Introduction

As a supplement to our January 2018 report, *Factors Contributing to Health of State Employee Pension Funds*, this policy brief analyzes the health of Connecticut's Teachers' Retirement System (TRS), examines the factors that led to the system's current funding level, and discusses the features of the system that differentiate it from other public pension systems, such as Connecticut's State Employees Retirement System (SERS). The policy brief also discusses three potential options for restructuring TRS' unfunded liabilities, as proposed by the Teachers' Retirement System Viability Commission in April 2018, and the process by which Connecticut could elect for TRS members to participate in Social Security.

As with all public pension systems, there are a number of factors that can contribute to the health of the system, which are discussed in detail in *Factors Contributing to the Health of State Pension Funds*. In summary, poorly-funded pension systems (typically defined as systems with funded ratios under 80 percent[1]), often have experienced a combination of the following factors:

- Failure to make adequate contributions to avoid increasing unfunded accrued actuarial liability (UAAL);
- Investment returns that underperform assumed rates of return;
- Use of amortization methods that cause increased annually required contributions (ARCs) at the end of the amortization schedule;
- Use of cost-of-living adjustments (COLAs) and early retirement incentive programs (ERIPs) without properly accounting for the increased cost of benefits; and
- Entering contractual agreements to reduce contributions, or to increase benefits without increasing contributions.

This policy brief discusses to what extent the aforementioned factors have influenced the health of TRS, and also highlights a number of uncommon features of TRS that differ from both SERS and many other state-managed pension systems. For example, one of TRS' uncommon features is that most TRS members are municipal employees, but the pension system is managed at the state level. This means that although salaries are set through collective bargaining agreements at the local level, retirement benefit rates are negotiated at the state level.

Also uncommon is the fact that TRS members, and their local district employers, do not contribute to Social Security. Local employers also do not make contributions to TRS, as the State of Connecticut has the sole responsibility of paying the ARC, and any additional unfunded liabilities, over and above the employee contribution made by active teachers (currently seven percent of their pay). Finally, the funding policy for TRS is constrained by a bond covenant for $2.27 billion in pension obligation bonds sold by the State in 2008.[2]

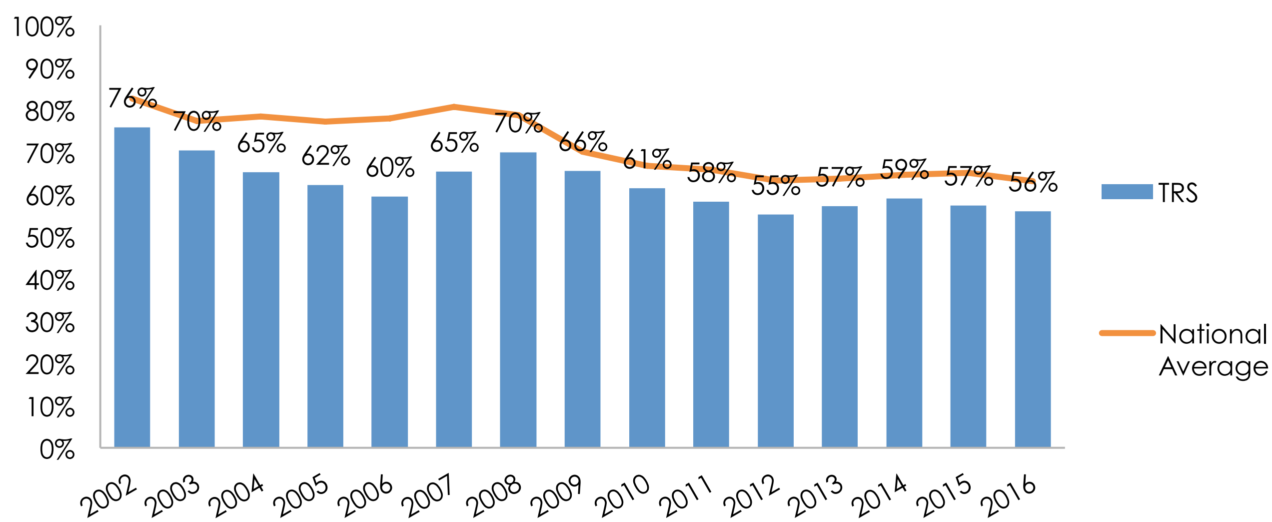
Analysis of Factors Contributing to the Health of Connecticut's Teachers' Retirement System

In fiscal year 2016, the year of the last available biennial actuarial valuation, TRS had a funded ratio of 56 percent,[3] while the national average for state-managed public employee pension plans in the same year was 71.4 percent.[4] The funded ratio of TRS has declined from a high of 83.6 percent in FY 2000, despite the addition of $2 billion to the fund through the sale of pension obligation bonds in FY 2008. In fact, with the exception FY 2012 (when the funded ratio was 55.2 percent), the current funded ratio for TRS is the lowest the system has seen since 1990 when the funded ratio was 51.8 percent.[5]

It is optimal for all pension systems to become 100 percent funded, meaning the system holds enough funds to cover both its normal costs and future obligations.[6] However, systems with funded ratios over 80 percent are generally considered healthy.[7] Since 1990, TRS has had a funded ratio of over 80 percent in only FYs 2000 and 2001,[8] which means TRS is not currently considered a healthy pension system. Figure 1 below illustrates the funded ratio of TRS, as compared to the national average for state pension plans, since FY 2002.

