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1969

## Countdown on Wall Street

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### Recommended Citation

H&S Reports, Vol. 06, (1969 autumn), p. 04-09

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# COUNTDOWN ON WALL STREET

H&S moves in on  
a major brokerage firm.  
Purpose:  
a "surprise" audit.

**Zero Hour Minus 15:** Nine accountants wait near the elevators on the twenty-second floor at Two Broadway in New York. One carries an H&S work bag. The senior in charge carries a briefcase. Two men join them. One a partner; the other, a principal.

**Zero Hour Minus 12:** The men crowd into the "down" elevators. Out the building the group marches, and through the narrow canyons of the financial district. Their mission: a surprise audit at the head office of a major downtown brokerage firm.

Moving in a tight phalanx, the accountants enter the target building, take the elevator to the designated floor, push aside double glass doors, and walk between rows of waiting messengers, who look at them with surprise. The leader opens a door to the cage and starts through it. An alert security man pushes forward to confront them.

"Who arranged this tour?" he demands, thinking this is a typical group of tourists.

"I did," says the New York Office partner. "We're from Haskins & Sells!" He holds his H&S identification card high. The guard relaxes, and ushers the auditors into the main part of the closely protected cage, or back-office, where all securities are handled. Time: Zero hour.

Client employees in adjacent glass-walled offices buzz about, asking one another what is happening. Old hands tell them as our senior accountant in charge signals to his men, deploying two of them to the doors to control visually all movements of securities to and from that area. With a take-over air about them, the accountants responsible for cage and vault control, commodities and other sections of the brokerage house quickly move to their assigned departments. The brokerage house work resumes under the watchful eyes of the H&S staff.

**Zero Hour Plus 30:** Fifteen people—client representatives and auditors—crowd into the office of the executive vice president. "My weekend's spoiled now. And I was going to have house guests!" groans one client supervisor. Then the practical questions fly fast: "When will securities in segregation and active box be counted?" "Where can we put thirty work tables and chairs?" "When will H&S cut off securities going to transfer?" "When will breaksheets come off the computer?" "When can we get computer time?" "Who's on the cash count?" The Haskins & Sells senior in charge runs

down the list on his clipboard, making notes and checking items. A telephone rings out above the talk. A client executive picks up, listens, nods assent, then places the phone back on its cradle.

"That was Dallas," he calls out. "Haskins & Sells has moved into our office there."

**Zero Hour Plus 115:** By now the air is thick with smoke and the ashtrays are full. The mechanics of the audit are settled; questions of who, where and when are answered. The senior in charge makes sure that everything on his checklist is covered. The meeting adjourns and the accountants are ready to go to work.

The following morning, 50 Haskins & Sells accountants report to count stocks and bonds. Over the next 45 days key accountants (section heads) and their assistants continue the audit. They request confirmation of customers' accounts and cash balances. The auditors working with the securities records, prepared by computer from magnetic tape under audit control, balance every security by identifying the physical location of all securities owned by customers of the broker. H&S counts the securities on hand and requests confirmations of those held by other brokers and banks. Hundreds of thousands of confirmation requests are sent to customers of the broker to make sure that they agree with the securities listed in the firm's records as being the property of these customers. After all securities have been accounted for, the accounts of customers are examined to ascertain that adequate margin is being maintained and that securities are being properly segregated. General ledger accounts are analyzed and they, along with the accounts of brokers, banks and customers are classified and prepared for assembly into the financial questionnaire.

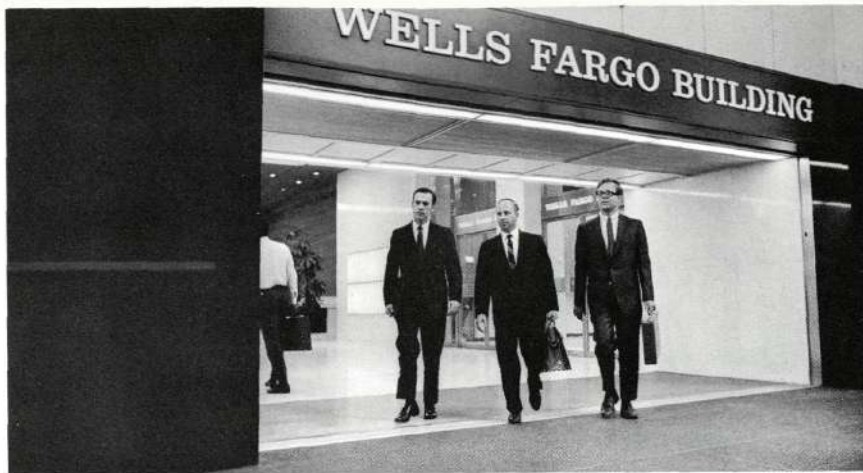
Computers manned by client teams and attended by our electronic data processing experts steadily spit out information essential to the confirming process, as security counts are reconciled with figures in the client's records.

