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

SEC FILE NUMBER
8-14148

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: SUNSET FINANCIAL SERVICES, INC

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

3520 BROADWAY

(No. and Street)

KANSAS CITY, MO 64111

(City)

(State)

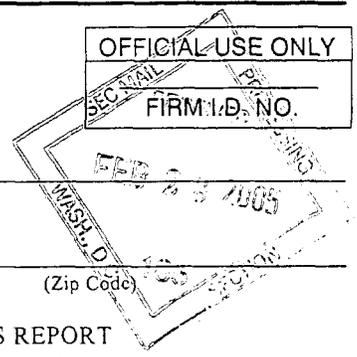
(Zip Code)

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

GREGORY E SMITH

816-753-7000

(Area Code - Telephone Number)



B. ACCOUNTANT IDENTIFICATION

INDEPENDENT PUBLIC ACCOUNTANT whose opinion is contained in this Report*

KPMG, LLP

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

TWO CENTRAL PARK PLAZA, STE 1501

(Address)

(City)

OMAHA

(State)

NE

68102-1626
(Zip Code)

CHECK ONE:

Certified Public Accountant

Public Accountant

Accountant not resident in United States or any of its possessions.

PROCESSED

MAR 17 2005

THOMSON FINANCIAL

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*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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3/16/05
S.S

OATH OR AFFIRMATION

I, GREGORY E SMITH, swear (or affirm) that, to the best of my knowledge and belief the accompanying financial statement and supporting schedules pertaining to the firm of SUNSET FINANCIAL SERVICES, INC, as of DECEMBER 31, 20 04, 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:

JANET L. TATE
Notary Public - State of Missouri
Commissioned in Lafayette County
My Commission Expires Jan. 24, 2007

Gregory E Smith
Signature

President

Title

Janet L. Tate
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.
- (o) Independent Auditor's Report of Internal Control Structure

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

SUNSET FINANCIAL SERVICES, INC.
STATEMENTS OF FINANCIAL CONDITION
(amounts in thousands)

	December 31	
	<u>2004</u>	<u>2003</u>
<u>Assets</u>		
Cash and cash equivalents	\$ 1,003	\$ 776
Accounts receivable (net of allowance of \$3,000 in 2004; \$10,000 in 2003)	186	333
Deferred taxes	18	-
Total assets	<u>\$ 1,207</u>	<u>\$ 1,109</u>
<u>Liabilities</u>		
Commissions payable	\$ 611	\$ 747
Due to affiliated entities	272	49
Accounts payable and accrued liabilities	107	64
Total liabilities	<u>990</u>	<u>860</u>
<u>Stockholder's equity</u>		
Common stock (par value \$10 authorized, 50,000 shares; issued and outstanding, 5,000 shares)	50	50
Additional paid in capital	300	50
Retained earnings (deficit)	<u>(133)</u>	<u>149</u>
Total stockholder's equity	<u>217</u>	<u>249</u>
Total liabilities and stockholder's equity	<u>\$ 1,207</u>	<u>\$ 1,109</u>

See accompanying Notes to Financial Statements.

SUNSET FINANCIAL SERVICES, INC.
STATEMENTS OF OPERATIONS

(amounts in thousands)

	Year Ended December 31	
	<u>2004</u>	<u>2003</u>
<u>Revenues</u>		
Commissions:		
Transactions from unaffiliated entities	\$ 11,193	\$ 8,821
Transactions from affiliated entities	4,161	3,979
Investment and other income	<u>7</u>	<u>4</u>
Total revenues	<u>15,361</u>	<u>12,804</u>
 <u>Expenses</u>		
Commissions	13,778	11,648
Administrative fees	1,572	1,155
Operating expenses	<u>311</u>	<u>3</u>
Total expenses	<u>15,661</u>	<u>12,806</u>
 Loss before income tax benefit	 (300)	 (2)
Income tax benefit	<u>(18)</u>	<u>-</u>
Net loss	\$ <u>(282)</u>	\$ <u>(2)</u>

See accompanying Notes to Financial Statements.

