

# **A Cost-Benefit Analysis of the New Alabama Immigration Law**

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## **Summary**

- This report presents an initial cost-benefit analysis of HB56, the new Alabama immigration law. Potential economic benefits of the law include (i) saving funds used to provide public benefits to illegal immigrants, (ii) increased safety for citizens and legal residents, (iii) more business, employment, and education opportunities, and (iv) ensuring the integrity of various governmental programs and services.
- The law's economic costs include implementation, enforcement, and litigation expenditures; increased costs and inconveniences for citizens, other legal residents, and businesses; fewer economic development opportunities; and the economic impact of reduced aggregate demand as some illegal immigrants leave and therefore no longer earn and spend income in the state. The annual economic and fiscal impacts of the reduction in aggregate demand caused by 40,000-80,000 unauthorized immigrant workers who earn between \$15,000 to \$35,000 a year leaving the state are reductions of about (a) 70,000-140,000 jobs with \$1.2-5.8 billion in earnings, (ii) \$2.3-10.8 billion in Alabama Gross Domestic Product (GDP) or 1.3-6.2 percent of the state's \$172.6 billion GDP in 2010, (iii) \$56.7-264.5 million in state income and sales tax collections, and (iv) \$20.0-93.1 million in local sales tax collections.
- Some of the law's costs and benefits are qualitative and others are quantifiable, but difficult to estimate. While the law's costs are certain and some are large, it is not clear that the benefits will be realized. From an economist's perspective, the question Alabama and its legislature have to ponder is this: Are the benefits of the new immigration law worth the costs?

## **Introduction**

HB56, Alabama's new immigration law, has generated a lot of attention since its passage in the 2011 legislative session. Portions of the law have been prevented from going into effect by various courts. Several business, religious, and civic organizations have opposed the law—though not always in its entirety—and from these groups have come calls for repealing or amending the law. There are debates as to whether the state or federal level is the proper place to tackle the illegal immigration issue. The Governor has called for the law to be simplified and some legislators have indicated a willingness to revisit the law. Yet it can be argued that the legislature was only doing what it thought the people wanted since surveys had routinely

indicated that people wanted something done about illegal immigration. People still want something done about the issue even after passage of the law, but at least one survey has shown that HB56 might not be ideal.

Section 1 of the law gives its formal name, the Beason-Hammon Alabama Taxpayer and Citizen Protection Act, and Section 2 provides the rationale or basis for the law.<sup>1</sup> Although not explicitly stated, one can deduce from these two sections that the intent of the law is to deal with the illegal immigration issue. The soundness of the findings in the rationale is debatable, but the intent cannot be faulted since it tries to deal with an identified problem. Despite the good intent, the law has costs and benefits that must be weighed as the legislature ponders next steps. This is not unique to this law as all policies, regulations, and laws need be subjected to serious economic analysis to ensure that they do not impose unnecessary or avoidable costs to society. Indeed, the goal is to ensure that they are beneficial to both the private and public sectors of the economy so that society reaps a net benefit.

No extensive economic analysis of the law has been presented since its passage and this has led to ongoing debates about the law's economic effects on the state. An extremely conservative example of an effect of the law that was in a preliminary macroeconomic assessment has been widely and wrongly referred to as the law's economic cost or impact.<sup>2</sup> The main point of the preliminary macroeconomic assessment is that the law will be costly to the state since it reduces aggregate demand in the Alabama economy. This is because economies are demand-driven and so any policy, regulation, law, or action that reduces demand will shrink the economy no matter how well-intentioned. More people translates into increased demand and fewer people means decreased demand. HB56 will cause the state population to be lower than it would otherwise be as some illegal immigrants leave. The law will therefore decrease demand and shrink the state economy.

Some might argue, wrongly, that supply activities contribute to economic growth. In truth, it is the demand creation (e.g., payroll and other expenditures) involved in goods production or service provision that drives the economy. After all, supply activities are only undertaken to meet demand somewhere (in domestic or export markets). Supply does not always meet demand as it sometimes can be short of or exceed demand, creating shortage or excess inventory. This is the basic reason why economic impact analysis is based on expenditures to meet demand and not revenues generated from supply.

