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Aids to Management of Stock-brokers' Offices

By J. PRYSE GOODWIN

An advocate of improvement in business methods cannot but be impressed with the comparatively slow introduction of scientific management into stock-brokers' offices compared with the great strides that have been made in this direction in industrial fields.

The large expansion in business brought about by the war necessitated improved methods of accounting and reporting, making it possible to handle expanded turnovers on disproportionate capital with the result that leading industrial organizations have had to take a keen and active interest in improved business methods affecting the hiring and directing of labor, purchasing of materials, methods of manufacture, methods of selling and methods of accounting. The functions of the modern controller's office have been perhaps a development of particular prominence during that period of trade expansion, enabling concerns through the maintenance of better records and improved statistics to secure closer alignment of purchases to inventories, of inventories to manufacturing requirements and of manufacturing programmes to unfilled orders and sales campaigns.

During the same period there has been a large expansion of capital, new organizations have been formed and stock underwritings floated. While it has been the practice of financiers to demand of industrials in conjunction with flotation of securities, balance-sheets, profit-and-loss accounts, earning statements, manufacturing costs and other statistics in great detail and drawn up in the most scientific form, it is doubted whether bankers and brokers themselves have profited by this experience and whether they have shown the same marked improvement in their own methods of internal management and accounting as has been going on in industrial fields.

Surveys of operating methods by industrial engineers and independent audits of accounts of stock-brokers' offices appear still to be sporadic rather than periodical, and as for the preparation of monthly comparative balance-sheets reflecting fluctuations in assets and liabilities and of earnings statements drawn up

scientifically to show comparative costs and operating results by departments, the brokerage offices that have developed their accounting systems to this point of perfection would appear to be limited to the leading firms.

In a business surrounded by great hazards, periodical and independent audits, protective systems of control and the preparation of statements and reports such as are prepared by controllers' offices in commercial concerns, would appear to be essential for the protection of customers, their employees and the brokers themselves, and to the lack of such safeguards can be attributed in some measure many defalcations and some failures.

On the other hand, surveys made for the development of scientific accounting and scientific management can be expected to and have induced some large firms to improve and change their operating methods to meet changes in conditions that are taking place in this transition period, while independent audits have the natural result of improving relations with bankers and inspiring customers' confidence, all of which assist in brokerage business development.

These comments must not be considered as reflecting on business integrity for it is doubted whether there be any calling in which so high a standard of business honor and business ethics is exercised as that among members of the New York Stock Exchange. Improved methods of accounting and reporting and independent audits, however, recommend themselves as matters of ordinary business prudence, especially where the liability is individual and personal.

While bookkeeping systems of stock-brokers' offices are generally good, there appears to be lacking in most offices a set of reports scientifically drawn to reflect the physical condition of the business at any given time and also the operating progress from month to month.

To furnish the information desired by executives, namely, the partners, the writer recommends as a result of his experience, the following monthly reports, viz.:

- Exhibit (a) Comparative balance-sheet
- Exhibit (b) Comparative statement of commissions
- Exhibit (c) Comparative profit-and-loss account
- Exhibit (d) Comparative statement of investments

Referring to these in order :

Comparative Balance-sheet (Exhibit A)

The comparative balance-sheet is furnished with analytical columns to show the book value of the assets and liabilities at the end of the current and of the previous month and the changes that have taken place therein during the month. Reference to this exhibit will show that both the assets and liabilities have been grouped according to their liquid condition, enabling a ready comparison to be made of the finances of the firm from a liquidation standpoint. Comparison of the figures relating to assets shows how the firm's own and its borrowed capital is invested in bank balances, accounts receivable, including customers' debit balances and investments; and comparison of these figures in relation to one another and to those of the previous month shows what changes have been effected during the period. In an era either of inflation or of deflation these comparative figures indicate relative progress made in either direction, which is invaluable information to brokerage executives.

In the lower section of the statement is shown the firm's liabilities grouped according to accounts payable, including customers' credit balances, loans, and partners' capital, and the same relative comparison of these figures with those of the previous month showing the increases and decreases are, in periods of inflation or deflation, of importance to the partners' furnishing a guide to executive policy such as the desirability of adjusting margins or interest rates charged on customers' accounts.

