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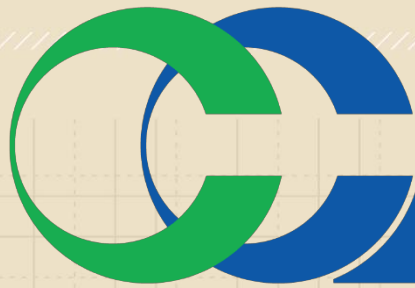


EXTENSION CENTER FOR COMMUNITY VITALITY

Local Option Sales Tax Analysis for Cottage Grove, MN

ESTIMATED CONTRIBUTIONS OF RESIDENTS AND NON-RESIDENTS TO A LOCAL OPTION SALES TAX

Authored by Eric King



Cottage
Grove

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REPORT SPONSOR: CITY OF COTTAGE GROVE, MINNESOTA

Local Option Sales Tax Analysis for Cottage Grove

ESTIMATED CONTRIBUTIONS OF RESIDENTS AND NON-RESIDENTS TO A LOCAL OPTION SALES TAX

March 2023

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City of Cottage Grove

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SUMMARY OF FINDINGS

University of Minnesota Extension conducted a study to estimate the proportion of sales proceeds attributed to both Cottage Grove residents and non-residents.

Using 2020 sales and use tax data available from the Minnesota Department of Revenue (MN Revenue), Extension estimated that non-residents account for 31.3 percent of taxable sales subject to a local option sales tax (LOST).

In 2020, total taxable sales in Cottage Grove were \$266 million. MN Revenue analysts estimate that approximately 98% of those sales would be subject to a LOST. With 31.3 percent of sales derived from non-resident spending, Extension estimated that Cottage Grove residents spent \$178 million of the total \$260 million in taxable sales subject to a LOST.

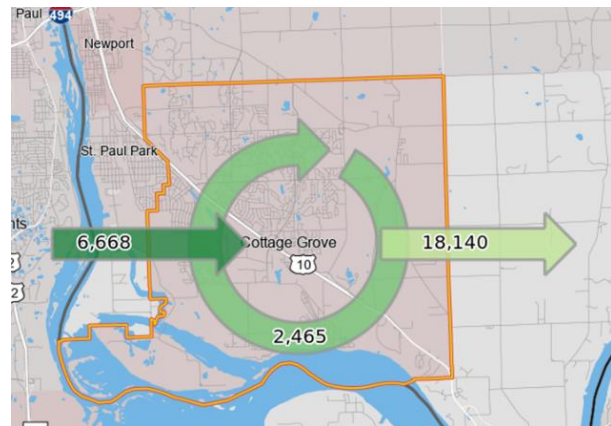
If the tax were in place in 2020, a 0.5 percent local option sales tax would have garnered \$1.3 million in tax proceeds according to MN Department of Revenue analysts. Cottage Grove residents would have contributed \$893,100 thousand in taxes, and non-residents would have contributed \$406,900 thousand. Based on these estimates, each Cottage Grove resident would have paid, on average, an additional \$22.99 in sales tax in 2020.

This report is based on a trade area analysis comparing actual taxable sales to potential sales. This is calculated by multiplying the Cottage Grove population in 2020 (MN Demographic Center) by the Minnesota average per capita sales for each category, and then adjusting for the county's personal income factor. This initial analysis provided an estimate of retail and service purchases made by Cottage Grove residents. For each merchandise group, the estimates for two types of purchasers—city residents and others—were calculated and adjusted considering the area economy. These adjustments were based on informed estimates and were aimed, in part, at reducing potential overestimates of the sales tax share attributable to non-residents. Assumptions and calculations are included for major retail and service categories so local decision makers can adjust totals if they have more nuanced insight.

