
September 15, 2006

CBO ANALYSIS FINDS INCREASED REVENUES WOULD OFFSET INCREASED ENTITLEMENT COSTS UNDER SENATE IMMIGRATION BILL

Often-cited Cost Figure of \$126 Billion Reflects Misreading of the CBO Report

by Robert Greenstein, Leighton Ku, James Horney, and Richard Kogan

Summary

The immigration bill passed by the U.S. Senate would affect the federal budget by increasing both the number of legal immigrants qualifying for federal entitlement programs *and* the number of immigrants filing tax returns and paying income and payroll taxes.

On August 18, the Congressional Budget Office (CBO) issued a new analysis of the budgetary effects of the immigration reform bill passed by the Senate.¹ The analysis shows that the increases in entitlement (mandatory) costs and the increases in tax revenues would roughly balance each other out. Entitlement costs would rise \$48 billion over ten years, while tax revenues would rise \$44 billion over the same period. These are essentially the budgetary effects of the controversial provisions of the Senate bill that would increase the number of legal immigrants who work in the United States, and provide a path to legalization for some workers who are currently undocumented. (Note: The CBO study presents two different estimates of the revenue effects of the bill, depending on whether an inadvertent drafting error in the bill is corrected. The estimate used here of a \$44 billion increase in revenues assumes the unintended drafting error is corrected, as it surely will be if the bill progresses.² This approach is consistent with recent CBO testimony before the Senate Budget Committee, in which CBO featured the \$44 billion estimate and said that if the bill was implemented as intended, it would increase revenues by \$44 billion over ten years.³)

¹ Congressional Budget Office, "Cost Estimate for S. 2611, Comprehensive Immigration Reform Act of 2006," Aug. 18, 2006. The new report, with revenue estimates provided by the Joint Committee on Taxation, updates an earlier CBO report (dated May 16), based on amendments adopted by the Senate before the bill passed, as well as revised technical estimates of the bill's effects on spending and revenues.

² The drafting error occurs in the section of the bill intended to exempt employers from civil and criminal tax penalties arising from the *past* employment of aliens who apply for an adjustment in status. Due to imprecise drafting, the Joint Tax Committee found that as currently written, the provision would exempt employers from such penalties even *after* immigrants apply for adjustment of status, which would enable employers not to pay payroll taxes for these workers for a substantial number of additional years. Senate Judiciary Committee staff have made clear this was not the intent; the intent was for the exemption to be applied *only* on a retrospective basis, in order to protect employers for past non-payment of such taxes, and *not* on a prospective basis. This drafting oversight could be readily fixed in conference; Judiciary Committee staff have affirmed that will be done if the bill moves forward.

³ Statement of Paul R. Cullinan, Chief of the Human Resources Cost Estimates Unit, Congressional Budget Office, before the Senate Budget Committee, August 30, 2006, page 1.

It has been reported that CBO found the Senate bill would cost the federal government \$126 billion over ten years. Not only did CBO *not* say that in its analysis, but deriving a \$126 billion estimate from what CBO did say is highly problematic in two respects and conveys a misimpression of CBO's findings. And, implying that the controversial guest worker and legalization provisions in the Senate bill would cost \$126 billion would clearly be wrong.

First, the \$126 billion figure ignores the added revenue that CBO (based on Joint Committee on Taxation estimates) found the bill would produce. The \$126 billion figure reflects the bulk of the bill's tax-related effects where there would be a cost (i.e., increased numbers of people receiving refundable Earned Income Tax Credits and Child Tax Credits) while ignoring all of the bill's effects that would generate significant increases in tax collections. Similarly, the \$126 billion estimate counts the increases in Social Security and Medicare costs that would occur under the bill while ignoring the increases in Social Security and Medicare payroll tax collections that CBO found would result. Yet most of these additional social insurance costs would occur only if the additional revenues are collected, since the payment of payroll taxes is a requirement for program eligibility.