SUNSET FINANCIAL SERVICES, INC.
STATEMENTS OF STOCKHOLDER'S EQUITY

(amounts in thousands)

	Year Ended December 31	
	<u>2004</u>	<u>2003</u>
Common stock, beginning and end of year	\$ <u>50</u>	\$ <u>50</u>
Additional paid in capital:		
Beginning of year	50	50
Additional paid in capital from parent	<u>250</u>	<u>-</u>
End of year	<u>300</u>	<u>50</u>
Retained earnings (deficit):		
Beginning of year	149	151
Net loss	<u>(282)</u>	<u>(2)</u>
End of year	<u>(133)</u>	<u>149</u>
Total stockholder's equity	\$ <u><u>217</u></u>	\$ <u><u>249</u></u>

See accompanying Notes to Financial Statements.

SUNSET FINANCIAL SERVICES, INC.

STATEMENTS OF CASH FLOWS

(amounts in thousands)

	Year Ended December 31	
	<u>2004</u>	<u>2003</u>
<u>Operating Activities</u>		
Net loss	\$ (282)	\$ (2)
Adjustments to reconcile net income to net cash used by operating activities:		
Accounts receivable	147	(217)
Deferred tax	(18)	-
Commissions payable	(136)	317
Due to affiliated entities	223	(92)
Accounts payable and accrued liabilities	<u>43</u>	<u>(22)</u>
Net cash used in operating activities	(23)	(16)
<u>Financing Activities</u>		
Additional paid in capital	<u>250</u>	<u>-</u>
Cash and cash equivalents at beginning of year	<u>776</u>	<u>792</u>
Cash and cash equivalents at end of year	<u>\$ 1,003</u>	<u>\$ 776</u>

See accompanying Notes to Financial Statements.

SUNSET FINANCIAL SERVICES, INC.

Notes to Financial Statements

Significant Accounting Practices

Organization

Sunset Financial Services, Inc. (the Company) is a full-service brokerage firm offering a wide range of financial products. The Company is a wholly-owned subsidiary of Kansas City Life Insurance Company (Kansas City Life). The Company is registered as a broker/dealer with the Securities and Exchange Commission and is a member of the National Association of Securities Dealers, Inc (NASD). The sales force of the Company consists primarily of agents of Kansas City Life and Sunset Life Insurance Company of America (Sunset Life), a wholly-owned subsidiary of Kansas City Life.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from such estimates.

Cash and Cash Equivalents

The Company considers all highly liquid instruments purchased with original maturity of three months or less when purchased to be cash equivalents.

Securities Transactions

Customers' securities and commodities transactions are reported on a trade date basis with related commission income and expenses reported on a trade date basis.

Amounts receivable and payable for securities transactions that have not reached their contractual settlement date are recorded net on the statement of financial condition.

Income Taxes

The Company files a consolidated tax return with certain non-insurance affiliates of its parent, Kansas City Life. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Gross deferred tax assets and liabilities are measured using enacted tax rates and are considered for admitted assets status according to the admissibility tests as set forth by the NASD. The Company recorded a deferred tax asset of \$18,000 at December 31, 2004. There were no deferred tax assets or liabilities at December 31, 2003.

Agreement with Clearing Broker

The Company acts as an introducing broker/dealer and clears all general securities transactions with and for customers on a fully disclosed basis with National Financial Services, a clearing broker. All customer funds and securities are received by the

SUNSET FINANCIAL SERVICES, INC.

Notes to Financial Statements

clearing broker which carries the customer accounts and maintains the records of customer transactions pursuant to the requirements of rules 17a-3 and 17a-4 of the Securities Exchange Act of 1934. For these services, the Company will pay clearing charges as set forth in the agreement between the Company and the clearing broker. The Company is contingently liable to the clearing broker for any losses incurred which may result from the clearing of customer transactions for the Company.

As of December 31, 2004 the Company had a receivable of \$12,000 (\$7,000 - 2003) with the clearing broker.

Net Capital Requirements

The Company is subject to the Securities and Exchange Commission 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. At December 31, 2004, the Company had net capital of \$177,000, which was \$111,000 in excess of its required net capital of \$66,000. The Company's ratio of aggregate indebtedness to net capital was 5.60 to 1.

