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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 2016-2019

Authored by Ryan Pesch



PROGRAM SPONSORS: CITY OF BLOOMINGTON, MINNESOTA

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EXECUTIVE SUMMARY

After an analysis of a Local Option Sales Tax potential in 2019 based on 2016 sales tax statistics, University of Minnesota Extension recently took a second look using 2017, 2018, and 2019 data.

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 two ways:

- (1) using the same proportions of non-resident spending for each category as estimated using 2016 data
- (2) adjusting proportions of non-resident spending using 2019 data based on shifts in taxable sales by category

Calculated in these two ways, Extension estimated that **non-residents comprised between 74.4% and 75.0% of 2019 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 uses only the estimate of retail and service categories plus more easily estimated non-service categories. This conservative estimate of non-resident spending was calculated using the same categories with 2019 data as the 2016 data from the original report.

Total taxable sales were \$3.2 billion in 2016 and dropped slightly to \$3.1 billion in 2019. 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 \$2.1 billion of would have been subject to a LOST in 2016 and 2019 respectively. **If a local option sales tax were in effect, the city would have generated \$11 million in 2016 and \$10.6 million in 2019**, the strong majority of which would have been garnered from non-residents. Tax proceeds could increase over \$12 million by 2022 if taxable sales follow past trends, however a historic shakeup in spending due to the pandemic leave forecasts uncertain.

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 data¹ 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.

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.
- 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 37,000 according to Census figures) and the close proximity of competing shopping areas (Figure 1). The proportion of residents leaving Bloomington for work increased between 2016 and 2018 (most recent published data).

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:

$$(T \div PMn) \times PB \times (YHC \div YMn) = \text{Potential Sales}$$

T = Total Minnesota taxable sales for a merchandise category

PMn = 2016 Population of Minnesota (5,528,630)

PB = 2016 Population of Bloomington (88,299)

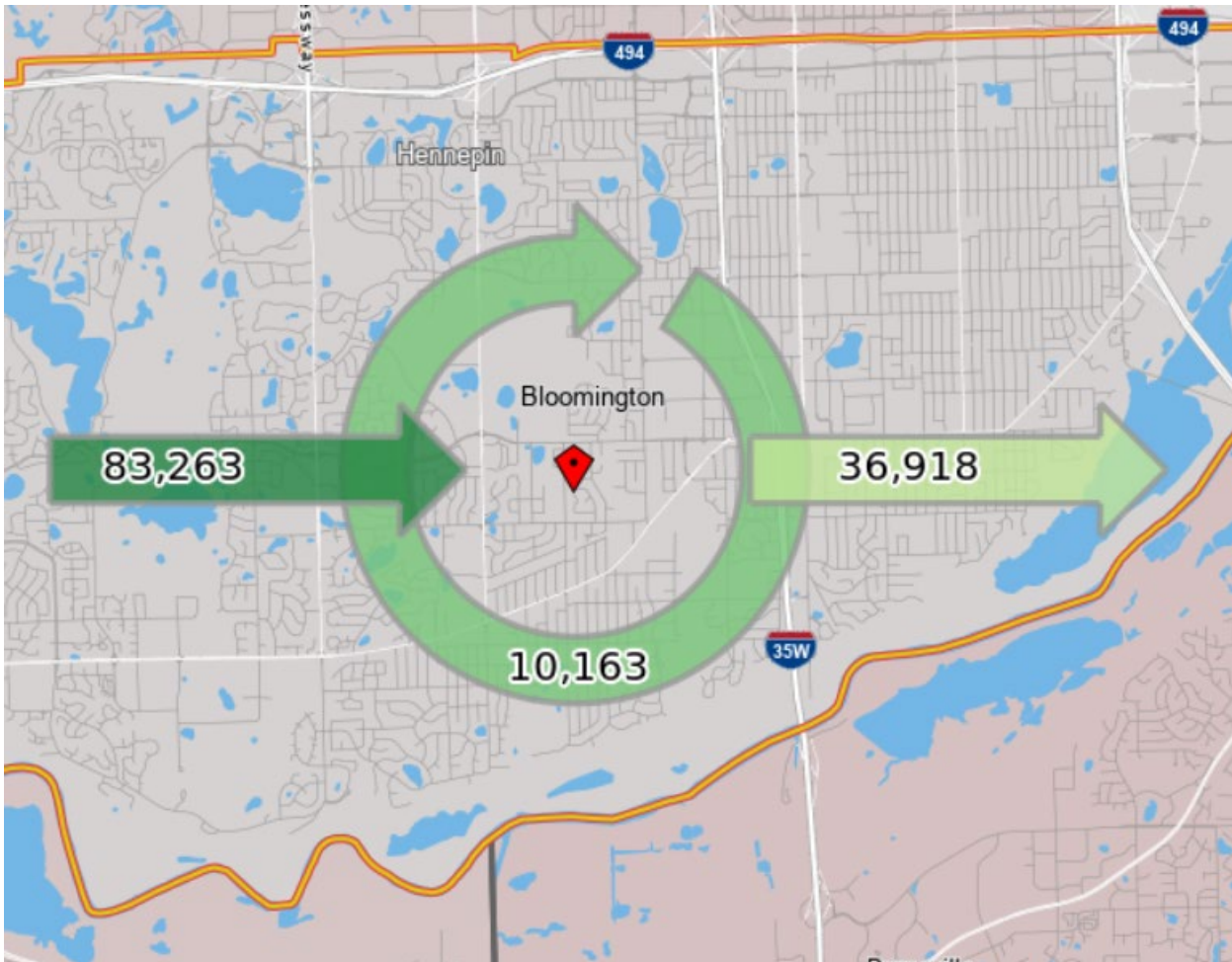
YHC = Per capita income of Hennepin County resident (\$68,022)