Tackling illegal immigration in an economic analysis is no easy task because their illegal status might cause these unauthorized immigrants to try to avoid notice as much as possible and thus make very solid data on such immigrants hard to come by. Indeed, one of the things HB56 tries to do is collect some pertinent data. Fortunately, the U.S. Department of Homeland Security (DHS) and the Pew Research Center (PRC) provide useful estimates of the unauthorized immigrant population in the nation and for the states.<sup>3</sup> The DHS Office of Immigration Statistics also publishes a yearbook of immigration statistics. Both PRC and DHS use the official statistics and U.S. Census Bureau surveys for their estimates of illegal immigrants in the country. It is

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<sup>1</sup> HB56 can be viewed online at <http://alisondb.legislature.state.al.us/acas/ACASLoginFire.asp>

<sup>2</sup> The preliminary macroeconomic assessment is available at <http://cber.cba.ua.edu/rbriefs/New%20AL%20Immigration%20Law%20-%20Prel%20Macro%20Assessment-1.pdf>

<sup>3</sup> See for example Passel and Cohn (2011) at <http://pewhispanic.org/files/reports/133.pdf> and Hoefler, Rytina, and Baker (2010) at [http://www.dhs.gov/xlibrary/assets/statistics/publications/ois\\_ill\\_pe\\_2010.pdf](http://www.dhs.gov/xlibrary/assets/statistics/publications/ois_ill_pe_2010.pdf)

common knowledge, however, that some illegal immigrants may be omitted because they do not respond to the Census Bureau surveys often out of fear of exposure and deportation. The PRC makes adjustments for those omitted and thus has somewhat higher estimates than the DHS, but the trends in both estimates are very similar (Table 1).

**Table 1. Estimates of Unauthorized Immigrant Population in the United States (Millions)**

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
U.S. Department of Homeland Security	10.5	11.3	11.8	11.6	10.8	10.8
Pew Research Center	11.1	11.3	12.0	11.6	11.1	11.2

Source: See footnote 3.

An economic analysis of HB56 is clearly needed, especially given the high likelihood that the law will be revisited in the 2012 legislative session. This report provides such an analysis of the law in the hopes that it will inform the debate and help the legislature to address the law in a manner that benefits the Alabama economy. To keep Alabama on a ROLL, any changes to the law must seek to boost economic development by growing demand and facilitating continuation of the economic strides that the state has been making.

## **Benefits and Costs of HB56**

In analyzing any policy, regulation, law, or action one has to consider the goal(s) or intent, consider options to achieve the goal(s) and their outcomes, and evaluate those outcomes and determine the best option in terms of outcomes and implementation in order to make a recommendation. The specific questions to ask in the analysis include:

1. What is the intent or what do we want to achieve?
2. What options are available to achieve the intent or goals?
3. What are the outcomes of each option?
4. What costs are involved in achieving the goals and how can they be minimized?
5. Are there any benefits to achieving the goals and if so, do they exceed the costs and how can they be maximized?
6. If there are no identifiable benefits, how much are we willing to spend?
7. Are costs and benefits distributed fairly and if not, how much should losing parties be compensated and how?
8. What is the best option to pursue and at what pace?

### **Benefits of HB56**

The text of the law suggests that its potential economic benefits to the state include (i) savings of funds used to provide public benefits to illegal immigrants, (ii) increased safety for citizens and other legal residents, (iii) more business, employment, and education opportunities for legal residents, and (iv) ensuring the integrity of various governmental programs and services. Some of these benefits are quantitative and others are qualitative. However, it is not clear that these benefits will be realized but each one is considered below.

***Savings of funds used to provide public benefits to illegal immigrants.*** The two most common benefits that illegal immigrants are said to enjoy are healthcare services at emergency hospitals and clinics and educational services (mainly for their children). No one knows for sure how much savings will be generated because of the significant uncertainty regarding the hard data required. However, as unauthorized immigrants try to avoid notice as much as possible any such savings is likely to be small. The Passel and Cohn (2011) report from the Pew Research Center notes that about 82 percent (4.5 million) of the estimated 5.5 million children of unauthorized immigrants in 2010 are U.S.-born. In 2000 this share was about 58 percent (2.1 million out of 3.6 million). Thus the number and share of U.S.-born children of unauthorized immigrants have been rising while those of unauthorized immigrant children have been falling and all indications are for this trend to continue. This means that savings on educational services are likely to be small and decline over time. On healthcare benefits, the contagious nature of some diseases could make it worthwhile to treat illegal immigrants when they get sick and so it is not clear that significant savings will be realized, especially if the law only causes unauthorized immigrants to go further underground and become less visible rather than leaving the state altogether. If the law causes them to self-deport, then some healthcare savings will be generated.

