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Trend Analysis: Local Option Sales Tax for Bloomington, MN

ESTIMATED CONTRIBUTIONS OF RESIDENTS AND NON-RESIDENTS TO A LOCAL OPTION SALES TAX AND AN EXAMINATION OF TRENDS FROM 2016-2020

Authored by Ryan Pesch

CITY OF BLOOMINGTON MINNESOTA

PROGRAM SPONSORS: CITY OF BLOOMINGTON, MINNESOTA

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Table of Contents

EXECUTIVE SUMMARY 4

BACKGROUND AND METHODOLOGY 5

TAXABLE SALES TRENDS 6

LOCAL OPTION SALES TAX ESTIMATES AND TRENDS 9

NON-RESIDENT ESTIMATES 11

APPENDIX 1: 'OTHER' CATEGORY TAXABLE SALES 13

APPENDIX 2: CALCULATION OF CONSTRUCTION, MANUFACTING, WHOLESALE 14

APPENDIX 3: DEFINITION OF TERMS 15

EXECUTIVE SUMMARY

After an analysis of a Local Option Sales Tax potential based on 2016 and 2018 sales tax statistics, University of Minnesota Extension recently took another look at the trends of taxable sales data for the city. A look at 2020 statistics points to the significant impacts of the pandemic on retail and service sales.

Extension conducted the study to estimate overall tax proceeds and the proportion of tax proceeds generated by Bloomington residents. Comparing these results to non-residents using sales and use tax data available from the Minnesota Department of Revenue (MN Revenue), Extension estimated non-residents spending in by adjusting proportions of non-resident spending using 2020 data based on shifts in taxable sales by category

Calculated in these two ways, Extension estimated that **non-residents comprised 60.4% of 2020 taxable sales subject to a local option sales tax (LOST)**. In comparison, Extension previously estimated that 74.6% of 2016 taxable sales subject to a local option sales tax come from non-residents. This conservative estimate of non-resident spending was calculated using the same categories with 2020 data as the 2016 data from the original report.

Total taxable sales were $3.2 billion in 2016 and dropped significantly to $2.0 billion in 2020. Minnesota Department of Revenue analysts estimated that 68.3% of all taxable sales would have been subject a local option sales tax. Therefore, $2.2 billion and $1.4 billion of would have been subject to a LOST in 2016 and 2020 respectively. **If a local option sales tax were in effect, the city would have generated $11 million in 2016 and a minimum of $6.8 million in 2020**, the strong majority of which would have been garnered from non-residents. Tax proceeds could increase over $12 million by 2023 if taxable sales return to pre-pandemic trends. The historic shakeup in spending due to the pandemic leave forecasts uncertain. One significant unknown in this analysis is the amount of online sales from Bloomington residents, which would be subject to the LOST. These online sales increased significantly during 2020 across the nation, yet Extension cannot estimate the amount of these sales from current sources and these sales would certainly have taken the tax proceeds above the $6.8 million based solely on this data used in this analysis.

The intent of this report was not to make recommendations to city officials about what actions to take, but rather determine the estimated sales tax proceeds from a local option tax program and what proportion of those dollars will likely be paid by year-round city residents versus non-residents to inform decision making.

METHODOLOGY

Extension initially generated a trade area analysis comparing actual taxable sales, based on Minnesota Revenue sales tax data[1] with a calculated "potential sales" amount. This amount was determined by multiplying the Bloomington population by the Minnesota average per capita sales and then adjusting for the city's income factor (See sidebar). Doing so provided an estimate of retail and service purchases made by year-round Bloomington residents. For each merchandise group, the estimates for two types of purchasers—city residents and others—were considered and adjusted considering the area economy. These adjustments involved informed estimates and were aimed, in part, at reducing what otherwise might have been overestimates of the sales tax share falling to non-residents.

Potential Sales estimate the dollar amounts for purchases made by local residents *if* local residents spend as much as the average Minnesota resident.

Potential sales are calculated by the following formula:
(T ÷ PMn) x PB x (YHC ÷YMn) = Potential Sales

T = Total Minnesota taxable sales for a merchandise category

PMn = 2020 Population of Minnesota (5,706,494)

PB = 2020 Population of Bloomington (89,987)

YHC = Per capita income of Hennepin County resident ($79,183)

