A MOCPA and Missouri Municipal League Special Report

Municipal Audit Scarcity Impact Factors

By Mary J. Sprung, CPA and Martin Ghafoori

It is well-known that today's business environment is marked by a fierce competition for talent across various sectors. Talent scarcity has notably impacted numerous industries, as highlighted by a June 2024 U.S. Chamber of Commerce report.[1] This report identifies manufacturing, financial activities, and professional and business services as the top three sectors facing labor shortages by industry. Leaders seeking to navigate this complex landscape must focus on both macro and industry-specific trends, data, and insights to address and resolve some of the most pressing challenges within the national human capital drought. Within the accounting sector, leaders have been grappling with strategies to resolve a range of talent pipeline issues. Those interested in the drivers behind these efforts can explore findings from organizations like AICPA, NASBA, NPAG, AAA, individual state CPA societies, CAQ, and other professional associations. While too numerous to cite in this whitepaper, collectively these entities are working to devise strategies that address both immediate and long-term human capital challenges.

To be clear, these efforts, writ large, attempt to solve for the *accounting profession* human capital conundrum. Simmering just under the surface of all of these wonderful efforts exists a nuanced set of pain points that are *specific to CPAs, CPA firms, and the clients* that those licensed professionals serve. While the two sets of considerations are adjacent, is to the detriment of this profession to lump them together. The trap is believing that if the profession makes strides to address human capital challenges for all, that is a proxy for solving for a dearth of CPAs. This is the "all boats rise with the tide" theory. While it is certainly true that attracting more talent to the broader accounting profession will likely pull more professionals through to become CPAs, the ratio is not 1:1. Today at best, we are aiming in dozens of different directions—"spaghetti at a wall" set of solutions. At worst, we may be rowing in opposite directions. At the end of the day, why might you (meaning the general public) care? The answer to "why" lands at the core legal privilege of CPAs and CPA firms: *the audit*. While the world focuses on solving for accounting profession challenges, audit-specific issues face unique considerations that need additional (and different) advocacy, attention, and understanding.

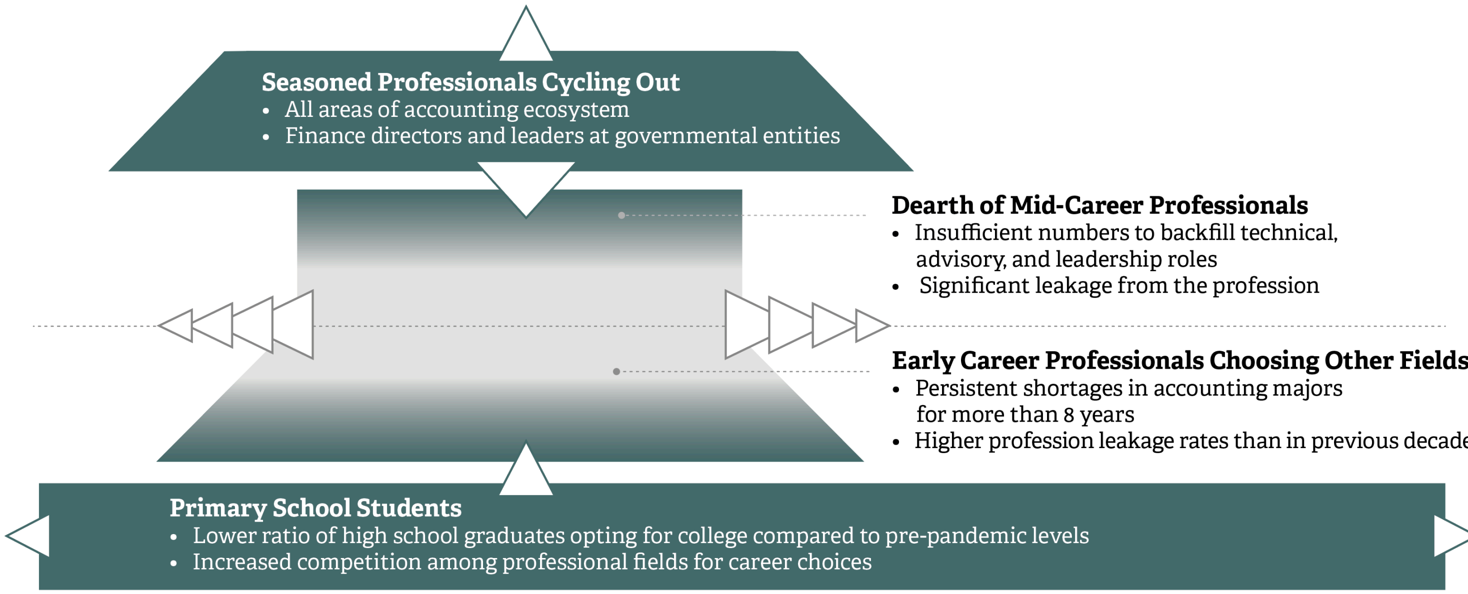
Very specifically for this whitepaper, CPAs and CPA firms—audits—require unique solutions to overcome the specific challenges faced by governmental auditors and smaller governmental entities. These entities encounter distinct issues that significantly impact the broader *accounting ecosystem*. This white paper attempts to shine a spotlight on governmental auditors and (especially) small and medium-sized governmental entities—both facing unique challenges that disproportionately negatively impact their portion of the accounting ecosystem. While many stakeholders participate in the accounting ecosystem, this discussion focuses on three specific areas: 1) CPAs and CPA firms, 2) governmental entities, and 3) the general public. This essay attempts to shine a light on why we must solve for *both* 1) accounting and 2) CPA-specific human capital challenges for today and decades that follow.