YMn = Per capita income of Minnesota resident (\$51,957)

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: 2016 U.S. Census Bureau OnTheMap application, Longitudinal-Employer Household Dynamics Program, <http://onthemap.ces.census.gov/>)



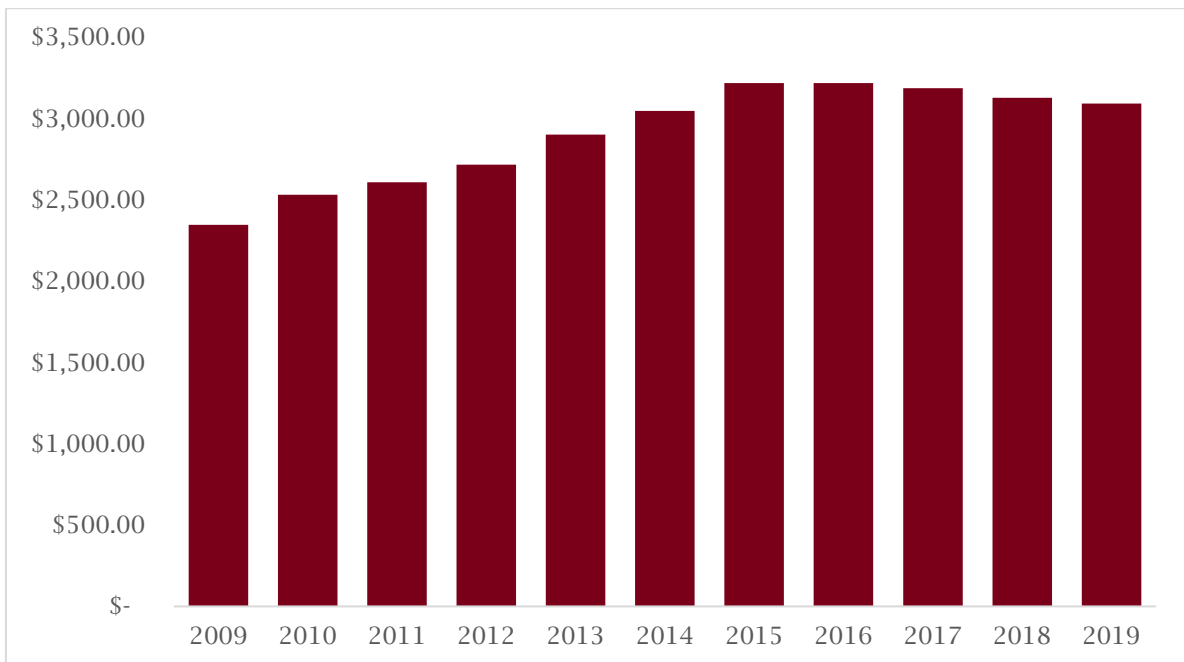
Taxable Sales Trends

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

Total taxable sales in the city have increased 31.7 percent from 2009 to 2019 from \$2.3 billion to \$3.1 billion, yet have decreased 3.9% from their high in 2016. After adjusting for inflation, Bloomington's taxable sales increased 10.6% since 2009.

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.

