

# Economic and Budgetary Implications of Immigration Reform

Testimony presented to the  
U.S. Senate  
Committee on the Judiciary

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\*The views expressed here are my own and do not represent the position of the American Action Forum. I thank Laura Collins, Gordon Gray, and Cameron Smith for tremendous assistance in preparing this testimony. All remaining errors are my own.

## Introduction

Chairman Leahy, Ranking Member Grassley and members of the Committee, I am pleased to have the opportunity to appear today. In this testimony, I wish to make three basic points:

- Immigration reform is a potentially powerful tool of economic policy that can positively affect economic growth and help shrink the federal deficit. My recent analysis of a benchmark reform puts the budgetary impact in the range of \$2.5 trillion over 10 years;
- The Congressional Budget Office's analysis of the proposed immigration reform legislation in 2007 provides a good starting point for estimating the budgetary costs of the current immigration reform proposal; and
- Immigration enforcement programs in the proposed legislation are largely expansions of current and well-established programs such as the Secure Fence Act and E-Verify, likely reducing the discretionary spending required to implement the expanded programs.

I will pursue each in additional detail.

### **The Federal Budget Costs of Immigration Reform: Overview**

An estimate how any reform to the nation's immigration system will ultimately affect federal finances will reflect the net effect of gross federal costs and gross federal savings and/or revenues in the context of the broader economy. There are thus many moving pieces to this calculation and it is critical to consider all them. This is properly the job of the Congressional Budget Office. However, some additional perspective may be helpful before, and even after, an official cost estimate for a reform proposal is available.

A good starting point for this discussion is the cost-estimate for the last comprehensive reform legislation considered by the Senate in 2007.<sup>1</sup> This is not meant to equate the 2007 proposal with the one considered at present. Rather, to the extent that any comprehensive immigration proposal involves key elements included in the 2007 bill, the associated cost estimate can provide a clearer picture of how those elements interact with the federal budget and provides a useful benchmark for assessing the potential costs of the current undertaking.

The cost estimate from the 2007 bill showed essentially three budgetary flows:

- An increase in federal direct spending of \$23 billion over the 2008-2017 period, most of which was attributable to refundable income tax credits and Medicaid;

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<sup>1</sup> <http://www.cbo.gov/publication/18716>

- An increase in federal revenues by \$48 billion over the 2008-2017 period, most of which from greater receipts payroll taxes, which are classified as off-budget; and
- An increase in discretionary spending (that is, spending subject to annual appropriation action) \$43 billion over the 2008-2017 period.

Gross costs exceeded gross receipts, and therefore yielded an increase in the unified budget deficit of \$18 billion over ten years. While not an insignificant sum, \$18 billion over a decade is swamped by the economic and technical changes that would be made over that period – and pales in comparison to the budgetary duress of these times. To my eye, it is essentially a budgetary wash.

This estimate offers a good starting point to illustrate the magnitudes of certain costs and benefits that we could expect to accrue from a comprehensive immigration reform. However, it is not 2007 anymore. It is important to consider what has happened since then to get a sense of how the relevant budgetary effects of a comprehensive immigration reform may have changed.

#### *Direct Spending*

The element subject to the largest degree of change is direct spending. Undoubtedly, the single largest change is the Patient Protection and Affordable Care Act (ACA), and the implications of comprehensive immigration *vis-à-vis* the ACA have necessarily received considerable attention.

I remain convinced that the ACA itself is poor economic, budget and health policy. However, I would caution policy-makers against reliance on any policy analysis that exploits the failures of the ACA to suggest a comprehensive immigration reform would pose outsized cost on taxpayers. There are two key flaws with some analysis I have seen on this matter. First, as noted above, any accurate measure of the budgetary effects of a comprehensive immigration reform will include multiple budgetary flows – including higher revenues from additional tax payers. An analysis that only focuses on costs is necessarily one-sided and tells only half the story.

Second, assumptions matter a great deal. Take-up and program participation rates significantly affect federal programmatic outlays. Assumptions of high program participation will drive up related spending, while assumptions of lower participation will diminish programmatic spending. Moreover, assumptions related to future changes in law can significantly alter federal spending.

