

JULY 11, 2018 | NUMBER 121

Understanding the Effects of Legalizing Undocumented Immigrants

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Many countries host large numbers of undocumented immigrants. By many accounts, the United States leads this ranking. According to the Pew Research Center, in 2010 there were as many as 11 million unauthorized immigrants on American soil, representing 26 percent of all immigrants. These large numbers of undocumented immigrants have led recent U.S. administrations, not without controversy, to consider either legalizing these immigrants or deporting many of them to their countries of origin.

The United States is not alone in hosting undocumented immigrants. Migration Watch UK estimated the undocumented immigrant population in the United Kingdom to be 1.1 million in 2010, representing more than 13 percent of all immigrants in the country. A European Commission research project on undocumented migration, the Clandestino Project, estimated that, in 2008, there were between 1.9 and 3.8 million undocumented immigrants in the EU27, representing between 7 percent and 13 percent of the total immigrant population.

In the early 2000s, Spain experienced a large immigration boom. From 1995 to 2004, the share of immigrants in the working-age population increased from less than 2 percent to around 10 percent. Many of these newly arrived immigrants lacked work permits. According to some accounts, as many

as 1 million immigrants—in a country of around 43 million inhabitants—were undocumented by 2004.

Despite the prominence of undocumented migration in public debates, we know relatively little about the effect of legalizing the work status of immigrants. Most academic research has focused on understanding how legal status affects immigrants themselves. We know from this work that gaining legal status is beneficial to immigrant workers in a number of ways. However, we still know relatively little about how the mass legalization of immigrants affects the overall host economy. Our research addresses this gap using a unique natural experiment.

On March 14, 2004, voters in the Spanish general election had to determine whether the Popular Party would continue in power or be replaced by the Socialist Party. In the week before the election, the outcome seemed clear: the polls were forecasting that José Luis Rodríguez Zapatero of the Socialist Party was trailing Mariano Rajoy of the Popular Party by 7 percentage points. Yet something completely unexpected happened just three days before the election which, as shown by economist José García-Montalvo, changed the final outcome: Madrid suffered the largest terrorist attack in Spanish history, a tragedy that was poorly managed by the Popular Party. As a result, the Socialist Party came to power, and one of the first policies it implemented was to legalize nearly 600,000 immigrants already living (and working illegally) in Spain.

Thus, we can use this episode as a natural experiment to estimate the effects of the policy change on a number of outcomes. To build a continuous difference-in-differences estimator, therefore, we compare Spanish provinces that had large immigrant populations before the policy with those that had small immigrant populations. Overall, we show that legalizing a large number of mainly low-skilled immigrants meant the following:

- Newly legal workers started to contribute to the social security system, thus increasing public revenues.
- Immigrant low-skilled workers became more than 30 percent more expensive, while still remaining cheaper than low-skilled natives.
- Immigrant low-skilled workers became closer substitutes for native low-skilled workers as they gained work permits.

These three insights guide our exploration of the effects of legalizing immigrant workers on public revenues and on the labor market.

We first estimate that, for each newly legal immigrant, payroll-tax revenues increased by around €4,189 at the local level. This increase is roughly 50 percent of what we would have anticipated given the 3 percentage-point increase in workers registered in the social security system as a result of the legalization. This finding suggests that either newly legal immigrants earned less than average workers or that other workers were also affected by the policy change—or a combination of both.

Second, we investigate the effect of the amnesty program on the labor-market outcomes of various types of workers. Using very detailed administrative and survey data on wages and employment, we show that the policy change disproportionately affected the labor market outcomes of workers in high-immigrant locations relative to low-immigrant locations. In particular, it worsened employment opportunities for both low-skilled natives and immigrants, while it improved them for high-skilled workers. Among low-skilled natives, those who lost their jobs were negatively selected—the policy change negatively affected employment prospects of native low-skilled workers at the bottom of the wage distribution. In total, the increased labor costs implied by the legalization meant that around 0.5 jobs were destroyed for each newly legal immigrant.

We also show that, following the reform, many immigrants moved from locations with a high population of immigrants to locations with a low population of immigrants. This finding is important because these immigrants also contributed to payroll tax revenues, but in locations that traditionally had a low population of immigrants. This, in turn, means that comparing local payroll tax revenues in areas that have a high population of immigrants with areas that have a low population of immigrants to evaluate the effect of the policy may underestimate the true effect of immigrant legalization on payroll tax revenues.

Once we take into account internal migration and selection, we argue that the true contribution was almost €5,000 per newly legal immigrant, which is substantially higher than what we would have been able to estimate on the basis of local tax revenue data alone. Given that before the policy change undocumented immigrants already had access to public education and public health care, this estimate represents a net gain in tax revenues. This estimate would be even larger if we included income taxes that newly legal immigrants started to pay. Thus, these results highlight important public revenue losses associated with not granting work permits to immigrant workers.

To the best of our knowledge, this research is the first to combine public-revenue data and detailed labor-market data to account for the various channels through which amnesty programs can affect the economy. It provides the first account of the potential gains and losses that such policies may bring. On the one hand, it provides clear evidence that the policy succeeded in one of its goals: increasing tax revenues from workers who were already working but were not contributing to public finances. On the other hand, we show how the policy had important distributional consequences—low-skilled workers probably lost, while highly skilled native and immigrant workers benefited.

NOTE

This research brief is based on Joan Monras, Javier Vázquez-Grenno, and Ferran Elias, “Understanding the Effects of Legalizing Undocumented Immigrants,” CEPR Discussion Paper no. 12726, Centre for Economic Policy Research, London, February 2018, https://cepr.org/active/publications/discussion_papers/dp.php?dpno=12726.