Figure 2: Total taxable sales (in millions) in Bloomington from 2009 to 2019 (source: Minnesota Department of Revenue)



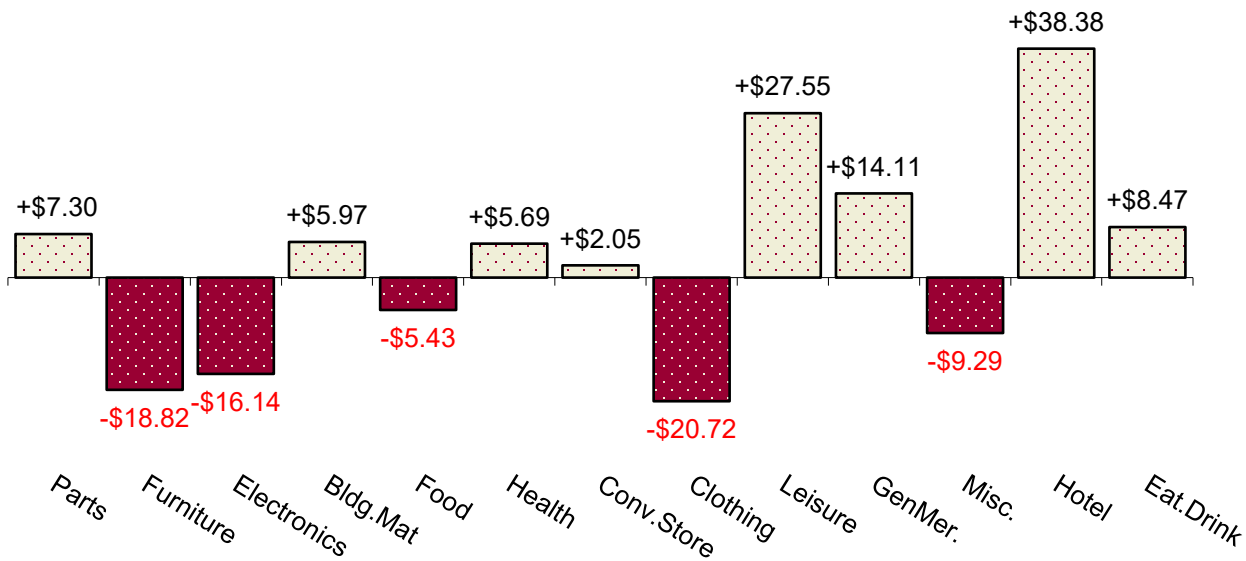
Since 2016 taxable sales by category have shifted in some notable retail categories including a marked decrease in furniture, clothing, and electronics. These losses were offset to a degree by increases leisure goods, health stores, and accommodations (Figures 3 and 4). These shifts impacted Extension estimates of non-resident proportion of spending. For example, accommodations sales are driven more by non-resident spending than any other category and an increase in sales in the accommodations category would tilt the mix of sales towards non-resident spending overall.

