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

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

SEC FILE NUMBER 8- 33443

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 4/1/2007 AND ENDING 3/31/2008 MM/DD/YY MM/DD/YY

A. REGISTRANT IDENTIFICATION

NAME OF BROKER-DEALER: Carnes Capital Corporation

OFFICIAL USE ONLY FIRM I.D. NO.

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

8889 Pelican Bay Boulevard, Suite 500 (No. and Street)

Naples

FL

34108

(City)

(State)

(Zip Code)

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

John F. Cheever

239-254-2520

(Area Code - Telephone Number)

B. ACCOUNTANT IDENTIFICATION

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

Price Waterhouse Coopers LLP

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

4221 West Boy Scout Boulevard, Ste 200, Tampa

(Address)

(City)

FL

(State)

SEC 33607 Mail Processing Section (Zip Code)

MAY 27 2008

Washington, DC 101

CHECK ONE:

[X] Certified Public Accountant

[ ] Public Accountant

[ ] Accountant not resident in United States or any of its possessions

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)

AB\* 5/29

PROCESSED MAY 30 2008 THOMSON REUTERS

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OATH OR AFFIRMATION

I, John F. Cheever, swear (or affirm) that, to the best of my knowledge and belief the accompanying financial statement and supporting schedules pertaining to the firm of Carnes Capital Corporation, as of March 31, 20 08, 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:

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



Deanna Adams  
Notary Public

John F. Cheever  
Signature  
CONTROLLER  
Title

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 15c3-1 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).

# Carnes Capital Corporation and Subsidiary

(an indirect wholly owned subsidiary of Legg Mason, Inc.)

Consolidated Statement of Financial Condition

March 31, 2008

SEC  
Mail Processing  
Section

MAY 27 2008

Washington, DC  
101

**Carnes Capital Corporation and Subsidiary**

(an indirect wholly owned subsidiary of Legg Mason, Inc.)

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**March 31, 2008**

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4221 West Boy Scout Boulevard  
Suite 200  
Tampa, FL 33607-5745  
Telephone (813) 229 0221  
Facsimile (813) 229 3646

**Report of Independent Certified Public Accountants**

To the Board of Directors and Stockholder of  
Carnes Capital Corporation and Subsidiary

In our opinion, the accompanying consolidated statement of financial condition presents fairly, in all material respects, the financial position of Carnes Capital Corporation and Subsidiary (the "Company") at March 31, 2008, in conformity with accounting principles generally accepted in the United States of America. This financial statement is the responsibility of the Company's management; our responsibility is to express an opinion on this financial statement based on our audit. We conducted our audit of this statement in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated statement of financial condition is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated statement of financial condition, assessing the accounting principles used and significant estimates made by management, and evaluating the overall consolidated statement of financial condition presentation. We believe that our audit of the consolidated statement of financial condition provides a reasonable basis for our opinion.



May 16, 2008

**Carnes Capital Corporation and Subsidiary**  
 (an indirect wholly owned subsidiary of Legg Mason, Inc.)  
**Consolidated Statement of Financial Condition**  
**March 31, 2008**

<b>Assets</b>	
Cash and cash equivalents	\$ 11,583,581
Receivable from clearing broker	1,888,076
Property and equipment at cost, less accumulated depreciation and amortization of \$3,545,186	253,069
Receivable from Parent	621,486
Deferred taxes, net	248,258
Other assets	<u>421,193</u>
Total assets	<u>\$ 15,015,663</u>
<b>Liabilities and Stockholder's Equity</b>	
<b>Liabilities</b>	
Payable to affiliate	\$ 462,835
Accrued compensation	11,148,817
Accounts payable and other accrued expenses	<u>52,867</u>
Total liabilities	<u>11,664,519</u>
Commitments and contingencies (Note 6)	
<b>Stockholder's Equity</b>	
Common stock, \$1 par value; 200,000 shares authorized; 105,600 shares issued and outstanding	105,600
Additional paid-in capital	4,282,726
Accumulated deficit	<u>(1,037,182)</u>
Total stockholder's equity	<u>3,351,144</u>
Total liabilities and stockholder's equity	<u>\$ 15,015,663</u>

The accompanying notes are an integral part of this consolidated financial statement.