Second, the \$126 billion figure assumes that enactment of the Senate immigration bill would result in an increase in *discretionary spending* of \$78 billion over the next ten years. But the immigration bill does not actually provide any new discretionary spending. As CBO makes clear in its analysis, the discretionary spending noted in the estimate will occur only if it is provided in future appropriation acts. The fact that the discretionary spending will not occur unless funding is enacted in future appropriation bills is the reason that — unlike in some news accounts of the estimate — CBO itself did *not* add the \$78 billion in discretionary spending to its estimate of the \$48 billion increase in entitlement costs that would occur if the Senate bill is enacted and did *not* say the bill would increase spending by \$126 billion over ten years.

The actual effect of the Senate-passed immigration bill on future discretionary spending is likely to be much smaller than \$78 billion over ten years. That figure is based on the assumptions that appropriations for every budget account authorized under the bill would be provided in every year *at the full amount authorized*⁴ — and that any increases in discretionary spending for the purposes identified in the Senate bill would simply add to the total amount of discretionary spending (that is, that there will not be *any* reductions in other discretionary spending to keep total discretionary spending within planned levels). These assumptions are highly implausible. The federal budget contains hundreds of discretionary budget accounts for which the amounts appropriated are below — often far below — the full amounts authorized. Authorizations of appropriations for discretionary programs do not constitute actual appropriations and, for that reason, generally are *not* counted by CBO, OMB, and the Congressional budget committees as representing increases in federal expenditures.⁵

⁴ In many instances, rather than authorizing a specific dollar amount of appropriations for an activity, the Senate immigration bill authorizes “such sums as may be necessary” to carry out the activity. In such cases, the dollar amount included in the estimate represents CBO's estimate of the additional funding that would be required, for instance, to increase the number of Border Patrol agents to the levels identified in the bill.

⁵ A clear indication that authorizations of appropriations neither constitute nor directly affect actual spending is that they are not subject to any controls under the Congressional Budget Act, which does impose controls on entitlement spending and appropriations, and are not even counted in the President's budget or the Congressional budget resolution.

Increases in discretionary spending can occur only when funds are actually appropriated through appropriations bills. And the Appropriations Committees must fit total appropriations for all federal programs and activities each year within an overall limit that is set in each year's Congressional budget resolution. Depending on where that limit is set, increases in appropriations for one set of programs, such as border enforcement, may result *either* in increased federal spending *or* in reduced funding levels for other appropriations programs. Such reductions may be achieved either through reductions in funding levels for specific discretionary programs or through an across-the-board reduction of a given percentage that is applied to most or all discretionary programs. An across-the-board reduction in discretionary programs has been part of the appropriations legislation enacted in *each of the past four years*.

For these reasons, even if some increase in total discretionary spending would occur in future years as a consequence of enactment of the Senate immigration bill, the actual increase would very likely be far below the \$78 billion figure included within the supposed \$126 billion total.

Moreover, it should be noted that *two-thirds* or more of the \$78 billion increase in discretionary spending would be for border and other law enforcement measures to reduce illegal immigration and apprehend and deport more illegal immigrants. And if funding to verify or adjudicate whether an immigrant is legally permitted to work in the United States is considered part of the effort to crack down on illegal immigration, the share of discretionary spending devoted to such enforcement efforts reaches 91 percent of the \$78 billion. These are costs that likely would be incurred in substantial part whether or not a measure like the Senate-passed bill is enacted. In fact, Congress already is increasing such spending without enactment of any legislation that increases the authorized level of enforcement funding. For example, in June, Congress enacted a supplemental appropriations bill that added \$1.9 billion in funding to the amounts already provided for border security. And while Congressional leaders have conceded that no agreement on an immigration bill is likely to be reached before this fall's elections, they nonetheless plan to add billions of dollars for border security and immigration enforcement to an appropriations bill they hope to enact in the next few weeks.⁶

That the growing focus in Congress on border security and enforcement makes it very likely that such costs will largely be incurred whether or not an immigration bill authorizing increased funding is enacted was made clear by Representative Harold Rogers (R-Ky), the Chairman of the House Appropriations Subcommittee on Homeland Security. At a September 12 immigration forum sponsored by the House Republican Policy Committee, Rogers said:

“ it doesn't matter whether we pass that so-called comprehensive bill with the Senate or not, insofar as border security is concerned; you're marching ahead on border security as it is, with new and innovative techniques, with *tons of money*, with increasing personnel...” (emphasis added).

