

BIG LOTS INC  
Form 10-K  
April 01, 2014  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended February 1, 2014  
or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-8897

BIG LOTS, INC.

(Exact name of registrant as specified in its charter)

Ohio

(State or other jurisdiction of incorporation or organization)

06-1119097

(I.R.S. Employer Identification No.)

300 Phillipi Road, P.O. Box 28512, Columbus, Ohio

(Address of principal executive offices)

43228-5311

(Zip Code)

(614) 278-6800

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Common Shares \$0.01 par value

Name of each exchange on which registered

New York Stock Exchange

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

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

Indicate by check mark whether 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

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

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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 Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

The aggregate market value of the Common Shares held by non-affiliates of the Registrant (assuming for these purposes that all executive officers and directors are “affiliates” of the Registrant) was \$2,075,281,384 on August 3, 2013, the last business day of the Registrant's most recently completed second fiscal quarter (based on the closing price of the Registrant's Common Shares on such date as reported on the New York Stock Exchange).

The number of the registrant's common shares, \$0.01 par value, outstanding as of March 28, 2014, was 58,152,451.

Documents Incorporated by Reference

Portions of the registrant's Proxy Statement for its 2013 Annual Meeting of Shareholders are incorporated by reference into Part III of this Annual Report on Form 10-K.

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BIG LOTS, INC.  
 FORM 10-K  
 FOR THE FISCAL YEAR ENDED FEBRUARY 1, 2014

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## Part I

## Item 1. Business

## The Company

Big Lots, Inc., an Ohio corporation, through its wholly owned subsidiaries (collectively referred to herein as “we,” “us,” and “our” except as used in the reports of our independent registered public accounting firm included in Item 8 of this Annual Report on Form 10-K (“Form 10-K”)), is the largest broadline closeout retailer in the United States of America (“U.S.”) (see the discussion below under the caption “Closeout Retailing”). At February 1, 2014, we operated a total of 1,570 stores in the U.S. and Canada. Our goal is to strengthen and build upon our leadership position in broadline closeout value retailing by providing our customers with great savings on brand-name closeouts and other value-priced merchandise. You can locate us on the Internet at [www.biglots.com](http://www.biglots.com). The contents of our websites are not part of this report.

Similar to many other retailers, our fiscal year ends on the Saturday nearest to January 31, which results in some fiscal years being comprised of 52 weeks and some being comprised of 53 weeks. Unless otherwise stated, references to years in this Form 10-K relate to fiscal years rather than to calendar years. The following table provides a summary of our fiscal year calendar and the associated number of weeks in each fiscal year:

| Fiscal Year | Number of Weeks | Year Begin Date  | Year End Date    |
|-------------|-----------------|------------------|------------------|
| 2014        | 52              | February 2, 2014 | January 31, 2015 |
| 2013        | 52              | February 3, 2013 | February 1, 2014 |
| 2012        | 53              | January 29, 2012 | February 2, 2013 |
| 2011        | 52              | January 30, 2011 | January 28, 2012 |
| 2010        | 52              | January 31, 2010 | January 29, 2011 |
| 2009        | 52              | February 1, 2009 | January 30, 2010 |

We manage our retailing business on the basis of two segments: U.S. and Canada. Please refer to the consolidated financial statements and related notes in this Form 10-K for our financial information.

On December 5, 2013, we announced our intention to wind down the operations of Big Lots Canada, Inc., the subsidiary operating our Canadian segment, in the first quarter of 2014 (“Canadian Wind Down”). Please refer to note 13 of the accompanying consolidated financial statements for our additional information regarding the wind down of our Canadian segment.

In our U.S. segment, we evaluate and report overall sales and merchandise performance based on the following key merchandising categories: Food, Consumables, Soft Home, Hard Home, Furniture & Home Décor, Seasonal, and Electronics & Accessories. The Food category includes our beverage & grocery, candy & snacks, and specialty foods departments. The Consumables category includes our health and beauty, plastics, paper, chemical, and pet departments. The Soft Home category includes the fashion bedding, utility bedding, bath, window, decorative textile, and flooring departments. The Hard Home category includes our small appliances, table top, food preparation, stationery, greeting cards, tools, paint, and home maintenance departments. The Furniture & Home Décor category includes our upholstery, mattress, ready-to-assemble, case goods, home décor, and frames departments. The Seasonal category includes our lawn & garden, summer, Christmas, toys, books, sporting goods, and other holiday departments. The Electronics & Accessories category includes the electronics, jewelry, apparel, hosiery, and infant accessories departments. See note 17 to the accompanying consolidated financial statements for the net sales results of our segments and these categories for 2013, 2012, and 2011.

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In May 2001, Big Lots, Inc. was incorporated in Ohio and was the surviving entity in a merger with Consolidated Stores Corporation, a Delaware corporation. By virtue of the merger, Big Lots, Inc. succeeded to all the business, properties, assets, and liabilities of Consolidated Stores Corporation. In July 2011, we acquired 100% of the outstanding shares of Liquidation World Inc. (now known as Big Lots Canada, Inc.).

Our principal executive offices are located at 300 Phillipi Road, Columbus, Ohio 43228, and our telephone number is (614) 278 6800.

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## Closeout Retailing

Closeout merchandise generally results from production overruns, packaging changes, discontinued products, order cancellations, liquidations, returns, and other disruptions in the supply chain of manufacturers. We can generally purchase closeout merchandise at lower costs than would be paid by traditional discount retailers, and offer closeout merchandise to our customers at lower prices than those offered by traditional discount retailers. We attempt to maximize the amount of closeout merchandise available in our stores. We work closely with our vendors to obtain brand-name closeout merchandise that is easily recognizable by our customers. In addition to closeout merchandise, we stock many products on a consistent basis that we believe provide strong value to our customers. For net sales and comparable store sales by merchandise category, see the discussion below under the captions “2013 Compared To 2012” and “2012 Compared To 2011” in “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” (“MD&A”) of this Form 10-K.

## Real Estate

The following table compares the number of our stores in operation, by segment, at the beginning and end of each of the last five fiscal years:

|  | 2013  | 2012  | 2011  | 2010  | 2009  |
|--|-------|-------|-------|-------|-------|
| U.S.                                     |       |       |       |       |       |
| Stores open at the beginning of the year | 1,495 | 1,451 | 1,398 | 1,361 | 1,339 |
| Stores opened during the year            | 55    | 87    | 92    | 80    | 52    |
| Stores acquired during the year          | —     | —     | —     | —     | —     |
| Stores closed during the year            | (57 ) | (43 ) | (39 ) | (43 ) | (30 ) |
| Stores open at the end of the year       | 1,493 | 1,495 | 1,451 | 1,398 | 1,361 |
| Canada                                   |       |       |       |       |       |
| Stores open at the beginning of the year | 79    | 82    | —     | —     | —     |
| Stores opened during the year            | 2     | —     | —     | —     | —     |
| Stores acquired during the year          | —     | —     | 89    | —     | —     |
| Stores closed during the year            | (4 )  | (3 )  | (7 )  | —     | —     |
| Stores open at the end of the year       | 77    | 79    | 82    | —     | —     |
| Consolidated                             |       |       |       |       |       |
| Stores open at the beginning of the year | 1,574 | 1,533 | 1,398 | 1,361 | 1,339 |
| Stores opened during the year            | 57    | 87    | 92    | 80    | 52    |
| Stores acquired during the year          | —     | —     | 89    | —     | —     |
| Stores closed during the year            | (61 ) | (46 ) | (46 ) | (43 ) | (30 ) |
| Stores open at the end of the year       | 1,570 | 1,574 | 1,533 | 1,398 | 1,361 |

During 2009, the U.S. commercial real estate market softened and, as a result, the availability of space improved and rental rates eased, which enabled us to experience net new store growth from 2009 through 2012. In addition, in 2011, we acquired 89 stores in Canada as a result of our acquisition of Liquidation World Inc. (subsequently named Big Lots Canada, Inc.). During the second half of 2012, we determined that rental rates had begun to stabilize, and in many markets increase, and availability of quality real estate was declining. The combination of these real estate factors, softness in our financial performance, and announced management transition plans led us to slow our net new store growth plans. Furthermore, during the fourth quarter of 2013, we finalized portions of our three-year strategic plan which led to our announcement of the Canadian Wind Down. For additional information about our real estate strategy, see the discussion under the caption “Operating Strategy - Real Estate” in the accompanying MD&A in this Form 10-K.





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The following table details our U.S. stores by state at February 1, 2014:

|             |     |                |    |                      |       |
|-------------|-----|----------------|----|----------------------|-------|
| Alabama     | 29  | Maine          | 7  | Ohio                 | 104   |
| Arizona     | 40  | Maryland       | 27 | Oklahoma             | 18    |
| Arkansas    | 12  | Massachusetts  | 20 | Oregon               | 14    |
| California  | 166 | Michigan       | 48 | Pennsylvania         | 70    |
| Colorado    | 19  | Minnesota      | 10 | Rhode Island         | 1     |
| Connecticut | 14  | Mississippi    | 14 | South Carolina       | 35    |
| Delaware    | 5   | Missouri       | 28 | South Dakota         | 1     |
| Florida     | 104 | Montana        | 2  | Tennessee            | 48    |
| Georgia     | 58  | Nebraska       | 3  | Texas                | 116   |
| Idaho       | 7   | Nevada         | 13 | Utah                 | 10    |
| Illinois    | 40  | New Hampshire  | 7  | Vermont              | 4     |
| Indiana     | 46  | New Jersey     | 25 | Virginia             | 41    |
| Iowa        | 3   | New Mexico     | 12 | Washington           | 27    |
| Kansas      | 9   | New York       | 63 | West Virginia        | 17    |
| Kentucky    | 40  | North Carolina | 74 | Wisconsin            | 14    |
| Louisiana   | 24  | North Dakota   | 1  | Wyoming              | 2     |
|             |     |                |    | District of Columbia | 1     |
|             |     |                |    | Total stores         | 1,493 |
|             |     |                |    | Number of states     | 48    |

Of the 1,493 stores in our U.S. segment, 33% operate in four states: California, Texas, Ohio, and Florida, and net sales from stores in these states represented 35% of our 2013 net sales in our U.S. segment. We have a concentration in these states based on their size, population, and customer base.

The following table details our Canadian stores by province at February 1, 2014:

|                  |    |               |    |                     |    |
|------------------|----|---------------|----|---------------------|----|
| Alberta          | 10 | New Brunswick | 2  | Saskatchewan        | 6  |
| British Columbia | 15 | Nova Scotia   | 4  |                     |    |
| Manitoba         | 4  | Ontario       | 36 |                     |    |
|                  |    |               |    | Total stores        | 77 |
|                  |    |               |    | Number of provinces | 7  |

As a result of the Canadian Wind Down, all 77 Canadian stores were closed in February 2014.

#### Associates

At February 1, 2014, we had approximately 38,100 active associates comprised of 13,100 full time and 25,000 part time associates. Of the 38,100 active associates, 36,600 were associates of our U.S. segment and 1,500 were associates of our Canadian segment. Approximately 66% of the associates employed throughout the year are employed on a part time basis. Temporary associates hired during the fall and winter holiday selling season increased the number of associates to a peak of approximately 41,400 in 2013. We consider our relationship with our associates to be good, and we are not a party to any labor agreements.

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### Competition

We operate in the highly competitive retail industry. We face strong sales competition from other general merchandise, discount, food, furniture, arts and crafts, and dollar store retailers, which operate in traditional brick and mortar stores and/or online. Additionally, we compete with a number of companies for retail site locations, to attract and retain quality employees, and to acquire our broadline merchandising assortment from vendors.

### Purchasing

An important part of our business is the sourcing and purchasing of quality closeout merchandise directly from manufacturers and other vendors typically at prices below those paid by traditional discount retailers. We believe that we have built strong relationships with many brand-name vendors and our relationships and purchasing power enable us to source merchandise that provides exceptional value to our customers. We have the ability to source and purchase significant quantities of closeout merchandise and to control distribution in accordance with vendor instructions. We believe our sourcing model, along with our strong credit profile, provides a high level of service and convenience to our vendors. We intend to continue to strengthen and deepen our relationships with our top 200 vendors. Our sourcing channels also include bankruptcies, liquidations, and insurance claims. We expect that the unpredictability of the retail and manufacturing environments coupled with what we believe is our significant purchasing power position will continue to support our ability to source quality closeout merchandise at competitive prices.

We compliment our brand-name closeout purchases with direct import and domestically-sourced merchandise, which represents merchandise that our customers expect us to consistently offer in our stores at a significant value savings.

During 2013, we purchased approximately 27% of our merchandise directly from overseas vendors, including approximately 23% from vendors located in China. Additionally, a significant amount of our domestically-purchased merchandise is manufactured abroad. As a result, a significant portion of our merchandise supply is subject to certain risks described in “Item 1A. Risk Factors” of this Form 10-K.

### Warehouse and Distribution

The majority of our merchandise offerings are processed for retail sale and distributed to our stores from our regional distribution centers. Our U.S. segment is serviced by regional distribution centers located in Pennsylvania, Ohio, Alabama, Oklahoma, and California. We selected the locations of our U.S. distribution centers in order to minimize transportation costs and the distance from distribution centers to our stores. Our Canadian segment was serviced by regional distribution centers located in British Columbia and Ontario, which were closed during the fourth quarter of 2013 in connection with our Canadian Wind Down. While certain of our merchandise vendors deliver directly to our stores, the large majority of our inventory is staged and delivered from our distribution centers to facilitate prompt and efficient distribution and transportation of merchandise to our stores and help maximize our sales and inventory turnover rate.

In addition to the regional distribution centers that handle merchandise, we operate a warehouse in Ohio that distributes fixtures and supplies to our stores.

For additional information regarding our warehouses and distribution facilities and related initiatives, see the discussion under the caption “Warehouse and Distribution” in “Item 2. Properties” of this Form 10-K.

### Advertising and Promotion

Our brand image is an important part of our marketing program. Our principal trademarks, including the Big Lots® family of trademarks, have been registered with the U.S. Patent and Trademark Office. We use a variety of marketing vehicles to promote our brand operations, including television, internet, in-store point-of-purchase, and print media.

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In all markets served by our U.S. stores, we design and distribute printed advertising circulars, through a combination of newspaper insertions and mailings. In 2013, we distributed multi-page circulars constituting 30 weeks of advertising coverage, which was consistent with promotions in multi-page circulars in 2012. We create regional versions of these circulars to tailor our advertising message to market differences caused by product availability, climate, and customer preferences. Another key element of our U.S. marketing efforts is our television campaign which combines elements of strategic branding and promotion. These same elements are also used in most of our other marketing media. Our highly-targeted media placement strategy uses national cable as the foundation of our television advertising. In addition, we use in-store promotional materials, including in store signage, to emphasize special bargains and significant values offered to our customers. As part of our overall strategic planning process coinciding with management transition, plans have been developed to shift a portion of our focus and advertising spend to social and digital media opportunities which began in the fourth quarter of 2013 and will be expanded further in 2014.

Our customer database, which we refer to as the Buzz Club® in the U.S., is an important marketing tool that allows us to communicate in a cost effective manner with our customers, including e-mail delivery of our circulars. In addition to the Buzz Club®, we operate the Buzz Club Rewards® program (“Rewards”), which allows us to send specialized promotions to targeted customer groups with the intention of reinforcing and expanding their desire to shop at our stores. Total advertising expense as a percentage of total net sales was 1.9% in each of 2013, 2012, and 2011.

## Seasonality

We have historically experienced, and expect to continue to experience, seasonal fluctuations in our sales and profitability, with a larger percentage of our net sales and operating profit realized in our fourth fiscal quarter. In addition, our quarterly net sales and operating profits can be affected by the timing of new store openings and store closings, the timing of advertising, and the timing of certain holidays. We historically receive a higher proportion of merchandise, carry higher inventory levels, and incur higher outbound shipping and payroll expenses as a percentage of sales in our third fiscal quarter in anticipation of increased sales activity during our fourth fiscal quarter. Performance of our fourth fiscal quarter typically reflects a leveraging effect which has a favorable impact on our operating results because net sales are higher and certain of our costs, such as rent and depreciation, are fixed and do not vary as sales levels escalate.

The seasonality of our net sales and related merchandise inventory requirements influences our availability of and demand for cash or access to credit. We historically have drawn upon our credit facility to assist in funding our working capital requirements, which typically peak near the end of our third fiscal quarter. We historically have higher net sales, operating profits, and cash flow provided by operations in the fourth fiscal quarter which allows us to substantially repay our seasonal borrowings. In 2013, our total indebtedness (outstanding borrowings and letters of credit) peaked in November 2013 at approximately \$358 million under our five-year \$700 million unsecured credit facility entered into in July 2011 (“2011 Credit Agreement”). At February 1, 2014, our total indebtedness under the 2011 Credit Agreement was \$82.6 million, which included \$77.0 million in borrowings and \$5.6 million in outstanding letters of credit. We expect that borrowings will vary throughout 2014 depending on various factors, including our seasonal need to acquire merchandise inventory prior to the peak selling season, the timing and amount of sales to our customers, and the cash needs of winding down the operations of our Canadian segment. For a discussion of our sources and uses of funds, see “Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities” and the discussion under the caption “Capital Resources and Liquidity” in the accompanying MD&A, in this Form 10-K.

## Available Information

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We make available, free of charge, through the “Investor Relations” section of our website ([www.biglots.com](http://www.biglots.com)) under the “SEC Filings” caption, our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended (“Exchange Act”), as soon as reasonably practicable after we file such material with, or furnish it to, the Securities and Exchange Commission (“SEC”).

In this Form 10-K, we incorporate by reference certain information from parts of our Proxy Statement for our 2014 Annual Meeting of Shareholders (“2014 Proxy Statement”).

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In the “Investor Relations” section of our website ([www.biglots.com](http://www.biglots.com)) under the “Corporate Governance” and “SEC Filings” captions, the following information relating to our corporate governance may be found: Corporate Governance Guidelines; charters of our Board of Directors’ Audit, Compensation, and Nominating/Corporate Governance Committees; and our Public Policy and Environmental Affairs Committee; Code of Business Conduct and Ethics; Code of Ethics for Financial Officers; Chief Executive Officer and Chief Financial Officer certifications related to our SEC filings; the means by which shareholders may communicate with our Board of Directors; and transactions in our securities by our directors and executive officers. The Code of Business Conduct and Ethics applies to all of our associates, including our directors and our principal executive officer, principal financial officer, and principal accounting officer. The Code of Ethics for Financial Professionals applies to our Chief Executive Officer and all other Senior Financial Officers (as that term is defined therein) and contains provisions specifically applicable to the individuals serving in those positions. We intend to post amendments to and waivers from, if any, our Code of Business Conduct and Ethics (to the extent applicable to our directors and executive officers) and our Code of Ethics for Financial Professionals in the “Investor Relations” section of our website ([www.biglots.com](http://www.biglots.com)) under the “Corporate Governance” caption. We will provide any of the foregoing information without charge upon written request to our Corporate Secretary. The contents of our websites are not part of this report.

### Item 1A. Risk Factors

The statements in this section describe the material risks to our business and should be considered carefully. In addition, these statements constitute cautionary statements under the Private Securities Litigation Reform Act of 1995.

Our disclosure and analysis in this Form 10-K and in our 2013 Annual Report to Shareholders contain forward-looking statements that set forth anticipated results based on management’s plans and assumptions. From time to time, we also provide forward-looking statements in other materials we release to the public as well as oral forward-looking statements. Such statements give our current expectations or forecasts of future events; they do not relate strictly to historical or current facts. Such statements are commonly identified by using words such as “anticipate,” “estimate,” “expect,” “objective,” “goal,” “project,” “intend,” “plan,” “believe,” “will,” “should,” “may,” “target,” “forecast,” and similar expressions in connection with any discussion of future operating or financial performance. In particular, forward-looking statements include statements relating to future actions, future performance, or results of current and anticipated products, sales efforts, expenses, interest rates, the outcome of contingencies, such as legal proceedings, and financial results.

We cannot guarantee that any forward-looking statement will be realized. Achievement of future results is subject to risks, uncertainties, and potentially inaccurate assumptions. If known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could differ materially from past results and those anticipated, estimated, or projected results set forth in the forward-looking statements. You should bear this in mind as you consider forward-looking statements.

You are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date thereof. We undertake no obligation to publicly update forward-looking statements, whether as a result of new information, future events, or otherwise. You are advised, however, to consult any further disclosures we make on related subjects in our Quarterly Reports on Form 10-Q and Current Reports on Form 8-K filed with the SEC.

The following cautionary discussion of material risks, uncertainties, and assumptions relevant to our businesses describes factors that, individually or in the aggregate, we believe could cause our actual results to differ materially from expected and historical results. Additional risks not presently known to us or that we presently believe to be immaterial also may adversely impact us. Should any risks or uncertainties develop into actual events, these developments could have material adverse effects on our business, financial condition, results of operations, and liquidity. Consequently, all of the forward-looking statements are qualified by these cautionary statements, and there

can be no assurance that the results or developments we anticipate will be realized or that they will have the expected effects on our business or operations. We note these factors for investors as permitted by the Private Securities Litigation Reform Act of 1995. There can be no assurances that we have correctly and completely identified, assessed, and accounted for all factors that do or may affect our business, financial condition, results of operations, and liquidity. as it is not possible to predict or identify all such factors. Consequently, you should not consider the following to be a complete discussion of all potential risks or uncertainties.

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Our ability to achieve the results contemplated by forward-looking statements is subject to a number of factors, any one, or a combination, of which could materially affect our business, financial condition, results of operations, or liquidity. These factors may include, but are not limited to:

The current economic conditions (including commodity price fluctuations and sustained underemployment) give rise to risks and uncertainties that may adversely affect our capital resources, financial condition, results of operations, and liquidity including, but not limited to the following:

- Fluctuating commodity prices, including but not limited to diesel fuel and other fuels used to generate power by utilities, may affect our gross profit and operating profit margins.

Our expectations regarding the demand for our merchandise may be inaccurate, which could cause us to under buy or over buy certain categories or departments of merchandise, which could result in customer dissatisfaction or require excessive markdowns to sell through the merchandise.

Our customers may experience reduced disposable income due to the implementation of new governmental programs, such as the Affordable Care Act.

The reaction of our competitors to the marketplace may drive our competitors, some of whom are better capitalized than us, to offer significant discounts or promotions on their merchandise, which could negatively affect our sales and profit margins.

If we are unable to successfully execute our operating strategies in our U.S. segment, our operating performance could be significantly impacted.

There is a risk that we will be unable to meet or exceed our operating performance targets and goals in the future if our strategies and initiatives are unsuccessful. From May through the end of 2013, we hired a new Chief Executive Officer and replaced several members of our senior leadership team. Together with our new CEO, the senior leadership team is in the process of developing a strategic plan for 2014 and beyond. Our ability to develop and execute our strategic plan and to execute the business activities associated with our strategic and operating plans, could impact our ability to meet our operating performance targets. See the accompanying MD&A in this Form 10-K for additional information concerning our operating strategy.

If we are unable to effectively and efficiently wind down the operations of our Canadian segment, our operating performance could be impacted more negatively than anticipated.

In 2011, we acquired Liquidation World Inc. in order to penetrate the Canadian retail market. In 2012, we began implementing an operating strategy in Canada similar to that of our U.S. segment. In the fourth quarter of 2013, as part of our strategic planning process under our new management team, we announced our intention to wind down the operations of our Canadian segment as our new senior leadership team and our Board of Directors determined that an orderly wind down would allow us to better focus our financial and management resources on our U.S. segment opportunities that provide a greater likelihood of more attractive long-term financial returns. If we are unable to effectively and efficiently execute our Canadian segment wind down activities, both our estimated costs and expected cash outflows could be negatively impacted (see the discussion under the caption “Critical Accounting Policies and Estimates” in the accompanying MD&A in this Form 10-K for additional information regarding our accounting policies for costs associated with exit or disposal activities).

If we are unable to compete effectively in the highly competitive discount retail industry, our business and results of operations may be materially adversely affected.

The discount retail industry, which includes both traditional brick and mortar stores and online marketplaces, is highly competitive. As discussed in Item 1 of this Form 10-K, we compete for customers, products, employees, real estate,



and other aspects of our business with a number of other companies. Certain of our competitors operate a larger number of stores and more advanced online selling capabilities than we do. Moreover, some of our competitors also have greater financial, broader distribution (e.g., more stores and a current online presence), marketing, and other resources than us. It is possible that increased competition or improved performance by our competitors may reduce our market share, gross margin, and operating margin, and may materially adversely affect our business and results of operations in other ways.

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If we are unable to compete effectively in the growing online retail marketplace, our business and results of operations may be materially adversely affected.

We are in the early stages of developing our online retailing capability and our online functionality and operations will not be fully implemented until after 2014. With the continued expansion of mobile computing devices, competition from other retailers in the online retail marketplace is expected to increase. Certain of our competitors, and a number of pure online retailers, have established online operations against which we compete for customers and products. It is possible that the increasing competition in the online retail space may reduce our market share, gross margin, and operating margin, and may materially adversely affect our business and results of operations in other ways. Our current strategic planning efforts include the development of an online retailing capability which we intend to use to increase the volume of our total net sales. Development of an online retail marketplace is a complex undertaking and there is no guarantee that the resources we apply to this effort will result in increased revenues or operating performance. If our online retailing initiatives do not meet our customers' expectations, it may reduce their desire to purchase goods from us both online and at brick and mortar stores and may materially adversely affect our business and results of operations.

Changes by vendors related to the management of their inventories may reduce the quantity and quality of brand-name closeout merchandise available to us or may increase our cost to acquire brand-name closeout merchandise, either of which may materially adversely affect our revenues and gross margin.