Narrowing Profession Impact Factors to Governmental Auditors

Before addressing specific considerations around the governmental audit scarcity discussion, it is important to briefly acknowledge broader challenges facing the profession. Our profession regularly interacts with a variety of organizations, businesses, and partners that collectively contribute to the *"Accounting Ecosystem."* This ecosystem is a concept that has been in existence for decades, yet we often are so focused on the activities in our own area of the pond it is easy to lose sight of other component parts. While every accounting ecosystem is constructed and supported by similar components, there is a wide variance for how well these parts function together across and among jurisdictions. The overall health and wellness for the profession can be impacted by various areas of an ecosystem, both positively and adversely. Why is this concept meaningful for consideration and discussion? It helps us locate exactly where this portion of the discussion rests, helping to shape the very fabric of how the profession operates.

To best understand downward pressures specific to the governmental accounting and auditing ecosystem, it is essential to acknowledge several well-documented meta-profession considerations.[2] "Population demographics" is a significant factor contributing to the human capital challenges faced today. Professionals are exiting all areas of the human capital pipeline, and in broad terms, creating several leakage points as illustrated in Figure 1. All the aforementioned entities are working hard to address behavior-based challenges, but age-stage cohort numbers and career stage cycles are unavoidable. In summary, every profession must exert more effort than in the past to maintain or expand their human capital share for the near future. These considerations highlight the present truths and future opportunities for positive impacts on all stakeholder groups.

Figure 1: Accounting Profession Human Capital Leakage



(**Source:** Adapted from "Accounting Talent Strategy Report" National Pipeline Advisory Group. July 2024.)

CPAs and CPA Firms: Where Are All the Auditors?

In today's business environment, if you were to ask 100 professionals what comes to mind when they hear "CPA," you might get 100 different answers. This exaggeration underscores the wide range of roles CPAs fulfill, such as tax professionals, business advisors, CFOs, owners, auditors, business valuation specialists, financial planning experts, supply chain managers, and controllers. While these are impressive roles for CPAs to play, it raises the question: "Why CPAs?"

It's often overlooked that the fundamental reason CPAs enjoy widespread respect and trust is their regulatory status. Observing a list of regulated professions like doctors, lawyers, CPAs, and...professional wrestlers might elicit amusement. However, these professions share a common attribute: legal privilege granted through regulation. To be clear, we are not talking about privilege like the attorney-client privilege we see in the movies. For CPAs, the rules are quite specific, and here in Missouri statute:[3]

> "Only [licensed CPAs] may issue a report on financial statements of any person, firm, organization, or governmental unit, or offer to render or render any attest service."

