

# **Bond Case Briefs**

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## **Muni Audit Reporting Times Worsened Over Last Decade.**

Municipal bond issuers took an average of 164 days from the close of their fiscal years to complete their comprehensive annual audits in 2020, up from 147 in 2009, a worsening trend that is beginning to affect issuers' credit ratings.

That's according to Merritt Research Service and the University of Illinois Chicago's Government Finance Research Center's new report comparing municipal bond issuers' audit times.

"In the interest of good governance and transparency and having adequate information to properly price these issues in the market, we felt that this is really important in terms of bringing attention to this issue," said Deborah Carroll, director of the Government Finance Research Center at the University of Illinois Chicago. "Unfortunately, the trend is going the wrong way."

Corporate bond issuers have median audit times of 60-90 days due to Securities and Exchange Commission requirements. Municipal bond issuers report audit times which are two to three times longer, averaging 140 to 160 days.

Late audits do weigh on ratings. S&P Global Ratings put New Orleans and 12 other local governments on a negative watch last week over failed filings.

"The withdrawal of the affected ratings could follow if we do not receive fiscal 2020 financial statements within 30 days," the agency said. "We consider the financial statements necessary to maintain and assess our ratings on these issuers. Accordingly, the ratings are now at risk of being withdrawn, preceded by any change to the rating we consider appropriate given available information."

If issuers provide their 2020 financial statements within 30 days, S&P said it would conduct a full review and take a rating action within 90 days of the negative watch action.

Both co-authors of the report stressed the timeliness of the report considering such recent actions by S&P.

"We think that's an appropriate action by the rating agencies and it's really needed from the marketplace itself in order to recognize that there's greater risk where there's not timely disclosure," said Rich Ciccarone, president of Merritt Research Services.

The report divides muni bond issuance into categories of revenue bonds, which includes hospitals and healthcare systems, community colleges, private higher education, public higher education, airports, retail electric, toll roads, water and sewer and wholesale electric. The report also includes government bonds, which are split up by cities, counties, dedicated tax, school districts and states and territories. All categories' audit times have increased in the period from 2009-2020.

The report cites community colleges as having the largest increase in median audit time, 24 days, but notes a potential cause in the significant growth in the number of issuers between 2009 and 2020, which increases the variation in audit completion times among individual issuers.

Issuers in the hospital and healthcare sector increased their median audit time by 10 days, water and sewer issuers by 9 days, and retail electric sector issuers increased by 8 days. Public higher education fared better, increasing a median of 1 day and toll road issuers increased by just 2 days in the period 2009-2020.

For what is designated governmental bond sectors, school districts increased their audit time by 22 days, counties increased by 16 days, the dedicated tax sector 11 days, cities by 10 days and states and territories worsened their audit time by 2 days.

But some audit times were affected significantly during the 2019-2020 period as a result of COVID-19, especially in the revenue bond category of health and higher education sectors.

"During this time, when staffs were short and people were becoming accustomed to remote work, we certainly expected audit times for all sectors to become slower," the report said.

But that isn't exactly how it turned out. Community colleges continued their lag in 2019-2020, worsening their median audit time by 13 days but issuers in public higher education increased their audit times by 5 days, followed by issuers of hospitals and healthcare systems which increased their reporting time by 4 days.

For government issuers during 2019-2020, issuers in the retail and wholesale electric and toll roads sectors maintain audit times that are considerably faster than all other sectors combined.

But states and territories are among the most affected by COVID-19, as the median audit time increased by 11 days between 2019 and 2020. The audit time for cities only increased by 2 days in the same time frame.

"Between 2019 and 2020 in most of the sectors, we do see an increase in audit times, as we would expect, because COVID-19 sort of screwed everything up for this time period," Carroll said. "But we're not seeing a huge increase in the timeliness of these audit completions."

But not all issuers wait years to complete their audits. The report also ranks the top 3 issuers in each category, as Port Authority of New York & New Jersey comes in first for airports, Sioux Falls, South Dakota comes in first for cities and Santa Barbara County, California wins for counties, all completing their audits in under 90 days.

"Generally speaking, that puts them very much on par with the private sector corporate bond issuers, which I think is a really great sign," Carroll said.

By Connor Hussey

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