For the closeout merchandise that we source for our business, we have very little control over the supply, design, function, availability, or cost of many of the products that we offer for sale in our stores. Our ability to meet or exceed our operating performance targets depends upon the sufficient availability of closeout merchandise that we can acquire and offer at prices that represent a value to our customers. To the extent that certain of our vendors are better able to manage their inventory levels and reduce the amount of their excess inventory, the amount of closeout merchandise available to us could be materially reduced. Shortages or disruptions in the availability of closeout merchandise of a quality acceptable to our customers and us would likely have a material adverse effect on our sales and gross margin and may result in customer dissatisfaction.

We rely on manufacturers located in foreign countries for significant amounts of merchandise and a significant amount of our domestically-purchased merchandise is manufactured abroad. Our business may be materially adversely affected by risks associated with international trade.

Global sourcing of many of the products we sell is an important factor in driving higher operating profit. During 2013, we purchased approximately 27% of our products directly from overseas vendors including 23% from vendors located in China, and a significant amount of our domestically-purchased merchandise is manufactured abroad. Our ability to identify qualified vendors and to access products in a timely and efficient manner is a significant challenge, especially with respect to goods sourced outside of North America. Global sourcing and foreign trade involve numerous factors and uncertainties beyond our control including increased shipping costs, increased import duties, more restrictive quotas, loss of most favored nation trading status, currency and exchange rate fluctuations, work stoppages, transportation delays, economic uncertainties such as inflation, foreign government regulations, political unrest, natural disasters, war, terrorism, trade restrictions (including retaliation by the United States against foreign practices), political instability, the financial stability of vendors, merchandise quality issues, and tariffs. These and other issues affecting our international vendors could materially adversely affect our business and financial performance.

Disruption to our distribution network, the capacity of our distribution centers, and the timely receipt of merchandise inventory could adversely affect our operating performance.

We rely on our ability to replenish depleted merchandise inventory through deliveries to our distribution centers and from the distribution centers to our stores by various means of transportation, including shipments by sea, rail and truck carriers. A decrease in the capacity of carriers and/or labor strikes or shortages in the transportation industry could negatively affect our distribution network, the timely receipt of merchandise and transportation costs. In addition, long-term disruptions to the U.S. and international transportation infrastructure from wars, political unrest, terrorism, natural disasters, governmental budget constraints and other significant events that lead to delays or interruptions of service could adversely affect our business. Also, a fire, earthquake, or other disaster at one of our distribution centers could disrupt our timely receipt, processing and shipment of merchandise to our stores which could adversely affect our business. As we seek to expand our operation through the development of our online retail capabilities, we may face increased or unexpected demands on distribution center operations, as well as unexpected demands on our distribution network. In addition, our new store locations receiving shipments may be further away from our distribution centers which may increase transportation costs, accentuated by fuel prices and may create transportation scheduling strains.

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Our inability to properly manage our inventory levels and offer merchandise that our customers want may materially impact our business and financial performance.

We must maintain sufficient inventory levels to successfully operate our business. However, we also must seek to avoid accumulating excess inventory to maintain appropriate in-stock levels. We obtain approximately one quarter of our merchandise directly from vendors outside of North America. These foreign vendors often require lengthy advance notice of our requirements in order to be able to supply products in the quantities that we request. This usually requires us to order merchandise and enter into purchase order contracts for the purchase of such merchandise well in advance of the time these products are offered for sale. As a result, we may experience difficulty in responding to a changing retail environment, which makes us vulnerable to changes in price and in consumer preferences. In addition, we attempt to maximize our operating profit and operating efficiency by delivering proper quantities of merchandise to our stores in a timely manner. If we do not accurately anticipate future demand for a particular product or the time it will take to replenish inventory levels, our inventory levels may not be appropriate and our results of operations may be negatively impacted.

Declines in general economic condition, disposable income levels, and other conditions could lead to reduced consumer demand for our merchandise thereby materially affecting our revenues and gross margin.

Our results of operations can be directly impacted by the health of the economy of the United States. Our business and financial performance may be adversely impacted by current and future economic conditions, including factors that may restrict or otherwise negatively impact consumer financing, disposable income levels, unemployment levels, energy costs, interest rates, recession, inflation, the impact of unseasonable weather, natural disasters or terrorist activities and other matters that influence consumer spending. Specifically, our Soft Home, Hard Home, Home Decor & Furniture and Seasonal merchandise categories may be threatened when disposable income levels are negatively impacted by economic conditions. Additionally, the net sales of cyclical product offerings in our Seasonal category may be threatened when we experience extended periods of unseasonable weather. In particular, the economic conditions and weather patterns of four states (Ohio, Texas, California, and Florida) are important as approximately 33% of our current stores in our U.S. segment operate in these states and 35% of our 2013 net sales in our U.S. segment occurred in these states.

Changes in federal or state legislation and regulations, including the effects of legislation and regulations on product safety, could increase our cost of doing business and adversely affect our operating performance.

We are exposed to the risk that new federal or state legislation, including new product safety laws and regulations, may negatively impact our operations and adversely affect our operating performance. Additional changes in product safety legislation or regulations may lead to product recalls and the disposal or write-off of merchandise, as well as fines or penalties and reputational damage. If our merchandise, including food and consumable products, do not meet applicable governmental safety standards or our customers' expectations regarding quality or safety, we could experience lost sales, increased costs and be exposed to legal and reputational risk. Our inability to comply on a timely basis with regulatory requirements, or execute product recalls in a timely manner, could result in fines or penalties which could have a material adverse effect on our financial results. In addition, negative customer perceptions regarding the safety of the products we sell could cause us to lose market share to our competitors. If this occurs, it may be difficult for us to regain lost sales.

We may be subject to periodic litigation and regulatory proceedings, including Fair Labor Standards Act, state wage and hour, and shareholder class action lawsuits, which may adversely affect our business and financial performance.

From time to time, we are involved in lawsuits and regulatory actions, including various collective or class action lawsuits that are brought against us for alleged violations of the Fair Labor Standards Act, state wage and hour laws

and federal securities laws. We also are involved in shareholder derivative lawsuits and investigations concerning our compliance with environmental and hazardous waste regulations. Due to the inherent uncertainties of litigation, we may not be able to accurately determine the impact on us of any future adverse outcome of such proceedings. The ultimate resolution of these matters could have a material adverse impact on our financial condition, results of operations, and liquidity. In addition, regardless of the outcome, these proceedings could result in substantial cost to us and may require us to devote substantial attention and resources to defend ourselves. For a description of certain current legal proceedings, see note 10 to the accompanying consolidated financial statements.

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Our current insurance program may expose us to unexpected costs and negatively affect our financial performance.

Our insurance coverage is subject to deductibles, self-insured retentions, limits of liability and similar provisions that we believe are prudent based on the dispersion of our operations. However, we may incur certain types of losses that we cannot insure or which we believe are not economically reasonable to insure, such as losses due to acts of war, employee and certain other crime, and some natural disasters. If we incur these losses and they are material, our business could suffer. Certain material events may result in sizable losses for the insurance industry and adversely impact the availability of adequate insurance coverage or result in excessive premium increases. To offset negative cost trends in the insurance market, we may elect to self-insure, accept higher deductibles or reduce the amount of coverage in response to these market changes. In addition, we self-insure a significant portion of expected losses under our workers' compensation, general liability, including automobile, and group health insurance programs. Unanticipated changes in any applicable actuarial assumptions and management estimates underlying our recorded liabilities for these losses, including potential increases in medical and indemnity costs, could result in materially different amounts of expense than expected under these programs, which could have a material adverse effect on our financial condition and results of operations. Although we continue to maintain property insurance for catastrophic events, we are self-insured for losses up to the amount of our deductibles. With the enactment of the Affordable Care Act, we may experience an increase in participation in our group health insurance programs, which may lead to a greater number of medical claims. If we experience a greater number of self-insured losses than we anticipate, our financial performance could be adversely affected.

A significant decline in our operating profit and taxable income may impair our ability to realize the value of our long-lived assets and deferred tax assets.

We are required by accounting rules to periodically assess our property and equipment, intangible assets, and deferred tax assets for impairment and recognize an impairment loss or valuation charge, if necessary. In performing these assessments for our U.S. segment, we use our historical financial performance to determine whether we have potential impairments or valuation concerns and as evidence to support our assumptions about future financial performance. If our financial performance significantly declines, it could negatively affect the results of our assessments of the recoverability of our property and equipment, intangible assets, and our deferred tax assets and trigger the impairment of these assets. Impairment or valuation charges taken against property and equipment, intangible assets, and deferred tax assets could be material and could have a material adverse impact on our capital resources, financial condition, results of operations, and liquidity (see the discussion under the caption "Critical Accounting Policies and Estimates" in the accompanying MD&A in this Form 10-K for additional information regarding our accounting policies for long-lived assets, and income taxes).

Our inability, if any, to comply with the terms of the 2011 Credit Agreement may have a material adverse effect on our capital resources, financial condition, results of operations, and liquidity.

We have the ability to borrow funds under the 2011 Credit Agreement and we utilize this ability at various times depending on operating or other cash flow requirements. The 2011 Credit Agreement contains financial and other covenants, including, but not limited to, limitations on indebtedness, liens, and investments, as well as the maintenance of a leverage ratio and a fixed charge coverage ratio. A violation of any of these covenants may permit the lenders to restrict our ability to further access loans and letters of credit and may require the immediate repayment of any outstanding loans. Our failure to comply with these covenants may have a material adverse effect on our capital resources, financial condition, results of operations, and liquidity.

If we are unable to maintain or upgrade our computer systems or if we are unable to convert to alternate systems in an efficient and timely manner, our operations may be disrupted or become less efficient.

We depend on a variety of computer systems for the efficient functioning of our business. We rely on certain hardware, telecommunications and software vendors to maintain and periodically upgrade many of these systems so that we can continue to support our business. Various components of our computer systems, including hardware, networks, and software, are licensed to us by third party vendors. We rely extensively on our computer systems to process transactions, summarize results, and manage our business. Our computer systems are subject to damage or interruption from power outages, computer and telecommunications failures, computer viruses, cyber-attack or other security breaches, catastrophic events such as fires, floods, earthquakes, tornados, hurricanes, acts of war or terrorism, and usage errors by our employees or our contractors. If our computer systems are damaged or cease to function properly, we may have to make a significant investment to fix or replace them, and we may suffer loss of critical data and interruptions or delays in our operations as a result. Any material interruption experienced by our computer systems could negatively affect our business and results of operations. Costs and potential interruptions associated with the implementation of new or upgraded systems and technology or with maintenance or adequate support of our existing systems could disrupt or reduce the efficiency of our business.

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If we are unable to secure customer, employee, vendor and company data, our systems could be compromised, our reputation could be damaged, and we could be subject to penalties or lawsuits.

The protection of our customer, employee, vendor and company data is critical to us. The regulatory environment surrounding information security and privacy is increasingly demanding, with the frequent imposition of new and constantly changing requirements across our business. In addition, customers have a high expectation that we will adequately protect their personal information from cyber-attack or other security breaches. A significant breach of customer, employee, or company data could attract a substantial amount of negative media attention, damage our customer relationships and our reputation, and result in lost sales, fines and/or lawsuits.

If we are unable to retain existing and secure suitable new store locations under favorable lease terms, our financial performance may be negatively affected.

We lease almost all of our stores and a significant number of these leases expire or are up for renewal each year, as noted below in “Item 2. Properties” to this Form 10-K. Our strategy to improve our financial performance includes sales growth while managing the occupancy cost of each of our stores. Components of our sales growth strategy are to open new store locations, either as an expansion in an existing market or as an entrance into a new market, and to relocate certain stores to a new location within an existing market. If the commercial real estate market does not allow for us to negotiate favorable new store leases and lease renewals, our financial position, results of operations, and liquidity may be negatively affected.

If we are unable to attract, train, and retain highly qualified associates while also controlling our labor costs, our financial performance may be negatively affected.

Our customers expect a positive shopping experience, which is driven by a high level of customer service from our associates and a quality presentation of our merchandise. To grow our operations and meet the needs and expectations of our customers, we must attract, train, and retain a large number of highly qualified associates, while at the same time control labor costs. We compete with other retail businesses for many of our associates in hourly and part-time positions. These positions have historically had high turnover rates, which can lead to increased training and retention costs. In addition, our ability to control labor costs is subject to numerous external factors, including prevailing wage rates, the impact of legislation or regulations governing labor relations or benefits, such as the Affordable Care Act, and health insurance costs.

The loss of key personnel may have a material impact on our future results of operations.

We believe that we benefit substantially from the leadership and experience of our senior executives. During 2013, we hired a new Chief Executive Officer and several other senior leadership team members. The loss of services of any of these individuals could have a material adverse impact on our business. Competition for key personnel in the retail industry is intense and our future success will depend on our ability to recruit, train, and retain our senior executives and other qualified personnel.

Changes in accounting guidance could significantly affect our results of operations and the presentation of those results.

Changes in accounting standards, including new interpretations and applications of accounting standards, may have adverse effects on our financial condition, results of operations, and liquidity. The governing accounting bodies, specifically the Financial Accounting Standards Board (“FASB”), have issued new guidance that proposes numerous significant changes to current accounting standards. This new guidance could significantly change the presentation of financial information and our results of operations. Additionally, the new guidance may require us to make systems



and other changes that could increase our operating costs. Specifically, implementing future accounting guidance related to leases and other areas impacted by the convergence projects between the FASB and the International Accounting Standards Board (“IASB”) could require us to make significant changes to our lease management system or other accounting systems.

The price of our common shares as traded on the New York Stock Exchange may be volatile.

Our stock price may fluctuate substantially as a result of factors beyond our control, including but not limited to, general economic and stock market conditions, risks relating to our business and industry as discussed above, strategic actions by us or our competitors, variations in our quarterly operating performance, our future sales or purchases of our common shares, and investor perceptions of the investment opportunity associated with our common shares relative to other investment alternatives.

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We also may be subject to a number of other factors which may, individually or in the aggregate, materially or adversely affect our business. These factors include, but are not limited to:

- Changes in governmental laws and regulations, including matters related to taxation;
- A downgrade in our credit rating could negatively affect our ability to access capital or could increase our borrowing costs;
- Events or circumstances could occur which could create bad publicity for us or for types of merchandise offered in our stores which may negatively impact our business results including our sales;
- Infringement of our intellectual property, including the Big Lots trademarks, could dilute their value;
- Other risks described from time to time in our filings with the SEC.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

Retail Operations

All of our stores are located in North America, predominantly in strip shopping centers. Our stores in our U.S. segment have an average store size of approximately 30,600 square feet, of which an average of 21,900 is selling square feet. For additional information about the properties in our retail operations, see the discussion under the caption “Real Estate” in Item 1. Business in this Form 10-K.

The average cost to open a new store in a leased facility during 2013 was approximately \$1.3 million, including the cost of inventory. Except for 55 owned sites in our U.S. segment, all of our stores are leased. In 2013, we sold one store property for a price of \$5.1 million. Additionally, we still own one site, which we closed in 2012, for which we have not yet completed the sale transaction. Since this owned site is no longer operating as an active store, it has been excluded from our store counts at February 1, 2014. The 55 owned stores are located in the following states:

| State      | Stores Owned |
|------------|--------------|
| Arizona    | 2            |
| California | 39           |
| Colorado   | 3            |
| Florida    | 3            |
| Louisiana  | 1            |
| Michigan   | 1            |
| New Mexico | 2            |
| Ohio       | 1            |
| Texas      | 3            |
| Total      | 55           |

Store leases generally obligate us for fixed monthly rental payments plus the payment, in most cases, of our applicable portion of real estate taxes, common area maintenance costs (“CAM”), and property insurance. Some leases require the payment of a percentage of sales in addition to minimum rent. Such payments generally are required only when sales exceed a specified level. Our typical store lease is for an initial minimum term of five to ten years with multiple five-year renewal options. Sixty-nine store leases have sales termination clauses which can result in our exiting a location at our option if certain sales volume results are not achieved.



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The following table summarizes the number of store lease expirations, by segment, in each of the next five fiscal years and the total thereafter. In addition, as stated above, many of our store leases have renewal options. The table also includes the number of leases, within our U.S. segment, that are scheduled to expire each year that do not have a renewal option. The information includes stores with more than one lease and leases for stores not yet open. It excludes 17 month-to-month leases and 55 owned locations.

| Fiscal Year: | Expiring Leases |        |       | Leases Without Options |
|--------------|-----------------|--------|-------|------------------------|
|              | U.S.            | Canada | Total | U.S.                   |
| 2014         | 285             | 10     | 295   | 54                     |
| 2015         | 248             | 9      | 257   | 42                     |
| 2016         | 274             | 12     | 286   | 48                     |
| 2017         | 197             | 22     | 219   | 33                     |
| 2018         | 247             | 3      | 250   | 46                     |
| Thereafter   | 190             | 21     | 211   | 17                     |

## Warehouse and Distribution

At February 1, 2014, we owned or leased approximately 9.5 million square feet of distribution center and warehouse space. We own and operate five regional distribution centers strategically located across the United States in Ohio, California, Alabama, Oklahoma, and Pennsylvania. In Canada, at February 1, 2014, we leased two regional distribution centers located in British Columbia and one located in Ontario, all of which we closed during the fourth quarter of 2013 as part of the Canadian Wind Down. The regional distribution centers in our U.S. segment utilize warehouse management technology, which we believe enables high accuracy and efficient processing of merchandise from vendors to our retail stores. The combined output of our regional distribution centers in our U.S. segment was approximately 2.7 million cartons per week in 2013. Certain vendors deliver merchandise directly to our stores when it supports our operational goal to deliver merchandise from our vendors to the sales floor in the most efficient manner.

The number of owned and leased distribution centers and warehouse space and the corresponding square footage of the facilities by state and province at February 1, 2014, were as follows:

| State / Province              | Owned | Leased | Total | Square Footage |        |       |
|-------------------------------|-------|--------|-------|----------------|--------|-------|
|                               |       |        |       | Owned          | Leased | Total |
| (Square footage in thousands) |       |        |       |                |        |       |
| U.S. segment:                 |       |        |       |                |        |       |
| Ohio                          | 1     | —      | 1     | 3,559          | —      | 3,559 |
| California                    | 1     | —      | 1     | 1,423          | —      | 1,423 |
| Alabama                       | 1     | —      | 1     | 1,411          | —      | 1,411 |
| Oklahoma                      | 1     | —      | 1     | 1,297          | —      | 1,297 |
| Pennsylvania                  | 1     | —      | 1     | 1,295          | —      | 1,295 |
| Sub-total                     | 5     | —      | 5     | 8,985          | —      | 8,985 |
| Canadian segment:             |       |        |       |                |        |       |
| British Columbia              | —     | 2      | 2     | —              | 229    | 229   |
| Ontario                       | —     | 1      | 1     | —              | 261    | 261   |
| Sub-total                     | —     | 3      | 3     | —              | 490    | 490   |
| Total                         | 5     | 3      | 8     | 8,985          | 490    | 9,475 |



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## Corporate Offices

We own the facility in Columbus, Ohio that serves as our corporate office for our U.S. associates. We lease the facility in Brantford, Ontario that serves as our corporate office for our Canadian associates. As part of the Canadian Wind Down, we intend to close our office in Brantford, Ontario in the first quarter of 2014.

## Item 3. Legal Proceedings

Item 103 of SEC Regulation S-K requires that we disclose actual or known contemplated legal proceedings to which a governmental authority and we are each a party and that arise under laws dealing with the discharge of materials into the environment or the protection of the environment, if the proceeding reasonably involves potential monetary sanctions of \$100,000 or more. Accordingly, please refer to the discussion in note 10 to the accompanying consolidated financial statements regarding the subpoena we received from the District Attorney for the County of Alameda, State of California.

Aside from this matter, no response is required under Item 103 of Regulation S-K. For a discussion of certain litigated matters, also see note 10 to the accompanying consolidated financial statements

## Item 4. Mine Safety Disclosures

None.

## Supplemental Item. Executive Officers of the Registrant

Our executive officers at February 1, 2014 were as follows:

| Name                  | Age | Offices Held  | Officer Since |
|-----------------------|-----|---|---------------|
| David J. Campisi      | 57  | Chief Executive Officer and President                           | 2013          |
| Lisa M. Bachmann      | 52  | Executive Vice President, Chief Operating Officer               | 2002          |
| Richard R. Chene      | 51  | Executive Vice President, Chief Merchandising Officer           | 2013          |
| Joe R. Cooper         | 56  | Executive Vice President and President, Big Lots Canada, Inc.   | 2000          |
| Timothy A. Johnson    | 46  | Executive Vice President, Chief Financial Officer               | 2004          |
| Lucy Cindric          | 58  | Senior Vice President, General Merchandise Manager              | 2013          |
| Leslie R. Johnson III | 50  | Senior Vice President, General Merchandise Manager              | 2013          |
| Ronald D. Parisotto   | 49  | Senior Vice President, General Counsel and Corporate Secretary  | 2014          |
| Carlos V. Rodriguez   | 46  | Senior Vice President, Distribution and Transportation Services | 2012          |
| Michael A. Schlonsky  | 47  | Senior Vice President, Human Resources                          | 2000          |
| Andrew D. Stein       | 48  | Senior Vice President, Chief Customer Officer                   | 2013          |
| Stewart W. Wenerstrom | 47  | Senior Vice President, Chief Information Officer                | 2005          |
| Martha Withers-Hall   | 60  | Senior Vice President, General Merchandise Manager              | 2013          |
| Paul A. Schroeder     | 48  | Vice President, Controller                                      | 2005          |

David J. Campisi is our Chief Executive Officer and President. Before joining Big Lots in May 2013, Mr. Campisi served as the Chairman and Chief Executive Officer of Respect Your Universe, Inc., an activewear retailer. Mr. Campisi previously served as the Chairman, President and Chief Executive Officer of The Sports Authority, Inc., a sporting goods retailer. Prior to that, Mr. Campisi served as Executive Vice President and General Merchandise Manager, Women's Apparel, Accessories, Intimates and Cosmetics of Kohl's Corporation, a department store retailer. Additionally, Mr. Campisi served as Senior Vice President and General Merchandise Manager, Apparel, Home, and Home Electronics of Fred Meyer's Corporation, a department store retailer.



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Lisa M. Bachmann is responsible for store operations, information technology, merchandise planning and allocation, and distribution and transportation services. Ms. Bachmann was promoted to Executive Vice President, Chief Operating Officer in August 2012, and assumed responsibility for store operations. Ms. Bachmann was promoted to Executive Vice President, Supply Chain Management and Chief Information Officer in March 2010 and assumed responsibility for distribution and transportation services. Ms. Bachmann assumed responsibility for information technology in 2005. Ms. Bachmann joined us as Senior Vice President, Merchandise Planning, Allocation and Presentation in March 2002. Prior to joining us, Ms. Bachmann was Senior Vice President of Planning and Allocation of Ames Department Stores, Inc., a discount retailer.

Richard R. Chene is responsible for merchandising and global sourcing. Mr. Chene joined us in 2013 as Executive Vice President, Chief Merchandising Officer. Prior to joining us, Mr. Chene was the President of The Kitchen Collection, a kitchenware retailer, which operates kitchenware stores and Vice President, General Merchandise Manager of Petco Animal Supplies, Inc., a pet store retailer. Additionally, Mr. Chene has served as a divisional merchandise manager at Sears Holdings Corporation, Giant Eagle, Inc., and May Department Stores, Co., which are general merchandise and grocery retailers.

Joe R. Cooper is responsible for our Canadian operations. Mr. Cooper was appointed President of Big Lots Canada, Inc. in July 2011. Mr. Cooper was promoted to Executive Vice President in March 2010. Prior to that, Mr. Cooper was promoted to Senior Vice President and Chief Financial Officer in February 2004. Mr. Cooper joined us as Vice President of Strategic Planning and Investor Relations in May 2000. In July 2000, he assumed responsibility for the treasury department and was appointed Vice President, Treasurer.

Timothy A. Johnson is responsible for financial reporting and controls, financial planning and analysis, treasury, risk management, tax, internal audit, investor relations, real estate and asset protection. Mr. Johnson was promoted to Executive Vice President, Chief Financial Officer in March 2014. Mr. Johnson assumed responsibility for real estate in June of 2013 and asset protection in November 2013. Mr. Johnson was promoted to Senior Vice President, Chief Financial Officer in August 2012, and assumed responsibility for our treasury and risk management. He was promoted to Senior Vice President of Finance in July 2011 after serving as Vice President of Strategic Planning and Investor Relations since January 2004. He joined us in August 2000 as Director of Strategic Planning. Prior to joining us, Mr. Johnson held various positions of increasing responsibility at The Limited, Inc, culminating in his last position as Director of Financial Reporting for Structure, a former division of The Limited, Inc, an apparel retailer.

Lucy Cindric is responsible for merchandising in our Seasonal and Electronics & Accessories merchandise categories. Ms. Cindric joined us in 2013 as Senior Vice President, General Merchandise Manager for our Seasonal and Electronics merchandise categories. Prior to joining us, Ms. Cindric held various senior merchandising positions, including Senior Vice President, General Merchandise Manager, with Stage Stores, Inc., a department store retailer. Additionally, Ms. Cindric served as Senior Vice President and General Merchandise Manager, Apparel and Home at Wal-Mart Stores, Inc., a discount retailer.