The important subject of equities is not introduced into this monthly balance-sheet to avoid delay in preparation, the pricing and extending of collateral involving a large amount of detail work. Equities on investments are shown in the separate schedule dealing with that subject and it is the writer's experience that margins on customers' accounts, equities on loans and the box count can be handled better on separate reports. Ascertainment of margins against customers' debit balances is, of course, a matter of daily and perhaps hourly necessity and a statement of accounts below margin requirements should at all times be before the executives.

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Exhibit A

| At | COMPARATIVE BALANCE-SHEET and previous month | | | |
|-----------------------|---|-------|-------------------|----------------------------|
| ASSETS | Current month DETAIL | TOTAL | Previous month | Increase decrease (Red) |
| Cash at banks | ..... |  | ..... | ..... |
| Cash & stamps on hand | ..... |  | ..... | ..... |
| Total |  | ..... | ..... | ..... |
| Accounts receivable | | | | |
| Customers' accounts | ..... |  | ..... | ..... |
| Employees' accounts | ..... |  | ..... | ..... |
| Partners' accounts | ..... |  | ..... | ..... |
| Failures to deliver | ..... |  | ..... | ..... |
| Less reserve | (Red) | | (Red) | (Red) |
| Total |  | ..... | ..... | ..... |
| Stocks borrowed |  | ..... | ..... | ..... |
| Investments long |  | ..... | ..... | ..... |
| Deferred charges |  | ..... | ..... | ..... |
| Total assets |  | ..... | ..... | ..... |
| LIABILITIES | | | | |
| Accounts payable | | | | |
| Customers' accounts | ..... |  | ..... | ..... |
| Employees' accounts | ..... |  | ..... | ..... |
| Partners' accounts | ..... |  | ..... | ..... |
| Failures to receive | ..... |  | ..... | ..... |
| Total |  | ..... | ..... | ..... |
| Investments short |  | ..... | ..... | ..... |
| Stocks loaned |  | ..... | ..... | ..... |
| Loans on collateral |  | ..... | ..... | ..... |
| Dividend accounts |  | ..... | ..... | ..... |
| Total liabilities |  | ..... | ..... | ..... |
| Partners' capital |  | ..... | ..... | ..... |
| Profits to date |  | ..... | ..... | ..... |
| Total |  | ..... | ..... | ..... |

Comparative Statement of Commissions (Exhibit B)

The comparative statement of commissions shows in comparative form for the period of the year to date and for the corresponding period of the previous year the total volume of shares dealt in on the stock exchanges and the relative increase or decrease—also the corresponding figures of commissions earned by the various offices of the brokerage house. The business being one subject to wide fluctuations, comparisons made between commissions earned in one year and another do not furnish relative guides as to the operating ability of the organization. If, however, the fluctuations in the volume of commissions earned in

each office be compared with the fluctuations in volume of shares dealt in on the local exchange, a comparison of percentages of increase or decrease will show to partners whether or not their organization is maintaining its relative position with their competitors, the value of which information needs no argument.

Exhibit B

| COMPARATIVE STATEMENT OF COMMISSIONS | | | | |
|--------------------------------------|------------------------|-------------------------|-------------------------|-----------------------|
| For | months ended | | | |
| SOURCE | Current yr. to date | Previous yr. to date | Increase decr. (Red) | % on prev. year |
| Shares New York stock exchange | | | | .. |
| Shares Chicago exchange | | | | .. |
| Shares Cincinnati exchange | | | | .. |
| | | | | |
| <i>Correspondents</i> | | | | |
| 1. | | | | .. |
| 2. | | | | .. |
| 3. | | | | .. |
| 4. | | | | .. |
| | | | | |
| Total correspondents | | | | .. |
| | | | | |
| <i>Branch offices</i> | | | | |
| 1. | | | | .. |
| 2. | | | | .. |
| 3. | | | | .. |
| | | | | |
| Total branch offices | | | | .. |
| | | | | |
| <i>Head office</i> | | | | |
| New York commissions | | | | .. |
| Chicago commissions | | | | .. |
| Cincinnati commissions | | | | .. |
| | | | | |
| Total head office | | | | .. |
| | | | | |
| Grand total | | | | .. |
| | | | | |

Comparative Profit-and-Loss Account (Exhibit C)

The comparative profit-and-loss account shows in columnar form comparative income, expenditure and profits for the expired months of the year to date compared with the corresponding period of the previous year, the increase or decrease and the percentage thereof.

