensation cost associated with stock awards recognized in all years presented includes: 1) amortization related to the remaining unvested portion of all stock awards based on the grant date fair value and 2) adjustments for the effects of actual forfeitures versus initial estimated forfeitures.

Recent Accounting Pronouncements

During the first quarter of fiscal 2013, the Company adopted guidance that requires additional disclosures on reclassifications from accumulated other comprehensive income into net income. The new accounting guidance requires entities to report either parenthetically on the face of the financial statements or in the footnotes of these reclassifications for each financial statement line item. This new guidance only impacts disclosures and as such will have no impact on the Company's consolidated financial position, results of operations or cash flows.

In the first quarter of fiscal 2014, the Company will adopt new accounting guidance which eliminates diversity in practice on the presentation of unrecognized tax benefits when a net operating loss, a similar tax loss, or tax credit carry forward exists at the reporting date. The new guidance may affect balance sheet classification of certain unrecognized tax benefits and will have no impact on the Company's consolidated results of operations or cash flows.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

2. Interest and Other Income:

The components of Interest and other income are shown below (in thousands):

	February 1, 2014	February 2, 2013	January 28, 2012
Dividend income	**$ (17)**	$ (19)	$ (16)
Interest income	**(1,288)**	(1,518)	(1,618)
Miscellaneous income	**(1,686)**	(1,852)	(1,943)
Net gain on investment sales	**(276)**	(393)	(240)
Interest and other income	**$ (3,267)**	$ (3,782)	$ (3,817)

3. Short-Term Investments:

At February 1, 2014, the Company's investment portfolio was primarily invested in governmental debt securities held in managed accounts. These securities are classified as available-for-sale as they are highly liquid and are recorded on the Consolidated Balance Sheets at estimated fair value, with unrealized gains and temporary losses reported net of taxes in Accumulated other comprehensive income.

The table below reflects gross accumulated unrealized gains (losses) in short-term investments at February 1, 2014 and February 2, 2013 (in thousands).

	February 1, 2014			February 2, 2013		
	Debt securities issued by various states of the United States and political subdivisions of the states	**Corporate debt securities**	**Total**	Debt securities issued by various states of the United States and political subdivisions of the states	Corporate debt securities	Total
Cost basis	157,358	2,795	160,153	148,605	7,989	156,594
Unrealized gains	971	4	975	980	46	1,026
Unrealized (loss)	-	-	-	(42)	-	(42)

Estimated fair value	$	158,329	$	2,799	$	161,128	$	149,543	$	8,035	$	157,578

Accumulated other comprehensive income on the Consolidated Balance Sheets reflects the accumulated unrealized net gains in short-term investments in addition to unrealized gains from equity investments and restricted cash investments. The table below reflects gross accumulated unrealized gains in these investments at February 1, 2014 and February 2, 2013 (in thousands).

	February 1, 2014						February 2, 2013					
Security Type		**Unrealized Gain/(Loss)**		**Deferred Tax Benefit**		**Unrealized Net Gain/ (Loss)**		Unrealized Gain/(Loss)		Deferred Tax Benefit		Unrealized Net Gain/ (Loss)
Short-Term Investments	$	978	$	(368)	$	610	$	990	$	(372)	$	618
Equity Investments		270		(102)		168		326		(123)		203
Total	$	1,248	$	(470)	$	778	$	1,316	$	(495)	$	821

41

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

4. Fair Value Measurements:

The following tables set forth information regarding the Company's financial assets that are measured at fair value (in thousands) as of February 1, 2014 and February 2, 2013.

Description	**February 1, 2014**	**Prices in Active Markets for Identical Assets Level 1**	**Significant Other Observable Inputs Level 2**	**Significant Unobservable Inputs Level 3**
Assets:				
State/Municipal Bonds	$ 159,074	$ -	$ 159,074	$ -
Corporate Bonds	2,799	-	2,799	-
Auction Rate Securities (ARS)	3,140	-	-	3,140
U.S. Treasury Notes	3,405	3,405	-	-
Cash Surrender Value of Life Insurance	2,957	-	-	2,957
Privately Managed Funds	392	-	-	392
Corporate Equities	585	585	-	-
Certificates of Deposit	100	100	-	-
Total Assets	$ 172,452	$ 4,090	$ 161,873	$ 6,489
Liabilities:				
Deferred Compensation	(3,298)	-	-	(3,298)
Total Liabilities	$ (3,298)	$ -	$ -	$ (3,298)

Description	**February 2, 2013**	**Prices in Active Markets for Identical Assets Level 1**	**Significant Other Observable Inputs Level 2**	**Significant Unobservable Inputs Level 3**
State/Municipal Bonds	$ 151,377	$ -	$ 151,377	$ -
Corporate Bonds	8,035	-	8,035	-
Auction Rate Securities (ARS)	3,450	-	-	3,450
U.S. Treasury Notes	3,906	3,906	-	-
	2,051	-	-	2,051

Cash Surrender Value of Life Insurance				
Privately Managed Funds	561	-	-	561
Corporate Equities	474	474	-	-
Certificates of Deposit	100	100	-	-
Total	$ 169,954	$ 4,480	$ 159,412	$ 6,062
Liabilities:				
Deferred Compensation	(2,178)	-	-	(2,178)
Total Liabilities	$ (2,178)	$ -	$ -	$ (2,178)