Figure 1[9,A]

Actuarial Funded Ratio for Connecticut's Teachers' Retirement System (TRS), FYs 2002-2016



[A] National data reflects the average for plans of similar type and Social Security coverage. National data averages are weighted by plan size.

Contributions

Connecticut does not require any local contributions to TRS although most TRS members are employees, or former employees, of local and regional boards of education.[B] Active teachers currently contribute seven percent of their salary to TRS, with the State of Connecticut responsible for making the entire employer contribution in the form of its ARC, which is alternately described as an actuarially determined employer contribution (ADEC).[10, C] The State's contribution comes in the form of an annual appropriation from Connecticut's General Fund.[11] If the calculated ARC is not high enough to prevent growth in TRS' UAAL, the State is also responsible for these additional liabilities.[12]

While TRS has been in existence since 1939, the State of Connecticut did not begin saving in advance for teachers' pensions until 1979.[13] At this time, the State implemented a gradual phase-in of funding ARC payments, from 35 percent of the ARC in 1979 to an intended 100 percent payment of the ARC by 1993. However, the State never made a full ARC payment during this time and, in 1993, the State paid just under 40 percent of its calculated ARC payment.[14] By the time the State implemented an actuarial funding policy, TRS had a funded ratio of only 40 percent and $1.5 billion in UAAL.[15] In their 2015 report on SERS and TERS, Jean Pierre Aubry and Alicia Munnell of the Center for Retirement Research at Boston College attributed $4.1 billion, or 38 percent, of TRS' $10.8 billion UAAL to legacy costs related to the period that the State did not contribute to future liabilities.[16]

In addition to legacy costs, TRS' UAAL grew approximately $8.5 billion from 1983-2014.[17] A variety of factors caused this increase, while some factors mitigated UAAL increases. From 1985 to 2006, the State of Connecticut never made its full ARC payment.[18] The Teachers' Retirement Board, which is responsible for managing TRS, had an unofficial policy of paying only 85 percent of the ARC from 1992 to 2006.[19] Aubry and Munnell's

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[B] *Teachers at charter schools, magnet schools operated by Regional Education Service Centers, and some teachers in the Connecticut Technical Education and Career System are also members of TRS, although the education agency that employs them is not directly associated with a tax base.*
State of Connecticut, Connecticut Teachers' Retirement Board. (2015). *Administrative Procedures Manual*. Hartford, CT: Author. Retrieved from http://www.ct.gov/trb/lib/trb/formsandpubs/trbmanual.pdf.