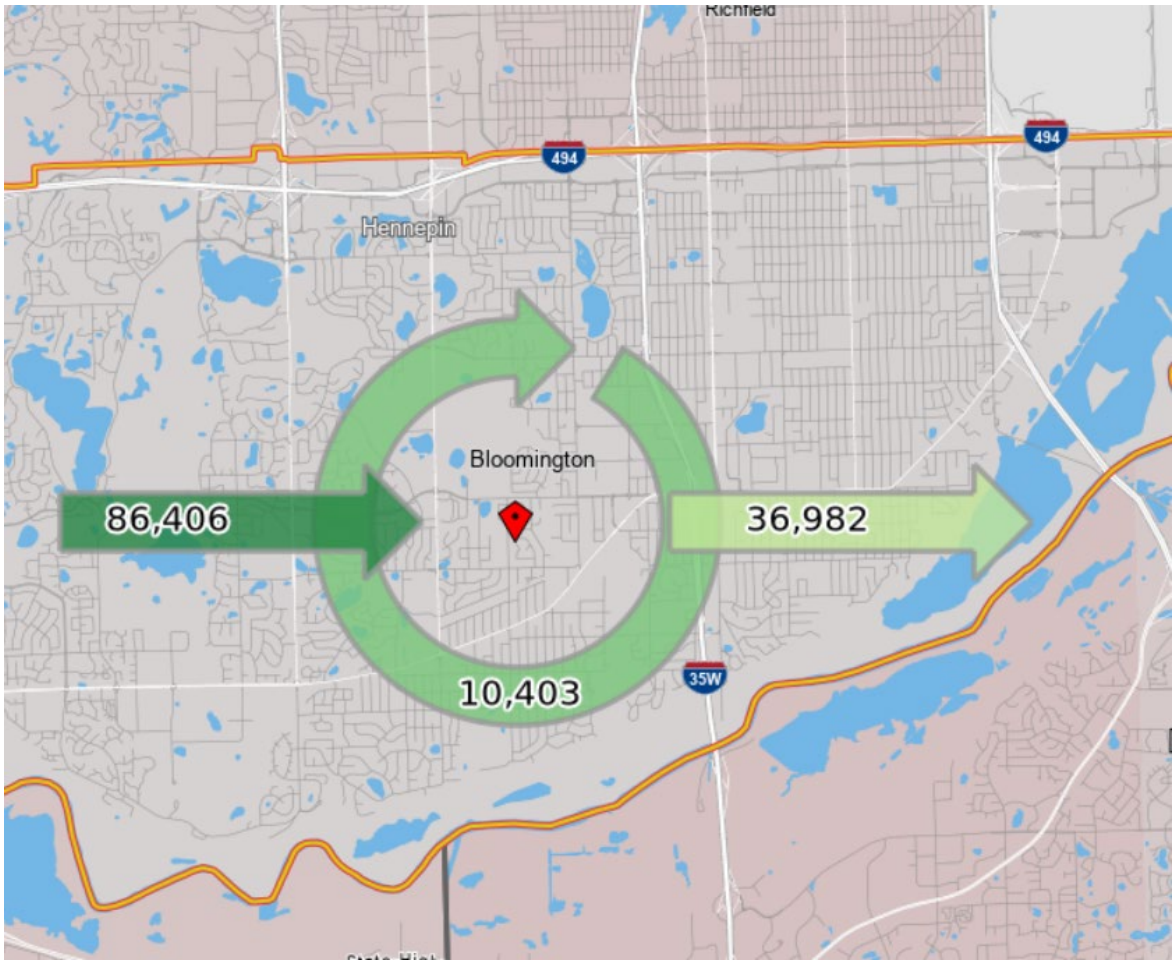
YMn = Per capita income of Minnesota resident ($62,005)

Several key factors and features in the Bloomington economy helped frame our analysis of the different merchandise categories:

- The strength of Bloomington's store mix attracts a significant number of regional and even international visitors and metro-area residents to shop in the community.
- Because of its job base, a large contingent of residents from other communities commute into Bloomington for work. We assume that these non-resident workers purchase goods and services in Bloomington due to convenience. The proportion of non-residents entering Bloomington for work increased by over 3,000 workers between 2016 and 2019 (most recent published data).
- We assume that Bloomington residents are pulled to other communities to shop, despite the strong retail mix in Bloomington. This is in part due to the number of residents that work outside of the community (nearly 30,000 according to Census figures) and the close proximity of competing shopping areas (Figure 1).

1. *MN City Sales Tax Statistics.* Minnesota Department of Revenue. Retrieved from https://www.revenue.state.mn.us/sales-and-use-tax-statistics-and-annual-reports

Figure 1: Bloomington worker in-flow and out-flow (Source: 2019 U.S. Census Bureau OnTheMap application, Longitudinal-Employer Household Dynamics Program, http://onthemap.ces.census.gov/)