The Company’s investment portfolio was primarily invested in corporate bonds and tax-exempt and taxable governmental debt securities held in managed accounts with underlying ratings of A or better at February 1, 2014. The state, municipal and corporate bonds have contractual maturities which range from 14 days to 12.8 years. The U.S. Treasury Notes and Certificates of Deposit have contractual maturities which range from 12 days to 1.6 years. These securities are classified as available-for-sale and are recorded as Short-term investments, Restricted cash and investments and Other assets on the accompanying Consolidated Balance Sheets. These assets are carried at fair value with unrealized gains and losses reported net of taxes in Accumulated other comprehensive income.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Additionally, at February 1, 2014, the Company had $0.4 million of privately managed funds, $0.6 million of corporate equities and a single auction rate security ("ARS") of $3.1 million which continues to fail its auction. All of these assets are recorded within Other assets in the Consolidated Balance Sheets. At February 2, 2013, the Company had $0.6 million of privately managed funds, $0.5 million of corporate equities, and a single ARS of $3.5 million, all of which are recorded within Other assets in the Consolidated Balance Sheets.

Level 1 category securities are measured at fair value using quoted active market prices. Level 2 investment securities include corporate and municipal bonds for which quoted prices may not be available on active exchanges for identical instruments. Their fair value is principally based on market values determined by management with assistance of a third party pricing service. Since quoted prices in active markets for identical assets are not available, these prices are determined by the pricing service using observable market information such as quotes from less active markets and/or quoted prices of securities with similar characteristics, among other factors.

The ARS of $3,450,000 par value was issued by the Wake County, NC Industrial Facilities & Pollution Control Financing Authority. The security is an obligation of Duke Energy Progress and has a credit rating of Aa2. The Company has collected all interest payments when due since the security was purchased and continues to expect that it will receive all interest due on the security in full and on a timely basis in the future.

During the fourth quarter of fiscal 2013, the ARS yield was substantially less than the comparative bond discount rate for two consecutive periods. As a result, the Company wrote down the ARS to approximate fair value as determined by publicly available data of recent sales for the security to third parties. This resulted in a loss of $310,500 included in interest and other income (or changes in net assets) with respect to its ARS Portfolio as of February 1, 2014.

The Company's failed ARS is recorded at $3,139,500 which approximates fair value using Level 3 inputs. Because there is no active market for this particular ARS, its fair value was analyzed through the use of a discounted cash flow analysis and observations from previous trades. The terms used in the analysis were based on management's estimate of the timing of future liquidity, which assumes that the security will be called or refinanced by the issuer or settled with a broker dealer prior to maturity. The discount rates used in the discounted cash flow analysis were based on market rates for similar liquid tax exempt securities with comparable ratings and maturities. Due to the uncertainty surrounding the timing of future liquidity, the Company also considered a liquidity/risk value reduction. In estimating the fair value of this ARS, the Company also considered recent trading activity, the financial condition and near-term prospects of the issuer, the probability that the Company will be unable to collect all amounts due according to the contractual terms of the security and whether the security has been downgraded by a rating agency. The Company's valuation is sensitive to market conditions and management's judgment and can change significantly based on the assumptions used.

The Company's privately managed funds consist of two types of funds. The privately managed funds cannot be redeemed at net asset value at a specific date without advance notice. As a result, the Company has classified the investments as Level 3.

Deferred compensation plan assets consist of life insurance policies. These life insurance policies are valued based on the cash surrender value of the insurance contract, which is determined based on such factors as the fair value of the underlying assets and discounted cash flow and are therefore classified within level 3 of the valuation hierarchy. The level 3 liability associated with the life insurance policies represents a deferred compensation obligation, the value of which is tracked via underlying insurance funds. These funds are designed to mirror existing mutual funds and money market funds that are observable and actively traded. Cash surrender values are provided by third parties and reviewed for reasonableness by the Company.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following tables summarize the change in fair value of the Company's financial assets and liabilities measured using Level 3 inputs as of February 1, 2014 and February 2, 2013 (in thousands):

	Fair Value Measurements Using Significant Unobservable Asset Inputs (Level 3)			
	Available-For-Sale Debt Securities ARS	Other Investments Private Equity	Cash Surrender Value	Total
Beginning Balance at February 2, 2013	$ 3,450	$ 561	$ 2,051	$ 6,062
Redemptions	-	(122)	-	(122)
Additions	-	-	775	775
Total gains or (losses)				
Included in interest and other income (or changes in net assets)	(311)	121	131	(59)
Included in other comprehensive income	-	(168)	-	(168)
Ending Balance at February 1, 2014	$ 3,140	$ 392	$ 2,957	$ 6,489

	Fair Value Measurements Using Significant Unobservable Liability Inputs (Level 3)	
	Deferred Compensation	Total
Beginning Balance at February 2, 2013	$ (2,178)	$ (2,178)
Additions	(863)	(863)
Total (gains) or losses		
Included in interest and other income (or changes in net assets)	(257)	(257)
Ending Balance at February 1, 2014	$ (3,298)	$ (3,298)

	Fair Value Measurements Using Significant Unobservable Asset Inputs (Level 3)			
	Available-For-Sale Debt Securities ARS	Other Investments Private Equity	Cash Surrender Value	Total

Beginning Balance at January 28, 2012	$	3,450	$	1,604	$	-	$	5,054
Redemptions		-		(1,041)		-		(1,041)
Additions						1,932		1,932
Total gains or (losses)								
Included in interest and other income (or changes in net assets)		-		-		119		119
Included in other comprehensive income		-		(2)		-		(2)
Ending Balance at February 2, 2013	$	3,450	$	561	$	2,051	$	6,062