Most of the controversy surrounding the Senate bill — and virtually all of the increase in entitlement costs and revenues that are projected to result from the bill — stem from its provisions to allow legalization of some undocumented immigrants and to increase levels of legal immigration, rather than from its border security provisions. To assess the fiscal impacts of the controversial

⁶ See Bill Swindell, “GOP Leaders Hope to Salvage Part of Immigration Package,” *CongressDailyAM*, September 7, 2006, p. 3.

components of the legislation, therefore, it is most appropriate to focus on the increases in entitlement expenditures and revenues. (As just explained, the bill's impact on discretionary spending is highly uncertain, and most of whatever added cost would be incurred in the discretionary area also would be incurred under immigration enforcement bills that do not increase legal immigration.)

- CBO found that over the next ten years, the *net* effect of the bill's impact on entitlement costs and revenues would be a *small* negative effect on the budget, with the new expenditures exceeding the new revenues by \$4.8 billion.
- Over the longer term, however, the bill's fiscal effects in the entitlement-and-tax area likely would be positive. The effects would be positive (i.e., they would *reduce* deficits) if the new revenues resulting from the bill rose faster than the new entitlement costs. According to CBO's analysis, that is precisely what would occur over the next ten years. In fact, over the second half of the ten-year period covered by the cost estimate (2012-2016), the estimated increase in revenues exceeds the estimated increase in entitlement costs by \$6.3 billion. In 2016, the tenth year, CBO estimates that revenues would be \$11.1 billion higher as a result of the bill while entitlement costs would be \$8.5 billion higher — resulting in a net gain for the federal government of \$2.6 billion, exclusive of any increases in discretionary spending costs.
- The new CBO analyses do not extend beyond the ten-year window, but the pattern at the end of the ten-year period suggests that federal revenue gains over the long term may equal or exceed the increases in entitlement expenditures.

Positive Effects on the Economy and Social Security Solvency

The Senate immigration bill almost certainly would increase economic growth in the United States. This is because the rate of economic growth essentially reflects the rate of growth in the U.S. labor force, the rate of growth in investment, and the rate of growth in productivity. The Senate bill would increase the size of labor force and would do so at a time when CBO, OMB, the GAO, the Social Security actuaries, and virtually all other experts forecast that labor-force growth will begin to slow down dramatically, as a result of the aging of the U.S. population, and will bring with it a slowdown in economic growth. CBO estimates that the increase in the size of the labor force that would result from the Senate immigration bill would help to address this problem and would lead to an increase in economic growth.

In an earlier analysis of the Senate bill as introduced, CBO projected that the legislation ultimately would increase the size of the U.S. economy by between 0.8 percent and 1.3 percent — amounts that are *higher* than the Administration's recently released optimistic estimate of the impact of the 2001 and 2003 tax cuts on the economy if the tax cuts are made permanent.⁷ (Due to amendments adopted on the Senate floor to reduce the size of the guest worker program, the final Senate bill would likely generate a somewhat smaller increase in growth than the original bill would.)

⁷ The Administration projects an ultimate increase in the size of the economy of as much as 0.7 percent if the tax cuts are made permanent and are paid for through spending cuts.

The Joint Committee on Taxation's estimate of the higher tax revenues that would result from the Senate bill (which is the basis for CBO's official cost estimate for the bill) only partially reflects the increase in economic growth that CBO projects would occur as result of the bill. In an addendum to its analysis of the bill as introduced in the Senate, CBO estimated that the economic factors *not* accounted for in the JCT estimate would improve the budgetary impact of the bill by *\$80 billion to \$160 billion over the next 10 years*, depending on the assumptions used about the effects of the increase in the labor force.⁸ The bill that the Senate subsequently passed would have a somewhat smaller impact since it would not increase the labor force by as much as the introduced bill.⁹ If the economic impact of the Senate-passed legislation is fully accounted for, however, the net effect of the legislation on the budget almost certainly is positive.

The immigration bill passed by the Senate also would contribute to strengthening Social Security finances, according to the Social Security actuaries. The actuaries have reported to Congress that by increasing the number of workers paying into the Social Security program, the Senate immigration bill would extend the solvency of the Social Security Trust Fund by two years (to 2042) and would reduce the Trust Fund's projected long-term deficit.¹⁰

Further detail on several of these matters follows.