**Carnes Capital Corporation and Subsidiary**  
(an indirect wholly owned subsidiary of Legg Mason, Inc.)  
**Notes to the Consolidated Statement of Financial Condition**

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**1. Summary of Significant Accounting Policies**

**Organization**

Carnes Capital Corporation and Subsidiary (the "Company"), a wholly owned subsidiary of PCM Holdings, Inc. (the "Parent"), which is a wholly owned subsidiary of Legg Mason, Inc. ("Legg Mason"), is a broker-dealer registered with the Securities and Exchange Commission under the Securities and Exchange Act of 1934 and is a member of the National Association of Securities Dealers, Inc. The Company provides securities trading and brokerage services to clients of an affiliated entity. Institutional Capital Management, Inc. ("ICM") is a wholly owned subsidiary of the Company. ICM is engaged in a business limited exclusively to investment research.

The consolidated financial statement includes the accounts of Carnes Capital Corporation and ICM. All significant intercompany balances and transactions are eliminated in consolidation.

**Cash and Cash Equivalents**

The Company considers money market instruments with original maturities of 90 days or less to be cash equivalents. Cash equivalents at March 31, 2008 represent money market accounts at an unaffiliated bank and an unaffiliated broker-dealer.

**Receivable from Clearing Broker**

Receivable from clearing broker represents commissions and interest receivable from the Company's clearing broker. Such amounts are not collateralized and are expected to be fully collectible.

**Property and Equipment**

Property and equipment are recorded at cost. Depreciation is provided on a straight-line basis using an estimated useful life of three to five years for equipment and five to seven years for furniture and fixtures. Software is amortized on a straight-line basis using an estimated useful life of three years. Leasehold improvements are amortized on a straight-line basis over the lesser of the useful life of the improvement or the term of the lease.

**Fair Value of Financial Instruments**

Statement on Financial Accounting Standards No. 107, *Disclosures about Fair Value of Financial Instruments*, requires that all entities disclose the fair value of financial instruments, as defined, for both assets and liabilities recognized and not recognized in the statement of financial condition. The Company's financial instruments, as defined, are carried at, or approximate, fair value.

**Clearing Arrangements**

Pursuant to agreements between the Company and its correspondent clearing broker, securities transactions effected by the Company are cleared on a fully disclosed basis through the correspondent clearing broker.

**Use of Estimates**

The consolidated financial statement is prepared in accordance with accounting principals generally accepted in the United States of America that require management to make assumptions and estimates that affect the amounts and disclosures presented. Actual results could differ from those estimates and the differences could have a material impact on the consolidated financial statements.

**Carnes Capital Corporation and Subsidiary**  
 (an indirect wholly owned subsidiary of Legg Mason, Inc.)  
**Notes to the Consolidated Statement of Financial Condition**

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**2. Property and Equipment**

The balances of property and equipment at March 31, 2008 are:

Leasehold improvements	\$ 1,493,823
Office furniture	845,887
Office equipment	654,551
Software	803,994
	<u>3,798,255</u>
Less: Accumulated depreciation and amortization	<u>(3,545,186)</u>
	<u>\$ 253,069</u>

**3. Net Capital Requirements**

Carnes Capital Corporation is subject to the Securities and Exchange Commission's Uniform Net Capital Rule pursuant to Rule 15c3-1 (the "Rule"), which requires the maintenance of minimum net capital equal to \$100,000 or 6-2/3% of total aggregate indebtedness, whichever is greater, and requires that the ratio of aggregate indebtedness to net capital, both as defined, shall not exceed 15 to 1. Net capital and the related ratio of aggregate indebtedness to net capital, as defined, may fluctuate on a daily basis.

