REGULATING IMMIGRATION THROUGH FISCAL POLICYMAKING: REEXAMINING TEXAS' NEW MARGIN TAX

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I. INTRODUCTION

Recently, the Texas legislature revamped the state's business tax system by significantly altering the state franchise tax.[1] This new franchise tax base is different than other franchise tax bases which tend to tax businesses on their assets, net worth, or capital stock.[2] That is, the Texas franchise tax is more of a modified income tax in that the tax base for this tax is generally the net of a company's gross revenue minus the greater of the company's cost of goods sold or compensation.[3] Within the Texas tax code this tax base is also known as the "taxable margin" which is presumably where the franchise tax received its popular name, the "Margin Tax."[4]

When House Bill 3 ("HB 3"), which created the Margin Tax, was passed through the Texas legislature in the Spring of 2006, it specified which items would be included in the cost of goods sold and compensation deductions.[5] The bill also specified which items would be excluded from these categories of deductions.[6] One of these items was compensation paid to undocumented workers, which is excluded for both the cost of goods sold[7] and compensation deductions in the Margin Tax. A deduction for this compensation expense is generally permitted for federal tax purposes.[8]

This article will discuss the legal validity of the Texas Legislature's attempt to deny a tax deduction for compensation paid to undocumented workers by taxpayer entities. In particular, the article will analyze to what extent the Texas

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1. *See* H.B. 3, 79th Leg., 3d C.S. (Tex. 2006).

2. *See* Franchise Tax, Investopedia.org, http://www.investopedia.com/terms/f/franchise_tax.asp (last visited Oct. 5, 2008).

3. The taxable margin is the lesser of 70% of an entity's total revenue or total revenue minus either the entity's compensation or cost of goods sold deductions, as defined by statute. *See* TEX. TAX CODE ANN. § 171.101 (Vernon 2008); Chris Atkins & Jonathan Williams, *Reforming Property Taxes in the Lone Star State*, THE TAX FOUNDATION, May 11, 2006, *available at* http://www.taxfoundation.org/commentary/show/1493.html; *see also* Texas Margin Tax FAQ, WOOD, JOHNSON, HEATH, P.C., *available at* http://www.wjh-cpa.com/faqs_and_tips/margin_tax_faq.html#why_a_new_law (last visited Oct. 5, 2008).

4. *See* TEX. TAX CODE ANN. § 171.101.

5. *See* H.B. 3, 79th Leg., 3d C.S. (Tex. 2006); TEX. TAX CODE ANN. § 171.1012; *see also* TEX. TAX CODE ANN. § 171.1012-13.

6. *See* TEX. TAX CODE ANN. §§ 171.1012(e), 171.1013(c), (f)(1), (h).

7. *See id.* §§ 171.1012(e)(14), 171.1013(c)(1).

8. *See* Andrew Sharp, *Tax Accounting for Illegal Activities*, ENTREPRENEUR.COM, Dec. 2006, *available at* http://www.entrepreneur.com/tradejournals/article/print/113306511.html; *see also* I.R.C. § 162(c) (2004).

legislature may regulate this area given the state and federal equal protection privileges and traditional federal preemption of state regulation in the immigration context. This article will also consider various public policy implications regarding this method of immigration regulation.

II. BACKGROUND

A. *Meeting the Texas Supreme Court's Deadline*

On November 22, 2005 the Texas Supreme Court ruled in *Neeley v. West Orange-Cove Consolidated Independent School District* that the state's public education finance system violated the Texas Constitution because the system amounted to an unconstitutional state property tax.[9] A year prior to that decision, on November 30, 2004, a Texas district court reached a similar conclusion and enjoined the Texas Commissioner of Education, the Texas Education Agency, the Texas Comptroller of Public Accounts, and the Texas State Board of Education "from continuing to fund public schools."[10] The district court, however, stayed the injunction for ten months, until October 1, 2005, "to give the Legislature a reasonable opportunity to cure the constitutional deficiencies in the finance system."[11] After the district court's ruling the legislature met three times, including twice by special session called by the Governor, and was unsuccessful each time in reaching a compromise on legislation to revamp the school financing system and comply with the district court's ruling.[12]

An appeal was also filed which stayed the district court's injunction that would have been effective on October 1, 2005.[13] Upon its ruling in *Neeley v. West Orange-Cove Consolidated Independent School District* on November 22, 2005, the Texas Supreme Court modified the effective date of the district court's injunction to June 1, 2006.[14] This ruling essentially gave the Texas Legislature less than six months to cure the public school

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9. 176 S.W.3d 746, 754-55 (Tex. 2005) ("[L]ocal ad valorem taxes have become a state property tax in violation of article VIII, section 1-e."). *See also* TEX. CONST. art. VIII, § 1-e ("No State ad valorem taxes shall be levied upon any property within this State.") [hereinafter *Neeley*].

10. *Neeley*, 176 S.W.3d at 753-54.

11. *See id.* at 754. *See also* W. Orange-Cove Consol. Indep. Sch. Dist. v. Neeley, No. GV-100528 (Tex. 250th Dist. Ct. 2004).

12. *See Neeley*, 176 S.W.3d at 754.

13. *See id.*

14. *See id.* at 800.

financing constitutional problems or risk forcing state officials to withhold state funding to school districts.[15]

In apparent anticipation of a ruling from the Texas Supreme Court that would require a quick overhaul of the public school finance system, Texas Governor Rick Perry established the Texas Tax Reform Commission ("the Commission") on November 4, 2005, just eighteen days before the court's ruling.[16] The Commission was tasked with developing "proposals to modernize the state tax system and provide long-term property tax relief as well as sound financing for public schools."[17] After conducting public hearings across the state and hearing oral and written testimony from individual taxpayers and various constituency groups, the Commission presented its recommendations on March 29, 2006 to the Governor, the Lieutenant Governor, the Speaker of the House of Representatives, and the Members of the Texas Legislature.[18]

On April 17, 2006, the Texas Governor called a special session to meet the Texas Supreme Court's deadline by considering legislation to revamp, among other things, school district property taxes and franchise, or business, taxes.[19] That same day, HB 3, which contained the recommendations of the Texas Tax Reform Commission, was filed in the Texas House of Representatives.[20]

HB 3 enjoyed a quick and relatively painless ride through the Texas Legislature probably because of the Supreme Court deadline. After spending seven days in committee, HB 3 was sent to the House floor on April 24 where it received several amendments.[21] That same day the bill was passed with an 80-68 vote.[22] Eight days later, on May 2, the bill narrowly passed the

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15. *Gov. Perry proclaims special session to consider legislation that provides for modification of certain taxes and that provides for an appropriation to the Texas Educations Agency*, April 17, 2006, http://governor.state.tx.us/news/proclamation/5296/.

16. Press Release, Office of the Governor, Gov. Perry Names 24-Member Tex. Tax Reform Comm. (Nov. 4, 2005), *available at* http://governor.state.tx.us/news/appointment/5077/; *see also Neeley*, 176 S.W.3d at 754.

17. Press Release, *supra* note 16.

18. *See* STAFF OF TEX. TAX REFORM COMM., TEX. TAX REFORM COMM. REP. 1, 15-16, *available at* http://www.truthabouttexastaxes.com/documents/TTRC_report.pdf.

19. Press Release, Office of the Governor, Gov. Perry Announces Special Session of Legislature (April 17, 2006), *available at* http://governor.state.tx.us/news/press-release/2465/.

20. Texas Legislature Online, Legislative History of H.B. 3, http://www.capitol.state.tx.us/BillLookup/History.aspx?LegSess=793&Bill=HB3 (last visited Oct. 8, 2008) [hereinafter *Legislative History of H.B. 3*].

21. *See id.*

22. H.J. of Tex., 79th C.S. 140 (2006).

Senate with a 16-14 vote and with no amendments added.[23] The Senate did not add any amendments because Senators were concerned with meeting the Supreme Court's deadline and anticipated that any desired changes to the tax would be addressed in a later technical corrections bill.[24] Accordingly, the following dialogue occurred on the Senate floor regarding HB 3:

> **Senator Averitt**: Senator Ogden, isn't it true that we are trying not to amend this bill so we can be sure to get our work done in this brief special session?
> **Senator Ogden**: Yes.
> **Senator Averitt**: So there may be some technical corrections that should be made but we're not doing that in this bill due to time constraints?
> **Senator Ogden**: Yes, and I have SB 6 that could be passed to make these changes.
> **Senator Averitt**: Just in case SB 6 doesn't pass, I want to call your attention to . . . [25]

Senate Bill 6 was not passed during that special session.[26] HB 3, however, was passed without amendments from the Senate and signed by the Governor on May 19, 2006.[27] The first margin tax returns for most businesses covered under the new franchise tax created by HB 3 were originally due May 15, 2008.[28] However, due to the complexities and newness of this tax law, the Texas Comptroller extended the filing deadline to June 16, 2008.[29] The legislature specified within HB 3 that the Texas Supreme Court has "exclusive and original jurisdiction over a

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23. S.J. of Tex., 69th C.S. 102-03 (2006).

24. *Id.* at 91 (statement of legislative intent).

25. *Id.*

26. Texas Legislature Online, Legislative History of S.B. 6, http://www.capitol.state.tx.us/BillLookup/History.aspx?LegSess=793&Bill=SB6 (last visited Oct. 5, 2008). However, a technical corrections bill, HB 3928, was considered and passed during the next legislative session in the Spring of 2007. Texas Legislature Online, Legislative History of HB 3928, http://www.legis.state.tx.us/BillLookup/History.aspx?LegSess=80R&Bill=HB3928 (last visited Oct. 5, 2008).

27. *See Legislative History of H.B. 3*, *supra* note 20.

28. 2008 Revised Tex. Franchise Tax Due Dates and Milestones, TEX. COMPTROLLER OF PUBLIC ACCOUNTS, *available at* http://www.window.state.tx.us/taxinfo/franchise/duedates.html (last visited Oct. 5, 2008).

29. Kate Alexander, *Small-business Owners Unite to Fight New Tax*, AUSTIN-AMERICAN STATESMAN, May 16, 2008, B01, *available at* http://www.statesman.com/news/content/region/legislature/stories/05/16/0516tax.html. *See also* Additional Time to File Texas Franchise Tax Reports, TEXAS COMPTROLLER OF PUBLIC ACCOUNTS, *available at* http://www.window.state.tx.us/taxinfo/franchise/ft_additional_time.html (last visited Oct. 5, 2008).

challenge to the constitutionality of" the new tax and that the Court has one-hundred and twenty days to rule on such a challenge from the date the challenge is filed.[30]

B. *The "Illegal Undocumented Worker" Provision*

As discussed above, on April 24, 2006, several amendments were added in the House of Representatives to HB 3 shortly before it was passed.[31] One of these amendments, introduced by Representative Anchia, purported to deny a compensation deduction for any wages or cash compensation paid to an "illegal undocumented worker."[32] This amendment also purported to deny a cost of goods sold deduction for any compensation paid to an "illegal undocumented worker used for the production of goods."[33] "Goods" was defined as including the "husbandry of animals, the growing and harvesting of crops, and the severance of timber from realty."[34] For purposes of this amendment, "illegal undocumented worker" was defined as "a person who is not lawfully entitled to be present and employed in the United States."[35] This amendment was passed in the House of Representatives with a 141-1 vote.[36] A subsequent perfecting amendment, also offered by Representative Anchia, struck "illegal" from the term "illegal undocumented worker" in the original amendment and instructed the Comptroller to "adopt rules to implement the legislative intent" of the amendment.[37]

When these amendments were introduced on the floor of the House of Representatives, Representative Anchia, the author of the amendments, stated that he was the son of immigrants and that he found the recent rhetoric referring to "illegal aliens" as criminals to be offensive.[38] Deflecting attention away from potential legislation that would criminalize the presence of undocumented workers who subsidize the Texas economy, Representative Anchia sought to penalize businesses who hire

30. Tex. H.B. 3, 79th Leg. (Tex. 2006), Sec. 24.

31. *See Legislative History of H.B. 3*, *supra* note 20.

32. H.J. of Tex., 79th C.S. 108 (2006).

33. *See id.*

34. *Id.*

35. *Id.*

36. *Id.* at 109.

37. *Id.*

38. *See* Internet Video, 3rd Called Spec. Sess., Part V, starting at 1:47:30 (Tex. H.R. Video Archives Apr. 24, 2006), *available at* http://www.house.state.tx.us/media/chamber/79.htm (voicing perceived offensiveness of both the term "illegal aliens," and the alignment of "illegal aliens" with "criminals").

these workers, or what he described as "the demand side of the issue."[39]

In delegating authority to the Comptroller to adopt rules to effectuate the amendment, Representative Anchia stated that his legislative intent would include "audits of Texas businesses" and provisions so that "companies . . . and CEO's could provide affidavits that they neither directly nor indirectly hire undocumented labor in the production of their goods."[40] He further stated that "if we are really serious about adopting policy in this State that deals with the flow of people across this border, than [sic] we need to adopt this amendment and hold businesses, illegal businesses, accountable for the demand that they create across this State in bringing undocumented labor here."[41] When the House floor was opened for questions relating to the amendment, Representative Otto congratulated and applauded Representative Anchia for bringing this issue[42] to the House floor for discussion, but he questioned the enforcement mechanism necessary for the successful implementation of the amendment.[43] Recognizing the added complexity upon businesses, Representative Otto, a CPA, noted that businesses who deduct compensation paid to undocumented workers for their federal tax return would need to "be truthful" and exclude that cost from their state tax return.[44] Representative Otto also predicted that the cost to the State for the proper identification, without federal assistance, of undocumented workers for the proper enforcement of this provision would prove more burdensome with the amendment than without the amendment.[45]

Representative Anchia responded to Representative Otto's comment as follows:

> John, the federal government has proven itself to be a disaster with respect to its . . . policy. Nothing is getting done in Washington and I'm tired of waiting on the administration and the Congress to come up with a solution. If we're serious about dealing with this problem, we will act at the state level . . . I'm sure that an administrative regime

39. *See id.*

40. *Id.*

41. *Id.*

42. *Id.* (Representative Otto was assumedly referring to the issue of illegal immigration, a controversial issue at the time of the bill's consideration).