Effect on Entitlement Costs and Revenues

As the CBO estimate indicates, the bill's impact on entitlement costs would be small in the initial years, because few immigrants would qualify in those years for benefits such as Medicare, Social Security, and Medicaid. Over time, more immigrants who are legalizing would qualify for assistance. The number of legalized immigrants who would receive means-tested assistance, however, would remain relatively modest. Under the Senate bill, to qualify for guest-worker status and eventually to earn citizenship, immigrants would have to meet a number of qualifications, including steady employment, payment of back-owed taxes, knowledge of English, and payment of substantial penalties and fees. The immigrants able to meet all of these criteria are likely primarily to be those who are self-supporting and do not need or qualify for most means-tested benefits.¹¹

⁸ CBO estimates that in addition to directly increasing economic output, the projected increase in the labor force also would lead to an increase in investment, which would further boost GDP. CBO's estimate of the overall effect of the Senate bill on economic growth depends on which of two alternative assumptions it makes about the extent of the increase in investment that would occur.

⁹ CBO did not update its economic analysis to reflect the changes made to the bill during Senate consideration, but CBO's Paul Cullinan testified that the Senate-passed bill also would have positive economic effects not reflected in in the Joint Committee on Taxation's estimate of the bill, although the effects "would be smaller because of that bill's more modest impact on the labor force." Testimony of Paul Cullinan before the Senate Budget Committee, August 30, 2006, page 8. Since CBO estimates the Senate-passed version of the bill would increase the workforce by about two-thirds as much as the introduced bill, the economic effects of the Senate-passed bill would likely be about two-thirds as large as CBO estimated for the original bill.

¹⁰ Letter from the Chief Actuary of the Social Security Administration to Senator Charles Grassley, July 24, 2006.

¹¹ Federal concerns about increased entitlement costs under the bill have been inflamed by a Heritage Foundation report claiming that the Senate bill would ultimately increase federal entitlement and discretionary program costs by \$30 billion per year. The CBO estimates suggest that the Heritage estimates are several times too high. The Heritage estimates have been sharply criticized by a number of other analysts as being severely flawed. See, for instance, White House Office of Media Affairs, "Setting the Record Straight: Heritage Foundation Report Overestimates Legal Immigration

CBO and Social Security Actuaries Find Senate Immigration Bill Would Promote Economic Growth and Strengthen Social Security's Finances

Critics of the Senate immigration bill portray it as a long-term drain on the budget and the economy. Analyses by CBO and the Social Security Administration, however, indicate that the Senate bill would have positive effects on the nation's economy and also would strengthen Social Security's finances.

In May, CBO estimated that the immigration bill introduced in the Senate would increase the size of the economy (the Gross Domestic Product, or GDP) by between 0.8 percent and 1.3 percent on average from 2012 to 2016.* This suggests that the nation's economy could be roughly \$170 billion to \$270 billion larger in 2016 than without the bill's enactment. The economy would grow more because there would be additional workers. The rate of economic growth is essentially determined by the rate of growth in the U.S. labor force, the rate of growth in investment, and the rate of growth in productivity.

CBO's estimate of increased economic growth was based on the Senate bill as introduced. Amendments passed on the Senate floor reduced the number of immigrants who would be admitted to the United States, so the economic impact for the final Senate bill would be somewhat less.

CBO has noted that the Joint Committee on Taxation, following its normal practice, did *not* take these macroeconomic estimates fully into account in estimating the bill's effect on tax revenues. Had the projections of the bill's effects on the economy been fully accounted for, the estimated revenue growth would be substantially larger than the official estimate and the budgetary effects of the legislation would almost certainly be shown to be beneficial.

Somewhat similar conclusions were reached by the Social Security actuaries.** Their analysis of the Senate immigration bill found that the increases that would result in the number of legal immigrant workers would produce increases in the level of payments made into the Social Security Trust Fund, which would help strengthen Social Security for citizens and immigrants alike. The Social Security actuaries project that the Senate-passed bill would extend Social Security solvency by two years (from 2040 to 2042) and that the Social Security Trust Fund balance would be improved in all of the next 75 years.