Related Party Transactions

Pursuant to terms of an agreement, Kansas City Life furnished certain fixed assets and administrative services to the Company. The administrative fees for providing such items, as determined by Kansas City Life, amounted to \$1,572,000 - 2004 (\$1,155,000 - 2003).

The Company executed brokerage transactions for Kansas City Life and Sunset Life and recorded brokerage commissions related to these transactions, as identified in the Statement of Operations. Accounts receivable at December 31, 2004 and 2003 included receivables from affiliates of \$12,900 and \$9,100, respectively.

Contingencies

In November 2000, the Company was named as a co-defendant, with numerous other defendants, in a lawsuit filed by a client of a former representative, alleging conversion of the client's funds. The amount alleged to have been converted is approximately \$400,000. The Company and its co-defendant, Kansas City Life, prevailed on their motion for summary judgment. Defendants have appealed that ruling.

SUNSET FINANCIAL SERVICES, INC.

Notes to Financial Statements

Contingencies (continued)

In September 2001, the Company was named as a co-defendant, with numerous other defendants, in a lawsuit filed by several clients of two former representatives. The lawsuit alleges that the former representatives participated in sales of offshore annuity products which were unsuitable to the clients' needs. The total amount of alleged damages is approximately \$500,000. Subsequently the case was consolidated with another case and was settled in 2004 for \$128,500, which was paid by the Company's co-defendant, Kansas City Life.

In October 2001, the Company was named as a co-defendant, with a former representative, in a lawsuit that alleged fraud and breach of fiduciary duty. The Company's Motion to Compel Arbitration, as provided in the new account form, was denied. The Company appealed the decision and won on appeal. The claimants have refiled the case as an arbitration proceeding under NASD arbitration rules and have requested actual damages of \$215,000.

In March 2002, the Company was named a defendant, with former representatives and employees, in a lawsuit brought by a state regulatory agency which alleged breach of securities laws and failure to supervise. The case was settled in December, 2004, for \$250,000 which was paid by the Company.

In January 2003, the Company was named as a defendant, along with Kansas City Life, two active representatives and an unrelated insurance company as co-defendants, in a lawsuit filed by a former client. The plaintiff alleged deceptive trade practices and fraud in the sale of securities. Actual damages of \$110,000 and emotional stress damages of \$350,000 were requested. The case was settled at mediation in January 2005 for \$38,500. The Company will pay \$9,250, one of its co-defendants, Kansas City Life will pay \$10,000 and the other co-defendants will pay \$19,250.

In June 2003, the Company and a former representative were sued by a customer for conversion of funds by the representative. Actual damages of \$222,000 were alleged. In 2004, the Company settled the case in principle for \$50,000. Payment will be made and the settlement will be finalized early in 2005.

In July 2003, the Company, with a representative and an unrelated insurance company, was sued by a customer. The customer alleged that the representative negligently failed to apply for a product feature. No specific amount of damages have been identified. The Company has moved to stay the court case and to arbitrate the claim. In a separate action, the customer has sued the unrelated insurance company for reformation of the policy. There has been no further action in this case.

SUNSET FINANCIAL SERVICES, INC.
Notes to Financial Statements

Contingencies (continued)

In October 2003, the Company and a former representative were sued by the trustee of the living trust of a deceased former customer. The suit alleged that the former representative, who was the customer's daughter, took advantage of the familial relationship and mismanaged the account. No specific amount of damages were stated, but it is inferred from the pleading that the Plaintiff claimed approximately \$40,000 from the Company. There has been no further action in this case.

In April 2004, two customers filed a NASD claim against the Company and two of the Company's representatives that arose out of the customers' purchase of several variable annuities. The claim alleged that the annuities were unsuitable investments, that the Company and its representatives failed to manage the investments and allowed them to significantly decrease in value, and that the Company failed to properly supervise the representatives. Specifically, the claim included allegations of breach of fiduciary duty, negligence, negligent supervision, misrepresentation, breach of contract, failure to supervise, and suitability violations arising out of the sale of those products. The claimants requested damages in the amount of approximately \$235,000, which was the aggregate amount of the losses incurred in the variable annuity products. The case will likely be arbitrated in July 2005.

It is not reasonably possible at this time to make any conclusion as to the outcome of active litigations, but based on information currently available management does not consider it likely that any of the active litigations will result in a material impact to the Company's net capital.