	Fair Value Measurements Using Significant Unobservable Liability Inputs (Level 3)			
		Deferred Compensation		Total
Beginning Balance at January 28, 2012	$	-	$	-
Additions		(2,001)		(2,001)
Total (gains) or losses				
Included in interest and other income (or changes in net assets)		(177)		(177)
Ending Balance at February 2, 2013	$	(2,178)	$	(2,178)

44

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Quantitative information regarding the significant unobservable inputs related to the ARS as of February 1, 2014 were as follows:

Fair Value	Valuation Technique	Unobservable Inputs	
$3,140	Net present value of cash flows	Total Term	8.66 Years
		Yield	0.07%
		Comparative bond discount rate	0.14%

Quantitative information regarding the significant unobservable inputs related to the ARS as of February 2, 2013 were as follows:

Fair Value	Valuation Technique	Unobservable Inputs	
$3,450	Net present value of cash flows	Total Term	9.66 Years
		Yield	0.23%
		Comparative bond discount rate	0.21%

Significant increases or decreases in certain of the inputs could result in a lower fair value measurement. For example, a decrease in the yield, or an increase to the comparative bond discount rate could result in a lower fair value.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

5. Accounts Receivable:

Accounts receivable consist of the following (in thousands):

		February 1, 2014		February 2, 2013
Customer accounts — principally deferred payment accounts	$	**27,414**	$	29,936
Miscellaneous trade receivables		**13,553**		12,133
Total		**40,967**		42,069
Less allowance for doubtful accounts		**1,743**		2,053
Accounts receivable — net	$	**39,224**	$	40,016

Finance charge and late charge revenue on customer deferred payment accounts totaled $6,220,000, $6,929,000 and $7,716,000 for the fiscal years ended February 1, 2014, February 2, 2013 and January 28, 2012, respectively, and charges against the allowance for doubtful accounts were approximately $1,009,000, $1,259,000 and $1,723,000 for the fiscal years ended February 1, 2014, February 2, 2013 and January 28, 2012, respectively. Expenses relating to the allowance for doubtful accounts are classified as a component of Selling, general and administrative expense in the accompanying Consolidated Statements of Income and Comprehensive Income.

6. Property and Equipment:

Property and equipment consist of the following (in thousands):

		February 1, 2014		February 2, 2013
Land and improvements	$	**7,851**	$	6,980
Buildings		**27,269**		25,948
Leasehold improvements		**94,185**		86,540
Fixtures and equipment		**208,902**		199,815
Information technology equipment and software		**58,705**		57,378
Construction in progress		**12,300**		9,004
Total		**409,212**		385,665
Less accumulated depreciation		**268,083**		251,438
Property and equipment — net	$	**141,129**	$	134,227

Construction in progress primarily represents costs related to new store development and investments in new technology.

7. Accrued Expenses:

Accrued expenses consist of the following (in thousands):

		February 1, 2014		February 2, 2013
Accrued payroll and related items	$	**7,608**	$	7,929
Property and other taxes		**15,285**		14,011
Accrued self-insurance		**10,605**		9,706
Other		**12,265**		12,127
Total	$	**45,763**	$	43,773

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

8. Financing Arrangements

As of February 1, 2014, the Company had an unsecured revolving credit agreement to borrow $35.0 million less the balance of revocable credits discussed below. During 2013, the revolving credit agreement was amended and extended to August 2015. The credit agreement contains various financial covenants and limitations, including the maintenance of specific financial ratios with which the Company was in compliance as of February 1, 2014. There were no borrowings outstanding under this credit facility during the periods ended February 1, 2014, February 2, 2013 or January 28, 2012. The weighted average interest rate under the credit facility was zero at February 1, 2014 due to no borrowings during the year.

At February 1, 2014, February 2, 2013 and January 28, 2012, the Company had approximately $0.4 million, $2.9 million and $2.3 million, respectively, of outstanding revocable letters of credit relating to purchase commitments.

9. Stockholders' Equity:

The holders of Class A Common Stock are entitled to one vote per share, whereas the holders of Class B Common Stock are entitled to ten votes per share. Each share of Class B Common Stock may be converted at any time into one share of Class A Common Stock. Subject to the rights of the holders of any shares of Preferred Stock that may be outstanding at the time, in the event of liquidation, dissolution or winding up of the Company, holders of Class A Common Stock are entitled to receive a preferential distribution of $1.00 per share of the net assets of the Company. Cash dividends on the Class B Common Stock cannot be paid unless cash dividends of at least an equal amount are paid on the Class A Common Stock.

The Company's certificate of incorporation provides that shares of Class B Common Stock may be transferred only to certain "Permitted Transferees" consisting generally of the lineal descendants of holders of Class B Stock, trusts for their benefit, corporations and partnerships controlled by them and the Company's employee benefit plans. Any transfer of Class B Common Stock in violation of these restrictions, including a transfer to the Company, results in the automatic conversion of the transferred shares of Class B Common Stock held by the transferee into an equal number of shares of Class A Common Stock.

On March 24, 2014, the Company paid a quarterly dividend of $0.30 per share.

47

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

10. Employee Benefit Plans:

The Company has a defined contribution retirement savings plan (“401(k) plan”) which covers all associates who meet minimum age and service requirements. The 401(k) plan allows participants to contribute up to 60% of their annual compensation up to the maximum elective deferral, designated by the IRS. The Company is obligated to make a minimum contribution to cover plan administrative expenses. Further Company contributions are at the discretion of the Board of Directors. The Company’s contributions for the years ended February 1, 2014, February 2, 2013 and January 28, 2012 were approximately $1,196,000, $1,186,000 and $1,200,000, respectively.

