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# What Price Property Tax Relief?

by Robert Kleine, Senior Economist

John Engler was elected governor for many reasons, but one of the most important was his promise to reduce property tax payments by 20 percent. On January 15 the governor unveiled his property tax plan. It includes, for school operating taxes only, a 10-percent cut in the assessment ratio[1] in 1991, and another 5 percent in both 1992 and 1993. This would reduce the ratio in 1993 and subsequent years to 40 percent, 20 percent below the current level of 50 percent. His plan would also limit annual assessment increases to 5 percent or the rate of inflation, whichever is less, for each class of property, freezes assessments in 1992, exempts most senior citizens from school taxes, and raises the maximum homestead property tax credit. This paper examines the details of the plan and what it will mean for Michigan taxpayers and for the state budget.

## MICHIGAN'S PROPERTY TAX BURDEN

Michigan clearly imposes a heavy property tax burden by almost any measure. In 1988–89 property taxes were 4.6 percent of personal income, 31.5 percent above the national average and tenth highest among the fifty states (see Exhibit 1). Per capita property taxes were $765, 33 percent above the national average. There is no recent data measuring the residential property tax burden; however, 1985 data indicate that it is even higher than the overall tax burden because a large amount of commercial and industrial property is exempt from taxes under the industrial facilities tax abatement program. As shown in Exhibit 2 Michigan relies more heavily on the property tax for tax revenues than all but eight other states.

Michigan property taxes increased 84.3 percent from 1980 to 1990, compared with a 78.8 percent increase in personal income. The increase in property taxes resulted from a 70-percent increase in assessments and a 8.6-percent increase in millage rates, from 53.4 mills in 1980 to an estimated 58 mills in 1990. The growth in property tax assessments over the decade was very uneven. Assessments increased at an annual rate of 9 percent from 1980 to 1982, 2.5 percent from 1982 to 1987, and 8.1 percent from 1987 to 1990 (see Exhibit 3). Residential assessments grew even faster in recent years, increasing at an annual rate of 9.2 percent from 1987 to 1990. This sharp jump in the growth rate of assessments since 1987 was concentrated in Macomb and Oakland counties and was a key factor in John Engler's strong showing in those counties. Assessments increased at an annual rate of 12 percent in Oakland County and 10 percent in Macomb County between 1987 and 1990.

If the Engler tax reduction plan had been in effect in FY 1988–89, Michigan per capita property taxes would have been $658, and property taxes would have been 4 percent of personal income, both measures about 14 percent above the national average.

1 The percentage of true cash value at which property is valued for tax purposes. State law requires property to be assessed at 50 percent of true cash value.

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## EXHIBIT 1

### State and Local Property Taxes as a Percentage of Personal Income, 1989

| Rank | State | Percent | Rank | State | Percent | Rank | State | Percent |
|---|---|---|---|---|---|---|---|---|
| 1 | Alaska | 6.62 | 18 | Arizona | 4.09 | 34 | Pennsylvania | 2.89 |
| 2 | Wyoming | 6.34 | 19 | Minnesota | 3.99 | 35 | Maryland | 2.85 |
| 3 | New Hampshire | 5.55 | 20 | Kansas | 3.94 | 36 | South Carolina | 2.76 |
| 4 | Oregon | 5.42 | 21 | Colorado | 3.88 | 37 | Mississippi | 2.62 |
| 5 | Montana | 5.29 | 22 | Illinois | 3.75 | 38 | Nevada | 2.32 |
| 6 | Vermont | 4.85 | 23 | Massachusetts | 3.59 | 39 | North Carolina | 2.28 |
| 7 | New York | 4.83 | | **United States** | **3.52** | 40 | Tennessee | 2.16 |
| 8 | New Jersey | 4.81 | 24 | Utah | 3.48 | 41 | Missouri | 2.06 |
| 9 | Nebraska | 4.75 | 25 | North Dakota | 3.40 | 42 | Hawaii | 2.03 |
| **10** | **MICHIGAN** | **4.63** | 26 | Florida | 3.40 | 43 | West Virginia | 2.00 |
| 11 | Wisconsin | 4.58 | 27 | Washington | 3.37 | 44 | Oklahoma | 2.00 |
| 12 | Maine | 4.46 | 28 | Indiana | 3.24 | 45 | Louisiana | 1.96 |
| 13 | Rhode Island | 4.38 | 29 | Virginia | 3.10 | 46 | Kentucky | 1.78 |
| 14 | Connecticut | 4.36 | 30 | Ohio | 3.09 | 47 | Arkansas | 1.73 |
| 15 | South Dakota | 4.28 | 31 | Idaho | 3.08 | 48 | Delaware | 1.60 |
| 16 | Iowa | 4.26 | 32 | California | 2.97 | 49 | New Mexico | 1.46 |
| 17 | Texas | 4.24 | 33 | Georgia | 2.95 | 50 | Alabama | 1.16 |