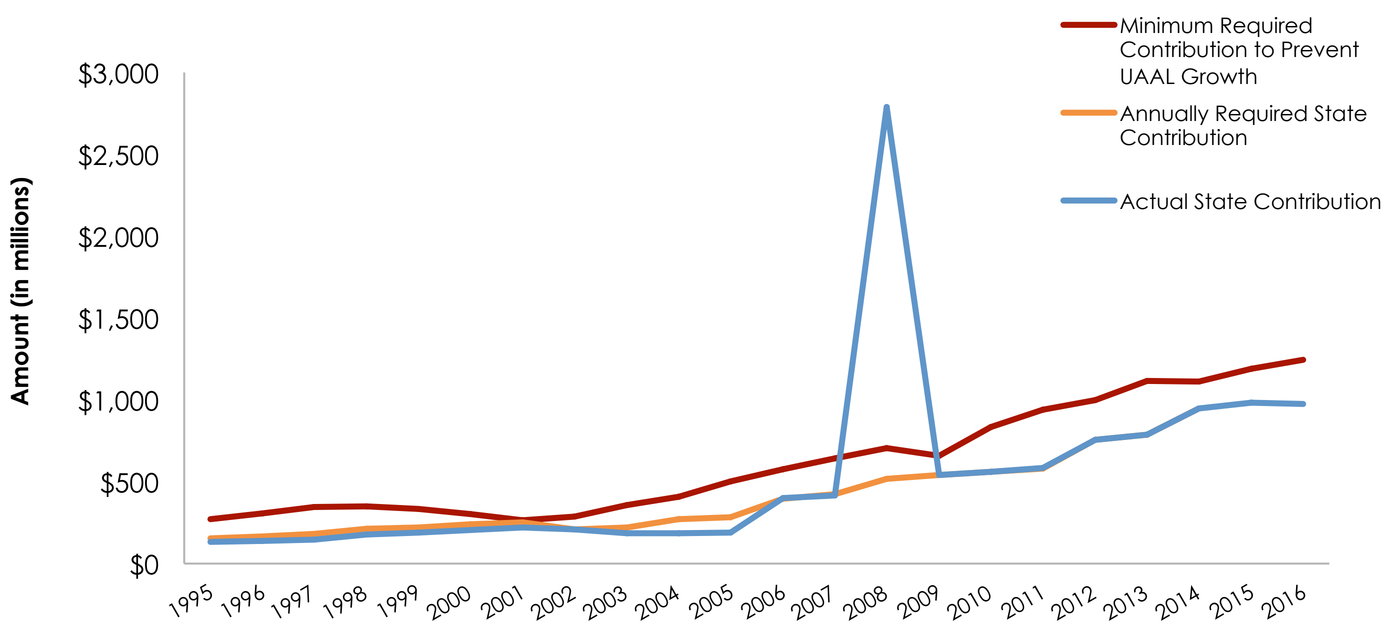
[C] *In 2012, the Government Accounting Standards Board (GASB), which sets accounting rules for public pension plans, issued GASB Statement No. 67 and GASB Statement No. 68, which contained updated standards for accounting practices in pensions. Under the new rules, the calculation of a pension system's annually required contribution (ARC) was replaced with the actuarially determined employer contribution (ADEC). For consistency, and to avoid confusion, the term annually required contribution (ARC) is used throughout this policy brief, even though TRS has recently moved to using an actuarially determined employer contribution (ADEC) calculation, as both calculated payment amounts are, in practice, nearly identical, and are both intended to represent the amount a government needs to contribute to a pension system in order to pay both the normal cost and the amortization payment of the system's UAAL.*
Weinberg, S., & Norcross, E. (2017, June 15). GASB 67 and GASB 68: What the New Accounting Standards Mean for Public Pension Reporting. Arlington, VA: George Mason University, Mercatus Center. Retrieved from https://www.mercatus.org/publications/gasb-67-68-public-pension-reporting.
Munnell, A.H., & Aubry, J. (2015, June). *The Funding of State and Local Pensions: 2014-2018* (Issue Brief No. 45). Chestnut Hill, MA: Center for Retirement Research at Boston College. Retrieved from http://crr.bc.edu/wp-content/uploads/2015/06/SLP45.pdf.

analysis notes that between 1983-2014, annual contributions made by the State that were less than the State's calculated ARC added an additional $1.5 billion to TRS' UAAL.[20]

In FY 2008, the State of Connecticut sold more than $2 billion in pension obligation bonds with the goal of improving the health of TRS.[21] The proceeds of the bond sales were added to the system and, under the bond covenant, the State has since been obligated to pay its full ARC until the bonds come to maturity.[22] As a result of this stipulation, the State has paid its full ARC each year since 2008.[23] However, it should be noted that the debt service on the bonds is not included in the UAAL calculation for TRS.[24] Thus, because the bond proceeds are leveraged until the bonds mature, the increase in the funded ratio — as a result of adding the proceeds of the bonds sales to TRS — is not fully realized until 2032.[25] Figure 2 below illustrates employer contributions, in the form of the State of Connecticut's ARC, to TRS since FY 2002. The spike in contributions in FY 2008 is due to the previously discussed pension obligation bonds.[26]

Figure 2[27]

State Contributions to Connecticut's
Teachers' Retirement System (TRS), FYs 1995-2016



Amortization Method

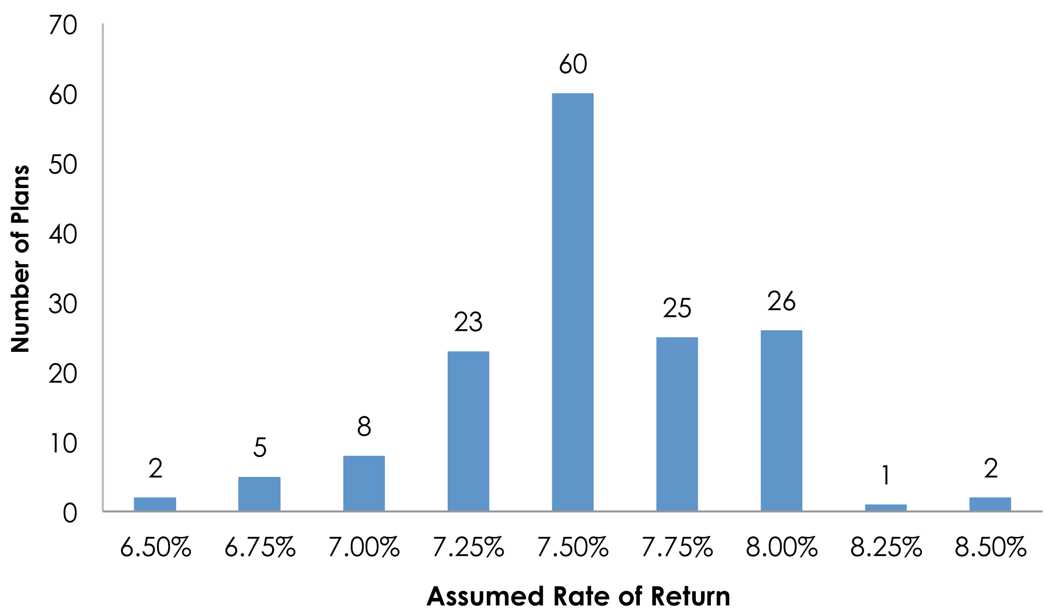
Since 1979, when the State began to pre-fund TRS, it has used a level percent of payroll amortization method. As discussed in *Factors Contributing to the Health of State Pension Funds*, the level percent of payroll amortization table tends to lead to lower ARC calculations at the initial period of amortization, which will not cover the full interest on the UAAL, and can lead to balloon payments toward the end of the amortization period.[28] Additionally, from 1979-1992, TRS reset its amortization period each year, for a period of 40 years.[29] This means that even if the State had made 100 percent of its ARC payment each year, this still would not have been enough to avoid increasing TRS' UAAL over time. In 2015, Aubry and Munnell calculated that $4 billion of the growth in TRS' UAAL since 1983 is attributable to these amortization practices.[30]

