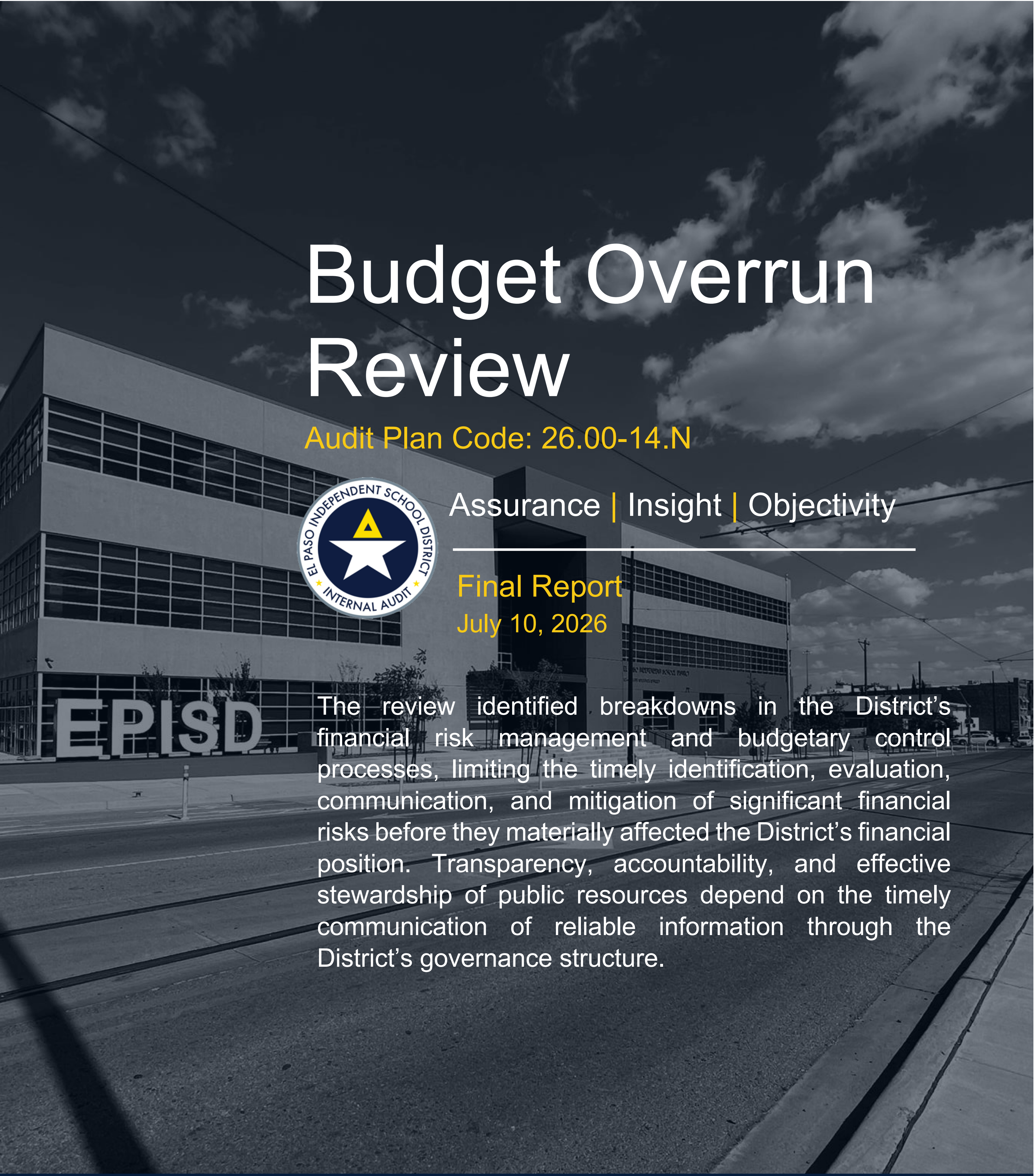

Budget Overrun Review

Audit Plan Code: 26.00-14.N

Assurance | Insight | Objectivity

Final Report

July 10, 2026

The review identified breakdowns in the District's financial risk management and budgetary control processes, limiting the timely identification, evaluation, communication, and mitigation of significant financial risks before they materially affected the District's financial position. Transparency, accountability, and effective stewardship of public resources depend on the timely communication of reliable information through the District's governance structure.

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Abbreviations

ABRs	Additional Budget Requests
BEFM	Budget & External Financial Management
CAP	Corrective Action Plan
CDHP	Consumer-Driven Health Plan
CFO	Chief Financial Officer
COSO	Committee of Sponsoring Organizations of the Treadway Commission
FTE	Full-time Equivalent
FY	Fiscal Year
HR	Human Resources
HSA	Health Savings Account
IDEA-B	Individuals with Disabilities Education Act, Part B
IIA	Institute of Internal Auditors
IST	Information Security & Technology
K	Thousand
M	Million
Policy CE	Annual Operating Budget
SPED	Special Education Department
TEA	Texas Education Agency
TEC	Texas Education Code
TRA	Teacher Retention Allotment

Executive Summary

ASSURANCE • INSIGHT • OBJECTIVITY

The following provides an overview of the results of Internal Audit's Budget Overrun Review, including key findings, expected outcomes, recommendations, and management's response.

WHAT WE FOUND

1. PRIMARY FACTORS CONTRIBUTING TO THE BUDGET OVERRUN

- FY2026 budget included a planned use of **$6M** fund balance
- **$10.3M** in unrealized savings and assumptions
- **$11.1M** in additional expenditures after adoption
- Budget did not fully reflect anticipated operating requirements
- **$21M** increase in General Fund costs

2. FINANCIAL RISK MANAGEMENT & REPORTING

- Significant financial risks were known within the District's financial management functions
- The cumulative impact was not communicated timely to the Superintement and Board
- Former CFO did not effectively fulfill key responsibilities
- Reduced transparency limited corrective action and public oversight

3. BUDGETARY CONTROLS

- Expenditures did not consistently remain within Board-approved appropriations
- Significant financial changes were not addressed through timely amendments
- **$30.7M** year-end budget amendment approved

14 RECOMMENDATIONS ISSUED

Designed to strengthen governance, financial oversight, accountability, transparency, and budgetary controls while improving decision-making and reinforcing public accountability.

WHAT WE RECOMMEND

1	FINANCIAL RISK MANAGEMENT, COMMUNICATION & ESCALATION	Strengthen processes for identifying, evaluating, monitoring, escalating, and communicating significant financial risks and their potential impact to District leadership and the Board, as appropriate.
2	FINANCIAL REPORTING & FORECASTING	Enhance financial reporting through meaningful trend analysis, financial forecasting, fund balance projections, and monitoring of significant budget assumptions.
3	BUDGET DEVELOPMENT & ACCOUNTABILITY	Establish accountability for significant budget assumptions and cost-saving initiatives through documented validation, approval, and ongoing monitoring processes.
4	BUDGET AMENDMENTS & FISCAL CONTROLS	Strengthen budget amendment processes to ensure significant expenditures, commitments, and financial impacts are timely incorporated into the Board-approved budget.
5	LONG-TERM FISCAL SUSTAINABILITY	Reduce and ultimately eliminate reliance on unsupported budgeted lapsed salary savings as a recurring budget-balancing strategy.

MANAGEMENT'S RESPONSE

Management and leadership agreed with the audit findings. District management and leadership submitted a Corrective Action Plan (CAP) outlining nine (9) activities to be implemented. All recommendations made by Internal Audit were incorporated into the CAP. The CAP appears to be sufficient to address the findings outlined in this report. Internal Audit will conduct follow-up reviews to validate CAP activities have been implemented.

Internal Audit has completed the Budget Overrun Review. This engagement was approved by the Board of Trustees (Board) as part of the 2025–2026 Internal Audit Plan. Following the Executive Summary, this section presents the detailed results of the review, including background information, objectives and scope, Internal Audit's conclusions, detailed findings, and recommendations. Appendix A provides the methodology used to perform the review. We would like to acknowledge and thank District leadership and management who participated in this review for their time.

Background

In May 2026, the Board requested that Internal Audit perform a review following concerns regarding the District's projected fiscal year 2025–2026 financial deficiency of approximately $52.79 million and the reduction in unassigned fund balance to approximately 37.89 days of operating expenditures.

To comply with state laws and Board policies, the District must continuously monitor its financial position, ensure expenditures remain within Board-approved authority, and formally approve budget amendments before committing to new spending. Texas Education Code (TEC) §44.006 provides that public funds may not be spent in a manner other than as provided in the adopted budget unless the Board approves a budget amendment or supplementary emergency budget.

Accordingly, a school district's financial management process includes annual budget development, ongoing monitoring of revenues and expenditures, financial forecasting, and periodic reporting to District leadership and the Board. As financial conditions, expenditures, or budget assumptions change throughout the fiscal year, management is expected to evaluate the impact of those changes and, when appropriate, recommend budget amendments or other corrective actions for Board consideration.

FY2025–2026 Budget Development, Governance, and Leadership Transition

Development of the fiscal year 2025–2026 budget began during fiscal year 2024–2025 and occurred during a period of significant governance and leadership transition. During budget workshops held between April and June 2025, District personnel presented multiple budget scenarios to the Board. Budget workshops conducted in April and May 2025 occurred under the direction of the former Superintendent and reflected uncertainty associated with the legislative session. Depending on the scenario presented, projected operating deficits ranged from approximately $3 million to $31.6 million.

Following the May 2025 Board election, the composition of the Board changed, and in June 2025 the former Superintendent departed the District pursuant to a voluntary separation agreement. The former Chief Financial Officer (CFO) subsequently assumed the dual role of Interim Superintendent and CFO. On June 18, 2025, the Interim Superintendent presented the proposed FY2026 budget to the Board for consideration and approval. The Board subsequently adopted the budget during the same meeting. The adopted budget projected the use of approximately $6 million of fund balance to support operations.