43. *Id.* at 1:52:45.

44. *See id.*

45. *See id.* at 1:52:45.

> can be constructed where this pays for itself . . . I imagine that the Comptroller can set some pretty stiff fines, and I would encourage her or a succeeding Comptroller to establish some pretty stiff fines to where this program pays for itself . . . I would further suggest to the Comptroller that, in adopting the rules, when a federal violation is found and there are a series of raids that are going on in the . . . State that these State penalties and State rules also be triggered.[46]

Representative Strama pointed out, and Representative Anchia agreed, that this issue was "primarily a federal problem not one that the State has a lot of tools at its disposal to address" but noted that Representative Anchia had "identified one tool that we can actually use to address the problem of illegal immigration."[47] Representative Strama also commented that:

> [C]ompared to some of the alternative proposals we have heard to address the issue of immigration, which include very expensive and costly efforts to build walls, you've proposed something that would instead address the demand for illegal labor and do so in a way that actually yields increased revenues to the State rather than costing us a lot of money on measures that probably wouldn't be very effective as long as American employers continue to employ illegal labor.[48]

Representative Anchia replied accordingly:

> I got to be honest with you, some of the proposals at the federal level to go ahead and build a wall are . . . laughable . . . With such a strong demand in our country . . . there's no way that a wall or . . . any other physical measure like that is going to keep workers who . . . want to create a better life for their families out of the State . . . The sucking sound is not coming from Mexico. The sucking sound is coming from the United States and it's bringing undocumented workers here . . . This is a very cost effective way; it deals with the demand side and . . . frankly holds businesses accountable.

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46. *Id.*
47. *Id.*
48. *Id.*

> If they are going to try to derive these deductions and these benefits . . . let's see if we do so honestly.[49]

During the next legislative session, a technical corrections bill, House Bill 3928 ("HB 3928"), was passed but did not make any changes to the "undocumented worker" provisions.[50] On December 11, 2007, the Texas State Comptroller released "rules", or regulations, interpreting the recent franchise tax bills, HB 3 and HB 3928.[51] Prior to adopting these rules, the Comptroller's office received numerous comments and requests from various groups for further clarification of particular provisions.[52]

One of these requests came from a collaboration of the Texas Restaurant Association, the Texas Nursery and Landscape Association, and the Texas Employers for Immigration Reform.[53] This group requested that the definition of "undocumented worker", for purposes of the compensation deduction, be changed to "refer to a person who is employed in violation of the employment eligibility laws of the United States."[54] The Comptroller's office declined this request, asserting that it was contrary to the statute in question.[55]

The Comptroller reiterated that the term "undocumented worker" for both compensation and cost of goods sold deduction purposes means "a person who is not lawfully entitled to be present and employed in the United States."[56] Accordingly, the Comptroller adopted verbatim the legislature's definition of "undocumented worker" to its rules. In January of 2008 the Comptroller released new franchise tax forms which specified, in the applicable instructions, that compensation paid to undocumented workers should reduce the cost of goods sold and compensation deductions.[57]

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49. *Id.*

50. *See* Tex. H.B. 3928, 80th Leg., R.S. (2007).

51. *See* Tax Policy News, TEXAS STATE COMPTROLLER (Dec. 2007), *available at* http://www.window.state.tx.us/taxinfo/taxpnw/tpn2007/tpn712.html#issue2.

52. *See* 32 Tex. Reg. 10038 (to be codified at 34 TEX. ADMIN. CODE § 3.589) (proposed Dec. 28, 2007).

53. *See id.*

54. *Id.*

55. *Id.*

56. *Id.*

57. *See* FORM 05-158-A, TEXAS FRANCHISE TAX REPORT, TEXAS STATE COMPTROLLER OF PUBLIC ACCOUNTS, *available at* http://www.window.state.tx.us/taxinfo/taxforms/05-158A-i.pdf (last visited Oct. 5, 2008). The most recent instructions to Form 05-158-A specify that compensation paid to an undocumented worker should be entered as a negative figure, or subtracted from the "Other" line of the cost of goods sold and compensation deduction (Lines 13, 17) sections. *See* FORM 05-392, 2008 TEXAS FRANCHISE

III. FEDERAL EQUAL PROTECTION CONCERNS

A. *Equal Protection of Undocumented Aliens*

The Fourteenth Amendment to the United States Constitution provides that "No state shall . . . deny to any person within its jurisdiction the equal protection of the laws."[58] The term "person" as used within the Fourteenth Amendment includes aliens "whose presence in this country is unlawful."[59] Accordingly, aliens whose presence in this country is unlawful are "guaranteed due process of the law by the Fifth and Fourteenth Amendments."[60] It is not clear, however, whether invidious state discrimination against aliens whose presence in this country is unlawful would be afforded the strict level of judicial scrutiny that is afforded to, for example, race based classifications.[61]

Previously, the Supreme Court has applied a strict scrutiny standard to classifications based upon national origin.[62] The Court has also applied the strict scrutiny standard to most discrimination based upon alienage.[63] This heightened level of scrutiny for alienage classifications, however, applies to *lawfully* admitted aliens to this country, not *unlawful* or *undocumented* aliens in this country.[64] The rationale for this distinction may be seen in *Graham v. Richardson* where the Court held that "once the federal government has decided to admit aliens, states cannot discriminate against those present."[65] In *Plyler v. Doe*, the Court stated that intermediate scrutiny should be applied to

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TAX REPORT INFORMATION AND INSTRUCTIONS, *available at* http://www.window.state.tx.us/taxinfo/taxforms/05-392.pdf (last visited Oct. 5, 2008).

58. U.S. CONST. amend. XIV, § 1.

59. Plyler v. Doe, 457 U.S. 202, 210, 102 S.Ct. 2382, 2391 (1982) (citing Shaughnessy v. Mezei, 345 U.S. 206, 212, 73 S. Ct. 625, 629 (1953); Wong Wing v. United States, 163 U.S. 228, 238, 16 S. Ct. 977, 981 (1896); Yick Wo v. Hopkins, 118 U.S. 356, 369, 6 S. Ct. 1064, 1070 (1886)).

60. *Plyler*, 457 U.S. at 210, 102 S. Ct. at 2391.

61. *See, eg.*, Adarand Constructors, Inc. v. Pena, 515 U.S. 200, 227, 115 S. Ct. 2097, 2112 (1995); Wygant v. Jackson Bd. Of Educ., 476 U.S. 267, 285, 106 S. Ct. 1842, 1852 (1986).

62. *See* Korematsu v. United States, 323 U.S. 214, 216, 65 S. Ct. 193, 199 (1944).

63. *See* Graham v. Richardson, 403 U.S. 365, 371-72, 91 S. Ct. 1848, 1851-52 (1971); Sugarman v. Dougall, 413 U.S. 634, 642, 93 S. Ct. 2842, 2847 (1973); *In re* Griffiths, 413 U.S. 717, 722, 93 S. Ct. 2851, 2855 (1973); Examining Bd. of Eng'rs, Architects and Surveyors v. Flores de Otero, 426 U.S. 572, 602, 96 S. Ct. 2264, 2281 (1976); Nyquist v. Mauclet 432 U.S. 1, 7, 97 S. Ct. 2120, 2124 (1977); Bernal v. Fainter, 467 U.S. 216, 219, 104 S. Ct. 2312, 2315 (1984).

64. *See* ERWIN CHEMERINSKY, CONSTITUTIONAL LAW: PRINCIPLES AND POLICIES, 775-76 (3d ed. 2006).

65. *Id.* at 770 (citing *Graham*, 403 U.S. at 378, 91 S. Ct. at 1855).

cases involving access to public education for undocumented aliens.[66] In *Plyler*, the Court reasoned that "[u]ndocumented aliens cannot be treated as a suspect class because their presence in this country in violation of federal law is not a constitutional irrelevancy."[67] The Court also reasoned that denying a basic education to this class of people deprives them of the "ability to live within the structure of our civic institutions, and foreclose[s] any realistic possibility that they will contribute in even the smallest way to the progress of our Nation."[68] Justice Powell's concurrence to the opinion echoed this sentiment, pointing out that, in spite of the fact that State resources are burdened,

> the ease of entry remains inviting, and the power to deport is exercised infrequently by the Federal Government . . . it hardly can be argued rationally that anyone benefits from the creation within our borders of a subclass of illiterate persons many of whom will remain in the State, adding to the problems and costs of both State and National Governments attendant upon unemployment, welfare, and crime.[69]

An unconstitutional classification based upon race or national origin may be proved if the applicable law discriminates on its face[70] or has a discriminatory impact[71] or administration.[72] For a law to be held unconstitutional because of discriminatory impact, however, it must be shown that the law had a

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66. *See* 457 U.S. 202, 238, 102 S. Ct. 2382, 2406 (1982); CHEMERINSKY, *supra* note 64, at 776. However, the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 ("PRWORA") and the Illegal Immigration Reform and Immigrant Responsibility Act of 1996 ("IIRIRA") may limit the significance of the Court's decision in *Plyler v. Doe* according to the District Court in Kansas. *See* Day v. Sebelius, 376 F. Supp. 2d 1022, 1026 (D. Kan. 2005), which states the following:

> This litigation arises from the passage of two laws by Congress in 1996 restricting immigration and the status of immigrants: the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA) and the Illegal Immigration Reform and Immigrant Responsibility Act of 1996 (IIRIRA). These laws were passed by the same Congress only about six weeks apart. They were passed in part in response to the Supreme Court's decisions in Plyler v. Doe, 457 U.S. 202, 102 S. Ct. 2382, 72 L. Ed. 2d 786 (1982) (Texas statute which denies free education to alien children violates Equal Protection Clause) and Toll v. Moreno, 458 U.S. 1, 102 S. Ct. 2977, 73 L. Ed. 2d 563 (1982) (University of Maryland's policy of denying treaty organization aliens the opportunity to pay reduced, in-state tuition constituted a violation of the Supremacy Clause).

67. *Plyler*, 457 U.S. at 223, 102 S. Ct. 2398 (internal quotations omitted).

68. *Id.*

69. *Id.* at 240–41 (Powell, J., concurring).

70. *See* Strauder v. West Virginia, 100 U.S. 303, 307-10 (1879).

71. *See, e.g.*, Washington v. Davis, 426 U.S. 229, 242, 96 S. Ct. 2040, 2048 (1976).

72. *See, e.g.*, *id.* at 241.

"discriminatory purpose."[73] Certain civil rights statutes, however, allow violations to be proved by discriminatory impact alone.[74]

In *Griggs v. Duke Power*, for example, the Supreme Court held that a company's practice of requiring either a high school diploma or the passage of a standardized intelligence test as a condition of employment constituted impermissible employment discrimination under the Civil Rights Act because the practice was not significantly related to successful job performance, had a disparate impact upon African-American applicants, and operated to maintain the *status quo* of giving preference to white applicants.[75] Absent an applicable civil rights statute or other authority on point, however, a discriminatory purpose may also be proved by showing that the impact of a law is "so clearly discriminatory as to allow no other explanation than that it was adopted for impermissible purposes", showing the "history surrounding the government's action", or showing the "legislative or administrative history of a law."[76] In explaining the last of these three factors, the Court in *Arlington Heights* specified that legislative history such as "statements by members of the decisionmaking body, minutes of its meetings, or reports" may be highly relevant in discerning possible legislative or administrative discriminatory purposes.[77]

B. *"Undocumented Worker" Provision Status Under Equal Protection*

Whether Texas' discrimination against undocumented workers via the imposition of a financial penalty upon businesses that employ this group is valid under the Federal Equal Protection Clause is an interesting question. Under federal law, employers are subject to a fine, imprisonment, or both for employing workers not eligible to work in the United States.[78]

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73. *See id.* at 239. *See also* Mobile v. Bolden, 446 U.S. 55, 67, 100 S. Ct. 1490, 1499 (1980); McCleskey v. Kemp, 481 U.S. 279, 292, 107 S. Ct. 1756, 1766 (1987).

74. *See* CHEMERINSKY, *supra* note 64, at 711-12 (citing an employment discrimination case, Griggs v. Duke Power Co., 401 U.S. 424, 91 S. Ct. 849 (1971), as well as several voting rights cases: Johnson v. DeGrandy, 512 U.S. 997, 114 S. Ct. 2647 (1994); Thornburg v. Gingles, 478 U.S. 30, 106 S. Ct. 2752 (1986); Rome v. United States, 446 U.S. 156, 100 S. Ct. 1548 (1980)).

75. *See Griggs*, 401 U.S. at 424, 430, 91 S. Ct. at 853.