Investment Assumptions

Assumed rates of return are intended to align with the long-term investment experience of a pension system, understanding that in some years returns may be higher than in others. TRS had an assumed rate of return of eight percent from 1984[D] to 1989,[31,32,33,34] before it was raised to 8.5 percent in 1990,[35] and then lowered back to eight percent in 2016.[36] The fact that TRS' assumed rate of return was set at 8.5 percent from 1990 to 2016 is unusual among public pension systems in the United States, as the national average assumed rate of return decreased from 8.22 percent in 1992 to just under 7.57 percent in 2016.[37]

Figure 3[38]

National Distribution of Assumed
Rates of Return for Public Pension Plans, 2016



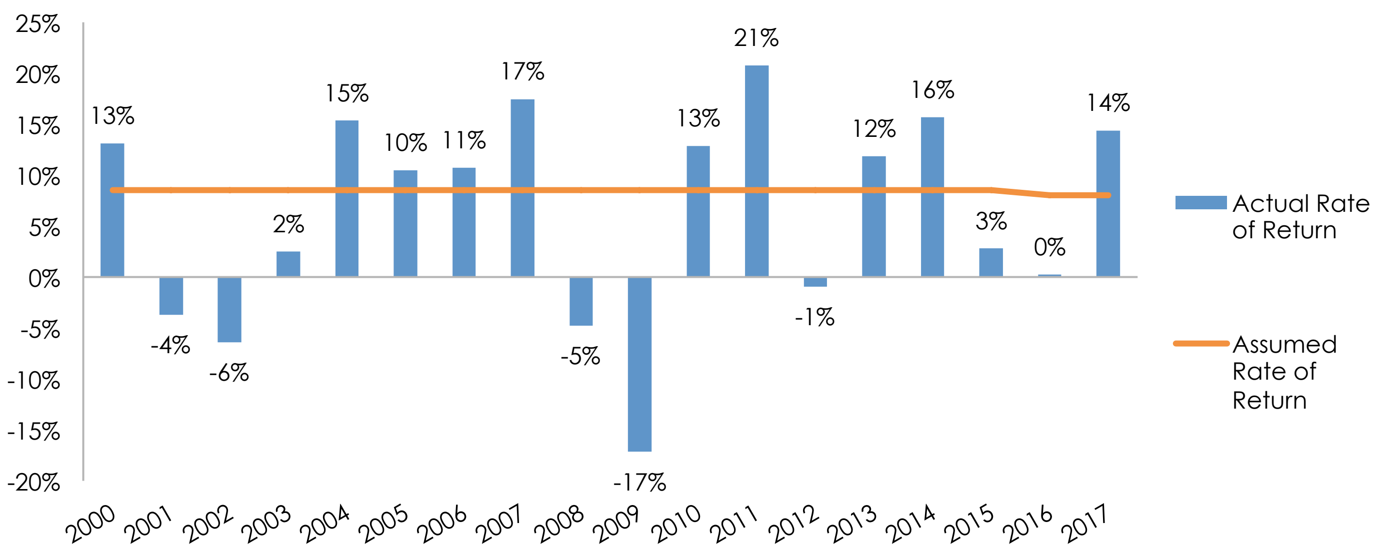
From 1983 to 2000, TRS' average investment returns were higher than assumed returns by 4.5 percentage points, which Aubry and Munnell estimate reduced TRS' UAAL by $3.5 billion during this period.[39] However, between 2001 and 2014, the average investment experience was lower than the assumed rate of return by three percentage points, which Aubry and Munnell estimate added $5.7 billion to TRS' UAAL.[40] In 2015, TRS'

[D] This is the earliest year of data available.

investment returns were 5.71 percentage points lower than its assumed rate of return and, in 2016, TRS' investment returns were 7.75 percentage points lower than its assumed rate of return. However, in 2017, TRS' investment returns exceeded its assumed rate of return by 6.38 percentage points.[41] Since 2001, the average actual rate of return for TRS has been six percent, which includes the high return rate of 14.38 percent in 2017.[42] Aubry and Munnell calculated that $2.7 billion in the growth of TRS' UAAL from 1983-2014 was attributable to investment returns.[43] Although investment experience continually fluctuates with markets, TRS has experienced investment returns well below assumptions over the past 17 years, which indicates the system's assumptions are not in alignment with the long-term investment experience of TRS. As a result, TRS' UAAL has increased substantially. Figure 4 below illustrates the actual versus assumed rates of return for TRS since FY 2000.