This may sound like a narrow scope, but it has significant business implications. The authority granted to auditors at CPA firms and state auditor offices supports business deals, financial markets, governmental operations, philanthropy, and most importantly: public trust. Over the years, this trust and respect have earned CPAs "trusted business advisor" status.

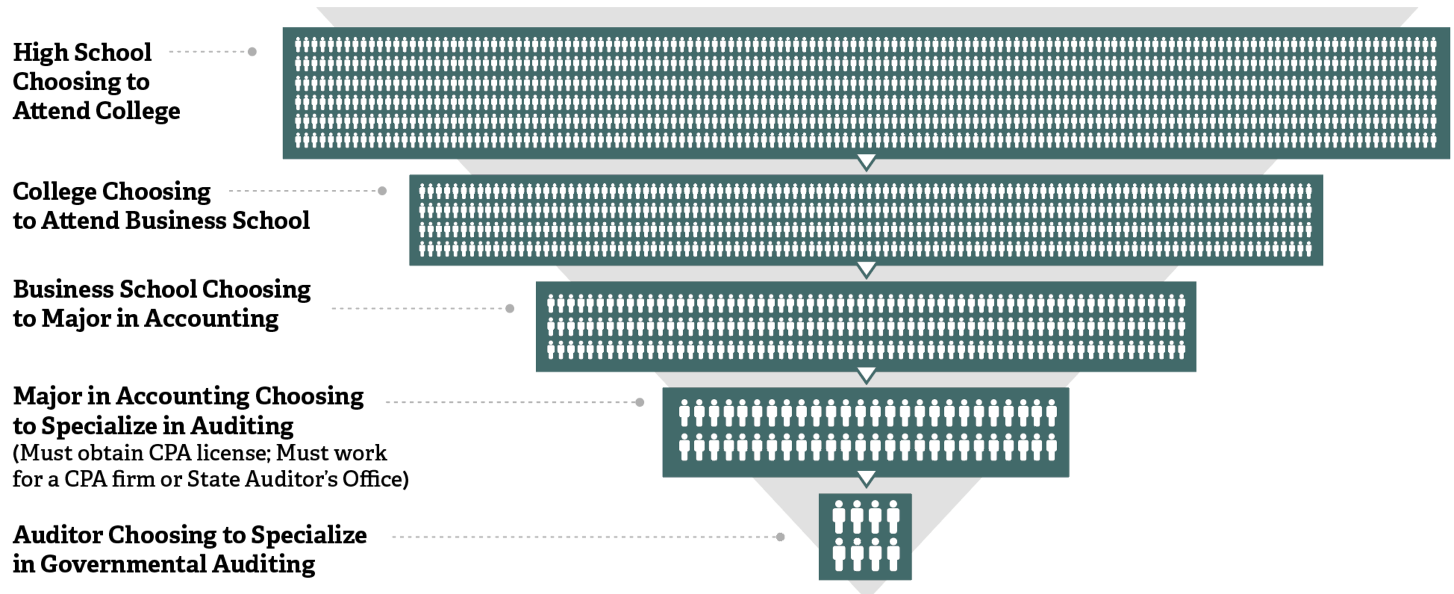
The role of CPAs has evolved over time. The term "business advisor" now includes much more than the traditional responsibilities. The reality is that auditing and consulting are two sides of the same coin. CPAs with technical auditing or accounting expertise often become advisors for a variety of business functions. However, over time, there has been a shift in the value placed on technical consultative services versus compliance-based services. The shift is not the fault of the practitioners; it is just how the industry has evolved. CPA firms have expanded their service offerings, driven by the lucrative nature of consulting, especially since the Sarbanes-Oxley Act. As more CPAs have moved into advisory roles, fewer are left to perform core audit and attest services.

This means that while "traditional" CPA activities like tax, audit, and bookkeeping are still important, growth is happening in advisory services. This has created a push-pull dynamic: the demand for advisory expertise has outpaced the supply, stretching human capital thin. Efforts to bridge this gap through technology, offshoring, M&A activities, and hiring non-accounting professionals have not kept up with broad market demands.