Leslie R. Johnson III is responsible for merchandising in our Food and Consumables merchandise categories. Mr. Johnson joined us in 2013 as Vice President, Divisional Merchandise Manager for the food category and was promoted to Senior Vice President, General Merchandise Manager for our Food and Consumables merchandise categories in 2013. Prior to joining us, Mr. Johnson held various senior merchandising positions with Family Dollar, Inc. a discount retailer and Sears Holding Corporation, a department store retailer.

Ronald D. Parisotto is responsible for legal affairs. Mr. Parisotto joined us in 2014 as Senior Vice President, General Counsel and Corporate Secretary. Prior to joining us, Mr. Parisotto was the Senior Vice President, General Counsel, Corporate Secretary and Chief Compliance Officer with Choice Hotels International, a global hotel franchising company.



Carlos V. Rodriguez is responsible for warehousing, distributing, and transporting merchandise. Mr. Rodriguez joined us in 2012 as Senior Vice President, Distribution and Transportation Services. Prior to joining us, Mr. Rodriguez held various supply chain management positions, including Vice President, Supply Chain Operations, with Office Depot, Inc., an office supply retailer.

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Michael A. Schlonsky is responsible for talent management and oversight of human resources. He was promoted to Senior Vice President, Human Resources in August 2012. Mr. Schlonsky was promoted to Vice President, Associate Relations and Benefits in 2010 and assumed responsibility for compensation in 2011. Prior to that, Mr. Schlonsky was promoted to Vice President, Associate Relations and Risk Management in 2005. Mr. Schlonsky joined us in 1993 as Staff Counsel and was promoted to Director, Risk Management in 1998, and to Vice President, Risk Management and Administrative Services in 2000.

Andrew D. Stein is responsible for marketing, advertising, brand development and merchandise presentation. Mr. Stein joined us in 2013 as Senior Vice President, Chief Customer Officer. Prior to joining us, Mr. Stein was the Chief Marketing Officer at Kmart, a division of Sears Holding Corporation, a retailer.

Stewart W. Wenerstrom is responsible for information technology. Mr. Wenerstrom was promoted to Senior Vice President, Chief Information Officer in 2013. He was promoted to Vice President, Program Management Office in 2012. Prior to that, Mr. Wenerstrom was promoted to Vice President, Merchandise Support in 2007 and prior to that he was promoted to Vice President, Furniture Allocation and Replenishment in 2005. He joined us in 2003 as Director, Merchandise Information Office. Prior to joining us, Mr. Wenerstrom was as associate partner with Accenture, a consulting firm.

Martha Withers-Hall is responsible for merchandising in our Soft Home, Hard Home, and Home Décor & Furniture merchandise categories. Ms. Withers-Hall joined us in 2013 as Senior Vice President, General Merchandise Manager for our Furniture and Home merchandise categories. Prior to joining us, Ms. Withers-Hall held various senior merchandising positions, including Senior Vice President, General Merchandise Manager, with Stage Stores, Inc., a department store retailer and Senior Vice President, General Merchandise Manager with Stein Mart, Inc., a discount clothing, accessories and housewares retailer.

Paul A. Schroeder is responsible for internal and external financial reporting and accounting operations including payroll, accounts payable, and inventory control. Mr. Schroeder joined us as Director, Accounting Operations in April 2005, and was promoted to Vice President, Controller in September 2005. Prior to joining us, Mr. Schroeder was Director of Finance at American Signature, Inc., a furniture retailer, and held various finance positions with Limited Brands, Inc., a retailer.

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## Part II. Other Information

## Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common shares are listed on the New York Stock Exchange ("NYSE") under the symbol "BIG." The following table reflects the high and low sales prices per common share for our common shares as reported on the NYSE composite tape for the fiscal periods indicated:

|                | 2013    |         | 2012    |         |
|----------------|---------|---------|---------|---------|
|                | High    | Low     | High    | Low     |
| First Quarter  | \$37.81 | \$32.07 | \$47.22 | \$34.46 |
| Second Quarter | 39.22   | 31.17   | 41.42   | 33.50   |
| Third Quarter  | 37.98   | 31.56   | 42.26   | 28.46   |
| Fourth Quarter | \$39.02 | \$26.49 | \$32.66 | \$26.69 |

Our Board of Directors historically has authorized reinvesting available cash in capital expenditures for growth opportunities, improving the Company's information systems, and maintaining our assets. After making such investments, the Company has utilized its excess cash for share repurchase programs. We historically have not paid dividends. Any future decisions on the uses of excess cash will be determined by our Board of Directors taking into account business conditions then existing, including our earnings, financial requirements and condition, opportunities for reinvesting cash, and other factors.

The following table sets forth information regarding our repurchase of our common shares during the fourth fiscal quarter of 2013:

(In thousands, except price per share data)

| Period                               | (a) Total Number of Shares Purchased | (b) Average Price Paid per Share | (c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | (d) Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs |
|--------------------------------------|--------------------------------------|----------------------------------|--|--|
| November 3, 2013 - November 30, 2013 | —                                    | \$—                              | —  | \$—  |
| December 1, 2013 - December 28, 2013 | —                                    | —                                | —  | —  |
| December 29, 2013 - February 1, 2014 | —                                    | —                                | —  | —  |
| Total                                | —                                    | \$—                              | —  | \$—  |

On March 5, 2014, our Board of Directors authorized a program for the repurchase of up to \$125.0 million of our common shares ("2014 Repurchase Program"). The 2014 Repurchase Program has no scheduled termination date.

At the close of trading on the NYSE on March 28, 2014, there were approximately 794 registered holders of record of our common shares.

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The following graph and table compares, for the five fiscal years ended February 1, 2014, the cumulative total shareholder return for our common shares, the S&P 500 Index, and the S&P 500 Retailing Index. Measurement points are the last trading day of each of our fiscal years ended January 30, 2010, January 29, 2011, January 28, 2012, February 2, 2013 and February 1, 2014. The graph and table assume that \$100 was invested on January 31, 2009, in each of our common shares, the S&P 500 Index, and the S&P 500 Retailing Index and reinvestment of any dividends. The stock price performance on the following graph and table is not necessarily indicative of future stock price performance.

| Company / Index         | Indexed Returns |           |           |           |           |           |
|-------------------------|-----------------|-----------|-----------|-----------|-----------|-----------|
|                         | Years Ended     |           |           |           |           |           |
|                         | Base            |           |           |           |           |           |
|                         | Period          |           |           |           |           |           |
|                         | January         | January   | January   | January   | January   | January   |
|                         | 2009            | 2010      | 2011      | 2012      | 2013      | 2014      |
| Big Lots, Inc.          | \$ 100.00       | \$ 211.23 | \$ 236.58 | \$ 297.40 | \$ 240.45 | \$ 199.18 |
| S&P 500 Index           | 100.00          | 133.14    | 161.44    | 170.03    | 199.96    | 240.88    |
| S&P 500 Retailing Index | \$ 100.00       | \$ 155.55 | \$ 197.80 | \$ 224.34 | \$ 285.12 | \$ 357.39 |

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## Item 6. Selected Financial Data

The following statements of operations and balance sheet data have been derived from our consolidated financial statements and should be read in conjunction with MD&A and the consolidated financial statements and related notes included herein.

| (In thousands, except per share amounts and store counts)                | Fiscal Year <sup>(d)</sup> |                         |                         |                     |                     |
|--|----------------------------|-------------------------|-------------------------|---------------------|---------------------|
|  | 2013 <sup>(a) (c)</sup>    | 2012 <sup>(b) (c)</sup> | 2011 <sup>(a) (c)</sup> | 2010 <sup>(a)</sup> | 2009 <sup>(a)</sup> |
| Net sales  | \$5,301,912                | \$5,367,165             | \$5,159,249             | \$4,905,631         | \$4,675,575         |
| Cost of sales (exclusive of depreciation expense shown separately below) | 3,236,606                  | 3,254,837               | 3,096,200               | 2,904,600           | 2,768,866           |
| Gross margin   | 2,065,306                  | 2,112,328               | 2,063,049               | 2,001,031           | 1,906,709           |
| Selling and administrative expenses                                      | 1,759,745                  | 1,708,160               | 1,629,218               | 1,569,271           | 1,525,074           |
| Depreciation expense   | 115,122                    | 106,137                 | 90,135                  | 78,540              | 74,822              |
| Gain on sale of real estate  | —                          | —                       | —                       | —                   | (12,964 )           |
| Operating profit   | 190,439                    | 298,031                 | 343,696                 | 353,220             | 319,777             |
| Interest expense   | (3,339 )                   | (4,192 )                | (3,530 )                | (2,573 )            | (1,840 )            |
| Other income (expense)   | (1,213 )                   | 51                      | (173 )                  | 612                 | 175                 |
| Income from continuing operations before income taxes                    | 185,887                    | 293,890                 | 339,993                 | 351,259             | 318,112             |
| Income tax expense   | 61,118                     | 116,921                 | 133,835                 | 131,132             | 119,852             |
| Income from continuing operations  | 124,769                    | 176,969                 | 206,158                 | 220,127             | 198,260             |
| Income from discontinued operations, net of tax                          | 526                        | 152                     | 906                     | 2,397               | 2,109               |
| Net income   | \$125,295                  | \$177,121               | \$207,064               | \$222,524           | \$200,369           |
| Earnings per common share - basic:                                       |                            |                         |                         |                     |                     |
| Continuing operations  | \$2.17                     | \$2.96                  | \$3.02                  | \$2.84              | \$2.43              |
| Discontinued operations  | 0.01                       | —                       | 0.01                    | 0.03                | 0.03                |
|  | \$2.18                     | \$2.96                  | \$3.03                  | \$2.87              | \$2.45              |
| Earnings per common share - diluted:                                     |                            |                         |                         |                     |                     |
| Continuing operations  | \$2.15                     | \$2.93                  | \$2.97                  | \$2.80              | \$2.40              |
| Discontinued operations  | 0.01                       | —                       | 0.01                    | 0.03                | 0.03                |
|  | \$2.16                     | \$2.93                  | \$2.98                  | \$2.83              | \$2.42              |
| Weighted-average common shares outstanding:                              |                            |                         |                         |                     |                     |
| Basic  | 57,415                     | 59,852                  | 68,316                  | 77,596              | 81,619              |
| Diluted  | 57,958                     | 60,476                  | 69,419                  | 78,581              | 82,681              |
| Balance sheet data:  |                            |                         |                         |                     |                     |
| Total assets   | \$1,739,599                | \$1,753,626             | \$1,641,310             | \$1,619,599         | \$1,669,493         |
| Working capital  | 543,614                    | 460,996                 | 421,836                 | 509,788             | 580,446             |
| Cash and cash equivalents  | 68,629                     | 60,581                  | 68,547                  | 177,539             | 283,733             |
| Long-term obligations under bank credit facility                         | 77,000                     | 171,200                 | 65,900                  | —                   | —                   |
| Shareholders' equity   | \$901,427                  | \$758,142               | \$823,233               | \$946,793           | \$1,001,412         |
| Cash flow data:  |                            |                         |                         |                     |                     |
| Cash provided by operating activities                                    | \$198,334                  | \$281,133               | \$318,471               | \$315,257           | \$392,026           |
| Cash used in investing activities  | \$(97,495 )                | \$(130,357 )            | \$(120,712 )            | \$(114,552 )        | \$(77,937 )         |
| Store data:  |                            |                         |                         |                     |                     |
| Total gross square footage   | 47,489                     | 47,376                  | 45,780                  | 42,037              | 40,591              |
| Total selling square footage   | 34,255                     | 34,267                  | 33,119                  | 30,210              | 29,176              |
| Stores opened during the fiscal year                                     | 57                         | 87                      | 92                      | 80                  | 52                  |
| Stores acquired during the fiscal year                                   | —                          | —                       | 89                      | —                   | —                   |

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|                                       |       |   |       |   |       |   |       |   |       |   |
|---------------------------------------|-------|---|-------|---|-------|---|-------|---|-------|---|
| Stores closed during the fiscal year  | (61   | ) | (46   | ) | (46   | ) | (43   | ) | (30   | ) |
| Stores open at end of the fiscal year | 1,570 |   | 1,574 |   | 1,533 |   | 1,398 |   | 1,361 |   |

(a) The period presented is comprised of 52 weeks.

(b) The period presented is comprised of 53 weeks.

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(c) On July 18, 2011, we completed our acquisition of Liquidation World Inc. (now known as Big Lots Canada, Inc.), whose results are included in the consolidated results since that date.

In the fourth quarter of 2013, we ceased the operations of our wholesale business; therefore, the results of (d) operations for all fiscal years presented have been reclassified to reflect the discontinuance of the wholesale business.

## Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Overview

The discussion and analysis presented below should be read in conjunction with the accompanying consolidated financial statements and related notes. Please refer to "Item 1A. Risk Factors" of this Form 10-K for a discussion of forward-looking statements and certain risk factors that may have a material adverse effect on our business, financial condition, results of operations, and/or liquidity.

Our fiscal year ends on the Saturday nearest to January 31, which results in some fiscal years with 52 weeks and some with 53 weeks. Fiscal years 2013 and 2011 were each comprised of 52 weeks. Fiscal year 2012 was comprised of 53 weeks. Fiscal year 2014 will be comprised of 52 weeks.

### Operating Results Summary

The following are the results from 2013 that we believe are key indicators of both our consolidated and segment operating performance when compared to 2012.

#### Consolidated Highlights

Net sales decreased \$65.3 million, or 1.2%.

Diluted earnings per common share from continuing operations decreased from \$2.93 in 2012 to \$2.15 in 2013.

Our 2013 results included the impact of the Canadian Wind Down, which involved an aggregate of \$23.7 million in impairments, severance charges, and contract termination costs and increased markdowns to begin liquidating our inventory, offset by a \$23.9 million U.S. deferred tax benefit.

Our 2012 results included the impact of a non-cash, non-recurring charge of \$0.06 per diluted share related to a change in accounting principle associated with the implementation of our new retail inventory systems in the U.S.

Inventory decreased by 0.3%, or \$3.1 million, to \$915.0 million in 2013.

#### U.S. Segment Highlights

Net sales decreased \$87.6 million or 1.7%.

Comparable store sales for stores open at least fifteen months decreased 2.7%.

Gross margin dollars decreased \$47.3 million and gross margin rate decreased 20 basis points from 39.4% to 39.2% of sales.

Selling and administrative expenses increased \$24.4 million. As a percentage of net sales, selling and administrative expenses increased 100 basis points to 32.5% of sales.

Operating profit rate decreased 150 basis points to 4.5%.

#### Canadian Segment Highlights

In the fourth quarter of 2013, we announced the Canadian Wind Down was to substantially occur during the first quarter of 2014.

Costs associated with the Canadian Wind Down are estimated to range from \$60 million to \$64 million, of which \$24 million were incurred in 2013.





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The following table compares components of our consolidated statements of operations as a percentage of net sales:

|  | 2013  | 2012    | 2011    |   |
|--|-------|---------|---------|---|
| Net sales  | 100.0 | % 100.0 | % 100.0 | % |
| Cost of sales (exclusive of depreciation expense shown separately below) | 61.0  | 60.6    | 60.0    |   |
| Gross margin   | 39.0  | 39.4    | 40.0    |   |
| Selling and administrative expenses                                      | 33.2  | 31.8    | 31.6    |   |
| Depreciation expense   | 2.2   | 2.0     | 1.7     |   |
| Operating profit   | 3.6   | 5.6     | 6.7     |   |
| Interest expense   | (0.1  | ) (0.1  | ) (0.1  | ) |
| Other income (expense)   | (0.0  | ) 0.0   | (0.0    | ) |
| Income from continuing operations before income taxes                    | 3.5   | 5.5     | 6.6     |   |
| Income tax expense   | 1.2   | 2.2     | 2.6     |   |
| Income from continuing operations  | 2.4   | 3.3     | 4.0     |   |
| Loss from discontinued operations, net of tax                            | 0.0   | 0.0     | 0.0     |   |
| Net income   | 2.4   | % 3.3   | % 4.0   | % |

See the discussion below under the captions “2013 Compared To 2012” and “2012 Compared To 2011” for additional details regarding the specific components of our operating results.

In December 2013, we announced the Canadian Wind Down would begin in the fourth quarter of 2013 and continue through the first quarter of 2014. During 2013, we recorded \$19.7 million in charges associated with the impairment of the property and equipment, goodwill, and certain intangible assets relating to our Canadian segment, \$2.7 million in severance charges associated with the closing of our Canadian distribution centers and certain functions within our Canadian administrative offices, and \$1.3 million in contract termination costs associated with the operating leases of our distribution centers. Please see note 13 to the accompanying consolidated financial statements for a more detailed discussion regarding the Canadian Wind Down activities. Additionally, in 2013, we recorded a \$23.9 million U.S. deferred tax benefit associated with the excess tax basis related to our investment in our Canadian segment.

In 2013, our selling and administrative expenses include a \$4.4 million charge associated with the settlement of a legal matter, which was partially offset by a \$3.6 million gain on the sale of a company-owned property in California.

In 2012, the cost of sales increase included a charge of \$5.6 million (0.1% of net sales) due to a change in accounting principle resulting from our successful implementation of new retail inventory management systems. This non-cash charge reduced both income from continuing operations and net income by \$3.4 million, or 10 basis points. Please see note 1 to the accompanying consolidated financial statements for a more detailed discussion regarding this change in accounting principle.

### Seasonality

As discussed in “Item 1. Business - Seasonality” of this Form 10-K, our financial results fluctuate from quarter to quarter depending on various factors such as the timing of new or closed stores, the timing and extent of advertisements and promotions, and the timing of holidays. We expect the Christmas holiday selling season to continue to produce a significant portion of our sales and operating profits. If our sales performance is significantly better or worse during the Christmas holiday selling season, we would expect a more pronounced impact on our annual financial results than if our sales performance is significantly better or worse in a different season.



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The following table sets forth the seasonality of net sales and operating profit for 2013, 2012, and 2011 by fiscal quarter:

|   | First | Second | Third  | Fourth |   |
|---|-------|--------|--------|--------|---|
| Fiscal Year 2013                              |       |        |        |        |   |
| Net sales as a percentage of full year        | 24.6  | % 23.0 | % 21.5 | % 30.9 | % |
| Operating profit as a percentage of full year | 30.0  | 17.2   | (4.0)  | ) 56.8 |   |
| Fiscal Year 2012                              |       |        |        |        |   |
| Net sales as a percentage of full year        | 24.0  | % 22.6 | % 20.9 | % 32.5 | % |
| Operating profit as a percentage of full year | 23.1  | 13.3   | (2.4)  | ) 66.0 |   |
| Fiscal Year 2011                              |       |        |        |        |   |
| Net sales as a percentage of full year        | 23.6  | % 22.4 | % 21.8 | % 32.2 | % |
| Operating profit as a percentage of full year | 24.9  | 17.1   | 2.3    | 55.7   |   |

## Operating Strategy

In May of 2013, Mr. Campisi joined us as our Chief Executive Officer and President. Under Mr. Campisi's leadership, we reevaluated the key components of our operating strategy, the organization's leadership and structure, and the businesses that we operated. After performing his review, Mr. Campisi and the senior management team introduced our new operating strategy, the Edit to Amplify strategy ("Edit to Amplify"), which applies to all aspects of our business, but has a particular focus on merchandising, marketing, and our customers' shopping experience, all of which we believe are the key drivers of our net sales. Edit to Amplify is a strategy that focuses our entire attention on our core customer. We believe our Edit to Amplify strategy will help us to exceed the expectations of our core customer, to whom we refer as Jennifer, by adopting a customer-first mentality and delivering a product assortment that meets her everyday needs while delivering excitement and surprises aimed to drive discretionary purchases. The following sections provide additional discussion and analysis of our Edit to Amplify strategy. During this transition period, as we embrace this new focus for our business, we anticipate in 2014:

Earnings per diluted share from continuing operations to be \$2.25 to \$2.45 for our U.S. segment.

Our earnings per diluted share from continuing operations assumes the Canadian Wind Down and the related reclassification of the results of our Canadian segment to discontinued operations. We anticipate a loss from discontinued operations in the range of \$37 million to \$41 million, or \$0.64 to \$0.71 per diluted share.

- Net sales for our U.S. segment will be in the range of flat to a slight decrease driven by comparable stores sales in the range of flat to an increase of 2%, partially offset by a lower expected store count.

• Opening 30 new stores and closing 50 stores in our U.S. segment.

• Cash flow (operating activities less investing activities) of approximately \$140 million for future reinvestment, return to shareholders, and / or to lower our obligations under the 2011 Credit Agreement.

Forecasting U.S. segment cash flow of \$165 million.

Our forecasted cash flow also includes payments of \$25 million associated with the Canadian Wind Down.

In March, our Board of Directors authorized the repurchase of up to \$125 million of our common shares, which is expected to be funded by our \$140 million of cash flow.

The "2013 Compared To 2012" section below provides additional discussion and analysis of our financial performance and the assumptions and expectations upon which we are basing our guidance for our future results.

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### U.S. Segment

#### Merchandising

The goal of exceeding our core customer's expectations will be driven by the delivery of a product assortment that is meaningful to our core customer, combined with the quality and ease of the shopping experience. Our Edit to Amplify strategy focuses on the two separate "Edit" and "Amplify" components to achieve our goal of exceeding our core customer's expectations. The "Edit" component focuses on continuously evaluating our product mix and downsizing, or potentially eliminating, those departments within our merchandise categories and product offerings which we believe are not top of mind with our core customer and we do not maintain a competitive advantage. The "Amplify" component of our Edit to Amplify strategy seeks to expand the assortment of those departments within our merchandise categories and product offerings that we believe are important to our core customer's shopping experience and with respect to which we believe we have a competitive advantage in pricing and sourcing. In the fourth quarter of 2013, we made significant changes to our merchandising team to execute our new strategy and we restructured our merchandise categories to: Food, Consumables, Soft Home, Hard Home, Furniture & Home Décor, Seasonal, and Electronics & Accessories. We believe the restructured merchandise categories better align our business with how our core customer shops our stores. Our restructured categories place differing emphasis on essential items (needs) and discretionary items (wants).

Our Food and Consumables categories will focus primarily on catering to our core customers' daily essentials, or "need, use, buy most" items. We believe our competitive advantage in the Food and Consumables categories revolves around our sourcing capabilities for closeout merchandise. Manufacturers and vendors have closeout merchandise for a number of different reasons, including other retailers canceling orders, other retailers going out of business, marketing or packaging changes, or a new product launch that has failed. We believe our vendor relationships along with the size and financial strength of our company afford us these opportunities. In addition to closeouts, we intend to expand our everyday offerings, including the roll-out of coolers and freezers in 2014.

Our Soft Home and Hard Home will address our core customers' cooking and living essentials, such as tabletop, bedding, and bath, as well as their home-related discretionary items, such as small appliances, home fashion, and accents. We believe that our competitive advantage in the Soft Home and Hard Home categories is principally based around value, which is a combination of the pricing and quality of our goods. In these categories, our merchandise mix is comprised of replenishable products as the closeout penetration is lower than Food and Consumables. As we edit to amplify, we will be consistently introducing more fashion based products that our core customer uses to decorate her home, while editing areas that our core customer has communicated are not important to her, such as home maintenance, tools, and paint.

Our Furniture & Home Décor category's primary focus will be our core customers' home furnishing needs, such as upholstery, mattresses, ready-to-assemble, and case goods, as well as discretionary items, such as décor, frames, and framed art. In Furniture & Home Décor, we believe our competitive advantage is our sourcing relationships and everyday value offerings. The majority of our offerings in these categories are replenishable products from recognized brand-name manufacturers or sold under our own brands. Our long-standing relationships with certain brand-name manufacturers, most notably in our mattresses and upholstery departments, allow for us to work directly with them to create product offerings specifically for our store, which allows for us to provide a high-quality product at a competitive price.

- Our Seasonal and Electronics & Accessories categories will focus around our core customers' discretionary purchases, such as patio furniture and Christmas trim. For the Seasonal and Electronics & Accessories categories, there is not always an abundant supply of closeout inventory. As such, we generally work with vendors to develop product for us based on our merchants' market evaluations. Much of this merchandise is

sourced on an import basis, which allows us to maintain our competitive pricing. During 2014, we will reduce our offerings in the Electronic & Accessories category, as we have concluded that we do not have a competitive advantage in pricing on products such as televisions, cameras, GPS devices, or gaming.

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In order to support our realigned merchandise categories, we updated our merchandising management organizational hierarchy by adding general merchandise managers, who report directly to our chief merchandising officer, back to our management team. Their responsibility is to ensure that our merchandise offerings are cohesive across merchandise categories throughout the year and to introduce and implement broader programs associated with merchandise execution. The expected outcome of our new strategies, re-alignment, and enhancement to our merchandising management team is to increase our total company comparable store sales (“comps”). We will focus our performance review of merchandise management on comps by merchandise category, as we believe it is the key metric that will drive long-term company net sales performance. By focusing on growing merchandise categories, which includes managing contraction in certain departments, we believe our merchandise management team can address our customer's changing shopping behaviors and implement more tailored programs within each merchandise category, which will lead to growing our comps by merchandise category in 2014.

## Marketing

In the fourth quarter of 2013, we began shifting our marketing efforts to focus on connecting with our core customer in new forms of media that she now uses in her daily life. Historically, our marketing communication efforts have involved a mix of printed ad circulars, television advertising, email advertising, and in-store signage. In the later parts of 2013 with the shift in the management team, we began a more concentrated effort on embracing social media as a method of communicating with our core customer through outlets such as Twitter, Facebook, and YouTube. With the continued proliferation of online and mobile technologies, we need to better compete for our core customer's attention and drive both brand and product awareness on platforms in which our core customer communicates. For example, in early 2014, we introduced a new campaign - “The Thrift is Back” - via social media which promotes our newly formed arrangement with Hostess, where we will effectively be functioning as Hostess's thrift outlet locations. We believe Jennifer responds to our brand-name offerings, therefore we want to ensure our message and promotions are delivered to her in a timely and meaningful way. In 2014, we intend to grow our presence and use of social media to connect with customers as we introduce new programs and campaigns.