Figure 3: Taxable sales changes by category (in millions), 2016-2019

| Selected Categories | Taxable Sales 2016 | Taxable Sales 2019 | Dollar Change | Percent Change |
|----------------------------------------|------------------------|------------------------|-----------------------|----------------|
| Vehicles & Parts | \$141,891,038 | \$149,187,347 | +\$7,296,309 | +5.14% |
| Furniture | \$52,647,749 | \$33,832,079 | -\$18,815,670 | -35.74% |
| Electronics | \$82,745,148 | \$66,601,504 | -\$16,143,644 | -19.51% |
| Building Materials | \$97,084,402 | \$103,056,242 | +\$5,971,840 | +6.15% |
| Food, Groceries | \$117,387,624 | \$111,958,570 | -\$5,429,054 | -4.62% |
| Health, Personal Stores | \$51,323,010 | \$57,012,512 | +\$5,689,502 | +11.09% |
| Gas/Convenience Stores | \$23,398,759 | \$25,451,703 | +\$2,052,944 | +8.77% |
| Clothing | \$97,075,726 | \$76,351,468 | -\$20,724,258 | -21.35% |
| Leisure Goods | \$73,779,679 | \$101,334,508 | +\$27,554,829 | +37.35% |
| General Merchandise Stores | \$165,534,692 | \$179,643,163 | +\$14,108,471 | +8.52% |
| Miscellaneous Retail | \$52,739,816 | \$43,447,467 | -\$9,292,349 | -17.62% |
| Accommodations | \$304,390,653 | \$342,765,972 | +\$38,375,319 | +12.61% |
| Eating & Drinking | \$319,867,700 | \$328,335,369 | +\$8,467,669 | +2.65% |
| Total Retail and Services Sales | \$2,825,688,643 | \$2,661,831,906 | -\$163,856,737 | -5.80% |

* Figures not adjusted for inflation.

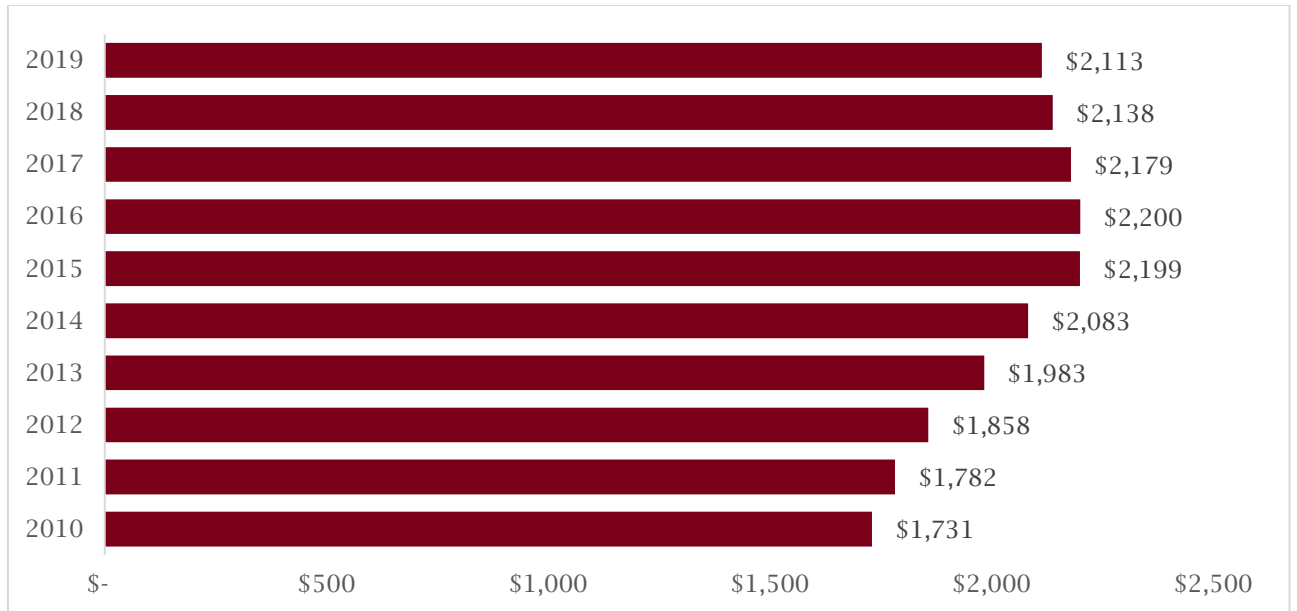
Figure 4: Taxable sales changes by category (in millions), 2016-2019



