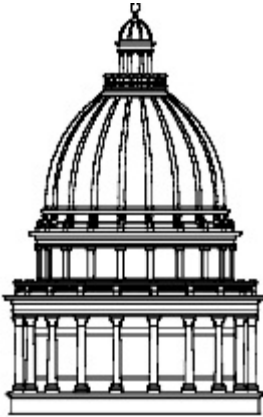


Offices of the
LEGISLATIVE AUDITOR GENERAL
and
LEGISLATIVE FISCAL ANALYST
State of Utah



January 2006

A Review of SITLA's Administrative Compensation

School and Institutional Trust Land Administration (SITLA) administrators are well compensated compared to their peers in state government and other Western states' trust land organizations. A key element of their compensation and a legislative concern has been SITLA's bonus program, which since 1997 has paid out almost \$2 million in bonuses. Annual bonuses are paid to the entire permanent staff and range from \$2,000 to \$40,000 per person, per year. SITLA's board created the bonus program as a staff inducement to create value for the organization. With these bonuses, SITLA's administrators are compensated, on average, 26 percent higher than their counterparts in Utah state government and trust land management organizations in other states. Few of the surveyed organizations pay bonuses, and none approach the bonus levels of SITLA.

SITLA cites, in defense of the bonus program, the organization's outstanding financial performance, specifically, increases in annual revenues. However, we believe that SITLA's increased revenues are not due to organizational performance as much as increases in natural gas and oil prices as well as an expanded land sales program—most recently selling prime trust land. Further, based on a review of historical revenues earned, we believe that revenue goals are set unrealistically low, making them easily attainable. Revenue goals are

set lower than the prior year's earned net revenue and as a result, SITLA has always met its revenue goals. See Appendices 1 and 2 for the historical patterns of mineral revenue, total revenue, and distributions to beneficiaries.

Much of Bonus Program Is Based on Market-Driven Factors

The majority of SITLA's bonus program is based on reaching net revenue goals that are primarily based on natural gas and oil prices and an expanded land sales program. Often revenue goals are set lower than the prior year's earned net revenue, and as a result, SITLA's administrators have always met the revenue goals. In addition to monetary goals, the board also sets annual non-monetary goals for senior management. When SITLA was created, *Utah Code 53C-1-201(3)(d)(v)* allowed the board to create an annual incentive and bonus plan for the director and other administration employees based upon the attainment of financial performance goals and other measurable criteria defined and budgeted in advance by the board.

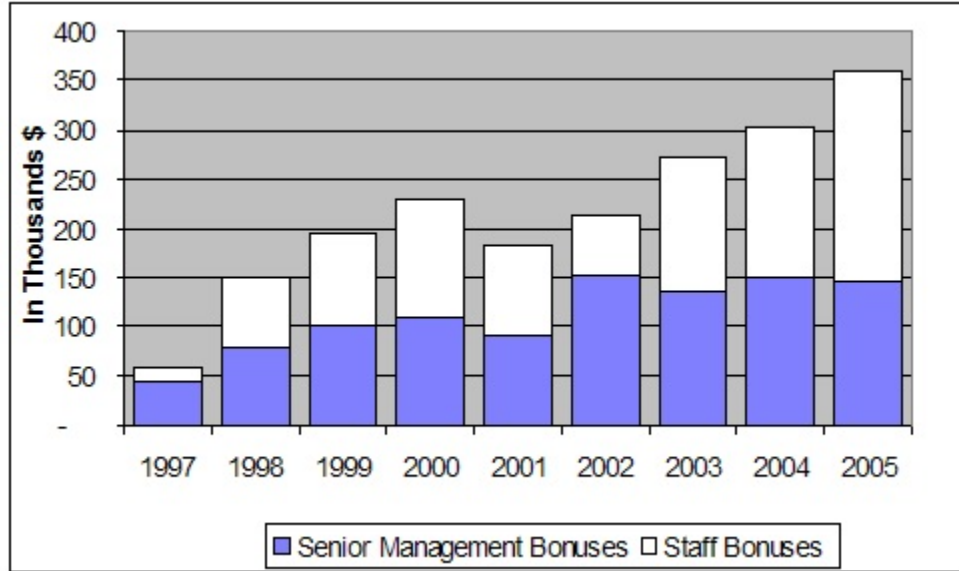
Revenues from natural gas, oil, and minerals produced on state lands consistently provide the majority of SITLA's operating revenues. A 446 percent increase in natural gas prices, from 1995 to 2005, significantly increased SITLA's revenues. SITLA's increased revenues also reflect an increase in land sales from \$600,000 in 1995 to \$23 million in 2005. As a result of increased revenues, the agency has paid out almost \$2 million in bonuses—with \$1 million going to senior management and the other million distributed in a second bonus program to the remaining agency staff.

Both Bonus Programs Have Grown

SITLA's two bonus programs are primarily based on revenue growth. Half of the bonus program for senior management and all of the agency staff bonus is based on SITLA achieving revenue goals established by the board each year. SITLA has achieved the revenue goals each year, and all senior management and staff have been rewarded with available bonus money as a result. Figure 1 demonstrates the growth in the bonus program.

SITLA has paid nearly \$2 million in bonuses since they became an independent state agency.

Figure 1 SITLA's Bonus Program Has Grown Over Time. Since fiscal year 1997, total bonuses have increased from \$59,000 per year to \$359,000 per year for a total of almost \$2 million.



The bonus program was created when SITLA was created.

Legislation allowed, and SITLA's board established, the bonus program when SITLA separated from state controls in 1994. The program's objective was to reward senior management for achieving revenue goals and becoming more efficient and effective, thus adding value to the organization. The first bonus payments were made to five senior managers in 1997. One year later, a second bonus program was created to reward the remaining SITLA staff.

Senior Management Bonuses Have Grown. The board rewards senior managers for exceeding specific board-established goals. One-half of the bonus is based on reaching a net revenue goal, and the other half is based on specific non-monetary goals established in conjunction with SITLA's director. Since the board bonus started in 1997, SITLA's senior managers have received a total of \$1 million in bonuses, ranging from \$4,500 to \$40,000 per person per year. Some of these amounts are higher than the \$8,000 annual cap currently allowed by Utah's Department of Human Resources Management rules. However, since SITLA's senior management is exempt from DHRM rules and SITLA is an independent state agency, these bonuses do not violate any rules or state laws.

Staff Bonuses Have Grown. Under this director-administered plan, all permanent employees are eligible for \$2,000 per year or a portion thereof based on full-time status. Additional bonuses are given to select employees, with a few employees receiving bonuses as high as \$10,500 per year. The plan was started as a result of complaints by the staff for not being rewarded for their contributions to reaching the overall revenue goal. This plan grew from \$70,750 in fiscal year 1998 to \$212,700 in fiscal year 2005, for a total payout of \$952,000. Prior to fiscal year 1998 a few select employees received bonuses.