The former CFO continued serving in the dual role of Interim Superintendent and CFO until December 2025. On December 10, 2025, Dr. Lusk assumed the role of Superintendent and responsibility for District operations during the second half of the fiscal year.

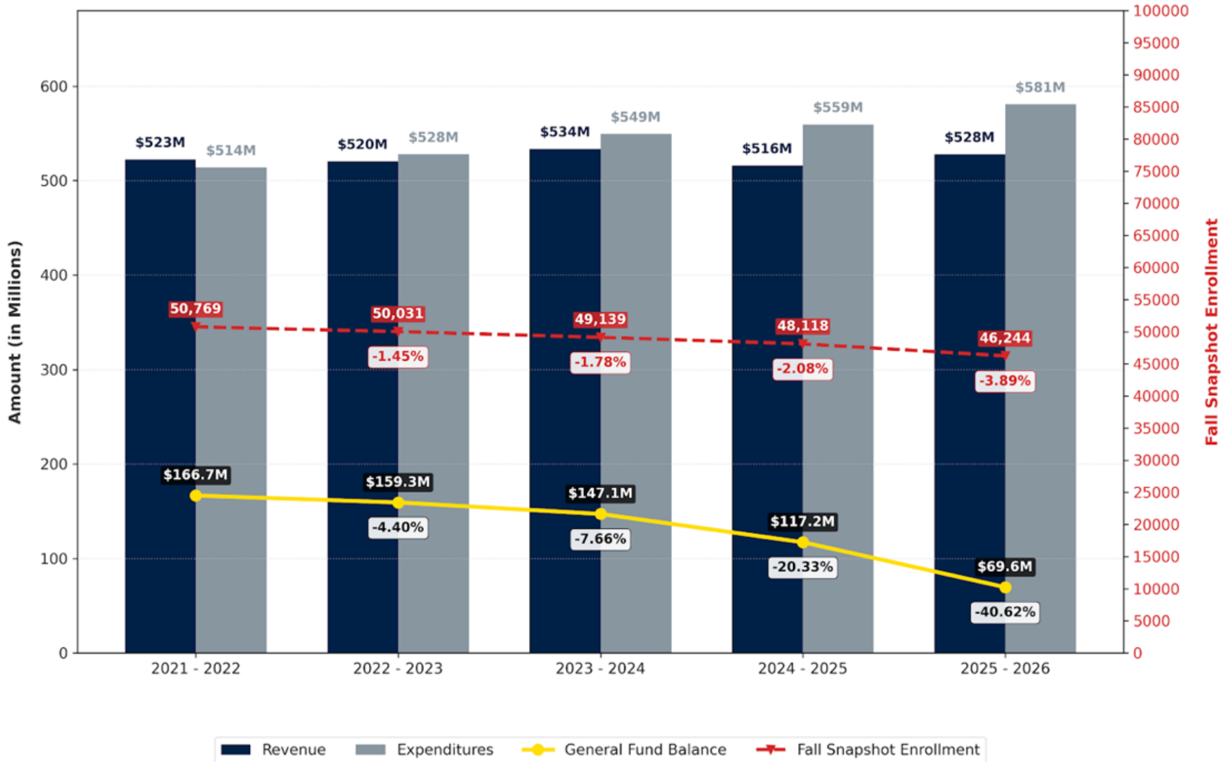
Historical Financial Context

While this review focused on fiscal year 2025–2026 (for specific scope refer to the section **Objective and Scope** section), historical financial and enrollment trends provide important context for the District's financial position.

As shown in Figure 1, from fiscal year 2021–2022 through fiscal year 2025–2026, Fall Snapshot Enrollment declined from 50,769 students to 46,244 students, a decrease of approximately 4,525 students (8.9%).

During the same period, General Fund revenues increased from $523 million to $528 million (1.0%), while General Fund expenditures increased from $514 million to $581 million (13.0%).

Figure 1: Historical General Fund Revenues, Expenditures, Fund Balance, and Enrollment Trends (FY2022–FY2026)



As expenditures grew faster than revenues, the District relied on fund balance to support operations. The General Fund balance declined from approximately $166.7 million in fiscal year 2021–2022 to a projected $69.6 million in fiscal year 2025–2026, a reduction of approximately $97.1 million (58.3%). Nearly half of this decline occurred in fiscal year 2025–2026, when fund balance decreased by approximately $47.6 million. Collectively, these trends reflect a pattern of declining enrollment, increasing expenditures and growing reliance on fund balance to support operations over the five-year period.

Figure 2 compares the District's unassigned fund balance with neighboring school districts over the five-year period. While all three of the largest school districts in El Paso County experienced declines in unassigned fund balance, EPISD's balance decreased from approximately $125.2 million in FY2022 to a projected $60.3 million in FY2026, representing a decline of approximately 51.8%. This trend illustrates the significant reduction in the District's available financial reserves during the period under review.

Figure 2: Historical Unassigned Fund Balance Compared to Neighboring Districts (FY2022–FY2026)

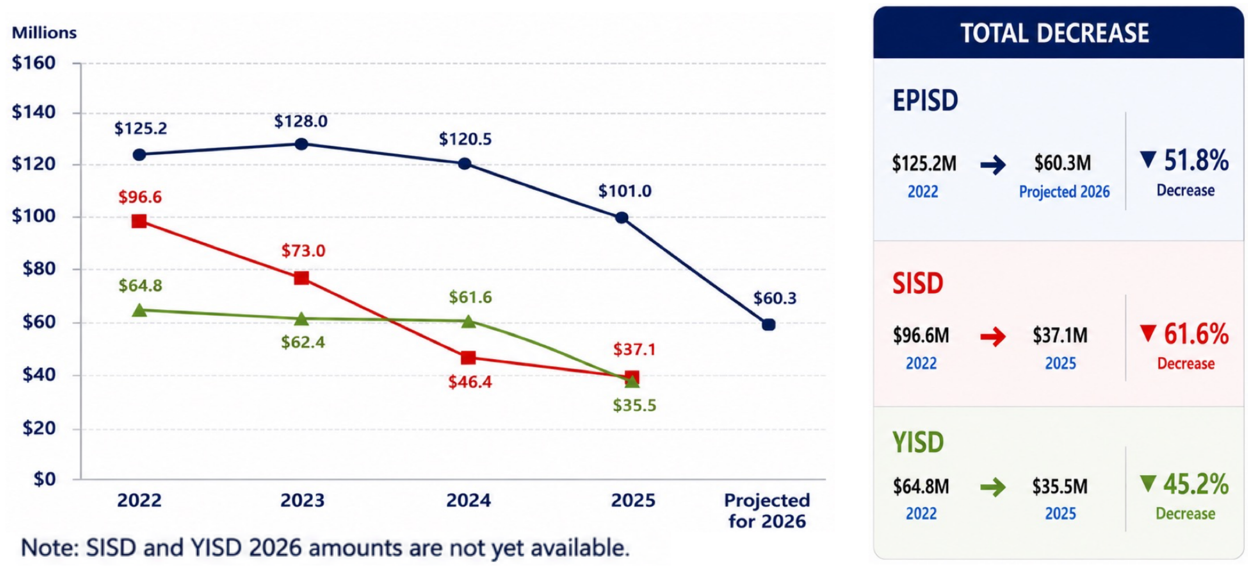
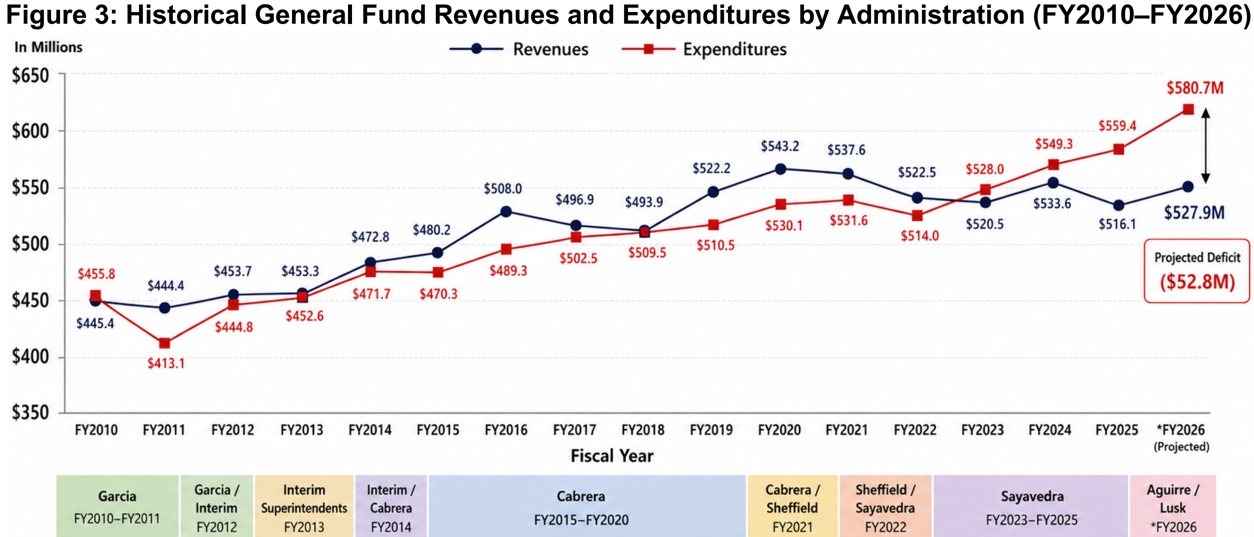


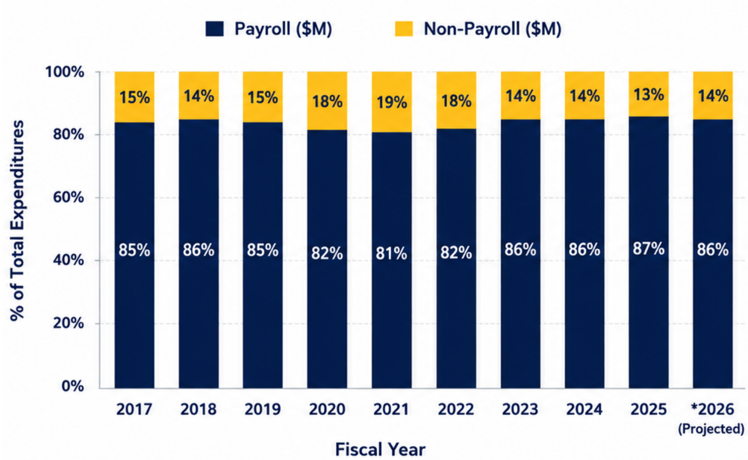
Figure 3 provides a longer-term perspective of the District's financial trajectory. Historically, General Fund revenues and expenditures generally tracked closely together. Beginning in fiscal year 2022-2023, expenditures consistently outpaced revenues, with the gap widening significantly in fiscal year 2025–2026. By the end of the review period, projected expenditures exceeded projected revenues by approximately $52.8 million, accelerating the decline in fund balance and contributing to the District's projected financial deficiency.