76. *See* CHEMERINSKY, *supra* note 64, at 715-17 (citing the analysis formed in Village of Arlington Heights v. Metropolitan Housing Development Corp., 429 U.S. 252, 97 S. Ct. 555 (1977)).

77. Vill. of Arlington Heights v. Metro. Hous. Dev. Corp., 429 U.S. 252, 268, 97 S. Ct. 555, 565 (1977).

78. *See* 8 U.S.C. § 1324a (2008).

Compliance with this law is done through the Form I-9[79] and other employment verification procedures. However, employer compliance with federal employment law is not the issue here. The issue is whether the state may impose its own additional tax burden on businesses that employ undocumented workers, which presumably has the effect of deterring businesses from employing undocumented workers within the state. To the extent that businesses are deterred from employing undocumented workers in Texas, this class of persons may find it more difficult to find gainful employment and therefore live in the state.

Based on the definition of "undocumented worker" under the Texas statute,[80] it is clear that the provision is aimed at workers "whose presence in this country is unlawful."[81] Accordingly, it is possible that this tax provision, because it has the impact of causing invidious discrimination of undocumented workers as a result of their federal immigration status, will be afforded an intermediate level of judicial scrutiny per *Plyler v. Doe*.[82] Extending this *Plyler* rationale, it may be argued that state action to deter employment of undocumented workers acts to deprive these people of the ability to function in society and contribute towards any sort of national progress. Combining these realities with the actuality of immigration inflow exceeding emigration outflow, and the federal government's infrequent exercise of its powers to deport,[83] poses a potentially grim picture. This tax provision may end up causing more problems and costing more resources at both the state and federal levels as a result of these unemployed, undocumented workers potentially becoming involved in crime and needing welfare, healthcare, and other state support.[84]

The deeper equal protection analysis of this tax provision, however, is not that clear. While it could possibly be argued that the tax provision facially discriminates against undocumented workers, the reality is that, due to the function of the tax statute, this provision has more of an indirect or disparate impact type of

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79. DEP'T OF HOMELAND SEC., U.S. CITIZENSHIP AND IMMIGRATION SERV., FORM I-9, EMPLOYMENT ELIGIBILITY VERIFICATION (2007), *available at* http://www.uscis.gov/files/form/I-9.pdf.

80. TEX. TAX CODE ANN. § 171.1012 (Vernon 2007).

81. *Plyler*, 457 U.S. at 210, 102 S. Ct. at 2391.

82. *Id.* at 208 (stating that legislation which imposes burdens on "undocumented" children must serve a "substantial goal of the State" rather than merely a rational one, and further, that the legislation will be invalid if "ineffective" in achieving its goal, even if it is "rationally related").

83. *See id.* at 240-41.

84. *See id.*

discrimination on this class. Accordingly, it must be shown that this tax provision had a discriminatory purpose.

Given that this tax bill was passed during an intense national debate on immigration reform, it is possible that Texas politicians used this tax provision as a political wedge in implementing their own brand of immigration reform.[85] The legislative history surrounding this amendment, which comments that this provision is a more practical means of regulating immigration over the proposed federal legislation to build a wall, certainly strengthens this notion. The fact that the word "illegal" was removed from the original amendment that inserted this tax provision could also be evidence, within the legislative history, of this political struggle. In addition, the Texas House of Representatives floor debate surrounding the amendment leaves little doubt that the provision targeted businesses who hire undocumented workers to stamp out the "demand for illegal labor." This intentional targeting can also be interpreted from a statement of Representative Anchia, the amendment's author, expressing his frustration from "waiting on the administration and the Congress to come up with a solution" and his belief that if state legislators were "serious about dealing with this problem, [they] will act at the state level."[86] The legislative history therefore highlights the possibility that this tax provision had the discriminatory purpose of deterring employment of undocumented workers and encouraging them to exit the jurisdiction. Such a conclusion may meet the Supreme Court's requirement of a discriminatory purpose for facially neutral discrimination.

C. Lawrence v. Texas, Romer v. Evans, *and Other Relevant Doctrine*

The Supreme Court generally grants broad deference for Fourteenth Amendment equal protection review of state economic and tax legislation.[87] The Court in *Nordlinger v. Hahn* explained this deference towards state tax laws as follows:

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85. *See* Cynthia Ohlenforst, *The New Texas Margin Tax: More Than a Marginal Change to Texas Taxation*, 60 TAX LAW. 959, 977 (2007)("Against the backdrop of the national debate on immigration law, this provision is not particularly surprising. Nor is it surprising that employers have already begun to ask what steps they should take to determine whether labor costs are attributable to undocumented workers.").

86. *See* Internet Video, *supra* note 38.

87. *See* Lawrence v. Texas, 539 U.S. 558, 579-80, 123 S. Ct. 2472, 2484-85 (2003) (O'Connor, J., concurring) (citing Cleburne v. Cleburne Living Center, 473 U.S. 432, 440, 105 S. Ct. 3249, 3254 (1985)).

> In general, the Equal Protection Clause is satisfied so long as there is a plausible policy reason for the classification, the legislative facts on which the classification is apparently based rationally may have been considered to be true by the governmental decision maker, and the relationship of the classification to its goal is not so attenuated as to render the distinction arbitrary or irrational. This standard is especially deferential in the context of classifications made by complex tax laws. "[I]n structuring internal taxation schemes 'the States have large leeway in making classifications and drawing lines which in their judgment produce reasonable systems of taxation.'".[88]

In *Nordlinger*, the Court held that the California property tax system, which provided that the assessed property tax value under the system could only increase each year by 2% except in cases of improvements or change in ownership, did not violate a taxpayer's equal protection.[89] This property tax limitation was implemented via Proposition 13, a statewide ballot initiative amending the California state constitution in response to "rapidly rising real property taxes."[90]

In 2003, the Supreme Court repeated this deference to state legislatures for tax laws in *Fitzgerald v. Racing Association of Central Iowa*.[91] In *Fitzgerald*, a state tax law sought to tax slot machines at racetracks at a 36% rate but tax the same slot machines on riverboats at a 20% rate.[92] The Iowa Supreme Court held that the tax violated the equal protection clause because the tax "frustrated" the law's central purpose which was to rescue racetracks from "economic distress."[93] The court stated that "no rational person" could claim otherwise.[94] The court also stated that "it is impossible to conclude the legislature actually had its alleged purpose in mind when enacting this taxing

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88. Nordlinger v. Hahn, 505 U.S. 1, 11-12, 112 S. Ct. 2326, 2332 (1992) (citations omitted).

89. *See id.* at 1.

90. *Id.*

91. Fitzgerald v. Racing Ass'n of Cent. Iowa, 539 U.S. 103, 104, 123 S. Ct. 2156 (2003).

92. *See id.* at 103-04.

93. *Id.* at 107 (citing Racing Ass'n of Cent. Iowa v. Fitzgerald, 648 N.W.2d 555, 561 (Iowa 2002)).

94. *Id.* at 107-08 (citing Racing Ass'n of Cent. Iowa v. Fitzgerald, 648 N.W.2d 555, 561 (Iowa 2002)).

statute."[95] The United States Supreme Court disagreed, reasoning that "not every provision in a law must share a single objective" and that, "seen as a whole," the law could rationally be understood to advance the racetracks' economic interests.[96]

Other federal equal protection challenges, however, may mitigate this deference given to state tax laws. In Justice O'Connor's concurrence in *Lawrence v. Texas*, for example, she stated the following:

> Laws such as economic or tax legislation that are scrutinized under rational basis review normally pass constitutional muster, since "the Constitution presumes that even improvident decisions will eventually be rectified by the democratic processes." We have consistently held, however, that some objectives, such as "a bare . . . desire to harm a politically unpopular group," are not legitimate state interests. When a law exhibits such a desire to harm a politically unpopular group, we have applied a more searching form of rational basis review to strike down such laws under the Equal Protection Clause.[97]

In *United States Department of Agriculture v. Moreno*, the Court provided a broader notion of this type of review when it stated that "if the constitutional conception of 'equal protection of the laws' means anything, it must at the very least mean that a bare congressional desire to harm a politically unpopular group cannot constitute a legitimate governmental interest."[98] In that case, the Court struck down an amendment to the Food Stamp Act that purposefully discriminated against hippies.[99] Such a view was reflected by Justice Powell in his concurrence in *Plyler v. Doe*, where he stated that a "legislative classification that threatens the creation of an underclass of future citizens and residents cannot be reconciled with one of the fundamental purposes of the Fourteenth Amendment."[100]

The Court stated similarly in *Romer v. Evans* that a Colorado constitutional amendment prohibiting all state and local laws protecting gays, lesbians, and bisexuals violated the

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95. *See* Racing Ass'n of Cent. Iowa v. Fitzgerald, 648 N.W.2d 555, 561 (Iowa 2002).

96. *See Fitzgerald*, 539 U.S. at 108-09, 123 S. Ct. at 2159-60.

97. Lawrence v. Texas, 539 U.S. 558, 579-80, 123 S. Ct. 2472, 2484-85 (2003) (citations omitted).

98. U.S. Dep't of Agric. v. Moreno, 413 U.S. 528, 534, 93 S. Ct. 2821, 2825-26 (1973).

99. *Id.* at 534-35.

100. Plyler v. Doe, 457 U.S. 202, 239, 102 S. Ct. 2382, 2406 (1982).

Fourteenth Amendment because, among other reasons, the law "impos[ed] a broad and undifferentiated disability on a single named group."[101] The Court also repeated the "politically unpopular group"[102] rationale and stated that "the amendment raises the inevitable inference that it is born of animosity toward the class that it affects."[103] Furthermore, the Court stated that the amendment "cannot be said to be directed to an identifiable legitimate purpose or discrete objective [and] is a status-based classification of persons undertaken for its own sake, something the Equal Protection Clause does not permit."[104]

D. *Analysis of the "Undocumented Worker" Provision Under Alternative Equal Protection Arguments*

Because state economic and tax legislation is afforded a rational basis review deference under the equal protection clause, the State might argue that its discrimination of undocumented workers within the tax law is within the State's broad latitude to create distinctions or classifications within such tax laws. Additionally, the State may argue, under the *Fitzgerald* rationale,[105] that the undocumented worker provision need not share the tax law's central objective and that "seen as a whole" the margin tax still accomplishes its main objective. Moreover, despite how undesirable this legislation may be to some, the State could also argue that it is entitled to rectify this "improvident" measure through the democratic process.[106]

Caveating the deference given to economic and tax legislation, however, the Court has repeatedly reminded legislative bodies that classifications must not be arbitrary or irrational.[107] More specifically, the State is not afforded a lenient rational basis deference, or virtual blank check, when it passes laws that exhibit a "bare desire to harm a politically unpopular group."[108] It is possible that the tax provision in question, aimed as it is at undocumented workers, exhibits such a desire. Surrounded by the national immigration debate, it is easy to see how, when this bill was passed in the spring of 2006, the topic of

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101. Romer v. Evans, 517 U.S. 620, 632, 116 S. Ct. 1620, 1627 (1996).

102. *Id.* at 634-35.

103. *Id.* at 621.

104. *Id.*

105. *See Fitzgerald*, 539 U.S. at 108, 123 S. Ct. at 2159.

106. Lawrence v. Texas, 539 U.S. 558, 579, 123 S. Ct. 2472, 2484 (2003) (O'Connor, J., concurring).

107. *See* Nordlinger v. Hahn, 505 U.S. 1, 10, 112 S. Ct. 2326 (1992).

108. *See Lawrence*, 539 U.S. 558, 579, 123 S. Ct. 2472, 2485 (2003) (citing Dep't of Agric. V. Moreno, 413 U.S. 528, 534, 93 S. Ct. 2821 (1973)).

immigration reform was particularly heated. Additionally, the considerable number of references to eradicating the problem of undocumented labor in the legislative history surrounding the amendment in question exhibits such an atmosphere.[109] Several other states and localities were considering similar measures during this time period.[110] It is logical, then, to see how an immigration reform provision could have ended up in a state tax bill during this time period.

The targeted nature of such a provision is also observed by reflecting upon the tax bill as a whole. That is, other than this undocumented worker provision, no other portion of HB 3 or HB 3928[111] touches upon the subject of immigration reform or undocumented workers. Because this tax provision is not germane or congruous to any other part of the tax bill, it can be argued that this tax provision, facially discriminatory as it is, targets this particular subclass of persons. Perhaps this occurred in the name of political gamesmanship. If so, it could logically be inferred that perhaps this classification scheme is arbitrary or capricious in relation to the goal of the tax bill.

It could also be reasonably argued that, similar to *Moreno*,[112] *Plyler*,[113] and *Romer*,[114] this classification acts to impose a substantial disability upon a single named group that hinders their future prosperity in this country. Such an argument gains strength when one considers the current state of immigration policy and the possibility of immigration reform and a guest worker program that would enable many of these persons to stay in the country. Moreover, these cases also necessarily raise the inquiry of whether regulation of immigration in this manner is a legitimate state interest. As discussed elsewhere in this article, due to the exclusive federal interest in regulating immigration, state regulation of immigration may not qualify as a legitimate state interest under the federal equal protection doctrine.[115] More generally, it is questionable whether the Texas legislature should be empowered to aid or supplement the federal government in its immigration enforcement when businesses lawfully comply with the state tax law. Such a scenario is observed where, due to the function of the provision, a higher

109. *See* Internet Video, *supra* note 38.

110. *See* discussion *infra* Part V.C.