A recent publication by the Senate Budget Committee suffers from both such flaws. The publication stated “that costs could be upwards of \$40 billion in 2022 alone, just for Medicaid and Obamacare. The long-term unfunded liability for Obamacare would grow another \$2 trillion.”<sup>2</sup> This estimate focuses exclusively on cost and ignores net new

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<sup>2</sup> <http://www.budget.senate.gov/republican/public/index.cfm/budget-background?ID=76f68efd-5f90-4301-aa2b-fdcfd18fe744>

revenue, and is by its nature incomplete. Setting aside this issue, the estimate itself relies on unrealistic assumptions. The estimate apparently assumes a 100 participation rate and assumes that the global cap on ACA subsidies in current law is not in place. With a more reasonable estimate of program participation and acknowledgement of current law – this single year estimate drops to less than 9 billion, based on the Committee’s own estimates. The long-term estimate similarly diminishes– revealing an overstatement of costs over the long by half an order of magnitude.

More directly, the immigration reform proposal considered today contemplates *no* new ACA spending for the currently undocumented population within the 10-year window. To the extent that reforms may increase *legal* immigration compared to what would otherwise be the case, the spending on Medicare, refundable tax credits, and other federal benefits would increase as the population of “eligible aliens” increases. This was also the case in 2007 and is not a new phenomenon.

### *Revenues*

There has been no change in payroll tax law since 2007 that would materially alter the relative magnitude of how an immigration reform would raise additional revenues.

### *Discretionary Spending*

Since 2007, border security continued to receive attention and federal resources. It is not within my expertise to assess the security state of the nation’s borders. Rather it is important to note that nearly 6 years have elapsed since the 2007 cost estimate during which time the nation has spent considerable sums on security and immigration enforcement measures. As such, incremental discretionary spending on the order of the 2007 bill may not be necessary to achieve similar outcomes, as much of that spending has occurred notwithstanding the failure to pass the 2007 measure.

Since 2007, immigration enforcement spending has totaled \$95 billion.<sup>3</sup> This includes *discretionary* spending on U.S. Customs and Border Protection (CBP), U.S. Immigration and Customs Enforcement (ICE), the United States Visitor and Immigrant Status Indicator Technology Office (US-VISIT), and U.S. Citizenship and Immigration Services (USCIS); and includes supplemental spending as well as funds provided by the American Recovery and Reinvestment Act (ARRA).

Some of this spending would have occurred anyway. However, it is useful to understand how much is essentially “new” – or above what would have otherwise been spent over that time period. This can be observed by establishing a baseline beginning with 2007 and projecting this type of spending in the future consistent with CBO methodology. This baseline would have seen \$82 billion spent on immigration enforcement over 2008-2013. Accordingly, the U.S. provided \$13 billion in *new* (i.e. above baseline) immigration enforcement over 2008-2013.

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<sup>3</sup> Similar to the methodology used to categorize “immigration enforcement” spending as defined here: <http://www.migrationpolicy.org/pubs/enforcementpillars.pdf>; all budget data can be found here: <http://www.dhs.gov/dhs-budget>

It is difficult to reconstruct funding streams from the programs proposed in the 2007 bill. Some may or may not have gone into place anyway (like E-Verify, additional Border Patrol agents, use of surveillance technology, and fences), or came about in different ways. This exercise does not seek to do that. Rather, it does suggest that to the extent the 2007 was proposing \$28 billion in new discretionary spending over 2008-2013, quite a bit has been spent anyway in pursuit of the same objective.<sup>4</sup>

This estimate suggests that the federal government spent close to but not quite half of what the 2007 bill proposed: 46 percent. This suggests that the additional discretionary spending in any bill subsequent to 2007 may be relatively smaller.

### *Dynamic Effects*

The CBO's cost estimate will provide key insight into how the current proposal will impact federal finances. However, consistent with scoring rules, it will do so on a "static" basis – one that does not take into account the effects of immigration reform on the national income. It is this element that must be considered even after a formal cost estimate is available.

The mechanics of reform and the research literature suggest that immigration reform can raise the overall pace of population growth – indeed, in the absence of immigration, low birth-rates mean that the U.S. population will actually shrink. Because foreign-born individuals tend to have higher rates of labor force participation, this translates into an even more rapid pace of growth in the labor force. At historic rates of population growth, this immediately translates into more rapid overall growth in Gross Domestic Product (GDP).