Our core customer remains active in electronic communication, and as such, we continue to market to our Buzz Club Rewards members through email campaigns and promotions. In 2013, we restructured our rewards program from a cumulative transaction approach for issuing promotional discounts to a program based on targeted promotions expected to attract members to our stores for new merchandise or promotional events. The goals of the promotions can vary from attempting to tailor the shopping experience based on past purchasing behaviors, to introducing products that a member has previously not purchased from us with the hope of changing their shopping habits. As we continue to learn additional information about our members, we will refine our methodologies for incenting our rewards members.

In 2014, we will continue to communicate our product offerings in order to grow comps through the following traditional approaches to advertise, in addition to social media and our rewards program:

• Printed advertising circulars and promotional pricing to create excitement surrounding the deals that we offer;

• Television commercials broadcast nationwide to promote our brand and, from time to time, promote items or special discounts in our stores; and

• In-store signage initiatives that focus on promoting value.

## Shopping Experience

During 2013, we tested a variety of initiatives aimed at improving our core customer's shopping experience with an overall goal of driving increased comps. Specifically, we identified two programs that we will be rolling-out on a broader scale during 2014 to further demonstrate our customer-first mentality.

First, we tested a cooler and freezer program in approximately 100 stores in 2013. The goal of the program was to increase the convenience of the shopping experience for our core customer in our Food category. We determined that our core customer could not complete a portion of the weekly grocery shopping in our stores, as we did not offer refrigerated and frozen food products needed to complete her basket. Our test results were positive; therefore, we will be implementing our cooler and freezer program to approximately 600 additional stores in 2014. Additionally, by introducing coolers and freezers, the Food assortment that we will offer in many of these locations will qualify for certain governmental assistance programs, such as the supplemental nutrition assistance program ("SNAP"), which will provide our customer with another source of funds to spend at our stores. We believe these programs will help drive comps in both our Food and Consumables categories.

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In 2013, we analyzed our customer financing program available in our Furniture & Home Décor category, and concluded that our current offering was not competitive as too few of our customers were qualifying for access. Effectively, we were not providing an adequate financing solution to assist our core customer in completing the larger purchases that the customer may have desired. In response to this conclusion, in the second half of 2013, we tested a new lease-to-purchase solution provided by a third party. To date, our new provider's program has qualified a larger percentage of our core customers for access to financing. In 2014, we will implement an expanded roll-out of the new lease-to-purchase program to approximately 1,300 stores, or more than 85% of our total fleet. We believe the new lease-to-purchase program will increase comps in the Furniture & Home Décor category as our core customer will have a convenient source of financing to either complete or expand her home furnishing purchases.

## Real Estate

We have determined our average store size of approximately 22,000 selling square feet is an appropriate size for us to provide our core customers with a positive shopping experience and properly present our restructured merchandise categories. This store size enables us to present a representative assortment of products in the merchandise categories that our core customer finds meaningful; therefore when we relocate or open new stores in the future, we intend to open stores of a similar size. In 2012 and 2013, we performed store remodel programs in approximately 3% of our stores in five geographic markets: Miami, Florida; Tampa, Florida; Modesto, California; San Francisco, California; and in the border region of Tennessee and Virginia. Although we believe the remodeled stores created an improved shopping experience, incremental sales results were inconsistent and did not generate enough evidence to support a broader roll-out this program.

Our focus will be on improving our comps and enhancing our core customer's shopping experience. Currently, we anticipate a slight decrease in our total store count in 2014. As discussed in "Item 2. Properties," of this Form 10-K, we have 285 U.S. store leases which will expire in 2014. During 2014, we anticipate closing approximately 50 of those locations. The majority of these closings will be the result of either relocation to a better location, a lack of renewal options, or our belief that a location's sales and operating profit volume are not strong enough to warrant additional investment in the location. As part of our evaluation of potential store closings, we consider our ability to transfer sales from a closing store to other nearby locations and generate a better overall financial result for the geographic market and the overall company. The balance of the closings will be the result of our choice to relocate the store to an improved location nearby. For our remaining store locations with fiscal 2014 lease expirations, we expect to exercise our renewal option or negotiate more favorable lease renewal terms sufficient enough to allow us to continue operations and achieve an acceptable return on our investment.

## Canadian Segment

During 2013, we announced that the Canadian Wind Down would begin in the fourth quarter of 2013 and continue through the first quarter of 2014. During the fourth quarter of 2013, we discontinued receiving merchandise and closed our distribution centers. During the first quarter of 2014 and prior to filing this Form 10-K, we closed all of our remaining stores. Additionally, we transferred the majority of our administrative functions from our office in Brantford, Ontario to our office in Columbus, Ohio.

We also intend to close our office in Brantford, Ontario in its entirety during the first quarter of 2014.

## Discontinued Operations

During 2013, we completed the wind down of the wholesale business within our U.S. segment. As the operations were ceased in 2013, we reported the results of our wholesale business as discontinued operations and reclassified our prior period results, both consolidated and those of our U.S. segment, to reflect this change from continuing operations to



discontinued operations.

We continue to incur an insignificant amount of costs on the 130 stores we closed in 2005 that are classified as discontinued operations. We also report certain activity related to our prior ownership of the KB Toys business in discontinued operations. See note 14 to the accompanying consolidated financial statements for a more detailed discussion of all of our discontinued operations.

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## 2013 COMPARED TO 2012

## U.S. Segment

## Net Sales

Net sales by merchandise category (in dollars and as a percentage of total net sales), net sales change (in dollars and percentage), and comparable store sales (“comp” or “comps”) in 2013 compared to 2012 were as follows:

| (In thousands)            | 2013        |       |   | 2012        |       |   | Change     |        |    | Comps  |    |  |
|---------------------------|-------------|-------|---|-------------|-------|---|------------|--------|----|--------|----|--|
| Furniture & Home Décor    | \$1,072,410 | 20.9  | % | \$1,060,993 | 20.4  | % | \$11,417   | 1.1    | %  | (0.5)  | )% |  |
| Seasonal                  | 958,681     | 18.7  |   | 971,003     | 18.6  |   | (12,322)   | (1.3)  | )  | (2.9)  | )  |  |
| Consumables               | 918,124     | 17.9  |   | 905,444     | 17.4  |   | 12,680     | 1.4    |    | 1.0    |    |  |
| Food                      | 747,840     | 14.6  |   | 742,267     | 14.2  |   | 5,573      | 0.8    |    | 0.0    |    |  |
| Hard Home                 | 514,232     | 10.0  |   | 543,954     | 10.4  |   | (29,722)   | (5.5)  | )  | (6.1)  | )  |  |
| Electronics & Accessories | 486,331     | 9.5   |   | 556,658     | 10.7  |   | (70,327)   | (12.6) | )  | (13.1) | )  |  |
| Soft Home                 | 427,137     | 8.4   |   | 431,999     | 8.3   |   | (4,862)    | (1.1)  | )  | (2.1)  | )  |  |
| Net sales                 | \$5,124,755 | 100.0 | % | \$5,212,318 | 100.0 | % | \$(87,563) | (1.7)  | )% | (2.7)  | )% |  |

In the fourth quarter of 2013, we realigned select merchandise categories to be consistent with the realignment of our merchandising team and changes to our management reporting. Our U.S. segment now uses the following merchandise categories, which match our internal management and reporting of merchandise net sales: Food, Consumables, Soft Home, Hard Home, Furniture & Home Décor, Seasonal, and Electronics & Accessories. The Food category includes our beverage & grocery, candy & snacks, and specialty foods departments. The Consumables category includes our health and beauty, plastics, paper, chemical, and pet departments. The Soft Home category includes the fashion bedding, utility bedding, bath, window, decorative textile, and flooring departments. The Hard Home category includes our small appliances, table top, food preparation, stationary, greeting card, tools, paint, and home maintenance departments. The Furniture & Home Décor category includes our upholstery, mattress, ready-to-assemble, case goods, home décor, and frames departments. The Seasonal category includes our lawn & garden, summer, Christmas, toys, books, sporting goods, and other holiday departments. The Electronics & Accessories category includes the electronics, jewelry, apparel, hosiery, and infant accessories departments. Fiscal 2013 and 2012 sales results have been reclassified to reflect this realignment.

Net sales decreased \$87.6 million or 1.7% to \$5,124.8 million in 2013, compared to \$5,212.3 million in 2012. The decrease in net sales was primarily driven by a 2.7% decrease in comparable store sales, which reduced net sales by \$131.5 million, and the reduction of one week of sales in 2013 compared to 2012, as 2012 was a 53-week retail calendar year. Our comps are calculated by using all stores that were open for at least fifteen months. This decline was partially offset by an increase of \$43.9 million, principally due to operating a higher average number of open stores during 2013 than 2012. Consumables experienced a comp increase, which was principally driven by growth in our pet department, which benefited from a product and space expansion during the first half of 2013. Food generated a flat comp, which was comprised of negative comps in the first half of 2013 and positive comps during the second half of 2013, as customers responded to improved consistency of quality, branded product assortments and closeouts in most major departments. The slight comp decrease in Furniture & Home Décor was driven by comp decreases in our home décor offerings, partially offset by a comp increase in our traditional furniture business (e.g. upholstery, mattresses, case goods, and ready-to-assemble departments). By re-aligning, our home décor and frames departments with our upholstery and case goods, we anticipate that we will be able to better coordinate our merchandise offerings and presentation, which should improve their comp performance. The decrease in Soft Home comps occurred in most departments, which was a significant contributing factor to the re-alignment of the former Home category. We believe separating Soft Home and Hard Home merchandise and aligning our merchants in those areas will narrow their focus and allow us to provide an assortment that is consistent with our core customer’s needs. The decrease in our Seasonal

category's comp was driven by an underperformance during our holiday selling season, particularly in our toys and Christmas trim departments, which was negatively impacted by the snow and cold weather which occurred early in the holiday selling season. The Seasonal category decrease was partially offset by a positive performance in our lawn & garden department driven by a better merchandise assortment in our patio offerings and a favorable summer weather pattern in 2013 compared to 2012. The decrease in Hard Home comps occurred in most departments and was driven by our home maintenance, auto, tools, and paint departments, which was a primary consideration when determining to exit these classifications after continued underperformance. The decrease in comps in Electronics & Accessories was primarily driven by lower electronics sales, particularly in tablet, digital camera, gaming and DVD products, as customers have not responded to our assortment of product

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offerings. Additionally, throughout 2013, we began to narrow our product offerings in our electronics department in order to appropriately react to our customer's response and overall trends for this category in the retail marketplace.

For 2014, we expect net sales to be in the range of a slight increase to a slight decrease to 2013, which is based on overall comps that range from flat to an increase of 2% and an expected overall lower store count. We expect above average comps from our Furniture & Home Décor and Food categories, driven by our chain wide roll-out of our lease-to-own program and investments in coolers and freezers. Additionally, we anticipate below average comps in our Hard Home and Electronics & Accessories categories due to our downsizing of numerous departments as we Edit to Amplify other categories.

### Gross Margin

Gross margin dollars decreased \$47.3 million or 2.3% to \$2,007.4 million in 2013, compared to \$2,054.7 million in 2012. The decrease in gross margin dollars was principally due to both a decrease in net sales, which decreased gross margin dollars by approximately \$34.5 million, and a lower gross margin rate, which decreased gross margin dollars by approximately \$12.8 million. Gross margin as a percentage of net sales decreased 20 basis points to 39.2% in 2013 compared to 39.4% in 2012. The gross margin rate decrease was principally due to a higher markdown rate during the fourth quarter of 2013 as compared to the fourth quarter of 2012. During the fourth quarter of 2013, we began implementing the "Edit" portion of our Edit to Amplify strategy, which involved conducting significant promotional activities to reduce our inventory in certain departments, including auto, tools, and home maintenance, as a result of our planned reductions in the focus and square footage we intend to dedicate to those departments as well as editing merchandise within other departments.

For 2014, we expect our gross margin rate to be slightly higher than 2013, as we anticipate lower levels of markdowns will be necessary to achieve our planned sales.

### Selling and Administrative Expenses

Selling and administrative expenses were \$1,664.2 million in 2013, compared to \$1,639.8 million in 2012. The increase of \$24.4 million or 1.5% was primarily due to increases in store occupancy expenses of \$18.5 million, distribution and transportation expenses of \$6.9 million, corporate office payroll of \$4.8 million, and a non-recurring litigation settlement of \$4.4 million, partially offset by decreases in professional fees of \$5.3 million and share-based compensation expense of \$4.7 million, and a gain on the sale of real estate of \$3.6 million. The increase in store occupancy expenses was primarily the result of an increase in the average number of stores operating per month in 2013 as compared to 2012. The increase in distribution and transportation expenses was primarily due to an increased number of merchandise cartons flowing from our distribution centers to our stores. The increase in general office payroll expenses was primarily driven by separation activities that occurred during the second, third, and fourth quarters of 2013 combined with annual merit increases. The non-recurring litigation settlement was the result of a loss contingency for a legal matter that was finalized in the second quarter of 2013. The decrease in share-based compensation expense was primarily driven by the forfeiture of awards by individuals affected by separation activities and the associated reversal of costs. The decrease in professional fees was primarily driven by decreased consulting fees related to various ongoing information systems projects and decreased legal expenses related to pending litigation and other matters. The gain on sale of real estate resulted from our sale of an owned store location in the third quarter of 2013.

As a percentage of net sales, selling and administrative expenses increased by 100 basis points to 32.5% in 2013 compared to 31.5% in 2012. The primary drivers of the 100 basis point deleverage in selling and administrative expenses were the 2.7% decrease in overall comp performance, as the percentage increase in expense dollars was commensurate with the growth in store count, and the increase in our distribution and transportation expenses. Our future selling and administrative expense as a percentage of net sales rate is dependent upon many factors including our level of net sales, our ability to implement additional efficiencies, principally in our store and distribution center

operations, and fluctuating commodity prices, such as diesel fuel, which directly affects our outbound transportation cost.

For 2014, we are forecasting an expense rate slightly higher than the rate achieved in 2013. Store expenses and distribution and transportation expenses are expected to leverage as dollar growth in these areas is forecasted to be at a slower rate than our anticipated sales growth. These leveraged expenses are expected to be offset by higher healthcare expenses from the enactment of the Affordable Care Act, higher bonus expenses as we expect to achieve our corporate financial goals in 2014 as compared to 2013 when those goals were not achieved, and certain operational investments in e-commerce activities.

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### Depreciation Expense

Depreciation expense increased \$10.1 million to \$113.2 million in 2013 compared to \$103.1 million in 2012. The increase is directly related to our new store openings in both 2013 and late 2012, investments in systems, and capital spending to support and maintain our stores and distribution centers. Depreciation expense as a percentage of net sales increased by 20 basis points compared to 2012.

For 2014, we expect capital expenditures of approximately \$115 million to \$120 million, which includes maintenance capital for our stores, distributions centers, and corporate offices, the construction and opening of 30 new stores and investing in coolers, freezers and e-commerce technologies. Using this assumption and the run rate of depreciation on our existing property and equipment, we expect 2014 depreciation expense to be approximately \$120 million, which would represent an increase from the \$113.2 million of depreciation expense in 2013.

### Operating Profit

Operating profit was \$229.9 million in 2013 as compared to \$311.7 million in 2012. The decrease in operating profit was primarily driven by the items discussed in the Net Sales, Gross Margin, Selling and Administrative Expenses, and Depreciation Expense sections above and the impact of the occurrence of a 53<sup>rd</sup> week in 2012 that did not recur in 2013. In addition, our operating profit in 2012 increased by approximately \$5.0 million from the occurrence of the 53<sup>rd</sup> week.

### Canadian Segment

Our Canadian segment's net sales increased \$22.4 million to \$177.2 million in 2013, as compared to \$154.8 in 2012. Our operating loss was \$39.5 million in 2013 compared to \$13.7 million in 2012. As we began to execute our wind down activities during the fourth quarter of 2013, we began a markdown program to facilitate the liquidation of inventory in the fourth quarter of 2013, which increased sales during the fourth quarter, but at a reduced gross margin rate. Additionally, during the fourth quarter of 2013, we impaired our goodwill associated with our Canadian segment by \$12.7 million, impaired the value of our property and equipment by \$6.5 million to its salvage value, reduced the value of our inventory to its net realizable value, which represents the lower of cost or market, and accrued for certain severance costs of \$2.7 million.

For 2014, we estimate a net loss of \$37 million to \$41 million as we incur additional wind down charges associated with contract termination costs, primarily associated with our facility operating leases, and severance actions. Additionally, we anticipate the results of our Canadian segment will be reclassified to discontinued operations as we complete the wind down during the first quarter of 2014.

### Other Performance Factors

#### Interest Expense

Interest expense decreased \$0.9 million to \$3.3 million in 2013 compared to \$4.2 million in 2012. The decrease in interest expense was primarily driven by decreased borrowings in 2013. We had total average borrowings (including capital leases) of \$158.7 million in 2013 compared to total average borrowings of \$200.3 million in 2012. The decrease in total average borrowings was primarily the result of utilizing the excess of our cash inflows from operations, which exceeded cash outflows from investing activities, to repay portions of our indebtedness.

#### Income Taxes

The effective income tax rate in 2013 and 2012 for income from continuing operations was 32.9% and 39.8%, respectively. The lower rate in 2013 is primarily due to the recognition of a U.S. deferred tax benefit associated with the excess tax basis related to our investment in our Canadian segment, partially offset by the nondeductible goodwill impairment charge related to our Canadian segment and a valuation allowance relative to the deferred tax benefit of

the loss generated by our Canadian segment on a lower pretax income base.

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## 2012 COMPARED TO 2011

## U.S. Segment

## Net Sales

Net sales by merchandise category, in dollars and as a percentage of total net sales, and net sales change in dollars and percentage from 2012 compared to 2011 were as follows:

| (In thousands)            | 2012        |         | 2011        |         | Change    |       | Comps   |  |
|---------------------------|-------------|---------|-------------|---------|-----------|-------|---------|--|
| Furniture & Home Decor    | \$1,060,993 | 20.4 %  | \$1,010,007 | 19.8 %  | \$50,986  | 5.0 % | (1.8 %) |  |
| Seasonal                  | 971,003     | 18.6    | 982,604     | 19.3    | (11,601)  | (1.2) | (5.4)   |  |
| Consumables               | 905,444     | 17.4    | 881,282     | 17.3    | 24,162    | 2.7   | (1.9)   |  |
| Food                      | 742,267     | 14.2    | 723,291     | 14.2    | 18,976    | 2.6   | (2.3)   |  |
| Electronics & Accessories | 556,658     | 10.7    | 550,513     | 10.8    | 6,145     | 1.1   | (3.9)   |  |
| Hard Home                 | 543,954     | 10.4    | 537,092     | 10.5    | 6,862     | 1.3   | (3.7)   |  |
| Soft Home                 | 431,999     | 8.3     | 412,355     | 8.1     | 19,644    | 4.8   | (1.1)   |  |
| Net sales                 | \$5,212,318 | 100.0 % | \$5,097,144 | 100.0 % | \$115,174 | 2.3 % | (2.7 %) |  |

As discussed above in the section “2013 Compared To 2012”, in the fourth quarter of 2013, we realigned our merchandise categories in our U.S. segment to be consistent with the realignment of our merchandising team and changes to our management reporting. All results for 2012 and 2011 have been reclassified to represent the current merchandise category structure for comparability.

Net sales increased \$115.2 million or 2.3% to \$5,212.3 million in 2012, compared to \$5,097.1 million in 2011. Net sales increased by \$247.0 million principally due to the net addition of 44 stores since the end of 2011 and an additional week of sales, as 2012 was a 53-week retail calendar year. This growth was partially offset by a 2.7% decrease in comps, which reduced net sales by \$131.8 million. Our comps are calculated by using all stores that were open for at least fifteen months. The decrease in comps in the Furniture & Home Décor category was driven by comp decreases in ready-to-assemble furniture, home décor, and case goods, partially offset by comp increases in upholstery and mattresses. The decrease in comps in the Consumables category was driven by comp decreases in our health and beauty care, home organization, and pet department, where our product assortment did not appeal to our customer’s needs, partially offset by comp increases in our paper, household chemicals and housekeeping departments, where we had an improved selection of closeout offerings. The decrease in comps of our Soft Home category was primarily due to comp declines in our decorative window and flooring offerings, partially offset by growth in both fashion bedding and utility bedding. During 2012, we allocated additional selling space in our stores to the Soft Home category in an effort to increase sales in this higher margin category. This initiative did not meet our expectations and was a factor in certain management changes of this key category. The Food category experienced a comp decrease driven by our beverage & grocery and candy & snack departments, partially offset by an increase in comps in our specialty foods department. The decrease in comps in our Electronics & Accessories category was primarily driven by lower sales in the apparel, lingerie and infant accessories departments as we allocated less space and reduced our assortments, which allowed for the space expansion in our Soft Home and Hard Home categories. These declines were partially offset by increased comps in jewelry and electronics. Comps in the Hard Home category decreased which was driven by comp decreases in tools, paint, and home maintenance, as the demand from our core customer for these offerings continued to decline. The comp decrease in Hard Home was partially offset by improved comps in the small appliances and food preparation departments, which benefited from an increase in branded closeouts in 2012 compared to 2011. The Seasonal category experienced a decrease in comps, which was driven by our toys, fall seasonal, and summer departments, partially offset by strong sales of our Christmas trim, which had positive comps as our customers responded to a new assortment of products. The decrease in our toys department was driven by additional downsizing of space allocated to the department during 2012.





Table of Contents**Gross Margin**

Gross margin dollars increased \$16.0 million or 0.8% to \$2,054.7 million in 2012, compared to \$2,038.7 million in 2011. The increase in gross margin dollars was principally due to an increase in net sales, which increased gross margin dollars by approximately \$46.1 million. Partially offsetting the increase was a lower gross margin rate, which decreased gross margin dollars by approximately \$30.1 million. Gross margin as a percentage of net sales decreased 60 basis points to 39.4% in 2012 compared to 40.0% in 2011. The gross margin rate decrease was principally due to a higher markdown rate and the \$5.6 million, or 10 basis points, impact of the change in accounting principle related to the implementation of new retail inventory systems implemented at the beginning of 2012.

**Selling and Administrative Expenses**

Selling and administrative expenses were \$1,639.8 million in 2012, compared to \$1,594.5 million in 2011. The increase of \$45.3 million or 2.8% was primarily due to increases in store occupancy expenses of \$16.5 million, store payroll expenses of \$15.9 million, health benefit expenses of \$11.4 million, corporate office payroll of \$6.3 million, and professional fees of \$3.0 million, partially offset by a decrease in share-based compensation expense of \$7.2 million and lower bonus expenses of \$5.3 million. The increase in store payroll and store occupancy expenses were primarily due to the net increase of 44 stores compared to the end of 2011. The increase in health benefits expense was primarily driven by costs associated with certain large claims that were expensed during 2012 as compared to 2011. Our corporate office payroll costs increased primarily due to the growth in our merchandising team and lower capitalization of salaries associated with information systems projects, as our SAP® implementation was completed at the end of 2011. The increase in professional fees was primarily driven by increased legal expenses related to pending litigation and other matters and consulting fees related to various on-going information systems projects. The decrease in share-based compensation expense was primarily driven by the nonvested restricted stock award granted to Mr. Fishman in 2012. In 2011, the corporate financial goal associated with the award granted to Mr. Fishman in 2011 was achieved, while in 2012, the corporate financial goal associated with the award granted to Mr. Fishman in 2012 was not achieved. Additionally, in the fourth quarter of 2012, management changed its estimate of the vesting period for the restricted stock awards granted in 2011 and 2012, exclusive of Mr. Fishman's grant, from three years to four years. This change resulted in a decrease in share-based compensation expense in the fourth quarter of 2012. The decrease in bonus expense was directly related to lower financial performance during 2012 as compared to the targets in our 2012 operating plan.

As a percentage of net sales, selling and administrative expenses increased by 20 basis points to 31.5% in 2012 compared to 31.3% in 2011. As noted above, selling and administrative expense dollars increased 2.8% primarily related to the 3% increase in store count. The primary driver of 20 basis point deleverage in selling and administrative expenses was the 2.7% decrease in comparable store sales performance, as the percentage increase in expense dollars was commensurate with the growth in store count.

**Depreciation Expense**

Depreciation expense increased \$14.8 million to \$103.1 million in 2012 compared to \$88.3 million in 2011. The increase is directly related to our new store growth, investments in systems, and capital spending to support and maintain our stores and distribution centers. Depreciation expense as a percentage of net sales increased by 30 basis points in 2012 compared to 2011.

**Operating Profit**

Operating profit was \$311.7 million in 2012 as compared to \$355.9 million in 2011. The change in operating profit was primarily driven by the items discussed in the Net Sales, Gross Margin, Selling and Administrative Expenses, and Depreciation Expense sections above and the impact of the occurrence of a 53<sup>rd</sup> week in 2012 that did not occur in 2011. We estimated our operating profit in 2012 increased by approximately \$5.0 million from the occurrence of the 53<sup>rd</sup> week.