* Congressional Budget Office, "Additional Information on the Estimated Budgetary And Economic Effects of S. 2611," May 16, 2006.

** Letter from the Chief Actuary of the Social Security Administration to Senator Charles Grassley, July 24, 2006.

CBO and the Joint Committee on Taxation also project that legalization would increase the size of the labor force in the United States and reduce the likelihood that immigrants are paid "under the table," thereby leading to increases in federal income and payroll tax collections. The bill would establish other fees and penalties, as well, which immigrants seeking to legalize would be required to pay.

CBO projects that the added federal revenues would rise gradually over the next ten years and reach \$11.1 billion in new revenue in 2016, which is \$2.6 billion more than the \$8.5 billion CBO projects in added entitlement costs for that year. If the entitlement costs and revenue increases

Increase Under Senate Immigration Bill," May 18, 2006, and The American Immigration Law Foundation, "Immigration Scare-Tactics: Exaggerated Estimates of New Immigration Under S.2611," May 2006. (http://www.aifl.org/ipc/policybrief/policybrief_2006_scaretactics.shtml)

resulting from the bill continued to rise after 2016 at the same pace that CBO projects for the years from 2013 to 2016, revenues would continue to outstrip entitlement costs over the longer term.

Border Security and Related Enforcement Costs

The CBO analysis shows that two-thirds or more of the discretionary costs authorized under the bill would be for increased border security and law enforcement. Of the \$33.2 billion in increased authorizations for discretionary expenditures under the bill over the next five years, \$21.5 billion — or 65 percent — would be for increases in the number of border agents and other law enforcement and legal personnel; detention facilities to detain aliens pending their removal from the United States; increased port security; expanded border-control infrastructure; new border-control aircraft and watercraft; additional State Department agents to investigate identify theft and document fraud; increased costs for National Guard units to perform security functions along the Mexican border; grants to reimburse state and local governments for costs of apprehending, deterring, and helping to prosecute illegal immigrants; expansion of a Justice Department system that assists in the removal of illegal immigrants from the country; and increased federal prison costs associated with the incarceration of individuals for offenses involving illegal entry into the United States. (CBO provides itemized break-outs for these costs only for the next five years.)¹² Moreover, if the additional costs of verifying or adjudicating employment and immigration status — which should be considered part of the immigration enforcement effort — are included in this category, the share of discretionary costs under the bill that would be dedicated to deterring illegal immigration rises to 91 percent of all discretionary costs.

Many of these costs would likely be incurred under any immigration bill, regardless of whether it provides illegal immigrant workers a path to legal status. In fact, many of these costs would likely be incurred under existing law; almost all of these activities are already authorized, and policymakers are increasingly focusing on these issues and on providing increased funding for border security and enforcement.

¹² The \$21.5 billion over five years consists of: \$7.74 billion in grants to state and local governments for costs of apprehending, deterring, and prosecuting illegal immigrants; \$3.58 billion for increases in the number of border agents and other law enforcement personnel dedicated to interdicting or apprehending illegal immigrants; \$3.26 billion for improved border-control infrastructure; \$2.64 billion for facilities to detain aliens pending their removal from the country; \$1.39 billion for border control aircraft and watercraft; \$850 million for port security; \$500 million for National Guard units to perform security support functions along the Mexican border; \$450 million for unmanned aerial reconnaissance vehicles; \$400 million to expand the Justice Department's system that assists in removing illegal immigrants from the country; \$310 million to reimburse local agencies for prosecution costs at U.S. border; \$195 million in grants to law enforcement agencies near U.S. borders; \$125 million for additional State Department agents to investigate identify theft and document fraud; and \$70 million for increased federal prison costs resulting from imposing mandatory minimum sentences on individuals for offences involving illegal entry into the United States. If additional costs for employment verification and status adjudication are included in this list, the total reaches \$30.3 billion over five years. These additional costs include \$3.6 billion for the new Labor Department investigators; \$2.5 billion for a major expansion of DHS Employment Eligibility Verification System; \$1.6 billion for an expansion of DHS immigration adjudication services; \$670 million for Justice Department immigration judges and attorneys; and \$410 million for the Labor Department's certification program.