***Increased safety for legal residents.*** This benefit depends on whether illegal immigrants commit crimes and endanger public safety at a higher or lower rate than citizens and other legal residents. There is a benefit only if the rate is higher for illegal immigrants. Considering that most illegal immigrants are seeking to better their lot, it is more likely that the rate would be lower for them. This could be partly because they are aware their status means that they are breaking the law in the first place. Some argue that this is the very reason that illegal immigrants should not be welcomed, but the law is not costless and its costs have to be considered.

***More business, employment, and education opportunities for legal residents.*** It is generally accepted that unauthorized immigrants work for low wages. As such, the absence of illegal immigrants is likely to improve competitiveness for businesses that found it extremely difficult to compete because they do not use such labor. This might make the business climate attractive for out-of-state businesses that do not use illegal immigrant labor to consider relocating to the state. Such benefits for some businesses do not translate into a benefit for the aggregate economy because they cannot fully make up for the reduced demand caused by the absence of unauthorized immigrant workers.

It is also argued that illegal immigrants take jobs that should have gone to citizens and other legal residents. If that were true, farmers and businesses that employed these workers and other business interests as well should not have complained about the law especially given the state's high unemployment rate. There was very little worker substitution and most of the few that considered the jobs previously performed by unauthorized immigrant workers did not have the requisite skills and productivity. With a focus on preparing the workforce for high-skill, high-wage and fast-growing jobs, it is unreasonable to expect people to flock to lower wage jobs that are performed under tough conditions. Rather the focus should be on facilitating economic development so that existing and new businesses are able to offer more high-skill, high-wage and fast-growing jobs. As a result, and also for other reasons, HB56 cannot be credited with reductions in the unemployment rate except when more previously-held by illegal immigrant jobs than the unemployment rate would cover are taken up by unemployed legal residents and citizens. This is because the unemployment rate is a ratio of the number of unemployed to the number of people in the labor force. So for example, if the unemployment rate is 9 percent, then

the law can be said to have provided employment opportunities only if unemployed legal residents and citizens fill more than 9 of every 100 jobs vacated by illegal immigrants at the same skill and productivity levels. Anecdotal evidence to date seems to point to less than 9 of every 100 vacated jobs being filled by unemployed legal residents and citizens. Also, recent data show employment falling in the four sectors (agriculture, construction, accommodation, and food and drinking places) that are often alleged to employ migrant and unauthorized workers. Other factors to consider before the law can be credited with respect to employment include (i) how many illegal workers were counted in the employed and unemployed components of the labor force, (ii) whether unemployed legal residents and citizens have the skills and desire to take and hold on to the jobs vacated by illegal immigrant workers at the wages that employers are willing to pay if they continue operating, and (iii) whether domestic and international trade can substitute for in-state activities that employed illegal workers.

Whether the law will provide improved or more education opportunities or not is debatable. The argument here is that education services funds spent on illegal immigrants and their children can be used to provide better education or cover more students. This is based on the wrong assumption that illegal immigrants do not pay taxes. They pay some taxes and the economy enjoys certain benefits as a result of the demand created by their presence. Also, they are not as much of a drain on the economic system as they are thought to be by some people. First, at the level of income they receive many illegal workers might not have to pay federal income tax because of the standard deduction and personal exemption levels allowed. Indeed they could receive earned income tax credit, which many do not file for because they wish to remain below the radar and their status makes it practically impossible. In addition, they make payroll taxes with little chance of ever benefiting from those social safety net programs unless somehow they become legal. They also pay sales and property taxes directly and indirectly through their income spending and consumption activities.