There are, however, two reasons for even further impacts. Immigrants have traditionally displayed an entrepreneurial bent, with rates of small business ownership above that of the native born population. New entrepreneurial vigor offers the potential for productivity-enhancing innovations. In addition, to the extent that new innovation is "embodied" in new capital and consumer goods, more rapid economic growth per se means that more output will have these advances embedded within, and productivity per worker will rise.

Taken as a whole, these channels of impacts suggest that any discussion of immigration reform that omits the benefits on economic performance is incomplete. Similarly, there will be direct feedback from better economic growth to more revenues, fewer federal outlays, and improved budgetary performance. These links are fundamentally "dynamic" in the jargon of federal budgeting. They stem from the fact that policy changes reshape the growth environment, and thus in turn reshape the budget. Traditional "static" budget analyses will be similarly incomplete.

Taken together, the overall growth rate in real GDP would rise from 3.0 percent to 3.9 percent, on average annually, over the first 10 years.<sup>5</sup> The upshot is that GDP after 10

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<sup>4</sup> The 2013 is an extrapolation of the 2008-2012 values presented in the cost estimate.

<sup>5</sup> Some of this rise would be "transitory" in that once labor force participation rates stabilized, the difference would decline to 0.6 percentage points over the longer term.

years would be higher – a difference of \$64,700 per capita versus \$62,900 per capita. This higher per capita income of \$1,700 after ten years is a core benefit of immigration reform.

This new growth drives the “dynamic” budgetary impacts of immigration reform. How large are these impacts? One metric is the CBO “rules of thumb” for the linkages between the pace of real GDP growth and the federal budget. These indicate that over 10 years an additional 0.1 percentage in average economic growth will reduce the federal deficit by a bit over \$300 billion.<sup>6</sup> In this context, the rules imply that over the first 10 years of the benchmark immigration reform, the federal deficit would be reduced by a cumulative amount of \$2.7 trillion.

#### *Net Effect*

Changes in direct spending and discretionary spending policies since 2007 will necessarily alter the federal costs of any new immigration proposal. However, the current proposal takes great care to mitigate the most significant change direct spending policy (ACA) while benefiting from significant resources having been devoted to immigration enforcement since 2007. These changes move in opposite directions. It is therefore reasonable that the net budgetary effects of the current proposal should be roughly neutral on a “static” basis. Taking into account the “dynamic” effects of immigration reform, the budgetary effect is far different. Deficit reduction from higher growth – combined higher tax revenues from higher incomes, lower mandatory spending from diminished participation in income and employment-related spending programs, and interest savings – would exceed \$2.5 trillion.

#### **Immigration Enforcement Programs Currently in Place**

As I stated earlier, border security programs have received attention and federal resources since before 2007. The current proposed immigration reform legislation expands some of the programs currently in place, such as the Secure Fence Act and E-Verify. As such, incremental discretionary spending on the order of 2007 may not be necessary to achieve similar outcomes as much of that spending has occurred notwithstanding the failure of the 2007 measure.

#### *The Secure Fence Act of 2006*

The Secure Fence Act of 2006 requires the Secretary of Homeland Security to take appropriate actions to achieve operational control over U.S. international land and maritime borders through the use of surveillance technology such as unmanned aerial vehicles, ground-based sensors, satellites, radar coverage, and cameras; checkpoints; and physical infrastructure such as fencing. The Act also requires the Secretary to conduct a study on border security on the northern international border.

The border security provisions of the proposed immigration reform legislation build on the provisions in the Secure Fence Act. These provisions include surveillance and detection capabilities developed or used by the Department of Defense; additional Border Patrol agents and Customs and Border Protection officers at and between ports of entry along the southern international border; fixed, mobile, and agent portable surveillance systems; and

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<sup>6</sup> [http://www.cbo.gov/sites/default/files/cbofiles/attachments/01-31-2012\\_Outlook.pdf](http://www.cbo.gov/sites/default/files/cbofiles/attachments/01-31-2012_Outlook.pdf)

unmanned aerial systems and fixed-wing aircraft with qualified staff and equipment to fully utilize the systems.