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 5).

Figure 5: Estimated taxable sales subject to location option sales tax (not adjusted for inflation)



Extension forecasted taxable sales subject to the local tax for 2020, 2021, and 2022 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 6 and 7). Considering the historic disruption of the pandemic and its uneven effect on business categories, this forecast is an unlikely scenario based only on past trends. National evidence shows that home-focused businesses like food, building materials, general merchandise, and furniture did well through the pandemic, whereas dining, accommodations, and personal services saw record sales decreases. Looking at Bloomington’s business mix, its concentration in accommodations and dining more than likely outweighed any positive changes. Moreover, the sharp rebound in sales in 2021 further complicates any forecast.

Figure 6: Sales forecast of taxable sales subject to local option sales tax

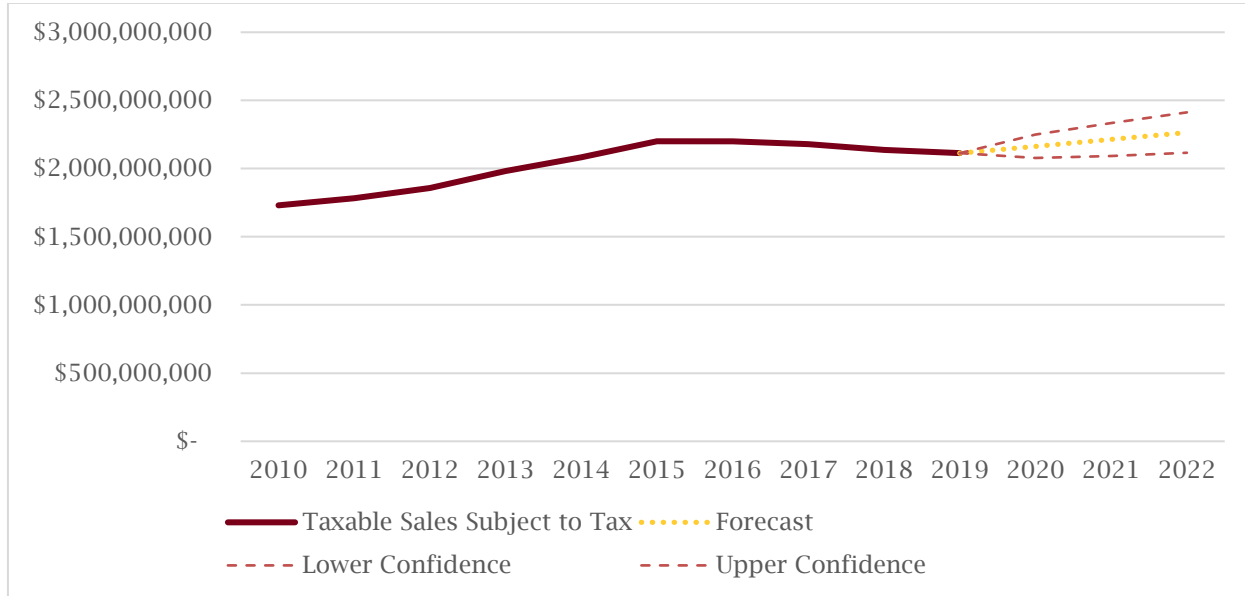


Figure 7: Forecast of taxable sales subject to tax with upper and lower bound at 95% confidence interval

| | Forecast | Lower bound | Upper bound |
|------|------------------|------------------|------------------|
| 2020 | \$ 2,163,641,425 | \$ 2,078,101,794 | \$ 2,249,181,056 |
| 2021 | \$ 2,213,984,977 | \$ 2,093,074,141 | \$ 2,334,895,813 |
| 2022 | \$ 2,264,328,530 | \$ 2,116,218,913 | \$ 2,412,438,147 |