Several factors and features of Cottage Grove's economy helped frame the analysis for the different merchandise categories:

- As a metro community with many nearby competing shopping centers, cross-hauling is a significant factor. Cottage Grove residents can easily shop outside of the community and residents of nearby communities can also easily access Cottage Grove businesses. For this analysis, cross-hauling has the net effect of increasing non-resident spending.
- Cottage Grove has less workers entering the city for employment than residents who leave for work (Figure 1). In this dynamic, commuters often shop for goods and services near where they work and those commuting into the city purchase in the city.

Figure 1: Cottage Grove worker in-flow and out-flow



Inflow and outflow of wage earners.

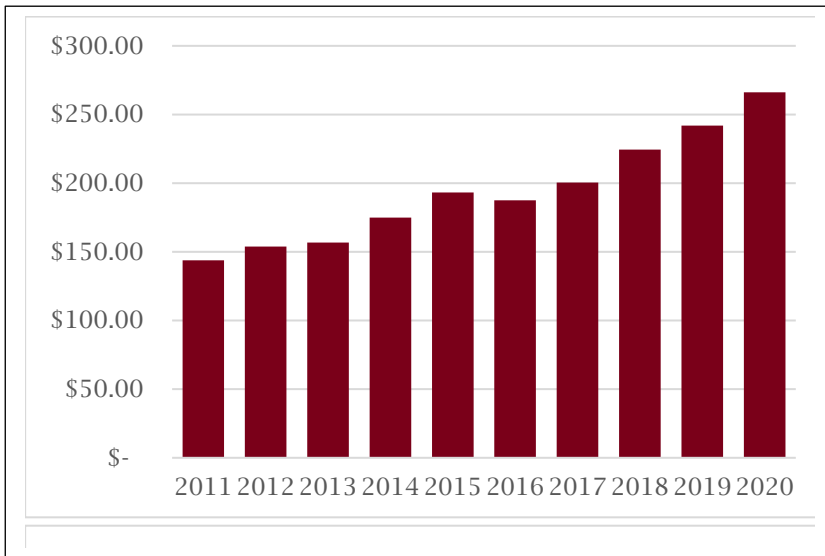
Source: 2019 U.S. Census Bureau On-The-Map

Figure 2 shows the estimated percentage of sales—across all merchandise categories—attributed to both residents and non-residents in 2020. These estimates are based on the adjusted analysis to more accurately reflect the city’s economic and consumption circumstances. Based on these findings, Extension estimates city residents represent 68.7 percent of all taxable retail and service sales subject to the tax (\$178 million), and the remaining 31.3 percent (\$81 million) are attributed to non-residents.

Figure 2: Estimated 2020 Taxable Sales Subject to LOST

| | Taxable Sales | Percent of Sales |
|----------------|---------------|------------------|
| City residents | \$178,620,000 | 68.7% |
| Non-residents | \$81,380,000 | 31.3% |

Figure 3: Total taxable sales in Cottage Grove from 2011-2020



Source: Minnesota Department of Revenue

The total taxable sales has been steadily rising from 2011 to 2015, a slight dip in 2016 followed by consistent growth through 2020 (Figure 3). Total taxable sales were \$143 million in 2011 and \$266 million in 2020. This provides some sense of the stability of a LOST going forward. The city also saw an increase from 2019 to 2020 in total taxable sales despite the impact of the pandemic.

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 4 and 5). This model estimates total tax proceeds in 2023 to be between an upper limit of \$1.62 million and a lower limit of \$1.48 million.