Where Are All of the Governmental Auditors?

If the sobering reality of shrinking audit talent isn't enough, consider that there is a subgroup of specialized audit professionals with the skills to perform governmental audits. The pressures on CPA firms only scratch the surface of why there are fewer governmental auditors than ever before. Unlike other types of audits, governmental audits must adhere to Generally Accepted Auditing Standards (GAAS) requiring additional specialized annual training. In addition, many governments must also adhere to Generally Accepted Government Auditing Standards (GAGAS), commonly known as "Yellow Book" standards if they receive government grants and awards. This further narrows the field of qualified auditors for governmental audit engagements. Considering the entirety of demographic realities, profession-related challenges, and specialization requirements to perform a Yellow Book audit, one can see how this specialization scarcity has evolved. Figure 2 illustrates the various points where human capital leakage occurs, leading to fewer governmental auditors today. →

Figure 2: Pathways to Exit Becoming a Governmental Auditor



We also see how thinly CPAs with governmental auditing experience are stretched through the Peer Review process. Peer Review is the audit profession's self-regulation mechanism. It is a mandatory program for all CPA firms that perform attest engagements in which CPAs review the attest work of other CPAs against certain Peer Review quality standards. When a firm performs governmental audits, the peer reviewer engaged by the firm is required to have certain relevant experience in order to perform the peer review. In recent years, it has become more and more difficult to find CPAs with that required experience and the availability to perform the peer review of these entities. MOCPA administers the Peer Review Program for the state and notes that only *eight* CPAs (out of nearly 12,000 licensed in Missouri) are qualified to perform peer reviews for these governmental entities. The demanding workload for those with this experience, as well as the additional required training, make it difficult to attract new CPAs to this niche practice area.

Impact on Governmental Entities

This white paper has outlined a complex set of challenges facing the accounting profession today, especially for CPA firms, auditors, and those specializing in governmental auditing. This is not a sudden issue; it is the result of years of trends, compounded by many experienced professionals retiring. While many companies might not feel the direct impact of these forces, governmental entities like municipalities, school districts, fire districts, public utilities, certain HUD entities, and others certainly do. It is also worth mentioning that similar issues affect nonprofit entities regarding audit scarcity, but this white paper does not dive into that topic.

Non-federal government entities receiving more than $750,000 in federal grants during a fiscal year must file a Single Audit report. This requirement represents a 10,000-foot view of governmental audit requirements, and readers should research their entities' specific requirements for financial reporting. The key point here is that many governmental entities must undergo an audit. Large governmental entities are familiar with annual audits, but medium and small entities might not be as prepared. They may struggle with understanding audit processes, finding qualified CPA firms, and preparing for an audit, especially with the influx of federal pandemic aid programs (like the CARES Act, ARPA, ESSER). Many of these smaller entities, needing an audit for the first time, may find the process more time-consuming and costly than anticipated. As a result, CPA firms and professional advocacy organizations have fielded an uptick in inquiries seeking help in this area.

While not all governmental entities operate the same way, there are often similar principles that impact how CPA firms with governmental auditing expertise work with governmental leadership teams. If you are a government leader working with a CPA firm for your audit, consider the following principles on an annual basis.

Principle 1: Elected Officials and Staff Working Relationships

Government entities usually have a mix of elected officials and staff, which creates unique interactions, especially with term limits. It can be tough to keep things running smoothly as elected leaders come and go. Policies, priorities, resources, and focus can change with elections, but the financial operations need to remain solid. Many governmental entities rely heavily on the expertise of financial staff and consultants to keep finances healthy and ensure compliance with financial regulations. Like any organization, strong partnerships between staff and elected officials are crucial. When these relationships are not aligned, financial reporting can suffer, leading to longer and more complicated audits.

Principle 2: Compliance Requirements

Every year, the AICPA and other profession-related publishers survey and highlight the biggest challenges in the CPA world.[4] Attracting and retaining talent is always at the top, but another major issue is keeping up with regulatory complexity. For CFOs, finance directors, and accounting professionals in government, staying on top of annual regulatory changes is critical. CPAs need to satisfy mandatory continuing professional education (CPE) requirements, annually, to stay updated. Understanding and applying Governmental Accounting Standards Board (GASB) financial reporting requirements start with in-house expertise and finish with the audit team. With the current scarcity of expertise on both sides, it is becoming harder for governmental entities to attract and retain the necessary talent.