## EXHIBIT 2

### Percentage of State and Local Tax Revenues Raised from Each of the Major Taxes, FY 1989 (ranked in order of reliance on the property tax)

| State | Property | Sales | Income | State | Property | Sales | Income |
|---|---|---|---|---|---|---|---|
| Alaska | 81% | 19% | 0% | Minnesota | 34% | 36% | 30% |
| New Hampshire | 79 | 18 | 2 | Indiana | 33 | 41 | 26 |
| Wyoming | 63 | 37 | 0 | Virginia | 33 | 35 | 32 |
| Montana | 55 | 18 | 27 | Pennsylvania | 33 | 38 | 29 |
| Oregon | 50 | 10 | 39 | Idaho | 31 | 41 | 28 |
| New Jersey | 50 | 33 | 17 | Ohio | 31 | 36 | 33 |
| Connecticut | 48 | 45 | 7 | Washington | 31 | 69 | 0 |
| South Dakota | 46 | 54 | 0 | California | 30 | 39 | 31 |
| **MICHIGAN** | **45** | **28** | **27** | Georgia | 30 | 42 | 28 |
| Nebraska | 45 | 36 | 19 | Maryland | 28 | 30 | 42 |
| Texas | 45 | 55 | 0 | Mississippi | 28 | 57 | 15 |
| Vermont | 44 | 33 | 23 | South Carolina | 27 | 45 | 28 |
| Rhode Island | 42 | 33 | 24 | Tennessee | 27 | 72 | 1 |
| Kansas | 41 | 37 | 22 | Nevada | 25 | 75 | 0 |
| Iowa | 40 | 33 | 27 | Missouri | 24 | 48 | 28 |
| Wisconsin | 39 | 32 | 29 | North Carolina | 24 | 42 | 34 |
| Illinois | 39 | 43 | 18 | West Virginia | 23 | 52 | 25 |
| Maine | 38 | 36 | 26 | Delaware | 23 | 20 | 57 |
| Colorado | 38 | 38 | 23 | Oklahoma | 22 | 53 | 24 |
| Florida | 38 | 62 | 0 | Louisiana | 21 | 65 | 14 |
| North Dakota | 37 | 50 | 13 | Arkansas | 20 | 53 | 27 |
| Massachusetts | 37 | 26 | 36 | Kentucky | 20 | 46 | 33 |
| Arizona | 36 | 49 | 15 | Hawaii | 15 | 55 | 30 |
| New York | 35 | 31 | 34 | New Mexico | 15 | 67 | 18 |
| **United States** | **35** | **41** | **24** | Alabama | 14 | 60 | 26 |
| Utah | 34 | 47 | 19 | | | | |

**EXHIBIT 3**

**Michigan Property Tax Assessments, Rates and Collections, 1980–90**

| Year | Assessments (millions) | Percentage Change | Residential Assessments | Percentage Change | Property Tax Millage Rate | Tax Collections (millions) | Percentage Change |
|---|---|---|---|---|---|---|---|
| 1980 | $82,581 | 13.9% | $46,669 | 16.8% | 53.4 | $4,411 | 13.4% |
| 1981 | 91,799 | 11.2 | 53,018 | 13.6 | 53.4 | 4,898 | 11.0 |
| 1982 | 98,139 | 6.9 | 57,491 | 8.4 | 52.7 | 5,173 | 5.6 |
| 1983 | 98,303 | 0.2 | 56,978 | –0.9 | 52.8 | 5,187 | 0.3 |
| 1984 | 100,152 | 1.9 | 58,003 | 1.8 | 53.7 | 5,374 | 3.6 |
| 1985 | 102,685 | 2.5 | 59,070 | 1.8 | 54.5 | 5,593 | 4.1 |
| 1986 | 106,155 | 3.4 | 60,682 | 2.7 | 55.1 | 5,851 | 4.6 |
| 1987 | 111,038 | 4.6 | 63,703 | 5.0 | 56.0 | 6,215 | 6.2 |
| 1988 | 119,014 | 7.2 | 68,852 | 8.1 | 56.8 | 6,761 | 8.8 |
| 1989 | 128,813 | 8.2 | 75,467 | 9.6 | 57.4 | 7,391 | 9.3 |
| 1990 | 140,171 | 8.8 | 82,928 | 9.9 | 58.0 (est.) | 8,130 (est.) | 10.0 |