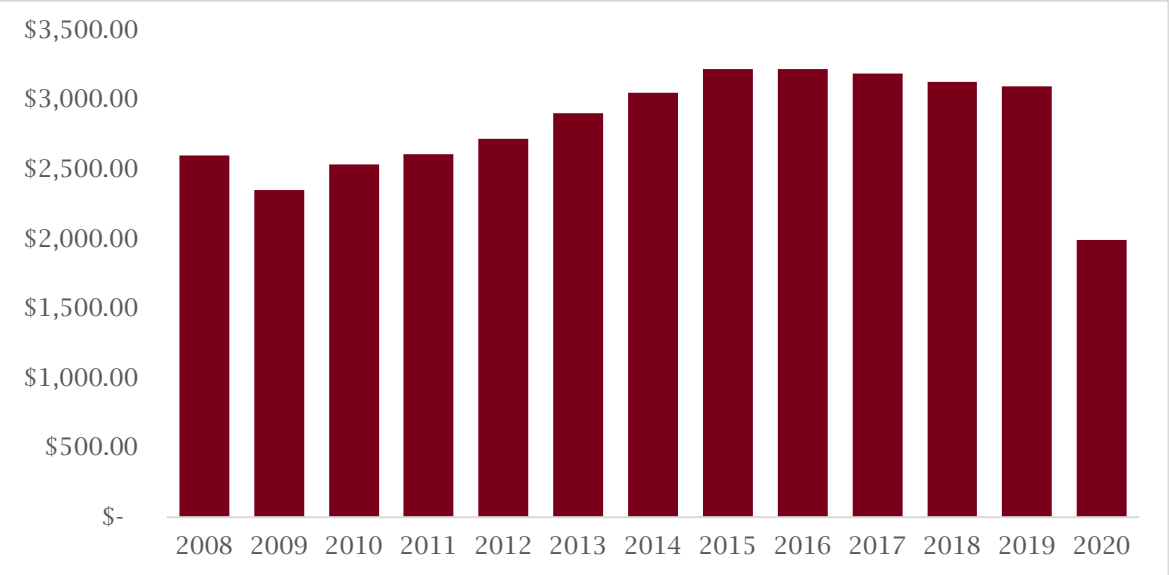


Taxable Sales Trends

Total taxable sales in Bloomington have grown over the past ten years, but with a slight decrease from 2016 to 2019 with a significant dip in 2020.

Total taxable sales in the city have increased 31.7 percent from 2009 to 2019 from $2.3 billion to $3.1 billion, yet dropped 35.6% or $1.1 billion between 2019 and 2020 due to the significant disruption caused by the pandemic (Figure 2).

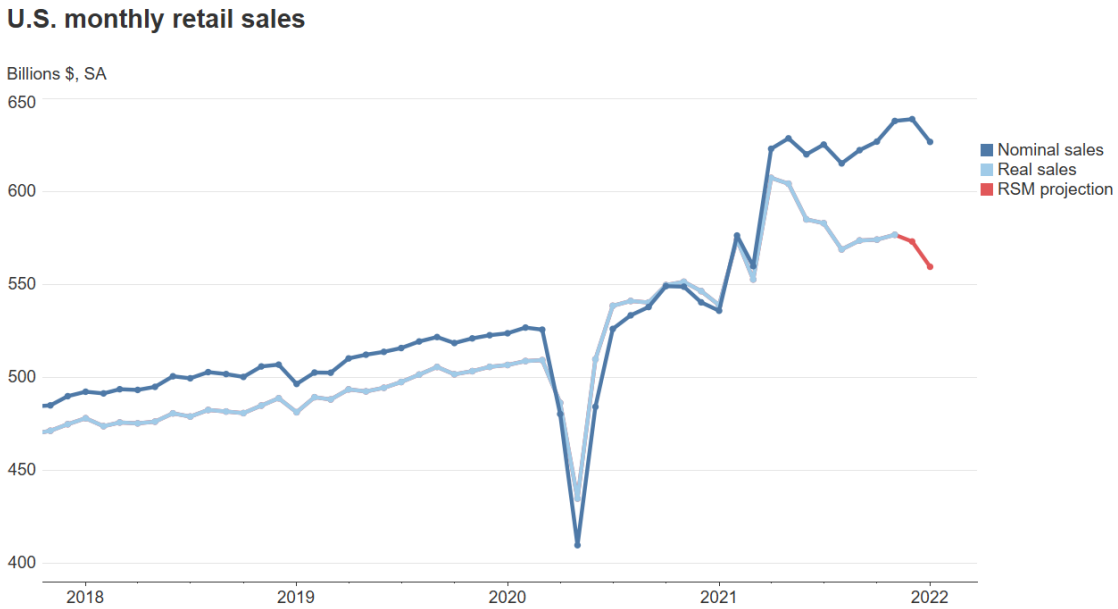
Figure 2: Total taxable sales (in millions) in Bloomington from 2008 to 2020 (source: Minnesota Department of Revenue)



Since tax proceeds are calculated as a percentage of total taxable sales subject to the sales tax, this increase during the past decade gives some sense of stability if a tax were enacted. Although the decrease between 2019 and 2020 was very significant, two national trends moderate any potential negative impacts of a LOST:

1. A large portion of consumer spending migrated from in-store sales to online sales during the pandemic. Any LOST would garner tax proceeds from online transactions whose nexus was in Bloomington. This includes any products delivered directly to Bloomington residents or customers who ordered online and picked up products at a Bloomington store.
2. Nationally the significant decreases in sale in 2020 were followed by significant increases in spending in 2021 (Figure 3). Extension does not have 2021 sales tax data to confirm that Bloomington followed this national trend.