Figure 4[44]

Annual Return for Connecticut's Teachers' Retirement System (TRS), FYs 2000-2017



In their 2015 report, Aubry and Munnel projected that if average annual returns continued at 5.5 percent (the average annual return from 2001-2014), ARC payments would eventually spike to $6.2 billion in 2032.[45] However, the Connecticut Teachers' Retirement Viability Commission report found an increase in ARC payments to that amount is not likely, as it is in the 18th percentile of projected outcomes, even if average rates of return are lower than the system's assumed rate of return of eight percent[E]. The Commission analysis shows that at the 50th percentile of probability, the State's ARC payment for TRS will increase to more than $3 billion in 2032.[46]

[E] For information on the methodology used to derive this conclusion, please see:
State of Connecticut Teachers' Retirement System Viability Commission. (2018). *Report of the Commission*. Hartford, CT: Author. Retrieved from
http://www.ct.gov/trb/lib/trb/formsandpubs/CT_TRS_Viability_Commission_Report_03192019.pdf.

Benefits Structure

When compared to inadequate contributions, poor amortization practices, and inaccurate investment assumptions, benefit changes have had a minimal impact on the growth of TRS' UAAL. However, Aubry and Munnell identify $1.2 billion of the growth in UAAL between 1983-2014 as being associated with benefit changes.[47]

In 2016, the average annual benefit per TRS annuitant ($50,976[48]) was substantially higher than that of the average annual benefit per SERS annuitant ($34,421) in the same year.[49] Although more generous benefits increase the total cost of the pension system, it is imperative to note that Connecticut teachers, and their employers, do not contribute to the federal Social Security system because of a decision made by TRS members in the 1950s not to participate.[50] As a result, teachers, unlike state and municipal employees, do not benefit from the additional income stream that Social Security provides in retirement. This lack of participation in Social Security explains the higher pension benefit per annuitant.

Additionally, Aubry and Munnell attribute the vast majority TRS' UAAL to benefits for TRS members hired prior to 1979, and estimate the funded ratio for this group of members was approximately 35.3 percent in 2014, while the funded ratio for members hired after 1979 was 96 percent.[51] However, the liability calculation for post-1979 hires includes the approximately $2 billion in pension obligation bonds, which has the impact of increasing the funded ratio. Because the proceeds of the pension obligation bonds are contained in TRS, but the bonds themselves are not yet fully mature, the increase to the funded ratio is not fully realized until the bond proceeds are no longer leveraged, which is not scheduled to occur until 2032.[52] If the original cost of the bonds ($2.27 billion[53]) is added to the $10.2 billion in liabilities that Aubry and Munnell attribute to post-1979 hires,[54] the 2014 funded ratio for this group drops to 78.6 percent.

Unique Features of Connecticut's Teachers' Retirement System

There are a number of features in the way TRS is structured that make it a fundamentally different retirement system than many other public pension systems, and more specifically, different from Connecticut's other state-managed retirement system: SERS. These systemic differences must be considered when comparing TRS with SERS, and when contemplating changes to the funding policy for TRS as a means of UAAL mitigation.

Connecticut TRS Members are Ineligible for Social Security

Under federal law, public employees are exempt from mandatory participation in Social Security,[55] due to constitutional concerns that the federal government cannot impose taxes on state governments.[56] In 1950, Congress amended the Social Security Act to allow voluntary participation among state and local employees. However, since 1983, states that opt to participate in Social Security may not reverse their decision.[57] There are 15 states and the District of Columbia where at least some teachers are ineligible for Social Security.[58] Connecticut is one of 13 states where all public school teachers are barred from participating in Social Security.[59]

Figure 5 below compares attributes of teacher pension systems in states where, like Connecticut, teachers do not participate in Social Security, and where the teachers' retirement system is separate from the larger state retirement system. Maine and Nevada are excluded because teachers are included in larger state retirement systems with other types of public employees.[60]

Figure 5[61]