Meanwhile, in four other cities where this brokerage firm has branch offices, similar H&S surprise audits are going on. Although we may have fewer accountants examining other offices, the procedure is much the same.

Toward the end of the audit, the accountants in charge prepare the financial questionnaire, called the "Q," required by the New York Stock Exchange and the U.S. Securities and Exchange Commission. The questionnaire

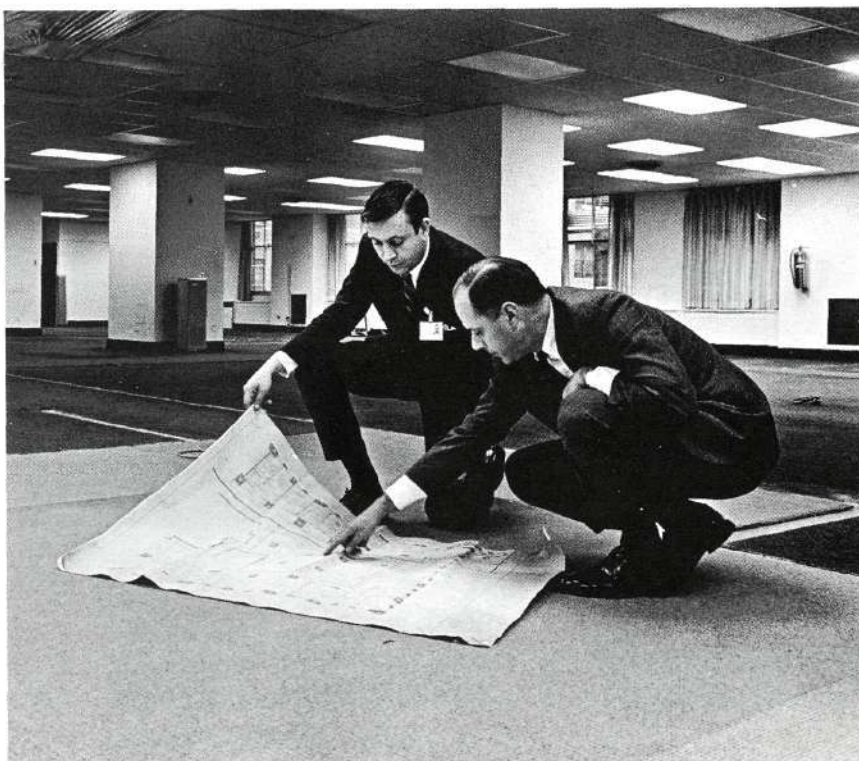
Zero hour minus 10: A phalanx of H&S auditors files out of the New York Office at Two Broadway—on the way to a "surprise" (unannounced) brokerage audit. Flanking the partner heading the engagement are principals, the coordinating senior accountant in charge and section heads—each an expert in a part of the audit.

Meanwhile—from the San Francisco Office—H&S accountants set out for a branch of the New York client. The same scene takes place in cities across the country where the same broker handles securities. The H&S office in charge of the engagement keeps in close touch with the auditors working on the client branch office operations.



Zero hour minus 60: Just before moving in, the key men of the audit team get together to nail down last-minute plans. Here in a conference room in the New York Office, they thrash out all remaining details.

"We'll set up for the security counts here." In the middle of an empty office, Douglas D. Milne, Jr. (r.), vice president in charge of operations of Merrill Lynch, Pierce, Fenner & Smith, Inc. discusses the layout with Ed Lill, H&S partner in charge of the engagement. Here for the next few days, H&S auditors and client employees will count securities. The audit hit Merrill Lynch while it was renovating its offices. H&S auditors moved in and that evening the walls came down to provide space for the count.





For many mornings, trains of file cabinets and drawers holding certificates worth billions of dollars are pushed from the security of the vault to the counting space. Standing near the massive, 2½-foot-thick vault door at Merrill Lynch, an H&S auditor monitors this whirl of activity.

displays the financial condition of the broker and permits the review of its compliance with the rules of both the Exchange and the SEC. Under the rules of the SEC the report of the broker "shall be certified by a certified public accountant . . ."

In January of this year there were more than 26 million individuals and institutions who owned shares in public corporations. The number has more than doubled in the past decade. As each year passed, the increased volume of stock transactions kept the brokerage houses maddeningly busy. Manual handling of stock certificates several times as each transaction was recorded caused an unprecedented acceleration in their workloads, and some houses were literally jammed at the paperwork bottleneck.