111. Also known as the "Technical Corrections Bill," *see* Tex. H.B. 3928, 80th Leg., R.S. (2007).

112. Dep't of Agric. v. Moreno, 413 U.S. 528, 93 S. Ct. 2821 (1973).

113. *See* Plyler v. Doe, 457 U.S. 202, 102 S. Ct. 2382 (1982).

114. Romer v. Evans, 517 U.S. 620, 116 S. Ct. 1620 (1996).

115. *See infra* Part III.F.

state tax bill is realized as a result of an employer violating the federal immigration employment laws by hiring undocumented labor and having to back out that expense from the compensation deduction on their Texas state tax return.

E. *State Equal Protection Afforded to Undocumented Aliens*

In addition to federal equal protection under the Fourteenth Amendment, the Texas Constitution states that "[a]ll free men, when they form a social compact, have equal rights, and no man, or set of men, is entitled to exclusive separate public emoluments, or privileges, but in consideration of public services."[116] This provision is known as the Texas Equal Protection Clause.[117] In 1972, the Texas Constitution was amended to specify that equality "shall not be denied or abridged because of sex, race, color, creed, or national origin."[118] Because of its additional guarantees, the Texas Equal Rights Amendment is "more extensive and provides more specific protection than both the United States and Texas due process and equal protection guarantees."[119] The Amendment was "designed expressly to provide protection which supplements the federal guarantees of equal treatment."[120]

To determine whether the Texas Equal Rights Amendment has been violated, a three-step process for evaluating the alleged violation must occur.[121] First, a court must decide "whether equality under the law has been denied."[122] Equality under the law has been denied where the discrimination is by "state action or private conduct that is encouraged by, enabled by, or closely interrelated in function with state action."[123] If equality under the law has been denied, then a court must determine whether it was denied "because of . . . sex, race, color, creed, or national origin."[124] Such classes are also referred to as "suspect classes."[125] If a court concludes that equality was denied because

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116. TEX. CONST. art. I, § 3.

117. *See* Bell v. Low Income Women of Tex., 95 S.W.3d 253, 265 (Tex. 2002).

118. TEX. CONST. art. I, § 3a.

119. *In re* McLean, 725 S.W.2d 696, 698 (Tex. 1987).

120. *Bell*, 95 S.W.3d at 257 (quoting TEX. LEGISLATIVE COUNCIL, 14 PROPOSED CONSTITUTIONAL AMENDMENTS 24 (1972)).

121. *See id.* (citing *In re McLean*, 725 S.W.2d at 697).

122. *Id.*

123. Junior Football Ass'n of Orange v. Gaudet, 546 S.W.2d 70, 71 (Tex. Civ. App. 1976).

124. *Bell*, 95 S.W.3d at 257.

125. *In re McLean*, 725 S.W.2d at 698 (stating that the Equal Rights Amendment elevates sex to a suspect classification).

of a person's membership in a protected class, the court will finally determine whether the challenged action is "narrowly tailored to serve a compelling governmental interest."[126] Such a level of judicial scrutiny is also referred to as "strict scrutiny."[127]

If a particular affected class does not fall within one of the specified classes in the Texas Equal Rights Amendment, the class is still entitled to normal equal protection security under Texas' Equal Protection Clause.[128] In evaluating equal protection challenges under the Texas Constitution, courts use the same standard for these challenges as that under the Federal Constitution.[129] Accordingly, violations of this clause undergo a rational basis judicial test whereby the applicable statutory classification must be rationally related to a "legitimate state interest."[130] These equal protection guarantees are offered to corporations as well as to individuals.[131]

Accordingly, in *HL Farm Corp. v. Self*, the Texas Supreme Court held that it is a violation of the Equal Protection Clause of the Texas Constitution to deny an open space land designation to land owned by a nonresident alien corporation because there is no rational basis to support that designation.[132] The statute in question, which provided for a reduced tax valuation for open-space land, denied the open-space land designation to foreign or nonresident corporations whose majority interest ownership was from a nonresident alien or foreign government.[133] The corporation in question, HL Farm Corp., a Virginia corporation which was owned by another Virginia corporation who was a subsidiary of a Switzerland corporation, owned land in Texas.[134] The purpose of the applicable statute was to "promote the preservation of open-space land devoted to farm or ranch purposes."[135] Finding that a "'foreign corporation' owned by a nonresident alien may contribute to the preservation of open-

126. *Bell*, 95 S.W.3d at 257 (citing *In re McLean*, 725 S.W.2d at 698).

127. *See id.* at 258.

128. *See* HL Farm Corp. v. Self, 877 S.W.2d 288, 290 (Tex. 1994); *see also Bell*, 95 S.W.3d at 265-66.

129. *See* Barshop v. Medina County Underground Water Conservation Dist., 925 S.W.2d 618, 631-32 (Tex. 1996).

130. *See also Bell*, 95 S.W.3d at 265-66.

131. *See* Grosjean v. Am. Press Co., 297 U.S. 233, 244, 56 S. Ct. 444, 446-47 (1936); *see also HL Farm Corp.*, 877 S.W.2d at 290 n.4 ("Despite [the Texas Equal Protection Clause's] gender specific language, *i.e.* 'men,' this provision applies to business entities, such as corporations, as well as to natural persons.")

132. *See HL Farm Corp.*, 877 S.W.2d at 292.

133. *Id.* at 289.

134. *Id.*

135. *Id.* at 292.

space land as well as any Texas individual or legal entity," the court held that the tax statute in question was "not rationally related to the promotion and preservation of open-space land," and thus violated the Equal Protection Clause of the Texas Constitution.[136]

The right of the legislature to regulate business or industry, however, often meets the rational basis test.[137] State regulation should be "reasonable, not arbitrary, and bear a reasonable relationship to a legitimate state objective."[138] Similarly, tax statutes are generally found to be constitutional under the equal protection clause unless no reasonable basis exists for the attempted classification.[139] Taxpayers challenging a tax statute have "the burden to show discrimination by negating every conceivable basis which might support it."[140]

A classification for tax purposes, however, may be found to be unconstitutional where the Legislative classification is "arbitrary, unreasonable, or capricious."[141] Accordingly, "a law [may be] void for vagueness if its prohibitions are not clearly defined."[142] However, "[a] statute is not unconstitutionally vague merely because a company . . . can raise uncertainty about its application to the facts of their case. A statute is unconstitutionally vague 'only where no standard of conduct is outlined at all; when no core of prohibited activity is defined.'"[143]

F. *"Undocumented Worker" Status Under State Equal Protection*

The purported discrimination with Texas' new undocumented worker tax provision is that entities that employ

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136. *Id.*

137. *See* Pollard v. Cockrell, 578 F.2d 1002, 1012 (5th Cir. 1978) ("[T]he theory that classifications affecting the right to pursue a legitimate business demand strict scrutiny flies in the face of the well established rule that state regulations of business or industry are to be reviewed under the less exacting 'rational basis' standard.").

138. Smith v. State, 866 S.W.2d 760, 764 (Tex. App.— Houston [1st Dist.] 1993).

139. *See, e.g.*, Hurt v. Cooper, 110 S.W.2d 896, 901 (Tex. 1937).

140. Bullock v. Marathon Oil Co., 798 S.W.2d 353, 359 (Tex. App.— Austin 1990) (quoting *Madden v. Kentucky*, 309 U.S. 83, 60 S. Ct. 406 (1940)). *See also* Cent. Power & Light Co. v. Sharp, 919 S.W.2d 485, 489 (Tex. App.— Austin 1996).

141. Upjohn Co. v. Rylander, 38 S.W.3d 600, 609 (Tex. App.— Austin 2000) (citing Hurt v. Cooper, 110 S.W.2d 896, 901 (Tex. 1937)). *See also* Fairmont Dallas Rests., Inc. v. McBeath, 618 S.W.2d 931, 933 (Tex. Civ. App. 1981).

142. Combs v. STP Nuclear Operating Co., 239 S.W.3d 264, 276 (Tex. App.— Austin 2007) (citing Grayned v. City of Rockford, 408 U.S. 104, 108, 92 S. Ct. 2294, 2298-99 (1972)).

143. Ford Motor Co. v. Tex. Dep't of Transp., 264 F.3d 493, 509 (5th Cir. 2001) (quoting Margaret S. v. Edwards, 794 F.2d 994, 997 (5th Cir. 1986)).

and pay compensation to undocumented workers are subject to a smaller deduction and therefore higher tax base under the tax code than entities that do not pay compensation to undocumented workers.[144] This differing treatment amongst taxpayers has an obvious purpose of providing a financial disincentive for taxpayers that employ and compensate undocumented workers.[145] Put another way, this tax provision provides a competitive incentive to entities that employ and compensate documented or "legal" workers.[146] By providing a disincentive, this tax provision naturally encourages taxpayers to not employ undocumented workers. Flowing logically, if undocumented workers are not able to obtain employment because employers are being penalized for employing them, then undocumented workers may find it more difficult to live in the jurisdiction.[147]

Applying the Texas Equal Rights Amendment analysis to the undocumented worker tax provision in question, the first prong of the analysis is likely met because the purported discrimination is being implemented by state action.[148] That is, the legislature is directing the State Comptroller to not permit companies a deduction for compensation paid to undocumented workers.[149] Moreover, the legislature instructed the Comptroller to adopt rules to implement its specific legislative intent, and specific legislator directives, in denying this deduction.[150]

Meeting the second prong that equality is being denied to one of the specified classes, may prove more difficult.[151] The observation that should be made here is that an entity does not have a sex, race, color, creed, or national origin as specified in the Texas Equal Rights Amendment.[152] Accordingly, an entity likely does not qualify for the heightened level of protection that the Texas Equal Rights Amendment offers.

Next, an entity should determine if the classification in question is protected under the Texas Equal Protection Clause.

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144. *See Legislative History of H.B. 3*, *supra* note 20; *supra* text accompanying notes 32-35.

145. *See* Internet Video, *supra* note 38; *supra* text accompanying notes 39-41.

146. *See* Internet Video, *supra* note 38; *supra* text accompanying notes 39-41.

147. *See supra* part III.B.

148. *See supra* part IV.A.

149. *See Legislative History of H.B. 3*, *supra* note 20; *supra* notes 32-33 and accompanying text.

150. *See Legislative History of H.B. 3*, *supra* note 20; *supra* text accompanying note 37. *See also* Internet Video, *supra* note 38; *supra* text accompanying note 47.

151. *See supra* part IV.A.

152. *See* TEX. CONST. art. I, § 3a.

As mentioned above, equal protection security is extended to entities under Texas law.[153] The standard of review for the statute in question is rational basis, whereby the classification must be rationally related to a legitimate state interest.[154] Using the *HL Farm Corp* analysis, it is questionable how the provision in question fits in with the purpose of the franchise tax.[155] The purpose of HB 3, the bill implementing the margin tax, is to raise state revenue by amending the tax code to "close the loopholes in the current franchise tax base by extending coverage to certain active businesses. At the same time, it broadens the tax base and lowers the rate."[156] More specifically, HB 3 sought to tax the "many Texas businesses that receive limited liability protection from the State [but] do not pay the franchise tax."[157] The legislation was not overtly intended to implement immigration reform.

While a denial of a deduction for businesses that pay compensation to undocumented workers undoubtedly raises the tax bill for businesses that wish to comply with this tax provision, the larger immigration reform that this tax provision effectuates amounts to more of a police power. Narrowing this line of thinking, the state could argue that this tax provision is rationally related to an attempt to deter businesses from hiring and employing undocumented workers, thus making it more difficult for this group to live in this jurisdiction.

Regarding the federal government's exclusive power to regulate in the immigration area, it is questionable whether immigration reform is a legitimate state interest. More globally, the tax provision, to the extent that it mandates a type of immigration reform, detracts from the central purpose of the taxing statute, HB 3. Accordingly, the tax provision denying a deduction for compensation paid to undocumented workers may not be rationally related to extending coverage of the franchise tax to more active businesses. The revised franchise tax, or margin tax, suitably accomplishes this task without the tax provision in question.

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153. *See* Grosjean v. Am. Press Co., 297 U.S. 233, 244, 56 S. Ct. 444, 446-47 (1936); *see also HL Farm Corp.*, 877 S.W.2d at 290, n.4 ("Despite [the Texas Equal Protection Clause's] gender specific language, *i.e.* 'men,' this provision applies to business entities, such as corporations, as well as to natural persons.")

154. *See HL Farm Corp.*, 877 S.W.2d at 290.

155. *Id.* (citing Whitworth v. Bynum, 699 S.W.2d 194, 197 (Tex. 1985)).

156. Texas Legislature Online, Bill Analysis of H.B. 3, http://www.capitol.state.tx.us/tlodocs/793/analysis/html/HB00003H.htm.

157. *Id.*

Despite the incongruity between the purpose of the taxing statute and the effect of the tax provision, a court may nevertheless hold that the tax provision is constitutional because of the rational basis review afforded to business regulation.[158] Accordingly, a court may find that the legislature could have reasonably wanted to deny a deduction for this type of activity simply to raise revenue and not because of its overall effects in immigration policy. The legislature could also argue that it wanted to protect the jobs of citizens of the State who are lawfully employed. Notwithstanding the leeway given to the legislature by the rational basis review standard, the classification that this tax provision creates may not meet the "arbitrary, unreasonable, or capricious" standard. That is, a state taxing statute that seeks to deny to all businesses that employ undocumented workers a deduction for compensation paid to those workers is uncommon if not unheard of. In other words, immigration policy is not normally found in a tax statute. In addition, the tax provision in question seems to be out of place in a taxing statute that appears to tax normal business operations.

