DATE: July 13, 2001

State of Minnesota
PERA
Public Employees Retirement Association
Office Memorandum

TO: Members, Legislative Commission
on Pensions and Retirement

The Honorable Phyllis Kahn
MN House of Representatives

FROM: Gary Austin, TRA, Executive Director
Dave Bergstrom, MSRS, Executive Director
Mary Most Vanek, PERA, Executive Director

SUBJECT: 1999 Laws of Minnesota, Chapter 222, Article 22
Report on Consolidating Administrative Functions in Joint Office Facility

Enclosed is our report, required under the law noted above. As part of the discussion about the retirement systems constructing and jointly owning a building, we testified that we believed collocation would afford us opportunities to gain some administrative efficiencies. We were asked to prepare a report on some of the areas we believed would afford us that opportunity.

This is the report referred to in Chapter 10 of the 2001 Special Session Laws requiring that this report be used to establish a basis for the February 15, 2003, more detailed report on a plan to consolidate the administration of the three statewide retirement systems.

If you have any questions about anything contained in our report, please feel free to contact any one of us. We look forward to your questions and comments.

Introduction

The 1999 Laws of Minnesota, Chapter 222, Article 22, authorizing the three statewide retirement systems to jointly construct and own an office facility also required a report to be submitted to the Legislature by July 15, 2001, with a plan to consolidate administrative services. Specifically, the law states:

> "The executive directors of the Minnesota state retirement system, the public employees retirement association and the teachers retirement association must jointly report to the legislature by July 15, 2001, on a plan to consolidate administrative services for the three pension systems if the systems share a building."

The retirement systems sought approval to construct and jointly own a building after studying the economics of leasing compared to owning. We understood that the costs of paying off the principal and interest on the bonds would increase our costs in the initial years. Since the goal was to construct a building that would stand for a minimum of 50 years, the economics of owning rather than leasing were definitely weighted in our favor. All three of the statewide retirement systems have for years been leasing space from private entities with lease rates increasing on a regular basis and expected to go up significantly over the next several years.

In our testimony regarding why we wanted to construct a joint office facility, we asserted that we could achieve some efficiency by collocating. We also focused our attention on better service to our members. Thousands of public employees have service in more than one of our systems. Collocation of the retirement agencies facilitates "one-stop shopping" for these individuals.

We have prepared this report to include the steps we have taken and the planning discussions that are underway. Since we are not yet in the new building, we have not had the opportunity to explore more thoroughly all of the options. Additional information will be provided in the report we will submit by February 15, 2003, as required by 2001 Laws of Minnesota, First Special Session, Chapter 10.

Overview of the Retirement Systems

The Minnesota State Retirement System (MSRS) administers six defined benefit plans, a defined contribution plan for unclassified state employees and the State's deferred compensation program available to all public employees through payroll deduction by their employers. The defined benefit plans provide benefits to all general employees of the State, the State's correctional system personnel, the State Patrol, judges, legislators and elected state officers. The MSRS currently provides benefit coverage to about 53,000 active employees and 12,000 individuals who have left state employment but to whom benefits are owed when they reach retirement age. About 22,000 individuals currently receive retirement disability or survivor benefits from the system. As of the

most recent actuarial valuation on July 1, 2000, the System had assets of approximately $10.5 billion.

The Public Employees Retirement Association (PERA) administers three defined benefit plans and one defined contribution plan. The Regular defined benefit plan provides benefit coverage to about 150,000 individuals currently employed by cities, counties and those employed by the school districts in non-teaching employment positions. The PERA also has a plan covering about 10,000 city and county police and fire personnel and one for county correctional personnel with a membership of about 3,000. The defined contribution plan administered by PERA primarily covers local government elected officials with a membership of about 4,500. There are also approximately 22,000 individuals who have left local government employment to whom PERA owes benefits at the time the individuals reach retirement age, and payments are currently being made to over 55,000 individuals in the form of retirement, survivor or disability benefits. As of the most recent actuarial valuation on July 1, 2000, the Association had assets of about $15.6 billion.