Figure 3: Historical General Fund Revenues and Expenditures by Administration (FY2010–FY2026)



While Figure 3 illustrates the District's widening gap between revenues and expenditures, Figure 4 provides additional context by showing the composition of those expenditures over time. Payroll represents the District's largest expenditure category, accounting for approximately 86% of projected General Fund expenditures in fiscal year 2025–2026. As illustrated in Figure 4, payroll expenditures increased by approximately $74.9 million between fiscal years 2017 and 2026, while non-payroll expenditures increased by approximately $3.3 million over the same period. Although non-payroll expenditures fluctuated during the period, they returned to levels comparable to fiscal year 2019 by fiscal year 2026. The chart illustrates that long-term expenditure growth has been driven primarily by payroll-related costs.

Figure 4: Historical General Fund Payroll and Non-Payroll Expenditures (FY2017–FY2026)



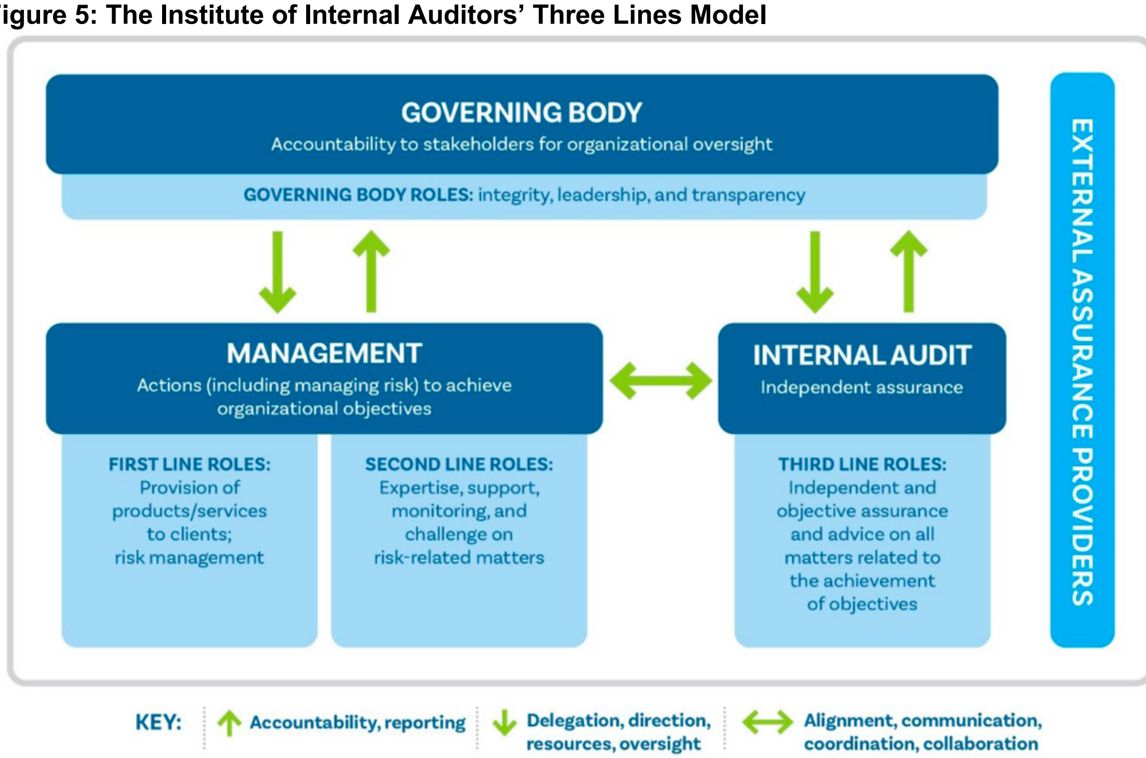
Fiscal Year	Payroll ($)	Payroll (% of Total)	Non-Payroll ($)	Non-Payroll (% of Total)
*2026	502,285,633	86%	78,442,103	14%
2025	486,232,609	87%	73,188,279	13%
2024	470,054,773	86%	79,281,595	14%
2023	451,580,674	86%	76,428,154	14%
2022	419,812,504	82%	94,191,425	18%
2021	432,798,926	81%	98,800,751	19%
2020	436,859,769	82%	93,238,295	18%
2019	431,633,538	85%	78,909,267	15%
2018	438,822,693	86%	70,632,890	14%
2017	427,383,273	85%	75,110,275	15%

* Projected

Governance Framework

Effective financial stewardship requires more than budget development and financial reporting. It also requires a governance structure that ensures significant financial risks are identified, evaluated, communicated, and addressed in a timely manner. The Institute of Internal Auditors' (IIA) Three Lines Model provides a globally recognized framework for governance, risk management, and accountability. Figure 5 illustrates the governance, oversight, and accountability relationships described in the Three Lines Model.

Figure 5: The Institute of Internal Auditors' Three Lines Model



Source: The Institute of Internal Auditors (2020), The IIA's Three Lines Model: An Update of the Three Lines of Defense.

Under the model, the Board serves as the governing body and is responsible for establishing policy, providing oversight, and making informed decisions based on information provided by management. Consistent with this role, Board Policy CE (LOCAL) establishes expectations for budget planning, monitoring, and evaluation. The policy states that budget planning and evaluation are continuous processes and part of each month's activities. As the District's primary financial authorization and control mechanism, the Board-adopted budget requires District management to continuously monitor financial performance and timely communicate material variances from budgeted revenues, expenditures, and assumptions to District leadership and the Board.

Management serves as the first and second lines and is led by the Superintendent, who serves as the District's chief executive officer. Management is responsible for achieving District goals and objectives, managing resources, identifying and addressing risks, and providing the Board with information necessary to support effective oversight and decision-making.

As part of the first and second lines, financial management functions, including the CFO, Comptroller, Budget & External Financial Management (BEFM) Office, Accounting and Financial Reporting, and Treasury, are responsible for monitoring the District's financial position, evaluating emerging risks, and providing financial information necessary to support decision-making, oversight, and accountability. As the District's principal financial advisor, the CFO plays a key role in coordinating these activities and communicating significant financial matters to the Superintendent and Board.

Independent of management, Internal Audit serves as the third line by providing objective assurance regarding the effectiveness of governance, risk management, and control processes. To maintain its independence and objectivity, Internal Audit does not perform management functions, participate in day-to-day operational decision-making, or assume responsibility for identifying, monitoring, or managing risks on behalf of management. Instead, Internal Audit evaluates whether management's processes and controls are designed and operating effectively through risk-based engagements approved by the Board. To fulfill its role effectively, the third line must maintain a clear separation from management responsibilities, enabling Internal Audit to provide independent assessments and recommendations without impairing its objectivity.

External auditors and other assurance providers provide additional independent assurance regarding specific financial reporting, compliance, and regulatory requirements. These assurance activities complement the work of Internal Audit and provide the Board and other stakeholders with additional assurance regarding the District's governance, risk management, and control processes.

Collectively, these roles are intended to provide a system of governance, risk management, oversight, and accountability that supports informed decision-making and responsible stewardship of public resources.

The effectiveness of the Three Lines Model depends upon timely communication, transparency, and accountability among all parties. Effective governance requires management to identify significant risks, evaluate their potential impact, and communicate accurate, complete, and timely information regarding financial conditions and other material matters to the Superintendent and Board. Without such information, decision-makers may be unable to fully understand emerging risks, implement corrective actions, or exercise effective oversight of the District's financial position.

Objectives and Scope

The objectives of the Budget Overrun Review were to:

1 Determine the primary factors contributing to the District's projected fiscal year 2025–2026 budget overrun, including expenditures incurred after budget adoption and budgeted cost savings assumptions that were not achieved as planned.

2 Assess whether significant financial risks were appropriately identified, monitored, and communicated to District Leadership and the Board in a timely manner.

3 Assess whether budgetary controls were operating effectively to ensure the adopted budget functioned as the District's primary authorization and control mechanism for expenditures and financial decisions.

SCOPE

The scope of the review was limited to fiscal year 2025–2026 General Fund budget development, financial monitoring, budget amendment processes, expenditures, and financial reporting activities through May 2026.

SUPPORTS LEVER IV: CULTURE OF ACCOUNTABILITY

This review supports Lever IV: Culture of Accountability, which promotes transparency, accountability, and the effective stewardship of resources to build fiscal stability.

CONDUCTED IN CONFORMANCE WITH GLOBAL INTERNAL AUDIT STANDARDS

In accordance with those Standards, Internal Audit exercised due professional care and professional skepticism in obtaining sufficient and appropriate information to provide a reasonable basis for the findings and conclusions presented in this report. Accordingly, the engagement provides reasonable, but not absolute, assurance that significant conditions, errors, omissions, and risks were identified.

Conclusion

The review concluded that the District's projected fiscal year 2025–2026 budget overrun and resulting financial deficiency, which significantly exceeded the Board-approved budget deficit, were attributable to a combination of expenditure-related factors, unrealized budget assumptions, and other significant financial risks identified during the review. Collectively, the expenditure-related factors and unrealized assumptions increased General Fund costs by approximately $21 million and significantly contributed to the District's projected financial deficiency.