Figure 3: Monthly Retail Sales, 2018-2022 (Source: RSM)

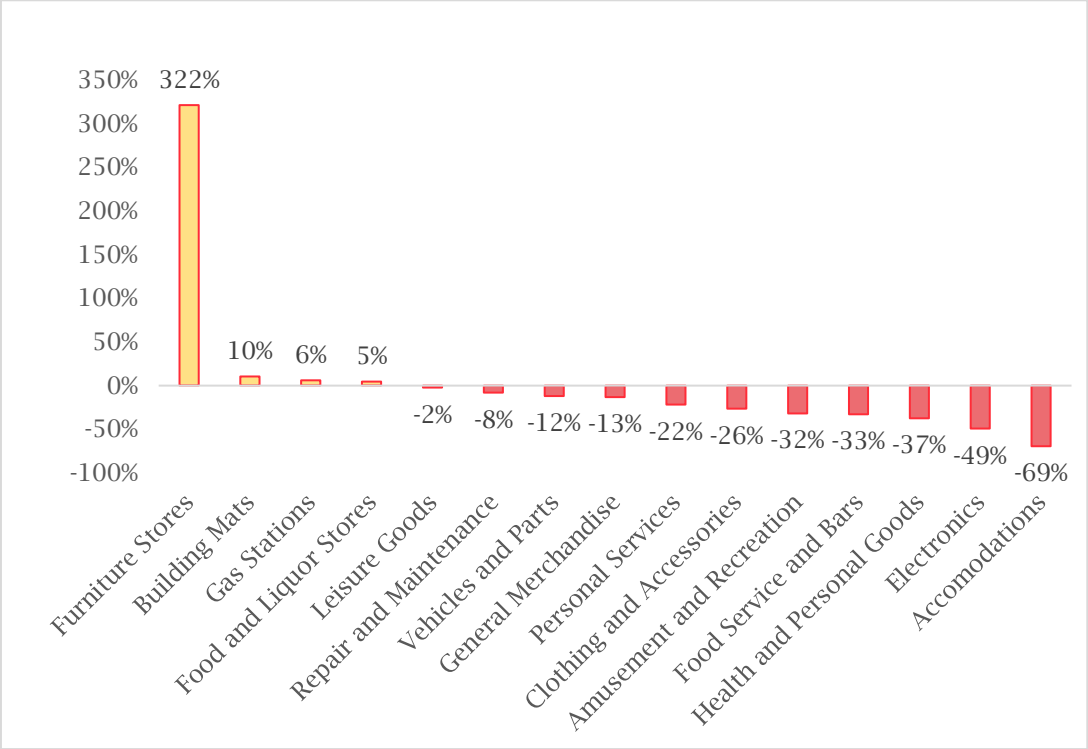


Between 2019 and 2020 taxable sales by category have shifted in some notable retail categories including very significant decreases in accommodations and food service as well as less severe decreases in electronics, general merchandise, and clothing. These losses were offset to a degree by a massive increase in the furniture category plus less dramatic but still significant increases in food, and building materials (Figures 4 and 5).

Figure 4: Taxable sales changes by category (in millions), 2019-2020

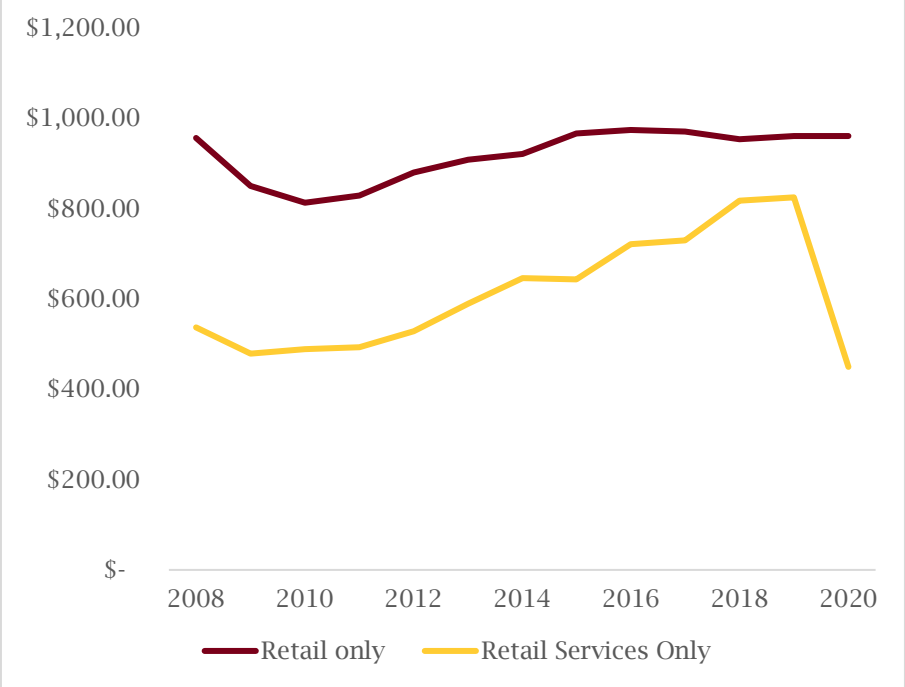
	2019 Taxable Sales	2020 Taxable Sales	Dollar Change	Percent Change
Vehicles and Parts	$149,187,347	$131,361,013	$(17,826,334)	-11.9%
Furniture	$33,832,079	$142,613,724	$108,781,645	321.5%
Electronics	$66,601,504	$33,843,362	$(32,758,142)	-49.2%
Building Mats.	$103,056,242	$113,771,349	$10,715,107	10.4%
Food and Liquor Stores	$111,958,570	$117,021,890	$5,063,320	4.5%
Health and Personal Goods	$57,012,512	$35,664,476	$(21,348,036)	-37.4%
Gas Stations	$25,451,703	$26,977,609	$1,525,906	6.0%
Clothing and Accessories	$76,351,468	$56,197,552	$(20,153,916)	-26.4%
Leisure Goods	$101,334,508	$99,080,350	$(2,254,158)	-2.2%
General Merchandise	$179,643,163	$155,973,504	$(23,669,659)	-13.2%
Misc. Store Retailers	$43,447,467	$39,109,398	$(4,338,069)	-10.0%
Amusement and Recreation	$27,193,590	$18,524,577	$(8,669,013)	-31.9%
Accommodations	$342,765,972	$104,722,830	$(238,043,142)	-69.4%
Food Service and Bars	$328,335,369	$220,494,656	$(107,840,713)	-32.8%
Repair and Maintenance	$48,048,141	$44,203,025	$(3,845,116)	-8.0%
Personal and Laundry Services	$78,922,520	$61,784,700	$(17,137,820)	-21.7%