The Teachers Retirement Association (TRA) administers one defined benefit plan for public school teachers and administrators throughout the state except for the teachers of the first class cities of Duluth, St. Paul and Minneapolis. The plan also includes members from the faculty of the state universities and community colleges. TRA currently has active membership of about 71,000 individuals and owes benefits to about 7,400 individuals who have left teaching covered by TRA, but who are entitled to benefits at retirement age. About 33,000 individuals are currently receiving retirement, survivor or disability benefits. As of the most recent actuarial valuation on July 1, 2000, the TRA had assets of about $17.7 billion.

Current Shared Administrative Activities

Asset Investment -- The assets of the three statewide retirement plans are invested by the State Board of Investment (SBI). The co-mingling of these assets for investment purposes allows less expensive investment administration and management. The SBI allocates investment expenses to the three plans on a prorated basis determined by the percentage of the assets owned by each plan.

Computer Links – Each of the three plans have their own information systems divisions and platforms to accommodate their specific data collection and record-keeping needs. The Benefits processing staff members have read-only access to data stored in other retirement plans' data systems, but due to the differences in the technology platforms, do not have the capability to change data or bring it directly into a benefit calculation program used by a different plan. The computer links are extremely helpful in getting to service credit and salary information when responding to requests for information from members with service in more than one plan.

Administrative Functions to be shared in Joint Facility

Board Room – An approximately 1,100 square foot meeting room was designed for the first floor of the building for use by all three boards and other tenants. The room includes built-in sound and tape recording systems, which eliminates the need for each of the retirement systems and SBI to own and maintain their own sophisticated recording systems for purposes of recording board meetings.

Training Room – Currently TRA and PERA have meeting room space n their separate facilities designed to accommodate educational programs for members, employers and staff. The new facility design includes a 2,700 square foot meeting room to be shared by TRA and PERA for the same purpose. This meeting space will also be available for use by other tenants of the building. There is another smaller meeting room designed specifically for computer training to be used by PERA and TRA, and if needed, by other tenants.

Mail Delivery Services – The State's Central Mail distribution services currently serve the retirement systems and SBI at their separate locations in the City of St. Paul. Once the retirement systems are moved into the new facility, mail will be delivered by the State's Central Mail staff to PERA, and other agencies will be contacted by PERA for daily pick-up in the PERA suite of offices.

Courier Services – Each of the retirement systems has a staff person assigned to providing courier services for their specific agency. Courier services are needed to pick up mail at the main post office so that checks for payment of contributions can be processed and deposited timely and to daily take back-up tapes off-site for disaster recovery storage purposes. While this is a job responsibility incorporated into a broader administrative position, three different individuals currently handle it since the retirement systems are housed in different locations. Upon moving into the new facility, one individual will be assigned this responsibility for all three agencies.

Communication and publications – MSRS and PERA are exploring the option of teaming staff responsible for the design, writing and layout of a variety of informational materials provided to members of the plans. The informational materials to be provided are similar in many ways, although there are important distinctions in provisions of the MSRS and PERA plans.

We expect this teaming arrangement could stimulate more creativity through the exchange of ideas, but most importantly we are hoping to reduce the need for additional staff in either of the two agencies. The intent is to have trained back-ups between the two agencies in this very specialized field.

Joint Educational Programs in Greater Minnesota -- TRA and PERA each provide educational programs to explain the reporting requirements of the plans to payroll and personnel officers of the school districts and other local governmental entities (cities, counties, townships, etc.). This fall, the two agencies are planning to conduct joint

sessions for school district personnel in order to share the cost of these out-state educational programs, thus reducing the cost of the programs by avoiding duplication of effort and meeting facility, equipment, and car rental expenses.

This joint effort is very timely as PERA rolls out the collection of hours for the purpose of prorating service credit for new members as of January 1, 2002. The reporting requirements for determining allowable credited service for teachers is very different than that being developed for PERA-covered participants. The joint sessions will allow staff to address questions on the differences and help facilitate some joint efforts to assist school districts and their regional computer services in adapting to PERA's new reporting requirements.

Satellite offices – Plans are currently underway to establish satellite offices in other areas of the state to house at least one full-time staff person from each of the systems. The thoughts are to have individuals cross-trained on the benefits of all the plans. Staff will be asked to accommodate individual counseling, process benefit applications, and facilitate the educational programs in the areas in which the offices will be located.