### *E-Verify*

Since it was originally created in the 1996 Illegal Immigration Reform and Immigrant Responsibility Act, E-Verify has been extended by legislation filed every few years. E-Verify has grown and changed since its creation, with enrollment increasing by 35% in 2012 and more than 424,000 employers enrolled. E-Verify is currently voluntary except for businesses in those states that have mandated its use.

The proposed immigration reform legislation mandates E-Verify nationwide, including for agricultural businesses, over a 5-year phase-in period. The mandated E-Verify system will also include biometric work authorization cards for non-citizens and a photo database for employers to use as part of the certification process. The Secretary of Homeland Security will create and administer a grant program to reimburse states that provide the Secretary access to driver's license information. The Secretary is also required to develop an effective security measure to verify individuals without the photo tool. Finally, the proposed legislation requires U.S. Customs and Immigration Services to develop a system for employees to check their own E-Verify history as well as "lock" their Social Security number in the system.

Because these programs are already well-established, the expansions required in the proposed immigration reform legislation are unlikely to result in discretionary spending at the levels estimated for the failed 2007 immigration reform legislation.

### **Dynamic Economic Analysis of the Current Immigration Reform Proposal**

The United States faces interrelated challenges of weak economic growth and dramatic levels of projected growth in federal debt. The threats posed by this environment on economic opportunity and the social safety net have been the focus of recent federal policy debates.

Inspection of the breadth of the impacts of immigration reform suggests that it will have important economic impacts. This represents an economic policy opportunity at the same time; indeed the degree to which immigration policy *is* economic policy has been traditionally underappreciated in the United States. In this way, immigration reform can be thought of as another tool to address its growth and fiscal challenges.

The mechanics of reform and the research literature suggest that immigration reform can raise the overall pace of population growth – indeed, in the absence of immigration, low birth-rates mean that the U.S. population will actually shrink. Because foreign-born individuals tend to have higher rates of labor force participation, this translates into an even more rapid pace of growth in the labor force. At historic rates of population growth, this immediately translates into more rapid overall growth in Gross Domestic Product (GDP).

There are, however, two reasons for even further impacts. Immigrants have traditionally displayed an entrepreneurial bent, with rates of small business ownership above that of the native born population. New entrepreneurial vigor offers the potential for productivity-enhancing innovations. In addition, to the extent that new innovation is “embodied” in new capital and consumer goods, more rapid economic growth *per se* means that more output will have these advances embedded within, and productivity per worker will rise.

Taken as a whole, these channels of impacts suggest that any discussion of immigration reform that omits the benefits on economic performance is incomplete. Similarly, there will be direct feedback from better economic growth to more revenues, fewer federal outlays, and improved budgetary performance. These links are fundamentally “dynamic” in the jargon of federal budgeting. They stem from the fact that policy changes reshape the growth environment, and thus in turn reshape the budget. Traditional “static” budget analyses will be similarly incomplete.

#### *U.S. Demography and Immigration Policy*

According to the Pew Research Center, America’s birth rate has fallen to its lowest level since 1920 when record keeping began. At current rates, there will be an average of 1.93 children born to each child bearing aged woman in the U.S. In contrast, the replacement rate in the U.S. and other developed countries is roughly 2.1. This leads to the most important and striking fact: because native-born women are having fewer than an average of 2.1 children in their lifetimes, in the absence of immigration the population of the United States will decline and the size of its economy will contract.

Immigrants have a much higher birth rate than native-born women. For native-born women in 2012, the birth rate was 58.4 per 1,000 women compared to 87.8 for foreign-born women.<sup>7</sup> In 2007, 25 percent of all U.S. births were from foreign-born mothers, compared with 16 percent in 1990. (That share has decreased slightly in more recent years to 23 percent.)