Subsequent Event

On January 24, 2005, the Kansas City Life Board of Directors approved a capital contribution of \$500,000 to be paid in the first quarter of 2005.

SUNSET FINANCIAL SERVICES, INC.
COMPUTATION OF NET CAPITAL UNDER RULE 15c3-1
OF THE SECURITIES AND EXCHANGE COMMISSION
(amounts in thousands)

	December 31 <u>2004</u>
<u>Schedule I</u>	
<u>Net Capital</u>	
Total stockholder's equity	\$ <u>217</u>
Non-allowable assets	20
Haircuts on securities (computed pursuant to Rule 15c3-1(c)(2)(vi)(D))	<u>20</u>
Net capital	177
Minimum net capital requirement	<u>66</u>
Excess net capital	<u><u>\$ 111</u></u>
<u>Aggregate Indebtedness</u>	
Commissions payable	\$ 611
Due to affiliated entities	272
Accounts payable and accrued liabilities	<u>107</u>
Aggregate indebtedness	<u><u>\$ 990</u></u>
Ratio of aggregate indebtedness to net capital	<u><u>5.60 to 1</u></u>

Statement regarding Rule 17a-5(d)(4)

There were no material differences between the computation of net capital under Rule 15c3-1 included in this audited report and the computation included in the Company's corresponding unaudited Form X-17A-5 Part IIA filing as of December 31, 2004.

SUNSET FINANCIAL SERVICES, INC.
EXEMPTIVE PROVISION UNDER RULE 15c3-3

Schedule II

The Company is exempt from Rule 15c3-3 of the Securities and Exchange Commission under paragraph (k)(1) of that Rule. The Company clears transactions through National Financial Services.



**Independent Auditors' Report on
Internal Control Required by SEC Rule 17a-5**

The Board of Directors
Sunset Financial Services, Inc.:

In planning and performing our audit of the financial statements and supplemental schedules of Sunset Financial Services, Inc. (the Company) for the year ended December 31, 2004, we considered its internal control, including control activities for safeguarding securities, in order to determine our auditing procedures for the purpose of expressing our 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 (SEC), we have made a study of the practices and procedures followed by the Company, including tests of such practices and procedures that we considered relevant to the objectives stated in Rule 17a-5(g), in making the periodic computations of aggregate indebtedness (or aggregate debits) and net capital under Rule 17a-3(a)(11) and for determining compliance with the exemptive provisions of Rule 15c3-3. Because the Company does not carry securities accounts for customers or perform custodial functions relating to customer securities, we did not review the practices and procedures followed by the Company in any of the following:

1. Making quarterly securities examinations, counts, verifications, and comparisons
2. Recordation of differences required by Rule 17a-13
3. Complying with the requirement for prompt payment for securities under Section 8 of Regulation T of the Board of Governors of the Federal Reserve System

The management of the Company 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 judgments 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 the Company 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 the 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. Our consideration of 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, we noted no matters involving internal control, including control activities for safeguarding securities, that we consider to be material weaknesses as defined above.

We 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 our study, we believe that the Company's practices and procedures were adequate at December 31, 2003 to meet the SEC's objectives.

This report is intended solely for the information and use of the board of directors, management, the SEC, the National Association of Securities Dealers, Inc., and other regulatory agencies that rely on Rule 17a-5(g) under the Securities 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.

KPMG LLP

February 18, 2005



Independent Auditors' Report

The Board of Directors
Sunset Financial Services, Inc.:

We have audited the accompanying statements of financial condition of Sunset Financial Services, Inc. (the Company) as of December 31, 2004 and 2003, and the related statements of operations, stockholder's equity, and cash flows for the years then ended that you are filing pursuant to Rule 17a-5 under the Securities Exchange Act of 1934. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. 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, the financial statements referred to above present fairly, in all material respects, the financial position of Sunset Financial Services, Inc. as of December 31, 2004 and 2003, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information contained in Schedules I and II is presented for purposes of additional analysis and is not a required part of the basic financial statements, but is supplementary information required by Rule 17a-5 under the Securities Exchange Act of 1934. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

KPMG LLP

February 18, 2005