MSRS and TRA are currently planning for an office in St. Cloud to be opened the beginning of 2002 as a pilot project. The PERA Board has chosen not to participate at this time, but will reevaluate this option in the future.

Current Information Systems Structures

One of the areas of interest from at least one member of the Legislature who requested this report was the potential for consolidating the information systems divisions of the three retirement systems. We thought it would first be instructive to explain our current structures and recent work undertaken to update those operations. With members becoming more educated about retirement, we needed better information system structures to more effectively meet the demands for providing service and information to our memberships and to meet the increase in retirements expected as the baby boom generation moves into the next phase of their lives.

Minnesota State Retirement System (MSRS)

The MSRS collects individual personal data and service and salary data from one major employer, the State, through its Central Payroll processing division. While there are a few other smaller entities reporting personal data on members to MSRS, the majority of the information the retirement system collects comes from Central Payroll.

The MSRS database, where all record keeping for the participants in all of the retirement plans administered by the System is done, is on Intertech's mainframe computer systems. Connectivity between the MSRS Local Area Network (LAN) and Intertech is done through MNET, the state's wide area network. Disaster recovery of MSRS operations is coordinated with Intertech, and the database is backed up daily to

two separate locations. The MSRS expects to continue to do the bulk of data processing for their operations on Intertech's mainframe for several years to come. In August 2000, MSRS introduced its interactive Web site. The site allows participants to access account values and calculate retirement estimates. To date, 2,200 different members have used the Web site to get personal account information. The static web site averages about 1,800 hits each month, and was recently upgraded to allow members of the Unclassified Plan to make changes to the investment allocation of new and existing contributions to their accounts. In April 2001, 57 percent of all asset allocation changes were handled over the Web, even though it had been available for less than one week.

Many of the estimates prepared internally by staff are completed using the Web site calculator. This allows the system to generate personalized, automated letters and to bring a lap top computer on road trips to prepare estimates for persons who attend individual meetings.

MSRS completed the imaging of its paper files in May 2001. Over 5 million pieces of paper that provided detailed data on individual participants of the plan were scanned into an optical storage system using Keyfile as the software to accommodate this storage. The entire process took over five years to complete. MSRS plans to update its imaging technology in the coming year.

The optical storage system has allowed MSRS counselors and staff to readily access member information via personal computers. It also has eliminated the need for counselors to take a name and number from a caller, retrieve a paper file and then call the member back. Counselors are able to answer a call, access a member's file in seconds and offer prompt assistance.

Teachers Retirement Association

The TRA collects individual personal data and service and salary data from nearly 500 school districts throughout the state, other than Minneapolis, St. Paul and Duluth. The retirement system requires school payroll personnel to report salary, contributions and credited service for each teacher covered by the plan.

In early 2000, the TRA Board of Trustees authorized a four-year $15 million project called FROST (Functional Redesign of Strategic Technologies.) The FROST project is designed as a comprehensive systems redesign of all major TRA business processes. As the baby-boom generation continues its march toward retirement, the implementation of FROST is designed to provide the automation necessary to process the nearly 3,500 annual retirements TRA actuaries are predicting by the year 2010.

FROST represents the first extensive new computer systems development in TRA in decades. For key administrative processes, TRA has been using antiquated computer programs first developed over 25 years ago. Since then, the programs have been modified as legislative changes have occurred. The integrated TRA database will

continue to reside on the AS-400 mainframe computer. Program applications will reside and process on a series of network servers providing Graphical User Interface (GUI) or "point and click" screens to a network of TRA employees. The applications are being developed in the Delphi computer language.

The FROST project has been divided into four phases. As of July 2001, Phase 2 of FROST has begun with the redesign of the employer reporting process in which participating employers communicate salary, service credit and other demographic changes periodically on over 70,000 active TRA members. Implementation of Phase 2 is expected by June 2002. Phase 3 of FROST will address benefit estimates, refund estimates, annual statements, leaves of absences and internet-based functionality. Phase 4 will redesign the actual benefit payment processes of retirement annuities, disabilities, survivor benefits and federal and state tax reporting. Phases 3 and 4 are scheduled for implementation in June 2003 and June 2004, respectively. Upon full implementation, FROST applications will be integrated with the document imaging system with workflow capabilities. The workflow applications will allow for automated, systematic processing of TRA customer service requests.