Figure 5: Taxable sales changes by category in Bloomington (in millions), 2019-2020



Generally these categories shifts follow the national trends, where retail goods categories held or increased, whereas the retail service industries saw significant declines (Figure 6):

Figure 6: Retail Goods vs. Retail Services by Year in Bloomington

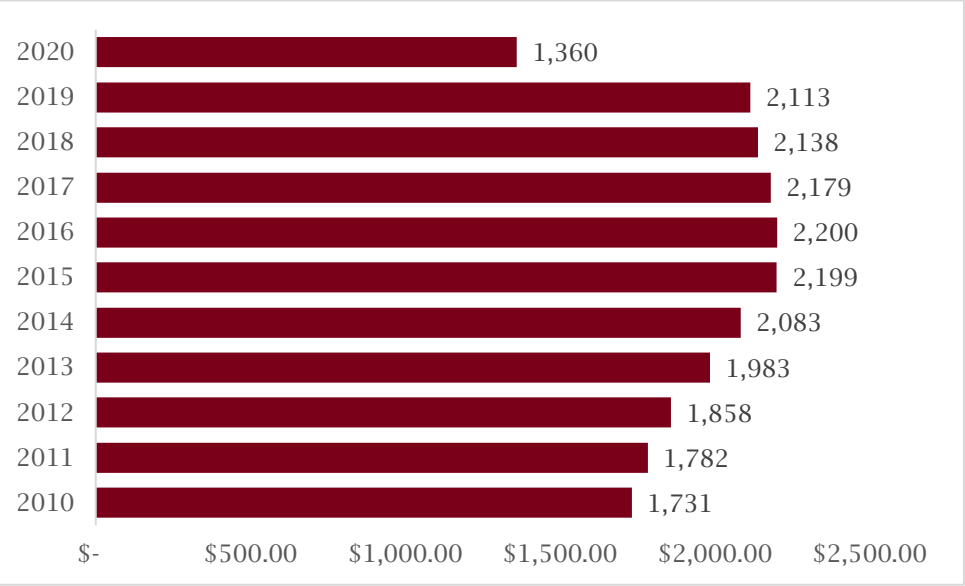


These shifts impacted Extension estimates of non-resident proportion of spending. For example, accommodations sales are driven more by non-resident spending than any other category and a serious decrease in sales in the accommodations category would tilt the mix of sales towards resident spending overall.

Local Option Sales Tax Estimates and Trends

Not all taxable sales are subject to a local option sales tax. A city such as Bloomington with many types and sizes of businesses will have business taxpayers with transactions that range across jurisdictions and complex operations. Extension consulted the MN Department of Revenue research division and their analysts estimated the percent of the total taxable sales subject to a local tax at 68.3% after looking at the firm-level sources of taxable sales in the state sales tax database. Extension used this proportion as a constant to estimate the total sales subject to a local option sales tax (Figure 7).

Figure 7: Estimated taxable sales subject to location option sales tax (not adjusted for inflation)



Extension forecasted taxable sales subject to the local tax for 2021, 2022, and 2023 using a simple exponential smoothing forecast model that employs a moving weighted average and a 95% confidence interval to provide an upper and lower bound to the estimate (Figures 8 and 9). Considering the historic disruption of the pandemic, the range of future tax proceeds is wide, a greater range than calculated in the 2021 report examining LOST trends since the trend of taxable sales for a decade previous the pandemic consisted of gradual increases and decreases.