Although SITLA pays large bonuses to senior management and bonuses to all permanent staff, few of the surveyed organizations reported paying bonuses. Only one other state trust land organization paid bonuses to five of the surveyed jobs. The bonuses ranged from \$139 to \$1,000 per year and averaged about \$400. One of the two independent entities paid bonuses to three of the surveyed jobs ranging from \$750 to \$10,000 and averaging \$3,833. Lastly, the BLM paid bonuses to two of the surveyed jobs. Awards ranged from \$364 to \$4,500. BLM noted that awards higher than \$4,500 were rare.

Revenue Goals May Be Inappropriate

One-half of the bonus for senior management and all of the bonuses for agency staff are based on reaching a net revenue goal set by the board. Net revenue is affected by the market prices of natural gas and oil and selling land—most recently selling prime trust land. Further, based on a review of historical revenues earned, the incentive program goal thresholds have been easily attainable. There are concerns by some within the agency that the bonus is tied to the market prices of oil and gas, which they cannot control. Legislators have raised concerns questioning the difficulty in attaining SITLA's goals that leads to such sizeable bonuses.

Revenue Goals Are Unrealistically Low. SITLA's board began the bonus program with a revenue goal of \$12 million and has increased the goal each year. However, the revenue increases have not reflected the actual net earnings of the agency. Although the board has increased the revenue goal each year, the annual increase has not always met the actual revenues earned by the agency in the previous year. This is due largely to the market-driven price fluctuations of natural gas and oil, and land sales.

Revenue goals for the bonus program are often set lower than the prior year's net earnings.

Figure 2 Revenue Goals for Monetary Portion of Board Bonus and Actual Revenue Earned by SITLA, Fiscal Years 1997-2005. SITLA's revenue goals have increased each year; however, they have not kept up with actual earnings by the agency.

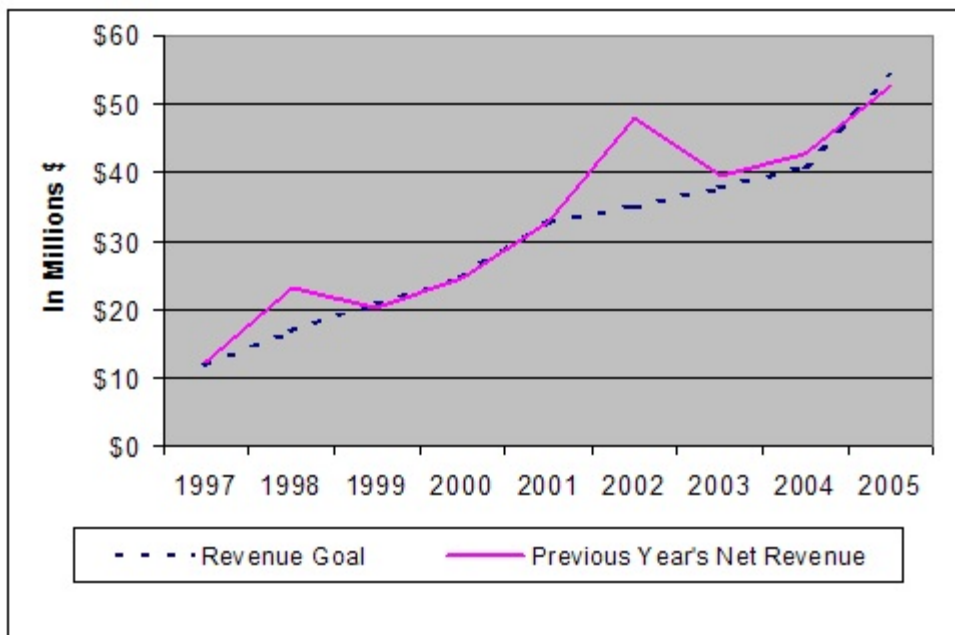


Figure 2 shows that revenue goal are often set lower than the prior year's earned revenue. As a result, SITLA has always met its revenue goals. It is concerning that the board-established revenue goals are usually lower than the prior year's generated revenue. This practice seems contrary to business principles of setting goals beyond the previous year's achievement. According to the Board chair and vice chair, the board bonuses focus the entire organization on forward thinking goals that are not easily attainable but are realistic.

Board Also Sets Non-Monetary Goals

In addition to revenue goals, SITLA's board sets annual non-monetary goals that allow senior management to share up to \$75,000 if the goals are realized. The board determines goals, bonus values, and agency priorities. At the end of the fiscal year, the board determines what percentage of the goal was attained and generates an associated bonus value. The 2005 objectives included:

- Implement a tactical plan for coal resources.
- Identify and rank for acquisition all producing and prospective federal oil and gas areas.
- Develop a forward looking business plan to govern the Planning/ Development Group's real estate activities over the next 10 years.
- Develop and implement a pilot biological management strategy on a selected block.
- Develop a plan for the prudent expenditure of monies received from the appropriation of OHV registration fees.
- Address outstanding in-lieu selection issues of concern to the beneficiaries.
- Take necessary steps to position Administration to pursue exchange opportunities.
- Merge the two ownership databases managed by the Administration so that "real-time" map making can be performed.

In fiscal year 2005, each non-monetary objective was worth \$10,000, except merging the databases, which was worth \$5,000.

The board has awarded additional bonuses to employees. The reasons vary widely as to why these bonuses were awarded. Some staff have received \$2,000 for completing a special project, while others were awarded \$1,000 each for a well-planned 10th anniversary party.

SITLA Total Compensation Appears High

Selected SITLA administrative and support staff job compensation is generally higher than that of comparable jobs in other states and organizations. It appears that neither span of control nor job responsibilities provide justification for the increased compensation. SITLA's jobs are generally equivalent to those of the surveyed organizations. Since SITLA was created, personnel expenditures have nearly doubled, while the number of new employees has increased by 37 percent. Personnel expense is the largest component of total expenses.

Administrative compensation has increased since 1994, when SITLA became an independent agency. At that time, *Utah Code* 53C-1-201(3)(d)(iv) provided:

“Salaries for exempted positions, except for the director, shall be set by the director, after consultation with the Director of the Department of Human Resource Management, within ranges approved by the board. The board and director shall consider salaries for similar positions in private enterprise and other public employment when setting salary ranges.”

We found no evidence that SITLA had considered salaries in the public sector or had any consultation with the Department of Human Resource Management. SITLA had only conducted compensation surveys for two staff positions—lands coordinator and resource specialist.

Since SITLA had only conducted compensation surveys for two jobs, we conducted a compensation survey for 10 jobs. We used a job-content-benchmark methodology, commonly used by human resource management, where one group provides job descriptions to other groups and allows them to determine if they have similar positions in their organizations. Working closely with Utah’s Department of Human Resource Management, SITLA’s Human Resource Director and DNR’s Human Resource Director specific jobs were selected in similar organizations for a comparative compensation survey.