The audit of any brokerage house provides a vast army of investors with an independent check that gives them confidence in the effectiveness of their brokers' operations. In 1968 U.S. brok-

ers handled three billion shares for their customers, many of them for amateur investors who have never seen the men who buy and sell stocks for them, and have never handled the certificates held at the brokerage house in their name. A sense of what the audit means to such a person is reflected in a short note, dated several years ago, which Harold V. Petrillo, New York partner, keeps in his desk drawer. It reads:

"Messrs. Haskins & Sells: Although you are being reimbursed for your services in connection with the enclosed audit, let me thank you personally for all the hard work which such an audit must entail. It brings an extra measure of peace of mind to the small investor. Thank you again. (signed)"

Rule 418, officially titled "Surprise Audits," is a regulation of the New York Stock Exchange. The Exchange is advised of the third of the year in which the audit is to be conducted; however, the exact date remains the accounting

firm's secret, and a well-kept one. Although the sudden, unannounced appearance of auditors sometimes causes temporary inconvenience—longer hours for client employees, disruption of physical facilities—the client brokerage house derives some benefit from the surprise. Because the broker is not expecting an audit, the H&S team sees it at a routine moment, and not in a specially prepared pose. The auditors come in at the end of a normal Stock Exchange trading day and observe the remainder of the back-office work day. In the event of a possible shortage of securities, the surprise factor is important in detecting it. Another benefit for the client, as Ed Lill, New York partner, puts it, is that the audit "gives the brokerage house a 'fix' on its operational and financial position as of a particular date, which it could normally not accomplish with its own staff."

As the market has grown, so have the complexities within brokerage houses. Some firms have merged and diversified. For example, Merrill Lynch, Pierce, Fenner & Smith, Inc.—the largest in the world—has expanded into many financial offshoots, including real estate financing, investment advisory service and major Canadian underwriting. Auditing such varied activities requires sharp, dexterous accountants and gives them a chance to gain broad experience in new areas of business and finance. In a sense, they are privileged to a look inside the workings of the New York financial and commercial power center that few are given. From brokerage house auditing they can gain an understanding, a perspective, of the world of finance that few obtain in years elsewhere.

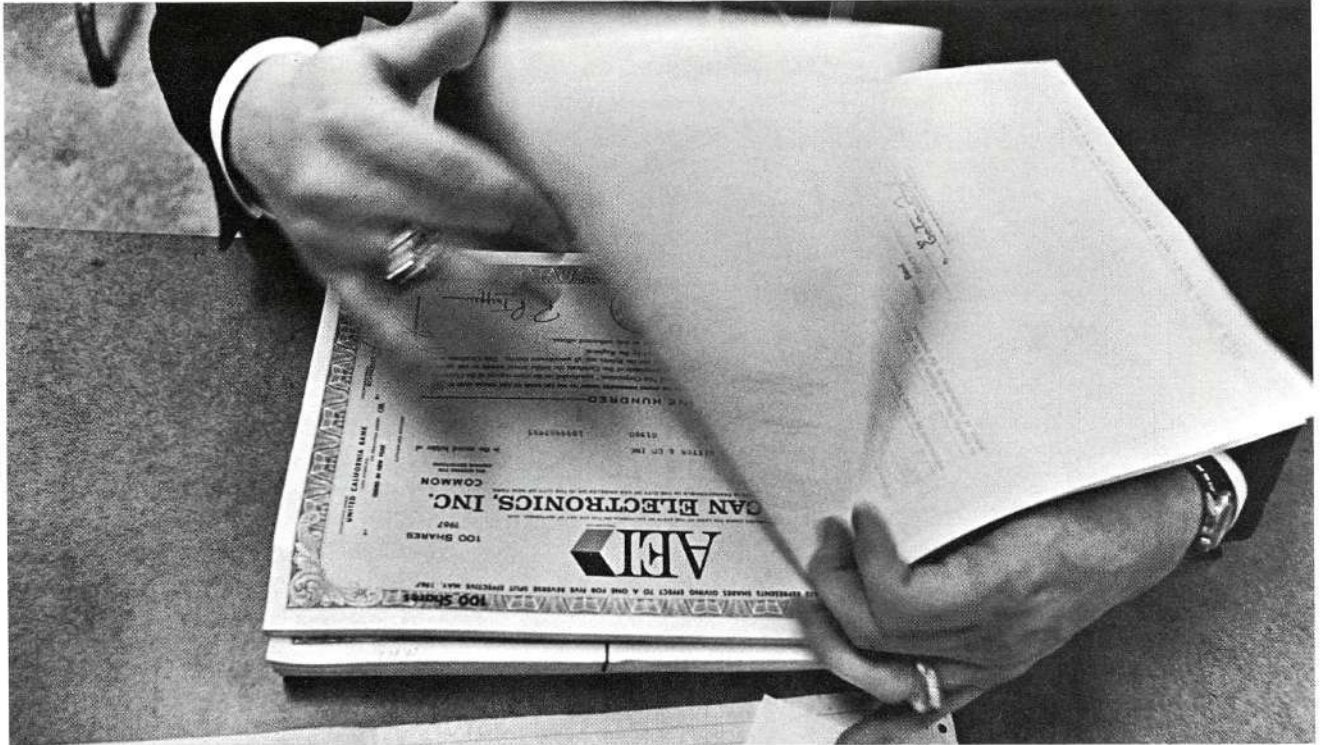
For the accountants, the surprise audit is often the result of many weeks, even months, of planning. In preparation for the audit they carefully review previous work papers, consider new

activities undertaken by the client, and outline operational strategies. On a large job H&S may fly in accountants from other offices, some as far away from New York as the Pacific Coast.