It is often said that demography is destiny. If so, the U.S. destiny is fairly daunting. As Jonathan Last put it, “If you strip these immigrants—and their relatively high fertility rates—from our population profile, America suddenly looks an awful lot like continental Europe, which has a fertility rate of 1.5, not quite as demographically terminal as Japan.”<sup>8</sup>

Given that immigration has such profound economic implications, it is interesting to note that immigration to the United States has primarily been concerned with family reunification. In 2010, 74 percent of our permanent immigrants were for purposes of family reunification, greater by far than any other OECD country. In this way, the U.S. remains an outlier when compared to the rest of developed economies, who since the 1980’s all promote reunification to a far lesser extent than we do. Australia, Canada, and the United Kingdom undertook reforms to focus their system on economic growth and less

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<sup>7</sup> <http://www.pewsocialtrends.org/2012/11/29/u-s-birth-rate-falls-to-a-record-low-decline-is-greatest-among-immigrants/>

<sup>8</sup> <http://online.wsj.com/article/SB10001424127887323375204578270053387770718.html>

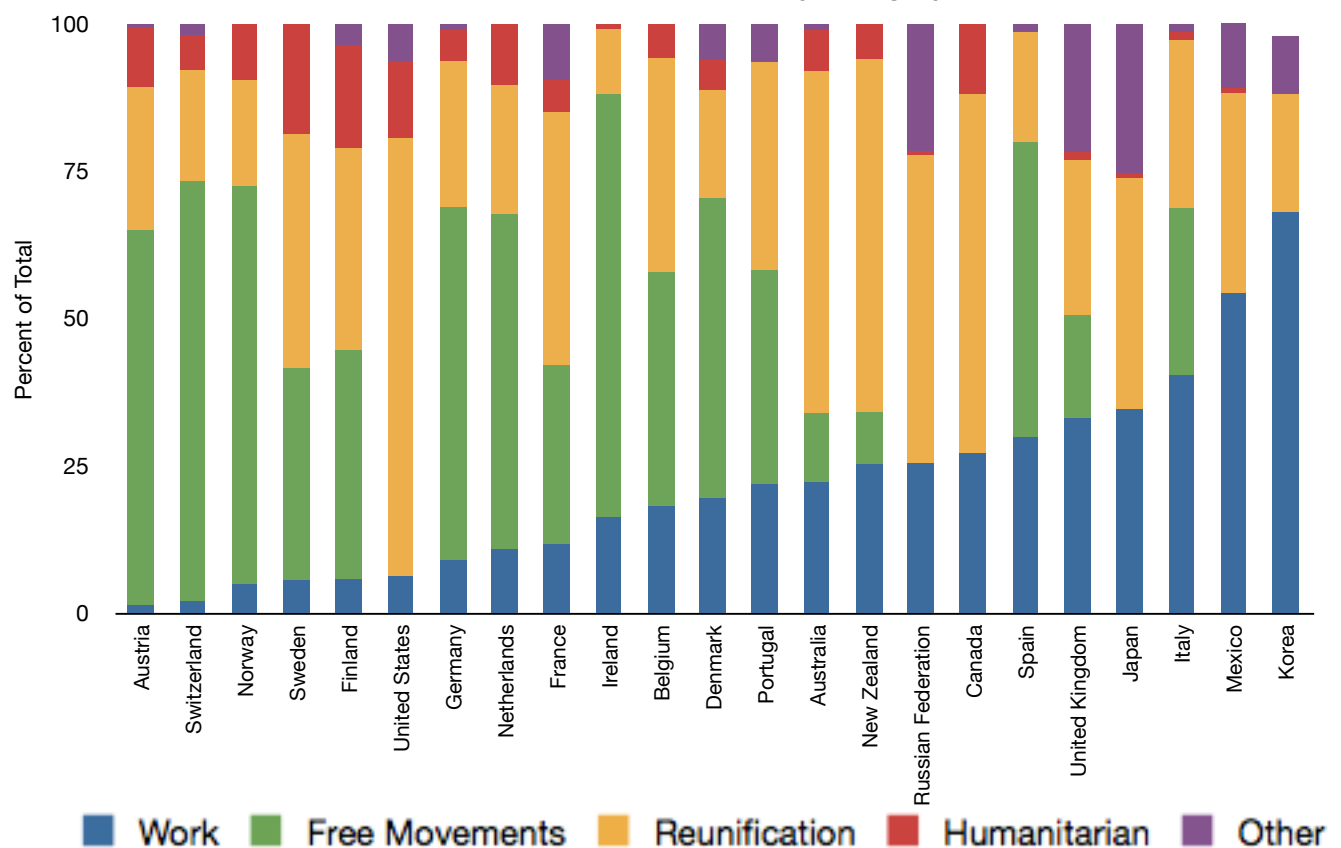


so on reunification. As evidenced in chart 1, the United States remains behind the bulk of other countries whose immigration policies attract immigrants for purposes of work. In 2010, the United States issued a mere 6.4 percent of visas for economic reasons, compared to the United Kingdom's 33 percent.

