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Washington, D.C. 20549

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**ANNUAL AUDITED REPORT  
FORM X-17A-5  
PART III**

SEC FILE NUMBER  
8- 44071

FACING PAGE

**Information Required of Brokers and Dealers Pursuant to Section 17 of the  
Securities Exchange Act of 1934 and Rule 17a-5 Thereunder**

REPORT FOR THE PERIOD BEGINNING 01/01/2004 AND ENDING 12/31/2004  
MM/DD/YY MM/DD/YY

**A. REGISTRANT IDENTIFICATION**

NAME OF BROKER-DEALER: Schnitzius & Vaughan

OFFICIAL USE ONLY  
FIRM I.D. NO.

ADDRESS OF PRINCIPAL PLACE OF BUSINESS: (Do not use P.O. Box No.)

700 Louisiana Street, Suite 2450

(No. and Street)

Houston,  
(City)

Texas  
(State)

77002  
(Zip Code)

NAME AND TELEPHONE NUMBER OF PERSON TO CONTACT IN REGARD TO THIS REPORT

Thomas H. Schnitzius

713-222-2170

(Area Code - Telephone Number)

**B. ACCOUNTANT IDENTIFICATION**

INDEPENDENT PUBLIC ACCOUNTANT whose opinion is contained in this Report\*

Wooten, Harris W.

(Name - if individual, state last, first, middle name)

9219 Katy Freeway, Suite 134  
(Address) (City)

Houston, Texas  
(State)

77024  
(Zip Code)

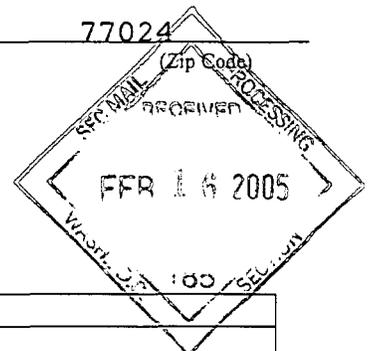
CHECK ONE:

- Certified Public Accountant
- Public Accountant
- Accountant not resident in United States or any of its possessions

PROCESSED

FEB 28 2005

THOMSON  
FINANCIAL



**FOR OFFICIAL USE ONLY**

\*Claims for exemption from the requirement that the annual report be covered by the opinion of an independent public accountant must be supported by a statement of facts and circumstances relied on as the basis for the exemption. See Section 240.17a-5(e)(2)

SEC 1410 (06-02)

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OATH OR AFFIRMATION

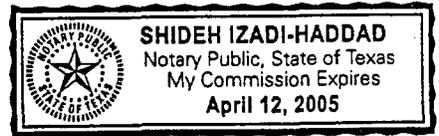
I, Thomas H. Schnitzius, swear (or affirm) that, to the best of my knowledge and belief the accompanying financial statement and supporting schedules pertaining to the firm of Schnitzius & Vaughan, as of December 31, 2004, are true and correct. I further swear (or affirm) that neither the company nor any partner, proprietor, principal officer or director has any proprietary interest in any account classified solely as that of a customer, except as follows:

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

*[Handwritten Signature]*  
\_\_\_\_\_  
Signature

PRINCIPAL  
\_\_\_\_\_  
Title

*[Handwritten Signature]*  
\_\_\_\_\_  
Notary Public



This report \*\* contains (check all applicable boxes):

- (a) Facing Page.
- (b) Statement of Financial Condition.
- (c) Statement of Income (Loss).
- (d) Statement of Changes in Financial Condition.
- (e) Statement of Changes in Stockholders' Equity or Partners' or Sole Proprietors' Capital.
- (f) Statement of Changes in Liabilities Subordinated to Claims of Creditors.
- (g) Computation of Net Capital.
- (h) Computation for Determination of Reserve Requirements Pursuant to Rule 15c3-3.
- (i) Information Relating to the Possession or Control Requirements Under Rule 15c3-3.
- (j) A Reconciliation, including appropriate explanation of the Computation of Net Capital Under Rule 15c3-3 and the Computation for Determination of the Reserve Requirements Under Exhibit A of Rule 15c3-3.
- (k) A Reconciliation between the audited and unaudited Statements of Financial Condition with respect to methods of consolidation.
- (l) An Oath or Affirmation.
- (m) A copy of the SIPC Supplemental Report.
- (n) A report describing any material inadequacies found to exist or found to have existed since the date of the previous audit.