Canadian Segment

Our Canadian segment's net sales increased \$92.7 million to \$154.8 million in 2012, as compared to \$62.1 in 2011. Net sales in 2011 represented results of our Canadian segment from the date of acquisition (July 18, 2011) through the end of the fiscal year 2011 as compared to a full fiscal year in 2012. Our operating loss was \$13.7 million in 2012 compared to \$12.2 million in 2011. The increase in operating loss was due to full year results in 2012 compared to only partial year results in 2011. Our operating loss as a percentage of net sales improved to 8.8% in 2012 as compared to 19.7% in 2011. The operating loss rate improvement was the result of positive sales trends from increased inventory levels and an improving merchandise assortment.

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### Other Performance Factors

#### Interest Expense

Interest expense increased \$0.7 million to \$4.2 million in 2012 compared to \$3.5 million in 2011. The increase in interest expense was primarily driven by increased borrowings in 2012. This increase was offset by decreases due to \$0.8 million of non-recurring prepayment fees in the second quarter of 2011 that were associated with repayment of the notes payable assumed in the acquisition of Liquidation World Inc. The increase was also offset by lower amortization of deferred bank fees on our 2011 Credit Agreement in 2012 as compared to deferred bank fees on our prior credit agreement in 2011. We had total average borrowings (including capital leases) of \$200.3 million in 2012 compared to total average borrowings of \$88.2 million in 2011. The increase in total average borrowings was primarily the result of our investment of \$298.5 million in 2012 to purchase approximately 8.1 million of our outstanding shares under the 2011 and 2012 Repurchase Programs.

#### Income Taxes

The effective income tax rate in 2012 and 2011 for income from continuing operations was 39.8% and 39.4%, respectively. The higher rate in 2012 is primarily due to a valuation allowance relative to the deferred tax benefit of the loss generated by our Canadian segment on a lower pretax income base and a net decrease in favorable discrete income tax items.

### Capital Resources and Liquidity

On July 22, 2011, we entered into the 2011 Credit Agreement, and it was amended on May 30, 2013 to lower our interest rates, pricing, and fees and the term was extended from July 22, 2016 to May 30, 2018. In connection with our entry into the 2011 Credit Agreement, we paid bank fees and other expenses in the aggregate amount of \$3.0 million, which are being amortized over the term of the agreement. In connection with the amendment of the 2011 Credit Agreement, we paid bank fees and other expenses in the aggregate amount of \$0.9 million, which are being amortized over the term of the agreement. Borrowings under the 2011 Credit Agreement are available for general corporate purposes and working capital. The 2011 Credit Agreement includes a \$30 million swing loan sublimit and a \$150 million letter of credit sublimit. The interest rates, pricing and fees under the 2011 Credit Agreement fluctuate based on our debt rating. The 2011 Credit Agreement allows us to select our interest rate for each borrowing from multiple interest rate options. The interest rate options are generally derived from the prime rate or LIBOR. The lenders under the 2011 Credit Agreement consented to the wind down of our Canadian segment, and, in connection therewith, in January 2014, we and the lenders agreed to eliminate Big Lots Canada, Inc. as a borrower under the 2011 Credit Agreement, which in turn resulted in the elimination of the \$10 million Canadian swing loan sublimit, the \$200 million Canadian revolving credit loan subfacility, and the CDOR interest rate option. The elimination of Big Lots Canada, Inc. as a borrower and the elimination of these provisions regarding Canadian borrowings did not change the total amount available under the 2011 Credit Agreement. We may prepay revolving loans made under the 2011 Credit Agreement. The 2011 Credit Agreement contains financial and other covenants, including, but not limited to, limitations on indebtedness, liens and investments, as well as the maintenance of two financial ratios – a leverage ratio and a fixed charge coverage ratio. A violation of any of the covenants could result in a default under the 2011 Credit Agreement that would permit the lenders to restrict our ability to further access the 2011 Credit Agreement for loans and letters of credit and require the immediate repayment of any outstanding loans under the 2011 Credit Agreement. At February 1, 2014, we were in compliance with the covenants of the 2011 Credit Agreement.

We use the 2011 Credit Agreement, as necessary, to provide funds for ongoing and seasonal working capital, capital expenditures, share repurchase programs, and other expenditures. In addition, we use the 2011 Credit Agreement to provide letters of credit for various operating and regulatory requirements, and if needed, letters of credit required to cover of our self-funded insurance programs. Given the seasonality of our business, the amount of borrowings under the 2011 Credit Agreement may fluctuate materially depending on various factors, including our operating financial

performance, the time of year, and our need to increase merchandise inventory levels prior to the peak selling season.

The primary source of our liquidity is cash flows from operations and, as necessary, borrowings under the 2011 Credit Agreement. Our net income and, consequently, our cash provided by operations are impacted by net sales volume, seasonal sales patterns, and operating profit margins. Our net sales are typically highest during the nine-week Christmas selling season in our fourth fiscal quarter. Generally, our working capital requirements peak late in our third fiscal quarter or early in our fourth fiscal quarter. We have typically funded those requirements with borrowings under our credit facility. In 2013, our total indebtedness (outstanding borrowings and letters of credit) under the 2011 Credit Agreement, peaked at approximately \$358 million in November.

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At February 1, 2014, we had \$77.0 million in outstanding borrowings under the 2011 Credit Agreement and \$617.4 million borrowings available under the 2011 Credit Agreement, after taking into account the reduction in availability resulting from outstanding letters of credit totaling \$5.6 million. We anticipate that total indebtedness under the 2011 Credit Agreement through June 15, 2014, will not exceed \$85 million, which includes our estimate of outstanding letters of credit and the estimated impact of cash needs of Big Lots Canada, but excludes the impact of any potential share repurchase activity under the 2014 Repurchase Program. Working capital was \$543.6 million at February 1, 2014.

Whenever our liquidity position requires us to borrow funds under the 2011 Credit Agreement, we typically repay and/or borrow on a daily basis. The daily activity is a net result of our liquidity position, which is generally driven by the following components of our operations: (1) cash inflows such as cash or credit card receipts collected from stores for merchandise sales and other miscellaneous deposits; and (2) cash outflows such as check clearings for the acquisition of merchandise, wire and other electronic transactions for the acquisition of merchandise, payroll and other operating expenses, income and other taxes, employee benefits, and other miscellaneous disbursements.

Cash provided by operating activities decreased by \$82.8 million to \$198.3 million in 2013 compared to \$281.1 million in 2012. The decrease was primarily driven by the decrease in net income of \$51.8 million to \$125.3 million in 2013 from \$177.1 million in 2012. Additionally, the change in our income tax related assets impacted our operating cash flows. Our net deferred tax assets increased more substantially during 2013 as compared to 2012 principally due to (1) the recognition of a U.S. deferred tax benefit associated with the excess tax basis related to our investment in our Canadian segment, (2) an increase in the deferred tax assets associated with nonvested restricted stock as no material vesting of restricted stock has occurred in 2013, (3) the impact of fewer stock option exercises in 2013 compared to 2012, and (4) the reduction of deferred tax liabilities associated with greater book depreciation compared to flat tax depreciation. These deferred tax items impacted our operating cash flows by \$44.6 million. Our current income taxes payable decreased more substantially during 2013 as compared to 2012, primarily due to our generation of higher taxable income during the first three quarters of 2013 as compared to the first three quarters of 2012, which resulted in higher estimated income tax installment payments during 2013 compared to 2012, coupled with the generation of lower taxable income in the fourth quarter of 2013 as compared to the fourth quarter of 2012. The result of the higher estimated income tax payments was a reduction of \$38.3 million of cash provided by operating activities. Partially offsetting these decreases in cash flows from operations were a net reduced amount of net cash used by certain operating asset and liabilities and an increase in non-cash impairment charges. During 2013, we generated cash from our inventories as we reduced our inventory levels as a result of the wind down of our Canadian segment and wholesale business, while during 2012, we used cash to grow our inventory levels. Our accounts payable have a direct correlation with our inventory; therefore as we reduced our inventory position during 2013, we also reduced our accounts payable, which required the use of cash, and during 2012, when we grew our inventory balances, our accounts payable increased, which provided cash flows. The impact of the movement in our inventory and accounts payable balances provided for \$23.1 million of net cash within operating activities. Non-cash impairment charges increased \$20.1 million, which were principally associated with the wind down of the operations of our Canadian segment, including the impairments of goodwill, fixed assets, and tradename intangible assets.

Cash used in investing activities decreased by \$32.9 million to \$97.5 million in 2013 compared to \$130.4 million in 2012. The decrease was primarily due to lower capital expenditures in 2013 as compared to 2012, which were \$104.8 million and \$131.3 million, respectively. The decrease in capital expenditures was principally driven by a reduction in new store openings in 2013 as compared to 2012, which decreased to 57 new stores in 2013 from 87 new stores in 2012. Additionally, we received greater proceeds on the sale of property and equipment in 2013, as we sold an owned store location, as compared to 2012, when we had no similar real estate transaction.

Cash used in financing activities decreased by \$67.1 million to \$91.2 million in 2013 compared to \$158.3 million in 2012. The decrease in the cash used in financing activities was principally due to the lack of an active share

repurchase program during 2013. Our use of cash for share repurchase activities decreased by \$303.8 million to \$0.2 million in 2013 as compared to \$304.0 million in 2012. The majority of the shares repurchased in 2012 were acquired under a board-authorized share repurchase program, while in 2013 no such program existed. In 2012, we utilized \$105.3 million of net proceeds from borrowings under our credit facility to partially fund our share repurchase activities. In 2013, we utilized a portion of our cash provided by operating activities to repay \$94.2 million of borrowings under our credit facility. Lastly, there was a reduction in the proceeds from the exercise of stock options of \$28.4 million, as fewer options were exercised in 2013 as compared to 2012.

Based on historical and expected financial results, we believe that we have or, if necessary, have the ability to obtain, adequate resources to fund ongoing and seasonal working capital requirements, proposed capital expenditures, new projects, and currently maturing obligations.

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## Contractual Obligations

The following table summarizes payments due under our contractual obligations at February 1, 2014:

| (In thousands)  | Payments Due by Period <sup>(1)</sup> |                     |              |              |                      |
|---|---------------------------------------|---------------------|--------------|--------------|----------------------|
|   | Total                                 | Less than<br>1 year | 1 to 3 years | 3 to 5 years | More than<br>5 years |
| Obligations under bank credit facility <sup>(2)</sup> | \$77,095                              | \$95                | \$—          | \$77,000     | \$—                  |
| Operating lease obligations <sup>(3) (4)</sup>        | 1,295,004                             | 338,237             | 499,523      | 285,556      | 171,688              |
| Capital lease obligations <sup>(4)</sup>              | 1,018                                 | 930                 | 88           | —            | —                    |
| Purchase obligations <sup>(4) (5)</sup>               | 628,909                               | 546,236             | 69,735       | 12,938       | —                    |
| Other long-term liabilities <sup>(6)</sup>            | 35,474                                | 7,172               | 7,190        | 7,200        | 13,912               |
| Total contractual obligations                         | \$2,037,500                           | \$892,670           | \$576,536    | \$382,694    | \$185,600            |

The disclosure of contractual obligations in this table is based on assumptions and estimates that we believe to be reasonable as of the date of this report. Those assumptions and estimates may prove to be inaccurate; consequently, the amounts provided in the table may differ materially from those amounts that we ultimately incur. Variables that may cause the stated amounts to vary from the amounts actually incurred include, but are not limited to: the termination of a contractual obligation prior to its stated or anticipated expiration; fees or damages incurred as a result of the premature termination or breach of a contractual obligation; the acquisition of more or less services or goods under a contractual obligation than are anticipated by us as of the date of this report; fluctuations in third party fees, governmental charges, or market rates that we are obligated to pay under contracts we have with certain vendors; and the exercise of renewal options under, or the automatic renewal of, contracts that provide for the same.

Obligations under the bank credit facility consist of the borrowings outstanding under the 2011 Credit Agreement, and the associated accrued interest of \$0.1 million. In addition, we had outstanding letters of credit totaling \$64.4 million at February 1, 2014. Approximately \$61.8 million of the outstanding letters of credit represent stand-by letters of credit and we do not expect to meet the conditions requiring significant cash payments on these letters of credit; accordingly, they have been excluded from this table. The remaining \$2.6 million of outstanding letters of credit represent commercial letters of credit whereby the related obligation is included in the purchase obligations. For a further discussion, see note 3 to the accompanying consolidated financial statements.

Operating lease obligations include, among other items, leases for retail stores, warehouse space, offices, and certain computer and other business equipment. The future minimum commitments for retail store, office, and warehouse space operating leases are \$1,003.1 million. For a further discussion of leases, see note 5 to the accompanying consolidated financial statements. Many of the store lease obligations require us to pay for our applicable portion of CAM, real estate taxes, and property insurance. In connection with our store lease obligations, we estimated that future obligations for CAM, real estate taxes, and property insurance were \$284.8 million at February 1, 2014. We have made certain assumptions and estimates in order to account for our contractual obligations relative to CAM, real estate taxes, and property insurance. Those assumptions and estimates include, but are not limited to: use of historical data to estimate our future obligations; calculation of our obligations based on comparable store averages where no historical data is available for a particular leasehold; and assumptions related to average expected increases over historical data. The remaining lease obligation of \$7.1 million relates primarily to operating leases for computer and other business equipment, including data center related costs. For our Canadian segment, we valued our operating lease obligations at their contractual amounts as of February 1, 2014. Since February 1, 2014, we have agreed to buy-outs with many of our landlords at amounts that were lower than our contractual obligation.

(4)



For purposes of the lease and purchase obligation disclosures, we have assumed that we will make all payments scheduled or reasonably estimated to be made under those obligations that have a determinable expiration date, and we disregarded the possibility that such obligations may be prematurely terminated or extended, whether automatically by the terms of the obligation or by agreement between us and the counterparty, due to the speculative nature of premature termination or extension. Where an operating lease or purchase obligation is subject to a month-to-month term or another automatically renewing term, we included in the table our minimum commitment under such obligation, such as one month in the case of a month-to-month obligation and the then-current term in the case of another automatically renewing term, due to the uncertainty of future decisions to exercise options to extend or terminate any existing leases.

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Purchase obligations include outstanding purchase orders for merchandise issued in the ordinary course of our business that are valued at \$464.6 million, the entirety of which represents obligations due within one year of February 1, 2014. In addition, we have a purchase commitment for future inventory purchases totaling \$49.0 million at February 1, 2014. While we are not required to meet any periodic minimum purchase requirements (5) under this commitment, we have included, for purposes of this tabular disclosure, the value of the purchases that we anticipate making during each of the reported periods as purchases that will count toward our fulfillment of the aggregate obligation. The remaining \$115.3 million of purchase obligations is primarily related to distribution and transportation, information technology, print advertising, energy procurement, and other store security, supply, and maintenance commitments.

Other long-term liabilities include \$21.4 million for obligations related to our nonqualified deferred compensation plan, \$6.5 million for expected contributions to the Pension Plan and our nonqualified, unfunded supplemental defined benefit pension plan (“Supplemental Pension Plan”), \$2.6 million for unrecognized tax benefits, and \$0.5 million for closed store lease termination costs related to stores closed in 2013 or earlier. Pension contributions are equal to expected benefit payments for the nonqualified plan plus expected contributions to the qualified plan using actuarial estimates and assuming that we only make the minimum required contributions (see note 8 to the (6) accompanying consolidated financial statements for additional information about our employee benefit plans). We have estimated the payments due by period for the nonqualified deferred compensation plan based on an average of historical distributions. We have included unrecognized tax benefits of \$2.6 million for payments expected in 2013 and \$0.7 million of timing-related income tax uncertainties anticipated to reverse in 2013. Unrecognized tax benefits in the amount of \$19.0 million have been excluded from the table because we are unable to make a reasonably reliable estimate of the timing of future payments. Our closed store lease termination cost payments are based on contractual terms.

## Off-Balance Sheet Arrangements

For a discussion of the KB Bankruptcy Lease Obligations, see note 14 to the accompanying consolidated financial statements. Because the KB Toys business filed for bankruptcy again in December 2008 and liquidated all of its store operations, we accrued a contingent liability on our balance sheet at January 30, 2010, for 31 KB Toys store leases for which we may have an indemnification or guarantee obligation and a former KB Toys corporate office lease for which we took an assignment in 2009. During the fourth quarter of 2013, we re-evaluated our liability and determined the likelihood of an unfavorable settlement had become remote; therefore at February 1, 2014, we had no contingent liability related to this matter. Because of uncertainty inherent in the assumptions used to estimate this liability, our estimated liability could ultimately prove to be understated and could result in a material adverse impact on our financial condition, results of operations, and liquidity.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“GAAP”) requires management to make estimates, judgments, and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period, as well as the related disclosure of contingent assets and liabilities at the date of the financial statements. The use of estimates, judgments, and assumptions creates a level of uncertainty with respect to reported or disclosed amounts in our consolidated financial statements or accompanying notes. On an ongoing basis, management evaluates its estimates, judgments, and assumptions, including those that management considers critical to the accurate presentation and disclosure of our consolidated financial statements and accompanying notes. Management bases its estimates, judgments, and assumptions on historical experience, current trends, and various other factors that management believes are reasonable under the circumstances. Because of the inherent uncertainty in using estimates, judgments, and assumptions, actual results may differ from these estimates.

Our significant accounting policies, including the recently adopted accounting standards and recent accounting standards - future adoptions, if any, are described in note 1 to the accompanying consolidated financial statements. We believe the following assumptions and estimates are the most critical to understanding and evaluating our reported financial results. Management has reviewed these critical accounting estimates and related disclosures with the Audit Committee of our Board of Directors.

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### Merchandise Inventories

Merchandise inventories are valued at the lower of cost or market using the average cost retail inventory method. Market is determined based on the estimated net realizable value, which generally is the merchandise selling price at or near the end of the reporting period. The average cost retail inventory method requires management to make judgments and contains estimates, such as the amount and timing of markdowns to clear slow-moving inventory and the estimated allowance for shrinkage, which may impact the ending inventory valuation and prior or future gross margin. These estimates are based on historical experience and current information.

When management determines the saleability of merchandise inventories is diminished, markdowns for clearance activity and the related cost impact are recorded at the time the price change decision is made. Factors considered in the determination of markdowns include current and anticipated demand, customer preferences, the age of merchandise, and seasonal trends. Timing of holidays within fiscal periods, weather, and customer preferences could cause material changes in the amount and timing of markdowns from year to year. During 2013, we announced our intentions to wind down the operations of our Canadian segment and have since implemented a markdown strategy in order to most efficiently execute the liquidation of the inventory in our Canadian segment. We have reduced the value of the inventory in our Canadian segment at February 1, 2014 to a level that reflects our net realizable value based on estimated cash proceeds prior to closing, which represents our estimate of its market value.

The inventory allowance for shrinkage is recorded as a reduction to inventories, charged to cost of sales, and calculated as a percentage of sales for the period from the last physical inventory date to the end of the reporting period. Such estimates are based on both our current year and historical inventory results. Independent physical inventory counts are taken at each store once a year. During calendar 2014, the majority of these counts will occur between January and July. As physical inventories are completed, actual results are recorded and new go-forward shrink accrual rates are established based on individual store, historical results. Thus, the shrink accrual rates will be adjusted throughout the January to July inventory cycle based on actual results. At February 1, 2014, a 10% difference in our shrink reserve would have affected gross margin, operating profit and income from continuing operations before income taxes by approximately \$3.4 million. While it is not possible to quantify the impact from each cause of shrinkage, we have asset protection programs and policies aimed at minimizing shrinkage.

### Long-Lived Assets

Our long-lived assets primarily consist of property and equipment. We perform annual impairment reviews of our long-lived assets at the store level, or when other impairment indicators are present. Generally, all other property and equipment is reviewed for impairment at the enterprise level. When we perform the annual impairment reviews, we first determine which stores had impairment indicators present. We use actual historical cash flows to determine which stores had negative cash flows within the past two years. For each store with negative cash flows, we obtain future cash flow estimates based on operating performance estimates specific to each store's operations that are based on assumptions currently being used to develop our company level operating plans. If the net book value of a store's long-lived assets is not recoverable through the expected future cash flows of the store, we estimate the fair value of the store's assets and recognize an impairment charge for the excess net book value of the store's long-lived assets over their fair value. The fair value of store assets is estimated based on expected cash flows, including salvage value, which is based on information available in the marketplace for similar assets.

In our U.S. segment, we identified seven stores and two stores, in 2013 and 2012, respectively, with impairment indicators as a result of our annual store impairment tests. For our U.S. stores, we recognized impairment charges of \$1.3 million and \$0.6 million in 2013 and 2012, respectively. We do not believe that varying the assumptions used to test for recoverability to estimate fair value of our long-lived assets would have a material impact on the impairment charges we incurred in 2013 or 2012.

Our December 2013 announcement of the Canadian Wind Down was a triggering event for an impairment review of the long-lived assets in our Canadian segment. As a result of the wind down, our Canadian segment will no longer generate sales or operating cash inflows after the end of the first quarter of 2014; therefore, we determined that we would not be able to recover the book value of our property and equipment and tradename intangible assets in our Canadian segment. As such, we recorded an impairment charge of \$7.0 million in 2013, which consisted of \$6.5 million associated with reducing the value of our property to its estimated salvage value and \$0.5 million associated with the full impairment of our tradename intangible assets. During 2012, we identified four Canadian stores in our impairment review, which resulted in a fourth quarter impairment charge of \$0.4 million.

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If our future operating results decline significantly, we may be exposed to impairment losses that could be material (for additional discussion of this risk, see “Item 1A. Risk Factors - A significant decline in our operating profit and taxable income may impair our ability to realize the value of our long lived assets and deferred tax assets.”).

In addition to our annual store impairment reviews, we evaluate our other long-lived assets at each reporting period to determine whether impairment indicators are present. In 2011, we reviewed our operational needs surrounding travel and determined that we needed to replace an aircraft due in part to the repair costs and declining reliability of the aging aircraft. As a result of this decision, we both purchased a new aircraft to meet our needs and placed an older aircraft in the market as available-for-sale. We recorded a \$2.2 million impairment charge on the held-for-sale aircraft, based on market conditions at the time the decision was executed.

### Share-Based Compensation

We grant stock options, non-vested restricted stock awards, and performance share units to our employees under shareholder approved incentive plans. Share-based compensation expense was \$13.2 million, \$17.9 million, and \$25.0 million in 2013, 2012, and 2011, respectively. Future share-based compensation expense for stock options is dependent upon the number and terms of future stock option awards and many estimates, judgments and assumptions used in arriving at the fair value of stock options. Future share-based compensation expense for the non-vested restricted stock awards are dependent upon the future number of awards, fair value of our common shares on the grant date, and the estimated vesting period. Future share-based compensation expense for performance share units is dependent upon the future number of awards, the estimated vesting period, and many estimates, judgments and assumptions used in arriving at the fair value of performance share units. Future share-based compensation expense related to stock options, non-vested restricted stock, and performance share units may vary materially from the currently amortizing awards.

We estimate the fair value of our stock options using a binomial model. The binomial model takes into account estimates, assumptions, and judgments about our stock price volatility, our dividend yield rate, the risk-free rate of return, the contractual term of the option, the probability that the option will be exercised prior to the end of its contractual life, and the probability of retirement of the option holder in computing the value of the option. Expected volatility is based on historical and current implied volatilities from traded options on our common shares and those of our peers. The dividend yield rate on our common shares is assumed to be zero since we have not paid dividends and have no current plans to do so. The risk-free rate is based on U.S. Treasury security yields at the time of the grant. The expected life is determined from the application of the binomial model and includes assumptions such as the expected employee exercise behavior and our expected forfeiture rate, which is based on analysis of historical data.

Compensation expense for non-vested restricted stock awards are recorded over the estimated vesting period based on the estimated achievement date of the performance criteria. An estimated target achievement date is determined at the time of the award based on historical and forecasted performance of similar measures. We monitor the achievement of the performance targets at each reporting period and make adjustments to the estimated vesting period when our models indicate that the estimated achievement date differs from the date being used to amortize expense. Any change in the estimated vesting date results in a prospective change to the related expense by charging the remaining unamortized expense over the remaining expected vesting period at the date the estimate was changed.

Compensation expense for performance share units is recorded over the estimated vesting period based on the estimated achievement date of the performance criteria. An estimated target achievement date is determined at the time of the award based on performing certain Monte Carlo simulation. We monitor the achievement of the performance targets at each reporting period and make adjustments to the estimated vesting period when our models indicate that the estimated achievement date differs from the date being used to amortize expense. Any change in the estimated vesting date results in a prospective change to the related expense by charging the remaining unamortized expense over the remaining expected vesting period at the date the estimate was changed.

Income Taxes

The determination of our income tax expense, refunds receivable, income taxes payable, deferred tax assets and liabilities and financial statement recognition, de-recognition and/or measurement of uncertain tax benefits (for positions taken or to be taken on income tax returns) requires significant judgment, the use of estimates, and the interpretation and application of complex accounting and multi-jurisdictional income tax laws.

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The effective income tax rate in any period may be materially impacted by the overall level of income (loss) before income taxes, the jurisdictional mix and magnitude of income (loss), changes in the income tax laws (which may be retroactive to the beginning of the fiscal year), subsequent recognition, de-recognition and/or measurement of an uncertain tax benefit, changes in deferred tax asset valuation allowances and adjustments of a deferred tax asset or liability for enacted changes in tax laws or rates. Although we believe that our estimates are reasonable, actual results could differ from these estimates resulting in a final tax outcome that may be materially different from that which is reflected in our consolidated financial statements.