The Company has a trusteed, non-contributory Employee Stock Ownership Plan (“ESOP”), which covers substantially all associates who meet minimum age and service requirements. The amount of the Company’s discretionary contribution to the ESOP is determined annually by the Compensation Committee of the Board of Directors and can be made in Company Class A Common stock or cash. The Company has chosen to contribute cash and the plan purchases stock on the open market consistent with prior years. The Committee approved a contribution of approximately $887,000 for year ended February 1, 2014. The Company’s contribution for the year ended February 2, 2013 was $508,000 and year ended January 28, 2012 was $514,000.

The Company is primarily self-insured for health care. These costs are significant primarily due to the large number of the Company’s retail locations and associates. The Company’s self-insurance liabilities are based on the total estimated costs of claims filed and estimates of claims incurred but not reported, less amounts paid against such claims. Management reviews current and historical claims data in developing its estimates. If the underlying facts and circumstances of the claims change or the historical trend is not indicative of future trends, then the Company may be required to record additional expense or a reduction to expense which could be material to the Company’s reported financial condition and results of operations. The Company funds health care contributions to a third party provider.

11. Leases:

The Company has operating lease arrangements for store facilities and equipment. Facility leases generally are at a fixed rate for periods of five years with renewal options. For leases with landlord capital improvement funding, the funded amount is recorded as a deferred liability and amortized over the term of the lease as a reduction to rent expense on the Consolidated Statements of Income. Equipment leases are generally for one to three year periods.

The minimum rental commitments under non-cancelable operating leases are (in thousands):

Fiscal Year		
2014	$	63,019
2015		49,792
2016		36,820
2017		24,118
2018		15,371
Thereafter		29,017
Total minimum lease payments	$	218,137

The following schedule shows the composition of total rental expense for all leases (in thousands):

Fiscal Year Ended		**February 1, 2014**		February 2, 2013		January 28, 2012
Minimum rentals	**$**	**61,889**	$	59,887	$	56,671
Contingent rent		**4**		16		28
Total rental expense	**$**	**61,893**	$	59,903	$	56,699

48

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

12. Income Taxes:

Unrecognized tax benefits for uncertain tax positions are established in accordance with ASC 740 when, despite the fact that the tax return positions are supportable, the Company believes these positions may be challenged and the results are uncertain. The Company adjusts these liabilities in light of changing facts and circumstances. As of February 1, 2014, the Company had gross unrecognized tax benefits totaling approximately $9.2 million, of which approximately $6.5 million would affect the effective tax rate if recognized. The Company had approximately $5.4 million, $5.0 million and $4.7 million of interest and penalties accrued related to uncertain tax positions as of February 1, 2014, February 2, 2013 and January 28, 2012, respectively. The Company recognizes interest and penalties related to the resolution of uncertain tax positions as a component of income tax expense. The Company recognized $927,000, $899,000 and $956,000 of interest and penalties in the Consolidated Statement of Income and Comprehensive Income for the years ended February 1, 2014, February 2, 2013 and January 28, 2012, respectively. The Company is no longer subject to U.S. federal income tax examinations for years before 2010. In state and local tax jurisdictions, the Company has limited exposure before 2004. During the next 12 months, various state and local taxing authorities' statues of limitations will expire and certain state examinations may close, which could result in a potential reduction of unrecognized tax benefits for which a range can not be determined.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

A reconciliation of the beginning and ending amount of gross unrecognized tax benefits is as follows (in thousands):

Fiscal Year Ended	**February 1, 2014**	February 2, 2013	January 28, 2012
Balances, beginning	**$ 8,892**	$ 8,689	$ 8,343
Additions for tax positions of the current year	**1,209**	1,222	1,118
Additions for tax positions prior years	**-**	-	250
Reduction for tax positions of prior years for:			
Settlements during the period	**(464)**	(581)	(685)
Lapses of applicable statue of limitations	**(423)**	(438)	(337)
Balance, ending	**$ 9,214**	$ 8,892	$ 8,689

The provision for income taxes consists of the following (in thousands):

Fiscal Year Ended	**February 1, 2014**	February 2, 2013	January 28, 2012
Current income taxes:			
Federal	**$ 31,699**	$ 38,415	$ 29,048
State	**3,032**	4,429	3,181
Total	**34,731**	42,844	32,229
Deferred income taxes:			
Federal	**(4,260)**	(4,952)	2,867
State	**(507)**	(589)	341
Total	**(4,767)**	(5,541)	3,208
Total income tax expense	**$ 29,964**	$ 37,303	$ 35,437

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Significant components of the Company's deferred tax assets and liabilities as of February 1, 2014 and February 2, 2013 are as follows (in thousands):

		February 1, 2014		February 2, 2013
Deferred tax assets:				
Allowance for doubtful accounts	**$**	**598**	$	772
Inventory valuation		**2,349**		1,232
Deferred lease liability		**2,940**		4,174
Non-deductible accrued liabilities		**1,133**		1,355
Other taxes		**1,668**		1,564
Federal benefit of uncertain tax positions		**4,292**		3,910
Equity compensation expense		**3,246**		2,728
Accrued Bonus		**800**		-
Other		**2,065**		1,952
Total deferred tax assets		**19,091**		17,687
Deferred tax liabilities				
Property and equipment		**8,690**		12,425
Unrealized gains on short-term investments		**469**		495
Health care expense		**1,383**		1,150
Other		**2,456**		2,316
Total deferred tax liabilities		**12,998**		16,386
Net deferred tax liabilities (assets)	**$**	**(6,093)**	$	(1,301)