This paucity of economic focus is not due to a lack of applications. The United States has always been a place that immigrants want to come to work and start businesses. According to the US Citizenship and Immigration Service, the denial rate for L-1B visas, those set aside for employees with “specialized knowledge,” reached an all-time high of 27 percent in 2011.<sup>9</sup>

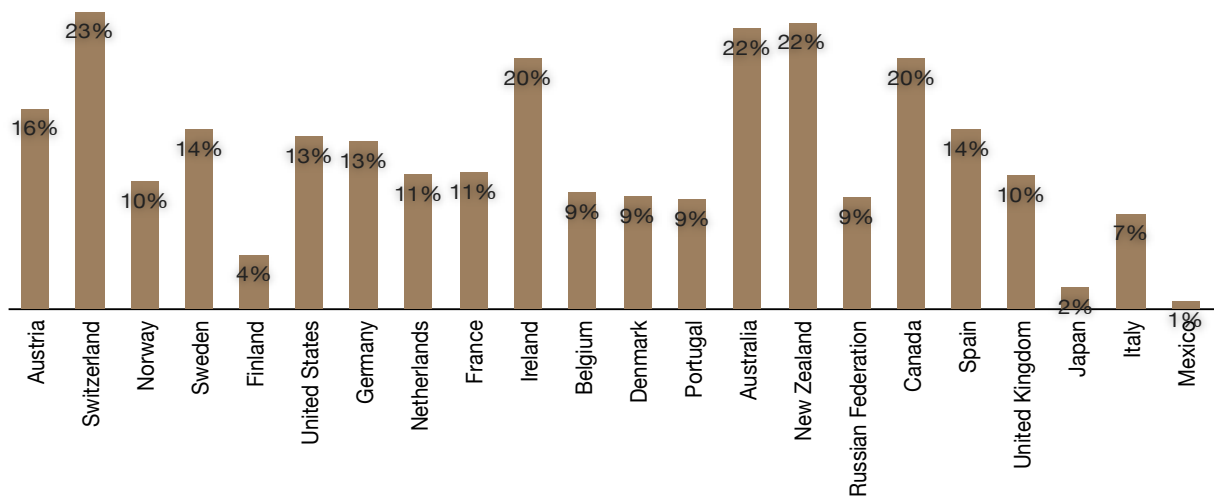
These trends suggest that any immigration reform will have deep economic implications, that such a reform should be thought as a one additional tool in economic policy, and that reform should be – at least in part – evaluated from an economic perspective.

**Chart 1: Permanent Inflows by Category, 2010**



<sup>9</sup>[http://www.nfap.com/pdf/NFAP\\_Policy\\_Brief.USCIS\\_and\\_Denial\\_Rates\\_of\\_L1\\_and\\_H%201B\\_Petitions.February2012.pdf](http://www.nfap.com/pdf/NFAP_Policy_Brief.USCIS_and_Denial_Rates_of_L1_and_H%201B_Petitions.February2012.pdf)

**Chart 2: Immigrants as a Percentage of Population, 2010**



### *Demography and Economic Growth*

The building blocks of economic growth are not complex. Total GDP stems from the total number of workers and the average output per worker, or productivity. The pace of overall population growth will raise the number of workers, and thus raise GDP. In addition, the structure of the population – by age, gender, and education – can influence the fraction of the population at work. Growth in the labor force participation rate can, in turn, raise the rate of GDP above the rate of population growth.

Similarly, the structure of the population affects productivity; thus changes in education and other aspects of the population can influence the growth of productivity. However, there is a further impact between demography and productivity that works through the overall pace of economic growth.