Principle 3: Full Audit Means Full Audit
Leadership looking for audit expertise, especially in this specific area, may not fully understand the different assurance services. One may hear something like, "Our operating financials are only $XYZ; we need an audit, but it should be easy and quick." This usually means one is hoping for an inexpensive option. However, audit standards do not care about the complexity of one's finances; the same procedures apply to all audits. There have been calls for "light audit" standards over the years, but not many know about the Other Comprehensive Basis of Accounting (OCBOA) financial statement frameworks, like the AICPA's Financial Reporting Framework for Small and Medium-Sized Entities (FRF for SMEs). The reality is, GASB audits are the norm and are often legally required for governmental entities.

Principle 4: Typical Government Bidding Process Requirements
Many government services contracts often go to the lowest bidder. While this may seem fair, over time it has driven CPAs and CPA firms away from these specific client offerings toward more lucrative work. As a result, numerous government entities struggle to find CPA firms that have both the capacity and willingness to take on new clients. Certain state laws require government audits to be conducted by local CPA firms, further limiting options. For example, in early 2024, a report out of Wyoming indicates that only two CPA firms in the entire state had the talent and bandwidth to manage a government audit.[5]

Principle 5: Credit Rating and Bond Issuance Challenges
Municipalities and special districts typically are required to post certain financial and operating data to the Municipal Security Rulemaking Board's (MSRB) portal for all things municipal securities on the EMMA website (*www.emma.msrb.org*). Oftentimes, this is completed by a third party under contract to assist the municipal entity. These filings include submitting a completed audit, as well as other operating data that has been agreed to in the bond documents that also govern the timing of submittal to the portal, as well as the list of topics to be shared on an annual basis. This one-stop-shop for disclosure items allows for investors to have the opportunity to make an educated decision as to whether they would like to hold, sell, or buy municipal bonds. If continuous filings were not required, or completed, the information available to bondholders would be stale—as of the date of the Official Statement (the prospectus for municipal securities). With bond issues outstanding for upwards of 30 years, transparency would be lacking.

Municipal bonds are oftentimes rated by a third-party agency—i.e. Standard & Poor's (S&P), Moody's Investor Services (Moody's) or Fitch Ratings (Fitch), to name the three largest—that examines the credit quality of each series of bonds and completes a rating call with the issuer to determine where the rating should land, based on local economic information, financials and the management of the issuer (policies and procedures). The ratings are then surveilled while the municipal securities are outstanding, and rating actions can be taken by the rating agency if the local economy, finances, or management declines, or improves, while the securities remain outstanding. If the timing of the audits and operating data is not aligned with the continuing disclosure requirements that have been laid out in the bond documents, this can be problematic.

Many issuers across the country have run into problems with timely audit filings, which can result in withdrawn ratings. In March 2023, S&P placed 149 municipal ratings on negative watch because of these delays in filing the financial and operating information. S&P was not able to conduct their surveillance for those municipal entities because the requested data was simply not available. Audit delays have increased over the past few years due to the lack of available CPAs and the increased reporting requirements dictated by GASB.

The remedy for late reporting to the rating agency is simply the completion and submittal of the requested reports, followed up with a rating call to have the rating reinstated. To access the public credit markets, the financing team must have a reasonable basis that the issuer will be able to comply with the continuing disclosure requirements in the future, and that they are currently in compliance, or the public markets may not be a viable option.

Principle 6: State Auditor's Office (SAO)
The Missouri SAO is tasked with oversight of how tax dollars are spent and provides reports and recommendations to improve transparency and accountability, among many other responsibilities (including registering general obligation bonds, and reviewing tax rates to ensure compliance with state law). An integral part of this supervision is the requirement for certain municipal entities[7] and special taxing districts to submit financial reports, or audits if available, to the SAO on an annual basis, per state statute. Not abiding by the state statute can lead to large, unexpected expenditures—the SAO is allowed to levy fines for late submittal of documents, at a daily rate. The SAO can also be charged with completing a petition audit, where the taxing entity would be required to pay for all audit expenses, including the auditor salaries.[8] These can be quite costly and are completed at the request of one's constituents, often because of either perceived or actual malfeasance. This further emphasizes the importance of timely financial reporting so that fines are not accumulating over time, which are often not a part of the budget.