The FY2026 budget adopted by the Board in June 2025, which included a planned use of approximately $6 million of fund balance to support operations, did not fully reflect the District’s anticipated operating requirements. Specifically, the adopted budget included approximately $3.99 million in projected savings associated with initiatives that District personnel had determined were not feasible prior to budget adoption. In addition, approximately $2.49 million of budget reductions incorporated during budget development were subsequently restored through approved Additional Budget Requests (ABRs) to support operational, contractual, programmatic, and compliance-related needs. Together, these factors contributed to a budget that did not fully reflect the District’s anticipated costs and projected operating deficit.

The review further concluded that financial risk management, monitoring, and reporting processes were not operating effectively. Although information regarding significant financial risks was available within the District’s financial management functions, the significance and cumulative impact of those risks on the District’s financial position were not communicated in a timely manner to the Superintendent and the Board. As a result, opportunities to evaluate, address, and mitigate emerging financial risks were diminished.

As the District’s primary financial advisor, the former CFO was responsible for ensuring the District’s financial position was appropriately evaluated; budget performance, expenditures, and fund balances were effectively monitored; the Superintendent and Board were timely informed of and advised regarding the District’s financial condition; and appropriate corrective actions were recommended to maintain fiscal stability. However, significant financial risks, including the revenue impacts associated with declining enrollment and attendance, unrealized budget assumptions, and expenditures incurred after budget adoption, were not adequately evaluated, addressed, or communicated in a manner that conveyed their cumulative effect on the District’s financial position or supported timely decision-making. As a result, the evidence obtained during this review indicates that the former CFO did not effectively fulfill these responsibilities.

Consistent with the Institute of Internal Auditors’ Three Lines Model, effective governance depends on management’s ability to provide those charged with governance with timely, reliable, and transparent information regarding significant risks and financial conditions. Without such information, the Superintendent and Board were not positioned to take timely and informed corrective action in response to emerging financial challenges. As the public’s elected governing body, the Board serves as the primary mechanism through which the public exercises oversight of the District’s financial stewardship. Consequently, incomplete communication of significant financial risks reduced the transparency and accountability necessary for effective public oversight of the District’s financial position.

The review also concluded that budgetary controls were not operating effectively to ensure expenditures remained within Board-approved appropriations and that significant financial changes were addressed through timely budget amendments. The Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control Framework recognizes budgets as a key control activity that establishes spending limits, monitors financial performance, and prompts corrective action when actual results materially differ from expectations. However, significant expenditures and known financial impacts were not consistently incorporated into the adopted budget through timely amendments. Consequently, the Board was required to approve a year-end budget amendment of approximately $30.7 million to align appropriations with projected expenditures and known financial conditions that had accumulated throughout the fiscal year.

The conclusions reached during this review extend beyond the budget overrun itself. The review identified breakdowns in the District’s financial risk management and budgetary control processes, limiting the timely identification, evaluation, communication, and mitigation of significant financial risks before they materially affected the District’s financial position. Transparency, accountability, and effective stewardship of public resources depend on the timely communication of reliable information through the District’s governance structure. Strengthening financial risk management, financial reporting, and budgetary control processes will better position the District to support informed decision-making, enhance public transparency, and build long-term fiscal stability.

The findings and recommendations that follow provide the detailed results of the review and support the conclusion summarized in this section.

Findings, Recommendations, and Management’s Response

I. Financial Oversight and Budgetary Control Deficiencies

Finding 1

Significant financial risks were not adequately monitored, communicated, or addressed

Significant financial risks were not adequately monitored by the financial management function or communicated and addressed by the former CFO during fiscal year 2025–2026. As a result, the Superintendent and Board were not provided the information necessary to fully understand the District’s deteriorating financial position and were not positioned to take timely and informed corrective action. Opportunities to reassess budget assumptions, reduce expenditures, implement cost-saving measures, and mitigate emerging financial risks were diminished.

According to projected year-end results presented by Moak Casey (Education Consulting Firm), the District faces an estimated financial deficiency of approximately $52.79 million and a reduction in unassigned fund balance to approximately 37.89 days of operating expenditures. These conditions ultimately contributed to the declaration of financial exigency and the need for significant workforce reductions and other budget-balancing measures in fiscal year 2026–2027.

Individuals entrusted with stewardship of public resources have a fiduciary responsibility to exercise due care, sound financial oversight, and transparency. Consistent with the IIA's Three Lines Model, management is responsible for identifying, monitoring, and communicating significant risks to senior leadership and those charged with governance. Within this structure, the District’s financial management functions are responsible for monitoring the District’s financial position, evaluating emerging risks, and providing financial information necessary to support decision-making, oversight, and accountability. As the District’s principal financial advisor, the CFO oversees and coordinates the District’s financial management functions, plays a key role in communicating significant financial matters to the Superintendent and Board, and recommends corrective action when significant financial risks emerge.

The evidence obtained during this review indicates that the former CFO did not effectively fulfill these responsibilities. Specifically, significant financial risks were known within the District’s financial management functions but were not adequately monitored, communicated, or addressed.

1. Financial Risks Were Known by Financial Management Leadership but Not Adequately Monitored

a. Throughout fiscal year 2025–2026, information indicating significant financial risks was available to members of the District's financial management leadership, including the former CFO, Comptroller, Director of BEFM, Director of Accounting and Financial Reporting, and the Treasurer. Collectively, this information reflected declining enrollment, revenue shortfalls, unrealized budget assumptions, staffing-related costs, and expenditures incurred after budget adoption.

b. By December 2025, sufficient information existed within the District's financial management functions to identify that the District's financial challenges extended beyond declining enrollment and revenue shortfalls. Information regarding additional expenditures and unrealized budget assumptions was available but was not collectively tracked, monitored, or evaluated to determine its cumulative impact on the District's financial position.

c. In December 2025, the former CFO communicated to two (2) Board members that enrollment was approximately 850 students below projections, resulting in an estimated $5 million revenue shortfall. The communication stated that the District had adopted a $6 million deficit budget and that the anticipated deficit was "closer to $11 million" while fund balance was "currently at 66 days." The former CFO further indicated that she would share the information with the incoming Superintendent. However, the Superintendent stated he was not informed of the enrollment-related revenue shortfall at that time. Additionally, no budget amendment was presented to revise projected revenues or formally communicate the increased deficit to the Board.

d. By March 2026, the spring financial forecast, completed by the Director of Accounting and Financial Reporting, had identified significant concerns regarding the District's projected year-end financial position. The Director of Accounting and Financial Reporting stated that the forecast results were communicated to the former CFO at that time. On April 1, 2026, a Microsoft Teams conversation between the former CFO and the Director of Accounting and Financial Reporting referenced an estimated $8.3 million revenue reduction and a preliminary payroll deficit of approximately $21 million.

e. The Comptroller recalled advising the former CFO in late April 2026 that the Superintendent should not publicly characterize the District as being in a strong financial position due to significant financial uncertainty. Similarly, the BEFM Director described concerns regarding the District's ability to fund proposed compensation increases based on the financial information available at the time.

f. Internal Audit discussed with financial management leadership how significant financial concerns were reported and to whom those concerns were communicated. The Comptroller stated that because the former CFO was also serving as Interim Superintendent, she relied on the established chain of command and assumed significant financial concerns were being communicated to the appropriate parties. Although she acknowledged that the Board may have been an appropriate avenue for reporting concerns, she indicated that she was unaware that significant financial concerns were not being communicated. The Director of BEFM stated that she was unaware of what information the former CFO communicated to the Superintendent, Leadership, or the Board because staff had no mechanism to verify those communications. Similarly, the Director of Accounting and Financial Reporting stated that she communicated financial information and concerns to the former CFO but was unaware of what actions, if any, were taken after the information was provided.

g. On May 7, 2026, the former CFO stated that she did not communicate concerns earlier because she was not aware of the full financial impact until the spring financial forecast. The former CFO estimated the projected impact to be approximately $28 million, inclusive of the previously approved budget deficit of $6M and noted that the projection included both expenditure and revenue considerations. She attributed the situation to breakdowns in staffing and budget-monitoring processes, including missed checkpoints, insufficient follow-through, and a lack of coordination among departments responsible for implementing and monitoring staffing reductions.

h. While the full financial impact may not have been quantified until the Spring forecast in March 2026, evidence indicates the former CFO had access to information reflecting emerging financial risks months earlier. Through monthly financial reports, expenditure approvals, and ongoing discussions regarding enrollment and budget performance, the former CFO was responsible for monitoring the District's financial position and assessing the significance of emerging financial risks. Accordingly, the former CFO should have communicated the existence and potential impact of emerging risks to the Superintendent and Board as they became known.

2. The Former CFO Did Not Timely Communicate Significant Financial Risks to the Superintendent and Senior Leadership

a. The Superintendent stated that he first became aware of the severity of the District's financial position on May 1, 2026, when the former CFO informed him that the District's unrestricted fund balance had declined to approximately 40 days. According to the Superintendent, prior to that discussion he had not been informed that significant budget assumptions were not being achieved, that substantial payroll deficits had been identified, or that the multiple financial issues collectively posed a significant risk to the District's financial position. The Superintendent indicated that he relied on the former CFO to identify and communicate material financial risks affecting the District.

b. Further supporting this understanding, during the April 2, 2026, Finance Committee meeting, the Superintendent stated that the District had previously balanced the budget, implemented nearly $20 million in reductions, and was preparing to discuss compensation increases before having to revisit budget balancing efforts due to revised state funding calculations.

c. The Superintendent further indicated that had he been aware of the District's deteriorating financial position earlier, discussions regarding employee compensation increases would not have occurred. Although the former CFO advised that adjustments would be necessary before compensation increases could be considered, he stated that he was not informed of the extent of the District's financial challenges.

d. Interviews with four (4) current senior leadership members who served in cabinet-level roles during budget development and implementation (former Deputy Superintendent of Academics and Technology, Chief Communications Officer, Chief Human Capital Management Officer, and Chief Academic Officer) indicated that staffing changes, program expansions, budget reductions, and operational needs were routinely discussed. However, they reported receiving limited information regarding the overall financial impact of those decisions, including projected deficits, fund balance implications, and the status of significant budget assumptions. Several indicated discussions focused primarily on operational approvals rather than broader fiscal risks.