As of March 31, 2008, Carnes Capital Corporation had net capital of \$1,559,894 which was \$781,650 in excess of required capital of \$778,244. Carnes Capital Corporation's percentage of aggregate indebtedness to net capital was 748% which does not exceed the maximum allowable percentage of 1,500%.

Carnes Capital Corporation is exempt from the SEC's Customer Protection Rule ("Rule 15c3-3"). Section (k)(2)(ii) of Rule 15c3-3 allows for this exemption since all customer transactions are cleared through other broker-dealers on a fully-disclosed basis.

**4. Income Taxes**

The Company has elected to be included in the consolidated federal income tax return with Legg Mason, Inc. and files a separate state income tax return. The Company's allocable share of federal income taxes and its separate state income taxes are recorded as a provision for income taxes and income taxes payable. The provision (benefit) for federal income taxes was determined as if the Company filed a separate return.

Deferred taxes are recorded to recognize the expected future obligation or benefit of temporary differences between the tax basis and financial reporting basis of assets and liabilities based on enacted tax laws and statutory rates applicable to the periods in which the differences are expected to effect taxable income. At March 31, 2008, the Company had a net deferred tax asset of \$248,258.

**Carnes Capital Corporation and Subsidiary**  
 (an indirect wholly owned subsidiary of Legg Mason, Inc.)  
**Notes to the Consolidated Statement of Financial Condition**

The income tax effects of temporary differences that give rise to deferred tax assets and liabilities are as follows:

<b>Deferred income tax assets</b>	
State net operating loss	\$ 59,248
Accrued compensation and benefits	6,796
Depreciation	352,042
	<u>418,086</u>
<b>Deferred income tax liabilities</b>	
Prepaid expenses	(162,454)
Loss on sale of assets	(7,374)
	<u>(169,828)</u>
Net deferred tax asset	<u>\$ 248,258</u>

The Company has a state net operating loss carryforward of approximately \$1,613,000 that expires after March 31, 2027.

The Company has considered the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, and determined there are no material uncertain tax positions for the year ended March 31, 2008.

**5. Commitments and Contingencies**

Under operating leases, with remaining noncancelable terms in excess of one year as of March 31, 2008, minimum aggregate annual rentals for office space are as follows:

Year Ending March 31,	
2009	\$ 453,172
2010	435,087
2011	439,019
2012	454,385
2013	470,288
Total	<u>\$ 2,251,951</u>

The Company clears all of its securities transactions through a clearing broker on a fully disclosed basis. Pursuant to the terms of the agreement between the Company and the clearing broker, the clearing broker has the right to charge the Company for losses that result from a counterparty's failure to fulfill its contractual obligations.

As the right to charge the Company has no maximum amount and applies to all trades executed through the clearing broker, the Company believes there is no maximum amount assignable to this right. At March 31, 2008, the Company has recorded no liabilities, and during the year then ended incurred no costs, with regard to this right.

In the normal course of business the Company enters into contracts that contain a variety of representations and warranties, and which provide general indemnifications. The Company's maximum exposure under these arrangements is unknown, as they would involve future claims that may be made against the Company that have not yet occurred.

**Carnes Capital Corporation and Subsidiary**  
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**Notes to the Consolidated Statement of Financial Condition**

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**6. Related Party Transactions**

The Company shares various assets with the investment advisor to the clients and the Company pays for those expenses. Other entities affiliated with Legg Mason also provide certain supporting administrative services to the Company that are reimbursable to these affiliated entities. The Company's financial condition may not be indicative of the financial condition of a stand-alone company.

In accordance with the purchase agreement with Legg Mason, 75% of the combined revenues of the Company and an affiliate, as defined, are distributed to Legg Mason. The remaining 25% is used to pay the operating expenses of the Company and its affiliate. During the year ended March 31, 2008, all payments required under the purchase agreement were made by this affiliate.

**7. Off-Balance-Sheet Risk**

In the normal course of business, the Company's customer activities involve the execution and settlement of various securities transactions. These activities may expose the Company to off-balance-sheet risk in the event the customer is unable to fulfill its contracted obligations.

**END**