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 \$10,566,000 in sales tax proceeds in 2016 and 2019 respectively if a half percent tax were in effect at that time. Looking forward, a local option sales tax may garner up to \$12,062,000 in 2022 according to forecast (Figure 8).

Figure 8: Estimated tax proceeds for 0.5% local option sales tax, 2010 - 2022

| | |
|------|--------------|
| 2010 | \$8,653,228 |
| 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* | \$10,391,000 - \$11,246,000 |
| 2021* | \$10,465,000 - \$11,674,000 |
| 2022* | \$10,581,000 - \$12,062,000 |

*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 2019 figures, city officials can expect an estimated additional \$835,000 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 in two ways to measure the impacts of changes in performance by business category between 2016 and 2019. This provided a range of non-resident spending overall between 74.4% and 75.0% using 2019 data.

Extension used the same proportions of non-resident spending for each category as estimated in 2019 report as one method (see Non-Resident % 2016 in Figure 9). This calculation allows for an apples-to-apples comparison with previous estimates to highlight how sales shifts alone would impact the proportion of non-resident spending overall. In essence, the assumption of how spending is split between residents and non-residents by category is held constant. Calculating the overall non-resident spending estimate in this way resulted in 74.8% of taxable sales coming from non-residents.

In reality, however, resident and non-resident spending patterns shift over time. Looking at the “On the Map” data about commuting patterns (Figure 1), a greater proportion of residents are working outside the community in 2019 than in 2016. This alone would reasonably shift more resident spending outside of Bloomington, if only for convenience goods near a place of work. In light of the increases and decreases in taxable sales between 2016 and 2019 (Figures 3 and 4), Extension adjusted the proportions of non-resident spending for each category (see Non-Resident % Adjusted in Figure 9). Calculating the overall non-resident spending estimate in this way resulted in 75.3% of taxable sales coming from non-residents.

In both methods, 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. It is difficult to know the nexus of their sales and whether those transactions would be subject to a local option sales tax. For transparency, see Appendix 1.

Figure 9: 2019 non-resident spending estimates using two methods and number of firms by category

| | 2019 Taxable Sales (in millions) | Non-Resident % 2016 | Non-Resident % adjusted | # firms 2016 | # firms 2019 |
|-------------------------------|-----------------------------------------|----------------------------|--------------------------------|---------------------|---------------------|
| Total | \$3,092.91 | 74.8% | 75.3% | 2,869 | 2,797 |
| Vehicles & Parts | \$149.19 | 75% | 75% | 44 | 46 |
| Furniture Stores | \$33.83 | 65% | 60% | 30 | 28 |
| Electronics | \$66.60 | 75% | 72% | 43 | 44 |
| Building Materials | \$103.06 | 27% | 28% | 25 | 27 |
| Food, Groceries | \$111.96 | 56% | 56% | 65 | 69 |
| Health, Personal Stores | \$57.01 | 84% | 85% | 63 | 57 |
| Gas/Convenience Stores | \$25.45 | 42% | 42% | 25 | 28 |
| Clothing | \$76.35 | 87% | 87% | 191 | 211 |
| Leisure Goods | \$101.33 | 82% | 84% | 72 | 76 |
| General Merchandise Stores | \$179.64 | 63% | 63% | 24 | 29 |
| Miscellaneous Retail | \$43.45 | 65% | 65% | 160 | 165 |
| Amusement & Recreation | \$27.19 | 75% | 70% | 26 | 23 |
| Accommodations | \$342.77 | 98% | 98% | 48 | 45 |
| Eating & Drinking Places | \$328.34 | 73% | 73% | 254 | 234 |
| Repair, Maintenance | \$48.05 | 55% | 55% | 99 | 100 |
| Personal Services, Laundry | \$78.92 | 62% | 79% | 114 | 121 |
| Construction, Manu, Wholesale | \$431.07 | 82% | 82% | 422 | 366 |
| Other (services, healthcare) | \$888.69 | NA | NA | 1,144 | 1,128 |