The survey was extensive and included questions regarding salary rates, annual bonuses, years of experience, number of employees supervised, level of education, and pay ranges. The survey was sent to 17 organizations, including trust land organizations in other states, the Federal Government’s Bureau of Land Management (BLM), two independent agencies in Utah, and the Department of Natural Resources (DNR). Thirteen of the 17 organizations responded with sufficient data. Data from two state land offices were not used because of their small size. See Appendix 3 for statistics from the surveyed organizations including original and current surface trust land grant acreage, number of FTEs, revenues, and operating budgets.

Administrative Compensation Is Higher than Comparable Organizations

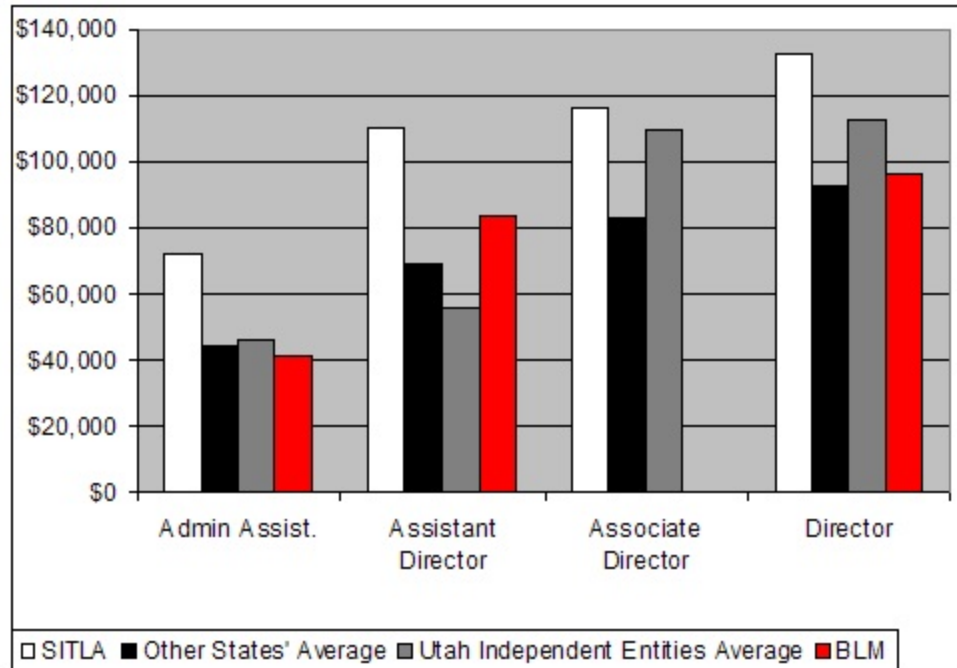
SITLA's compensation is higher than that of some comparable jobs in similar organizations.

SITLA's compensation measured higher than the compensation of comparable organizations in each of four administrative job categories: director, assistant director, associate director, and administrative assistant. In part, the higher SITLA compensation is due to higher board-set salary ranges. Additionally, other organizations give their employees little or no bonuses, while SITLA employees receive large bonuses.

The two independent entities were compared to SITLA, based on their similar staff sizes and operating budgets. Independent entities are created by the state and have a public purpose relating to the state or its citizens. SITLA's human resource specialist agreed with the use of these organizations. In addition, comparisons with other states' land trust organizations were based on benchmarked jobs developed with SITLA. Figure 3 graphically demonstrates the compensation for SITLA, seven other western trust land offices, the U.S. Bureau of Land Management (BLM) in Utah, and two comparably sized independent entities in Utah.

Figure 3 Actual Administrative Compensation Comparison (Salary & Bonus), Fiscal Year 2004. State trust land offices in seven western states, the BLM, and two independent entities in Utah report lower compensation than SITLA.

SITLA's administrators receive greater compensation than any of their respective counterparts.



With the exception of one independent entity director, SITLA's administrators receive greater compensation than any of their respective counterparts in all of the organizations that responded to the survey.

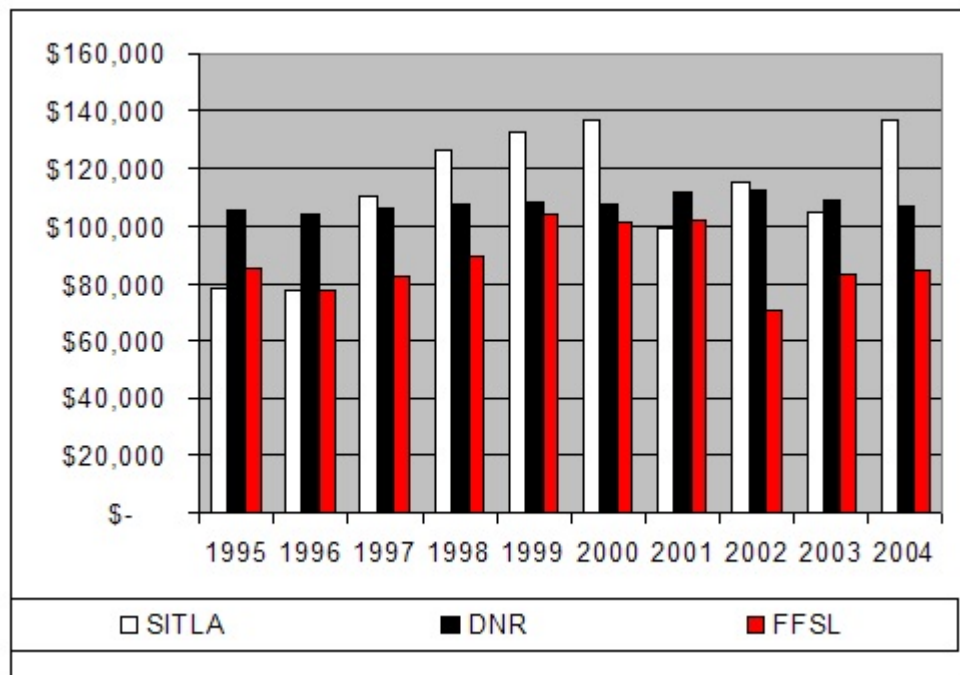
While SITLA's director is the highest paid trust land director, his experience level is not significantly different than some of his counterparts. The directors of other land management offices have significant work experience that they believe correlates well to the experience level necessary for an agency director. The deputy director of the BLM in Utah (whose job the BLM benchmarked with the SITLA director) has nearly as much experience, at 21 years, and makes about \$96,000. Some of the other states did not report years of experience because the equivalent job is an elected position. The BLM's benchmarked job manages 22.9 million acres of land in Utah, 6.5 times more land than SITLA's director. Yet the SITLA director's compensation is 38 percent more (\$36,000) than the BLM-benchmarked job in the Utah division.

SITLA's compensation has grown and surpassed rates of state government counterparts.

SITLA Compensation Surpasses the DNR

Compensation for SITLA's administration have surpassed the rates of their counterparts in the Department of Natural Resources (DNR), which was SITLA's previous departmental supervisor, and the Division of Forestry, Fire, and State Lands, (FFSL), which was SITLA's previous co-division member within the DNR. Figure 4 compares the directors' total compensation histories for each of these organizations.