We evaluate our ability to recover our deferred tax assets within the jurisdiction from which they arise. We consider all available positive and negative evidence including recent financial results, projected future pretax accounting income from continuing operations and tax planning strategies (when necessary). This evaluation requires us to make assumptions that require significant judgment about the forecasts of future pretax accounting income. The assumptions that we use in this evaluation are consistent with the assumptions and estimates used to develop our consolidated operating financial plans. If we determine that a portion of our deferred tax assets, which principally represent expected future deductions or benefits, are not likely to be realized, we recognize a valuation allowance for our estimate of these benefits which we believe are not likely recoverable. Additionally, changes in tax laws, apportionment of income for state and provincial tax purposes, and rates could also affect recorded deferred tax assets.

We evaluate the uncertainty of income tax positions taken or to be taken on income tax returns. When a tax position meets the more-likely-than-not threshold, we recognize economic benefits associated with the position on our consolidated financial statements. The more-likely-than-not recognition threshold is a positive assertion that an enterprise believes it is entitled to economic benefits associated with a tax position. When a tax position does not meet the more-likely-than-not threshold, or in the case of those positions that do meet the threshold but are measured at less than the full benefit taken on the return, we recognize tax liabilities (or de-recognize tax assets, as the case may be). A number of years may elapse before a particular matter, for which we have derecognized a tax benefit, is audited and fully resolved or clarified. We adjust unrecognized tax benefits and the income tax provision in the period in which an uncertain tax position is effectively or ultimately settled, the statute of limitations expires for the relevant taxing authority to examine the tax position, or as a result of the evaluation of new information that becomes available.

#### Pension

Actuarial valuations are used to calculate the estimated expenses and obligations for our Pension Plan and Supplemental Pension Plan. Inherent in the actuarial valuations are several assumptions including discount rate and expected return on plan assets. We review external data and historical trends to help determine the discount rate and expected long-term rate of return. Our objective in selecting a discount rate is to identify the best estimate of the rate at which the benefit obligations would be settled on the measurement date. In making this estimate, we review rates of return on high-quality, fixed-income investments available at the measurement date and expected to be available during the period to maturity of the benefits. This process includes a review of the bonds available on the measurement date with a quality rating of Aa or better. The expected long-term rate of return on assets is derived from detailed periodic studies, which include a review of asset allocation strategies, anticipated future long-term performance of individual asset classes, risks (standard deviations) and correlations of returns among the asset classes that comprise the plan's asset mix. While the studies give appropriate consideration to recent plan performance and historical returns, the assumption is primarily a long-term, prospective rate of return. The weighted average discount rate used to determine the net periodic pension cost for 2013 was 4.6%. A 1.0% decrease in the discount rate would increase net periodic pension cost by \$0.6 million. The long-term rate of return on assets used to determine net periodic pension cost in 2013 was 5.1%. A 1.0% decrease in the expected long-term rate of return on plan assets would increase the net periodic pension cost by \$0.5 million.

During 2013, we reclassified \$1.0 million, net of tax, from other comprehensive income to expense in our consolidated statement of operations. We also recognized a benefit of \$0.1 million, net of tax, to other comprehensive



income in 2013, which was principally driven by the recognition of \$0.1 million (pretax) in settlement charges as participants elected more lump sum payments than originally estimated. At February 1, 2014, the accumulated other comprehensive income amount associated with the plans, which was principally unrealized actuarial loss, was an \$8.5 million loss, net of tax. During 2013, and in future periods, we expect to reclassify approximately \$1.2 million from other comprehensive income to expense, assuming we achieve our estimated rate of return on pension plan investments in future periods. Additionally, in the event that we have future settlements, as occurred in 2013, 2012 and 2011, we would expect that the pretax expense related to future settlements would be in the range of \$0.3 million to \$1.8 million in charges based on historical experience.

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### Insurance and Insurance-Related Reserves

We are self-insured for certain losses relating to property, general liability, workers' compensation, and employee medical and dental benefit claims, a portion of which is funded by employees. We purchase stop-loss coverage from third party insurance carriers to limit individual or aggregate loss exposure in these areas. Accrued insurance liabilities and related expenses are based on actual claims reported and estimates of claims incurred but not reported. The estimated loss accruals for claims incurred but not paid are determined by applying actuarially-based calculations taking into account historical claims payment results and known trends such as claims frequency and claims severity. Management makes estimates, judgments, and assumptions with respect to the use of these actuarially-based calculations, including but not limited to, estimated health care cost trends, estimated lag time to report and pay claims, average cost per claim, network utilization rates, network discount rates, and other factors. A 10% change in our self-insured liabilities at February 1, 2014 would have affected selling and administrative expenses, operating profit, and income from continuing operations before income taxes by approximately \$7 million.

General liability and workers' compensation liabilities are recorded at our estimate of their net present value, using a 4.0% discount rate, while other liabilities for insurance reserves are not discounted. A 1.0% change in the discount rate on these liabilities would have affected selling and administrative expenses, operating profit, and income from continuing operations before income taxes by approximately \$1.9 million.

### Costs Associated with Exit or Disposal Activities

Our accruals for costs associated with exit or disposal activities arise from management's decision to wind down certain operations and require significant judgment, the use of estimates, and the interpretation and application of complex accounting principles. The accruals for costs associated with exit or disposal activities primarily consist of contract termination costs, principally related to operating leases, and severance benefits. For our contract termination cost estimates, management utilizes the advice and input of outside real estate specialists when determining its valuation of the liabilities. The accruals for contract termination costs and severance benefits factor in many variables including, but not limited to, expected vacancy periods, tenancy rates per square foot, buy-out scenarios, costs of capital, operating performance during the wind down period, and forfeitures. A 10% change in our accrued liabilities for costs associated with exit disposal activities at February 1, 2014 would have affected selling and administrative expenses, operating profit, and income from continuing operations before income taxes by approximately \$0.4 million.

### Lease Accounting

In order to recognize rent expense on our leases, we evaluate many factors to identify the lease term such as the contractual term of the lease, our assumed possession date of the property, renewal option periods, and the estimated value of leasehold improvement investments that we are required to make. Based on this evaluation, our lease term is typically the minimum contractually obligated period over which we have control of the property. This term is used because although many of our leases have renewal options, we typically do not incur an economic or contractual penalty in the event of non-renewal. Therefore, we typically use the initial minimum lease term for purposes of calculating straight-line rent, amortizing deferred rent, and recognizing depreciation expense on our leasehold improvements.

### Commitments

For a discussion on certain of our commitments, refer to note 3, note 5, note 10, note 13, and note 14 to the accompanying consolidated financial statements.

### Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are subject to market risk from exposure to changes in interest rates on investments and on borrowings under the 2011 Credit Agreement that we make from time to time. We had borrowings of \$77.0 million under the 2011 Credit

Agreement at February 1, 2014. An increase of 1.0% in our variable interest rate on our investments and expected future borrowings would not have a material effect on our financial condition, results of operations, or liquidity.

Through the operations of Big Lots Canada, we are subject to market risks associated with foreign currency exchange rate fluctuations between the Canadian Dollar and the U.S. Dollar. An increase or decrease of 1% in foreign currency exchange rates would not have a material effect on our financial condition, results of operations, or liquidity.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Big Lots, Inc.  
Columbus, Ohio

We have audited the internal control over financial reporting of Big Lots, Inc. and subsidiaries (the "Company") as of February 1, 2014, based on criteria established in Internal Control - Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting in Item 9A. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of February 1, 2014, based on the criteria established in Internal Control - Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended February 1, 2014 of the Company and our report dated April 1, 2014 expressed an unqualified opinion on those consolidated financial statements.

/s/ DELOITTE & TOUCHE LLP

Dayton, Ohio  
April 1, 2014

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Big Lots, Inc.  
Columbus, Ohio

We have audited the accompanying consolidated balance sheets of Big Lots, Inc. and subsidiaries (the "Company") as of February 1, 2014 and February 2, 2013, and the related consolidated statements of operations, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended February 1, 2014. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Big Lots, Inc. and subsidiaries at February 1, 2014 and February 2, 2013, and the results of their operations and their cash flows for each of the three years in the period ended February 1, 2014, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of February 1, 2014, based on the criteria established in Internal Control - Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 1, 2014 expressed an unqualified opinion on the Company's internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

Dayton, Ohio  
April 1, 2014

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## BIG LOTS, INC. AND SUBSIDIARIES

## Consolidated Statements of Operations

(In thousands, except per share amounts)

|   | 2013        | 2012        | 2011        |
|---|-------------|-------------|-------------|
| Net sales   | \$5,301,912 | \$5,367,165 | \$5,159,249 |
| Cost of sales (exclusive of depreciation expense shown separately below)  | 3,236,606   | 3,254,837   | 3,096,200   |
| Gross margin  | 2,065,306   | 2,112,328   | 2,063,049   |
| Selling and administrative expenses   | 1,759,745   | 1,708,160   | 1,629,218   |
| Depreciation expense  | 115,122     | 106,137     | 90,135      |
| Operating profit  | 190,439     | 298,031     | 343,696     |
| Interest expense  | (3,339)     | (4,192)     | (3,530)     |
| Other income (expense)  | (1,213)     | 51          | (173)       |
| Income from continuing operations before income taxes   | 185,887     | 293,890     | 339,993     |
| Income tax expense  | 61,118      | 116,921     | 133,835     |
| Income from continuing operations   | 124,769     | 176,969     | 206,158     |
| Income from discontinued operations, net of tax expense of \$351, \$195 and \$710 in fiscal years 2013, 2012 and 2011, respectively | 526         | 152         | 906         |
| Net income  | \$125,295   | \$177,121   | \$207,064   |
| <br>  |             |             |             |
| Earnings per common share - basic   |             |             |             |
| Continuing operations   | \$2.17      | \$2.96      | \$3.02      |
| Discontinued operations   | 0.01        | —           | 0.01        |
|   | \$2.18      | \$2.96      | \$3.03      |
| <br>  |             |             |             |
| Earnings per common share - diluted   |             |             |             |
| Continuing operations   | \$2.15      | \$2.93      | \$2.97      |
| Discontinued operations   | 0.01        | —           | 0.01        |
|   | \$2.16      | \$2.93      | \$2.98      |

The accompanying notes are an integral part of these consolidated financial statements.

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## BIG LOTS, INC. AND SUBSIDIARIES

## Consolidated Statements of Comprehensive Income

(In thousands)

|  | 2013      | 2012      | 2011      |   |
|--|-----------|-----------|-----------|---|
| Net income   | \$125,295 | \$177,121 | \$207,064 |   |
| Other comprehensive income (loss):   |           |           |           |   |
| Foreign currency translation   | (3,589    | ) (383    | ) (1,050  | ) |
| Amortization of pension, net of tax benefit of \$(665), \$(921), and \$(703), respectively                     | 1,005     | 1,403     | 1,066     |   |
| Valuation adjustment of pension, net of tax (benefit) expense of \$(1,589), \$(766), and \$3,337, respectively | 2,403     | 1,169     | (5,065    | ) |
| Total other comprehensive income (loss)  | (181      | ) 2,189   | (5,049    | ) |
| Comprehensive income   | \$125,114 | \$179,310 | \$202,015 |   |

The accompanying notes are an integral part of these consolidated financial statements.



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## BIG LOTS, INC. AND SUBSIDIARIES

## Consolidated Balance Sheets

(In thousands, except par value)

|   | February 1, 2014 | February 2, 2013 |
|---|------------------|------------------|
| <b>ASSETS</b>   |                  |                  |
| Current assets:   |                  |                  |
| Cash and cash equivalents   | \$68,629         | \$60,581         |
| Inventories   | 914,965          | 918,023          |
| Deferred income taxes   | 59,781           | 37,696           |
| Other current assets  | 77,686           | 74,330           |
| Total current assets  | 1,121,061        | 1,090,630        |
| Property and equipment - net  | 569,682          | 593,562          |
| Deferred income taxes   | 5,106            | —                |
| Goodwill  | —                | 13,522           |
| Other assets  | 43,750           | 55,912           |
| Total assets  | \$1,739,599      | \$1,753,626      |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>   |                  |                  |
| Current liabilities:  |                  |                  |
| Accounts payable  | \$365,772        | \$393,652        |
| Property, payroll, and other taxes  | 73,334           | 74,973           |
| Accrued operating expenses  | 57,167           | 53,788           |
| Insurance reserves  | 37,607           | 36,861           |
| KB bankruptcy lease obligation  | —                | 3,069            |
| Accrued salaries and wages  | 29,175           | 26,753           |
| Income taxes payable  | 14,392           | 40,538           |
| Total current liabilities   | 577,447          | 629,634          |
| Long-term obligations   | 77,000           | 171,200          |
| Deferred income taxes   | —                | 2,693            |
| Deferred rent   | 76,364           | 73,658           |
| Insurance reserves  | 55,755           | 63,332           |
| Unrecognized tax benefits   | 17,975           | 16,335           |
| Other liabilities   | 33,631           | 38,632           |
| Shareholders' equity:   |                  |                  |
| Preferred shares - authorized 2,000 shares; \$0.01 par value; none issued   | —                | —                |
| Common shares - authorized 298,000 shares; \$0.01 par value; issued 117,495 shares; outstanding 57,548 shares and 57,269 shares, respectively | 1,175            | 1,175            |
| Treasury shares - 59,947 shares and 60,226 shares, respectively, at cost  | (1,670,041)      | (1,677,610)      |
| Additional paid-in capital  | 562,447          | 551,845          |
| Retained earnings   | 2,021,357        | 1,896,062        |
| Accumulated other comprehensive loss  | (13,511)         | (13,330)         |
| Total shareholders' equity  | 901,427          | 758,142          |
| Total liabilities and shareholders' equity  | \$1,739,599      | \$1,753,626      |

The accompanying notes are an integral part of these consolidated financial statements.

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## BIG LOTS, INC. AND SUBSIDIARIES

## Consolidated Statements of Shareholders' Equity

(In thousands)

|  | Common   |          | Treasury |               | Additional<br>Paid-In<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Loss |           | Total |
|--|----------|----------|----------|---------------|----------------------------------|----------------------|---|-----------|-------|
|  | Shares   | Amount   | Shares   | Amount        |                                  |                      |   |           |       |
| Balance - January 29,<br>2011                              | 73,894   | \$ 1,175 | 43,601   | \$(1,079,130) | \$523,341                        | \$ 1,511,877         | \$(10,470)                                    | \$946,793 |       |
| Comprehensive income                                       | —        | —        | —        | —             | —                                | 207,064              | (5,049)                                       | 202,015   |       |
| Purchases of common<br>shares                              | (11,063) | —        | 11,063   | (363,957)     | —                                | —                    | —   | (363,957) |       |
| Exercise of stock<br>options                               | 500      | —        | (500)    | 12,800        | (2,391)                          | —                    | —   | 10,409    |       |
| Restricted shares vested                                   | 271      | —        | (271)    | 6,731         | (6,731)                          | —                    | —   | —         |       |
| Tax benefit from<br>share-based awards                     | —        | —        | —        | —             | 2,701                            | —                    | —   | 2,701     |       |
| Share activity related to<br>deferred compensation<br>plan | 7        | —        | (7)      | 32            | 247                              | —                    | —   | 279       |       |
| Share-based employee<br>compensation expense               | —        | —        | —        | —             | 24,993                           | —                    | —   | 24,993    |       |
| Balance - January 28,<br>2012                              | 63,609   | 1,175    | 53,886   | (1,423,524)   | 542,160                          | 1,718,941            | (15,519)                                      | 823,233   |       |
| Comprehensive income                                       | —        | —        | —        | —             | —                                | 177,121              | 2,189   | 179,310   |       |
| Purchases of common<br>shares                              | (8,232)  | —        | 8,232    | (304,038)     | —                                | —                    | —   | (304,038) |       |
| Exercise of stock<br>options                               | 1,406    | —        | (1,406)  | 37,266        | (3,978)                          | —                    | —   | 33,288    |       |
| Restricted shares vested                                   | 478      | —        | (478)    | 12,649        | (12,649)                         | —                    | —   | —         |       |
| Tax benefit from<br>share-based awards                     | —        | —        | —        | —             | 8,117                            | —                    | —   | 8,117     |       |
| Share activity related to<br>deferred compensation<br>plan | 8        | —        | (8)      | 37            | 316                              | —                    | —   | 353       |       |
| Share-based employee<br>compensation expense               | —        | —        | —        | —             | 17,879                           | —                    | —   | 17,879    |       |
| Balance - February 2,<br>2013                              | 57,269   | 1,175    | 60,226   | (1,677,610)   | 551,845                          | 1,896,062            | (13,330)                                      | 758,142   |       |
| Comprehensive income                                       | —        | —        | —        | —             | —                                | 125,295              | (181)   | 125,114   |       |
| Purchases of common<br>shares                              | (6)      | —        | 6        | (214)         | —                                | —                    | —   | (214)     |       |
| Exercise of stock<br>options                               | 214      | —        | (214)    | 5,949         | (1,065)                          | —                    | —   | 4,884     |       |
| Restricted shares vested                                   | 65       | —        | (65)     | 1,805         | (1,805)                          | —                    | —   | —         |       |
| Tax benefit from<br>share-based awards                     | —        | —        | —        | —             | 123                              | —                    | —   | 123       |       |
| Share activity related to<br>deferred compensation         | 6        | —        | (6)      | 29            | 166                              | —                    | —   | 195       |       |

|   |        |         |        |               |           |             |            |           |
|---|--------|---------|--------|---------------|-----------|-------------|------------|-----------|
| plan                                      |        |         |        |               |           |             |            |           |
| Share-based employee compensation expense | —      | —       | —      | —             | 13,183    | —           | —          | 13,183    |
| Balance - February 1, 2014                | 57,548 | \$1,175 | 59,947 | \$(1,670,041) | \$562,447 | \$2,021,357 | \$(13,511) | \$901,427 |

The accompanying notes are an integral part of these consolidated financial statements.

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## BIG LOTS, INC. AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

(In thousands)

|  | 2013       | 2012        | 2011        |
|--|------------|-------------|-------------|
| Operating activities:  |            |             |             |
| Net income   | \$ 125,295 | \$ 177,121  | \$ 207,064  |
| Adjustments to reconcile net income to net cash provided by operating activities:                    |            |             |             |
| Depreciation and amortization expense  | 102,196    | 95,602      | 82,851      |
| Deferred income taxes  | (32,138)   | ) 12,482    | 10,456      |
| Non-cash share-based compensation expense  | 13,183     | 17,879      | 24,993      |
| Excess tax benefit from share-based awards   | (123)      | ) (8,144)   | ) (2,701)   |
| Non-cash impairment charge   | 21,091     | 984         | 2,242       |
| (Gain) loss on disposition of property and equipment   | (3,036)    | ) 432       | 1,376       |
| Pension expense, net of contributions  | 3,378      | 3,810       | 2,023       |
| Change in assets and liabilities, excluding effects of acquisition and foreign currency adjustments: |            |             |             |
| Inventories  | 1,385      | (92,721)    | ) (54,512)  |
| Accounts payable   | (27,468)   | ) 43,460    | 31,555      |
| Current income taxes   | (28,538)   | ) 9,844     | 10,293      |
| Other current assets   | 420        | (4,078)     | ) (6,082)   |
| Other current liabilities  | 4,350      | 397         | (16,465)    |
| Other assets   | 10,300     | (17,894)    | ) (4,098)   |
| Other liabilities  | 8,039      | 41,959      | 29,476      |
| Net cash provided by operating activities  | 198,334    | 281,133     | 318,471     |
| Investing activities:  |            |             |             |
| Capital expenditures   | (104,786)  | ) (131,273) | ) (131,293) |
| Cash proceeds from sale of property and equipment  | 7,260      | 912         | 867         |
| Purchase of business, net of cash acquired   | —          | —           | 1,835       |
| Return from restricted account   | —          | —           | 8,000       |
| Other  | 31         | 4           | (121)       |
| Net cash used in investing activities  | (97,495)   | ) (130,357) | ) (120,712) |
| Financing activities:  |            |             |             |
| Net proceeds from borrowings under bank credit facility  | (94,200)   | ) 105,300   | 65,900      |
| Payment of notes payable   | —          | —           | (16,664)    |
| Payment of capital lease obligations   | (1,089)    | ) (1,321)   | ) (1,953)   |
| Proceeds from the exercise of stock options  | 4,884      | 33,288      | 10,409      |
| Excess tax benefit from share-based awards   | 123        | 8,144       | 2,701       |
| Payment for treasury shares acquired   | (214)      | ) (304,038) | ) (363,957) |
| Deferred bank credit facility fees paid  | (895)      | ) —         | (2,970)     |
| Other  | 195        | 353         | 279         |
| Net cash used in financing activities  | (91,196)   | ) (158,274) | ) (306,255) |
| Impact of foreign currency on cash   | (1,595)    | ) (468)     | ) (496)     |
| Increase (Decrease) in cash and cash equivalents   | 8,048      | (7,966)     | ) (108,992) |
| Cash and cash equivalents:   |            |             |             |
| Beginning of year  | 60,581     | 68,547      | 177,539     |
| End of year  | \$ 68,629  | \$ 60,581   | \$ 68,547   |

The accompanying notes are an integral part of these consolidated financial statements.

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BIG LOTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE 1 – BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

We are the largest broadline closeout retailer in the U.S. At February 1, 2014, we operated 1,570 stores in the United States of America (“U.S.”) and Canada. Our goal is to strengthen and build upon our leadership position in broadline closeout retailing by providing our customers with great savings on brand-name closeouts and other value-priced merchandise.

During the first quarter of 2014, we ceased all operations in Canada. Please see the Canadian Segment section of note 13 to the consolidated financial statements for further information on the wind down of our operations in Canada.

Basis of Presentation

The consolidated financial statements include Big Lots, Inc. and all of its subsidiaries, have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”), and include all of our accounts. We consolidate all majority-owned and controlled subsidiaries. All intercompany accounts and transactions have been eliminated.

Management Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates, judgments, and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period, as well as the related disclosure of contingent assets and liabilities at the date of the financial statements. The use of estimates, judgments, and assumptions creates a level of uncertainty with respect to reported or disclosed amounts in our consolidated financial statements or accompanying notes. On an ongoing basis, management evaluates its estimates, judgments, and assumptions, including those that management considers critical to the accurate presentation and disclosure of our consolidated financial statements and accompanying notes. Management bases its estimates, judgments, and assumptions on historical experience, current trends, and various other factors that it believes are reasonable under the circumstances. Because of the inherent uncertainty in using estimates, judgments, and assumptions, actual results may differ from these estimates.

Fiscal Periods

Our fiscal year ends on the Saturday nearest to January 31, which results in fiscal years consisting of 52 or 53 weeks. Unless otherwise stated, references to years in this report relate to fiscal years rather than calendar years. Fiscal year 2013 (“2013”) is comprised of the 52 weeks that began on February 3, 2013 and ended on February 1, 2014. Fiscal year 2012 (“2012”) was comprised of the 53 weeks that began on January 29, 2012 and ended on February 2, 2013. Fiscal year 2011 (“2011”) was comprised of the 52 weeks that began on January 30, 2011 and ended on January 28, 2012.

Segment Reporting

We manage our broadline closeout retailing business based on two segments: the U.S. and Canada.

Cash and Cash Equivalents

Cash and cash equivalents primarily consist of amounts on deposit with financial institutions, outstanding checks, credit and debit card receivables, and highly liquid investments, including money market funds and variable rate demand notes, which are unrestricted to withdrawal or use and which have an original maturity of three months or less. We review cash and cash equivalent balances on a bank by bank basis in order to identify book overdrafts. Book

overdrafts occur when the amount of outstanding checks exceed the cash deposited at a given bank. We reclassify book overdrafts, if any, to accounts payable on our consolidated balance sheets. Amounts due from banks for credit and debit card transactions are typically settled in less than seven days, and at February 1, 2014 and February 2, 2013, totaled \$24.5 million and \$24.6 million, respectively.

#### Restricted Cash

Our restricted cash served as collateral, in place of an irrevocable stand-by letter of credit, to provide financial assurance that we would fulfill our obligations with respect to cash requirements associated with self-insurance. The cash was on deposit with our insurance carrier.

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### Investments

Investment securities are classified as available-for-sale, held-to-maturity, or trading at the date of purchase. Investments are recorded at fair value as either current assets or non-current assets based on the stated maturity or our plans to either hold or sell the investment. Unrealized holding gains and losses on trading securities are recognized in earnings. Unrealized holding gains and losses on available-for-sale securities are recognized in other comprehensive income, until realized. We did not own any held-to-maturity or available-for-sale securities as of February 1, 2014 and February 2, 2013.

### Merchandise Inventories

Merchandise inventories are valued at the lower of cost or market using the average cost retail inventory method. Cost includes any applicable inbound shipping and handling costs associated with the receipt of merchandise into our distribution centers (See the discussion below under the caption "Selling and Administrative Expenses" for additional information regarding outbound shipping and handling costs to our stores). Market is determined based on the estimated net realizable value, which generally is the merchandise selling price. Under the average cost retail inventory method, inventory is segregated into classes of merchandise having similar characteristics at its current retail selling value. Current retail selling values are converted to a cost basis by applying an average cost factor to each specific merchandise class' retail selling value. Cost factors represent the average cost-to-retail ratio computed using beginning inventory and all fiscal year-to-date purchase activity specific to each merchandise class.

Under our previous inventory management system which was used through the end of 2011, we calculated average cost at the department level which constituted 50 inventory cost pools. On January 29, 2012, the first day of 2012, we completed the implementation of our new inventory management systems, which has allowed us to more precisely determine our inventory cost under the average cost retail inventory method. We now calculate average cost at the class level which constitutes approximately 350 inventory cost pools.

As the impact of the accounting change in the beginning of the 2012 inventory was immaterial, we recognized the cumulative effect of the change in accounting principle as an expense in 2012 by recording a reduction in inventory and a corresponding increase to cost of sales of approximately \$5.6 million in the first quarter of 2012. This non-cash charge reduced the 2012 income from continuing operations and net income by approximately \$3.4 million and reduced 2012 basic and diluted earnings per share from continuing operations by \$0.06.