Conclusion and Calls to Action

Widening cracks exist in the foundation between governmental entities and CPA firm audit professionals, but what may seem like collateral damage might be the most important factor in this discussion: the general public. This perspective is easy to overlook, especially when dealing with immediate and short-term operational challenges in both areas of the profession. However, the bridge that connects both is their shared goal of serving and helping the general public. Holding and maintaining public trust is critical for a strong and thriving economy, and even broader society. The overall health and welfare of citizens are impacted by governmental leaders, departments, and agencies, all of which rely on accurate financial information and disclosures.

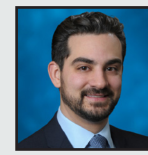
For the General Public: A decline in expertise, access, funding, and attention to governmental audit scarcity only weakens the financial stability of our society. To be clear, the governmental entities most at risk for audit delays or noncompliance are often small- and medium-sized ones, although none are immune. The services these entities provide and the citizens they support should not suffer due to audit noncompliance issues. Engage with your local governmental leaders and pay attention to annual financial reports and especially audit findings.

For Governmental Entity Leadership: Professionals in leadership roles should continue to engage in conversations, contributions, and collaborations with all parties involved. Keep in mind that at the end of the day, all the factors outlined in this white paper ultimately lead to continued annual audit fee increases in the future due to supply and demand. *In other words, you will almost certainly be paying more than in previous years* for your annual or single audit. Be proactive and discuss the implications of this article with your staff, board, and other stakeholder groups.

For CPA Firms and CPAs: There are some great opportunities to showcase your firm to municipal officials in Missouri. By getting involved with the Missouri Municipal League (MML) and the Missouri Government Finance Officers Association (MO GFOA), you can connect with key decision-makers and boost visibility. These groups offer fantastic platforms for networking and sharing your expertise with municipal professionals. Joining both organizations is a great way to show how your firm can benefit local governments. At MOCPA, consider collaborating with other CPAs in this space through MOCPA's Government and Not-for-Profit Community.

Mary J. Sprung, CPA, is the Finance Director for the City of Kirkwood and has been a CPA since 1999 and has over 25 years of experience specializing in governmental accounting.

sprungmj@kirkwoodmo.org



Martin Ghafoori is a managing director at Stifel in St. Louis. Martin provides investment banking services to municipalities of all types across Missouri.

ghafoorim@stifel.com

Disclaimer: This white paper is a joint publication between the Missouri Society of CPAs (MOCPA) and Missouri Municipal League (MML). It does not represent the official positions of MOCPA, MML, AICPA, GASB, or any other standard-setting body. This publication does not render legal, accounting, or other professional services. For specific advice or clarification, research the applicable statutes, rules, standards, or seek advice from appropriate governing or regulatory bodies. With respect to any information regarding municipal securities, such information is intended to consist of factual or general information that should not be construed as advice. Unless otherwise engaged, no entities or individuals involved in writing this article are serving, or seeking to serve, as financial advisor or municipal advisor.

Sources

1 Ferguson, S. "Understanding America's Labor Shortage." U.S. Chamber of Commerce. July 2024.

2 "Accounting Talent Strategy Report" National Pipeline Advisory Group. July 2024.

3 RSMo Chapter 326: Missouri Accountancy Act, §326.292 (1).

4 "2024 PCPS CPA Firm Top Issues Survey." AICPA. June 2024.

5 Beaudet, Joseph. "City, county audits delayed." *The Sheridan Press*. January 8, 2024.

6 Moran, Danielle. "Cities' Credit Ratings Are at Risk Because There Aren't Enough Accountants." *Bloomberg*. March 2023.

7 RSMo Chapter 67: County, Township, and Political Subdivision Government, §67.287 2(2).

8 https://auditor.mo.gov/petition-audits