Moreover, the tax provision may be too vague to pass constitutional muster. In its current form, the tax statute does not specify how a company is to make a determination of a person's immigration status. That is, an undocumented worker is defined as a "person who is not lawfully entitled to be present *and* employed in the United States."[159] While companies are equipped with tools to check employment eligibility through the Form I-9[160] and other employment verification tools, companies are not in a position to determine whether a person is lawfully *present* in the United States. Such a determination should be made by immigration officials and should not be delegated to employers.

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158. *See supra* Part III.E.

159. H.J. of Tex., 79th Leg., 3rd C.S. 108 (2006) (emphasis added).

160. Also note that the IRS has, as of 2006, not imposed penalties upon employers for Social Security Number mismatches where applicable. In February 2006, the IRS Commissioner testified before the House Ways and Means Committee that "because of the reasonable cause provision in the tax law, I am unaware of IRS sustaining any penalty against an employer for failure to provide an accurate SSN for an employee. That has not changed." *Second in a Series of Subcommittee Hearings on Social Security Number High-Risk Issues: Hearing Before the Subcomm. on Social Security and Subcomm. on Oversight of the H. Comm. on Ways and Means*, 109th Cong. 13 (2006) (Statement of Mark W. Everson, Comm'r, Internal Revenue Service); *see also* Juan F. Vasquez, Jr. & Peter A. Lowy, *Social Security Number Mismatches and Workforce Validity*, 70 TEX. B.J. 148, 149 (2007).

Similarly, the statutory and administrative scheme may also be impermissibly vague because employers are given inadequate guidance on how to determine employment eligibility. To comply with federal employment laws, employers are given specific guidance to make a determination of employment eligibility, such as having workers complete Form I-9.[161] No similar guidance is given with the undocumented worker tax provision. During the House floor debate, Representative Anchia directed the legislative history to include, among other requests, provisions so that "companies . . . and CEO's could provide affidavits that they neither directly nor indirectly hire undocumented labor in the production of their goods."[162]

To strengthen these directives, Representative Anchia added a perfecting amendment that instructed the Comptroller to "adopt rules to implement the legislative intent" of the applicable sections from the amendment.[163] The Comptroller, however, has not issued significant additional guidance. When asked to clarify the definition of "undocumented worker" by several Texas business associations, the Comptroller declined the request by yielding to the legislative intent.[164] Additionally, when given an opportunity to correct vague or unclear provisions in the original bill, HB 3, the Legislature failed to clarify the tax provision when it passed the technical corrections bill, HB 3928.[165] Without additional guidance from either the legislature or the Comptroller, taxpayer entities and their executives may be at a loss in terms of properly complying with the current version of the undocumented worker tax provision.[166] The current statutory and administrative scheme surrounding this tax provision may therefore be impermissibly vague as to be unenforceable or invalid.

IV. FEDERAL PREEMPTION OF STATE IMMIGRATION REGULATION

A. *Background Legal Doctrine*

Article VI of the United States Constitution provides that the "Constitution, and the Laws of the United States which shall

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161. *See* FORM I-9, EMPLOYMENT ELIGIBILITY VERIFICATION, *supra* note 79.

162. *See* Internet Video, *supra* note 38.

163. *See* H.J. of Tex., 79th Leg., 3rd C.S. 109 (2006).

164. *See* 32 Tex. Reg., at 10038.

165. *See* Tex. H.B. 3928, 80th Leg., R.S. (2007).

166. *Cf.* Ohlenforst, *supra* note 85, at 977 (noting that employers have "already begun to ask what steps they should take to determine whether labor costs are attributable to undocumented workers").

be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land."[167] Known popularly as the "Supremacy Clause," the Supreme Court has interpreted the clause to preempt "any state law, however clearly within a State's acknowledged power, which interferes with or is contrary to federal law."[168]

Generally, two types of preemption can occur: express preemption and implied preemption.[169] A federal law expressly preempts a state or local law when Congress explicitly states so in the statutory language.[170] A federal law impliedly preempts a state or local law where there exists a clear congressional intent contained in the structure and purpose of the federal regulation.[171] Two types of implied preemption have generally been recognized: field preemption and conflict preemption.[172] Field preemption exists when:

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167. U.S. CONST. art. VI, cl. 2.

168. Gade v. Nat'l Solid Waste Mgmt. Ass'n, 505 U.S. 88, 108, 112 S. Ct. 2374, 2388 (1992) (quoting Felder v. Casey, 487 U.S. 131, 138, 108 S. Ct. 2302, 2306 (1988)). *See also* Gibbons v. Odgen, 22 U.S. 1, 81-82 (1824) (stating the following:

> [I]t has been contended, that if a law passed by a State, in the exercise of its acknowledged sovereignty, comes into conflict with a law passed by Congress in pursuance of the constitution, they affect the subject, and each other, like equal opposing powers . . . . But the framers of our constitution foresaw this state of things, and provided for it, by declaring the supremacy not only of itself, but of the laws made in pursuance of it. The nullity of any act, law. The appropriate inconsistent with the constitution, is produced by the declaration, that the constitution is the supreme law. The appropriate application of that part of the clause which confers the same supremacy on laws and treaties, is to such acts of the State Legislatures as do not transcend their powers, but, though enacted in the execution of acknowledged State powers, interfere with, or are contrary to the laws of Congress, made in pursuance of the constitution, or some treaty made under the authority of the United States. In every such case, the act of Congress, or the treaty, is supreme; and the law of the State, though enacted in the exercise of powers not controverted, must yield to it.

Id.).

169. *See* CHEMERINSKY, *supra* note 64, § 5.2.

170. *See Gade*, 505 U.S. at 98, 112 S. Ct. at 2383 ("Pre-emption may be . . . compelled [if] Congress' command is explicitly stated in the statute's language. . . . "). *See also* Am. Airlines, Inc. v. Wolens, 513 U.S. 219, 115 S. Ct. 817 (1995) (holding that claims based on the Illinois Consumer Fraud and Deceptive Business Practices Act are explicitly preempted by the Airline Deregulation Act); Morales v. Trans-World Airlines, Inc., 504 U.S. 374, 112 S. Ct. 2031 (1992) (holding that state regulation of airline fare advertising is explicitly preempted by the Airline Deregulation Act); Jones v. Rath Packing Co., 430 U.S. 519, 97 S. Ct. 1305 (1977) (finding that California's bacon labeling laws are explicitly preempted by the Federal Meat Inspection Act).

171. *See Gade*, 505 U.S. at 98, 112 S. Ct. at 2393 ("Pre-emption may be . . . implicitly contained in [the statute's] structure and purpose.").

172. *See id.* at 98 ("Absent explicit pre-emptive language, we have recognized at least two types of implied pre-emption: field pre-emption . . . and conflict pre-emption. . . . ").

> [1] the pervasiveness of the federal regulation precludes supplementation by the States, [2] the federal interest in the field is sufficiently dominant; or [3] the object sought to be obtained by the federal law and the character of obligations imposed by it reveal the same purpose.[173]

Conflict preemption exists where either:

> 1. The "state law 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress'", [174] or
> 2. "[I]t is 'impossible for a party to comply with both state and federal requirements.'"[175]

B. *"De Canas" and Preemption of State Regulation of the Employment of Undocumented Immigrants*

The Supreme Court has, in several cases, found that state regulation in the immigration context was preempted by federal law.[176] In *Hines v. Davidowitz*, for example, the Court held that the Alien Registration Act adopted by the Commonwealth of Pennsylvania was preempted by federal law because the law was

> [I]n a field which affects international relations, the one aspect of our government that from the first has been most generally conceded imperatively to demand broad national authority. . . . [T]he power to restrict, limit, regulate, and register aliens as a distinct group is not an equal and continuously existing concurrent power of state and nation, but that whatever power a state may have is subordinate to supreme national law.[177]
>
> [The Alien Registration Act] require[d] every alien 18 years or over . . . to register once each year; pay $1 as an annual registration fee; receive an alien

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173. Schneidewind v. ANR Pipeline Co., 485 U.S. 293, 300, 108 S. Ct. 1145, 115-51 (1988) (citations omitted).

174. Geier v. Am. Honda Motor Co. Inc., 529 U.S. 861, 899, 120 S. Ct. 1913, 1935 (2000) (quoting Hines v. Davidowitz, 312 U.S. 52, 67, 61 S. Ct. 399, 404 (1941)).

175. *Id.* (quoting English v. Gen. Elec. Co., 496 U.S. 72, 79, 110 S. Ct. 2270, 2275 (1990).

176. *See* CHEMERINSKY, *supra* note 64, § 5.2.3.

177. Hines v. Davidowitz, 312 U.S. 52, 68, 61 S. Ct. 399, 404-05 (1941)*; see also* CHEMERINSKY, *supra* note 64, § 5.2.3.

> identification card and carry it at all times; show the card whenever it may be demanded by any police officer or any agent of the Department of Labor and Industry; and exhibit the card as a condition precedent to registering a motor vehicle in his name or obtaining a license to operate one.[178]

In *Takahashi v. Fish and Game Comm'n*, the Court found that the State of California could not deny a fishing license to an alien who was ineligible for citizenship.[179] The California law burdened a person of Japanese descent who was precluded by federal law at the time, along with "certain other nonwhite racial groups," from obtaining citizenship in the United States.[180] The Court reasoned, in part, the following:

> The Federal Government has broad constitutional powers in determining what aliens shall be admitted to the United States, the period they may remain, regulation of their conduct before naturalization, and the terms and conditions of their naturalization. Under the Constitution the states are granted no such powers; they can neither add to nor take from the conditions lawfully imposed by Congress upon admission, naturalization and residence of aliens in the United States or the several states. State laws which impose discriminatory burdens upon the entrance or residence of aliens lawfully within the United States conflict with this constitutionally derived federal power to regulate immigration, and have accordingly been held invalid.[181]

In 1976 the Court, however, set out a different standard for state regulation of the employment of undocumented immigrants in *De Canas v. Bica*.[182] In *De Canas*, immigrant migrant farm workers challenged a California statute which provided that "no employer shall knowingly employ an alien who is not entitled to lawful residence in the United States if such employment would

178. *Hines*, 312 U.S. at 59, 61 S. Ct. at 400; *see also* CHEMERINSKY, *supra* note 64, § 5.2.3.

179. Takahashi v. Fish and Game Comm'n, 334 U.S. 410, 414-15, 422, 68 S. Ct. 1138, 1140-41, 1144 (1948); CHEMERINSKY *supra* note 64, § 5.2.3.

180. *Takahashi*, 334 U.S. at 412, 61 S. Ct. at 1139.

181. *See id.* at 419 (citation omitted); *see also* CHEMERINSKY, *supra* note 64, § 5.2.3.

182. 424 U.S. 351, 96 S. Ct. 933 (1976).

have an adverse effect on lawful resident workers."[183] In an opinion written by Justice Brennan, the Court found that the California law was not preempted by the applicable federal law, the Immigration and Nationality Act ("INA"), because "States possess broad authority under their police powers to regulate the employment relationship to protect workers within the State" and because "Congress intends that States may, to the extent consistent with federal law, regulate the employment of illegal aliens."[184] In declining to find express preemption, the Court explained that there was no "specific indication in either the wording or the legislative history of the INA that Congress intended to preclude even harmonious state regulation touching on aliens in general, or the employment of illegal aliens in particular."[185] In declining to find implied preemption, the Court explained that the "comprehensiveness of the INA scheme for regulation of immigration and naturalization, without more, cannot be said to draw in the employment of illegal aliens as 'plainly within . . . [that] central aim of federal regulation.'"[186] Buttressing its argument that express preemption of state regulation in this area was not Congress' objective, the Court reasoned that the 1974 amendments to the Farm Labor Contractor Registration Act expressed Congress' intent that "States may, to the extent consistent with federal law, regulate the employment of illegal aliens."[187] The Court also distinguished its opinion from prior holdings in the area, *Hines v. Davidowitz*[188] and *Pennsylvania v. Nelson*[189], by finding that those cases dealt with federal statutes that were in the specific field that the States were attempting to regulate whereas in *De Canas* "there [was] no indication that Congress intended to preclude state law in the area of employment regulation."[190] The Court also distinguished its holding in *De Canas* from those cases on the grounds that there was

> [A]ffirmative evidence . . . that Congress sanctioned concurrent state legislation on the subject covered by the challenged state law . . .

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183. *Id.* at 352-53.

184. *Id.* at 351, 356, 361.

185. *Id.* at 357-58.

186. *Id.* at 359 (quoting San Diego Unions v. Garmon, 359 U.S. 236, 244, 79 S. Ct. 773, 779 (1959)).

187. *De Canas*, 424 U.S. at 361, 96 S. Ct. at 939; s*ee also* CHEMERINSKY, *supra* note 64, § 5.2.3.

188. 312 U.S. 52, 61 S.Ct. 399 (1941).

189. 350 U.S. 497, 76 S.Ct. 477 (1956).

190. *De Canas v. Bica*, 424 U.S. 351, 96 S. Ct. 933 (1976).

