

**Referendum H
Limiting a State Business Income Tax Deduction**

1 **Referendum H is a proposed amendment to the Colorado statutes that:**

- 2 ♦ increases state income taxes owed for some businesses that deduct wages or
3 other compensation paid to unauthorized aliens; and
- 4 ♦ defines an unauthorized alien as a person who is not eligible under federal
5 immigration law to work in the United States.

6 **Summary and Analysis**

7 *How do business income taxes work?* Like individuals, businesses pay taxes
8 based on the amount of income they earn. In determining the amount of income on which
9 federal taxes are owed, federal law allows businesses to deduct all expenses that are
10 considered ordinary and necessary in conducting business, including wages. These
11 deductions lower the amount of federal taxes owed. Federal law does not specifically
12 exclude wages paid to unauthorized aliens from a business' income tax deductions. State
13 income taxes are based on federal taxable income. Therefore, any deductions claimed on
14 the federal form also lower the amount of state income taxes owed.

15 *How does Referendum H affect state income taxes?* Beginning January 1, 2008,
16 Referendum H requires businesses to pay state income taxes on wages paid to unauthorized
17 aliens that were deducted on their federal income tax forms. This requirement applies only
18 to annual wages paid of \$600 or more per employee, and only in cases where the business
19 knew it had hired an unauthorized alien. For example, Referendum H is not likely to affect
20 a business that was given fraudulent documents when hiring a worker.

21 **Arguments For**

22 1) Referendum H is part of a broad strategy for addressing the illegal immigration
23 problem at the state level. It targets the employment of unauthorized aliens, which is the
24 root of the illegal immigration problem. As long as job opportunities for unauthorized
25 aliens exist, the incentive to come to Colorado or overstay visas will persist.

26 2) By creating a disincentive for hiring unauthorized aliens, Referendum H
27 reduces the financial advantage that a business gains when it pays lower wages to
28 unauthorized aliens. As a result, it provides a more competitive environment for
29 businesses that pay higher wages to legal workers. By reducing the number of jobs

1 available to unauthorized aliens, more job opportunities will be open to Colorado residents.

2 **Arguments Against**

3 1) Referendum H will likely have little or no impact on illegal immigration. In
4 fact, the measure only increases taxes if a business is willing to acknowledge that it paid
5 wages to unauthorized aliens and used the wages to reduce the amount of federal taxes
6 owed. Furthermore, Referendum H would not impact a business that pays for services in
7 cash or pays wages to an unauthorized alien using fraudulent documentation. As a result,
8 no business in Colorado is likely to pay higher taxes. Finally, there is little incentive to
9 stop hiring unauthorized aliens because a business can get a federal tax break worth at least
10 five times as much as the additional taxes owed to Colorado under this measure.

11 2) Illegal immigration is a national issue, and therefore it is the responsibility of
12 the federal government to enforce and protect the country's borders. Hiring unauthorized
13 aliens is already against the law, which means that the issue Referendum H tries to address
14 would not exist if current laws were enforced.

15 **Estimate of Fiscal Impact**

16 Referendum H may increase state income tax collections. Increased tax collections
17 are expected to be minimal because Referendum H does not apply in a variety of
18 circumstances, such as wages paid in cash or employment gained using fraudulent
19 documents, and compliance is expected to be inconsistent. Any increased tax collections
20 are likely to come through an audit process. A small expenditure for the Department of
21 Revenue will be necessary for computer programming in order to add a line on the state
22 income tax form.