Testimony to the Appropriations Committee, regarding HB 07148 and the State Appropriation for the University of Connecticut
March 7, 2019

Co-Chairs Osten and Walker, Vice Chairs Hartley, DiMassa and Horn, Ranking Members Formica and Lavielle and members of the Appropriations Committee,

My name is Tom Bontly. I am a faculty member in the Philosophy Department at the University of Connecticut and currently serve as President of the UConn Chapter of the American Association of University Professors (UConn-AAUP).

Thank you for this opportunity to speak in favor of state support for higher education in general and UConn in particular. I would also like to express our concern with the increase in fringe benefit rates and the effect it is having on research and tuition.

As you, our elected representatives, struggle once again to balance our state’s budget, I hope you will be able to think not only of the state’s current budget deficit, but also of the future: of the kind of vibrant state we want to have, of the need to give our young people a reason to stay in Connecticut, of the need to attract the innovators and entrepreneurs and industries of tomorrow, so that we can build a better future for our children.

Crucial to building that future is an on-going commitment to invest in higher education. The benefits thereof to individuals, families, communities, and states are well-known:

- Individuals with college degrees tend to earn higher incomes and live longer, healthier, happier lives.
- Increased funding for higher education generally correlates with decreased need for social services and correctional systems.
- Higher ed funding also makes a state more attractive to business and industry, giving them access not only to a highly educated workforce but also to advanced research – in science and engineering, medicine, education, agriculture, and even the humanities.

In today’s knowledge-driven economy, the path to economic prosperity runs through higher education.

But accessible, high quality higher education requires investment, which is why I hope that the General Assembly will fully fund UConn’s budget request, as included in the Governor’s proposed budget for the coming biennium. After several years of budget cuts, the strain on the academic operation is showing. Class sizes are up, course offerings are down, and departments have had to absorb 3% cuts for three years running. Any further reduction in state support for UConn at this time would have a disastrous effect: on students, on the research enterprise, and on faculty retention. Fully funding UConn’s budget request is a big step in the right direction.
Fringe benefit rates
Another concern for the UConn faculty is the sky-rocketing cost of fringe benefits, the driver of which is the state’s massive accrued unfunded retirement liability – the result of the state’s failure, for decades, to save for the retirement benefits they promised. The sins of the past are causing difficulties throughout state government but at UConn in particular. As I have argued in prior testimony to the Higher Education and Employment Advancement Committee (dated February 21, 2019), the inflated rate which UConn pays for fringe benefits is both unjust and counterproductive.

First, inflated fringe rates increase the cost of educating our students, which drives up tuition and fees. In essence, the state of Connecticut is levying a hidden tax on students and their families, making our children pay for the sins of the past. This arrangement is unjust. The unfunded liability was not created by these students, nor by our institutions of higher education. It was created by the state as a whole: by past legislators and governors who chose to underfund the retirement benefits they were promising, and ultimately by the voters who elected them. And the state as a whole benefited (at least temporarily) from those choices: for by neglecting to save money for future retirements, the state was able to spend that money on government services and infrastructure while still keeping tax rates low.

Since the state as a whole created the unfunded liability problem, and since the state as a whole reaped the benefits, it is only fair that the state as a whole pay the bill.

Second, the current policy is inefficient and counterproductive. In particular, the inflated fringe rates drive up the cost of doing research at UConn, making our researchers less productive and less competitive for federal grant money. Grant awards are typically capped; granting agencies (e.g., NIH) generally do not increase the size of an award to cover the state’s high fringe. Instead, it comes out of the researcher’s budget, with the result that he or she can hire fewer people. Fewer people means that less work gets done, which means fewer discoveries, fewer inventions, fewer publications, and fewer grant applications going out the next funding cycle. And those grant applications that do go out are less competitive, because the granting agencies know that they will get more research for their money if they give it to another institution.

How much less competitive is UConn for grant funding these days? I do not know precisely, but a comparison with the fringe rates of other, comparable institutions is instructive. According to numbers provided by CFO Scott Jordan’s office, the average fringe rate on UConn faculty runs about 20 percentage points higher than it does on average at UConn’s peer and aspirant institutions. The average fringe rate on non-faculty professional staff at UConn runs about 30 percentage points higher than average.

Very roughly, then, a grant which supports three staff members at UConn would support four at one of our competitors and produces proportionally more research work. Granting agencies know this, and it factors into their decision-making. While it is hard to be certain, I would guess that our inflated fringe rates are a big part of the reason why UConn’s grant awards and expenditures have been basically flat since 2011, after many years of growth. The state is effectively squandering the considerable investment in research infrastructure it has made over the last two decades.