Figure 8: Sales forecast of taxable sales subject to local option sales tax

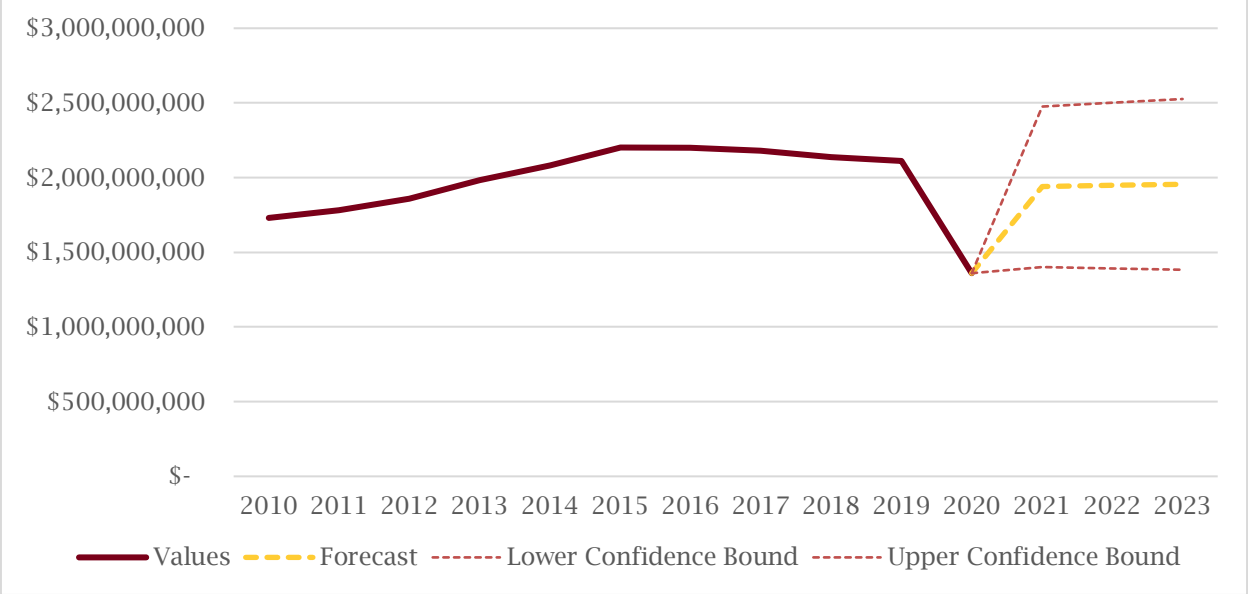


Figure 9: Forecast of taxable sales subject to tax with upper and lower bound at 95% confidence interval

	Forecast	Lower bound	Upper bound
2021	$1,939,368,482	$1,401,310,668	$2,477,426,296
2022	$1,947,305,070	$1,392,557,026	$2,502,053,114
2023	$1,955,241,658	$1,384,163,560	$2,526,319,757

Tax proceeds estimates

Extension estimated the dollars generated by a local option sales tax historically and using its forecast of taxable sales subject to the tax. Bloomington would have realized as much as $11,000,000 and $6,800,000 in sales tax proceeds in 2016 and 2020 respectively if a half percent tax were in effect at that time. Because the 2020 estimate is based only on the taxable sales published for Bloomington-based business alone, this is a lower than expected tax proceed estimate in light of the shift to consumer online purchases during 2020, which are not included. Any online sales picked up at Bloomington-based stores would be included, yet online purchases by Bloomington residents are not. Looking forward, a local option sales tax may garner up to $12,632,000 in 2023 according to forecast (Figure 10).

Figure 10: Estimated tax proceeds for 0.5% local option sales tax, 2011 - 2023

2011	$8,911,509
2012	$9,287,969
2013	$9,916,634
2014	$10,413,311
2015	$10,997,290

2016	$11,000,000
2017	$10,895,288
2018	$10,689,139
2019	$10,566,489
2020	$6,800,192
2021*	$7,006,553-$12,387,131
2022*	$6,962,785 - $12,510,266
2023*	$6,920,818-$12,631,599

*Range uses upper and lower bound of taxable sales forecast (Figure 7)

Proceeds from *use* taxes would also be added to the estimated tax proceeds from a local option sales tax. Use taxes derive from city businesses purchasing products from out-of-state sources and in other Minnesota locations, which are often less consistent and more difficult to accurately estimate than sales taxes. Based on 2020 figures, city officials can expect an estimated additional $65,000 in use (not sales) tax proceeds with a half-percent enacted tax.

Non-resident estimates

Extension calculated the proportion of non-resident spending in Bloomington using the same method of comparing actual to potential as done in the first LOST analysis using 2016 data. In this analysis, Extension sets non-resident portion of spending in relation to the capture of Bloomington resident spending. For example, furniture stores in Bloomington report $111 million more in taxable sales than the potential sales calculation. Clearly there's a surplus. If only $111 million or 78% of sales in the category were attributed to non-residents, 100% of Bloomington resident spending in this category would stay in Bloomington. Since this is unrealistic in a competitive metro market, Extension adjusted the non-resident spending up to 85%, which brought the Bloomington resident capture rate to a more reasonable 68% of their spending. Again, in a competitive metro market, a 68% capture rate is still conservative as Bloomington residents can easily reach and shop at other furniture stores.

Working through the business categories in this way, this analysis provided a range of non-resident spending overall between 74.8% using 2016 data and 59.7% using 2020 data (Figure 11).