Research suggests that innovation is at least in part embodied into the quality of consumer and, especially, capital goods.<sup>10</sup> To the extent this is true, productivity will be higher as the opportunities for this embodiment to take place are greater. In particular, at higher rates of *overall* GDP growth, there will be greater replacement of existing capital goods and investment in new capital goods.<sup>11</sup>

<sup>10</sup> For a nice discussion, see <http://www.frbsf.org/publications/economics/letter/2002/el2002-05.html>

<sup>11</sup> Estimates suggest that this channel could be responsible for up to 20 percent of productivity growth. See <http://www.nber.org/papers/w3971.pdf> or <http://www.carnegie-rochester.rochester.edu/april03-pdfs/a03laitnerstolyarov.pdf>

To close the circle, more rapid overall population growth would generate more rapid GDP growth, which would in turn raise productivity growth. The latter raises GDP per capita, or the standard of living.

### *Immigration Reform and Growth*

As federal policymakers contemplate immigration reform, it is useful to include in the discussion the demographic channels on economic growth. For example, the difference between the low-immigration and high-immigration projections by the U.S. Census amounts to more rapid population growth of nearly 0.2 percent annually (from 0.81 percent to 0.99 percent).<sup>12</sup> If we think of the difference between these projections as a hypothetical immigration reform, such a population-enhancing reform would raise GDP growth as well.

As noted above, there would be effects above and beyond that of greater population as well. Labor force participation rates are higher among the foreign-born, especially among males and later in work careers.<sup>13</sup> Similarly, the rates of entrepreneurship among immigrants are higher than among the native born population, raising the possibility of greater innovation and productivity growth in the aftermath of immigration reform.<sup>14</sup> Finally, the combined effect of these impacts on economic growth would allow greater productivity growth through the embodiment effect on quality of capital goods.

How large might these effects be? Returning to the Census projections permits one to piece together the kinds of impacts immigration reform might produce. In the interest of being conservative, consider the difference between the “constant net migration” and “high net migration” scenarios.<sup>15</sup> The more rapid population growth translates directly into more rapid GDP growth rates by 0.25 percent annually over the first 10 years. As noted above, there would be an additional growth impact as the economy benefited from adjusting to a labor force growth rate that would be higher by 3.2 percentage points (after fully phasing in the immigration population). In addition, the more rapid economic growth might raise productivity by another 20 percent through the embodiment effect. Summing the impacts, the overall growth rate in real GDP would rise from 3.0 percent to 3.9 percent, on average annually, over the first 10 years.<sup>16</sup> The upshot is that GDP after 10 years would be higher – a difference of \$64,700 per capita versus \$62,900 per capita. This higher per capita income of \$1,700 after ten years is a core benefit of immigration reform.

### *The Economy and the Budget*

Immigration reform will also influence the budget outlook through its impacts on economic growth. These impacts are “dynamic” effects in the parlance of federal budgeting. That is,

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<sup>12</sup> See <http://www.census.gov/population/projections/data/national/>

<sup>13</sup> See [http://www.census.gov/compendia/statab/cats/labor\\_force\\_employment\\_earnings/labor\\_force\\_status.html](http://www.census.gov/compendia/statab/cats/labor_force_employment_earnings/labor_force_status.html)

<sup>14</sup> For a great summary, see <http://www.sba.gov/sites/default/files/rs396tot.pdf>

<sup>15</sup> The computations here use actual 2012 GDP and economic growth rates in the most recent CBO *Budget and Economic Outlook* as the baseline for comparison.

<sup>16</sup> Some of this rise would be “transitory” in that once labor force participation rates stabilized, the difference would decline to 0.6 percentage points over the longer term.

any budgetary analysis that is conducted strictly using the baseline economic growth impacts will necessarily be incomplete by excluding the impacts that produce more rapid economic growth.

How large are these impacts? One metric is the CBO “rules of thumb” for the linkages between the pace of real GDP growth and the federal budget.<sup>17</sup> These indicate that over 10 years an additional 0.1 percentage in average economic growth will reduce the federal deficit by a bit over \$300 billion. In this context, the rules imply that over the first 10 years of the benchmark immigration reform, the federal deficit would be reduced by a cumulative amount of \$2.7 trillion.

It is important to emphasize that ballpark estimates of this type are exactly that: ballpark. At even half the estimated size, they should be an important component of the debate. Even more important, it would be even more incorrect to exclude these effects and thus *de facto* assert that they are zero.

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<sup>17</sup> See [http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/120xx/doc12039/01-26\\_fy2011outlook.pdf](http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/120xx/doc12039/01-26_fy2011outlook.pdf)