3. The Former CFO Did Not Communicate Significant Financial Risks to the Board

a. According to the five (5) current Board members, they did not become aware of the severity of the District's financial position until May 2026, when the Superintendent communicated the projected budget shortfall and declining fund balance. Each Board member stated, separately, that they had not previously been informed that multiple financial issues had collectively created a material risk to the District's financial position. Additionally, two (2) Board members expressed concern that information requested from the former CFO was not always provided and that some responses received did not directly address the information requested.

b. Information available to the former CFO and financial management leadership throughout fiscal year 2025–2026 reflected significantly greater financial risk than what was communicated to the Board through quarterly financial reports and Finance Committee discussions.

c. Quarterly financial reports were included in the November 2025 and February 2026 Board meeting consent agendas and were not removed for separate discussion. The budget and expenditure reporting primarily consisted of accounting-based financial statements and did not include trend analyses, meaningful budget-to-actual comparisons, status updates regarding significant budget assumptions, or other information necessary to assess the District's changing financial position.

d. Finance Committee meetings held in January, February, March, and April 2026 included discussions regarding enrollment, attendance, administrative cost ratio, budget development, revenue projections, expenditures, and fund balance levels. However, the former CFO, who took the lead in presenting financial information to the Board, did not provide a comprehensive assessment of the District's projected financial position, as known financial risks, including unrealized budget assumptions, staffing-related expenditures, and other post-budget adoption costs, were not consolidated and communicated in a manner that reflected their cumulative impact on the District's fiscal sustainability.

- During the January 2026 Finance Committee meeting, the Comptroller presented the November 30, 2025, financial statement. The Comptroller reminded attendees that the District had adopted a $6 million deficit budget and that Board-approved budget amendments had increased the budgeted deficit to approximately

$20.7 million. No significant discussion occurred regarding the budget amendments.

- During the February 2026 Finance Committee meeting, the former CFO reported the adopted $6 million deficit, approximately 67 days of fund balance, and stated that hiring had largely been paused to recover the deficit. Information presented did not include the previously identified enrollment-related revenue shortfall ($8.3 million), projected deficit increases ($11 million and $20.7 million), or additional personnel costs associated with Special Education staffing changes.

- During the March 2026 Finance Committee meeting, the former CFO noted that the increase in the homestead exemption from $100,000 to $140,000 reduced taxable property values and that the State's offset was not provided on a dollar-for-dollar basis. The Treasurer also discussed a potential $5 million revenue loss related to changes commercial property exemption.

- During the April 2, 2026, Finance Committee meeting, the former CFO reported that revised Texas Education Agency (TEA) funding calculations had reduced anticipated Hold Harmless funding for FY2025–2026 by approximately $17 million. However, the former CFO did not disclose the approximately $21 million payroll deficit reflected in the April 1, 2026, Microsoft Teams conversation with the Director of Accounting and Financial Reporting, nor the potential effect of that deficit on the District's projected year-end financial position.

- During the April 14, 2026, Finance Committee meeting, the former CFO presented updates related to FY2026–2027 budget development. The former CFO also discussed efforts to reduce central office staffing and realign resources closer to campuses. The meeting did not include discussion of the District's projected FY2025–2026 financial deficiency.

e. While the former CFO communicated certain information, including declining enrollment and revenue shortfalls, the information provided to the Superintendent and Board did not reflect the full scope or combined effect of known financial risks. Reporting and discussions did not integrate key factors such as unrealized budget assumptions, staffing-related expenditures, and post-budget adoption costs into a consolidated assessment of the District's projected financial position and fiscal sustainability.

4. Opportunities to Take Corrective Action Were Diminished

The Superintendent and Board were not provided with timely and comprehensive information necessary to fully understand the District's deteriorating financial position. Consequently, opportunities to evaluate corrective measures, including expenditure reductions, staffing adjustments, and other cost-saving initiatives, were diminished before the District's financial position further deteriorated. Earlier communication may have provided additional opportunities to evaluate and implement measures intended to mitigate the District's projected financial deficiency.

Recommendations and Management's Response

1.1 District Leadership should establish and implement formal financial transparency, risk reporting, escalation, and corrective action procedures to ensure material financial risks are identified and communicated in a timely manner to District leadership and the Board. Procedures should include the following components:

a. Required monthly financial reporting that include both quantitative and narrative analysis sufficient to assess the District's overall financial position. At a minimum, reports should include key financial indicators and trend analyses:
   - Budget-to-actual comparisons of revenues and expenditures to expected percentages based on the portion of the fiscal year completed.
   - Projected year-end results and fund balance projections.
   - Enrollment and attendance trends and their related financial impact.
   - Identification and explanation of material variances.

b. A formal financial risk escalation process that defines the types of financial conditions requiring notification, the thresholds and timelines for escalation, the individuals responsible for identifying and communicating financial risks, and requirements for notifying the Superintendent and Board when material changes occur in the District's financial position, projections, or significant budget assumptions.

c. A formal financial corrective action and budget response process that requires management to:
   - Develop and implement corrective action plans for material budget variances, revenue shortfalls, or projected deficits.
   - Evaluate and implement expenditure reductions, revenue enhancements, staffing adjustments, or other corrective measures, as appropriate.
   - Initiate budget amendments when financial projections materially deviate from adopted assumptions or when significant expenditures become known.
   - Present significant budget changes to the Board in a timely manner.
   - Monitor and report on the implementation and effectiveness of corrective actions until the identified financial risk has been resolved.

d. Require quarterly financial reports to be presented as regular discussion items at Board meetings and not included on consent agendas. Financial management leadership should provide a summary of the District's financial position, significant variances, emerging financial risks, and projected year-end results and allow for Board discussion and questions.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activities 1a, 1b, and 2.

Persons Responsible and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems.

Implementation Date: September 30, 2026, and November 30, 2026

1.2 District leadership should promote a culture of professionalism, collaboration, transparency, and shared responsibility by fostering an environment in which employees and leaders engage in open, constructive dialogue, proactively identify challenges, communicate material operational, financial, and compliance information in a timely manner, and work collaboratively to develop solutions that support informed decision-making. These principles will be embedded within and aligned to the District's strategic plan

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity 3.

Persons Responsible and Accountable: Deputy Superintendent of Operations and Support Systems and Superintendent of Schools.

Implementation Date: September 30, 2026

II. Budgeted Savings and Financial Assumptions Were Not Achieved

Finding 2

The adopted FY2026 budget included $3.99M in savings assumptions that were not feasible and ultimately not realized

The FY2026 budget, proposed by the former CFO while serving as Interim Superintendent and subsequently adopted by the Board, included three significant savings assumptions that lacked supporting documentation, validation, or adjustment prior to budget adoption, indicating weaknesses in the processes used to develop, evaluate, and approve significant budget assumptions. As a result, approximately $3,992,349 in projected savings were not realized. The inclusion of these savings assumptions understated projected expenditures, reduced the reliability and transparency of the budget projections, and contributed to the District's budget deficit.

During the Board Budget Workshops held from April 1, 2025, to June 3, 2025, District personnel, which included the former CFO, presented multiple versions of the FY2026 proposed budget due to the uncertainties associated with the legislative session. The proposed budgets incorporated savings assumptions and reflected projected deficits ranging from $3 million to $31.6 million. However, the presentations and supporting budget materials did not disclose that the savings assumptions were included in the budget projections, nor did they identify the associated risks should the anticipated savings not be realized.

On June 9, 2025, the former CFO held a meeting titled "FY 26 Proposed Staffing Final Review" with the Chief Human Capital Management Officer, Comptroller, Director of BEFM, Senior Director of Talent Acquisition and Personnel Administration, and other staff to discuss personnel-related reductions and projected savings incorporated into the budget. According to the Director of BEFM, the projected savings amounts were provided by the former CFO and Chief Human Capital Management Officer. The Chief Human Capital Management Officer and Senior Director of Talent Acquisition and Personnel Administration stated that at those meetings "we are looking at campus numbers and ratios and movement of people. That's it. The budget is not part of the conversation" and "you have discussions about different things right throughout to see what could potentially come to fruition, but we don't talk about what's put in the budget."

During the meeting, participants reviewed savings initiatives that remained pending prior budget discussions, including the Multi-Age Classroom Option and Teacher Certification Assignment Review, which collectively represented approximately $2.4 million in projected savings. According to the Director of BEFM, during the meeting, these initiatives were determined to be not feasible, and she advised that the associated savings should be removed from the budget projections. However, she stated that the former CFO directed that the savings remain in the budget because removing them would have required presenting a substantially different budget projection reflecting a larger projected deficit.

On May 7, 2026, the former CFO admitted that the District ultimately did not realize certain staffing-related savings incorporated into the budget. She stated that projected savings associated with position reductions, staff reassignments, and other personnel actions required ongoing monitoring and coordination among BEFM, Human Resources (HR), Analytics, school leadership, and District staff. According to the former CFO, follow-up and reconciliation processes were not performed timely or consistently, resulting in missed checkpoints, insufficient follow-through, and a failure to identify that certain budgeted savings assumptions were not being achieved.

The District's adopted FY2026 budget included the following projected savings assumptions, which were either subsequently not realized or determined to not be feasible:

1. <u>Multi-Age Classrooms – $1,407,000</u>: The initiative involved combining students from multiple grade levels into a single classroom to reduce the number of teacher positions required. Projected savings were included in the budget; however, prior to budget adoption, the initiative was determined to be operationally not feasible due to curriculum, staffing, and operational constraints and was not implemented. The savings were calculated based on approximately 21 full-time employee (FTE) positions at an estimated average cost of $67,000 per position.

