

Analysis: U.S. immigration probe fears weigh on Chipotle

Mon, Feb 28 2011

By [Lisa Baertlein](#) and [Mary Milliken](#)

LOS ANGELES (Reuters) - An investigation by U.S. immigration officials into illegal unemployment at Chipotle Mexican Grill Inc (CMG.N: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#)) is making some investors nervous and could have implications for the fast-food industry as a whole.

Chipotle, based in Denver, is one of the highest-profile employers to come under the scrutiny of Immigration and Customs Enforcement (ICE) in recent years. And the investigation into its hiring practices has served as a wake-up call for the nation's nearly 580,000 restaurants.

The rapidly expanding burrito chain -- famous for keeping a tight grip on labor costs and coming off a two-year stock gain of 350 percent -- far exceeded Wall Street's profit expectations when it reported quarterly results on February 10.

But the shares have since fallen 4.5 percent. A handful of analysts have downgraded Chipotle shares due in part to uncertainty about the liabilities and costs related to immigration audits, which have expanded from about 50 restaurants in Minnesota to Chipotle's 60 restaurants in Virginia and Washington, D.C.

Some industry watchers downplay the risk because the audits are not happening in the usual hot spots such as California, New York or Chipotle's home state of Colorado. But others are not so quick to dismiss the extent to which labor costs may rise if Chipotle were forced to replace illegal workers.

"My gut tells me this is a real issue, especially for fast-food restaurant chains leveraging cheap labor in high immigration states," said Richard Fearon, founder and chief investment officer at Accretive Capital, a hedge fund based in Madison, Connecticut.

"There is a large, vote-yielding bull's-eye painted on its back and sitting in the cross-hairs of the politicians," said Fearon, who invests in restaurant operators, but does not hold Chipotle shares.

Chipotle fired 450 people, or nearly 40 percent of its workers in Minnesota, following the ICE probe.

So far, the affected restaurants represent just a fraction of the 1,084 Chipotle locations nationwide, but analysts and fund managers that follow the stock market darling are now asking how many other states and how many of its roughly 25,000 employees could be ensnared.

Probes in additional markets "would create downward pressure for the stock. I think it's a risk," said Miller Tabak analyst Stephen Anderson, who downgraded Chipotle last month to "hold" from "buy."

Anderson told Reuters that a federal immigration probe in California -- home to 165, or about 15 percent, of the company's total restaurants -- would be "very significant" in terms of incremental costs for Chipotle, which owns and operates its restaurants, if it resulted in mass firings.

Investors also are worried about the impact on the \$300 billion U.S. restaurant industry, which historically is heavily dependent on immigrant labor and is now getting squeezed by higher costs for everything from beef to produce.

While some experts estimate that legal and illegal immigrant workers account for around one-fourth of the restaurant industry work force, 40 percent of workers surveyed by Restaurant Opportunities Center for a 2005 report said they did not have legal status to work in the United States.

WORKING ON TIPS

ICE fines are not the primary worry because they totaled a paltry \$7 million last year.

"The potential penalties are unlikely to significantly impact shareholder value. I think it is the prospect of these chains needing to access more expensive labor pools which may rattle the market a bit more," Fearon said.

ICE will not give any clues to its next moves and has not publicly acknowledged it has audited Chipotle.

Chipotle, meanwhile, is publicly contrite, but confident it can turn the corner and get back to living by its motto "Food With Integrity."

The likelihood of future audits depends on results from current audits, said Victor Cerda, a former general counsel at ICE, who is now a partner at the law firm Jackson Lewis in Washington, D.C.

"It doesn't cost ICE much to expand an audit," said Cerda, who does not represent Chipotle.

The question is what happens next. Experts said ICE does not necessarily crack down harder on employers in states or cities where illegal laborers are more prevalent.

One thing ICE will say is that it now works on leads, whereas years ago it targeted specific industries where it believed there was a high risk of hiring unauthorized workers.

"Although by law we are allowed to randomly pick companies or self select, by practice we prefer to go after companies where we have leads or information," an ICE official told Reuters on the condition of anonymity.

Who tipped them off to Chipotle is still a mystery.

U.S. immigration enforcement has shifted considerably over the decades and most recently the Obama administration has chosen to crack down on employers rather than the illegal workers themselves.

Many employers complain government guidance on how to comply with immigration law is unclear and burdensome. They question the effectiveness of enforcement as the country struggles with its 12 million illegal immigrants and the growing anger in the electorate about the jobs they take.

ICE's ultimate goal is to show "that there is knowledge by the employer or reckless disregard for the law," the official said, adding that the 26 officers in charge located throughout the country have great authority to choose who they target.

"If we are going to dedicate resources to something, we want to make sure it is in our best interest," said the ICE official. "We would love to have the resources to go after every employer in every location, but we need to be smart about how we spend our time and resources."

(Additional reporting by [Herbert Lash](#); editing by [Andre Grenon](#), [Bernard Orr](#))