The reconciliation of the Company's effective income tax rate with the statutory rate is as follows:

<u>**Fiscal Year Ended**</u>	**February 1, 2014**	February 2, 2013	January 28, 2012
Federal income tax rate	**35.0 %**	35.0 %	35.0 %
State income taxes	**2.8**	3.2	1.7
Tax credits	**(1.4)**	(1.1)	(1.0)
Tax exempt interest	**(0.5)**	(0.5)	(0.5)

Effects of permanent differences	**0.1**	0.1	(0.1)
Other	**(0.4)**	1.0	0.2
Effective income tax rate	**35.6 %**	37.7 %	35.3 %

51

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

13. Quarterly Financial Data (Unaudited):

Summarized quarterly financial results are as follows (in thousands, except per share data):

Fiscal 2013	**First**	**Second**	**Third**	**Fourth**
Total revenues	$ 269,698	$ 231,718	$ 201,043	$ 217,574
Gross profit (exclusive of depreciation)	112,797	86,768	72,256	76,966
Net income	30,839	14,775	4,885	3,823
Basic earnings per share	$ 1.05	$ 0.51	$ 0.17	$ 0.13
Diluted earnings per share	$ 1.05	$ 0.51	$ 0.17	$ 0.13
Fiscal 2012	**First**	**Second**	**Third**	**Fourth**
Total revenues	$ 275,344	$ 234,063	$ 200,005	$ 234,636
Gross profit (exclusive of depreciation)	117,512	91,604	69,606	83,365
Net income	31,723	17,333	4,669	7,944
Basic earnings per share	$ 1.09	$ 0.59	$ 0.16	$ 0.27
Diluted earnings per share	$ 1.09	$ 0.59	$ 0.16	$ 0.27

As discussed in Note 1, the company has corrected its consolidated financial statements by recording the following out of period adjustments in fiscal year 2012.: (1) corrected its accounting for accrued landlord insurance by recording additional pre-tax expense of $1.2 million in 2012 which originated prior to fiscal year 2008; (2) corrected fiscal year 2011 federal income tax expense by recording an additional $1.1 million of income tax expense in 2012; and (3) corrected prior period state income tax expense of $0.6 million in 2012, of which $0.5 million originated in fiscal year 2011 and $0.1 million in fiscal year 2010. The Company has assessed the materiality of these errors and concluded that the errors were not material to any of the current or previously issued financial statements.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

14. Reportable Segment Information

The Company has determined that it has four operating segments, as defined under ASC 280-10, including Cato, It's Fashion, Versona Accessories and Credit. As outlined in ASC 280-10, the Company has two reportable segments: Retail and Credit. The Company has aggregated its retail operating segments based on the aggregation criteria outlined in ASC 280-10, which states that two or more operating segments may be aggregated into a single reportable segment if aggregation is consistent with the objective and basic principles of ASC 280-10, if the segments have similar economic characteristics, similar product, similar production processes, similar clients and similar methods of distribution.

The Company's retail operating segments have similar economic characteristics and similar operating, financial and competitive risks. They are similar in nature of product, as they all offer women's apparel, shoes and accessories. Merchandise inventory of the Company's operating segments is sourced from the same countries and some of the same vendors, using similar production processes. Clients of the Company's operating segments have similar characteristics. Merchandise for the Company's operating segments is distributed to retail stores in a similar manner through the Company's single distribution center and is subsequently distributed to clients in a similar manner.

The Company operates its women's fashion specialty retail stores in 32 states as of February 1, 2014, principally in the southeastern United States. The Company offers its own credit card to its customers and all credit authorizations, payment processing, and collection efforts are performed by a separate subsidiary of the Company.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following schedule summarizes certain segment information (in thousands):

Fiscal 2013		**Retail**		**Credit**		**Total**
Revenues	$	913,813	$	6,220	$	920,033
Depreciation		21,785		40		21,825
Interest and other income		(3,267)		-		(3,267)
Income before taxes		81,709		2,577		84,286
Total assets		524,908		72,010		596,918
Capital expenditures		31,423		119		31,542
Fiscal 2012		**Retail**		**Credit**		**Total**
Revenues	$	937,119	$	6,929	$	944,048
Depreciation		22,404		51		22,455
Interest and other income		(3,782)		-		(3,782)
Income before taxes		95,972		2,999		98,971
Total assets		463,527		69,119		532,646
Capital expenditures		44,924		251		45,175
Fiscal 2011		**Retail**		**Credit**		**Total**
Revenues	$	923,742	$	7,716	$	931,458
Depreciation		21,785		40		21,825
Interest and other income		(3,817)		-		(3,817)
Income before taxes		97,037		3,234		100,271
Total assets		471,397		79,692		551,089
Capital expenditures		35,804		86		35,890

The accounting policies of the segments are the same as those described in the summary of significant accounting policies in Note 1. The Company evaluates performance based on profit or loss from operations before income taxes. The Company does not allocate certain corporate expenses to the credit segment.