2. <u>Teacher Certification Assignment Review (Staff Teachers)– $1,005,000</u>: The initiative involved reassigning unassigned or displaced teachers to existing vacant positions to reduce the need for new hires. The District implemented reassignment efforts to place displaced teachers into vacancies; however, actual savings were not tracked or validated. Additionally, staff displacement occurred after budget development, and the full projected savings remained in the adopted budget without adjustment. The projected savings assumed approximately 15 FTE positions at an estimated average cost of $67,000 per position.

3. <u>Special Education Department (SPED) Operating Budget Shift to IDEA-B – $1,580,349:</u> The initiative involved shifting eligible Special Education operating costs from the General Fund (199) to the IDEA-B grant (224) to reduce the General Fund expenditures. The planned transfer of expenditures was not fully realized because the grant funds had been exhausted. The projected savings were based on approximately 26 FTE positions.

Per Board Policy CE (Regulation), a budget is an estimate of anticipated revenues and expenditures and expenditures should be adjusted when revenues or other assumptions are not achieved. However, significant savings assumptions were incorporated and retained in the FY2026 budget despite being unsupported, determined to not be feasible, or dependent upon actions that had not been implemented.

Additionally, the BEFM Manual does not establish procedures requiring significant budget assumptions to be documented, validated, assigned, monitored, and reassessed prior to budget adoption.

Recommendations and Management's Response

2.1 District Leadership should develop and implement written procedures governing the identification, evaluation, approval, documentation, and communication, of significant budget assumptions. The procedures should establish criteria for determining significance, such as dollar thresholds, fiscal impact, implementation risk, or assumptions that require operational changes to achieve projected savings. At a minimum, procedures should require:

a. Documented assumptions supported by data-driven analyses.
b. Validation of assumptions with departments responsible for implementation.
c. Clearly defined roles, responsibilities, approval authority, and accountability for significant budget assumptions.
d. Verification that approved savings and funding source changes are accurately reflected in the adopted budget.
e. Retention of budget development records documenting supported analyses, approvals, decisions, and rationale for significant budget assumptions.
f. Documentation provided to the Superintendent and Board supporting significant budget assumptions and disclosing material risks associated with achieving projected savings during the budget development and adoption process.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity 1c.

Persons Responsible: and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems.

Implementation Date: September 30, 2026

2.2 District Leadership should establish monitoring procedures for significant budget assumptions that require:

a. Assignment of ownership for each savings initiative to a responsible administrator.
b. Monthly review of budget-to-actual results and projected savings realization, including documentation and investigation of significant variances.
c. Escalation of unrealized or infeasible savings assumptions to Senior Leadership and the Superintendent, with evaluation of the need for budget amendments, expenditure reductions, or alternative funding strategies.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity number 1d.

Persons Responsible and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems.

Implementation Date: September 30, 2026

Finding 3

The BEFM Director, per the directive of the former CFO, included $20.0 million in projected lapsed salary savings to offset payroll expenditures in the FY2026

The District budgeted a savings assumption of $20M for lapsed salaries to offset payroll expenses. However, $6.31M was not realized

adopted budget. However, actual lapsed salary savings realized during the fiscal year totaled approximately $13.7 million, resulting in $6.31 million unrealized savings. The inclusion of lapsed salaries savings understated projected payroll expenditures, reduced the reliability and transparency of the District's budget, and contributed to the deficit.

Lapsed salaries are the unspent budget dollars that accumulate when a funded position remains vacant or is filled at a lower salary than originally budgeted. Historically, the District has incorporated budgeted lapsed salary savings into its annual budget for at least the past 14 fiscal years, including periods under multiple Superintendents and Interim Superintendents. See **Table 1** below for historical costs.

Table 1: Lapsed Salaries 2012-2026

FY	Amount
2012	$ 28,005,224
2013	14,789,974
2014	28,633,236
2015	19,338,207
2016	26,182,047
2017	35,126,315
2018	29,493,490
2019	26,973,557
2020	16,342,564
2021	14,972,922
2022	14,157,949
2023	17,227,999
2024	17,230,000
2025	20,000,000
2026	20,000,000
Total	**$ 328,473,484**

District personnel were unable to provide a documented methodology supporting the $20.0 million estimate for FY2026. According to the BEFM Director, the amount was carried forward from the prior year budget and was not recalculated using current staffing vacancies, historical trends, or other supporting analyses.

The BEFM Director further stated that a vacancy analysis performed during the budget development process indicated potential lapsed salary savings of approximately $10.0 million. According to both the BEFM Director and the Comptroller, concerns were raised during the budget development process that the estimate was not supported by the available vacancy analysis; however, the $20.0 million estimate remained in the adopted budget per the former CFO's directive.

Interviews with the Chief Human Capital Management Officer, Senior Director of Talent Acquisition and Personnel Administration, and Director of Middle School Personnel & Recruiting indicated they were not consulted regarding the development or validation of the lapsed salary estimate. The individuals stated they were unaware the FY2026 budget included a $20.0 million lapsed salary savings assumption and were not asked to provide information regarding vacancy trends, historical hiring patterns, staffing plans, or other personnel data that could have supported the estimate.

Because procedures were not established to require significant budget assumptions to be supported by documented analyses, reviewed against current operational data, and formally validated prior to budget adoption, lapsed salary savings estimates were incorporated into the budget without sufficient evidence that they could be realized.

Board Policy CE (Regulation) recognizes that a budget is an estimate of anticipated revenues and expenditures that should be adjusted when underlying assumptions are no longer achievable. However, the FY2025–2026 budget continued to rely on projected lapse salary savings despite indications that the assumption was not being achieved and that projected payroll expenditures would exceed budgeted amounts.

Recommendation and Management's Response

3.1 District Leadership should reduce and ultimately eliminate reliance on budgeted lapsed salary savings as a recurring budget-balancing mechanism within two (2) fiscal years. During the transition period, any budgeted lapsed salary savings should be supported by a documented methodology based on historical vacancy trends and current staffing data. Budget-to-actual results should be monitored throughout the fiscal year to assess the reasonableness of the assumption, evaluate the financial impact of variances, and implement corrective actions or budget adjustments when necessary.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity 4.

Persons Responsible and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems

Implementation Date: June 30, 2027

III. Expenditures Were Incurred Outside the Board-Approved Budget

Finding 4

Approximately $3M in ABRs were approved by District Leadership after the budget was adopted by the Board

During the period July 2025 through May 2026, 27 ABRs totaling approximately $3 million in General Fund expenditures were approved by the former CFO and current Superintendent. However, the associated expenditures were not timely incorporated into the adopted budget through the budget amendment process as required by Board Policy CE (Legal). The Board subsequently approved a budget amendment on June 16, 2026, to align the budget with operational needs and year-end financial projections.

- Seventeen (17) ABRs, totaling $1,742,199 were approved by the former CFO in her dual roles as CFO and Interim Superintendent.
- Ten (10) ABRs, totaling $1,260,455 were approved by the current Superintendent and the former CFO in her capacity as CFO.

The current Superintendent stated that several of the ABRs he approved were intended to restore funding for operational needs that had been reduced or removed during the budget development process. Interviews and supporting documentation confirmed that approximately $900,000 of the ABRs approved during his tenure restored budgeted funding that had previously been reduced or removed during budget development.

In total, approximately $2.49 million of approved ABRs restored budgeted funding for Athletics, Information Security & Technology (IST), Facilities, Gifted and Talented, Career and Technical Education, Strategic Planning, Analytics, Accountability, and other departments. According to the Comptroller, the former Superintendent and cabinet (currently referred to as senior leadership) undertook a collaborative process to identify and implement reductions districtwide to help address the projected fiscal year 2025–2026 budget deficit. The funding was subsequently reinstated through 11 ABRs to support contractual obligations, critical operational and program needs, and compliance requirements.

Of approximately $3 million in approved ABRs, $2.5 million were funded through transfers from payroll accounts. The District's financial system (Frontline) allows payroll expenditures to continue processing and posting even when sufficient budget is not available at the account level.

Board Policy CE (Legal) states that public funds may not be spent in any manner other than as provided in the budget adopted by the Board. The Board may amend the budget or adopt a supplementary emergency budget to cover necessary unforeseen expenses. Any amendment or supplementary budget must be prepared and filed in accordance with State Board of Education rules (TEC §44.006). In addition, the BEFM Manual (April 2023) requires departments to review existing budgets and identify available funding before submitting ABRs. ABRs are intended to be used as a last resort and must be supported by documented need, funding availability, and alignment with District priorities. Requests exceeding $50,000 require Superintendent approval.

Recommendations and Management's Response

4.1 District leadership should establish and implement written procedures for the budget development process to ensure all known and ongoing costs are included in the proposed budget. At a minimum, the procedures should require:

a. Department administrators to certify that budget submissions include all known contractual, operational, programmatic, staffing, and compliance-related expenditures anticipated for the fiscal year.
b. Financial Services and BEFM to review and validate funding sources and cost estimates before budget consolidation.
c. Proposed budget reductions, staffing changes, and cost-saving measures to be developed and reviewed in collaboration with affected departments.
d. A summary of proposed department budget reductions, including the amount, purpose, justification, and potential impact on contractual, operational, programmatic, or compliance obligations should be provided to the Superintendent before the submission of the proposed budget to the Board.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity number 5.

Persons Responsible and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems

Implementation Date: January 31, 2027

4.2 District leadership should establish procedures requiring that, prior to approval of an ABR:

a. Funding availability is verified and documented
b. The funding source and estimated fiscal impact on the District's budget position are identified and communicated to the approving authority.

c. All required approvals are obtained and documented in accordance with District policy.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity number 6.

Persons Responsible and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems

Implementation Date: August 31, 2026

4.3 District leadership should establish procedures to ensure approved ABRs that increase expenditures beyond amounts authorized in the adopted budget are evaluated for inclusion in a Board-approved budget amendment as required by Board Policy CE(Legal).

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity number 6.