Figure 4 Director Compensation Comparison (Inflation Adjusted), Fiscal Years 1995-2004. The total compensation of SITLA's director has increased much more rapidly than those of the executive director of the Department of Natural Resources and the division director of FFSL.



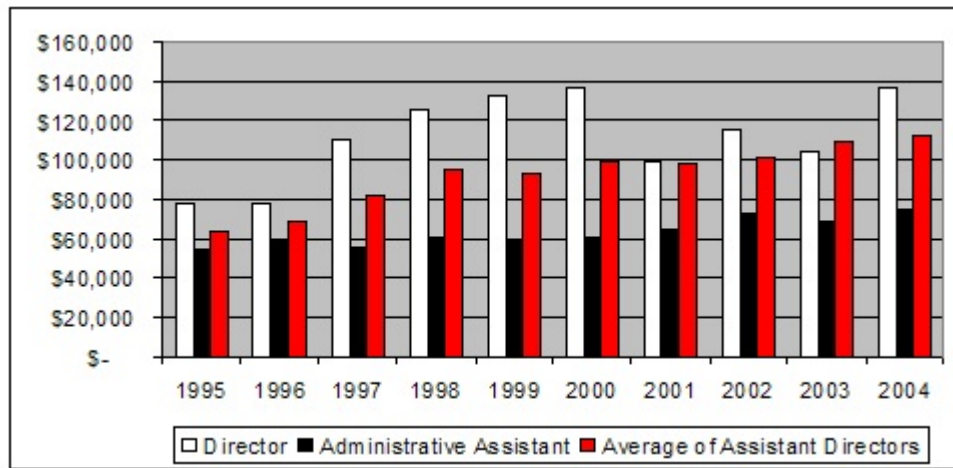
Beginning in 1997, the compensation for SITLA's director surpassed the level of compensation for DNR's executive director and continued to increase in subsequent years. In the years 2001-2003, a change in SITLA directors affected compensation. In 2004, the SITLA director's compensation was 28 percent higher than the compensation of DNR's executive director and 61 percent higher than the FFSL division director. The DNR executive director's salary includes a \$3,000 car allowance.

Since SITLA's creation, total compensation for senior management has grown by 75 percent.

Compensation Increases Occurred After Separation from the State

SITLA became an independent state agency in 1994. Since that time, total compensation for SITLA's senior administrators has grown, mostly due to the annual bonuses. Figure 5 shows total administrative compensation growth over the last 10 years.

Figure 5 Administrative Compensation Growth (Inflation Adjusted), Fiscal Years 1995-2004. Administrative compensation has grown steadily since separation.

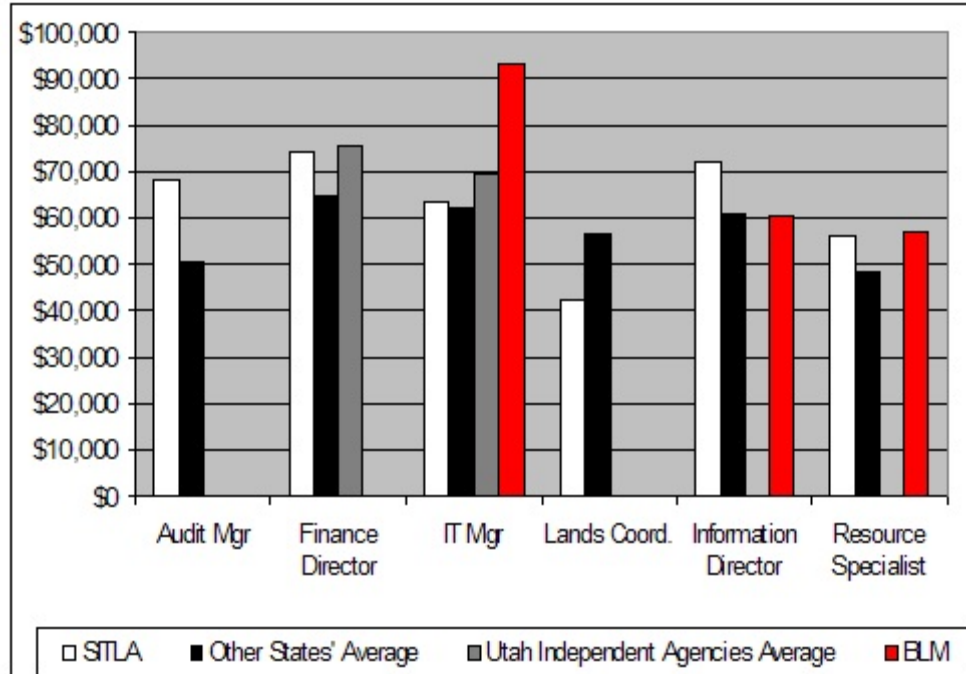


The director's and assistant directors' total compensation has grown by 76 percent since 1995. The administrative assistant's total compensation has grown by 36 percent. Several management changes from 2001-2003 resulted in a lower director's compensation during this period.

Support Staff Compensation Is More in Line with the Market

The compensation of most SITLA support staff are, for the most part, in line with compensation of their counterparts in other organizations. While some SITLA staff receive somewhat higher compensation, others receive less compensation than the other organizations. Figure 6 demonstrates key support staff compensation in greater detail.

Figure 6 Support Staff Compensation Comparison, Fiscal Year 2004. Some SITLA support staff compensation is greater than that of comparable organizations, while other compensation is similar or lower.



Note: Not all jobs were available in other state land organizations, independent entities, or the BLM.

When compared to positions in other state trust land organizations, some SITLA support staff positions receive higher-than-average compensation. However, when compared to other independent entities in Utah and the BLM, they receive similar or lower compensation. This analysis shows wide variations in the compensation for these support staff positions.

SITLA Has Similar Functions to Trust Land Organizations in Other Western States

SITLA, as an independent state agency, is thought by its board and administrators to have a unique status that justifies its salary and bonus structure. They believe that their salaries and bonuses should be compared to private trusts and major land developers. In our opinion, SITLA manages a public trust and not a private trust. There are major differences between private and public trusts according to the Western States Land Commissioners Association.

The majority of trust land organizations appear to be as independent as SITLA.

The majority of trust land organizations appear to be as independent as SITLA. We define an independent agency as one that deals exclusively with trust land issues and goals of its beneficiaries and is free from management from another agency. Furthermore, SITLA is an organization that manages lands that are more commensurate with other trust land organizations than with private land developers. Figure 7 lists the seven states used in the survey, their oversight entities and their management structures. For further information, see Appendix 3.

Figure 7 Oversight of Trust Land Organizations in a Selection of Western States. The majority of trust land organizations in other states are also independent.