SOURCE: Michigan State Tax Commission.

## THE ENGLER PROPOSAL

The Engler property tax proposal has four major components.

1. The proposal's centerpiece is a reduction in the assessment ratio from the current 50 percent to 40 percent in 1993 and subsequent years, for school operating purposes. The ratio is reduced to 45 percent in 1991, 42.5 percent in 1992, and 40 percent thereafter. This, in effect, will reduce total property taxes by 12 percent (less the loss of property tax credits and federal tax deductions), as school operating taxes account for about 60 percent of total taxes.

2. Assessment increases for each class of property (residential, commercial, and so forth) are limited to 5 percent or the rate of inflation, whichever is less, plus new construction. This will require a constitutional amendment. In addition, assessments will be frozen in 1992. If the amendment is not approved, assessments will be frozen every other year, and the 1978 Headlee tax limitation, which holds increases in total assessments to the rate of inflation, will apply each year. Out-of-formula school districts and other local governments will not be reimbursed for revenues lost due to the freeze in 1992 or in subsequent years. In-formula school districts will be reimbursed by the state school aid fund.

3. Senior citizens earning less than $73,500 will be exempt from school property taxes by 1993. The exemption will be 50 percent in 1991, 75 percent in 1992, and 100 percent thereafter.

4. The maximum homestead property tax credit will be increased from the current $1,200 to $1,400 in 1991. Thereafter, the credit will be increased $100 each year until it reaches $2,500, after which it will be adjusted annually for inflation.

The cost to the state budget, after homestead tax credit savings, is estimated at about $450 million in FY 1991–92, $900 million in FY 1992–93, and $1.2 billion in FY 1993–94. The state currently reimburses taxpayers for 60 percent (100 percent for senior citizens) of all property taxes above 3.5 percent of household income. Therefore, a reduction in property taxes reduces the credit and saves the state money.

**OTHER PROPERTY TAX PROPOSALS**

The legislature soon may be given two other property tax plans to consider. The Board of Canvassers will be meeting in the near future to rule on whether the Headlee iniative petition[2] has enough signatures to meet the constitutional requirement. If the signatures for the Headlee proposal are validated, the legislature has forty session days to enact the proposal or it will be placed on the 1992 ballot. The legislature is likely to feel considerable political pressure to approve the Headlee plan, which if approved would take effect 90 days after the end of the current legislative session or in March 1993. However, the measure can be given immediate effect with two-thirds approval of both houses. The legislature also has the option of putting a competing plan on the ballot.

In addition, the Democrats are planning to introduce their own property tax reduction plan soon. The plan would exempt the first $30,000 of the market value of a home for school operating taxes (limited to 50 percent of the value of a home), provide relief for renters, increase homestead tax credits for seniors and others, and limit residential assessments to the rate of inflation (the assessment would be adjusted upward when the home is sold); the latter would require a constitutional amendment. The plan would take effect in 1991 and would cost about $0.8 billion. The Democrats recommend new funding sources to cover the cost of the program. The introduction of the plan has been delayed by a Michigan Court of Appeals ruling that could expand the capital acquisition deduction in the single business tax, costing the state about $500 million annually. The Democratic plan provides no tax relief for businesses and targets more relief to lower value homes than does the Engler proposal.

There are several important differences between the Engler and Headlee proposals. First, the Headlee proposal would reduce **all** property tax assessments by 20 percent; it would reduce assessments by 10 percent as of December 31, 1990, and by another 10 percent on December 31, 1991, and would require that local governments be reimbursed by the state.