> [and that there was no] similar federal interest in a situation in which the state law is fashioned to remedy local problems, and operates only on local employers, and only with respect to individuals whom the Federal Government has already declared cannot work in this country.[191]

In 1982, the Court reaffirmed the authority of its *De Canas v. Bica* decision when it distinguished this holding from its finding in *Plyler v. Doe.*[192] Restating that the *De Canas* holding stands for the proposition that "States do have some authority to act with respect to illegal aliens, at least where such action mirrors federal objectives and furthers a legitimate state goal," the Court in *Plyler v. Doe* held, in part, that there was "no indication that the disability imposed by [a Texas statute precluding free education to children of undocumented aliens] corresponds to any identifiable congressional policy."[193] Since *Plyler v. Doe,* the Supreme Court has not directly dealt with these issues relating to undocumented immigrants.[194]

C. LULAC v. Wilson, Hazleton, *and Other Recent Developments*

1. *LULAC v. Wilson*

In 1994 California voters passed by statewide referendum Proposition 187, which was intended to "provide for cooperation between [the] agencies of state and local government with the federal government, and to establish a system of required notification by and between such agencies to prevent illegal aliens in the United States from receiving benefits or public services in the State of California."[195] Proposition 187 required law enforcement, social services, health care and public education personnel to:

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191. *Id.* at 363.

192. *See* Plyler v. Doe, 457 U.S. 202, 225-26, 102 S. Ct. 2382, 2399 (1982).

193. *Id. See* TEX. EDUC. CODE § 21.031 (2007).

194. *See* CHEMERINSKY, *supra* note 64, § 9.5.5. *But see id.* § 9.5.5 n.69, (discussing two Supreme Court cases dealing with other issues concerning undocumented aliens, *Martinez v. Bynum,* 461 U.S. 321, 103 S. Ct. 1838 (1983) and *Reno v. Flores,* 507 U.S. 292, 113 S. Ct. 1439 (1993)). *See also* Toll v. Moreno, 458 U.S. 1, 102 S. Ct. 2977 (1982); Hoffman Plastic Compounds, Inc. v. N.L.R.B., 535 U.S. 137, 122 S. Ct. 1275 (2002); Sure-Tan Inc. v. N.L.R.B., 467 U.S. 883, 104 S. Ct. 2803 (1984) (three more examples of Court decisions dealing with other issues concerning undocumented aliens).

195. League of United Latin Am. Citizens v. Wilson, 908 F. Supp. 755, 763 (C.D. Cal. 1995) (quoting Prop. 187, § 1 (Ca. 1994)) [hereinafter LULAC v. Wilson].

> (i) verify the immigration status of persons with whom they come in contact;
> (ii) notify certain defined persons of their immigration status;
> (iii) report those persons to state and federal officials; and
> (iv) deny those persons social services, health care, and education.[196]

Public interest groups and individual citizens brought action challenging these provisions in *LULAC v. Wilson*.[197] In this case, the District Court for the Central District of California was not unsympathetic with the California voters' decision, noting that the "overwhelming approval of Proposition 187 reflects their justifiable frustration with the federal government's inability to enforce the immigration laws effectively."[198] The court noted, however, that despite the problem created by the federal government, "the authority to regulate immigration belongs exclusively to the federal government and state agencies are not permitted to assume that authority. The State is powerless to enact its own scheme to regulate immigration or to devise immigration regulations which run parallel to or purport to supplement the federal immigration laws."[199] Specifically, the court preempted, under the *De Canas* rationale, the provisions which created "a regulatory scheme (1) to detect persons present in California in violation of state-created categories of lawful immigration status; (2) to notify state and federal officials of their purportedly unlawful status; and (3) to effect their removal from the United States."[200] The court also preempted the provision which provided for a denial of a primary and secondary education to illegal aliens as it conflicted with federal law established in *Plyler v. Doe*.[201] The provisions for denial of benefits, however, were not preempted because they "have only an incidental impact on immigration" and no authority was presented "that Congress intended to completely oust state authority to legislate in the area of benefits denial."[202]

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196. *Id.* The proposition passed with a 59% to 41% voter margin. *Id.*

197. *See id.* at 763 nn. 1-2.

198. *See id.* at 786.

199. *Id.*

200. *Id.* at 786-87.

201. LULAC v. Wilson, 908 F. Supp. 755, 787 (C.D. Cal. 1995). The court, however, did not preempt the provision providing a denial of *postsecondary* education as it did "not appear to conflict with any federal law." *See id.* at 782.

202. *Id.*

After the *LULAC v. Wilson* decision, Congress enacted the Personal Responsibility and Work Opportunity Reconciliation Act ("PRA"), which specified that "it is the immigration policy of the United States to restrict alien access to substantially all public benefits."[203] In light of this act and upon request from defendants, the District Court for the Central District of California reconsidered its original decision in *LULAC v. Wilson*.[204] The court analyzed the effects of the PRA on Proposition 187 and concluded the following:

> [T]he PRA ousts state power to legislate in the area of public benefits for aliens. When President Clinton signed the PRA, he effectively ended any further debate about what the states could do in this field. As the Court pointed out in its prior Opinion, California is powerless to enact its own legislative scheme to regulate immigration. It is likewise powerless to enact its own legislative scheme to regulate alien access to public benefits. It can do what the PRA permits, and nothing more. Federal power in these areas was always exclusive and the PRA only serves to reinforce the Court's prior conclusion that substantially all of the provisions of Proposition 187 are preempted under *De Canas v. Bica*.[205]

Accordingly, upon reconsideration, the court expanded its original holding in *LULAC v. Wilson* to also preempt California's provisions denying benefits to undocumented aliens.[206]

2. *Lozano v. Hazleton*

On July 13, 2006 the City of Hazleton, Pennsylvania began implementing several ordinances "aimed at combating what the city viewed as the problems created by the presence of 'illegal

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203. League of United Latin Am. Citizens v. Wilson, 997 F. Supp. 1244, 1261 (C.D. Cal. 1997) [hereinafter LULAC v. Wilson II].

204. *See id.* at 1244.

205. *Id.* at 1261.

206. *Id.* The court ultimately found the denial of health and social services and postsecondary education benefits to aliens under Proposition 187 preempted by the PRA. *Id.* at 1256. Additionally, the sections of Proposition 187 that denied public elementary benefits, secondary education benefits, public social services, and health benefits were found to be invalid. *Id.* at 1255-56. The court held that those portions of the proposition that had been preempted for violating federal law were not functionally severable from the rest of the proposition. *Id.* at 1259. However, the court did uphold the enforceability of § 3 of the proposition, allowing persons who use false documents to conceal their citizenship or resident alien status to be penalized. *Id.* at 1261.

aliens.'"[207] One of these ordinances was the Illegal Immigration Relief Act Ordinance ("IIRA"), which "prohibit[ed] the employment and harboring of undocumented aliens in the City of Hazleton."[208]

Other ordinances passed included the Tenant Registration Ordinance ("RO"), which precluded non-citizens and unlawful residents from renting apartments, and the Official English Ordinance.[209] The "IIRA define[d] 'illegal alien' as an alien who is not lawfully present in the United States, according to the terms of the United States Code Title 8, section 1101 et seq."[210] The United States Code Title 8, section 1101 et seq. is also known as the Federal Immigration and Nationality Act ("INA") and does not provide a definition for "illegal alien" or "lawfully present."[211]

On August 15, 2006 a group of plaintiffs filed suit challenging these ordinances.[212] The plaintiffs included lawful permanent residents, undocumented aliens, the Hazleton Hispanic Business Association, a group of approximately twenty seven Hispanic business and property owners, and a few other public interest groups.[213] Among other challenges, the plaintiffs claimed that the Hazleton ordinances violated the United States Constitution's Supremacy Clause.[214] The court agreed with this challenge, finding that the Hazleton ordinances violated federal preemption on both express and implied preemption grounds.[215]

In finding the Hazleton ordinance to be expressly preempted, the court explained that the federal Immigration Reform and Control Act of 1986 ("IRCA") "contains an express pre-emption clause that pre-empts State or local laws dealing with the employment of unauthorized aliens."[216] The applicable pre-emption clause states as follows: "The provisions of this section preempt any State or local law imposing civil or criminal sanctions (other than through licensing and similar laws) upon those who employ, or recruit or refer for a fee for employment, unauthorized aliens."[217]

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207. Lozano v. Hazleton, 496 F. Supp. 2d 477, 484 (M.D. Pa. 2007).
208. *Id.*
209. *Id.*
210. *Id.* at 485 (citing IIRA § 3.D.).
211. *Id.*
212. *Id.*
213. *Lozano*, 496 F. Supp. 2d, at 485-86.
214. *Id.* at 517.
215. *Id.* at 517-29.
216. *Id.* at 519.
217. *Id.* (quoting 8 U.S.C. § 1324a(h)(2)).

The City of Hazleton defended its business regulation, arguing that the regulation was expressly within the IRCA pre-emption clause which empowered the City to suspend a business permit, or license, for businesses that hired and employed undocumented workers.[218] The court disagreed, stating that this "ultimate sanction" of putting a company out of business was "at odds with the plain language of the express pre-emption provision."[219] The court reasoned that "[i]t would not make sense for Congress in limiting the state's authority to allow states and municipalities the opportunity to provide the ultimate sanction, but no lesser penalty."[220] The court also found that the ordinance was counterintuitive to the federal legislative history of the "licensing" exception within the pre-emption clause.[221] The court reasoned that the legislative history showed that the statute focused on revocation of a "license" in violation of IRCA, whereas the Hazleton ordinance focused on a violation of local laws.[222]

In finding the Hazleton ordinance to be impliedly pre-empted, the court explained, at length, that the ordinance violated both field and conflict pre-emption doctrines.[223] The court found that the ordinance violated the field pre-emption doctrine because the ordinance supplemented areas that were precluded by the pervasiveness of the federal regulation and because the federal interest in the field was sufficiently dominant.[224] The court explained that the "federal interest in the field was sufficiently dominant" due, in part, to the over one hundred years of federal regulation establishing the federal supremacy over immigration as an "intricate affair" and the presumption that States do not have a strong constitutional interest in immigration.[225]

In finding that "the pervasiveness of the federal regulation" precludes supplementation provided by the Hazleton ordinance, the court declined to extend the rationale provided in *De*

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218. *Id.* at 519.

219. *Lozano,* 496 F. Supp. 2d, at 519.

220. *Id.*

221. *Id.*

222. *Id.* at 519-20.

223. *See id.* at 521-33.

224. *See id.* at 521. The court explained that "[f]ield pre-emption is present where 1) 'the pervasiveness of the federal regulation precludes supplementation by the States'; 2) 'the federal interest in the filed is sufficiently dominant' or 3) 'the object sought to be obtained by the federal law and the character of obligations imposed by it reveal the same purpose.'" *Id.* (quoting Schneidewind v. ANR Pipeline Co., 485 U.S. 293, 300, 108 S. Ct. 1145, 1150-51 (1988)).

225. *Lozano,* 496 F. Supp. 2d, 521-22.

Canas.[226] The court explained that since *De Canas*, which interpreted a proviso to one section of the INA, Congress has passed the IRCA which laid out a "complete statutory scheme that addresse[d] the employment of [undocumented] workers."[227] Accordingly, any supplementation by state law in this area is "either in conflict with the law or a duplication of its terms – the very definition of field pre-emption."[228]

In concluding that the Hazleton ordinance violated the conflict pre-emption doctrine, the court explained that the ordinance "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" and that "it is impossible for a party to comply with both state and federal law."[229] Acknowledging that the federal IRCA and Hazleton's IIRA have the same goals, the court reasoned that the two laws had different means to reach those goals.[230] That is, whereas to comply with the IRCA, employers could utilize Form I-9 and other employment verification mechanisms, the Hazleton ordinance required employers to collect "identification papers" from the employees and provide these papers to the Hazleton Code Enforcement Office.[231] The court concluded that this extra step supplemented the requirements of federal law and was therefore precluded.[232]

The court also found that the IIRA was in conflict with federal law because, unlike the IRCA, the IIRA did not exempt employers from verifying certain categories of workers, such as casual domestic workers and independent contractors.[233] Additionally, unlike the IRCA, the IIRA did not provide for an appeal by the excluded employee to contest an employer's classification of the employee.[234] In addition, the Hazleton ordinance conflicted with federal law because the IIRA provided for strict liability without the element of knowledge whereas the IRCA contained a knowledge requirement.[235] Moreover, the ordinance, unlike the IRCA, was not considerate of foreign policy implications or discrimination against lawful residents as it did

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226. *See id.* at 523-25.

227. *Id.* at 524.

228. *Id.* at 523.

229. *Id.* at 525 (citing Geier v. Am. Honda Motor Co., Inc., 529 U.S. 861, 899, 120 S. Ct. 1913, 1935 (2000)).

230. *Lozano*, 496 F. Supp. 2d, *at* 525-26.

231. *Id.* at 526.

232. *Id.*

233. *Id.*

234. *Id.* at 527.

235. *Id.* at 526.

not contain an anti-discrimination provision.[236] Accordingly, the court explained that the City of Hazleton failed to acknowledge that the ordinance will affect not only illegal aliens, but "every employer, every employee who is challenged as an illegal alien and every prospective employee especially those who look or act as if they are foreign."[237]

3. Other Recent Cases in the Area

A number of other jurisdictions have recently enacted laws targeting the employment and living arrangements of undocumented persons.[238] Below is a sampling of some of the recent court decisions in these cases.