The income, in this statement, is divided according to departments, and against each department's earnings are charged those expenses which are peculiar to the department, thereby enabling department profits and the percentage of same compared to department gross income to be determined by departments. Com-

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parison of these percentages showing how much of the earnings of each department is conserved and represents department profit is found to be invaluable to executives, drawing attention to opportunities for increasing departmental earnings or reducing department costs, just as is indicated by controllers' reports, and is done in industrial fields.

Referring to the lower half of the statement—expenses have been classified according to those which are normal and general to all departments, namely, office salaries and expenses, and those which are of a fluctuating or miscellaneous nature classified as miscellaneous expenses.

By use of the same classification of both income and expenditure from month to month and year to year relative percentages of profits and expenses indicate opportunities for increasing earnings and reducing operating costs, according to changes in fundamental conditions.

Exhibit C

| COMPARATIVE PROFIT AND LOSS ACCOUNT | | | | | | |
|-------------------------------------|--------------|---------------|-------|----------------------|---|------------|
| For | months ended | | 19 | and 19 | | |
| INCOME | DETAIL | 1921 TOTAL | 1920 | Increase decrease | % | on 1920 |
| <i>Stock department</i> | | | | | | |
| Commissions | | | | | | .. |
| Less salaries and expenses | | | | | | .. |
| Profit | | | | | | .. |
| % on income | | .. | .. | .. | | |
| <i>Investment department</i> | | | | | | |
| Profits less losses | | | | | | .. |
| Less salaries and expenses | | | | | | .. |
| Profit | | | | | | .. |
| % on income | | .. | .. | .. | | |
| <i>Trading department</i> | | | | | | |
| Profits less losses | | | | | | .. |
| Less salaries and expenses | | | | | | .. |
| Profit | | | | | | .. |
| % on income | | .. | .. | .. | | |
| <i>Interest</i> | | | | | | |
| Income | | | | | | .. |
| Expenditure | | | | | | .. |
| Profit | | | | | | .. |
| % of income | | .. | .. | .. | | |
| Total department profits | | | | | | .. |

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| For | months ended | | 19 | and 19 | |
|-------------------------------------|--------------|-------|-------|----------------------|--------------|
| EXPENDITURE | DETAIL | TOTAL | 1920 | Increase decrease | % on 1920 |
| <i>Office salaries and expenses</i> | | | | | |
| Salaries | | | | | |
| Rent | | | | | |
| Postage | | | | | |
| Stationery | | | | | |
| | | | | | |
| | | | | | |
| | | | | | |
| Total | | | | | .. |
| <i>Miscellaneous expenses</i> | | | | | |
| Advertising | | | | | |
| Donations | | | | | |
| Auditing | | | | | |
| Legal | | | | | |
| | | | | | |
| | | | | | |
| | | | | | |
| Total | | | | | .. |
| Total expenses | | | | | .. |
| Net profit to date | | | | | .. |
| Deduct partners' salaries | | | | | .. |
| Balance undivided profit to date | | | | | .. |

Comparative Statement of Investments (Exhibit D)

The comparative statement of investments contains a complete list of the firm's investments showing in comparative form their book and market value and the book profit or loss on each.

In the last few years there has been a tendency on the part of stock-brokers to expand into the investment or bond field, and while the methods and principles of doing business differ materially from those of the commission business, this has perhaps not been thoroughly appreciated by some of the houses which have ventured into it until they have come to take inventory of their investments. These inventories perhaps have disclosed securities remaining unsold for long periods and carried at unprofitable rates of interest from which the market has been allowed to slip away, allowing the securities to be marketed only at a loss. The comparative statement of investments is intended to keep partners informed from month to month and at more frequent intervals, if required, how and to what extent the capital of the

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firm is being absorbed in the investment department and the condition of those investments compared with their current market value and present financial outlook. All this is found to tend to increase turnover and disclose losses before opportunities for cutting them have expired.

Exhibit D

COMPARATIVE STATEMENT OF INVESTMENTS AT ———

| Shares | Security | Book | | Market | | Book | |
|--------|----------|-------|--------|--------|--------|--------|-------|
| | | Price | Amount | Price | Amount | Profit | Loss |
| | | | | | | | |
| | | | | | | | |
| | | | | | | | |
| | | | | | | | |

There are, of course, many other forms of reports and statistics of aid to partners and executives in this business and those submitted are subject to amplification and modification to meet special conditions, but they are intended to be illustrative only of general principles and fundamentals and to arouse interest in the subject with a view to improvement in business methods of stock-brokers' offices for the benefit of themselves, their customers and their employees.