

TESTIMONY OF RICHARD K. VEDDER  
BEFORE THE SUBCOMMITTEE ON RESEARCH AND TECHNOLOGY AND THE  
SUBCOMMITTEE ON OVERSIGHT,  
COMMITTEE ON SCIENCE, SPACE AND TECHNOLOGY  
U.S. HOUSE OF REPRESENTATIVES  
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Chairs Comstock and LaHood, Dr. Lipinski, Mr. Beyer, and Members of the Committee:

I am the Director of the Center for College Affordability and Productivity, and Distinguished Professor Emeritus of Economics at Ohio University.

The policy of the federal government regarding overhead or indirect cost reimbursement to universities holding research grants is seriously flawed, and potentially reduces the amount of conducted scientific research while burdening American taxpayers. Not a lot has been written about this by academic scholars who are usually not hesitant about exposing public policy deficiencies, probably largely because many of them have an enormous conflict of interest, as they themselves are recipients of federal research funds. I have not had federal research money for at least 20 years and do not expect to ever do so again, thus I am free of those conflicts.

I should say, however, that I am not alone among academics in condemning current policy. Two highly regarded economists, from Stanford and Northwestern Universities, Roger Noll and William Rogerson, writing in 1998 concluded, talking about overhead costs: "the existing system for reimbursing those costs creates unnecessary distortions in the operations of universities and has very high transactions costs. Instead, both universities and the federal government would be better off if the existing indirect cost reimbursement system were replaced by a system of fixed reimbursement rates that were not related to a university's actual indirect costs."

The reimbursement system has not changed; each university has a negotiated overhead rate, with the most prestigious, wealthiest schools typically getting much more than lowly endowed state schools with lesser resources. For example, I have read that the reimbursement rate at Harvard is about 69 percent, but at my fairly typical mid-quality state university it is only about 50 percent. To be sure, actual reimbursement for overhead is typically a good deal less than the official institutional overhead rate because of various items excluded from the base used to determine overhead amounts. Somewhat surprisingly, university overhead rates are not routinely on websites of organizations like NIH and NSF, and access to that information in the past has been restricted to the general public on the grounds that it is proprietary, an absolutely outrageous practice that should be outlawed if the current system of variable indirect cost reimbursement rates continues, which I hope it does not.

Suppose the NIH or NSF makes a new \$1 million grant to a Harvard researcher. The immediate increase in indirect costs to Harvard for buildings, administration, electricity and the

like as a consequence of that grant is probably at most a few thousand dollars; for example a bit more electricity and water may be used. However, Harvard will get several hundred thousand dollars in overhead funds. In the short run, the depreciation of building facilities tends to be ignored, and the administrative burden of having one more grant is small enough that no new staff must be added. Therefore, Harvard makes a large short-term financial gain, and thus it likely incentivizes its faculty to seek more grants. Getting a grant typically helps faculty members seeking promotion or larger salaries. It is revealing that at many schools, including my own, researchers getting federal grants directly receive a kick back of some of the overhead money for non-salary uses as an incentive to seek more grants. Schools likely would not do that unless they considered federal research grants to be at least somewhat financially lucrative.

To be sure, in the long run, the buildings and equipment where research takes place need to be replaced and there are administrators who have tasks to perform regarding sponsored research activities. In short, there are real, legitimate long run indirect costs. Yet the current system seems to incentivize universities to pad their bureaucracies, and to have excessively fancy buildings. As Boston area academic Wick Sloane put it in a *Boston Globe* story on this topic in 2013, “the more you spend, the more you get. Where’s the incentive to have linoleum floors instead of marble?” My own discussions with grant-receiving researchers find in general they believe overhead amounts are excessive. Among other things, overhead money funds bureaucrats whose job it is to promote strategies for winning grants, money better used from a broader social perspective for actual research. A fairly considerable amount of resources is devoted to justifying and verifying overhead costs—a cost with no direct impact on the quality or quantity of academic research.

Anecdotal evidence suggests that non-governmental foundations and other charitable organizations making grants to universities typically allow far lower amounts for indirect costs. What is the typical overhead reimbursement amounts for, say, the Rockefeller, Ford, Gates, or Lumina foundations? For grants I have received from private donors, it is vastly lower than the 40 percent or so typical of federal research grants. What are the policies regarding state government funded research? Again, anecdotal evidence suggests the overhead provision is smaller. What little information I have gathered hints that overhead reimbursement is lower in neighboring Canada. Why? Perhaps you should ask the Government Accountability Office to look at the reimbursement rates used by non-governmental grantors and by also by governments such as Canada, the United Kingdom, and the American states.

What should we do? The current system of negotiated rates is administratively expensive, supports excessive bureaucracies, and is arguably unfair, favoring wealthy schools over other institutions. There are two approaches to replacing the current system, either one of which would represent a great improvement, freeing up more research dollars for actual research rather than funding administrators, and promoting the use of serviceable linoleum floors over extravagant marble ones.

The first approach would be to adopt a uniform national reimbursement rate. This was proposed in the Obama Administration but was shot down by relentless lobbying by top research universities. This approach could save a good deal of money by ending the negotiations and verifications surrounding the unique individual rates on various campuses. I would predict that if a uniform federal rate of say 30 percent were adopted, you would be able to increase the amount of money going directly for research, that universities would complain bitterly but still apply for grants nearly as vigorously as ever, that over time they would pare down a bit their bureaucracies, hold fewer grant writing workshops and the like, but that life would go on much as before, with a bit more research being performed. In short, there would be more bang for the buck.

There is an alternative approach that is in some ways even more appealing, although there are some disadvantages as well. Under this approach, the decision as to who would receive research grants would be partly determined by the price of it—a radical idea perhaps to researchers but not anywhere else in society. Suppose NSF or NIH grants are made on a point system, with 100 being a maximum. Have 75 points be determined, as now, by the scientific merit of the proposal using current procedures. Have the remaining 25 points be determined by the amount of overhead the university requests, with the more points gained the *lower* the overhead request. Universities demanding huge overhead amounts would risk losing grants on the basis of cost. A school asking for 60 percent overhead for a grant might get only 1 point on the indirect cost portion of the score for the grant application, while one asking only 30 percent might get 22 points. Greedy universities with extravagant indirect cost requests would likely get fewer grants, while frugal universities willing to accept modest overhead provision would gain some advantage. The notion that indirect costs should *not* have a bearing in determining the success of a proposal is inconsistent with our scarcity of resources. The Law of Demand should apply here as it does virtually everywhere else in life.

We are in a slow growth economy with huge unfunded liabilities arising from our system of entitlements, especially Social Security and medical care expenses. Resources are scarce. Irresponsible past fiscal behavior imperils future generations, so we have a moral as well as a financial obligation to seek to minimize outlays for any given provision of public service. Consistent with that objective, it is possible to get more actual research activity per dollar of total funding by paring our support for indirect cost provisions in funded grants.

Thank you.