State	Land Management Agency	Oversight Entity	Management Structure
Colorado	State Land Board	State Board of Land Commissioners	Division of DNR
Idaho	Idaho Department of Lands	Board of Land Commissioners	Independent
Montana	Trust Land Management Division	State Board of Land Commissioners	Division of DNR
New Mexico	State Land Office	State Land Office Advisory Board	Independent
Oregon	Department of State Lands	State Land Board	Independent
Utah	SITLA	Board of Trustees	Independent
Washington	Department of Natural Resources	Board of Natural Resources	Division of DNR
Wyoming	Office of State Lands and Investments	Board of Land Commissioners	Independent

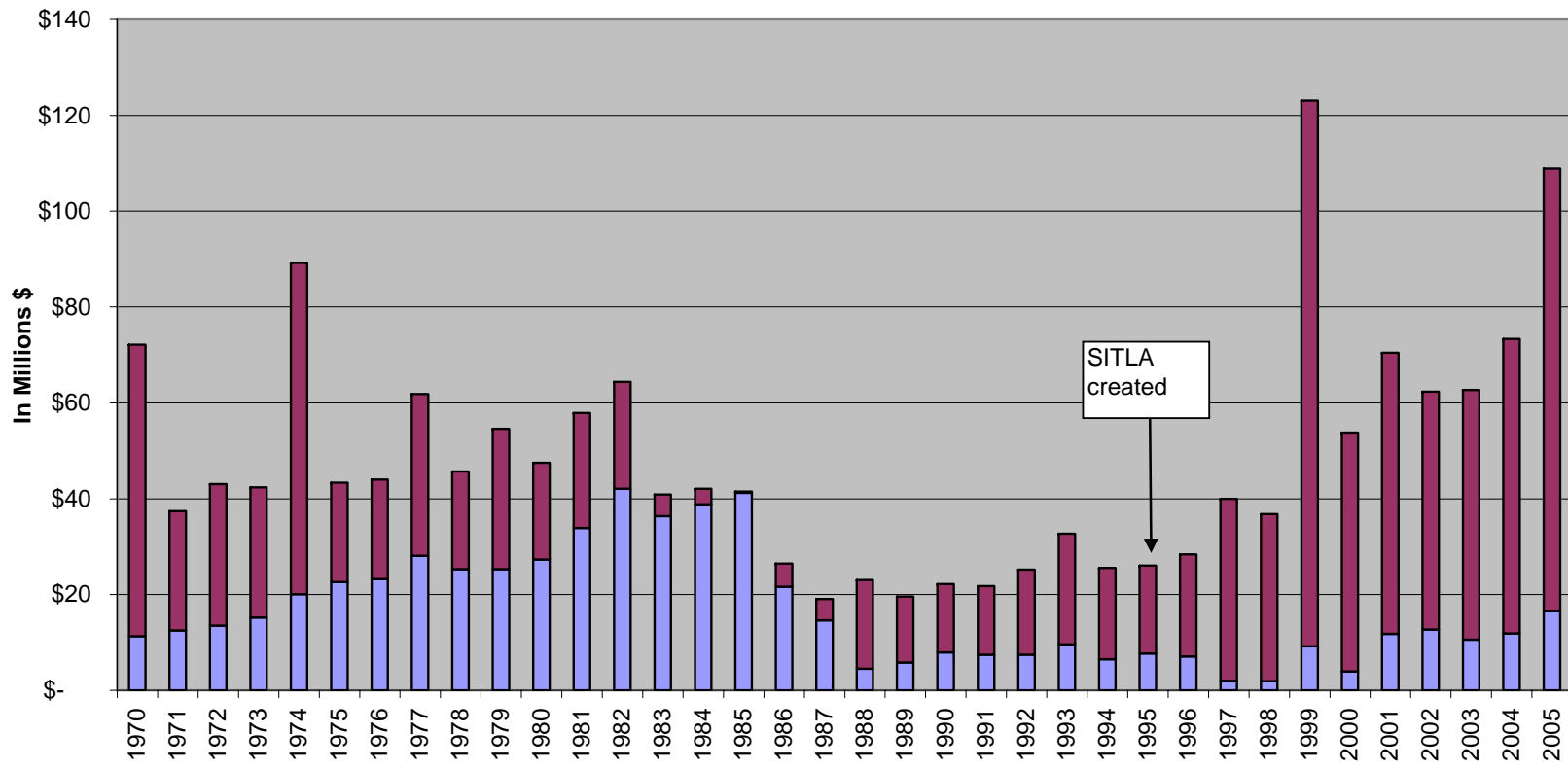
The duty of virtually all state trust land organizations is to provide revenue for current and future beneficiaries with the resources given the state at statehood. All land organizations face similar obstacles and challenges as they determine the best ways to utilize their resources within their fiduciary responsibilities.

Recommendations

1. We recommend that if bonuses continue, they be based on appropriate and measurable goals.
2. We recommend that the Legislature provide SITLA with guidelines for salaries and bonuses.

Appendices

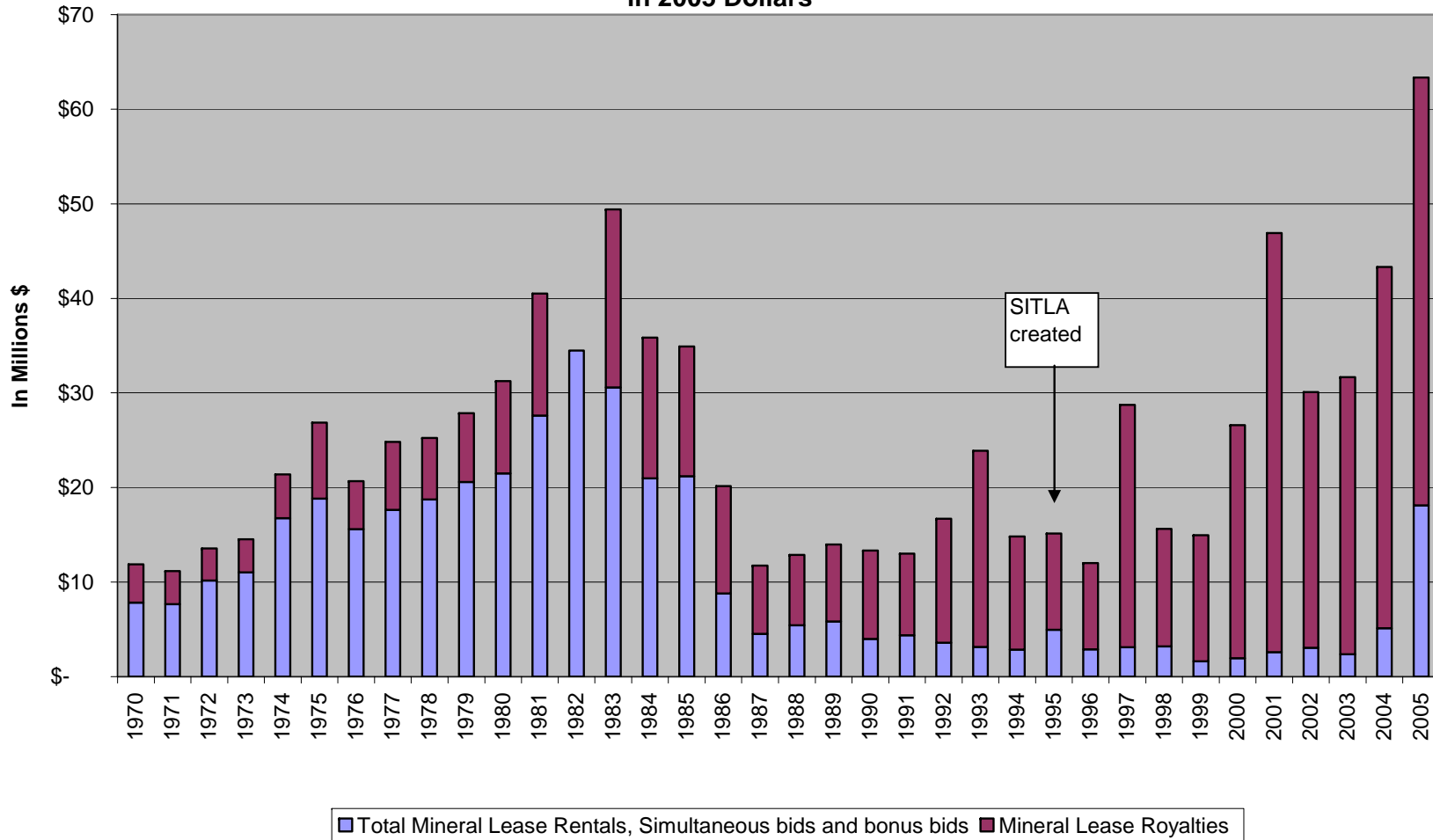
Appendix 1
Gross Revenues (Agency Earnings and Investment Earnings)
and Distributions to Beneficiaries
Fiscal Years 1970-2005
in 2005 Dollars