The following schedule summarizes the direct expenses of the credit segment which are reflected in selling, general and administrative expenses (in thousands):

		February 1, 2014		February 2, 2013		January 28, 2012
Bad debt expense	**$**	**1,009**	$	1,259	$	1,723
Payroll		**907**		919		954
Postage		**744**		751		757

Other expenses	**943**	950	1,008
Total expenses	**$ 3,603**	$ 3,879	$ 4,442

54

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

15. Stock Based Compensation:

As of February 1, 2014, the Company had three long-term compensation plans pursuant to which stock-based compensation was outstanding or could be granted. The Company's 1987 Non-Qualified Stock Option Plan is for the granting of options to officers and key employees. The 2013 Incentive Compensation Plan and 2004 Incentive Compensation Plan are for the granting of various forms of equity-based awards, including restricted stock and stock options for grant, to officers, directors and key employees. Effective May 23, 2013, shares for grant were no longer available under the 2004 Amended and Restated Incentive Compensation Plan.

The following table presents the number of options and shares of restricted stock initially authorized and available for grant under each of the plans as of February 1, 2014:

	1987 Plan	2004 Plan	2013 Plan	Total
Options and/or restricted stock initially authorized	5,850,000	1,350,000	1,500,000	8,700,000
Options and/or restricted stock available for grant:				
February 2, 2013	20,127	443,566	-	463,693
February 1, 2014	-	-	1,489,152	1,489,152

In accordance with ASC 718, the fair value of current restricted stock awards is estimated on the date of grant based on the market price of the Company's stock and is amortized to compensation expense on a straight-line basis over a five year vesting period. As of February 1, 2014, there was $8,298,000 of total unrecognized compensation expense related to nonvested restricted stock awards, which is expected to be recognized over a remaining weighted-average vesting period of 2.6 years. The total fair value of the shares recognized as compensation expense during the twelve months ended February 1, 2014, February 2, 2013 and January 28, 2012 was $2,924,000, $2,669,000 and $2,475,000, respectively. The expenses are classified as a component of Selling, general and administrative expenses in the Consolidated Statements of Income.

The following summary shows the changes in the shares of restricted stock outstanding during the years ended February 1, 2014, February 2, 2013 and January 28, 2012:

	Number of Shares		**Weighted Average Grant Date Fair Value Per Share**
Restricted stock awards at January 29, 2011	509,456	$	20.32

Granted	102,449		25.41
Vested	(128,103)		20.53
Forfeited or expired	(22,461)		21.33
Restricted stock awards at January 28, 2012	461,341	$	21.44
Granted	110,397		28.23
Vested	(114,172)		18.83
Forfeited or expired	(17,420)		24.95
Restricted stock awards at February 2, 2013	440,146	$	23.70
Granted	214,637		23.57
Vested	(121,692)		19.82
Forfeited or expired	(27,468)		24.71
Restricted stock awards at February 1, 2014	505,623	$	24.52

55

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The Company's Employee Stock Purchase Plan allows eligible full-time employees to purchase a limited number of shares of the Company's Class A Common Stock during each semi-annual offering period at a 15% discount through payroll deductions. During the twelve month periods ended February 1, 2014, the Company sold 19,070 shares to employees at an average discount of $3.65 per share under the Employee Stock Purchase Plan. The compensation expense recognized for the 15% discount given under the Employee Stock Purchase Plan was approximately $70,000, $128,000 and $84,000 for fiscal years 2013, 2012 and 2011, respectively. These expenses are classified as a component of selling, general and administrative expenses.

The following is a summary of changes in stock options outstanding during the year ended February 1, 2014.

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value(a)
Options outstanding at February 2, 2013	9,550	$ 13.47	2.12 years	$ 136,185
Granted	20,127	-		
Forfeited or expired	-			
Exercised	(9,050)	-		
Outstanding at February 1, 2014	20,627	$ 23.33	9.04 years	$ 163,000
Vested and exercisable at February 1, 2014	500	$ 14.17	0.67 years	$ 8,500

During fiscal 2013, 20,127 options were granted. No options were granted in fiscal 2012 and 2011. The Company utilizes the Black–Scholes method to estimate the fair value of share based payments.

The total intrinsic value of options exercised during the years ended February 1, 2014, February 2, 2013 and January 28, 2012 was $112,000, $79,000 and $57,000, respectively.

The stock option expense was $13,000 for the twelve months ended February 1, 2014 and zero for the twelve months ended February 2, 2013 and January 28, 2012.

Stock option awards outstanding under the Company's current plans were granted at exercise prices which were equal to the market value of the Company's stock on the date of grant, vest over five years, and expire no later than ten years after the grant date.

16. Commitments and Contingencies:

The Company does not have any guarantees with third parties.

The Company is a defendant in legal proceedings considered to be in the normal course of business. The resolution of such currently pending matters, individually or collectively, are not expected to have a material effect on the Company's results of operations, cash flows or financial position.

THE CATO CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

17. Accumulated Other Comprehensive Income:

The following table sets forth information regarding the reclassification out of Accumulated other comprehensive income (in thousands) as of February 1, 2014:

		Changes in Accumulated Other Comprehensive Income (a) Unrealized Gains and (Losses) on Available-for-Sale Securities
Beginning Balance at February 2, 2013	$	821
Other comprehensive income before reclassification		125
Amounts reclassified from accumulated other comprehensive income (b)		(168)
Net current-period other comprehensive income		(43)
Ending Balance at February 1, 2014	$	778

(a) All amounts are net-of-tax. Amounts in parentheses indicate a debit/reduction to other comprehensive income ("OCI").

(b) Includes $269 impact of accumulated other comprehensive income reclassifications into Interest and other income for net gains on available-for-sale securities. The tax impact of this reclassification was $101.

Amounts in parentheses indicate a debit/reduction to OCI.