A second difference is that the Headlee proposal is less flexible as to when the reductions take effect and would affect the budget more. It would reduce the summer 1991 property tax assessments by 10 percent, or about $400–450 million, which the state would be obligated to reimburse to local governments. Summer property tax payments are due in August, but the state likely would have the option of delaying the payments until October to avoid affecting the FY 1990–91 budget. Winter property tax payments are due in February, and the cost to the state also would be about $400–450 million. We estimate the total cost for FY 1991–92 at about $880 million but do not have specific numbers on the distribution of summer and winter taxes. In the second year, the Headlee proposal would cost the state an additional $930 million, for a total of about $1.8 billion, assuming a 6-percent increase in property taxes between 1991 and 1992. The state would save an estimated $160 million in reduced homestead property tax credits in the first year

2 The Headlee iniative reduces property tax assessments by 20 percent over a two-year period and requires the state to reimburse local units of government.

and $300 million in the second and subsequent years. (See below.) The net cost to the state, after the reduction in tax credits, of the full 20 percent reduction under the Headlee proposal thus would be about $1.5 billion.

If the signatures on the Headlee initiative are not validated, the legislature will have more flexibility in implementing a property tax reduction plan. The effective date could be delayed to December 31, 1991, for example, and the program could be phased in over three or four years. If the reduction is delayed until December 31, 1991, the fiscal effect could be delayed until the FY 1992–93 budget. One option would be to reduce assessments by 5 percent in each of the first two years and 10 percent the third year. A 5-percent reduction would cost the state about $440 million (less about $75 million in homestead property tax credit savings).

## MECHANICS OF PROPERTY TAX RELIEF

Currently, the state constitution requires that real and personal property be uniformly assessed at no more than 50 percent of true cash value, and state law requires that property be assessed at 50 percent of true cash value. The Engler and Headlee proposals both reduce the required assessment ratio to 40 percent (45 percent in the first year and 40 percent in the second year in the case of the Headlee plan). However, the Engler plan reduces the ratio only for school operating taxes. For example, if the local assessor determines that the true cash value of a property is $100,000, the assessment under current law would be $50,000. At a 40-percent assessment ratio the assessment would be $40,000. The taxpayer would receive a tax reduction of $10,000 times the local millage rate under the Headlee plan and that amount times the school operating millage rate under Engler's plan. At the state average school operating millage rate of 35 mills, the savings would be $350 (less homestead tax credits). The cost to the school district also would be $350, which would be reimbursed by the state. In-formula school districts would be reimbursed automatically, and out-of-formula districts and other local governments (if the Headlee proposal is enacted) would have to keep track of the cost of the assessment reduction and submit a claim to the state.

One administrative problem with the Engler plan is that two assessments would appear on the tax bill, one for school property taxes and one for all other taxes. This will create additional costs for local treasurers and could confuse taxpayers. An option would be for the treasurer to compute the amount of tax relief and show it as a credit against the total liability.

## EFFECT ON TAXPAYERS

The amount of relief provided to taxpayers under the Engler and Headlee proposals varies widely depending on the value of the home, the local millage rate, household income, the age of the taxpayer, and whether the household currently receives a homestead property tax credit.

Under the Engler or Headlee proposals all taxpayers will receive a reduction in property taxes: 20 percent under the Headlee plan and about 12 percent under the Engler plan. However, owners of residential or agricultural property will lose some of the credits they currently received under the state homestead property tax relief program. The program provides a rebate of 60 percent of all property taxes in excess of 3.5 percent of household income for nonsenior homeowners and 100 percent of the excess for senior citizens. Owners of agricultural property receive a special credit for all property taxes in excess of 7 percent of household income. The effect of the loss of tax credits under both tax reduction plans is that nonsenior homeowners who are eligible for the homestead tax credit will receive a net reduction of 8 percent under the Headlee plan and 4.8 percent under the Engler plan, while senior citizens will receive no additional relief (except for those constrained by the $1,200 maximum credit). Taxpayers who itemize for federal tax purposes also will lose a portion of their federal tax deduction.