***Ensuring the integrity of various governmental programs and services.*** This can only be a benefit of the immigration law if illegal immigrants use governmental programs and services dishonestly. Because they wish to remain undetected, illegal immigrants usually apply for services for their legal children when required to by state and national laws; sometimes these laws specify provision of the services to children. As such, the integrity of governmental programs and services is ensured by HB56 only if illegal immigrants fraudulently use the services at a higher rate than legal residents fraudulently use the same services.

### **Costs of HB56**

The law's economic costs to the state include (i) implementation, enforcement, and litigation expenditures, (ii) increased costs and inconveniences for citizens, other legal residents, and businesses, (iii) reduced economic development opportunities, and (iv) the economic impact of reduced aggregate demand due to some illegal immigrants leaving and therefore not earning and spending income in the state. Some of these costs are qualitative and others are quantifiable, but difficult to estimate. These possible costs are addressed below.

***Implementation, enforcement, and litigation costs.*** HB56 calls for the Alabama Department of Homeland Security (ADHS) and the Attorney General (AG) to see to the implementation and enforcement of the law by giving them additional duties that include (i) ADHS putting together a unit of state law enforcement officers who will be trained to specifically enforce the immigration

law and (ii) the AG defending the law in court, ensuring that policies do not restrict HB56 or federal immigration laws, and entering into a memorandum of agreement with the United States Department of Homeland Security concerning enforcement of federal immigrations laws. These activities will certainly impose additional costs on the state, but it is not currently known by how much. Some might argue that enforcement expenditures will also help the economy, but without additional revenue this spending will take funds away from provision of other public services and as such is sure to have a net negative macroeconomic effect especially at a time when government funds are tight because of the contraction in demand that the law causes and the slow economic recovery.

***Increased costs and inconveniences for citizens, other legal residents, and businesses.*** Besides the numerous penalties for violating the law, HB56 seems to impose additional costs and burdens on businesses and citizens and other legal residents. People have had to spend long times in lines for basic services like car tag renewals because of the lawful presence verification requirements of the law. Businesses have to use E-Verify and ensure for the purposes of contracts with the state that they deal only with other businesses that also use E-Verify so as to not violate the law. The Immigration Policy Center (IPC) issued a special report detailing how two of the law's 34 sections—Sections 27 and 30—make life harder for all not just the illegal immigrants.<sup>4</sup> These increased costs and inconveniences are real but difficult to estimate.

***Reduced economic development opportunities.*** Many economic development practitioners have noted that the new immigration law projects a negative image of the state to the world making it difficult to recruit foreign companies. This is mainly because the law seems to paint Alabama as an anti-immigrant state even though the law is supposed to target illegal immigration. Two incidents involving Mercedes and Honda officials were really embarrassing and there was an ad in a Missouri newspaper inviting the Mercedes plant in Alabama to relocate. Many economic developers and existing businesses believe that the law increases costs and time for doing business but produces no return. Reduced economic development opportunities present a mix of qualitative and quantitative costs that are not easy to estimate.

***Economic impact of reduced aggregate demand.*** The law has caused some illegal immigrants to leave, in some cases even when their children or other family members are legal residents. This reduces the population which in turn causes aggregate demand to fall, a negative shock to the state economy. The economy can still grow but it will be on a lower growth path than would have been the case without the law. The reduction in aggregate demand affects business sales, employment, earnings, the state's Gross Domestic Product (GDP), and tax collections. It is not known exactly how many people left the state due to the law and it is also somewhat early to fully determine the total economic effects of the law on the state economy. However, using 2010 data as basis because it is the most recent year for which there is a complete set of data, some preliminary estimates of impact follow. Multipliers obtained from the Regional Input-Output Modeling System (RIMS II), which was developed and is maintained by the U.S. Department of Commerce's Bureau of Economic Analysis (BEA), were used in a model developed specifically for this analysis. Ranges of the number of people who actually left and the income they could have earned are used in the model to allow for uncertainty.