1999 - \$62.5 million extraordinary income

■ Distributions to Beneficiaries ■ Deposits to Permanent Fund or operating expenditures

**Appendix 2
Mineral Lease Rentals and Royalties
Fiscal Years 1970-2005
in 2005 Dollars**



Appendix 3

Statistics from Surveyed Organizations

Surveyed Organizations	Original Surface Trust Land Grant Acreage	FY 2004 Trust Land Holdings	FY 2004 Number of FTE's	FY 2004 Agency Revenues In Millions	FY 2004 Operating Budget in Millions
State Trust Land Organizations:					
New Mexico State Land Office	8.7	9.0	155	\$278.7	\$ 14.0
Washington DNR – Trust Lands Management Activities	2.4	2.8	770	215.9	23.6
Wyoming Office of State Lands and Investments	3.5	3.5	97	93.0	10.0
Idaho Department of Lands	3.0	2.2	29	65.6	4.6
Utah – SITLA	5.8	3.4	62	60.4	7.5
Montana Trust Land Management Division	5.2	5.1	108	46.3	5.2
Colorado Land Board	3.7	2.8	34	36.4	3.5
Oregon Department of State Lands	3.4	0.7	86	15.8	6.9
Other Organizations:					
Utah BLM, Lands & Minerals Division		22.0	38		
Utah Department of Natural Resources (DNR)			1,230		115.0
Utah Division of Forestry, Fire and State Lands (FFSL)			138		15.0
Utah Housing Corp. (Independent Entity)			55		3.5
Utah State Fair (Independent Entity)			50		3.5

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Agency Response



State of Utah

School and Institutional
TRUST LANDS ADMINISTRATION

COPY

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January 4, 2006

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Legislative Auditor General
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Mr. John E. Massey, Director
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Re: Review of Administrative Compensation -- School and Institutional Trust
Lands Administration

Dear Mr. Schaff:

On behalf of the Board of Trustees of the School and Institutional Trust Lands Administration ("SITLA"), thank you for the opportunity to respond to the above-referenced report concerning the compensation of SITLA management and staff. The Board of Trustees is responsible by statute for setting policies for the effective and profitable management of Utah's trust lands, including setting salary ranges for SITLA management and creating an annual incentive and bonus plan. The Board welcomes input and guidance from the Legislative Auditor General and the Utah legislature, in light of the legislature's role as the ultimate trustee over management of trust lands. While the Board does disagree with several conclusions reached by the review, as described below, we share your goal that Utah's trust lands be managed prudently for the long-term benefit of the trust beneficiaries, and we look forward to working with the Legislature to address any concerns raised by the review. We specifically plan, in light of the concerns raised by the review, to undertake an independent professional review of SITLA management compensation prior to finalizing such compensation for the upcoming fiscal year.

Summary of Board Response

(1) The salary review compares SITLA management salaries only to those of other government employees. This fails to take into account the Utah legislature's express directive in *Utah Code Ann.* § 53C-1-201(3)(d)(iv) that compensation for SITLA management should be based upon compensation for similar positions in private enterprise as well as in other public employment. The Board of Trustees, in keeping with

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the legislature's directive, has applied its best business judgment in setting compensation for SITLA management, based upon the need to retain qualified staff in competition with the private sector, and upon the value added by their activities for the benefit of the trust beneficiaries.

(2) The report contends that SITLA's increased revenues were the result of higher mineral prices in recent years, rather than any particular actions by SITLA managers. The Board believes that SITLA's actions have played a large role in creating opportunities to capitalize on higher mineral prices, including through acquisition of federal lands with major energy resources through land exchanges. We note that SITLA has substantially outperformed state land management agencies in other western states that also rely upon mineral revenues for substantial portions of their income, and we believe that value added by SITLA management has substantially contributed to this outperformance.

(3) In the Board's business judgment, the revenue goals upon which a portion of SITLA's management bonuses were based have not been set unrealistically low. During the initial portion of the period in question, the goals were based upon compounded annual operating income growth of 15%, and the goals have subsequently been increased substantially. We believe that this type of benchmarking is consistent with practice in the private sector. Bonuses paid to SITLA management constitute less than 2/10 of 1% of agency revenues since inception, and the Board believes that these amounts are reasonable under the circumstances.

Background

SITLA was created by the Utah legislature in 1994 to apply businesslike management practices to the management of the state's trust lands. Prior to that time, Utah had consistently underperformed the other western states in using its trust lands to build permanent endowments for the support of the state's public schools and other public institutions. In a survey of the western states' permanent funds and trust lands revenues in 1990, Utah ranked dead last among the public lands states in its accumulated permanent funds, and in the bottom three in annual income.¹ Based in part on this underperformance, the Utah legislature created the School and Institutional Trust Lands Advisory Board in 1993 to undertake a comprehensive review of trust lands management and policy.

The Trust Lands Advisory Board determined that the appropriate policy for trust lands was for the management agency to operate like a business, with reasonable

¹ J. Souder & S. Fairfax, *State Trust Lands* (University Press of Kansas 1990), Tables 2.5, 2.6.