\*\*For conditions of confidential treatment of certain portions of this filing, see section 240.17a-5(e)(3).

Schnitzius & Vaughan

Financial Statements and Schedules

December 31, 2004 and 2003

(With Independent Auditor's Report Thereon)

**Independent Auditor's Report**

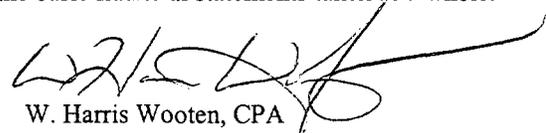
The Partners of  
Schnitzius & Vaughan

I have audited the accompanying statements of financial condition of Schnitzius & Vaughan (a Texas General Partnership) as of December 31, 2004 and 2003 and the related statements of income, changes in partners' capital and cash flows for years ended December 31, 2004 and 2003 that you are filing pursuant to Rule 17a-5 under the Securities and Exchange Act of 1934. These financial statements are the responsibility of the company's management. My responsibility is to express an opinion on these financial statements based on my audits.

I conducted my audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that I plan and perform the audits to obtain reasonable assurance 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. I believe that my audits provide a reasonable basis for my opinion.

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Schnitzius & Vaughan as of December 31, 2004 and 2003 and the results of its operations and its cash flows for the years ended December 31, 2004 and 2003 in conformity with accounting principles generally accepted in the United States of America.

My audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The information contained in Schedules I through III is presented for purposes of additional analysis and is not required for a fair presentation of the basic financial statements, but is supplementary information required by Rule 17a-5 under the Securities and Exchange Act of 1934. Such information has been subjected to the auditing procedures applied in my audits of the basic financial statements and, in my opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



W. Harris Wooten, CPA

February 7, 2005

Houston, Texas

**SCHNITZIUS & VAUGHAN**  
**Statements of Financial Condition**

<b>Assets</b>	<b>December 31,</b>	
	<b>2004</b>	<b>2003</b>
Cash, including interest-bearing deposits	\$ 114,714	\$ 91,549
Receivables from clients	23,978	29,892
Investments (Note 2)	1,650	3,300
Office equipment, at cost, less accumulated depreciation of \$148,301 and \$143,276 in 2004 and 2003, respectively	28,284	22,324
Other assets	400	400
	<b>\$ 169,026</b>	<b>\$ 147,465</b>
<b>Liabilities and Partners' Capital</b>		
Accounts payable and accrued expenses	\$ 4,741	\$ 2,323
	4,741	2,323
Partners' capital (notes 3, 4 and 5):		
Bracey, Inc.	(36,193)	(45,764)
LWC Investments, Inc.	200,478	190,906
	164,285	145,142
	<b>\$ 169,026</b>	<b>\$ 147,465</b>

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

**SCHNITZIUS & VAUGHAN**  
**Statements of Income**  
**For the years ended December 31, 2004**  
**and 2003**

	December 31,	
	2004	2003
Revenues:		
Fee income	\$ 641,649	\$ 536,628
Interest income	961	362
	642,610	536,990
Expenses:		
Broker dealer expenses	7,449	5,820
Employee compensation	182,841	135,000
Partner and employee benefits	15,518	17,417
Office rent	70,205	70,148
Office expense	95,045	108,556
Depreciation	5,025	3,689
Payroll and property taxes	14,397	10,616
Bad debt	1,337	3,434
Investment loss	1,650	-
	393,467	354,680
Net Income (Loss)	\$ 249,143	\$ 182,310

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

**SCHNITZIUS & VAUGHAN**  
**Statement of Changes in Partners' Capital**  
**For the years ended December 31, 2004**  
**and 2003**