The impact of this problem on the state should be obvious. Inflated fringe rates mean less grant revenue – probably tens of millions of dollars less grant revenue per year. Less grant revenue means fewer laboratory jobs for CT residents to fill, fewer patents and start-ups, and generally less capacity for UConn to serve as an economic engine for the state.
In his written testimony on HB 7118, Comptroller Lembo, while certainly recognizing the problem our institutions of higher education face, raises certain concerns about whether the best solution is to remove the unfunded liability surcharge on the fringe rate, or whether it would be better instead to provide these institutions with additional state support to cover the differential. These questions are important, and we are eager to work both with Comptroller Lembo and our elected representatives to find the best solution.

When evaluating possible solutions, it is important to keep in mind that the high fringe rate on state employees has nothing to do with the real cost of current employees’ benefits. Rather, the run up in fringe rates is due entirely to the state’s accrued unfunded liability in the State Employee Retirement System (SERS). This can be seen from information provided by the UConn’s Chief Financial Officer. The fringe benefit rate for employees in SERS, as set by the Comptroller, is currently 96.4% of salary. Out of that 96.4%, a whopping 33.61% goes just to pay down the SERS plan’s unfunded liability, and another 20.94% goes to cover unfunded liabilities for retiree health care program.

For comparison, the actual cost of pension benefits for employees in SERS is 5.3% of salary, and the actual cost that employee’s post-retirement health benefit (what are referred to as “OPEBs”) is 2.86% of salary. This means that 85% of what the University is charged for SERS goes to unfunded liability, to cover pension benefits for people, most of whom are already retired, who participated in Tier I of SERS (which has been closed to new employees since 1984). The cost of funding current employees’ SERS benefits, on the other hand, makes up about 15% of the cost of SERS.

Altogether, the charge for unfunded liability (pension plus health care) makes up 56% of the fringe benefit rate. In other words, more than half of the fringe benefit rate which the university pays on SERS-participants has nothing whatsoever to do with the real cost of their benefits. (The remainder covers the actual cost of retirement benefits, plus the employer contribution to health insurance, FICA, and so on.)

Some people have suggested that the root of the state’s problems is the 2017 SEBAC agreements (of which there were two). Again, nothing could be further from the truth. In January 2017, SEBAC agreed to a plan by the Malloy administration to refinance the pension debt. By spreading the payments out over a longer time, that agreement is currently saving the state billions of dollars per year. Subsequently, in July 2017, SEBAC agreed to a package of salary freezes, furlough days, and cuts to current employees’ pension and health care benefits. That agreement saved the state $5 billion in the biennium and will save $25 billion over 20 years.

Very roughly, then, each state employee gave up, on average, $17,500 per year – or $437,000 over 25 years. If the state wants now to renegotiate the July 2017 SEBAC agreement, I have a feeling that those employees will want their money back.

I have also heard it suggested that we could solve the state’s budget problems by moving state employees into a 401k-style plan, like the Alternative Retirement Plan open to employees in higher ed. After all, the fringe rate for the ARP is only 54.12% of salary, compared to 96.4% for SERs. So switching everyone to an ARP-style plan would help, right?

Sadly, no. The difference between the SERS rate and the ARP rate is due entirely to the accrued unfunded liability. As pointed out above, the fringe rate on SERs employees includes a 33.61% charge for unfunded pension liability and another charge of 20.94% to retiree health care liability, whereas the
surcharge on ARP is a mere 3.89% to make up for past underfunding of retiree health benefits. So, were the state to move all employees into the ARP, the fringe rate would go down, but the unfunded liability would be there, big as ever. The state would simply have to account for it another way.

Indeed, moving state employees from SERS into the ARP (if you could even get SEBAC to agree to such a change, not to mention the IRS) would actually be counterproductive. When you look at the actual cost of employees’ retirement benefits, SERS is actually quite a bit cheaper than ARP: 5.41% of salary for SERS, compared to 7.44% for ARP (as of FY 18 – these numbers have both gone down slightly for FY 19 due to the SEBAC 2017 agreement). Why is SERS cheaper? Because the state assumes all of the investment risk; to get employees to assume the risk, as they do in the ARP, you have to give them an incentive.

So, including the cost of unfunded liability in the fringe rate for current employees creates an illusion – that the state could save money by transferring state employees from SERS to an ARP-style plan – when the opposite is true. There are other problems with such a proposal. For instance, if the state wanted to eliminate SERS altogether and transfer current employees retrospectively into the ARP, it would have to pre-fund the retirement benefits they would have earned had they been in the ARP since their date of hire. Doing so would require billions of dollars which the state does not have.

Through a combination of bad luck and bad policy, Connecticut has accumulated a lot of pension debt. There is no easy fix, but at least we could stop shooting ourselves in the foot, which is precisely what we do when we inflate the fringe rate paid by our students and our researchers. For these reasons, I hope that the Appropriations Committee will find some way either to reduce the fringe rate applied to University employees or, alternatively, provide UConn with additional support for fringe benefits to keep our research grants competitive.

Thank you for all your efforts on behalf of the people of Connecticut.

Sincerely,

Thomas D. Bontly
President, UConn-AAUP