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<sup>4</sup> The IPC special report is available at [http://www.immigrationpolicy.org/sites/default/files/docs/Friedland\\_-\\_Alabama\\_Contracts\\_and\\_Business\\_110111\\_0.pdf](http://www.immigrationpolicy.org/sites/default/files/docs/Friedland_-_Alabama_Contracts_and_Business_110111_0.pdf)

In the analysis, fiscal impacts are derived from the earnings impacts allowing for the fact that not all of the earnings impacts are sales or income taxable. Spending on sales taxable items constitute 42.4 percent of total earnings based on U.S. Bureau of Labor Statistics (BLS) data and state taxable income (net income) is about 66 percent of earnings. Sales tax rates used are 4.0 percent for the state and 5.0 percent for local (combined county and city) jurisdictions; local sales tax rates vary between 3.0 to 7.0 percent but are usually at 5.0 percent. The state income tax rate is essentially 5.0 percent on net income; the first \$500 and the next \$2,500 are taxed at 2.0 percent and 4.0 percent, respectively, for single persons, head of family, and married persons filing separately while for married persons filing joint returns the first \$1,000 and the next \$5,000 are taxed at 2.0 percent and 4.0 percent, respectively, and excess net income is taxed at the 5.0 percent rate. Corporations pay at a 6.5 percent rate and corporate income tax averages about 15 percent of individual income tax. State law in 2006 increased the individual income tax threshold by raising the standard deduction for taxpayers with adjusted gross income of \$30,000 or less and by increasing the dependent exemption for taxpayers with adjusted gross income of \$100,000 or less. State sales and income taxes are the largest components (constituting about 62 percent) of total state tax collections; residents and businesses pay a host of other taxes and fees. Only sales and income taxes are reported here and as such the fiscal impacts are conservative.

Table 2 shows employment and earnings per worker in 2010 for the four sectors that are often alleged to employ unauthorized workers. Successful unannounced immigration officer raids of businesses reported in the media suggest that other sectors (e.g., manufacturing) also employ such workers. There were more than 361,000 workers earning a little over \$30,000 on average in the four sectors. This information and the Passel and Cohn (2011) PRC estimates of the illegal immigrant population in Alabama are used to determine the economic impact of the reduction in aggregate demand caused by HB56 (See Footnote 3 for source.). For 2010 there were 120,000 unauthorized immigrants in the state with 95,000 in the labor force. Assuming 10,000 were unemployed means that there were 85,000 employed illegal immigrants in the state for the year; an upper bound of 80,000 vacated jobs and a lower bound of 40,000 are used in the impact analysis.

**Table 2. Employment and Earnings in Sectors Alleged to Use Illegal Immigrant Workers**

	<u>2010 Employment</u>	<u>4-Sector Share</u>	<u>Earnings per Worker</u>
Agriculture (crop and animal production)	50,224	13.9%	\$18,150
Construction	147,637	40.9%	\$47,250
Accommodation	17,187	4.8%	\$22,964
Food services and drinking places	146,314	40.5%	\$17,954
<b>All four sectors</b>	<b>361,362</b>	<b>100.0%</b>	<b>\$30,189</b>

Source: U.S. Bureau of Economic Analysis and Center for Business and Economic Research, The University of Alabama.

Major assumptions in the analysis are that (1) HB56 causes unauthorized immigrant workers to vacate jobs primarily in the four sectors shown in Table 2 and that the vacated jobs are distributed according to the 4-sector shares; (2) about 40,000 to 80,000 illegal immigrant workers earning \$15,000-\$35,000 annually have left the state as result of the immigration law, and (3) unauthorized immigrant workers send 20 percent of their earnings to their home countries. The income range chosen is lower than the state's roughly \$40,000 average earnings

per worker in keeping with the belief that these workers hold low-wage jobs. Table 3 shows that the annual economic and fiscal impacts of the law given the assumptions are reductions than would otherwise have been of (a) 69,768-139,536 jobs with \$1.2-5.8 billion in earnings for these jobs, (ii) \$2.3-10.8 billion in Alabama Gross Domestic Product (GDP) or 1.3-6.2 percent of the state's \$172.6 billion GDP in 2010, (iii) \$56.7-264.5 million in state income and sales tax collections, and (iv) \$20.0-93.1 million in local sales tax collections.