Attributes of Teacher Pension Systems in Comparison States, 2016

State	Funded Ratio	Normal Cost as % of Payroll	ARC as % of Payroll	% of ARC Paid	Assumed Rate of Return	10-year Annualized Rate of Return	Employee Contribution Rate as % of Pay	Local (Employer) Contribution Rate as % of Payroll[F]	Actuarial Method
Connecticut	56.0%	3.7%	24.7%	100%	8.0%	5.3%	7.00%	0.00%	Level Percent of Pay
Alaska	75.8%	8.0%	75.9%	34.4%	8.0%	5.5%	8.65%	12.56%	Level Percent of Pay
California	63.7%	8.4%	26.0%	65.8%	7.5%	5.6%	10.21%	14.43%	Level Percent of Pay
Colorado	56.3%	4.2%	22.8%	82.1%	7.25%	5.2%	8.00%	12.58%	Level Percent of Pay
Illinois	39.8%	8.3%	46.7%	85%	7.5%	5.4%	9.00%	0.00%[G]	Level Percent of Pay
Kentucky	54.6%	7.6%	28.3%	56.5%	7.5%	6.3%	12.855%	0.00%	Level Percent of Pay
Louisiana	62.4%	4.3%	30.4%	105.6%	7.75%	6.1%	8.0%	26.4%	Multiple
Massachusetts	52.8%	3.6%	17.6%	100%	7.5%	5.7%	11.0%	0.0%%	Level Percent of Pay
Missouri	84.8%	1.8%	14.1%	104.3%	7.75%	5.8%	14.5%	14.5%	Level Percent of Pay
Ohio	69.6%	0.0%	10.6%	124.5%	7.75%	6.1%	14.0%	14.0%	Level Percent of Pay
Texas	79.7%	2.2%	7.6%	98.7%	8.0%	5.9%	7.70%	1.50%	Level Percent of Pay

In Connecticut, the decision to opt-out of Social Security for TRS members was made in the 1950s when the members of TRS voted against participating in the program.[62] In 1959, the Connecticut General Assembly passed a law prohibiting current and future TRS members from holding a referendum to reverse this decision,[63] which still applies to current Connecticut teachers.[64] In contrast, SERS members do participate in Social Security because Connecticut is covered by what is known as a "divided vote referendum," wherein different groups of public employees are separately able to elect whether or not to participate in Social Security.[65]

Because members of TRS do not participate in Social Security, and are required to participate in TRS,[66] their pension is their sole source of retirement income from teaching. For this reason, it is more difficult to reduce full pension benefits for TRS members than it is for SERS members, and the TRS average benefit amount is necessarily higher than the average SERS pension benefit[67] — especially compared to the SERS Tier IV category created in 2017.[68] However, an analysis by the Teachers' Retirement System

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[F] If the local contribution is zero, this means the state contributes the full ARC payment.
[G] Half of Illinois' school districts "pick up" the employee contribution to the state's teacher retirement system as a part of teacher contracts.
Teachers' Retirement System of the State of Illinois. (2017, October 1). School Districts "Picking Up" Members' TRS Contributions. Retrieved from https://www.trsil.org/news-and-events/pension-issues/districts-picking-up-members-trs-contributions.

Viability Commission shows that at a retirement age of 62, TRS benefits are nearly double that of Social Security, and TRS benefits cost 13.5 percent of payroll, while Social Security benefits cost 12.4 percent of payroll. However, this analysis does not provide for increased benefits at later retirement ages in the Social Security system.[69] The full retirement age for TRS is 62, while the full retirement age for Social Security is 65, with benefit levels increasing up to a retirement age of 70.[70]

Please see the appendix for a discussion of the process by which Connecticut teachers could elect to participate in Social Security.

Pension Obligation Bonds Covenant

The sale of $2.27 billion in pension obligation bonds in FY 2008[71] has placed constraints on potential options for the State of Connecticut to change the structure of TRS in order to mitigate the system's UAAL growth and increase the system's funded ratio. The proceeds from the bonds were added into the Teacher Retirement Fund (TRF) and are subject to a bond covenant, in which the State pledged to contribute the ARC to the TRF for the life of the bonds. In addition, the state pledged that the General Assembly would not enact legislation diminishing the amount of the ARC, as calculated by biennial actuarial valuations in the manner required under 2008 statutes.

There are two exceptions to this requirement. The first is that "adequate provision" be made by law for the protection of the holders of the bonds. The second is that the governor declares an emergency, or the existence of extraordinary circumstances, and at least three-fifths of the General Assembly votes to diminish the contribution, and the funded ratio of TRS is at least equal to the funded ratio immediately after the sale of the bonds (calculated using the same actuarial methods used in 2008).[72] If an emergency determination is made, the reduction in the ARC may not cause a reduction in the TRS funded ratio of more than five percent of the current funded ratio, as calculated using 2008 actuarial methods, or the funded ratio immediately following the sale of the bonds, whichever is greater. The bond attorney for the state treasurer, Day Pitney LLP, released a formal opinion noting changing the statutes related to the actuarial funding of TRS is prohibited under the bond covenant, unless the requirements of adequate provision or emergency determination are met.[73]

There is some disagreement between state officials regarding whether restructuring debts within TRS would amount to adequate provision and, as a result, it is unclear which changes the State may be able to make to mitigate the possibility of spiking ARC payments. Connecticut State Treasurer Denise Nappier has stated it is her opinion that any changes to the TRS actuarial funding policies would make the State noncompliant with the bond covenant.[74] However, Governor Dannel Malloy has suggested that if changes to the actuarial methods result in a stronger pension system, he does not believe changing the funding policy would violate the bond covenant, and if there were a conflict with the bond covenant, it would increase the health of the fund so that bondholders would not object to changes in the funding policy. [75] This argument falls under the condition that adequate provision be made to protect the bondholders.