TRA implemented a document imaging system in 1999 to replace the ever-growing volume of member files in paper format. Document imaging has improved the processing efficiency of agency operations by organizing documents systematically, allowing use by multiple users and providing disaster recovery protection in the event that the paper records are lost or destroyed. The document imaging system runs on the TRA AS-400 mid-range computer using IBM's VisualInfo application program. The cost of the programming, systems maintenance and records conversion is estimated at about $1.5 million, and the work to complete full implementation will be spread over a five-year period.

All active member records are on the document imaging system. TRA is in the process of converting persons retiring prior to July 1, 1999 onto the imaging system. As of July 1, 2001, the retiree conversion process is approximately 25 percent complete. The records of members not teaching for many years and of former members who have taken refunds of their contributions more than three years ago are largely still in microfiche format. As some of these individuals return to teaching or take refunds, their microfiche records are converted electronically. TRA management is currently evaluating whether microfiche format remains the most cost-effective storage means for records of individuals for whom further TRA activity is highly uncertain.

Public Employees Retirement System

The PERA collects individual personal data and service and salary data from over 2,000 local governmental entities including school districts, cities, counties, townships and a variety of miscellaneous entities such as joint powers boards, soil and water conservation districts, etc. The retirement system also collects similar data on a number of state employees who were formerly county employees within the State's judicial districts or school district employees for the State's community college system.

PERA has just completed a $10 million project that encompassed the reengineering of its three major operational activities (collecting personal, salary and contribution data on individual members; delivering information and computing benefit estimates and final payments; and paying benefits, refunds and DCP distributions). The last major implementation of systems development occurred in the late 1970's and early 1980's. The information systems used by PERA prior to our recent reengineering effort were antiquated and inflexible. As more plans have been added under our administration and benefit provisions changed, it became increasingly difficult to modify the old systems to meet our operational needs. Also, the membership record-keeping system was extremely limited in its capacity to store additional data on individuals. We learned over the years that we could not accommodate many requests for information about our members from the Legislature, because we did not have the capacity in our data files to record those types of information.

The reengineering project, begun in 1995 with the Board's adoption of a five-year strategic plan, converted years of data maintained on an AS-400 mainframe operating system to a client-server central database supported through a complex network of servers connected to personal computers on every workstation. As of July 1, 2001, we no longer maintain any of our major operational activities on a mainframe, and do not plan to move our current mainframe to the new facility.

Our information technology systems have been designed to pre-define reporting fields for the specific data we require be reported on our members. We work with local government entities ranging from those that are quite advanced technologically to small townships where information forms are still completed manually and sent through the mail. Our systems must be flexible to accommodate the variety of pay schedules used by the local units of government and their service agencies and be capable of processing an average of 20,000 contribution transactions a day and 70,000 payments (via Electronic Funds Transfer and paper checks) a year.

PERA undertook the process of defining requirements and purchasing hardware and software to accommodate imaging of our more than 600,000 paper and microfilmed files on current and former members and all benefit recipients. The process to convert approximately 3 million documents on active members to electronic images and to fully integrate optical storage of our records is just underway and will take years to complete. We have acquired Panagon IDM software from Filenet to accommodate our optical storage imaging needs and developed a custom workflow application using @Work Custom Solution software to route electronic documents within the agency. Total costs to date for imaging consulting, programming, equipment and software are $1.3 million.

Like TRA and MSRS, the use optical storage of members' records will provide access to an individual's account information simultaneously by multiple users and allow us to provide prompt service to callers or individuals who visit with our counselors in the field. Of great importance to the Board and to our members, this storage provides optimal disaster recovery protection of paper documentation collected over the many years an

individual is covered by PERA and beyond for those who may return to public employment for whom service and salary data must be regenerated for active management.

TRA and PERA Customer Service Call Centers

The TRA has a dedicated a group of five retirement services specialists to staff the Telephone Service Center that receives about 60,000 calls a year. The goal of the center is to address over 90 percent of calls on a first-time basis, without the need for further transferring within the office. TRA uses a telephone system built by Executone. The Executone system allows for call routing to available operators, provides detailed reports of call volume and waiting times, and integrates with the state telephone system maintained by the Department of Administration. TRA will upgrade its existing telephone system upon its move into the new building to provide for additional call capacity and new features developed by Executone.