**Table 3. Economic and Fiscal Impacts of HB56 the New Alabama Immigration Law**

<b>Employment Impact</b>			
Direct jobs vacated	40,000	60,000	80,000
Total direct and indirect job loss	69,768	104,652	139,536
<b>Total Direct and Indirect Earnings Lost (\$ Billions)</b>			
	Number of direct jobs vacated		
Earnings per job	<u>40,000</u>	<u>60,000</u>	<u>80,000</u>
\$15,000	1.2	1.9	2.5
\$25,000	2.1	3.1	4.1
\$35,000	2.9	4.3	5.8
<b>Alabama GDP Contraction (\$ Billions)</b>			
	Number of direct jobs vacated		
Earnings per job	<u>40,000</u>	<u>60,000</u>	<u>80,000</u>
\$15,000	2.3	3.5	4.6
\$25,000	3.8	5.8	7.7
\$35,000	5.4	8.1	10.8
<b>State Sales and Income Taxes Lost (\$ Millions)</b>			
	Number of direct jobs vacated		
Earnings per job	<u>40,000</u>	<u>60,000</u>	<u>80,000</u>
\$15,000	56.7	85.0	113.4
\$25,000	94.5	141.7	189.0
\$35,000	132.3	198.4	264.5
<b>City and County Sales Tax Loss (\$ Millions)</b>			
	Number of direct jobs vacated		
Earnings per job	<u>40,000</u>	<u>60,000</u>	<u>80,000</u>
\$15,000	20.0	29.9	39.9
\$25,000	33.3	49.9	66.5
\$35,000	46.6	69.8	93.1

Rounding effects may be present.

Source: U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics, Alabama Department of Revenue, Alabama Department of Industrial Relations, and Center for Business and Economic Research, The University of Alabama.



## Conclusions and Discussions

This report presents an initial cost-benefit analysis of HB56, the new Alabama immigration law and finds that the law is rather costly to the state. Economies are demand-driven so any policy, regulation, law, or action that reduces demand will not contribute to economic development no matter how well-intentioned. Nobody can fault the intent of the immigration law, which targets illegal immigration, but the law itself is costly mainly because it reduces demand in the state economy. Instead of boosting state economic growth, the law is certain to be a drag on economic development even without considering costs associated with its implementation and enforcement. Some of the law's costs and benefits are qualitative and others are quantifiable, but difficult to estimate. While the law's costs are certain and some are large, it is not clear that the benefits will be realized. From an economics perspective, the preferences of a state are not to be judged and therefore the issue is whether the benefits of HB56 are worth the costs.

Many farmers and business owners have been complaining about and fighting the law. At best, the new immigration law might help to reduce illegal immigration and lower the unemployment rate, but even those effects are not guaranteed. Economies have formal and informal components and the law is likely to drive a portion of the formal component into the informal, basically sending illegal immigrants out of state or underground. In either case, demand in the Alabama economy is reduced since the income generated by these people and their spending will decline. That results in a shrinking of the state economy and will be seen in lower economic output, personal income, fewer jobs, and lower tax revenues than would otherwise have been.

Potential economic benefits of the law include saving funds used to provide public benefits to illegal immigrants; increased safety for citizens and legal residents; more business, employment, and education opportunities; and ensuring the integrity of various governmental programs and services. The law's economic costs include the spending on its implementation, enforcement, and defense in court; increased costs and inconveniences for citizens, other legal residents, and businesses; fewer economic development opportunities; and the economic impact of reduced aggregate demand as some illegal immigrants leave and therefore no longer earn and spend income in the state. Assuming that the law causes 40,000-80,000 unauthorized immigrant workers who earn \$15,000-35,000 a year to leave the state, the resulting decline in aggregate demand would have annual economic and fiscal impacts of reductions of about (i) 70,000-140,000 jobs with \$1.2-5.8 billion in earnings, (ii) \$2.3-10.8 billion in Alabama GDP or 1.3-6.2 percent of the state's \$172.6 billion GDP in 2010, (iii) \$56.7-264.5 million in state income and sales tax collections, and (iv) \$20.0-93.1 million in local sales tax collections. The law is well-intentioned but just one cost component, the impact of the reduction in aggregate demand that the law causes, shows that the law will be costly to the state even without considering other costs.

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