Under the average cost retail inventory method, permanent sales price markdowns result in cost reductions in inventory. Our permanent sales price markdowns are typically related to end of season clearance events and are recorded as a charge to cost of sales in the period of management's decision to initiate sales price reductions with the intent not to return the price to regular retail. Promotional markdowns are recorded as a charge to net sales in the period the merchandise is sold. Promotional markdowns are typically related to specific marketing efforts with respect to products maintained continuously in our stores or products that are only available in limited quantities but represent substantial value to our customers. Promotional markdowns are principally used to drive higher sales volume during a defined promotional period.

We record a reduction to inventories and charge to cost of sales for a shrinkage inventory allowance. The shrinkage allowance is calculated as a percentage of sales for the period from the last physical inventory date to the end of the reporting period. Such estimates are based on our historical and current year experience based on physical inventory results.

We record a reduction to inventories and charge to cost of sales for any excess or obsolete inventory. The excess or obsolete inventory is estimated based on a review of our aged inventory and takes into account any items that have already received a cost reduction as a result of the permanent markdown process discussed above. We estimate the reduction for excess or obsolete inventory based on historical sales trends, age and quantity of product on hand, and



anticipated future sales.

**Payments Received from Vendors**

Payments received from vendors relate primarily to rebates and reimbursement for markdowns and are recognized in our consolidated statements of operations as a reduction to cost of inventory purchases in the period that the rebate or reimbursement is earned or realized and, consequently, result in a reduction in cost of sales when the related inventory is sold.

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## Store Supplies

When opening a new store, a portion of the initial shipment of supplies (including primarily display materials, signage, security-related items, and miscellaneous store supplies) is capitalized at the store opening date. These capitalized supplies represent more durable types of items for which we expect to receive future economic benefit. Subsequent replenishments of capitalized store supplies are expensed. The consumable/non-durable type items for which the future economic benefit is less measurable are expensed upon shipment to the store. Capitalized store supplies are adjusted periodically for changes in estimated quantities or costs and are included in other current assets in our consolidated balance sheets.

## Property and Equipment - Net

Depreciation and amortization expense of property and equipment are recorded on a straight line basis using estimated service lives. The estimated service lives of our property and equipment by major asset category were as follows:

|  |              |
|--|--------------|
| Land improvements                                      | 15 years     |
| Buildings  | 40 years     |
| Leasehold improvements                                 | 5 years      |
| Store fixtures and equipment                           | 5 years      |
| Distribution and transportation fixtures and equipment | 5 - 15 years |
| Office and computer equipment                          | 5 years      |
| Computer software costs                                | 5 - 8 years  |
| Company vehicles                                       | 3 years      |

Leasehold improvements are amortized on a straight-line basis using the shorter of their estimated service lives or the lease term. Because our most common initial lease term range from five to seven years and the majority of our lease options have a term of five years, we estimate the useful life of leasehold improvements at five years. This amortization period is consistent with the amortization period for any lease incentives that we would typically receive when initially entering into a new lease that are recognized as deferred rent and amortized over the initial lease term. Depreciation estimates are revised prospectively to reflect the remaining depreciation or amortization of the asset over the shortened estimated service life when a decision is made to dispose of property and equipment prior to the end of its previously estimated service life. The cost of assets sold or retired and the related accumulated depreciation are removed from the accounts with any resulting gain or loss included in selling and administrative expenses. Major repairs that extend service lives are capitalized. Maintenance and repairs are charged to expense as incurred. Capitalized interest was not significant in any period presented.

## Long-Lived Assets

Our long-lived assets primarily consist of property and equipment - net. In order to determine if impairment indicators are present for store property and equipment, we review historical operating results at the store level on an annual basis, or when other impairment indicators are present. Generally, all other property and equipment is reviewed for impairment at the enterprise level. If the net book value of a store's long-lived assets is not recoverable by the expected future cash flows of the store, we estimate the fair value of the store's assets and recognize an impairment charge for the excess net book value of the store's long-lived assets over their fair value. Our assumptions related to estimates of future cash flows are based on historical results of cash flows adjusted for management projections for future periods. We estimate the fair value of our long-lived assets using expected cash flows, including salvage value, which is based on readily available market information for similar assets.

## Goodwill

Instead of being amortized, goodwill is tested for impairment annually and whenever events or changes in circumstances indicate the carrying value of the asset may not be recoverable. We use an income approach and a

market approach in determining fair value for purposes of goodwill impairment tests. We perform our annual impairment testing during our second fiscal quarter of each year.

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### Closed Store Accounting

We recognize an obligation for the fair value of lease termination costs when we cease using the leased property in our operations. In measuring fair value of these lease termination obligations, we consider the remaining minimum lease payments, estimated sublease rentals that could be reasonably obtained, and other potentially mitigating factors. We discount the estimated obligation using the applicable credit adjusted interest rate, resulting in accretion expense in periods subsequent to the period of initial measurement. We monitor the estimated obligation for lease termination liabilities in subsequent periods and revise any estimated liabilities, if necessary. Severance and benefits associated with terminating employees from employment are recognized ratably from the communication date through the estimated future service period, unless the estimated future service period is less than 60 days, in which case we recognize the impact at the communication date. Generally all other store closing costs are recognized when incurred.

When material, we classify the results of operations of closed stores to discontinued operations when the operations and cash flows of the stores have been (or will be) eliminated from ongoing operations and we no longer have any significant continuing involvement in the operations associated with the stores after closure. We generally meet the second criteria on all closed stores as, upon closure, operations cease and we have no continuing involvement. To determine if cash flows have been (or will be) eliminated from ongoing operations, we evaluate a number of qualitative and quantitative factors, including, but not limited to, proximity of a closing store to any remaining open stores and the estimated sales migration from the closed store to any stores remaining open. The estimated sales migration is based on historical estimates of our sales migration upon opening or closing a store in a similar market. For purposes of reporting closed stores as discontinued operations, we report net sales, gross margin, and related operating costs that are directly related to and specifically identifiable with respect to the stores' operations identified as discontinued operations. Certain corporate-level charges, such as general office cost, field operations, national advertising, fixed distribution costs, and interest cost are not allocated to closed stores' discontinued operations because we believe that these costs are not specific to the stores' operations.

### Income Taxes

We account for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statement basis and tax basis of assets and liabilities using enacted law and tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

We assess the adequacy and need for a valuation allowance for deferred tax assets. In making such determination, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial operations. We have established a valuation allowance to reduce our deferred tax assets to the balance that is more likely than not to be realized.

We recognize interest and penalties related to unrecognized tax benefits within the income tax expense line in the accompanying consolidated statements of operations. Accrued interest and penalties are included within the related tax liability line in the accompanying consolidated balance sheets.

The effective income tax rate in any period may be materially impacted by the overall level of income (loss) before income taxes, the jurisdictional mix and magnitude of income (loss), changes in the income tax laws (which may be retroactive to the beginning of the fiscal year), subsequent recognition, de-recognition and/or measurement of an uncertain tax benefit, changes in a deferred tax valuation allowance, and adjustments of a deferred tax asset or liability for enacted changes in tax laws or rates.



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### Pension

Pension assumptions are evaluated each year. Actuarial valuations are used to calculate the estimated expenses and obligations related to our pension plans. We review external data and historical trends to help determine the discount rate and expected long-term rate of return. Our objective in selecting a discount rate is to identify the best estimate of the rate at which the benefit obligations would be settled on the measurement date. In making this estimate, we review rates of return on high-quality, fixed-income investments available at the measurement date and expected to be available during the period to maturity of the benefits. This process includes a review of the bonds available on the measurement date with a quality rating of Aa or better. The expected long-term rate of return on assets is derived from detailed periodic studies, which include a review of asset allocation strategies, anticipated future long-term performance of individual asset classes, risks (standard deviations), and correlations of returns among the asset classes that comprise the plan's asset mix. While the studies give appropriate consideration to recent plan performance and historical returns, the assumption for the expected long-term rate of return is primarily based on our expectation of a long-term, prospective rate of return.

### Insurance and Insurance-Related Reserves

We are self-insured for certain losses relating to property, general liability, workers' compensation, and employee medical and dental benefit claims, a portion of which is paid by employees. We purchase stop-loss coverage to limit significant exposure in these areas. Accrued insurance-related liabilities and related expenses are based on actual claims filed and estimates of claims incurred but not reported. The estimated accruals are determined by applying actuarially-based calculations. General liability and workers' compensation liabilities are recorded at our estimate of their net present value, using a 4% discount rate, while other liabilities for insurance-related reserves are not discounted.

### Fair Value of Financial Instruments

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy, as defined below, gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs.

Level 1, defined as observable inputs such as unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2, defined as observable inputs other than Level 1 inputs. These include quoted prices for similar assets or liabilities in an active market, quoted prices for identical assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

The carrying value of cash equivalents, accounts receivable, accounts payable, and accrued expenses approximates fair value because of the relatively short maturity of these items.

### Costs Associated with Exit or Disposal Activities

Our accruals for costs associated with exit or disposal activities primarily consist of contract termination costs, principally related to operating leases, and severance benefits. The costs arose from our decision to wind down the operations of certain businesses and/or segments. When determining the valuation of the liabilities for our contract termination cost estimates, we utilize the advice and input of outside experts who specialize in real estate activities. The accruals for contract termination costs and severance benefits factor in many variables including, but not limited to, expected vacancy periods, tenancy rates per square foot, buy-out scenarios, costs of capital, operating performance during the wind down period, and forfeitures. Additionally, these liabilities have been recorded at their net present value, which represents their fair value. Given the number of assumptions and the unobservable nature of certain of

the inputs, these accruals for costs associated with exit or disposal activities are considered to be Level 3.

#### Commitments and Contingencies

We are subject to various claims and contingencies including legal actions and other claims arising out of the normal course of business. In connection with such claims and contingencies, we estimate the likelihood and amount of any potential obligation, where it is possible to do so, using management's judgment. Management uses various internal and external specialists to assist in the estimating process. We accrue, if material, a liability if the likelihood of an adverse outcome is probable and the amount is estimable. If the likelihood of an adverse outcome is only reasonably possible (as opposed to probable), or if it is probable but an estimate is not determinable, disclosure of a material claim or contingency is made in the notes to our consolidated financial statements and no accrual is made.

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### Revenue Recognition

We recognize sales at the time the customer takes possession of the merchandise. Sales are recorded net of discounts and estimated returns and exclude any sales tax. The reserve for merchandise returns is estimated based on our prior return experience.

We sell gift cards in our stores and issue merchandise credits, typically as a result of customer returns, on stored value cards. We do not charge administrative fees on unused gift card or merchandise credit balances and our gift cards and merchandise credits do not expire. We recognize sales revenue from the use of gift cards and merchandise credits when (1) the gift card or merchandise credit is redeemed in a sales transaction by the customer or (2) breakage occurs. We recognize gift card and merchandise credit breakage when we estimate that the likelihood of the card or credit being redeemed by the customer is remote and we determine that we do not have a legal obligation to remit the value of unredeemed cards or credits to the relevant regulatory authority. We estimate breakage based upon historical redemption patterns. For 2013, 2012, and 2011, we recognized in net sales on our consolidated statements of operations breakage of \$0.2 million, \$0.5 million, and \$0.6 million, respectively, related to unredeemed gift card and merchandise credit balances that had aged at least four years beyond the end of their original issuance month. The liability for the unredeemed cash value of gift cards and merchandise credits is recorded in accrued operating expenses.

We offer price hold contracts on merchandise. Revenue for price hold contracts is recognized when the customer makes the final payment and takes possession of the merchandise. Amounts paid by customers under price hold contracts are recorded in accrued operating expenses until a sale is consummated.

### Cost of Sales

Cost of sales includes the cost of merchandise, net of cash discounts and rebates, markdowns, and inventory shrinkage. Cost of merchandise includes related inbound freight to our distribution centers, duties, and commissions. We classify warehousing and outbound distribution and transportation costs as selling and administrative expenses. Due to this classification, our gross margin rates may not be comparable to those of other retailers that include warehousing and outbound distribution and transportation costs in cost of sales.

### Selling and Administrative Expenses

Selling and administrative expenses include store expenses (such as payroll and occupancy costs) and costs related to warehousing, distribution, outbound transportation to our stores, advertising, purchasing, insurance, non-income taxes, and overhead. Selling and administrative expense rates may not be comparable to those of other retailers that include warehousing, distribution, and outbound transportation costs in cost of sales. Distribution and outbound transportation costs included in selling and administrative expenses were \$170.5 million, \$165.3 million, and \$159.6 million for 2013, 2012, and 2011, respectively.

### Rent Expense

Rent expense is recognized over the term of the lease and is included in selling and administrative expenses. We recognize minimum rent starting when possession of the property is taken from the landlord, which normally includes a construction or set-up period prior to store opening. When a lease contains a predetermined fixed escalation of the minimum rent, we recognize the related rent expense on a straight-line basis and record the difference between the recognized rental expense and the amounts payable under the lease as deferred incentive rent. We also receive tenant allowances, which are recorded in deferred incentive rent and are amortized as a reduction to rent expense over the term of the lease.

Our leases generally obligate us for our applicable portion of real estate taxes, common area maintenance (“CAM”), and property insurance that has been incurred by the landlord with respect to the leased property. We maintain accruals for our estimated applicable portion of real estate taxes, CAM, and property insurance incurred but not settled at each



reporting date. We estimate these accruals based on historical payments made and take into account any known trends. Inherent in these estimates is the risk that actual costs incurred by landlords and the resulting payments by us may be higher or lower than the amounts we have recorded on our books.

Certain of our leases provide for contingent rents that are not measurable at the lease inception date. Contingent rent includes rent based on a percentage of sales that are in excess of a predetermined level. Contingent rent is excluded from minimum rent and is included in the determination of total rent expense when it is probable that the expense has been incurred and the amount is reasonably estimable.

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### Advertising Expense

Advertising costs, which are expensed as incurred, consist primarily of television and print advertising, internet marketing and advertising, and in-store point-of-purchase presentations. Advertising expenses are included in selling and administrative expenses. Advertising expenses were \$98.6 million, \$101.1 million, and \$98.5 million for 2013, 2012, and 2011, respectively.

### Store Pre-opening Costs

Pre-opening costs incurred during the construction periods for new store openings are expensed as incurred and included in our selling and administrative expenses.

### Share-Based Compensation

Share-based compensation expense is recognized in selling and administrative expense in our consolidated statements of operations for all options that we expect to vest. We estimate forfeitures based on historical information. We value and expense stock options with graded vesting as a single award with an average estimated life over the entire term of the award. The expense for options with graded vesting is recorded straight-line over the vesting period. We estimate the fair value of stock options using a binomial model. The binomial model takes into account variables such as volatility, dividend yield rate, risk-free rate, contractual term of the option, the probability that the option will be exercised prior to the end of its contractual life, and the probability of retirement of the option holder in computing the value of the option. Expected volatility is based on historical and current implied volatilities from traded options on our common shares. The dividend yield on our common shares is assumed to be zero since we have not paid dividends and have no current plans to do so in the future. The risk-free rate is based on U.S. Treasury security yields at the time of the grant. The expected life is determined from the binomial model, which incorporates exercise and post-vesting forfeiture assumptions based on analysis of historical data.

Compensation expense for non-vested restricted stock awards and performance share units is recorded based on fair value of the award on the grant date and the estimated achievement date of the performance criteria. An estimated target achievement date is determined at the time of the award based on historical and forecasted performance of similar measures. We monitor the projected achievement of the performance targets at each reporting period and make prospective adjustments to the estimated vesting period when our internal models indicate that the estimated achievement date differs from the date being used to amortize expense.

### Earnings per Share

Basic earnings per share is based on the weighted-average number of shares outstanding during each period. Diluted earnings per share is based on the weighted-average number of shares outstanding during each period and the additional dilutive effect of stock options and non-vested restricted stock awards, calculated using the treasury stock method.

### Guarantees

We have lease guarantees which were issued prior to January 1, 2003. We record a liability for these lease guarantees in the period when it becomes probable that the obligor will fail to perform its obligation and if the amount of our guarantee obligation is estimable.

### Foreign Currency Translation

The functional currency of our international subsidiary is the local currency of the country in which the subsidiary is located. We have one foreign subsidiary domiciled in Canada. Foreign currency denominated assets and liabilities are translated into U.S. Dollars using the exchange rate in effect at the consolidated balance sheet date. Results of operations and cash flows are translated using the average exchange rates throughout the period. The effect of exchange rate fluctuations on translation of assets and liabilities is included as a component of shareholders' equity in accumulated other comprehensive income (loss). Gains and losses from foreign currency transactions, which are

included in other income (expense), were a loss of \$1.2 million for 2013, immaterial for 2012, and a loss of \$0.4 million for 2011.

#### Other Comprehensive Income

Our other comprehensive income includes the impact of the amortization of our pension actuarial loss, net of tax, the revaluation of our pension actuarial loss, net of tax, and the impact of foreign currency translation.

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## Supplemental Cash Flow Disclosures

The following table provides supplemental cash flow information for 2013, 2012, and 2011:

| (In thousands)  | 2013        | 2012        | 2011      |
|---|-------------|-------------|-----------|
| Supplemental disclosure of cash flow information:             |             |             |           |
| Cash paid for interest, including capital leases              | \$2,687     | \$3,369     | \$2,742   |
| Cash paid for income taxes, excluding impact of refunds       | \$122,672   | \$95,596    | \$114,406 |
| Gross proceeds from borrowings under the bank credit facility | \$1,330,100 | \$1,448,800 | \$846,300 |
| Gross payments of borrowings under the bank credit facility   | \$1,424,300 | \$1,343,500 | \$780,400 |
| Non-cash activity:  |             |             |           |
| Assets acquired under capital leases                          | \$—         | \$392       | \$2,925   |
| Accrued property and equipment                                | \$5,296     | \$6,824     | \$8,711   |
| Notes payable assumed in acquisition                          | \$—         | \$—         | \$16,664  |

## Reclassifications

## Wholesale Business

During the fourth quarter of 2013, we executed our wind down plan and ceased the operations of our wholesale business; therefore, we determined the results of our wholesale business should be reported as discontinued operations. As such, we have reclassified our results for all periods presented. Please see the Wholesale Business section of note 13 and note 14 to the consolidated financial statements for further discussion of the wind down and the costs incurred during 2013.

## Merchandise Categories

In the fourth quarter of 2013, we realigned select merchandise categories to be consistent with the realignment of our merchandising team and changes to our management reporting in our U.S. segment. We moved our toys, books, and sporting goods departments out of the Hardlines & Toys category and into our Seasonal category. We moved our table top, food preparation, stationary, gift wrap, and greeting card departments out of our Home category and into our Hard Home. Additionally, we moved our home décor and frames departments out of our Home category and into our Furniture category. We subsequently renamed the remaining classifications in our Home category as Soft Home. We also renamed our Furniture category to Furniture & Home Décor. Furthermore, we renamed our Electronics & Other category to Electronics & Accessories.

Also in the fourth quarter of 2013, we separated several of our existing merchandise departments into new departments to be consistent with the realignment of our merchandising team and changes to our management reporting. Prior to the fourth quarter of 2013, our Food category consisted of our food and specialty food departments. We separated our food department into two separate departments named candy & snacks and beverage & grocery. In our Home category, we separated our domestics department into six new departments named fashion bedding, utility bedding, bath, window, decorative textile, and flooring.

Our U.S. segment now uses the following merchandise categories, which match our internal management and reporting of merchandise net sales: Food, Consumables, Soft Home, Hard Home, Furniture & Home Décor, Seasonal, and Electronics & Accessories. The Food category includes our beverage & grocery, candy & snacks, and specialty foods departments. The Consumables category includes our health and beauty, plastics, paper, chemical, and pet departments. The Soft Home category includes the fashion bedding, utility bedding, bath, window, decorative textile, and flooring departments. The Hard Home category includes our small appliances, table top, food preparation, stationary, greeting card, tools, paint, and home maintenance departments. The Furniture & Home Décor category includes our upholstery, mattress, ready-to-assemble, case goods, home décor, and frames departments. The Seasonal category includes our lawn & garden, summer, Christmas, toys, books, sporting goods, and other holiday departments. The Electronics & Accessories category includes the electronics, jewelry, apparel, hosiery, and infant accessories

departments. In order to provide comparative information, we have reclassified our results into the new alignment for all periods presented.

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## Recent Accounting Standards

There are currently no new accounting pronouncements with a future effective date that are of significance, or potential significance, to us.

## Subsequent Events

We have evaluated events and transactions subsequent to the balance sheet date. Based on this evaluation, we are not aware of any events or transactions (other than those disclosed elsewhere) that occurred subsequent to the balance sheet date but prior to filing that would require recognition or disclosure in our consolidated financial statements.

## NOTE 2 – PROPERTY AND EQUIPMENT - NET

Property and equipment - net consist of:

| (In thousands)                                 | February 1, 2014 | February 2, 2013 |
|--|------------------|------------------|
| Land and land improvements                     | \$50,830         | \$50,797         |
| Buildings and leasehold improvements           | 835,117          | 803,267          |
| Fixtures and equipment                         | 692,152          | 674,684          |
| Computer software costs                        | 128,787          | 114,572          |
| Transportation equipment                       | 26,763           | 27,303           |
| Construction-in-progress                       | 6,791            | 23,759           |
| Property and equipment - cost                  | 1,740,440        | 1,694,382        |
| Less accumulated depreciation and amortization | 1,170,758        | 1,100,820        |
| Property and equipment - net                   | \$569,682        | \$593,562        |

Property and equipment - cost includes \$4.2 million and \$4.2 million at February 1, 2014 and February 2, 2013, respectively, to recognize assets from capital leases. Accumulated depreciation and amortization includes \$3.2 million and \$2.2 million at February 1, 2014 and February 2, 2013, respectively, related to capital leases.

During 2013, 2012, and 2011 respectively, we invested \$104.8 million, \$131.3 million, and \$131.3 million of cash in capital expenditures and we recorded \$115.1 million, \$106.1 million, and \$90.1 million of depreciation expense.

We incurred \$7.8 million, \$1.0 million, and \$2.2 million in asset impairment charges in 2013, 2012, and 2011, respectively. The charges in 2013 principally related to the write-down of long-lived assets in our Canadian segment as a result of our announced intention to wind down the operations of our Canadian segment. As there will be no expected future cash flows from our Canadian segment beyond the first quarter of 2014, we impaired our property and equipment to its estimated salvage value at February 1, 2014, which resulted in an impairment charge of \$6.5 million. Additionally, in 2013, we wrote down the value of long-lived assets at seven U.S. stores identified as part of our annual store impairment review. The charges in 2012 principally related to the write-down of long-lived assets at one U.S. store and four Canadian stores identified as part of our annual store impairment review. The charges in 2011 relate to asset impairments from the valuation of the Company's oldest airplane.

Asset impairment charges are included in selling and administrative expenses in our accompanying consolidated statements of operations. We perform annual impairment reviews of our long-lived assets at the store level. When we perform the annual impairment reviews, we first determine which stores had impairment indicators present. We generally use actual historical cash flows to determine if stores had negative cash flows within the past two years. For each store with negative cash flows, we obtain future cash flow estimates based on operating performance estimates specific to each store's operations that are based on assumptions currently being used to develop our company level operating plans. If the net book value of a store's long-lived assets is not recoverable by the expected future cash flows of the store, we estimate the fair value of the store's assets and recognize an impairment charge for the excess net book

value of the store's long-lived assets over their fair value.

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NOTE 3 – BANK CREDIT FACILITY

On July 22, 2011, we entered into a \$700 million five-year unsecured credit facility and, on May 30, 2013, we entered into an amendment of the credit facility that extended its expiration from July 22, 2016 to May 30, 2018 (“2011 Credit Agreement”). The 2011 Credit Agreement replaced the \$500 million three-year unsecured credit facility we entered into on April 28, 2009 (“2009 Credit Agreement”). We did not incur any material termination penalties in connection with the termination of the 2009 Credit Agreement. In connection with our entry into the 2011 Credit Agreement, we paid bank fees and other expenses in the aggregate amount of \$3.0 million, which are being amortized over the term of the agreement. In connection with the amendment of the 2011 Credit Agreement, we paid additional bank fees and other expenses in the aggregate amount of \$0.9 million, which are being amortized over the term of the amended agreement.

Borrowings under the 2011 Credit Agreement are available for general corporate purposes and working capital. The 2011 Credit Agreement includes a \$30 million swing loan sublimit and a \$150 million letter of credit sublimit. The interest rates, pricing and fees under the 2011 Credit Agreement fluctuate based on our debt rating. The 2011 Credit Agreement allows us to select our interest rate for each borrowing from multiple interest rate options. The interest rate options are generally derived from the prime rate or LIBOR. We may prepay revolving loans made under the 2011 Credit Agreement. The 2011 Credit Agreement contains financial and other covenants, including, but not limited to, limitations on indebtedness, liens and investments, as well as the maintenance of two financial ratios – a leverage ratio and a fixed charge coverage ratio. A violation of any of the covenants could result in a default under the 2011 Credit Agreement that would permit the lenders to restrict our ability to further access the 2011 Credit Agreement for loans and letters of credit and require the immediate repayment of any outstanding loans under the 2011 Credit Agreement. At February 1, 2014, we had \$77.0 million of borrowings outstanding under the 2011 Credit Agreement and \$5.6 million was committed to outstanding letters of credit, leaving \$617.4 million available under the 2011 Credit Agreement.