As part of its reengineering efforts, PERA implemented a call center in April 1997 using an automatic call distribution (ACD) system like that used by the Office of the Secretary of State. This system includes a Management Information System (MIS) that allows PERA to track call volumes and other management data important to ensuring the proper level of staffing required to accommodate our service demands. PERA has three full-time staff responsible for taking calls with the goal of handling those calls at the first point of contact with the agency. There are about 20 other Pension Services Division staff, whose primary responsibilities are to calculate estimates and final benefit payments, and to provide individual counseling to members in the office and out-state, who are available to sign onto the system when call volumes require additional staff support. PERA receives over 106,000 calls each year.

In anticipation of the move, PERA looked into whether or not it would be prudent to change its phone system to coordinate with either TRA or MSRS. The MSRS purchased a new phone system, but rather than using a call distribution system, maintained a central operator and receptionist to direct calls to the appropriate staff within the office. Since PERA had already in 1997 moved to a distribution system, rather than a single receptionist, as a better means to meet its caller service demands, there was no opportunity to share in the purchase of phones or systems with MSRS. PERA also found that while the system it currently uses is similar to that used by TRA, it is sufficiently different to require significant cost to make a change. The cost did not justify the end results; thus, PERA will move its current phone system to the new building.

If upgrades or replacement systems are found necessary in the future, discussions will be held to determine opportunities for sharing costs associated with replacing or upgrading the phone systems.

Cost and Other Considerations for Consolidating Information Systems Operation and Structures

Initial Considerations

The first areas to be considered for joint administration related to technology include such things as a hot site for disaster recovery, Integrated Voice Response Systems, and Web services. While we have not had an opportunity to have any discussion on these ideas yet, a joint information technology investment committee will be developed when we move into the building to share on an ongoing basis information about each agency's anticipated technology upgrades and to attempt to leverage opportunities for joint investments and where possible, shared systems development.

The Department of Administration's InterTechnologies Group (InterTech) will be leasing space in the Retirement Systems' building to accommodate an off-site facility for other agencies served by InterTech. For disaster recovery purposes, it would be prudent for the retirement systems to have a computer operations site (hot site) available at another location in the case of a catastrophic event that would prohibit the use of the computer operations in the building. A duplication of expense could be avoided if the three retirement systems could enter into an agreement with an off-site facility to accommodate a disaster recovery computer operations center that could accommodate all three systems.

The use of Integrated Voice Response Systems has been studied by the three systems, but is not widely used at this time. As the demands for immediate access to information and to handle the increasing volumes of calls to the agencies, this technology may provide some efficiency in managing those volumes. This is another area where the three systems may be able to leverage some opportunities to share costs and develop a common system to accommodate all three agencies' needs.

The retirement systems each have developed web sites to provide quick access to information to members and participating employers. The extent to which those sites provide interaction with the retirement system's main database varies. There are direct links established from each of the sites to the other retirement systems as well as to other useful retirement and financial planning sites available on the World Wide Web. As the retirement systems' web development evolves, a Joint Committee will be able to determine ways to consolidate efforts and perhaps reduce investment costs to keep up with the demand for faster, more immediate access to general and specific member data.

Future Considerations

The idea of consolidating the administration of our information systems requires some careful study of the extent of the consolidation. We have tried to put together thoughts about the low to high end of possibilities, but will not be able to go into much depth at this time. More detail will be provided in the report that must be presented to the Legislature in February 2003.

At the low end of the spectrum, managerial functions, network operations or business operations may be able to be consolidated at little cost, but will create a host of other issues. One of the most significant issues would be how priorities are decided when two or more of the different systems need development work, but there may not be enough resources (or the right competencies) available to accommodate the work. The data and data structures between the three funds are very different. Opportunities to develop more than read-only access to those structures will be explored as part of the planning for satellite offices.