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independence from the state's bureaucratic structures, so that it could respond in a timely fashion to business opportunities.² The Advisory Board recommended that compensation for the trust land manager should be market-based, with reference to similar private and public positions, and should include bonuses based upon factors similar to those used for private sector executives, as the Board found appropriate.³

These concepts were expressly adopted by the Utah legislature when it adopted the Utah Trust Lands Management Act in 1994. The Board of Trustees, each member of which is required to have outstanding professional qualifications in areas of business, real estate and asset management, acts as the equivalent of a corporate board in directing management of SITLA, including the hiring and compensation of the director. The Board of Trustees and the director are expressly directed by the Act to consider similar positions in private enterprise in setting management salaries.⁴ An annual incentive and bonus plan is authorized for the director and other SITLA employees based upon attainment of financial performance goals and other measurable criteria defined and budgeted in advance.⁵

The Board of Trustees believes that SITLA has fulfilled the intent of the legislature to bring competent, focused and businesslike management to the management of Utah's trust lands. In the 11 years since SITLA was created, Utah's permanent school fund has increased from \$85.6 million in 1994 (the entire amount accrued in the 98 years since statehood) to over \$580 million today. Instead of being dead last among the 23 public lands states, Utah is now solidly in the middle in terms of permanent fund size. Total trust assets (including the assets of other beneficiaries, but excluding the market value of trust lands) exceed \$680 million. Annual income has increased from slightly over \$14 million in 1994 to \$93.9 million in 2005, with over \$100 million in net revenues expected from SITLA operations in the current fiscal year.

Response to Review

1. Introduction.

The Board is composed of seven members, all of whom have lengthy experience in the business world, including the hiring and compensation of professional business

² *Statement of Intent for Management of School and Institutional Trust Lands*, School and Institutional Trust Lands Advisory Board (December 13, 1993) at 2.

³ Proposed H.B. 350 at 17-18.

⁴ *Utah Code Ann.* §53C-1-201(3)(d)(iv).

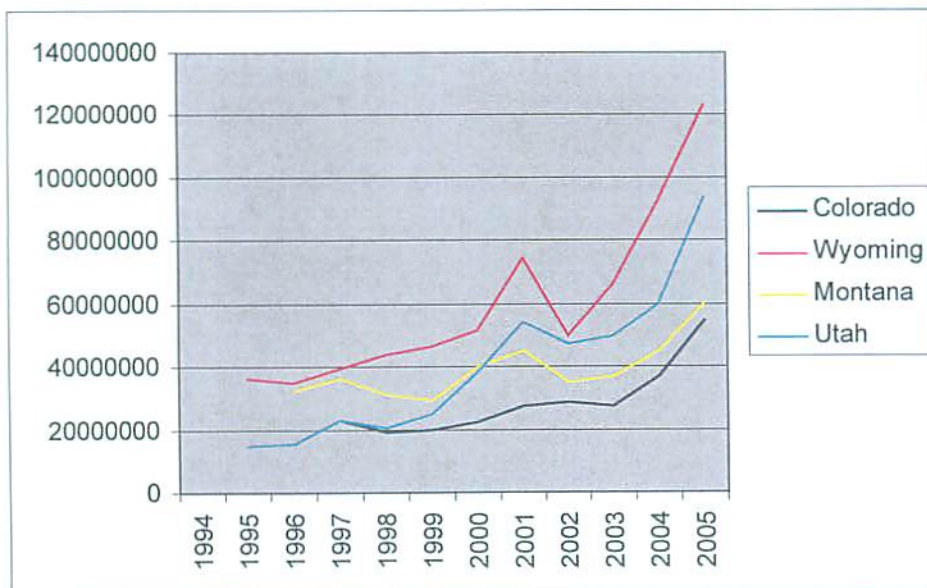
⁵ *Utah Code Ann.* §53C-1-201(3)(d)(v).

managers. In fulfilling the Legislature's guidance that the state's trust lands be managed profitably for the financial benefit of the trust beneficiaries, the Board has sought to hire and retain management for SITLA who have the skills, motivation and experience to add value to the state's land portfolio, rather than passively managing the lands as was the practice of land management agencies prior to SITLA.

2. The Salary Review Understates SITLA's Efforts In Increasing Revenue.

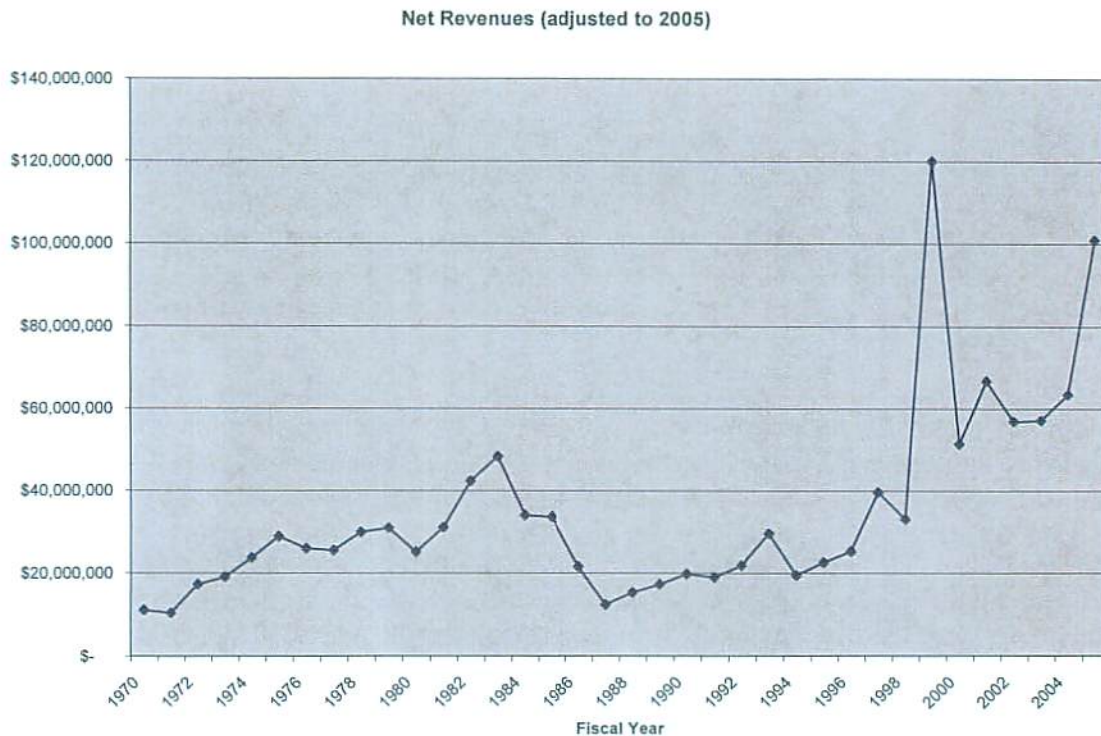
The Board of Trustees believes that the salary review incorrectly infers that increases in SITLA revenues, upon which the Board's incentive program was partially based, were mainly or solely the result of external forces rather than the efforts of agency staff. In particular, the review concludes that the bonus program is primarily linked to increased natural gas and oil prices and sales of "prime" trust land. In fact, during much of the period in question, natural resources prices were flat or down, but the agency was still able to significantly increase revenue year over year. In more recent years, when natural gas prices have risen greatly, SITLA's revenue growth has exceeded gas price growth by significant margins. A useful point of comparison is to look at other western states where commodity production forms a large portion of revenues, as depicted in Figure 1. Since 1994, Montana trust land revenues have increased 85%; Colorado revenues have increased 136%; and Wyoming revenues have increased 240%. During this same period, Utah trust land revenues increased 531%.