Persons Responsible and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems

Implementation Date: August 31, 2026

4.4 The future CFO, should provide the Superintendent with a monthly report of approved ABRs that includes:

a. Requesting department.
b. Amount approved.
c. Purpose of the request.
d. Funding source.
e. Available fund balance at the time of approval.
f. Whether the expenditure was included in the adopted budget.
g. Estimated fiscal impact on the District's budget position.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity number 6.

Persons Responsible and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems

Implementation Date: August 31, 2026

Finding 5

Special Education staffing changes resulted in approximately $2.35 M in Unbudgeted Payroll Costs

On September 2, 2025, the District's Cabinet, now referred to as Senior Leadership, approved revisions to the SPED staffing guidelines. At the time, Cabinet consisted of the former Interim Superintendent, who concurrently served as CFO; former Deputy Superintendent of Academics and Technology; former Deputy Superintendent of Administration; Chief Academic Officer; Chief Human Capital Management Officer; General Counsel; Chief Communications Officer; former Chief Organizational Transformation and Innovation Officer; and former Chief of Police Services.

Internal Audit requested that HR identify the positions added as a result of the staffing guideline revisions. HR initially identified 77 additional positions; however, subsequent information provided by HR reflected a net increase of 134 positions. Internal Audit's review also identified inconsistencies between the information provided and the District's position inventory records in Frontline, including differences in the status of certain positions. As a result, Internal Audit was unable to independently verify the precise number of positions attributable to the staffing guideline revisions. These inconsistencies indicate weaknesses in the maintenance and monitoring of position inventory and limit the District's ability to accurately quantify the operational and financial impact of staffing changes.

However, Internal Audit reviewed the methodology and calculations used by Financial Services to estimate the associated payroll impact and determined the analysis was sufficiently reliable for the purposes of this review. Based on that analysis, the staffing guideline revisions resulted in approximately $2.35 million in additional General Fund expenditures.

Interviews further indicated that funding was neither formally discussed nor validated before implementation:

1. Interviews with four current senior leadership members who served in cabinet-level roles during budget development and implementation (former Deputy Superintendent of Academics and Technology, Chief Communications Officer, Chief Human Capital Management Officer, and Chief Academic Officer) reported that discussions focused on operational and programmatic needs and did not include the anticipated cost of the positions, funding source, or budget impact.

2. The Senior Director of Talent Acquisition & Personnel Administration stated that HR processed the staffing changes based on Senior Leadership direction and assumed funding had been secured. However, she stated that HR was not involved in funding discussions and did not verify funding availability prior to establishing the positions.

3. The Assistant Superintendent of Specialized Services was unable to identify the precise number of positions added or the associated financial impact of the staffing guideline revisions.

4. The Comptroller and Director of BEFM confirmed that no budget transfer was processed, and no budget was established to fund the positions, despite the creation of position control numbers (PCNs).

The staffing guideline revisions were approved and implemented without a documented evaluation of funding availability, identification of a funding source, or assessment of the budgetary impact. In addition, the associated expenditures were not timely incorporated into the budget amendment process.

Board Policy CE(LEGAL) requires expenditures not included in the adopted budget to be incorporated through the budget amendment process. Although a budget amendment was ultimately approved in June 2026, the financial impact of the staffing changes was not incorporated into the budget until after the positions had been approved and implemented.

Recommendations and Management's Response

5.1 District leadership should establish and implement a formal review and approval process for staffing changes and revisions to staffing guidelines. The process should require:

  a. A documented cost analysis that identifies the estimated number of positions to be added, modified, or removed and the estimated financial impact of the proposed change.

b. Verification by BEFM and Financial Services that funding sources have been identified and sufficient funding is available before approval.
c. Review and approval by HR, BEFM, Financial Services, and the Superintendent before implementation of staffing changes with a material financial impact.
d. Evaluation of whether the proposed staffing changes require incorporation into the budget amendment process and, when applicable, timely presentation to the Board.
e. Post-implementation verification and reporting to confirm the number of positions added, modified, or removed, the actual financial impact of the staffing changes, and whether the changes remain within approved budget authority.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity 7.

Persons Responsible and Accountable: Chief Human Capital Management Officer, Chief Financial Officer, and Deputy Superintendent of Operations and Support Systems

Implementation Date: September 30, 2026

5.2 District leadership should establish procedures to maintain and monitor the District's position inventory listing. Procedures at a minimum should require:
a. Tracking positions added, removed, frozen, or modified throughout the fiscal year.
b. Periodic reconciliation of approved positions, position control numbers, and budgeted staffing levels.
c. Calculation and documentation of the financial impact associated with staffing changes.
d. Communication of material staffing changes and related budget impacts to the Superintendent budget monitoring and reporting purposes.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity number 7.

Persons Responsible and Accountable: Chief Human Capital Management Officer, CFO, and Deputy Superintendent of Operations and Support Systems

Implementation Date: September 30, 2026

Finding 6

HSA has not been budgeted from inception, with costs absorbed by the General Fund, costs incurred year to date are

According to the Comptroller, the District has historically not budgeted for Health Savings Account (HSA) disbursements at the directive of the former CFO. Instead, the Health Savings Account (HSA) costs were allocated to the funding source that paid an employee's salary. As most District employees are funded through the General Fund (199), most HSA costs were charged to the General Fund.

The Director of Employee Benefits indicated he was not aware that the HSA was excluded from the budget until May 19, 2026. The Comptroller and Director of BEFM stated that they communicated to the former CFO that HSA disbursement costs should be included in the budget based on anticipated expenditures. According to both individuals, the former CFO directed that HSA costs not be included in the budget.

approximately $2.98 M

Health Savings Account disbursements began in September 2019 at $250 per employee for employees enrolled in the Consumer-Driven Health Plan (CDHP). Beginning in 2023, the District increased its employer HSA disbursement to $1,000 per enrolled employee. As CDHP enrollment increased, annual HSA disbursement costs also increased.

As of June 10, 2026, the District has incurred approximately $2.98 million in HSA expenditures that were not included in the approved budget. This contributed to unfavorable budget variances during a fiscal year in which the District had already adopted a budget with a projected deficit. The omission reduced budget transparency and the reliability of budget-to-actual comparisons, weakening budgetary control. See **Table 2** for details of HSA historical costs.

Table 2: HSA Disbursements From 2020 to 2026

Year	Disbursement Amount	Fund 199 HSA Total Per Year
2020	$ 250.00	$ 857,033.29
2021	$ 500.00	$ 1,275,672.98
2022	$ 300.00	$ 753,977.17
2023	$ 1,000.00	$ 2,306,059.98
2024	$ 1,000.00	$ 2,671,251.94
2025	$ 1,000.00	$ 2,756,778.23
2026*	$ 1,000.00	$ 2,985,591.49
		$ 13,606,365.08

* As of June 10, 2026 - Year 2026 is not complete.

Board Policy CE(LOCAL) requires budget planning to reflect the District's programs, activities, and related resource requirements. Budget planning is intended to be an ongoing process that incorporates known and anticipated expenditures into the adopted budget. However, the former CFO, Comptroller, and BEFM Director did not include the anticipated cost of HSA contributions in the FY2025–2026 budget despite the expenditure being a recurring employee benefit with known historical costs.

Recommendation

Refer to recommendation 4.1.

Finding 7

$1.03M in TRA compensation costs for federally funded employees were absorbed by the General Fund

After adoption of the FY2025–2026 budget, the BEFM Office, Financial Services, and Treasury Department identified that Teacher Retention Allotment (TRA) compensation attributable to federally funded teachers could not be charged to federal grants. The Texas Education Agency guidance requires the TRA portion of eligible teachers' salaries to be funded with state or local funds to avoid a noncompliant supplanting situation. The Comptroller stated that the former CFO was informed of the funding restrictions and the related financial impact in September 2025. According to the Comptroller, the former CFO directed staff to address the matter but did not instruct them to present or escalate the issue to the Board.

In September 2025, Financial Services updated payroll funding codes for approximately 202 federally funded teachers identified as TRA-eligible. As a result, the TRA portion of eligible employees' salaries was charged to the General Fund, while the base salary costs continued to be charged to federal grants. This change will result in approximately $1.03 million in TRA-related payroll expenditures being charged to the General Fund.

Although the District is expected to receive state TRA funding for eligible teachers, the corresponding General Fund expenditures were not included in the adopted FY2025–2026 budget, and no budget amendment was processed after the funding change was identified. This reduced budget transparency and limited the District's ability to effectively monitor and control General Fund expenditures.

According to the Chief Human Capital Management Officer, HR was not involved in determining funding allocations for TRA compensation for federally funded employees. Human Resources was also not aware of the resulting General Fund budget impact at the time payroll adjustments were made.

Board Policy CE(LEGAL) requires that expenditures be authorized through the adopted budget and provides a mechanism for budget amendments when additional expenditures become necessary during the fiscal year.

Recommendation and Management's Response

7.1 District leadership in coordination with the BEFM Office, Financial Services, and HR Department should develop and implement procedures to ensure TRA compensation for federally funded employees is properly identified, funded, and included in the budget. Procedures should at a minimum include:

a. Verifying eligibility for TRA compensation.
b. Identifying appropriate funding sources and ensuring TRA compensation is charged to state or local funds in accordance with federal requirements.
c. Reviewing payroll funding allocations to ensure they are correctly applied and maintained
d. Monitoring changes in employee eligibility, salary amounts, and TRA compensation, and updating payroll and budget records on a timely basis.
e. Establishing a coordinated review process among BEFM, Financial Services, and HR to ensure funding and budget impacts are identified before payroll changes are implemented.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity 8.

Persons Responsible and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems

Implementation Date: March 31, 2027

Finding 8

Approximately $627K of IDEA-B expenditures were reclassified to the General Fund due to late

The BEFM Office reclassified Special Education expenditures from IDEA-B federal funding to the General Fund after the Special Education staff submitted the IDEA-B grant application after the start of the grant performance period for program year 2026. According to the Comptroller, the former CFO was informed of the required reclassification through their regular financial briefings.