At the high end of the spectrum would be the decision to build a singe set of core business applications that must support the three retirement systems and particularly the variety of benefit plans administered by MSRS and PERA. We have determined that it could cost as much as $20 to $35 million dollars to develop this concept, with minimal return on recent technology investments made by PERA and TRA. The benefits returned from the recent investments made by these two systems will be less than the costs incurred for the development of the new structures. It is also expected that an attempt to provide a common application architecture will not likely provide significantly new business functionality, thus the cost of developing a common application would not justify the end results given the recent investment made by PERA and TRA.

Other considerations as we prepare for the delivery of the 2003 report include:

- Combining the applications to support the three distinct business units (MSRS, PERA and TRA) will complicate the application design and software code, making it more difficult to modify and maintain. Even if all the applications were to be rewritten in a common platform, the business logic will still be reasonably complex. Detailed business rules, constituencies, employers from whom data is collected on individual members, operating modes, and managerial philosophies are very different for each fund, requiring an enormous design and implementation effort.

- The application architectures and platforms between the three agencies are very different. TRA is a mid range environment (AS-400), PERA is client/server based, and MSRS is mainframe. This means that it would not be easy or cost efficient to just standardize platforms (and keep business applications separate), because so many changes would be required to the applications themselves. Even if network operations were to be consolidated, labor savings will be minimal, because the platforms are so different that the staff experts currently supporting them would still be needed.

- MSRS is currently fully integrated with the InterTechnologies Group. They are the only system with the majority of their membership already integrated through the State's mainframe through Central Payroll. If MSRS were to decide to disengage from the State's mainframe and fully redesign their applications, possibly integrating with either PERA or TRA's current applications, they could expect to incur a cost of $8 to $10 million.

- Some of the fundamental differences in the structures of the plans administered by the three retirement systems have evolved over time to accommodate the special needs and demographics of the members of the systems. Service credit determinations, leave of absence provisions, reduction and other actuarial factors used to calculate benefits, and actuarial assumptions are different for the plans, because of the differences in the types of employees for which those plans provide benefits. For example, the TRA provides for special treatment of sabbatical leaves of absence, which have been deemed appropriate for teachers, but these types of leaves are not common practice in state and local government personnel practices. Therefore, sabbatical leave of absence provisions are not part of PERA and MSRS plan provisions.

  The reason for pointing out these differences is that common business rules and an "enterprise-wide" database cannot begin to be formulated and developed without some fundamental changes in these types of plan provisions. It would seem that to be fair and prudent in making any changes to the plan provisions, discussions and planning with the affected constituencies would be required.

- The best time to entertain the development of a an "enterprise-wide" database may not be for another six to ten years when both PERA and TRA will be looking at leveraging new technology to provide vastly new business functionality. MSRS would have to weigh the advantages and disadvantages of moving away from the State's mainframe computer, which currently provides essential integration with the State's payroll process that reports contributions for the majority of MSRS' members.

Conclusion

The retirement systems have come a long way in providing service to their members in the last decade. All have developed web sites that are easily accessed by their members and others who navigate the Internet. With the adoption of laws allowing purchases of service, the web site calculators developed by all three systems were key in helping manage the significant increase in requests for information on this complicated calculation. Further development of the web is helping us meet our information service demands and will continue to do so.

The use of technology in administering our operations has proven absolutely critical in meeting information service demands, but has also provided an opportunity to expand the scope of service we can provide. Questions about moving to another career, retiring, or just trying to understand what is needed to prepare for retirement life increasingly become a part of the individual discussions members have with our counselors. Defining the appropriate information to share, training staff, developing web applications or links and expanding our assistance through information networks and contacts have become more of the norm for our staff and will continue to expand. We look forward to increasing our ability to assist our members in those areas.

Combining administrative functions to gain efficiency in service delivery while trying to minimize costs will require strategic planning and well thought out design and implementation schedules. The cost associated with planning a major consolidation effort will be considerable, and the resources to accommodate such planning efforts will take away from some of the critical work facing the retirement systems as we prepare to move our members who are part of the baby boom generation into retirement. We have a lot of work ahead of us.

This report highlights some of the areas we will be researching and in which detailed analysis will be required to meet the requirements of the 2003 report. Some of the thoughts presented in this report provide an insight into what we should be considering and will be instructive as we begin that work.