Figure 1:



Similarly, SITLA net revenues (which reflect amounts actually available for investment or distribution after the agency's expenses) have exceeded the historic high achieved by all prior agencies in every year since 2000, as depicted in Figure 2.

Figure 2.



The review also states that SITLA's revenue growth was based in part on the sale of "prime" trust lands. In fact, the agency's primary land sale program seeks to identify trust lands for sale where the returns that can be generated from investing the sales proceeds in financial assets exceed the income-generating potential of the property. Most of these lands are remote and rural rather than "prime" lands. The Board carefully watches to ensure that SITLA does not place property onto the market solely to meet revenue goals, and has by policy capped annual sales at \$3 million in appraised value to avoid any perception that the agency is liquidating lands. The \$50 million in cash received in the Grand Staircase Exchange was not counted toward income goals in the year received, and revenues received from any decision to market a large, valuable property would similarly be excluded from bonus calculations. Other significant sale revenues were generated from selling lands trapped within desert tortoise habitat which had no potential for future development. In most sales, we believe that value-added

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activities by the agency such as planning and marketing significantly increased values obtained.

3. The Review Does Not Mention the Small Relative Size of Bonus Compensation.

The Board of Trustees is concerned that the review creates a misleading impression by reporting the total bonuses paid to staff without reference to the total amount of revenue generated by the agency. Bonuses awarded by the Board to SITLA management total approximately \$1 million to date, with staff bonuses awarded by the director adding approximately \$952,000. Over the period in question, SITLA direct revenues were over \$520 million. In context, total bonuses paid to management comprised less than 2/10 of 1 percent of revenues, and staff bonuses a similarly small percentage. In light of the significant increases in trust revenues during this period, the Board believes that bonuses of this size are not excessive. The Board further notes that the primary criterion set by *Utah Code Ann. § 53C-1-201(d)(v)* for the award of bonuses is attainment of financial performance goals, which were in fact met. It might have been more informative to report these incentive amounts in context rather than standing alone.

4. Incentives for Performance Were Based Upon the Board's Business Judgment.

The Board's incentive bonuses for SITLA management have been based upon the agency's meeting both operating profit (i.e. revenue less operating expenses) goals, and non-monetary performance goals. With respect to the operating profit goals, the Board originally based its incentives on the goal of increasing net revenues by 15% per year, compounded annually, over a multi-year period, which the Board felt was a significantly difficult hurdle for management to reach, and a goal that would be deemed significant in the private sector. As the review notes, this policy resulted in the goal being below actual revenues for the prior year in some years. With increases in mineral revenue in the last several years as a result not only of increased resource prices but also because of the successful completion of two large land exchanges, the Board has increased the revenue goals by much more than a 15% compounded annual rate, but still at a level that the Board deemed achievable if management worked hard to achieve the goal, taking into account reasonable projections for agency revenues.

The Board of Trustees also believes that non-monetary performance objectives, which have comprised 50% of the management bonus program, are a worthy tool in guiding management performance in accordance with the Board's statutory role in setting policy to guide the agency. Our goal has been to use the non-monetary portion of the objectives to put SITLA in a position to capture future value through positioning the agency to take advantage of emerging opportunities. As an example, one Board priority

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in recent years has been to encourage SITLA management to prepare aggressively to pursue land exchanges with the United States. In furtherance of this policy, the Board directed the agency to take specific actions in preparation for an exchange of lands in the West Desert area. Lands identified as part of the incentive objective were ultimately acquired, and have since been included in a transaction for a solid waste facility that is expected to provide many millions of dollars for the school trust from one small portion of the exchange lands.

The Board of Trustees believes that the incentive program, properly managed, can be and is a valuable means to incentivize SITLA management to find new ways to generate revenue for the school trust, and to set the stage for future revenue growth. The goals set by the Board in past years have been carefully examined during the years in question, and reflect the Board's business judgment.

5. The Salary Review Does Not Consider Comparable Private Sector Positions.

The Utah legislature's intent in creating SITLA was for the agency to act in a businesslike manner in managing trust assets. In doing so, the legislature expressly directed that the Board and director consider similar positions in the private sector, as well as comparable public sector positions, in setting management salaries. *Utah Code Ann.* § 53C-1-201(3)(iv). The same statute provides for SITLA's director to consult with the director of the Division of Human Resource Management in setting salaries for exempt positions in the agency. The director in fact has done so, without adverse comment from the director of DHRM.

The Board of Trustees has attempted to follow all legislative directives in managing SITLA, and, more specifically, in compensating SITLA management. The Board has sought to retain management staff with significant private sector experience, who can add value to trust lands and assets rather than simply managing the lands in a custodial capacity. In contrast, the auditors considered only public sector jobs in their survey of "comparable" positions, and did not consider even public sector entities with a business focus (e.g. the Salt Lake Airport Authority, the Utah Transit Authority, etc.). While the data in the review is relevant, we feel it should take into account the legislature's direction that SITLA salaries be based upon both public and private salaries.

With respect to the first of the review's recommendations, the Board of Trustees concurs that any SITLA management bonuses should be based on appropriate and measurable goals. Prior to the commencement of the legislative audit, the Board

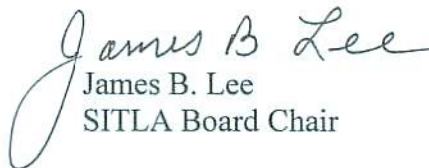
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appointed a subcommittee to examine bonus issues. This subcommittee is currently addressing issues such as the non-financial goals and modifying the financial goals so that more emphasis is given to achieving premiums over fair market value and other benchmarks rather than gross revenue.

With respect to the second of the review's recommendations, the Board looks forward to working with you, the Legislative Audit Committee, and the relevant appropriations committees to ensure that our compensation practices are open and appropriate. At the time that it considers compensation for the upcoming fiscal year, the Board will seek independent professional examination of both the incentive program and SITLA management salaries to ensure a fair compensation package that promotes hiring and retention of the best possible management team, while protecting the interests of the trust beneficiaries.

The Board of Trustees appreciates the opportunity for comment in connection with the review, and shares with you the common goal of causing Utah's trust lands to be managed prudently and profitably for the benefit of the trust beneficiaries. In the meantime, please feel free to contact any of us if you have any questions or comments, and thank you for your hard work.

FOR THE BOARD:


James B. Lee
SITLA Board Chair

SITLA Board Members:

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