In *Roe v. Prince William County*, persons of varying immigration status and several public interest groups challenged a Virginia county resolution, before it became effective, that authorized police to "inquire into an individual's immigration status when that person is otherwise lawfully detained for a violation of federal or state law" and "direct[ed] [local authorities] to provide a report to the Board regarding the legal authority of the County to restrict services based on immigration status."[239] The District Court in the Eastern District of Virginia ruled that the plaintiffs lacked standing but noted that the holding in *Lozano v. Hazleton* was not applicable as the county resolution did not deal with business regulation or the leasing of property.[240]

Similarly, in *National Coalition of Latino Clergy v. Henry*, the District Court in the Northern District of Oklahoma ruled that the plaintiffs did not have standing to challenge Oklahoma House Bill 1804 ("HB 1804") prior to its effective date.[241] The plaintiffs feared that HB 1804, if enforced, would criminalize persons who "harbor[ed]" an "undocumented person."[242] The court noted, however, that its holding "does not close the

236. *Id.* at 527-28.

237. *Id.* at 529.

238. *See* Villas at Parkside Partners v. City of Farmers Branch, 496 F. Supp. 2d 757 (N.D. Tex. 2007); Garrett v. City of Escondido, 465 F. Supp. 2d 1043 (S.D. Cal. 2006); Lozano v. Hazleton, 496 F. Supp. 2d 477 (M.D. Pa. 2007); Gray v. City of Valley Park, No. 07-0088, 2008 WL 294294, slip op. (E.D. Mo. Jan. 31, 2008).

239. 525 F. Supp. 2d 799, 801-02 (E.D. Va. 2007).

240. *See id.* at 806-07.

241. No. 07-CV-594-JHP, 2007 WL 3113427, slip op., at *6 (N.D. Okla. Oct. 22, 2007). *See also* Rachel Morse, *Following Lozano v. Hazleton: Keep States and Cities Out of the Immigration Business*, 28 B.C. THIRD WORLD L.J. 513, 532 (2008).

242. *Id.* at *4.

courthouse door to those wishing to challenge the constitutional soundness of HB 1804."[243]

In *Villas at Parkside Partners v. City of Farmers Branch*, the District Court for the Northern District of Texas held that a city ordinance which required evidence of citizenship or eligible immigration status as a prerequisite for entering into a lease was preempted by federal immigration law.[244] In May 2008, the court extended the preliminary injunction which enforced this holding to a permanent injunction.[245] The court reasoned as follows:

The court rejects the city's thinly-veiled argument that tries to distinguish its Ordinance as no more than a system of recordkeeping that is intended to assist the federal government in its enforcement of immigration laws. While the city may describe the Ordinance in this way, it is clear that the actual text of the Ordinance makes the provision of immigration documentation a "prerequisite" to the renting of an apartment in Farmers Branch.[246]

The court also distinguished its holding from those in *Arizona Contractors Ass'n v. Candelaria* and *Gray v. City of Valley Park*.[247] In *Garrett v. City of Escondido*, the District Court for the Southern District of California held that a city ordinance that sanctioned landlords who rented to illegal aliens was unconstitutional and preempted by federal law.[248]

In *Arizona Contractors Ass'n v. Candelaria*, a group of non-profit employer organizations challenged the constitutionality of the Legal Arizona Workers Act which granted the Superior Court of Arizona the power to "suspend or revoke the business licenses of employers who intentionally or knowingly employ unauthorized aliens."[249] The District Court for Arizona held, among other things, that the statute was not preempted by IRCA.[250] Similarly, in *Gray v. City of Valley Park*, the District Court for the Eastern District of Missouri held that a city

243. *Id.* at *7.

244. 496 F. Supp. 2d 757 (N.D. Tex. 2007).

245. *See* Villas at Parkside Partners v. City of Farmers Branch, No. 3:06-CV-2376-L, 2008 WL 2201980, slip op., at *19-20 (N.D. Tex. May 28, 2008).

246. *See id.* at *12.

247. *See id.* at *4.

248. 465 F. Supp. 2d 1043, 1057 (S.D. Cal. 2006).

249. 534 F. Supp. 2d 1036, 1040 (D. Ariz. 2008); *see also* Ariz. Contractors Ass'n, Inc. v. Napolitano, No. CV07-1355-PHX-NVW, at *1 (D. Ariz. Dec. 21, 2007).

250. *See Candelaria*, 534 F. Supp. 2d at 1051.

ordinance which limited the employment of illegal immigrants was not preempted by federal immigration law.[251]

D. *Federal Preemption of Texas' "Undocumented Worker" Provision*

How a court would rule on the constitutionality of Texas' "Undocumented Worker" tax provision under the preemption doctrine is an interesting question. Presuming that this law is a form of regulation on business,[252] one must navigate *De Canas* and its surrounding doctrine. While the cases of *Hines v. Davidowitz*[253] and *Takahashi v. Fish and Game Commission*[254] provide broad language precluding state regulation in the immigration context, they can be distinguished by *De Canas*, which deals with the more specific context of state regulation of undocumented aliens.[255] Accordingly, to the extent that the Texas law is harmonious and consistent with federal law in the area, a court could find that state regulation is not preempted under express and implied doctrine under the *De Canas* rationale. As the Texas statute defines an undocumented worker as "a person who is not lawfully entitled to be present and employed in the United States,"[256] such a conclusion could be plausible given that the law broadly defers to United States, or federal law.

Recent developments in the area stemming from Congressional immigration reform acts passed subsequent to *De Canas*, however, have brought into question the *De Canas* rationale. In the two *LULAC v. Wilson* decisions, for example, a court used the *De Canas* rationale to strike down and preempt benefits denial provisions of California's Proposition 187 because it was clear that recent Congressional legislation intended to "oust state power to legislate in the area."[257] Accordingly, the court explained that "the State is powerless to enact its own scheme to regulate immigration or to devise immigration regulations which run parallel to or purport to supplement the federal immigration laws."[258] While the *LULAC v. Wilson*

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251. *See* Gray v. City of Valley Park, No. 4:07CV00881 ERW, slip op. at *19 (E.D. Mo. Jan. 31, 2008).

252. *See supra* Part III-V.

253. 312 U.S. 52, 61 S.Ct. 399 (1941).

254. 334 U.S. 410, 68 S. Ct. 1138 (1948).

255. *See supra* notes 183-192 and accompanying text.

256. H.J. of Tex., 79th Leg., 3d C.S. 108 (2006).

257. LULAC v. Wilson II, 997 F. Supp. 1244, 1261 (C.D. Cal. 1997).

258. LULAC v. Wilson, 908 F. Supp. 755, 786 (1995).

decisions dealt with denial of benefits provisions, another court may find deference in the *LULAC v. Wilson* court's posture with regard to general state legislation in the area and immigration regulations that run parallel to or supplement federal immigration laws.[259] Accordingly, a court may find that the Texas undocumented worker tax provision, applying the *LULAC v. Wilson* rationale, impermissibly attempts to provide a parallel or supplemental state level penalty for what is otherwise a violation of federal law.[260]

More on point, the *Hazleton* decision provides an interesting interpretation of the potential interplay between IRCA and the Texas provision. On the express preemption side, a court may find that the Texas provision does not comply with the IRCA's preemption clause.[261] That is, the Texas provision imposes a civil sanction of sorts upon businesses that employ "unauthorized aliens"[262] and comply with the Texas tax law. This civil sanction is in the form of a higher tax bill due to the denial of a deduction for compensation paid to this category of workers.[263] This civil sanction preclusion could also apply if the Comptroller imposes "stiff" state level sanctions, such as those that are triggered by federal violations, as directed by Representative Anchia.[264] On the other hand, if businesses that employ this category of workers choose to deduct this compensation,[265] then these businesses risk, upon a tax audit, being civilly sanctioned for taxes due. This scenario could result even where a business does not knowingly employ undocumented workers and deducts

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259. *Id.*

260. No disallowance of a deduction appears to be present under the Internal Revenue Code for compensation paid to an undocumented worker. *See* Sharp, *supra* note 8. The Internal Revenue Code denies a deduction for an impermissible *payment*, not a deduction, under state law (if such state law is generally enforced). *See* I.R.C. § 162(c)(2) (2008) (stating the following:

> (2) Other illegal payments.—No deduction shall be allowed . . . for any payment . . . made, directly or indirectly, to any person, if the payment constitutes an illegal bribe, illegal kickback, or other illegal payment under any law of the United States, or under any law of a State (but only if such State law is generally enforced), which subjects the payor to a criminal penalty or the loss of license or privilege to engage in a trade or business.

Id.)

261. *See, e.g.*, *Lozano*, 496 F. Supp. 2d at 518.

262. Tex. H.B. 3, 79th Leg., 3d C.S. (2006).

263. *Id.*

264. Internet Video: 3rd Called Spec. Sess., Part 5, starting at 1:55:08 (Tex. H.R. Video Archives Apr. 24, 2006), *available at* http://www.house.state.tx.us/media/chamber/79.htm.

265. *See infra* Part VI.

compensation paid to this group in the normal course of business.[266]

Taken to an extreme, if these civil tax penalties are indeed valid and are not paid by the business, then the State could enforce the tax due by revoking the business's license.[267] As far-fetched as this extreme example seems, it highlights the sort of "ultimate sanction" that the court in *Hazleton* was concerned about. This same point touches upon the *Hazleton* decision's distinction of revoking a "license" for a violation of the IRCA versus a violation of state statute.[268] In addition, the Texas tax provision may lead to personal liability, in violation of the IRCA's express preemption clause, for corporate management who intentionally misreport the applicable tax position.[269]

The implied preemption analysis of the undocumented worker tax provision is also interesting. Compared to *Hazleton*, the Texas provision may be field preempted as the IRCA lays out a "complete statutory scheme" addressing the employment of undocumented workers. Accordingly, similar to the point made earlier regarding express preemption, to the extent that the Texas provision purports to add or supplement a civil penalty for this alleged violation of federal law, the provision may be precluded under the field preemption doctrine.

The Texas tax provision may also be conflict preempted. In contrast to *Hazleton*, the Texas tax provision provides virtually no guidance as to how an employer is to comply with the statute. In addition, the Comptroller has provided little additional guidance as to how to comply with this provision despite a legislative mandate[270] and requests from taxpayers.[271] Because of this lack of guidance, taxpayers may be at a loss as to how to comply with this provision which seeks to impose a state civil penalty for not complying with federal law. In addition, similar to the *Hazleton* rationale, given that the Comptroller's Office would presumably be the one ultimately reviewing the employer's verification of the worker's employment status, this extra step could be interpreted as a supplementation of the requirements under federal law and therefore precluded. The lack of guidance provided by the Texas statute and State

266. *See infra* Part VI. *Cf.* Lozano v. City of Hazleton, 496 F. Supp. 2d 526 (M.D. Pa. 2007).

267. *See* TEX. TAX CODE ANN. § 111.0047 (2007).

268. *Lozano*, 496 F. Supp. 2d at 519.

269. *See* TEX. TAX CODE ANN. § 111.0611 (2007).

270. *See* H.J. of Tex., 79th Leg., 3d C.S. 109 (2006).

271. *See* 32 Tex. Reg. 10035, 10038 (Dec. 28, 2007), *available at* http://www.sos.state.tx.us/texreg/pdf/backview/1228/1228is.pdf.

Comptroller may also cause the provision to conflict, similar to the outcome in *Hazleton*, with the IRCA's exemption for certain categories of workers[272] and appeal mechanisms.[273] In addition, in possible conflict with the IRCA, the Texas tax provision provides no anti-discrimination provisions to mitigate the burdens imposed on persons who "look or act as if they are foreign" and other misclassified persons due to over enforcement.[274] Finally, the Texas provision contains no *intent* or *knowing* element and is thus a strict liability regulation, in contrast with the IRCA.[275]

Given other recent cases, however, the outcome of a challenge like the one to the Texas provision may stray from the *Hazleton* decision depending on the jurisdiction. That is, at the federal district court levels in Arizona and Missouri, state and local regulations targeted at the employment of undocumented workers were held not to be preempted by federal immigration law.[276] However, state regulation of federal immigration law, as it applied to apartment leasing, was held to be preempted by federal district courts in Texas[277] and California.[278] Moreover, as was the case in *Hazleton* and in challenges to Virginia and Oklahoma regulations of undocumented immigrants, Texas taxpayers seeking to challenge this Texas tax provision must have proper standing.[279]

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272. *See* Lozano v. City of Hazleton, 496 F. Supp. 2d 526 (M.D. Pa. 2007).

273. *Id.*

274. *See Lozano*, 496 F. Supp. 2d at 527-29.

275. *See* Juan Vasquez & Jaime Vasquez, *Section 10.35(b)(4)(ii) of Circular 230 is Invalid (But Just In Case It Is Valid, Please Note That You Cannot Rely On This Article To Avoid The Imposition Of Penalties)*, 7 HOUS. BUS. & TAX L.J. 293 (2007). *See also Legislative History of H.B. 3*, *supra* note 20; *supra* text accompanying notes 32-35. Also note that no reasonable cause exception exists within the undocumented worker tax provision. Therefore this scheme may be stricter than applicable IRS rules. *See Lozano*, 496 F. Supp. 2d at 525-26.

276. *See Arizona Contractors Ass'n, Inc. v Canderlaria,* 534 F. Supp. 2d 1036, 1040-41 (D. Ariz. 2008).

277. *See* Nat'l Coal. of Latino Clergy, Inc. v. Henry, No. 07-CV-594-JHP, 2007 WL 3113427, slip op. at *7 (N.D. Okla. Oct. 22, 2007).