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) |
| 2019 Actual taxable sales | \$888.69 |
| % of total taxable retail and service sales | 33.4% |

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 | 2019 Taxable Sales |
|-------------------------------|--------------------|--------------------|
| 454 RETL -NONSTORE RETAILERS | \$18,931,796 | \$13,925,256 |
| 484 TRANSPORTATION -TRUCK | \$383 | \$0 |
| 488 TRANSPORTATION -SUPPORT | \$41,377 | \$210,389 |
| 492 TRANSPORTATION -COURIERS | \$218,773 | \$211,355 |
| 493 TRANSPORTATION -STORAGE | \$23,031 | \$26,761 |
| 511 INFO -PUBLISHING INDUSTRY | \$893,335 | \$2,787,781 |
| 512 INFO -MOVIES, MUSIC IND | \$6,344,140 | \$6,792,264 |
| 517 INFO -TELECOMMUNICATIONS | \$734,738,005 | \$624,231,504 |
| 518 INFO -INTERNET SERVICE | \$34,280,570 | \$35,615,922 |
| 519 INFO -OTHER SERVICES | \$3,474,455 | \$1,956,705 |
| 522 CREDIT INTERMEDIATION | \$4,987,093 | \$4,645,674 |
| 523 SECURITIES, COMMODITIES | \$266,564 | \$804,591 |
| 524 INSURANCE CARRIERS | \$67,225 | \$45,274 |
| 531 REAL ESTATE | \$41,393,468 | \$43,995,900 |
| 532 RENTAL, LEASING SERVICES | \$42,289,408 | \$40,165,339 |
| 533 LESSORS NONFINAN ASSETS | | \$75,108 |
| 541 PROF,SCIENTIFIC,TECH SERV | \$43,009,980 | \$45,079,950 |
| 551 MGMT OF COMPANIES | \$124,130,869 | \$1,063,680 |
| 561 ADMIN, SUPPORT SERVICES | \$71,969,069 | \$44,727,948 |
| 562 WASTE MGMT, REMEDIATION | \$6,532,296 | \$6,607,464 |
| 611 EDUCATIONAL SERVICES | \$3,317,746 | \$3,312,215 |
| 621 HEALTH -AMBULATORY CARE | \$5,531,992 | \$4,888,140 |
| 623 HEALTH -NURSING,HOME CARE | \$653,049 | \$567,973 |
| 624 HEALTH -SOCIAL ASSISTANCE | \$176,282 | \$138,688 |
| 711 PERF ART, SPECTATOR SPRTS | \$1,837,695 | \$1,429,523 |

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

The above industries and services generate \$431 million in taxable sales, a measurable portion of total taxable sales in Bloomington (16.2%). A significant portion of this amount will be subject to any new sales taxes, including a local option sales tax.

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 | 2019 Taxable Sales | Non-local estimate |
|--------------------|---------------------------|---------------------------|
| Construction | \$33,801,147 | 60% |
| Manufacturing | \$119,442,426 | 90% |
| Transportation | \$448,505 | 90% |
| Wholesale | \$264,225,926 | 80% |
| Undesignated | \$13,155,350 | 50% |
| Total | \$431,073,354 | 80% |

Extension estimated that overall 82 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. Extension assumed that 90% of taxable sales in transportation were to non-residents.

| | (\$Millions) |
|------------------------|--------------|
| Residents' \$ share | \$77.59 |
| Non-residents \$ share | \$353.48 |
| Total | \$431.07 |
| Non-resident share | 80% |

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 - 2019 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.