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American Institute of Accountants. Committee on Member Firms of the New York Stock Exchange

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Audits of Stockbrokers' Accounts

AS REPORTED in the Notes of the Month department of the April issue, the committee on member firms of the New York Stock Exchange on March 20th announced the adoption of regulations to be applied under new rules requiring annual audit of the accounts of member firms. This action followed some weeks of study in cooperation with special committees of the American Institute of Accountants and the New York State Society of Certified Public Accountants.

Following is the text of a letter addressed by the Exchange to member firms describing the new requirements, and also the text of the forms and regulations to which reference is made:

GENTLEMEN:

The Committee on Member Firms is sending you herewith copy of a questionnaire to be answered by registered member firms in reporting their financial condition to it, in accordance with rule 531 of the rules of the Board of Governors.

At your *earliest* convenience, but not later than, you are requested to forward in the enclosed envelope *addressed to the Committee on Member Firms, Room 2000, New York Stock Exchange*, the position of your firm as of

Rule 532 of the rules of the Board of Governors calls for an audit of the books, which audit must be made by an independent public accountant and must be coincident with the preparation of your answer to the questionnaire.

The answer to the questionnaire must also be prepared or verified by the independent public accountant making the coincident audit.

Your answer must be accompanied by the form of attestation enclosed herewith, which is to be signed by each general partner of your firm and by the independent public accountant.

When the audit has not been completed by the date on which the answer to the questionnaire is required to be filed, please have such answer accompanied by a letter signed by at least two general partners of the firm and by the independent public accountant attesting the accuracy of it; and thereafter, when the audit is completed, but not later than sixty days after date of answer, the form of attestation herewith enclosed, signed by all general partners and by the independent public accountant, should be submitted to the Committee on Member Firms.

Very truly yours,
Manager

REGULATIONS PRESCRIBED BY THE COMMITTEE ON MEMBER FIRMS FOR AUDIT UNDER AUTHORITY OF RULE 532 (AS AMENDED OCTOBER 26, 1938) OF THE RULES OF THE BOARD OF GOVERNORS.

All member firms doing any securities business with others than members or member firms shall have an audit of their books, records and accounts made by independent public accountants at least once in each year upon call of the Committee on Member Firms.

The audit shall be, at least, such as to substantiate the stated assets and liabilities of such member firm as of the date selected by the Committee on Member Firms, and the scope and comprehensiveness thereof shall be such as would enable the independent public accountant to express an opinion as to the stated financial condition of the member firm as of that date.

The scope of the audit shall comprehend at least the following:

Comparison of ledger accounts with a trial balance obtained from the general and private ledgers and proofs of the aggregates of subsidiary ledgers with the respective controlling accounts therein.

Physical examination and comparison with books and records of all securities, currencies, tax stamps, warehouse receipts and other such assets

Audits of Stockbrokers' Accounts

- on hand in vault or box or otherwise in physical possession.
- Verification of securities in transit or in transfer.
- Balancing of positions in all securities and commodities ("spot" and "future") as shown by the books and records.
- Obtaining of written confirmations with respect to the following:
 - Bank balances.
 - Clearing corporation or association deposits or funds and open contractual positions.
 - Money borrowed and detail of collateral.
 - Accounts, commodities, securities and commitments carried for the firm by others.
- Details of:
 - Securities borrowed.
 - Securities loaned.
 - Securities failed to deliver.
 - Securities failed to receive.
 - When issued contracts.
 - Delayed delivery and other similar open contracts.
 - Open commodity contracts with other firms.
- Customers', partners' and firm's Accounts:
 - Ledger balance.
 - Securities long and short.
 - When issued contracts.
 - Delayed delivery and other similar open contracts.
 - Open commodity contracts.
- Guarantees in cases where required to protect accounts guaranteed as of audit date.
- All other accounts which in the opinion of the independent public accountant should be confirmed.
- A written statement from a partner of the member firm as to all assets, liabilities and accountabilities, contingent or otherwise, not recorded upon the books of the member firm.
- Compliance with requirements for obtaining written confirmation with respect to the above accounts shall be deemed to have been made if requests for confirmation have been mailed by the independent public accountant in an envelope bearing his own return address and a second request

similarly mailed to those not replying to the first request.