Taxable sales and businesses in the "other" category were left out due to the complexity of individual firms and their associated tax burden to make for a more conservative estimate of non-resident spending. For example, a very large portion of taxable sales in 'other' were in the telecommunications and management of companies subcategories. Moreover, the telecommunications category had a massive decrease in taxable sales between 2019 and 2020 of over $600 million. These unexplained swings in sales and difficulty knowing the nexus of their sales or whether those sales would be subject to the local option sales tax, give reason to keep them out of the analysis. For transparency, see Appendix 1.

Figure 11: 2020 non-resident spending estimates using two methods and number of firms by category

	Non-Resident estimate sales % 2016	Non-Resident estimate sales % 2020	2020 Taxable Sales (in millions)	# firms 2016	# firms 2020

Total	74.8%	60.4%	$1,990.48	2,869	2,656
Vehicles & Parts	75%	64%	$131.36	44	37
Furniture Stores	65%	85%	$142.61	30	24
Electronics	75%	35%	$33.84	43	47
Building Materials	27%	10%	$113.77	25	23
Food, Groceries	56%	40%	$117.02	65	55
Health, Personal Stores	84%	75%	$35.66	63	54
Gas/Convenience Stores	42%	10%	$26.98	25	28
Clothing	87%	82%	$56.20	191	184
Leisure Goods	82%	83%	$99.08	72	66
General Merchandise Stores	63%	44%	$155.97	24	19
Miscellaneous Retail	65%	39%	$39.11	160	128
Amusement & Recreation	75%	15%	$18.52	26	25
Accommodations	98%	97%	$104.72	48	46
Eating & Drinking Places	73%	58%	$220.49	254	237
Repair, Maintenance	55%	45%	$44.20	99	104
Personal Services, Laundry	62%	82%	$61.78	114	113
Construction, Manu, Wholesale	82%	67%	$392.30	422	403
Other (services, healthcare)	NA	NA	$196.83	1,144	1,063

Appendix 1: 'Other' category taxable sales – non-store retail and other services (North American Industrial Classification System 511-813 Sales Amounts Released by MN Revenue)

	($Millions)
2020 Actual taxable sales	$196.83
% of total taxable retail and service sales	12.3%

Analysis and Recommendations for Retail and Other Services

This group includes healthcare, telecommunications, waste management, rental/lease services, administrative support, and the performing arts. This mix of business types is too diverse and complex in term of their reach and sales tax burden to include in the trade area analysis and use in calculations for a local option sales tax.

Category	2016 Taxable Sales	2020 Taxable Sales
454 RETL -NONSTORE RETAILERS	$18,931,796	$10,136,578
484 TRANSPORTATION -TRUCK	$383	$0
488 TRANSPORTATION -SUPPORT	$41,377	$101,475
492 TRANSPORTATION -COURIERS	$218,773	
493 TRANSPORTATION -STORAGE	$23,031	$41,372
511 INFO -PUBLISHING INDUSTRY	$893,335	$1,956,751
512 INFO -MOVIES, MUSIC IND	$6,344,140	$1,537,488
517 INFO -TELECOMMUNICATIONS	$734,738,005	$12,718,517
518 INFO -INTERNET SERVICE	$34,280,570	$29,209,203
519 INFO -OTHER SERVICES	$3,474,455	$1,492,936
522 CREDIT INTERMEDIATION	$4,987,093	$6,063,314
523 SECURITIES, COMMODITIES	$266,564	$1,694,143
524 INSURANCE CARRIERS	$67,225	$11,266
531 REAL ESTATE	$41,393,468	$12,983,537
532 RENTAL, LEASING SERVICES	$42,289,408	$25,502,682
533 LESSORS NONFINAN ASSETS		$70,299
541 PROF, SCIENTIFIC,TECH SERV	$43,009,980	$40,258,532
551 MGMT OF COMPANIES	$124,130,869	$1,551,815
561 ADMIN, SUPPORT SERVICES	$71,969,069	$37,401,123
562 WASTE MGMT, REMEDIATION	$6,532,296	
611 EDUCATIONAL SERVICES	$3,317,746	$2,106,857
621 HEALTH -AMBULATORY CARE	$5,531,992	$4,707,931
623 HEALTH -NURSING,HOME CARE	$653,049	$466,419
624 HEALTH -SOCIAL ASSISTANCE	$176,282	$67,468
711 PERF ART, SPECTATOR SPRTS	$1,837,695	$334,406

Appendix 2: Calculation of Construction, Manufacturing, Wholesale Operations, Transportation, and Sales Information Suppressed for Business Confidentiality

A diverse mix of businesses fall into these non-retail categories and a portion of sales are within a suppressed or non-disclosed subcategory. This diversity makes it difficult to understand the customer mix of these businesses, however Extension broke out each known subcategory and assigned assumptions according to their business type:

Subcategory	2020 Taxable Sales	Non-local estimate
Construction	$19,341,700	60%
Manufacturing	$90,852,050	90%
Transportation	$142,847	60%
Wholesale	$272,591,775	70%
Undesignated	$9,371,660	50%
Total	$392,300,032	67%

The above industries and services generate $392 million in taxable sales, a measurable portion of total taxable sales in Bloomington (24.5%). A significant portion of this amount will be subject to any new sales taxes, including a local option sales tax.