Examples of the effects of the Engler plan on various types of homeowners is presented in Exhibit 4. Note that the senior citizen household earning $15,000 receives a tax reduction of $870, but also loses a $870 tax credit. The advantage for most seniors is that their tax will be reduced up front, and they will not have to pay the bill and wait for a refund from the state.[3] The seniors who will benefit most from the Engler proposal are those who currently are constrained by the $1,200 maximum credit. As shown in the exhibit the senior citizen earning $15,000 and living in a $100,000 home will save $1,175 in property taxes. Another interesting example is the comparison of two households earning $50,000. One family lives in a $50,000 house and currently receives no tax credit, while the other family lives in a $100,000 house and receives a credit of $690. Under the Engler plan, the first household saves $174 in property taxes and has no credits to lose; it receives the full 12-percent tax break. The second family receives a property tax reduction of $348, but loses $209 in tax credits, netting an additional $139 in property tax relief, or 4.8 percent of their property tax bill. However, this family receives total property tax relief of $829 (tax credit plus additional tax relief), 28.5 percent of their property tax bill.

Taxpayers earning less than $73,650 will receive less relief from the proposed tax reduction than taxpayers earning more than that amount because the homestead tax credit begins to phase out at that income level (refer to examples in Exhibit 4).

## STRENGTHS AND WEAKNESSES OF THE ENGLER PROPOSAL

The Engler proposal has several **strengths** from the taxpayer's viewpoint. First, it reduces property taxes, which are clearly too high, and limits increases in future assessments (if this provision is approved by the voters in November 1992).

Second, it increases the maximum homestead property tax credit, which has not been increased since 1976 and currently limits tax relief for a number of taxpayers, particularly senior citizens.

Third, the proposal caps revenue growth for fast growing jurisdictions, which are generally the richer ones, by limiting assessment increases to no more than 5 percent and reimbursing local governments for no more than that amount. In effect, this allows poorer districts to close the resource gap with richer school districts because the school aid formula reimburses in-formula districts on the basis of property tax value per pupil. Therefore, any limit on the growth in property values is made up by the state. For example, the FY 1990–91 school aid formula guarantees a district levying 35 mills $3,485 per pupil less locally raised revenue. If the district's property value (SEV) per pupil is $50,000, locally raised revenue will be $1,750 per pupil. This will be deducted from the guarantee, and the state will pay the district $1,735 per pupil. A change in the district's SEV per pupil will not change its total revenue. An increase in SEV to $55,000 per pupil would result in the district receiving $1,925 per pupil in local revenue and $1,560 from the state, for the same total of $3,485. Changes in assessment levels have no effect on the total resources available to in-formula school districts.

3 Current law allows many seniors to defer their summer taxes and to file for their credit after December 1. Therefore, those seniors who take advantage of this law receive their credit before their property tax bill comes due in February.

EXHIBIT 4

**Effect of Engler Tax Reduction Proposal on Various Households**

| Income (000) | Age | Home Value (000) | Millage Rate (58) | Property Taxes | Tax Savings[a] (20% + Senior Exemption) | Current Tax Credit | Credit Reduction | Net Savings | Dollar Effect of Federal Deductibility[b] | % of Tax Liability | % of Tax Liability after Federal Taxes |
|---|---|---|---|---|---|---|---|---|---|---|---|
| $10 | <65 | $30 | 5.8% | $870 | $104 | $312 | $63 | $42 | – | 4.8% | 4.8% |
| 15 | >65 | 50 | 5.8 | 1,450 | 870 | 925 | 870 | 0 | – | 0.0 | 0.0 |
| 15 | >65 | 100 | 5.8 | 2,900 | 1,740 | 1,200 | 565 | 1,175 | – | 40.5 | 40.5 |
| 25 | <65 | 50 | 5.8 | 1,450 | 174 | 345 | 104 | 70 | – | 4.8 | 4.8 |
| 50 | <65 | 50 | 5.8 | 1,450 | 174 | 0 | 0 | 174 | –$57 | 12.0 | 8.0 |
| 50 | <65 | 100 | 5.8 | 2,900 | 348 | 690 | 209 | 139 | –46 | 4.8 | 3.2 |
| 75 | <65 | 125 | 5.8 | 3,625 | 435 | 600 | 261 | 174 | –57 | 4.8 | 3.2 |
| 85 | <65 | 125 | 5.8 | 3,625 | 435 | 0 | 0 | 435 | –144 | 12.0 | 8.0 |
| 100 | <65 | 150 | 5.8 | 4,350 | 522 | 0 | 0 | 522 | –172 | 12.0 | 8.0 |
| 100 | <65 | 120 | 5.8 | 3,480 | 418 | 0 | 0 | 418 | –138 | 12.0 | 8.0 |
| 150 | <65 | 250 | 5.8 | 7,250 | 870 | 0 | 0 | 870 | –287 | 12.0 | 8.0 |

[a]Assumes that school operating taxes are 60 percent of total property taxes.
[b]Assumes households with incomes over $50,000 itemize deductions and pay the 33 percent marginal rate.