Employer Contributions are Entirely State-funded

Most of Connecticut's public school teachers are employees of local and regional boards of education, which are essentially functions of municipalities, as towns have final authority over school district budgets and over revenue generation through property taxation.[76] Local and regional boards of education are empowered to negotiate teacher contracts,[77] which include salary scales and increases. However, local governments do not contribute to TRS on behalf of their employees. In addition, local governments do not contribute to Social Security on behalf of teachers. In contrast, municipalities do contribute 6.25 percent of employees' salaries for Social Security, and contribute to the retirement plans of all municipal employees, as well as board of education employees, who are not members of TRS.[78] Instead, the State makes what is commonly known as the employer contribution to TRS in the form of the ARC payment.[79] Each teacher in the TRS system is eligible for the same retirement benefits, which are determined as a percentage, based on years of service, of each teacher's average salary.[80] This means that although the State makes the entire employer contribution to TRS, it does not have control over the cost of retirement benefits to TRS members, as benefit amounts are based on salary agreements in contracts negotiated at the local level.

Current Mitigation Plans Under Discussion

Connecticut Teachers' Retirement Viability Commission Report

As part of the biennial budget for FYs 2018-19, the General Assembly formed a Teachers' Retirement Viability Commission, which was tasked with developing a plan to achieve the short and long-term sustainability of TRS.[81] The Commission was not to consider the State's ability to raise new revenue but was required to consider the State's financial capability. In its final report, the Commission made a number of findings, with two recommended overall changes to funding policy: 1) the assumed rate of return be lowered to somewhere near seven percent, and 2) a level dollar amortization method be implemented. Commission findings also note it is imperative that the State make its full ARC payments for any mitigation efforts to be successful.[82]

In its final report, the Commission also noted that the normal cost of TRS is considered moderate when compared to other states where teachers do not participate in Social Security, and that even if TRS' discount rate were lowered from the current eight percent to 6.9 percent, the normal cost would still be 13.51 percent of payroll, with 6.51 percent being the State's responsibility. Therefore, the Commission focused on plans that would reduce TRS' UAAL, and assist the State in making its ARC payments.[83]

Additionally, if no changes are made to TRS' amortization methodology, the Commission found TRS would be nearly 100 percent funded by 2032 (according to the 50th percentile of probability), provided the State makes its full ARC payments. However, if state funding constraints are taken into consideration, the 50th percentile of probability indicates TRS' funded ratio would be just over 70 percent by 2032, with some projections showing a decrease in the funded ratio to just over 40 percent.[84] The Commission did not consider the option of adding an additional revenue stream to TRS through a local contribution to the system.[85]

The Commission provided three mitigation plans for consideration, which are summarized briefly below.[86] For more information on these mitigation plans, please refer to the Commission's final report, which contains detailed descriptions and charts of projected outcomes. The Commission notes that among all options, plans that implement a level-dollar amortization methodology "demonstrate more favorable measures of long-term affordability."[87]

1. ***Pension Obligation Bond (POB) Settlement Plan***
   Proposed by State Treasurer Nappier, this plan would maintain current assumptions and actuarial methodology until 2025 — the earliest date the pension obligation bonds can be called and paid off. Under this plan, approximately $1.94 billion in bonds would be paid off and diverted from TRS, which would cause a decrease in the funded ratio. However, the treasurer estimates paying off the bonds would save $2.2 billion in future interest payments.[88] After 2025, the discount rate would be reduced to 6.9 percent, and the system would shift to either a 25-year layered level percent of payroll amortization methodology.[89]

2. ***Change of Funding Policy Plan***
   Under this plan, which was proposed by Connecticut's Office of Policy and Management, the discount rate would be immediately lowered to 6.9 percent, and a 30-year level dollar amortization methodology would be phased-in over five years for TRS' current UAAL, with a 25-year layered amortization method for future UAAL changes. All modeled outcomes show a steadily increasing funded ratio under this plan.[90]

3. ***Asset Transfer Plan***
   Under the asset transfer plan, the State would transfer state assets, such as real estate or the state lottery, to TRS. The actuarial analysis in the Commission's final report assumes the asset being transferred would provide $350 million in net revenue to the General Fund in FY 2019 (with an expected annual increase in value of two percent), the asset would have a market value of $5 billion, and the transfer would occur in FY 2019. However, the Commission's report does not specify which asset would be transferred, and does not provide analysis of whether these assumptions are feasible. The asset transfer plan is the only mitigation plan presented in the Commission's report that shows an over 50 percent likelihood that TRS' funded ratio would increase to 80 percent by 2038, which the analysis projects is a 68 percent probability. The asset transfer plan is also the only plan that shows an improved probability of increased funded ratios in all future years. Additionally, the asset transfer plan would lower the discount rate to 6.9 percent in FY 2020. [91]