In addition to the reconciliation and confirmation of bank balances as of the date of the audit, the independent public accountant shall, at a later date, after giving ample time for clearance of outstanding checks and transfers of funds, obtain from depositaries canceled checks and statements of the bank accounts as of such date, and reconcile the balances shown thereon with the balances shown by the books of the member firm.

A written report shall be submitted by the independent public accountant in which he shall attest that the requirements of these regulations have been observed in the conduct of the audit.

Any condition disclosed by the audit that would cause the capital or net worth of the member or member firm to be less than that prescribed by the Committee on Member Firms shall be reported to that Committee by the member firm immediately upon the ascertainment of such facts.

QUESTIONNAIRE FOR MEMBER FIRMS DOING ANY SECURITIES BUSINESS WITH OTHERS THAN MEMBERS OR MEMBER FIRMS OR DOING A GENERAL BUSINESS WITH THE PUBLIC

1. *Total Bank Balances and Other Deposits.*

State total of each of contributions to clearing funds and commodity margin or other deposits. (State segregated funds separately with adequate description.)

2. *Total Money Borrowed and Open "Street" Items.*

State separately:

Total money borrowed and total market value of collateral;
"Omnibus" accounts (each account individually) carried for your firm by other banking or brokerage houses, showing debit and credit money balances, market value of securities both long and short, and status of commodity positions; and

Ledger balances and market value of securities in accounts for: securities borrowed, securities loaned, securities failed to deliver and securities failed to receive.

Responses to this question should indicate any borrowings or "omnibus" accounts adequately collateralized by securities exempted from registration under the securities exchange act of 1934, otherwise than by action of the Securities and Exchange Commission, and by securities owned by respondent member firm or general partner thereof if exception from capital requirement thereon is desired.

3. *Total Market Value of Negotiable Securities in Box and in Transfer.*
4. *Customers' Accounts.* (All accounts for others than the firm or general partners thereof.)

State separately totals of ledger debit balances and totals of ledger credit balances, with totals of "long" security valuations, totals of "short" security valuations and status of commodity positions in customers' accounts in classifications as follows:

- (a) Accounts in which the margin is equal to or greater than New York Stock Exchange requirements or accounts with current outstanding margin calls and bona fide "cash" accounts which are expected to be cleared up within the time prescribed by Regulation T of the Board of Governors of the Federal Reserve System or by the New York Stock Exchange margin requirements;
- (b) Accounts in which the margin is less than New York Stock Exchange minimum requirements and which are not in such status as to warrant classification in section (a) above;
(State the total of "cash" necessary, for these accounts, to bring margin up to New York Stock Exchange margin requirements.)

- (c) Accounts in deficit or unsecured and which are not in such status as to warrant classification in section (a) above;
- (d) Accounts with "free" credit balances; and
- (e) Commodity accounts.

Customers' accounts with commodity positions should be so stated as to indicate accounts in "deficit" and accounts with "spot" commodities in which accounts the equity is less than 30% of the debit balance.

The total of any "equities" in customers' "future" commodity accounts not segregated under the Commodities Exchange Act must be clearly indicated.

Accounts of any single entity with both security and commodity positions may be stated in a combined status. If so stated all relevant factors must be indicated.

Customers' accounts with no ledger balance but with open commitments, contracts or positions should be stated separately in such manner as to indicate clearly whether or not the item is in "equity" or "deficit."

Balances and positions in each particular kind of security carried in accounts related by guarantees, if the guarantees are in an acceptable form and sufficiently comprehensive to warrant merging balances and security valuations, may be treated net and the consolidated position included as the account of a single entity in the proper classification determined by the consolidated position.

5. *Partners' Accounts.*

State total of debit balances and total of credit balances, also total market value of long securities and "spot" commodities and total market value of short securities and total of net "profits" or total of net "losses" in "future" commodity positions in the following accounts:

- (a) General partners' individual accounts;

Audits of Stockbrokers' Accounts

- (b) Firm investment and trading accounts;
- (c) Underwriting and syndicate participation accounts; and
- (d) Capital accounts.