The following table sets forth information regarding the reclassification out of Accumulated other comprehensive income (in thousands) as of February 2, 2013:

		Changes in Accumulated Other Comprehensive Income (a) Unrealized Gains and (Losses) on Available-for-Sale Securities
	$	936

Beginning Balance at January 28, 2012		
Other comprehensive income before reclassification		(98)
Amounts reclassified from accumulated other comprehensive income (b)		(17)
Net current-period other comprehensive income		(115)
Ending Balance at February 2, 2013	$	821

(a) All amounts are net-of-tax. Amounts in parentheses indicate a debit/reduction to OCI.
(b) Includes $27 impact of accumulated other comprehensive income reclassifications into Interest and other

income for net gains on available-for-sale securities. The tax impact of this reclassification was $10.

Amounts in parentheses indicate a debit/reduction to OCI.

Item 9. ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure:***

None.

Item 9A. ***Controls and Procedures:***

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

We carried out an evaluation, with the participation of our Principal Executive Officer and Principal Financial Officer, of the effectiveness of our disclosure controls and procedures as of February 1, 2014. Based on this evaluation, our Principal Executive Officer and Principal Financial Officer concluded that, as of February 1, 2014, our disclosure controls and procedures, as defined in Rule 13a-15(e), under the Securities Exchange Act of 1934 (the "Exchange Act"), were effective to ensure that information we are required to disclose in the 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 that such information is accumulated and communicated to our management, including our Principal Executive Officer and Principal Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Exchange Act Rule 13a-15(f). Under the supervision and with the participation of our management, including our Principal Executive Officer and Principal Financial Officer, we carried out an evaluation of the effectiveness of our internal control over financial reporting as of February 1, 2014 based on the *Internal Control – Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on this evaluation, management concluded that our internal control over financial reporting was effective as of February 1, 2014.

PricewaterhouseCoopers LLP, our independent registered public accounting firm, has audited the effectiveness of our internal control over financial reporting as of February 1, 2014, as stated in its report which is included herein.

Changes in Internal Control Over Financial Reporting

No change in the Company’s internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) has occurred during the Company’s fiscal quarter ended February 1, 2014 that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

Item 9B. ***Other Information:***

None.

PART III

Item 10. ***Directors, Executive Officers and Corporate Governance:***

Information contained under the captions “Election of Directors,” “Meetings and Committees,” “Corporate Governance Matters” and “Section 16(a) Beneficial Ownership Reporting Compliance” in the Registrant’s Proxy Statement for its 2014 annual stockholders’ meeting (the “2014 Proxy Statement”) is incorporated by reference in response to this Item 10. The information in response to this Item 10 regarding executive officers of the Company is contained in Item 3A, Part I hereof under the caption “Executive Officers of the Registrant.”

Item 11. ***Executive Compensation:***

Information contained under the captions "2013 Executive Compensation," "Fiscal 2013 Director Compensation," "Corporate Governance Matters-Compensation Committee Interlocks and Insider Participation" in the Company's 2014 Proxy Statement is incorporated by reference in response to this Item.

Item 12. ***Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters:***

Equity Compensation Plan Information

The following table provides information about stock options outstanding and shares available for future awards under all of Cato's equity compensation plans. The information is as of February 1, 2014.

Plan Category	(a) Number of Securities to be Issued upon Exercise of Outstanding Options, Warrants and Rights(1)	(b) Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights(1)	(c) Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a)) (2)
Equity compensation plans approved by security holders	20,627	$23.33	1,737,917
Equity compensation plans not approved by security holders	-	-	-
Total	20,627	$23.33	1,737,917

(1) This column contains information regarding employee stock options only; there are no outstanding warrants or stock appreciation rights.

(2) Includes the following:

Under the Company's stock incentive plan, referred to as the 2013 Incentive Compensation Plan, 1,489,152 shares are available for grant. Under this plan, non-qualified stock options may be granted to key associates.

Under the 2013 Employee Stock Purchase Plan, 248,765 shares are available. Eligible associates may participate in the purchase of designated shares of the Company's common stock. The purchase price of this stock is equal to 85% of the lower of the closing price at the beginning or the end of each semi-annual stock purchase period.

Information contained under "Security Ownership of Certain Beneficial Owners and Management" in the 2014 Proxy Statement is incorporated by reference in response to this Item.

Item 13. ***Certain Relationships and Related Transactions and Director Independence :***

Information contained under the caption "Certain Relationships and Related Person Transactions," "Corporate Governance Matters-Director Independence" and "Meetings and Committees" in the 2014 Proxy Statement is incorporated by reference in response to this Item.

Item 14. ***Principal Accountant Fees and Services:***

Information contained under the captions "Ratification of Independent Registered Public Accounting Firm-Audit Fees" and "Policy on Audit Committee Pre-Approval of Audit and Permissible Non-Audit Service by the Independent Registered Public Accounting Firm" in the 2014 Proxy Statement is incorporated by reference in response to this item.

PART IV

Item 15. ***Exhibits and Financial Statement Schedules:***

(a) The following documents are filed as part of this report:

(1) Financial Statements:

Page

(2) Financial Statement Schedule: The following report and financial statement schedule is filed herewith:

All other schedules are omitted as the required information is inapplicable or the information is presented in the Consolidated Financial Statements or related Notes thereto.