	<u>Bracey, Inc.</u>	<u>LWC Investments Inc.</u>	<u>Total Partners' Capital</u>
Balance at December 31, 2002	\$ (109,419)	\$ 162,251	\$ 52,832
Net income (loss) for the year ended December 31, 2003	91,155	91,155	182,310
Contribution from partners	35,000	-	35,000
Distribution to partners	<u>(62,500)</u>	<u>(62,500)</u>	<u>(125,000)</u>
Balance at December 31, 2003	<u>\$ (45,764)</u>	<u>190,906</u>	<u>\$ 145,142</u>
Net income for the year ended December 31, 2004	124,571	124,572	249,143
Contribution from partners	-	-	-
Distribution to partners	<u>(115,000)</u>	<u>(115,000)</u>	<u>(230,000)</u>
Balance at December 2004	<u>\$ (36,193)</u>	<u>\$ 200,478</u>	<u>\$ 164,285</u>

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

**SCHNITZIUS & VAUGHAN**  
**Statements of Cash Flows**  
**For the years ended December 31, 2004**  
**and 2003**

	2004	2003
Cash flows from operating activities:		
Net earnings	\$ 249,143	\$ 182,310
Adjustments to reconcile net earnings to net cash used in operating activities:		
Depreciation	5,025	3,689
Investment loss	1,650	-
Changes in assets and liabilities:		
(Increase) decrease in receivables from clients and others	5,914	(12,367)
Increase (decrease) in accounts payable and accrued expenses	2,421	(69)
Total adjustments	15,010	(8,747)
Net cash provided (used) by operating activities	264,153	173,563
Cash flows used in investing activities:		
Purchase of office equipment	(10,988)	-
Partner contribution	-	35,000
Partners' distribution	(230,000)	(125,000)
Net increase (decrease) in cash	23,165	83,563
Cash at beginning of period	91,549	7,986
Cash at end of period	\$ 114,714	\$ 91,549
Supplemental disclosure of cash flow information -		
Cash paid during the year for interest	0	0
Cash includes cash and cash equivalents.		

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

## SCHNITZIUS & VAUGHAN

### Notes to Financial Statements

December 31, 2004 and 2003

#### (1) Summary of Significant Accounting Policies

Schnitzius & Vaughan ("S&V"), a Texas general partnership, was formed October 1, 1987, and is a member of the National Association of Securities Dealers, Inc. S&V acts primarily as a financial consultant working with clients to obtain financing or as an intermediary in merger or acquisition transactions.

Depreciation of office equipment is provided using accelerated depreciation methods based on estimated useful lives of five to seven years.

Prior to 2002, intangible assets are amortized on a straight-line basis over 40 years. In 2002, the Company adopted FASB #142 ("Goodwill and other Intangible Assets") and as a result an impairment loss of \$131,395 was recognized as a change in accounting principle in the accompanying financial statements.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures.

S&V is recognized as a partnership under the Internal Revenue Code and therefore does not provide for federal income taxes.

#### (2) Investments

Investments represents 300 warrants recorded at their fair value, which are exercisable at various times at \$13 to \$16 per share and expire on June 26, 2006, exercisable in four tranches for 300 shares in another company. As of December 31, 2004, two of the tranches have expired and investment loss of \$1,650 was recognized.

#### (3) Liabilities Subordinated to Claims of Creditors

As of December 31, 2004 and 2003, and for the years ended December 31, 2004 and 2003, S&V had no liabilities subordinated to the claims of general creditors.

#### (4) Minimum Capital Requirements

S&V is subject to the Securities and Exchange Commission's Uniform Net Capital Rule (Rule 15c3-1), which requires the maintenance of minimum net capital and requires that the ratio of aggregate indebtedness to net capital, both as defined, shall not exceed 15 to 1. Partners' capital may be restricted as to payment of distributions if this ratio exceeds 10 to 1. At December 31, 2004 and 2003, S&V had net capital of \$109,973 and \$89,226, respectively, which exceeded its required net capital of \$5,000 by \$104,973 and \$84,226, respectively. S&V's ratio of aggregate indebtedness as to net capital was .0431 to 1 and .0268 to 1 at December 31, 2004 and 2003, respectively.