Engler's plan also has a number of important weaknesses. First, it does nothing to help school districts that are constrained by the constitutional 50-mill limit. This could be done by reducing total millage rates by 20 percent or school millage rates by about 33 percent, rather than by reducing assessments.

Second, the plan will require two assessment figures on the tax bill, which places an administrative burden on local treasurers and likely will be confusing to taxpayers.

Third, it will provide substantial relief to the wealthiest homeowners and those owning two homes. Many argue that the current homestead tax credit provides sufficient relief from excessive property tax burdens, and that it could be improved and made more generous for a fraction of the cost of the Engler or Headlee proposals.

Fourth, there is no rationale for exempting senior citizens from school taxes. Everyone benefits from the education system, and everyone who is able should pay. Income, not age, should determine the amount of tax relief. Many senior citizens are better off than the general population, and seniors already receive a very generous homestead property tax credit. The exemption could become a particularly costly provision in about twenty years when the baby boom generation begins to turn 65.

Fifth, the proposal may impede the effort to reform our method of financing K-12 education, as it expends dollars on property tax relief that could be used to help reduce the disparities in resources among districts. Also, the proposal may allow wealthier districts to raise additional revenues. This could occur because the reduction in property taxes will make it easier for districts to raise millage rates. (The state will provide reimbursement for higher millage rates levied on the 20-percent assessment reduction.) Increases in millage rates are more likely to occur in wealthier districts with low millage rates than in poorer, in-formula districts with higher millage rates; wealthier districts generally have been more supportive of millage increases, as has been demonstrated by their success in winning voter approval to override Headlee rollback provisions. However, the state's reimbursement to school districts for the reduction in property taxes will be subject to the annual appropriations process, and future legislatures could make changes that reduce reimbursements, particularly to out-of-formula school districts. The legislature is moving in this direction, as demonstrated by the $50-million increase in the amount of revenue captured from out-of-formula districts in the 1990–91 school aid formula.

Sixth, the Engler plan provides no relief for renters, who make up about 27 percent of the population. Taxes for owners of rental property will be reduced, but owners are not likely to pass savings on to renters.

Seventh, freezing assessments every other year could create a problem because the constitution currently limits annual assessment increases to the rate of inflation. The result could be that assessment increases for a two-year period will be limited in one year's rate of inflation. This is very restrictive and could create severe fiscal problems for many units of local government.

## FUNDING THE PROPERTY TAX REDUCTION

Everyone wants property tax relief, but few want to pay the cost, which is going to be either fewer government services or higher taxes. There are three basic options available for financing the tax reduction.

1. **The state could increase taxes.** For example, increasing the income tax rate from 4.6 to 5.7 percent would raise the $1.2 billion needed to finance the Engler property tax cut. The state also could raise substantial revenues by raising the single business tax ($750 million in revenue per one-percent increase), extending the sales tax to services, or eliminating certain tax expenditures. As shown in Exhibit 5, Michigan has a lower sales tax burden, 2.9 percent of personal income, than every state that levies a general sales tax except Massachusetts. However, it is clear that the public does not want taxes to be raised, and John Engler has no intention of doing so.