(3) Index to Exhibits: The following exhibits listed in the Index below are filed with this report or, as noted, incorporated by reference herein. The Company will supply copies of the following exhibits to any shareholder upon receipt of a written request addressed to the Corporate Secretary, The Cato Corporation, 8100 Denmark Road, Charlotte, NC 28273 and the payment of $.50 per page to help defray the costs of handling, copying and postage. In most cases, documents incorporated by reference to exhibits to our registration statements, reports or proxy statements filed by the Company with the Securities and Exchange Commission are available to the public over the Internet from the SEC's web site at http://www.sec.gov. You may also read and copy any such document at the SEC's public reference room located at Room 1580, 100 F. Street, N.E., Washington, D.C. 20549 under the Company's SEC file number (1–31340).

Exhibit Number	Description of Exhibit
3.1	Registrant's Restated Certificate of Incorporation of the Registrant dated March 6, 1987, incorporated by reference to Exhibit 4.1 to Form S-8 of the Registrant filed February 7, 2000 (SEC File No. 333–96283).
3.2	Registrant's By Laws incorporated by reference to Exhibit 99.2 to Form 8-K of the Registrant filed December 10, 2007.
4.1	Rights Agreement dated December 18, 2003, incorporated by reference to Exhibit 4.1 to Form 8-A12G of the Registrant filed December 22, 2003 and as amended in Form 8-A12B/A filed on January 6, 2004.
10.2+	1999 Incentive Compensation Plan dated August 26, 1999, incorporated by reference to Exhibit 4.3 to Form S-8 of the Registrant filed February 7, 2000 (SEC File No. 333–96283).
10.3+	2004 Incentive Compensation Plan, amended and restated as of May 22, 2008, incorporated by reference to Appendix A to Definitive Proxy Statement on Schedule 14A filed April 11, 2008.
10.4+	2013 Incentive Compensation Plan, incorporated by reference to Exhibit 4.1 to Form S-8 of the Registrant filed May 31, 2013 (SEC file No. 333-188993).
10.5+	Form of Agreement, dated as of August 29, 2003, between the Registrant and Wayland H. Cato, Jr., incorporated by reference to Exhibit 99(c) to Form 8-K of the Registrant filed on July 22, 2003.
10.6+	Form of Agreement, dated as of August 29, 2003, between the Registrant and Edgar T. Cato, incorporated by reference to Exhibit 99(d) to Form 8-K of the Registrant filed on July 22, 2003.
10.7+	Retirement Agreement between Registrant and Wayland H. Cato, Jr. dated August 29, 2003 incorporated by reference to Exhibit 10.1 to Form 10-Q of the Registrant for quarter ended August 2, 2003.
10.8+	Retirement Agreement between Registrant and Edgar T. Cato dated August 29, 2003, incorporated by reference to Exhibit 10.2 to Form 10-Q of the Registrant for the quarter ended

	August 2, 2003.
10.9+	Letter Agreement between the Registrant and John R. Howe dated as of August 28, 2008, incorporated by Reference to Exhibit 99.1 to Form 8-K of the Registrant filed September 3, 2008.
10.10+	Deferred Compensation Plan effective July 28, 2011, incorporated by reference to Exhibit 10.1 to Form 8-K of the Registrant filed on July 19, 2011.
21.1**	Subsidiaries of Registrant.
23.1**	Consent of Independent Registered Public Accounting Firm.
31.1***	Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer.
31.2***	Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer.
32.1***	Section 1350 Certification of Chief Executive Officer.
32.2***	Section 1350 Certification of Chief Financial Officer.
101.1**	The following materials from Registrant's Annual Report on form 10-K for the fiscal years ended February 1, 2014, formatted in XBRL: (i) Consolidated Statements of Income and Comprehensive Income for the fiscal years ended February 1, 2014, February 2, 2013 and January 28, 2012; (ii) Consolidated Balance Sheets at February 1, 2014 and February 2, 2013; (iii) Consolidated Statements of Cash Flows for the fiscal years ended February 1, 2014, February 2, 2013 and January 28, 2012; (iv) Consolidated Statements of Stockholders' Equity for the fiscal years ended February 1, 2014, February 2, 2013 and January 28, 2012; and (v) Notes to Consolidated Financial Statements.

**Previously filed as an exhibit to our Original Form 10-K.

***Filed electronically herewith.

+Management contract or compensatory plan required to be filed under Item 15 of this report and Item 601 of Regulation S-K.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, Cato has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

The Cato Corporation

By	/s/ JOHN P. D. CATO John P. D. Cato Chairman, President and Chief Executive Officer	By	/s/ JOHN R. HOWE John R. Howe Executive Vice President Chief Financial Officer
By	/s/ JEFFREY R. SHOCK Jeffrey R. Shock Senior Vice President Controller		

Date: April 10, 2014

Schedule II

VALUATION AND QUALIFYING ACCOUNTS

	Allowance for Doubtful Accounts(a)	Self Insurance Reserves(b)
Balance at January 29, 2011	$ 2,985	$ 6,519
Additions charged to costs and expenses	1,723	5,062
Additions (reductions) charged to other accounts	609 (c)	(961)
Deductions	(2,955)(d)	(4,288)
Balance at January 28, 2012	2,362	6,332
Additions charged to costs and expenses	1,259	3,525
Additions (reductions) charged to other accounts	756 (c)	1,974
Deductions	(2,324)(d)	(3,744)
Balance at February 2, 2013	$ 2,053	$ 8,087
Additions charged to costs and expenses	1,221	4,497
Additions (reductions) charged to other accounts	425 (c)	(611)
Deductions	(1,956)(d)	(2,861)
Balance at February 1, 2014	$ 1,743	$ 9,112

(a) Deducted from trade accounts receivable.
(b) Reserve for Workers' Compensation and General Liability.
(c) Recoveries of amounts previously written off.
(d) Uncollectible accounts written off.

64