#### (5) Partnership Agreement

The partners of S&V have executed a partnership agreement, which grants preemptive rights to S&V and the existing partner in the event of the death, the removal of a partner, or the voluntary or involuntary dissolution of the partnership.

**SCHNITZIUS & VAUGHAN**

**Notes to Financial Statements**

**December 31, 2004 and 2003**

**(6) Commitments**

S&V leases office facilities under a noncancellable operating lease expiring July 31, 2010. At December 31, 2004, future minimum rental commitments on such lease is as follows:

<u>Year Ending December 31</u>	<u>Amount</u>
2005	65,222
2006	56,163
2007	57,539
2008	58,915
2009 and thereafter	95,929

Rental expense relating to office facilities and office equipment was approximately \$70,205 and \$70,148 for the year ended December 31, 2004 and 2003, respectively. One of the partners of S&V is the signatory of the lease.

**(7) Concentration of Credit Risk**

The Company maintains its cash balances in one financial institution located in Houston, Texas. The balances are insured by the Federal Deposit Insurance Corporation up to \$100,000. The maximum loss that would have resulted from that risk totaled \$10,224.

Approximately 50% and 46% of the Company's revenues for 2004 and 2003 was earned from two separate clients.

**(8) Fair Values of Financial Instruments**

The following methods and assumptions were used to estimate the fair value of financial instruments:

Cash and cash equivalents – The carrying amount reported in the Statement of Financial Condition for cash and cash equivalents approximate its fair value.

Account receivable and accounts payable – The carrying amount reported in the Statement of Financial Condition for accounts receivable and accounts payable approximate its fair value.

Investments – The carrying amount reported in the Statement of Financial Condition for investments approximate its fair value.

**SCHNITZIUS & VAUGHAN**  
**Computation of Net Capital Under Rule 15c3-1**

As of December 31, 2004 and 2003

	December 31,	
	2004	2003
Net Capital:		
Partners' capital	\$ 164,285	\$ 145,142
Less non-allowable assets:		
Receivables	23,978	29,892
Investments	1,650	3,300
Office equipment, net	28,284	22,324
Other assets	400	400
Net Capital	109,973	89,226
Net capital requirement	5,000	5,000
Net capital in excess of required amount	104,973	84,226
Net Capital	\$ 109,973	\$ 89,226
Aggregate indebtedness	4,741	2,323
Ratio of aggregate indebtedness to net capital	4.31%	2.60%

Note - This computation differs from the computation of net capital under Rule 15c3-1 as of December 31, 2004, filed by Schnitzius & Vaughan with the National Association of Securities Dealers on Part II of Form X-17A-5, as follows:

	Net Capital	Aggregate Indebtedness
As reported on Part II of Form X-17A-5	\$ 111,185	\$ 3,529
Audit adjustment	(1,212)	1,212
As presented above	\$ 109,973	\$ 4,741

**SCHNITZIUS & VAUGHAN**

**Computation for Determination of Reserve  
Requirements Under Rule 15c3-3**

**December 31, 2004**

Schnitzius & Vaughan is exempt from the reserve requirements and the related computations for the determination thereof under paragraph (k) (2) (i) of Rule 15c3-3 under the Securities Exchange Act of 1934 as S&V carries no margin accounts in connection with its activities as a broker or dealer, does not otherwise hold funds or securities for, or owe money or securities to customers and effectuates all financial transactions with customers through unaffiliated clearing organizations.

During the years ended December 31, 2004 and 2003, S&V has maintained its compliance with the conditions for exemption specified in paragraph (k) (2) (i) of Rule 15c3-3.