**EXHIBIT 5**

**State and Local Sales Taxes as a Percentage of Personal Income, 1989**

| Rank | State | Percent | Rank | State | Percent | Rank | State | Percent |
|---|---|---|---|---|---|---|---|---|
| 1 | Hawaii | 7.45 | 18 | West Virginia | 4.49 | 34 | Nebraska | 3.73 |
| 2 | Washington | 7.37 | 19 | Maine | 4.26 | 35 | Vermont | 3.63 |
| 3 | Nevada | 6.93 | 20 | New York | 4.24 | 36 | Kansas | 3.36 |
| 4 | New Mexico | 6.73 | 21 | Minnesota | 4.22 | 37 | Iowa | 3.55 |
| 5 | Louisiana | 5.99 | 22 | Missouri | 4.12 | 38 | Ohio | 3.52 |
| 6 | Tennessee | 5.77 | 23 | Idaho | 4.12 | 39 | Rhode Island | 3.46 |
| 7 | Arizona | 5.66 | 24 | Indiana | 4.12 | 40 | Pennsylvania | 3.27 |
| 8 | Florida | 5.45 | 25 | Georgia | 4.11 | 41 | Virginia | 3.25 |
| 9 | Mississippi | 5.28 | | **United States** | **4.10** | 42 | New Jersey | 3.14 |
| 10 | Texas | 5.24 | 26 | Kentucky | 4.10 | 43 | Maryland | 3.11 |
| 11 | South Dakota | 4.94 | 27 | Connecticut | 4.10 | **44** | **MICHIGAN** | **2.87** |
| 12 | Alabama | 4.89 | 28 | Illinois | 4.08 | 45 | Massachusetts | 2.51 |
| 13 | Utah | 4.79 | 29 | North Carolina | 4.06 | 46 | Montana[a] | 1.73 |
| 14 | Oklahoma | 4.77 | 30 | Colorado | 3.85 | 47 | Alaska[a] | 1.57 |
| 15 | Arkansas | 4.64 | 31 | California | 3.80 | 48 | Delaware[a] | 1.37 |
| 16 | North Dakota | 4.55 | 32 | Wisconsin | 3.77 | 49 | New Hampshire[a] | 1.27 |
| 17 | South Carolina | 4.53 | 33 | Wyoming | 3.74 | 50 | Oregon[a] | 1.12 |

[a]These states doe not impose a general sales tax.

2. **Expenditures can be reduced to allow the state to cover the cost of the reduction.** This becomes very difficult, however, in light of the large cuts already required to balance the current year budget. If the budget is balanced in the current year and revenues increase by about 5 percent or $500 million each year for the next three fiscal years, the tax cut could be financed by holding expenditure increases to about one percent annually. This will mean sharp cuts in some programs, however, if the Engler administration is to keep its promise to increase spending for education. Clearly, this would be difficult coming on top of the large cuts in FY 1990–91. The effect on the budget could be reduced by stretching out the tax cut by reducing assessments only 5 percent the first year and an additional 5 percent for the next three years, reaching the full 20 percent in 1994. This could be financed by holding spending increases to about 2 to 3 percent a year, assuming revenues increase about 5 percent a year. The result would be a "real" reduction of about one to 2 percent each year, after allowing for inflation. This would be painful but could be achieved given the new administration's strong commitment to downsize state government.

3. **Local governments could be required to share a portion of the cost.** This is not likely to happen. The Headlee proposal requires the state to reimburse local governments fully, and John Engler also has promised full reimbursement. This also would be unsound policy, as many local governments are in worse shape than the state and would have to ask voters to raise property tax millages. A policy that does make sense, however, is to limit all reimbursements after year one to the average assessment increase statewide. This would have the effect of equalizing resources among local governments, including school districts. Local governments where property values are increasing slowly would benefit, while local governments where assessments are increasing rapidly would lose some revenue growth. The redistribution effect of such a plan would be sharply limited if assessments are held to the rate of inflation, as proposed by the Engler plan. Clearly, any plan to redistribute local resources is controversial and would generate substantial opposition.

## CONCLUSION

The Engler administration is committed to property tax relief and may have to deliver to win reelection. However, because of the current fiscal crisis the Democrats are not likely to vote for any tax cut without an offsetting revenue source. The governor may be able to win Democratic votes by compromising on the budget. A package that includes more money from the Budget Stabilization Fund (BSF) and the elimination of some tax expenditures may convince the Democrats to vote for tax relief. However, use of temporary measures and one-time revenue sources, such as BSF monies, only push part of the problem into the next fiscal year.

We believe that property taxes will be reduced, but negotiations could go on for a long while. We urge the administration to develop a responsible long-term plan that addresses the major issues—including the budget, tax expenditures, school finance reform, and tax relief—together rather than separately.