278. *See* Garrett v. City of Escondido, 465 F. Supp. 2d 1043, 1057-59 (S.D. Cal. 2006).

279. *See Lozano*, 496 F. Supp. 2d at 487-504; *see also* Roe v. Prince William County, 525 F. Supp. 2d 799, 802 (E.D. Va. 2007); Nat'l Coal. of Latino Clergy, Inc. v. Henry, No. 07-CV-594-JHP, 2007 WL 3113427, slip op. at *4-6 (N.D. Okla. 2007 Oct. 22, 2007). But challenges to the constitutionality of the Texas Margin Tax may be decided quickly once standing is accomplished. *See* Tex. H.B. 3, 79th Leg., 3d C.S. (2006), Sec. 24, *available at* http://www.legis.state,tx.us/tlodocs/793/billtext/pdf/HBoooo3.pdf.

V. CONCLUSION AND PUBLIC POLICY CONSIDERATIONS

A major piece of legislation which is rushed through a legislature is bound to be plagued with problems down the road.[280] Such is the case with the Texas margin tax, which had to be revisited before its implementation by the legislature, the Comptroller, and taxpayer advocacy groups alike.[281] Perhaps the legislature is not at fault as it was trying to preserve the state public school financing system from the Texas Supreme Court's injunctive deadline. According to the Texas Supreme Court, however, the legislature had several opportunities to fix the property tax flaw prior to the court's mandate.[282] Regardless of who is at fault, the margin tax is truly unique in its kind, and Texas taxpayers and the Comptroller will be having to deal with this new tax, whether they like it or not.[283] The saying "it is what it is" certainly applies here.

Given this context, Texas taxpayers, the Texas Comptroller of Public Accounts, the Texas Attorney General, and Texas and federal courts will have to deal with the "undocumented worker" provision that was added to this legislation. Given the surrounding national and local sentiment regarding immigration reform during the time period that this legislation was considered, it is not surprising that this provision was added.[284] Now that the provision exists in the statute, however, it is subject to legal constitutional challenges. Some of these challenges include federal and state equal protection challenges and federal preemption challenges.

The traditional federal equal protection challenge will be interesting given the rational basis review deference afforded to discrimination against unprotected classes and state tax laws in general.[285] However, the *Plyler v. Doe* rationale strengthens the counterargument that discrimination against undocumented workers should be analyzed under a higher level of scrutiny.[286]

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280. *See, e.g.*, Tex. H.B. 3, 79th Leg., 3d C.S. (2006), Legis. History, Tex. S., Statement of Legis. Intent, TEX. LEG. ONLINE, *available at* http://tlo2.tlc.state.tx.us/sjrnl/793/pdf/3sj05-01-f1.pdf#page=5.

281. *See, e.g.*, S. J. of Tex., 79th Leg., 3d C.S. 91 (2006); Tex. H.B. 3928, 80th Leg. (2007); 32 Tex. Reg. 10035, 10038 (Dec. 28, 2007), *available at* http://www.sos.state.tx.us/texreg/pdf/backview/1228/1228is.pdf. *See also, e.g.*, Tax Policy News, *supra* note 51.

282. *See* Neeley v. West Orange-Cove Consol. Indep. Sch. Dist., 176 S.W.3d 746, 754 (Tex. 2005).

283. *See* Atkins & Williams, *supra* note 3; Texas Margin Tax FAQ, *supra* note 3.

284. *See* Ohlenforst, *supra* note 85, at 977.

285. *See* Lawrence v. Texas, 539 U.S. 558, 579-80; 123 S. Ct. 2472, 2484 (2003).

286. *See* CHEMERINSKY, *supra* note 64, at 775-76; *see also* Plyler v. Doe, 457 U.S. 202, 102 S. Ct. 2382 (1982).

Such an argument may require a disparate impact analysis that mandates a finding of discriminatory purpose. The legislative history surrounding this amendment provides strong evidence of the existence of such a discriminatory purpose.[287]

The alternative federal equal protection argument discussed in this article is also persuasive.[288] Using the rationale of *Lawrence v. Texas* combined with that of *Plyler v. Doe, Department of Agriculture v. Moreno*, and *Romer v. Evans*, there is a plausible argument that this Texas law is a "bare . . . desire to harm a politically unpopular group."[257] That is, again, given the surrounding national and local sentiment regarding immigration reform during the time period that this legislation was considered, it can be argued that the law targeted undocumented workers, which were (and still are) a politically unpopular, and arguably powerless, group. Compelling direct evidence of this targeting can be seen in the statements and actions of legislators noted in the legislative history.[289] Such an inference can also be made given the incongruity or non-germaneness of this provision within the larger tax bill. In addition, it could be argued that the provision impermissibly creates and continues to subdue a subclass of persons, many of whom will likely not leave the country. It is also questionable whether state regulation of immigration, a field that has traditionally been reserved to the federal government, is a legitimate state interest.

On the state equal protection front, a corporation likely will not qualify for the strict judicial scrutiny offered to classes covered under the Texas Equal Rights Amendment. However, a credible argument exists that the tax provision violates the Texas Equal Protection Clause because it is not rationally related to a legitimate state interest,[290] detracts from the central purpose of the tax statute,[291] and is impermissibly arbitrary, unreasonable, capricious, and vague.[292] These arguments may enable the undocumented worker tax provision to be scrutinized more strictly than the normal rational basis review.

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287. *See* Internet Video, *supra* note 38; *see also* Ohlenforst, *supra* note 85, at 977.

288. *See supra* Part III.D.

[257] *See* Romer v. Evans, 517 U.S. 620, 634, 116 S. Ct. 1620, 1628 (1996) (quoting Dep't of Agric. v. Moreno, 413 U.S. 528, 534, 93 S. Ct. 2821, 2825-26 (1973)).

289. *See* Internet Video, *supra* note 38.

290. *See* Smith v. State, 866 S.W.2d 760, 764 (Tex. App.— Houston [1st Dist.] 1993).

291. *See* HL Farm Corp. v. Self, 877 S.W.2d 288, 290 (Tex. 1994).

292. *See* Fairmont Dallas Rests., Inc. v. McBeath, 618 S.W.2d 931, 933 (Tex. Civ. App. 1981).

Preemption of state and local immigration regulation is another persuasive challenge to this tax provision. Given that the federal government has a primary and exclusive interest in regulating immigration, states and localities are virtually powerless to implement regulation in this area.[293] However, *De Canas* and a few other federal cases have held that this type of regulation is not preempted by federal immigration law to the extent that the state and local regulation is consistent with, and not in conflict with or supplemental to, federal law.[294]

The recent *Hazleton* decision and other recent decisions, however, take a different viewpoint from the perspective of regulating the employment of undocumented persons.[295] Particularly, the *Hazleton* decision's analysis of the impact that the Immigration Reform and Control Act has had on express and implied preemption of state immigration regulation is compelling.[296]

One point referred to above is quite relevant: the impact of this tax provision on Texas taxpayer entities subjected to the new margin tax.[297] Many Texas businesses, like many other businesses all over the country, employ undocumented workers.[298] Many of these businesses are unknowingly or unintentionally employing these workers. For many of these businesses, complying with a new Texas business tax, that is perceived as the largest tax increase in the State's history,[299] will prove burdensome at the very least. Due in part to the unfamiliarity of filing this type of business tax, which is the first of its kind, many businesses will likely fail to comply with the tax law in the first few filing years.[300] This presumption would include businesses that employ undocumented workers. While a multitude of resources are available on the web and at the

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293. *See* De Canas v. Bica, 424 U.S. 351, 354, 96 S. Ct. 933, 936 (1976).

294. *Id.* at 358.

295. *See supra* Part V.C.

296. Lozano v. City of Hazelton, 496 F. Supp. 2d 477, 518-24 (M.D. Pa. 2007).

297. *See supra* notes 144-147 and accompanying text.

298. *See* TEXAS COMPTROLLER OF PUBLIC ACCOUNTS, SPECIAL REPORT: UNDOCUMENTED IMMIGRANTS IN TEXAS 3 (Dec. 2006) (discussing the number of undocumented workers in Texas and the industries in which they work), *available at* http://www.window.state.tx.us/specialrpt/undocumented/undocumented.pdf.

299. *Texas Margin Tax: Big Changes in the Lone Star State*, STATE AND LOCAL TAX WATCH (RSM McGladrey, Inc.), Summer 2006, at 1, http://www.rsmmcgladrey.com/RSM-Resources/Publications/State-Local-Tax/Summer-2006/Texas-margin-tax/?year=2006.

300. *See generally* Terrence Stutz, *State Legislature*, THE DALLAS MORNING NEWS, June 16, 2008, *available at* http://www.dallasnews.com/sharedcontent/dws/news/texassouthwest/stories/DN-biztax_16tex.ART.State.Edition1.4d51c91.html. (noting the Comptroller's extension of the tax due date one month due to the unfamiliarity with the tax and its complex provisions.)

Comptroller's website to help comply with the tax law, there are still a number of open questions regarding the tax law and many taxpayers are frankly confused and bewildered.[301] Accordingly, some businesses that employ undocumented workers may not know to exclude compensation to undocumented workers from the compensation deduction.

Other businesses may still not comply with the law even though they have diligently studied the tax and hired tax counsel to help comply because they are not aware that some of their employees may be ineligible to work due to their immigration status. Accordingly, many businesses will, like businesses in other states do as a normal practice, mimic their federal computation for their state compensation deduction computation. Representative Otto is concerned that these businesses risk, perhaps unknowingly, being "untruthful" on their Texas state tax return.[302] If these businesses are audited, they risk federal sanctions and a larger tax bill in the form of past taxes due plus interest.[303] These businesses may also be subject to stiff state-level penalties that are triggered by federal violations.[304] If, however, certain taxpayer entities do comply with the tax provision and exclude these payments from applicable deductions then these businesses risk the Comptroller reporting the businesses' practices to the federal government. The point here is that businesses risk being harmed by both complying and not complying with the Texas tax law. Perhaps such a burden imposed by state tax law should be reconsidered.

Rather than waiting for the courts to determine the state and federal constitutional considerations, if parties decide to litigate them, the Texas legislature should consider removing the "undocumented worker" tax provision. As this article discusses, the costs and burdens of such a provision outweigh the tangible benefits. Moreover, it has yet to be determined whether the federal government and applicable courts will bar trigger-happy state and local officials from implementing rules and legislation that effectuate such burdens upon undocumented people present in the United States. Significant case law appears to preclude such practices. Some of these constitutional considerations,

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301. *See* Alexander, *supra* note 29, at B01.
302. *See* Internet Video, *supra* note 38, at 1:53:22.
303. *Id.*
304. *See id.*, at 1:55:08.

however, may be decided sooner rather than later by the Texas Supreme Court.[305]

305. *See* Tex. H.B. 3, 79th Leg., 3rd C.S. § 24 (2006). Some of the other potential constitutional challenges to the Texas Margin Tax other than those related to the undocumented work provision include:

- The claim that the Texas Margin Tax is an invalid income tax under the Texas Constitution notwithstanding the assertion within the legislation itself that it is not an income tax. Tex. Const. art. VIII, § 24, cl. a; H.B. 3, 79th Leg., 3rd Spec. Sess. § 21 (Tex. 2006) ("The franchise tax imposed by Chapter 171, Tax Code, as amended by this Act, is not an income tax and Pub. L. No. 86-272 does not apply to the tax."); *see also* Letter from Carole Strayhorn, Texas Comptroller of Public Accounts, to Greg Abbott, Texas Attorney General (April 21, 2006), *available at* http://www.cpa.state.tx.us/news/60421letter.html (requesting official opinion on whether House Bill No. 3 will require submission to the voters under the Texas Constitution); *see also* posting of Alan E. Sherman to Texas State and Local Tax Law Blog, http://www.txsaltlaw.com/archives/55504-print.html (June 12, 2006) (discussing potential consequences of granting primary authority to the Texas Supreme Court over challenges to the Texas Margin Tax).
- The claim that the Texas Margin Tax violates Public Law 86-272 which precludes a state from maintaining an income tax on businesses whose only contact with the state is the solicitation of orders for the sale of tangible personal property. *See* Giles Sutton et al., *Texas' New Margin Tax*, 24 J. STATE TAX'N 35, 37 (2006) (questioning whether the Comptroller will apply the Texas Margin Tax to businesses covered by Public Law 86-272).
- The claim that the requirement that all rate increases of the Texas Margin Tax have approval of a majority of voters in a statewide referendum is an invalid delegation of the Legislature's authority. *See* Carl S. Richie, Jr., *Wrap-up Report: 3rd Special Session of the 79th Texas Legislature*, TEXAS LEGISLATIVE REPORT (Gardere Wynne Sewell LLP), June 2006, at 2, *available at* http://www.gardere.com/Content/hubbard/tbl_s31Publications/FileUpload137/1449/LRA__Report.FINAL.pdf.
- The claim that the Texas Margin Tax's preferential tax rate of one half of a percent for wholesalers and retailers is a violation of equal protection considerations because other businesses are subject to a one percent rate. *See* Letter from Carole Strayhorn, Texas Comptroller of Public Accounts, to Greg Abbott, Texas Attorney General (April 21, 2006), *available at* http://www.cpa.state.tx.us/news/60421letter.html (requesting official opinion on whether the disparate tax rates in House Bill No. 3 are permissible).