Recent Legislation and Legislative Proposals

During the 2017 regular and special legislative sessions of the Connecticut General Assembly, there were a number of proposals made to mitigate the quickly increasing ARC payments paid from the State's General Fund, which are, as a result, restricting funding for the provision of other services. However, it should be noted all proposals and legislation introduced reduced the State's payment proportionally to new revenue, and therefore would not have contributed to the overall health of TRS. Three of these proposals are:

1. ***Governor Malloy's Proposed Biennial Budget, February 8, 2017 (Proposed)***
   Governor Malloy proposed municipalities bear one-third of the cost of the ARC for teacher pensions, and that the State's ARC payment be reduced proportionately.[92]

2. ***Democrats' "Compromise Budget," House Bill 7501, June Special Session (Proposed)***
   Democratic legislators proposed municipalities contribute 50 percent of TRS' normal cost, and that the State's ARC payment be reduced proportionally.[93]

3. ***Conn. Acts 17-2 (June Special Session) (Enacted)***
   The General Assembly included a provision in the biennial budget for FYs 2018-19 that increased teachers' employee contribution to TRS from six percent to seven percent of their salaries in FY 2018, and then to eight percent in FY 2019. The State's ARC was then reduced proportionally, after an updated valuation report.[94]

Appendix

History of Legislation Regarding Public Employees and Social Security

In 1950, the federal Social Security Act of 1935 was amended to include Section 218, which is the portion of the law that allows public employees not covered by a public retirement plan to voluntarily participate in Social Security, from which they were previously excluded. In 1954, Section 218 was expanded to allow public employees that are enrolled in a public retirement system to also participate in Social Security. In 1956, Section 218 was again amended to allow for states to divide a public retirement system, so that only members who voted to participate are covered by Social Security, while the remaining members are not enrolled. In 1983, the prior provision that allowed states to terminate Section 218 agreements, and withdraw their public employees from Social Security coverage, was repealed.[95]

Process by which Public Employees Elect to Participate in Social Security

States whose public employees elect to participate in Social Security enter into what is known as a Section 218 Agreement with the federal government. Section 218 Agreements may extend Social Security or Medicare benefits only to public employees. All states, Puerto Rico, and the U.S. Virgin Islands have original Section 218 Agreements, but these agreements may be modified in certain ways.[96]

States must hold a referendum with members of a public retirement system before modifying a Section 218 Agreement. There are two types of referendum procedures: a majority vote referendum and a divided vote referendum. All states are authorized to hold referenda of public retirement system members to determine by majority vote whether all members of the system will participate in Social Security. Certain states, including Connecticut, are also authorized to hold divided vote referenda, which allow states to divide a retirement system based on whether the employees currently in the system vote for or against participating in Social Security. In a divided vote referendum, the employees that elect to participate in Social Security will receive coverage, and the employees that elect not to participate remain uncovered. However, the coverage group will also include all future members of the system. Additionally, under a divided referendum, federal law allows states to give employees who previously elected not to participate in Social Security a second chance to participate in coverage, within two years of the modification of the Section 218 Agreement that extended coverage to certain employees in the system.[97]

Because Section 218 Agreements are legal contracts between state governments and the federal government, states that enter into an agreement must enact enabling legislation that outlines the state's responsibilities under the agreement. Modifications may be made to Section 218 Agreements to extend coverage to new groups of employees, to identify new political subdivisions joining a retirement system, to correct errors in the agreement, or to implement changes in state or federal law. States must initiate modifications to Section 218 Agreements, and then send the proposed modifications to the Social Security Administration (SSA). In the modification document, the state is to determine when coverage will begin for newly covered employees in each coverage group, and the coverage can be retroactive or prospective. The appropriate SSA Regional Office then reviews the modification to ensure it complies with state and federal laws. The agreement is considered executed when signed by the SSA regional commissioner.[98]

Issues Specific to Connecticut

If Connecticut wanted to consider offering Social Security to members of TRS, it is entirely within the auspices of the state to initiate a referendum.[99] However, state legislation passed in 1959 currently bars TRS members from holding such a referendum.[100] This means that Connecticut does not yet have the enabling legislation to amend the Section 218 Agreement, as this statute would need to be modified to allow a referendum.

Connecticut currently has a Section 218 Agreement[101] and its state and municipal employees are generally covered by Social Security. Connecticut has modified its Section 218 Agreement as recently as 2008,[102] but it is unclear what modifications were made. Connecticut's agreement is a divided referendum agreement, which allows employees to individually elect coverage.[103] This means that if a divided referendum with TRS members were to occur, current members would not be required to participate in Social Security. Currently, most members of SERS are covered by Social Security, while most members of TRS are not covered.[104] Interestingly, judges in eight of 14 probate court systems (which are considered governmental subdivisions) were not covered by Social Security as of 2011.[105]

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