State separately:

Any amounts or valuations requested herein resulting from borrowings under subordination agreements or otherwise;

Any market valuations of long securities exempted from registration under the securities exchange act of 1934, otherwise than by action of the Securities and Exchange Commission; and

Any market valuations of "spot" commodities which are hedged.

6. Profit-and-Loss Accounts.

Surplus and undivided profits, including balances in income and expense accounts (commission, interest, expenses, etc.) which will eventually be closed by journalizing to a profit-and-loss account. This question may be answered by giving one net amount, specifying debit or credit.

7. Other Accounts.

State details (ledger balances, market values of securities, status of commodity positions, and any other relevant information) of any accounts which have not been included in one of the answers to the above questions, entering each account separately. These accounts will include exchange memberships, office furniture and other fixed assets, if carried on the books, revenue-stamp accounts, dividend accounts, "floor" brokerage receivable, other commission receivable (commission receivable currently from other member firms should be stated separately), and commodity "difference" accounts.

8. Contingent Items.

Give a description of any open contingent assets, liabilities and accountabilities of the firm, other than

customers' "regular way" purchases and sales, that are not included in a ledger account, showing the full application of such items to any existing positions as well as to each other. Items of this nature may include:

- Purchases and sales for account of firm and partners.
- Underwriting commitments.
- "When-issued" contracts.
- Delayed delivery items.
- Commitments in foreign currencies.
- Accommodation endorsements.
- Endorsements of puts and calls.
- Rediscounted notes.

9. Partners' Accounts in Other Offices.

Have any general partners of your firm, individually or collectively, any security or commodity accounts or commitments carried by banks, trust companies, or other banking or brokerage houses, which are not reflected on your books? If so, state debit and credit balances, value of securities and "spot" commodities long or short, and profit or loss in open commodity contracts.

Name of Firm
 Address
 19..

COMMITTEE ON MEMBER FIRMS,
 New York Stock Exchange,
 11 Wall Street, New York, N. Y.

GENTLEMEN:

We, the undersigned, members of the firm of have caused an audit to be made in accord with our answer to the questionnaire as of 19.., in accordance with the regulations prescribed by your committee under rule 532 of the rules of the Board of Governors.

We hereby certify that, to the best of our knowledge and belief, the above mentioned answer to the questionnaire represents a true and correct financial statement of our firm.

.....
.....
I (we) hereby attest that the above mentioned audit has been made, and also that the coincident answer to the questionnaire has been prepared or verified, by me (us).

.....
GENERAL INSTRUCTIONS

**PLACE YOUR NAME ON EACH SHEET
OF THE ANSWERS YOU SUBMIT**

All answers must be prepared as of the same date and must also be prepared or verified by the independent public accountant making the coincident audit.

In stating ledger balances, specify debit or credit, and in stating security valuations, state whether long or short.

"Foreign" currency may be converted to United States dollars at the current rate of exchange and where carried in conjunction with United States dollar balances for the same entity may be consolidated with such United States dollar balances and the gross or net position reported in its proper classification, all only if the "foreign" currency is not subject to any restrictions as to conversion. If any material "foreign" currency position is so treated some indication of its size should be given on a separate schedule or otherwise.

Funds, commodities, or securities segregated under the commodities-exchange act, as well as the accounts in which reflected, should be clearly indi-

cated in the various classifications of the answers.

Each joint account in which the firm or any general partner has an interest should be stated separately as a customer's account in the proper classification in answer to question 4.

State separately any valuations of securities held in "safekeeping" for partners or otherwise made unavailable for claims of creditors of the firm.

Submit, in a separate schedule, full details of security and commodity positions (long and short) carried for firm and partners' accounts and for customers' accounts classified in section 4 (c).

The valuations of customers' "segregated" securities may be excluded from answers.

Material facts in regard to substantial amounts of securities which do not have an active market on a recognized exchange or which are subject to sudden changes in value, and also in regard to accounts in which such securities are carried, should be stated in the answers or in a separate schedule.

Retain a copy of your answers to this form of questionnaire and all working papers and memoranda covering the answer for at least two years. (Working papers, etc., may be retained in custody of your independent public accountant if available to Exchange for audit and review.)

Send answers in enclosed envelope, or in one similarly addressed to *Committee on Member Firms, Room 2000, New York Stock Exchange.*