NOTE 4 – FAIR VALUE MEASUREMENTS

In connection with our nonqualified deferred compensation plan, we had mutual fund investments of \$21.2 million and \$20.7 million at February 1, 2014 and February 2, 2013, respectively, which were recorded in other assets. These investments were classified as trading securities and were recorded at their fair value. The fair values of mutual fund investments were Level 1 valuations under the fair value hierarchy because each fund’s quoted market value per share was available in an active market.

The fair values of our long-term obligations are estimated based on the quoted market prices for the same or similar issues and the current interest rates offered for similar instruments. These fair value measurements are classified as Level 2 within the fair value hierarchy. Given the variable rate features and relatively short maturity of the instruments underlying our long-term obligations, the carrying value of these instruments approximates the fair value.

NOTE 5 – LEASES

Leased property consisted primarily of 1,515 of our retail stores, 0.5 million square feet of warehouse space, and certain transportation, information technology and other office equipment. Many of the store leases obligate us to pay for our applicable portion of real estate taxes, CAM, and property insurance. Certain store leases provide for contingent rents, have rent escalations, and have tenant allowances or other lease incentives. Many of our leases contain provisions for options to renew or extend the original term for additional periods.

Total rent expense, including real estate taxes, CAM, and property insurance, charged to continuing operations for operating leases consisted of the following:



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| (In thousands)     | 2013      | 2012      | 2011      |
|--------------------|-----------|-----------|-----------|
| Minimum leases     | \$329,654 | \$309,526 | \$284,697 |
| Contingent leases  | 391       | 460       | 637       |
| Total rent expense | \$330,045 | \$309,986 | \$285,334 |

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Future minimum rental commitments for leases, excluding closed store leases, real estate taxes, CAM, and property insurance, at February 1, 2014, were as follows:

| Fiscal Year  | (In thousands) |
|--------------|----------------|
| 2014         | \$260,921      |
| 2015         | 213,657        |
| 2016         | 173,486        |
| 2017         | 127,602        |
| 2018         | 92,941         |
| Thereafter   | 134,505        |
| Total leases | \$1,003,112    |

We have obligations for capital leases for office equipment, included in accrued operating expenses and other liabilities on our consolidated balance sheet. Scheduled payments for all capital leases at February 1, 2014, were as follows:

| Fiscal Year                                | (In thousands) |
|--|----------------|
| 2014                                       | \$930          |
| 2015                                       | 86             |
| 2016                                       | 2              |
| 2017                                       | —              |
| 2018                                       | —              |
| Thereafter                                 | —              |
| Total lease payments                       | \$1,018        |
| Less amount to discount to present value   | (8 )           |
| Capital lease obligation per balance sheet | \$1,010        |

## NOTE 6 – SHAREHOLDERS’ EQUITY

## Earnings per Share

There were no adjustments required to be made to weighted-average common shares outstanding for purposes of computing basic and diluted earnings per share and there were no securities outstanding in any year presented, which were excluded from the computation of earnings per share other than antidilutive employee and director stock options and non-vested restricted stock awards. Stock options outstanding that were excluded from the diluted share calculation because their impact was antidilutive at the end of 2013, 2012, and 2011 were as follows:

| (In millions)   | 2013 | 2012 | 2011 |
|---|------|------|------|
| Antidilutive stock options excluded from dilutive share calculation | 2.8  | 1.9  | 1.5  |

Antidilutive options are excluded from the calculation because they decrease the number of diluted shares outstanding under the treasury stock method. Antidilutive options are generally outstanding options where the exercise price per share is greater than the weighted-average market price per share for our common shares for each period. The number of shares of non-vested restricted stock that were antidilutive, as determined under the treasury stock method, is immaterial for all years presented.

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A reconciliation of the number of weighted-average common shares outstanding used in the basic and diluted earnings per share computations is as follows:

| (In thousands)  | 2013   | 2012   | 2011   |
|---|--------|--------|--------|
| Weighted-average common shares outstanding:                   |        |        |        |
| Basic   | 57,415 | 59,852 | 68,316 |
| Dilutive effect of stock options and restricted common shares | 543    | 624    | 1,103  |
| Diluted   | 57,958 | 60,476 | 69,419 |

## NOTE 7 – SHARE-BASED PLANS

Our shareholders approved the Big Lots 2012 Long-Term Incentive Plan (“2012 LTIP”) in May 2012. The 2012 LTIP authorizes the issuance of incentive and nonqualified stock options, restricted stock, restricted stock units, deferred stock awards, performance share units, stock appreciation rights, cash-based awards, and other share-based awards. We have issued only nonqualified stock options, restricted stock, and performance units under the 2012 LTIP. The number of common shares available for issuance under the 2012 LTIP consists of an initial allocation of 7,750,000 common shares plus any common shares subject to the 4,702,362 outstanding awards as of March 15, 2012 under the Big Lots 2005 Long-Term Incentive Plan (“2005 LTIP”) that, on or after March 15, 2012, cease for any reason to be subject to such awards (other than by reason of exercise or settlement). The Compensation Committee of our Board of Directors (“Committee”), which is charged with administering the 2012 LTIP, has the authority to determine the terms of each award. Nonqualified stock options granted to employees under the 2012 LTIP, the exercise price of which may not be less than the fair market value of the underlying common shares on the grant date, generally expire on the earlier of: (1) the seven year term set by the Committee; or (2) one year following termination of employment, death, or disability. The nonqualified stock options generally vest ratably over a four-year period; however, upon a change in control, all awards outstanding automatically vest.

Our former equity compensation plan, the 2005 LTIP, approved by our shareholders in May 2005, expired on May 16, 2012. The 2005 LTIP authorized the issuance of nonqualified stock options, restricted stock, and other award types. We issued only nonqualified stock options and restricted stock under the 2005 LTIP. The number of common shares available for issuance under the 2005 LTIP consisted of: (1) an initial allocation of 1,250,000 common shares; (2) 2,001,142 common shares, the number of common shares that were available under the predecessor Big Lots, Inc. 1996 Performance Incentive Plan (“1996 LTIP”) upon its expiration; (3) 2,100,000 common shares approved by our shareholders in May 2008; and (4) an annual increase equal to 0.75% of the total number of issued common shares (including treasury shares) as of the start of each of our fiscal years during which the 2005 LTIP was in effect. The Committee, which was charged with administering the 2005 LTIP, had the authority to determine the terms of each award. Nonqualified stock options granted to employees under the 2005 LTIP, the exercise price of which was not less than the fair market value of the underlying common shares on the grant date, generally expire on the earlier of: (1) the seven year term set by the Committee; or (2) one year following termination of employment, death, or disability. The nonqualified stock options generally vest ratably over a four-year period; however, upon a change in control, all awards outstanding automatically vest.

We previously maintained the Big Lots Director Stock Option Plan (“Director Stock Option Plan”) for non-employee directors. The Director Stock Option Plan was terminated on May 30, 2008. The Director Stock Option Plan was administered by the Committee pursuant to an established formula. Neither the Board of Directors nor the Committee exercised any discretion in administration of the Director Stock Option Plan. Grants were made annually at an exercise price equal to the fair market value of the underlying common shares on the date of grant. The annual grants to each non-employee director of an option to acquire 10,000 of our common shares became fully exercisable over a three year period: 20% of the shares on the first anniversary, 60% on the second anniversary, and 100% on the third anniversary. Stock options granted to non-employee directors expire on the earlier of: (1) 10 years plus one month; (2) one year following death or disability; or (3) at the end of our next trading window one year following termination. In

connection with the amendment to the 2005 LTIP in May 2008, our Board of Directors amended the Director Stock Option Plan so that no additional awards may be made under that plan. Our non-employee directors did not receive any stock options in 2013, 2012, and 2011, but did, as discussed below, receive restricted stock awards under the 2012 and 2005 LTIPs.

Share-based compensation expense was \$13.2 million, \$17.9 million and \$25.0 million in 2013, 2012, and 2011, respectively. We use a binomial model to estimate the fair value of stock options on the grant date. The binomial model takes into account variables such as volatility, dividend yield rate, risk-free rate, contractual term of the option, the probability that the option will be exercised prior to the end of its contractual life, and the probability of retirement of the option holder in computing the value of the option. Expected volatility is based on historical and current implied volatilities from traded options on our common shares. The dividend yield on our common shares is assumed to be zero since we have not paid dividends and have no current plans to do so in the future. The risk-free rate is based on U.S. Treasury security yields at the time of the grant. The expected life is determined from the binomial model, which incorporates exercise and post-vesting forfeiture assumptions based on analysis of historical data.

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The weighted-average fair value of stock options granted and assumptions used in the stock option pricing model for each of the respective periods were as follows:

|  |         |         |         |   |
|--|---------|---------|---------|---|
|  | 2013    | 2012    | 2011    |   |
| Weighted-average fair value of stock options granted | \$12.08 | \$14.15 | \$14.43 |   |
| Risk-free interest rates                             | 0.8     | %0.6    | %1.8    | % |
| Expected life (years)                                | 4.2     | 4.2     | 4.2     |   |
| Expected volatility                                  | 41.9    | %41.1   | %41.7   | % |
| Expected annual forfeiture rate                      | 3.0     | %3.0    | %1.5    | % |

The following table summarizes information about our stock options outstanding and exercisable at February 1, 2014:

| Range of Prices |                       | Options Outstanding |   | Options Exercisable             |                     |                                 |
|-----------------|-----------------------|---------------------|---|---------------------------------|---------------------|---------------------------------|
| Greater Than    | Less Than or Equal to | Options Outstanding | Weighted-Average Remaining Life (Years) | Weighted-Average Exercise Price | Options Exercisable | Weighted-Average Exercise Price |
| \$10.01         | \$20.00               | 483,603             | 2.0                                     | \$ 17.18                        | 483,603             | \$ 17.18                        |
| 20.01           | 30.00                 | 163,763             | 1.3                                     | 23.63                           | 162,825             | 23.60                           |
| 30.01           | 40.00                 | 1,571,187           | 5.1                                     | 35.82                           | 440,437             | 35.84                           |
| \$40.01         | \$50.00               | 1,158,750           | 4.6                                     | 42.59                           | 493,250             | 42.22                           |
|                 |                       | 3,377,303           | 4.3                                     | \$ 34.88                        | 1,580,115           | \$ 30.86                        |

A summary of the annual stock option activity for fiscal years 2011, 2012, and 2013 is as follows:

|  | Number of Options | Weighted Average Exercise Price Per Share | Weighted Average Remaining Contractual Term (years) | Aggregate Intrinsic Value (000's) |
|--|-------------------|---|---|-----------------------------------|
| Outstanding stock options at January 29, 2011  | 3,578,683         | \$24.59                                   |   |                                   |
| Granted  | 918,500           | 40.85                                     |   |                                   |
| Exercised                                      | (500,085)         | )20.81                                    |   |                                   |
| Forfeited                                      | (320,675)         | )33.84                                    |   |                                   |
| Outstanding stock options at January 28, 2012  | 3,676,423         | \$28.36                                   |   |                                   |
| Granted  | 982,000           | 43.23                                     |   |                                   |
| Exercised                                      | (1,406,262)       | )23.67                                    |   |                                   |
| Forfeited                                      | (223,075)         | )40.18                                    |   |                                   |
| Outstanding stock options at February 2, 2013  | 3,029,086         | \$34.49                                   |   |                                   |
| Granted  | 1,159,500         | 35.80                                     |   |                                   |
| Exercised                                      | (213,520)         | )22.87                                    |   |                                   |
| Forfeited                                      | (597,763)         | )38.97                                    |   |                                   |
| Outstanding stock options at February 1, 2014  | 3,377,303         | \$34.88                                   | 4.3   | \$5,264                           |
| Vested or expected to vest at February 1, 2014 | 3,227,442         | \$34.71                                   | 4.3   | \$5,264                           |
| Exercisable at February 1, 2014                | 1,580,115         | \$30.86                                   | 3.0   | \$5,264                           |

The number of stock options expected to vest was based on our annual forfeiture rate assumption.



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A summary of the nonvested awards other than stock options activity for fiscal years 2011, 2012, and 2013 is as follows:

|  | Number of<br>Shares | Weighted<br>Average<br>Grant-Date Fair<br>Value Per Share |
|--|---------------------|---|
| Outstanding non-vested awards other than stock options at January 29, 2011 | 503,784             | \$35.88   |
| Granted  | 564,589             | 40.76   |
| Vested   | (271,784            | ) 35.84   |
| Forfeited  | (55,300             | ) 38.72   |
| Outstanding non-vested awards other than stock options at January 28, 2012 | 741,289             | \$39.40   |
| Granted  | 589,784             | 42.90   |
| Vested   | (477,664            | ) 38.52   |
| Forfeited  | (69,800             | ) 43.04   |
| Outstanding non-vested awards other than stock options at February 2, 2013 | 783,609             | \$42.25   |
| Granted  | 496,376             | 35.47   |
| Vested   | (64,784             | ) 37.79   |
| Forfeited  | (513,300            | ) 41.86   |
| Outstanding non-vested awards other than stock options at February 1, 2014 | 701,901             | \$38.15   |

The non-vested restricted stock awards granted to employees (other than the awards granted to Mr. Fishman, our former CEO in 2011 and 2012) vest if certain financial performance objectives are achieved. If we meet a threshold financial performance objective and the grantee remains employed by us, the restricted stock will vest on the opening of our first trading window five years after the grant date of the award. If we meet a higher financial performance objective and the grantee remains employed by us, the restricted stock will vest on the first trading day after we file our Annual Report on Form 10-K with the SEC for the fiscal year in which the higher objective is met.

On the grant date of the 2011 restricted stock awards (other than the award granted to Mr. Fishman), we estimated a three-year period for vesting based on the assumed achievement of the higher financial performance objective. In the fourth quarter of 2012, based on operating results and future projections, we changed the estimated vesting period of the 2011 restricted stock awards to four years. In the fourth quarter of 2013, based on operating results and future projections, we changed the estimated vesting period of the 2011 restricted stock awards to five years. The impact of this change in estimate will be recognized ratably over the remaining vesting period.

On the grant date of the 2012 restricted stock awards (other than the award granted to Mr. Fishman), we estimated a three-year period for vesting based on the assumed achievement of the higher financial performance objective. In the fourth quarter of 2012, based on operating results and future projections, we changed the estimated vesting period of the 2012 restricted stock awards to four years. In the fourth quarter of 2013, based on operating results and future projections, we changed the estimated vesting period of the 2012 restricted stock awards to five years. The impact of this change in estimate will be recognized ratably over the remaining vesting period.

On the grant date of the 2013 restricted stock awards, we estimated a three-year period for vesting based on the assumed achievement of the higher financial performance objective. In the fourth quarter of 2013, based on operating results and future projections, we changed the estimated vesting period of the 2013 restricted stock awards to five years. The impact of this change in estimate will be recognized ratably over the remaining vesting period.

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In the second quarter of 2013, in connection with his appointment as CEO and President, Mr. Campisi was awarded 37,800 performance share units, which vest based on the achievement of share price performance goals. The performance share units have a contractual term of seven years. If the performance goals applicable to the performance share units are not achieved prior to expiration, the awards will be forfeited.

The restricted stock award granted to Mr. Fishman in 2011 vested in 2012 based on achievement of the corporate financial goals for 2011. The nonvested restricted stock award granted to Mr. Fishman in 2012 was forfeited in the first quarter of 2013, because we failed to achieve a corporate financial goal set for 2012.

In 2013, 2012, and 2011, we granted to each non-employee member of our Board of Directors a restricted stock award. In 2013, each had a fair value on the grant date of approximately \$100,000. These awards vest on the earlier of (1) the trading day immediately preceding the next annual meeting of our shareholders or (2) the death or disability of the grantee. However, the restricted stock award will not vest if the non-employee director ceases to serve on our Board of Directors before either vesting event occurs.

During 2013, 2012, and 2011, the following activity occurred under our share-based compensation plans:

| (In thousands)                                   | 2013    | 2012     | 2011     |
|--|---------|----------|----------|
| Total intrinsic value of stock options exercised | \$2,646 | \$29,350 | \$8,747  |
| Total fair value of restricted stock vested      | \$2,237 | \$21,907 | \$11,618 |

The total unearned compensation cost related to all share-based awards outstanding at February 1, 2014 was approximately \$27.6 million. This compensation cost is expected to be recognized through January 2019 based on existing vesting terms with the weighted-average remaining expense recognition period being approximately 2.5 years from February 1, 2014.

## NOTE 8 – EMPLOYEE BENEFIT PLANS

## Pension Benefits

We maintain the Pension Plan and Supplemental Pension Plan covering certain employees whose hire date was on or before April 1, 1994. Benefits under each plan are based on credited years of service and the employee's compensation during the last five years of employment. The Supplemental Pension Plan is maintained for certain highly compensated executives whose benefits were frozen in the Pension Plan in 1996. The Supplemental Pension Plan is designed to pay benefits in the same amount as if the participants continued to accrue benefits under the Pension Plan. We have no obligation to fund the Supplemental Pension Plan, and all assets and amounts payable under the Supplemental Pension Plan are subject to the claims of our general creditors.

The components of net periodic pension expense were comprised of the following:

| (In thousands)                                | 2013    | 2012    | 2011    |
|---|---------|---------|---------|
| Service cost - benefits earned in the period  | \$2,086 | \$2,171 | \$2,211 |
| Interest cost on projected benefit obligation | 3,041   | 3,292   | 3,496   |
| Expected investment return on plan assets     | (2,893) | (3,089) | (4,627) |
| Amortization of prior service cost            | (34)    | (34)    | (34)    |
| Amortization of transition obligation         | 12      | 13      | 13      |
| Amortization of actuarial loss                | 1,692   | 2,345   | 1,796   |
| Settlement loss                               | 83      | 298     | 298     |
| Net periodic pension cost                     | \$3,987 | \$4,996 | \$3,153 |



In 2013, 2012, and 2011, we incurred pretax non-cash settlement charges of \$0.1 million, \$0.3 million and \$0.3 million, respectively. The settlement charges were caused by lump sum benefit payments made to plan participants in excess of combined annual service cost and interest cost for each year.

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The weighted-average assumptions used to determine net periodic pension expense were:

|   | 2013 | 2012  | 2011  |   |
|---|------|-------|-------|---|
| Discount rate                           | 4.6  | % 5.0 | % 5.7 | % |
| Rate of increase in compensation levels | 3.5  | % 3.5 | % 3.9 | % |
| Expected long-term rate of return       | 5.1  | % 5.5 | % 8.0 | % |

The weighted-average assumptions used to determine benefit obligations were:

|   | 2013 | 2012  |   |
|---|------|-------|---|
| Discount rate                           | 5.0  | % 4.6 | % |
| Rate of increase in compensation levels | 3.0  | % 3.5 | % |

The following schedule provides a reconciliation of projected benefit obligations, plan assets, funded status, and amounts recognized for the Pension Plan and Supplemental Pension Plan at February 1, 2014 and February 2, 2013:

| (In thousands)  | February 1, 2014 | February 2, 2013 |   |
|---|------------------|------------------|---|
| Change in projected benefit obligation:                           |                  |                  |   |
| Projected benefit obligation at beginning of year                 | \$70,210         | \$69,942         |   |
| Service cost  | 2,086            | 2,171            |   |
| Interest cost   | 3,041            | 3,292            |   |
| Benefits and settlements paid                                     | (5,035)          | (6,437)          | ) |
| Actuarial (gain) loss   | (5,424)          | 1,242            | ) |
| Projected benefit obligation at end of year                       | \$64,878         | \$70,210         |   |
| Change in plan assets:  |                  |                  |   |
| Fair market value at beginning of year                            | \$59,376         | \$58,662         |   |
| Actual return on plan assets                                      | 1,379            | 5,969            |   |
| Employer contributions  | 609              | 1,182            |   |
| Benefits and settlements paid                                     | (5,035)          | (6,437)          | ) |
| Fair market value at end of year                                  | \$56,329         | \$59,376         |   |
| Under funded and net amount recognized                            | \$(8,549)        | \$(10,834)       | ) |
| Amounts recognized in the consolidated balance sheets consist of: |                  |                  |   |
| Noncurrent assets   | \$—              | \$—              |   |
| Current liabilities   | (340)            | (361)            | ) |
| Noncurrent liabilities  | (8,209)          | (10,473)         | ) |
| Net amount recognized   | \$(8,549)        | \$(10,834)       | ) |

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The following are components of accumulated other comprehensive income and, as such, are not yet reflected in net periodic pension expense:

| (In thousands)                               | 2013      | 2012     |   |
|--|-----------|----------|---|
| Unrecognized transition obligation           | \$—       | \$(12    | ) |
| Unrecognized past service credit             | 56        | 90       |   |
| Unrecognized actuarial loss                  | (14,124   | )(19,808 | ) |
| Accumulated other comprehensive loss, pretax | \$(14,068 | )(19,730 | ) |

We expect to reclassify \$1.2 million of the actuarial loss along with immaterial amounts of transition obligation and past service credit into net periodic pension expense during 2014.

The following table sets forth certain information for the Pension Plan and the Supplemental Pension Plan at February 1, 2014 and February 2, 2013:

| (In thousands)                   | Pension Plan     |                  | Supplemental Pension Plan |                  |
|----------------------------------|------------------|------------------|---------------------------|------------------|
|                                  | February 1, 2014 | February 2, 2013 | February 1, 2014          | February 2, 2013 |
| Projected benefit obligation     | \$59,724         | \$63,951         | \$5,154                   | \$6,259          |
| Accumulated benefit obligation   | 54,635           | 57,224           | 4,643                     | 5,080            |
| Fair market value of plan assets | \$56,329         | \$59,376         | \$—                       | \$—              |

We elected not to make a discretionary contribution to the Pension Plan in 2013 or in 2012. Our funding policy of the Pension Plan is to make annual contributions based on advice from our actuaries and the evaluation of our cash position, but not less than the minimum required by applicable regulations. Currently, we expect no required contributions to the Pension Plan during 2014, however, discretionary contributions could be made depending upon further analysis.

Using the same assumptions as those used to measure our benefit obligations, the Pension Plan and the Supplemental Pension Plan benefits expected to be paid in each of the following fiscal years are as follows:

| Fiscal Year | (In thousands) |
|-------------|----------------|
| 2014        | \$ 5,242       |
| 2015        | 5,435          |
| 2016        | 5,438          |
| 2017        | 5,334          |
| 2018        | 5,283          |
| 2019 - 2023 | \$ 25,409      |

Our overall investment strategy is to earn a long-term rate of return sufficient to meet the liability needs of the Pension Plan, within prudent risk constraints. In order to develop the appropriate asset allocation and investment strategy, an actuarial review of the Pension Plan's expected future distributions was completed. The strategy provides a well-defined risk management approach designed to reduce risks based on the Pension Plan's funded status.

Assets can generally be considered as filling one of the following roles within the strategy: (1) liability-hedging assets, which are designed to meet the cash payment needs of the plan's obligation and provide downside protection, primarily invested in intermediate and long maturity investment grade bonds; or (2) return-seeking assets, which are designed to deliver returns in excess of the Pension Plan's obligation growth rates, with broadly diversified assets including U.S. and non-U.S. equities, real estate, and high yield bonds. The current target allocation is approximately 80% liability-hedging assets and 20% return-seeking assets. Target allocations may change over time due to changes in the plan's funded status, or in response to changes in plan or market conditions. All assets must have readily

ascertainable market values and be easily marketable. The portfolio of assets maintains a high degree of liquidity in order to meet benefit payment requirements and to allow responsiveness to evolving Pension Plan and market conditions.

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The investment managers have the discretion to invest within sub-classes of assets within the parameters of their investment guidelines. Fixed income managers can adjust duration exposure as deemed appropriate given current or expected market conditions. Additionally, the investment managers have the authority to invest in financial futures contracts and financial options contracts for the purposes of implementing hedging strategies. There were no futures contracts owned directly by the Pension Plan at February 1, 2014 and February 2, 2013. The primary benchmark for assessing the effectiveness of the Pension Plan investments is that of the plan's liabilities themselves. Asset class returns are also judged relative to common benchmark indices such as the Russell 3000 and Barclay's Capital Long Credit Bond. Investment results and plan funded status are monitored daily, with a detailed performance review completed on a quarterly basis.

The fair value of our Pension Plan assets at February 1, 2014 and February 2, 2013 by asset category was comprised of the following:

| (In thousands)             | February 1, 2014 |         |         |         | February 2, 2013 |         |         |         |
|----------------------------|------------------|---------|---------|---------|------------------|---------|---------|---------|
|                            | Total            | Level 1 | Level 2 | Level 3 | Total            | Level 1 | Level 2 | Level 3 |
| Cash and Cash Equivalents  | \$1,418          | \$1,418 | \$—     | \$—     | \$821            | \$821   | \$—     | \$—     |
| Common / Collective Trusts |                  |         |         |         |                  |         |         |         |
| Long Credit                | 44,239           | —       | 44,239  | —       | 30,924           | —       | 30,924  | —       |
| High Yield                 | 2,629            | —       | 2,629   | —       | 3,074            | —       | 3,074   | —       |
| Global Real Estate         | 2,623            | —       | 2,623   | —       | 3,244            | —       | 3,244   | —       |
| International Equities     | 2,172            | —       | 2,172   | —       | 2,643            | —       | 2,643   | —       |
| U.S. Equity Index          | 2,165            | —       | 2,165   | —       | 2,538            | —       | 2,538   | —       |
| U.S. Small Cap             | 1,075            | —       | 1,075   | —       | 1,254            | —       | 1,254   | —       |
| Intermediate Credit        | 8                | —       | 8       | —       |                  |         |         |         |