Extension estimated that overall 67 percent of sales are to non-residents. Extension assumed that some subcategories such as manufacturing sell primarily (90%) to non-resident customers, whereas subcategories like undesignated and construction split their sales between resident and non-resident customers.

	($Millions)
Residents' $ share	$129.46
Non-residents $ share	$262.85
Total	$392.31
Non-resident share	67%

APPENDIX 3: DEFINITIONS OF TERMS

Gross Sales
Gross sales include taxable sales and exempt businesses with sales and use tax permits. This is the most inclusive indicator of business activity for the reporting jurisdictions, but it can be misleading when used in comparisons. At times, non-taxable commodity items (e.g., gasoline) can have large price variations, creating huge swings in gross sales.

Taxable Sales
Taxable sales are those sales subject to sales tax. Taxable sales exclude exempt items, items sold for resale, items sold for exempt purposes, and items sold to exempt organizations. For the purpose of this study, taxable sales were the focus of the analysis. For more information on what is taxed in Minnesota, see the "Minnesota Sales and Use Tax Instruction Booklet" available at http://www.revenue.state.mn.us/Forms_and_Instructions/sales_tax_booklet.pdf

Taxable Retail and Service Sales
In this study and other retail trade analyses conducted by University of Minnesota Extension, the term “taxable retail and service sales” refers to the North American Industry Classification System (NAICS) numbers of 441 to 454 (retail) and 511 to 812 (most service industries) released by the Minnesota Department of Revenue for a geographic area.

Current and Constant Dollar Sales
Current dollar (or “nominal dollar”) sales are those reported by the state. No adjustment has been made for price inflation. In general, this measure of sales is not satisfactory for comparisons over long periods of time since it does not account for changes in population, inflation, or the state's economy. Constant dollar (or “real dollar”) sales reflect changes in price inflation by adjusting current dollar sales according to the Consumer Price Index (CPI). Constant dollar sales indicate the real sales level with respect to a base year. This is a more realistic method of evaluating sales over time than current dollar comparisons, but it still does not take into consideration changes in population or the state’s economy.

Number of Businesses
The number of sales and use tax permit holders who filed one or more tax returns for the year.

Index of Income
This index provides a relative measure of income, calculated by dividing local per capita income by state per capita income. The base is 1.00. For example, a 1.20 index of income indicates that per capita income in the area is 20 percent above the state average.

Potential Sales
Potential sales are an estimate of the amount of money spent on retail goods and services by residents of a county. It is the product of county population, state per capita sales, and the index of income. Potential sales for counties is similar to expected sales for cities. Potential sales, however, do not utilize a measure of average pulling power (like the typical pull factor used in the expected sales equation). Since a county is a relatively large region where retail business takes place, counties are compared without adjustments for trade area size.

Actual Sales
For this study, the Minnesota Department of Revenue’s 2016 - 2020 sales data for City of Bloomington provides the actual sales numbers used.

Variance between Actual and Potential Sales

The variance between actual and expected sales is the difference in sales from the "norm" (i.e., the amount above or below the standard established by the expected sales formula). When actual sales exceed expected sales, the county has a "surplus" of retail sales. When actual sales fall short of expected sales, the county has a retail sales "leakage." Discrepancies between expected and actual sales occur for a variety of reasons. For this study, we use potential sales per merchandise group to create a first-cut estimate of residents' purchase activities.

Cautions

Gross Sales

Gross sales are a comprehensive measure of business activity, but it should be noted the numbers in this report are self-reported. Furthermore, gross sales are not audited by the State of Minnesota. It is believed gross sales figures are generally reliable, but there is the possibility of distortions, especially in smaller cities where misreporting may have occurred.

Misclassification

Holders of sales and use tax permits select the North American Industry Classification System (NAICS) category that best fits their business. Regardless of who makes this classification, errors are occasionally made. Also, sometimes a business will start out as one type but evolve over time to a considerably different type. Misclassifications can distort sales among business categories, especially in smaller cities. For example, a furniture store that is classified as a general merchandise store will under-report sales in the furniture store category and over-report sales in the general merchandise category.

Suppressed Data

The sales data for merchandise categories that have less than four reporting firms are not reported. This is a measure taken by most states to protect the confidentiality of sales tax permit holders. Sales for suppressed retail categories are placed into the miscellaneous retail category (NAICS 999) and included in total sales but not total sales of a typical retail trade analysis. For this report, however, all taxable sales—including NAICS 999—are part of calculating the amount of special taxes collected.

Consolidated Reporting

Vendors with more than one location in Minnesota have the option of filing a separate return for each location or filing one consolidated return for all locations. The consolidated return shows sales made, tax due, and location by city and county for each business. Data for consolidated filers are combined with data for single-location filers to produce the figures in this report. Occasionally, consolidated reports may not be properly deconstructed, and all sales for a company may be reported for one town or city. Whenever misreporting is discovered, the Minnesota Department of Revenue is contacted to clarify the situation.