A timely budget amendment was not submitted to the Board for approval to incorporate the additional expenditures into the General Fund budget. Consequently, these expenditures that were anticipated to be funded through submission of the grant application

federal grant resources were absorbed by the General Fund, reducing budgetary transparency and contributing to the District's year-end budget deficit.

The Assistant Superintendent of Specialized Learning Services acknowledged that the 2025–2026 IDEA-B grant application was submitted on July 25, 2025, after the BEFM Office identified that July payroll expenditures would require funding from the new grant period. According to the Assistant Superintendent, the department believed the application could be submitted any time before the TEA's September 30 deadline and was unaware that expenditures incurred before grant approval would not qualify for reimbursement under the grant's performance period. The Assistant Superintendent further stated that procedures were subsequently implemented to ensure future applications are submitted before June 30.

On October 23, 2025, the Assistant Director of Grant Accounting and Reporting notified the Assistant Superintendent of Specialized Learning Services, via email, that $627,812 in SPED expenditures incurred between July 1 and July 24, 2025, were not eligible to be charged to the FY2026 IDEA-B grant. The communication thread that followed, which also included the Comptroller, BEFM Director, Director of Accounting and Financial Reporting, and Chief Academic Officer, stated that the ineligible expenditures consisted primarily of July payroll costs incurred before the grant became effective and mentioned a reclassification to the General Fund was needed.

To help prevent recurrence, the Assistant Superintendent of Specialized Learning Services stated that all Special Education department staff have been notified of the June 30 deadline for submitting the IDEA-B grant application, and calendar reminders have been established to ensure future applications are completed and submitted before the beginning of the grant performance period.

Board Policy CE (LEGAL) requires expenditures to be accounted for within the Board-approved budget and provides for budget amendments when additional expenditures or funding changes materially affect the adopted budget.

Recommendations and Management's Response

8.1 District leadership should establish procedures requiring expenditures that become ineligible for grant reimbursement, within established thresholds, and must be reclassified to the General Fund to be:
   a. Quantified and communicated to the Superintendent within 30 days of identification; and
   b. Assessed for budgetary impact to determine whether a Board-approved budget amendment is necessary based on the significance of the resulting General Fund expenditures.

   Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity 1e.

   Persons Responsible and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems

   Implementation Date: September 30, 2026.

Finding 9

In February and April 2026, the former CFO and Chief Human Capital Management Officer recommended, and the Board approved a Resign/Retire Early Notification Incentive Program providing eligible employees with incentive

Resign/retire early notification incentive program was proposed without a corresponding budget amendment

payments of up to $3,000. However, the anticipated financial impact of the program was not identified, documented, or communicated before Board approval was obtained. A subsequent budget amendment was approved by the Board on June 16, 2026, to help ensure year-end expenditures are aligned with functional appropriations.

A total of 224 employees elected to participate in the program, which will result in expenditures of approximately $672,000. Consequently, the District will incur expenditures that were not included in the Board-approved budget, reducing budget transparency and weakening the effectiveness of the District's budgetary control process.

The program was approved on February 2, 2026, expanded through an amendment approved on February 17, 2026, and later extended to April 21, 2026. The February 2 and April 21 agenda items did not identify a funding source or fiscal impact for the proposed incentive program. Although the February 17 agenda item identified the General Operating Fund as the funding source, the anticipated cost of the program was not quantified.

Board Policy CE(LEGAL) requires that expenditures be reflected in the Board-approved budget and provides for budget amendments when additional expenditures become known during the fiscal year. Accordingly, the anticipated financial impact of Board-approved programs should be evaluated and incorporated into the budget amendment process in a timely manner.

Recommendation and Management's Response

9.1 District leadership should implement a standardized process requiring a written Financial Impact Analysis for new proposed programs, initiatives, and unforeseen expenditures when they are proposed or become known based on established local thresholds. This analysis must be attached to the respective Board agenda item prior to Board consideration and must, at a minimum:

a. Determine all prospective funding sources.
b. Evaluate the short- and long-term financial impacts on each funding source.
c. Identify any direct or indirect impacts on the District's General Fund.
d. Determine if a budget amendment is required based on established legal and local thresholds.
e. Ensure that any required budget amendment is presented to the Board in a timely manner once costs are incurred or reliable cost estimates become available.

Management and Leadership Response: Concurred with recommendation and incorporated into the CAP as activity 9.

Persons Responsible: and Accountable: Chief Financial Officer and Deputy Superintendent of Operations and Support Systems

Implementation Date: October 31, 2026

Finding 10

Leadership transition expenditures included the former Superintendent's retirement settlement ($347,851), supplemental compensation for the Interim Superintendent ($60,556), and the annuity and relocation benefits for the newly hired Superintendent ($50,700).

Leadership transition costs increased General Fund expenditures by approximately $459K

On June 3, 2025, the Board approved the former Superintendent's voluntary retirement agreement and appointed the CFO as Interim Superintendent, effective June 16, 2025. On June 18, 2025, the Board approved the Interim Superintendent Agreement. By September 2025, approximately $408K of the eventual leadership transition costs were known or reasonably estimable. At that time, the former CFO was serving as Interim Superintendent while continuing to oversee the District's financial operations. Despite knowledge of the anticipated costs associated with the leadership transition, a budget amendment was not submitted to the Board for their approval.

A subsequent budget amendment was submitted to and approved by the Board on June 16, 2026, to help ensure year-end expenditures are aligned with functional appropriations.

Texas Education Code § 44.006(a) requires that public funds be expended only as provided in the budget adopted by the Board and authorizes budget amendments to address necessary unforeseen expenditures. Additionally, the job responsibilities of the CFO and Comptroller require them to monitor fund balances, oversee related financial activity, and ensure expenditures remain within budget limits and established fiscal practices.

Recommendation

Refer to recommendation 9.1.

Observation and Recommendations

During the course of our review, we identified a matter that, while not rising to the level of a finding, may be of interest to management and the Board in evaluating long-term planning, resource allocation, and operational risk. The observation presented below relates to a budgetary decision that was subsequently addressed through Board action; however, the circumstances surrounding the decision highlight opportunities to strengthen planning processes, evaluate long-term impacts of budget reductions, and ensure significant operational risks are appropriately considered during budget development.

Observation 1

Known technology replacement needs were excluded from the FY2025-2026 budget to reduce the budget deficit

During development of the FY2025–2026 budget, the planned 1:1 Chromebook student device refresh was excluded from the proposed technology budget as part of efforts to reduce the overall budget deficit. According to the former Deputy Superintendent of Academics and Technology, approximately $3–$4 million allocated for 1:1 testing devices was removed from the IST budget despite identified replacement needs and associated risks. This decision was not consistent with Board Policy CE (Local), which requires that budget planning align with program needs and ensure that sufficient resources are allocated to support effective program implementation.

On May 30, 2025, the former Deputy Superintendent of Academics Technology notified the former Superintendent and cabinet members (currently referred to as senior leadership) of the potential impact of not implementing the device refresh for the 2025–2026 school year.

On June 30, 2025, after the budget adoption, District staff were notified that updated Cambium state testing requirements would no longer support aging devices. District staff subsequently confirmed that approximately 7,690 students would not have compatible devices for STAAR and TELPAS testing and that continued use of the obsolete devices presented both instructional and security risks.

On August 19, 2025, IST and Procurement Services submitted an item to the Board seeking approval to acquire Chromebooks through a lease-purchase arrangement. The agenda item identified the FY2025–2026 General Operating Fund as the funding source. During the same meeting, a corresponding budget amendment was recommended by the Comptroller and approved by the Board.

Following Board approval, a Budget Change Request was approved on August 25, 2025, by the Director of BEFM. To fund the purchase, $500,000 was transferred to the Technology Equipment account from Insurance and Bonding Costs ($477,591) and Other Payroll Payments ($22,409) accounts.

As a result, the District entered into a lease agreement totaling $5.86 million over the course of four (4) years, including unplanned $500,000 in FY2025–2026 and $1.79 million annually beginning in FY2026-2027 through FY2028-2029.

Recommendations and Management's Response

Refer to recommendation 4.1.

Methodology

To achieve the review objectives, Internal Audit performed the following procedures:

1. Reviewed applicable state laws, Board policies, administrative procedures, and related department manuals for budget development, budget monitoring, and budget amendment requirements. Applicable relevant criteria are referenced throughout the report.

2. Reviewed and evaluated budget development, financial forecasting, budget monitoring, variance analysis, and budget amendment practices to assess how the District identified, communicated, and addressed changing financial conditions and budgetary impacts.

3. Reviewed and analyzed budgetary and financial records, including adopted budgets, budget amendments, financial forecasts, quarterly financial reports, position inventory listing, staffing information, and PEIMS reports, to identify significant variances and determine the factors contributing to the projected fiscal year 2025–2026 financial deficit.

4. Reviewed and evaluated documentation related to significant expenditure categories and budget assumptions identified during the review, including staffing guideline changes, personnel actions, incentive programs, federally funded position reallocations, health savings account contributions, technology purchases, and other transactions relevant to the review objectives.

5. Reviewed and evaluated ABRs, including approval documentation, funding sources, budgetary treatment, prior budget consideration, and associated expenditures, to assess their impact on the adopted budget.

6. Reviewed Regular and Special Board meeting and Board Finance Committee agendas, minutes, presentations, and recorded actions within the scope of the review to determine whether budget amendments were approved and whether significant financial risks, budgetary impacts, and emerging fiscal concerns were communicated to the Board and its Finance Committee.

7. Reviewed selected emails, electronic communications, and chat logs from the former Superintendent, former CFO, and Comptroller obtained from the District's systems to evaluate budget development activities, financial decision-making, and communications related to the review objectives.

8. Conducted interviews with 25 District employees and the five (5) current Board Trustees, and spoke to the former CFO to corroborate information, understand relevant processes and decision-making, assess governance and oversight practices, and evaluate the identification, monitoring, communication, and management of significant financial risks.

9. Corroborated information obtained through interviews with documentary evidence, financial records, Board records, and electronic communications to assess the accuracy, consistency, and completeness of information relevant to the review objectives.

Internal Audit

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