Starting out on his first brokerage house assignment, a typical H&S accountant inspects thousands of stock and bond certificates. This part of the job demands speed and accuracy, because securities enroute to another brokerage firm can be held only a short time. Counting itself is not exciting. But from this basic part of the job a young accountant can learn, as he advances from one function to another, how the pieces of brokerage house

work fit together to make the big picture. When he is thoroughly familiar with the audit he is an extremely valuable professional whose skills are vitally needed by the Firm.

One reward for conscientious service and meticulous attention to detail can be advancement to supervision of a particular section of the audit. In fact, brokerage house auditing offers the young accountant one of the best opportunities to get administrative experience. This is clearly illustrated by the fact that more than 50 separate operations must be performed within a 45-day period. To accomplish this on some of our engagements more than



"Recount!" Waving a paper, an H&S auditor signals a brokerage supervisor to verify his count. Here in the New York office of Dean Witter & Co., he counts both stocks and bonds, checks his figures with those recorded by the client on punch cards. If there is a difference, a recount is in order.

Opposite page:  
From "Babylon (New York) to Button Willow (California)," municipal bonds are the base of the building boom. At Dean Witter & Co., Gustave Steenstra, assistant vice president, checks over bonds the firm files under the town name.



100 accountants are needed. The supervising accountants must have administrative talent to organize, plan, delegate and supervise the work in a way that successfully completes it accurately and on time.

Accountants working in supervisory capacities on brokerage engagements find the work extremely challenging in that many administrative and technical decisions must be made quickly.

Haskins & Sells has been a leader in brokerage house auditing for 50 years, since the day when Thomas N. Willins, a New York partner, set out to build up this part of the H&S practice. Inspired by Managing Partner Arthur H.

Carter, Mr. Willins became the spark plug of a team of financial district specialists who developed our Firm's eminence in brokerage house auditing, work which has the advantage of being scheduled mainly in the summer months after the peak of the busy season elsewhere.

Today H&S is by far the largest auditor of brokerage houses. Our Firm audits about 100 such clients nationally and internationally. More than 800 of our staff people work on brokerage engagements at some time during the year. In connection with the Merrill Lynch audit alone, more than 500 H&S accountants were used and 1.5 million

requests for confirmations of customers' statements were mailed. The New York Office audits 80 brokerage clients with 27 other domestic offices and three Canadian offices joining in the work. Of those, Los Angeles, San Francisco, Chicago, Boston and Atlanta are the most active. These and smaller offices lend accountants where needed, and New York Office accountants sometimes serve as consultants on audits in other cities. In addition to those brokers served by the New York Office, we serve such large firms as Courts & Co. (Atlanta), Dean Witter & Co., Inc. (San Francisco) and F. S. Moseley & Co. (Boston). Through our DPH&S offices we are deeply involved in foreign operations of U.S. and non-U.S. broker clients, with the result that the expertise of our people in international brokerage house work is unsurpassed.

The enormous burden of paperwork in brokerage houses lately has been caused not only by the escalating number of transactions but also by the pressure to move securities quickly. But new operating methods for brokers, designed to break the paperwork jam, are under study or in experimental use. One is the New York Stock Exchange Central Certificate Service (CCS), which holds securities for the brokerage firm and automatically records all debits and credits as the concerns transact business. This system should reduce hand-to-hand movement of securities between and within brokerage firms.

Other paperjam-breaking and mistake-eliminating methods are being examined carefully. The Committee on Uniform Security Identification Procedures (CUSIP) has developed standardized code numbers that should simplify securities identification. Multi-sized certificates may be replaced one day by punch cards, or may be made in a form suitable for optical scanning. Or we may shift to a "certificate-less society," whereby a customer's account with his broker could be credited and debited much like a bank account.

Whatever technical steps are taken to assist and speed the work in back-offices of brokerage houses, Haskins & Sells will continue to need skillful, persistent accountants to carry out the audit. For our Firm the challenge is great, and will become greater. We are continually training an increasing number of imaginative and alert men and women to take part in this team effort, carried out in the public interest, which is essential to the smooth operation of the greatest, most active marketplace in the world. □