SCHNITZIUS & VAUGHAN

Information for Possession or Control  
Requirements under Rule 15c3-3

December 31, 2004

	<u>Market Value</u>	<u>Number of Items</u>
Customers' fully paid securities and excess margin securities not in S&V's possession or control as of December 31, 2004 for which instructions to reduce to possession or control had been issued as of December 31, 2004, but for which the required action was not taken within the time frames specified under Rule 15c3-3.	<u>None</u>	<u>None</u>
Customers' fully paid securities and excess margin securities for which instruction to reduce to possession or control had not been issued as of December 31, 2004, excluding items arising from "temporary lags which result from normal business operations" as permitted under Rule 15c3-3.	<u>None</u>	<u>None</u>

**Independent Auditor's Report on**  
**Internal Accounting Control**  
**Required by SEC Rule 17a-5**

The Partners of  
Schnitzius & Vaughan

In planning and performing my audits of the financial statements of Schnitzius & Vaughan ("S&V") (a Texas General Partnership) for the years ended December 31, 2004 and 2003 respectively, I considered its internal control including control activities for safeguarding securities and in order to determine my auditing procedures for the purpose of expressing my opinion on the financial statements and not to provide assurance on internal control.

Also, as required by Rule 17a-5(g)(1) of the Securities and Exchange Commission (the SEC), I have made a study of the practices and procedures followed by S&V including tests of such practices and procedures that I considered relevant to the objectives stated in Rule 17a-5(g) in making periodic computations of aggregate indebtedness and net capital under Rule 17a-3(a)(11) and for determining compliance with the exemptive provisions of Rule 15c3-3. Because S&V does not carry securities accounts for customers, or perform custodial functions relating to customer securities, I did not review the practices and procedures followed by S&V (i) in making the quarterly securities examinations, counts, verifications, comparisons, (ii) recordation of differences required by Rule 17a-13 or (iii) in complying with the requirements for prompt payment for securities under section 8 of Regulation T of the Board of Governors of the Federal Reserve System.

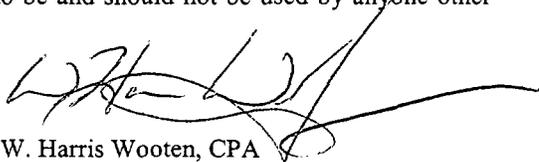
The management of S&V is responsible for establishing and maintaining internal control and the practices and procedures referred to in the preceding paragraph. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of controls and of the practices and procedures referred to in the preceding paragraph and to assess whether those practices and procedures can be expected to achieve the SEC's above-mentioned objectives. Two of the objectives of internal control and the practices and procedures are to provide management with reasonable but not absolute, assurance that assets for which S&V has responsibility are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with management's authorization and recorded properly to permit preparation of financial statements in conformity with accounting principles generally accepted in the United States of America. Rule 17a-5(g) lists additional objectives of the practices and procedures listed in the preceding paragraph.

Because of inherent limitations in internal control or the practices and procedures referred to above, error or fraud may occur and not be detected. Also, projection of any evaluation of them to future periods is subject to the risk that they may become inadequate because of changes in conditions or that the effectiveness of their design and operation may deteriorate.

My consideration of the internal control would not necessarily disclose all matters in internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of the specific internal control components does not reduce to a relatively low level the risk that error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, I noted no matters involving internal control, including control activities for safeguarding securities that I consider to be material weaknesses as defined above.

I understand that practices and procedures that accomplish the objectives referred to in the second paragraph of this report are considered by the SEC to be adequate for its purposes in accordance with the Securities Exchange Act of 1934 and related regulations, and that practices and procedures that do not accomplish such objectives in all material respects indicate a material inadequacy for such purposes. Based on this understanding and on my study, I believe that S&V's practices and procedures were adequate at December 31, 2004 and 2003 to meet the SEC's objectives.

This report is intended solely for the information and use of management, the NASD Regulation, Inc., SEC and other regulatory agencies that rely on rule 17a-5(g) under the Securities and Exchange Act of 1934 in their regulation of registered brokers and dealers, and is not intended to be and should not be used by anyone other than these specified parties.



W. Harris Wooten, CPA

February 7, 2005

Houston, Texas