Figure 4: Forecast for Tax Proceeds based on Past Trends 2011 to 2020

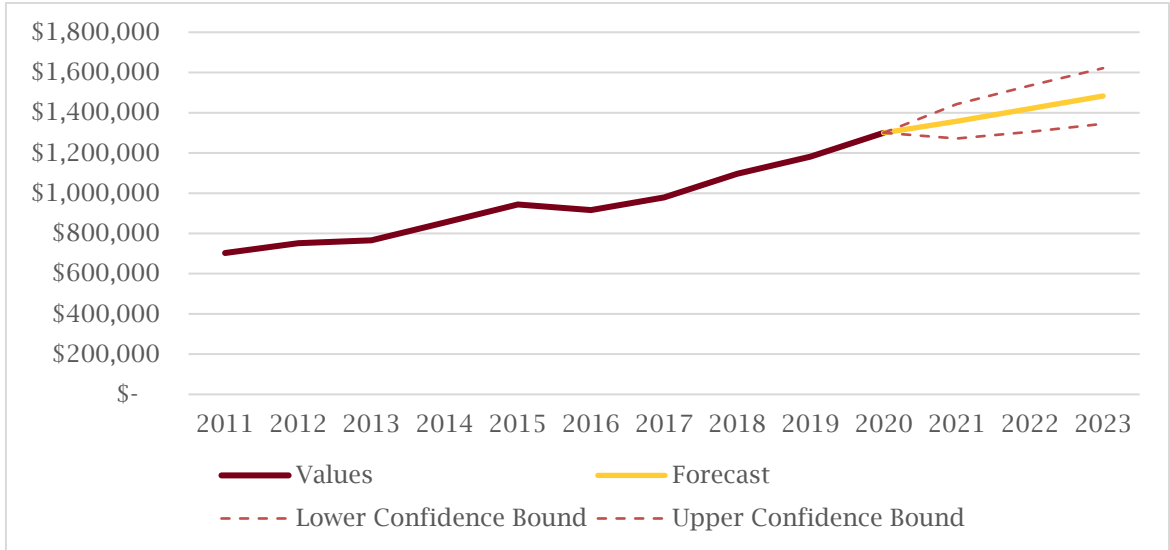


Figure 5: Forecast with Upper and Lower Bound 2021-24

| | Forecast | Lower Bound | Upper Bound |
|------|-------------|-------------|-------------|
| 2021 | \$1,357,193 | \$1,271,879 | \$1,442,508 |
| 2022 | \$1,420,176 | \$1,305,340 | \$1,535,012 |
| 2023 | \$1,483,159 | \$1,344,923 | \$1,621,395 |
| 2024 | \$1,546,142 | \$1,387,888 | \$1,704,396 |

Use taxes also affect the 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. Use taxes are often less consistent and more difficult to estimate accurately than sales taxes. In 2019, the city received \$450,904 in use (not sales) tax proceeds. It would have garnered \$33,400 for a LOST at the 0.5 percent rate.

Policymakers must also consider the impacts that a LOST may have on consumer purchasing behavior, particularly whether it will result in a loss of consumer purchases to other jurisdictions. Extension examined records of 11 cities that enacted a local option sales tax between 1999 and 2006 (information available on the Minnesota Department of Revenue website). Records do not indicate a major purchasing change due to the additional sales tax, and most of the jurisdictions have shown continued sales growth (see Appendix A). These communities, however, may not be comparable to Cottage Grove. All communities included in this analysis are located outside the Twin Cities metro area and may retain more shoppers than communities in the metro area where one can easily switch spending from one jurisdiction to another.

BACKGROUND AND METHODOLOGY

Community economics educators at University of Minnesota Extension provide applied research and education to help community and business partners make better informed decisions. In recent years, Minnesota has adopted laws enabling local governments to enact a local option sales tax. Extension has assisted these administrations in estimating their potential tax proceeds and the portion of taxes paid by local residents.

This report estimates the proportion of tax proceeds generated by Cottage Grove residents compared to non-residents. The most recently available state sales tax data (2020) from the Minnesota Department of Revenue (MN Revenue) was used.

Trade Area Analysis and Calculations

Extension conducted a trade area analysis of retail and service sales in select merchandise categories, estimating the amount of taxable sales subject to sales taxes made by both local residents and non-residents. Use tax is a much smaller portion of the total collection compared to sales tax proceeds. It is also estimated using a different formula.

Extension calculated potential sales for the city in each merchandise category and compared this calculation to actual taxable sales from the Minnesota Department of Revenue sales tax statistics for the same category. Actual sales greater than potential sales indicate the county attracts sales from outside its boundaries or has sales greater than one would expect from its residents. Extension used the difference between potential and actual sales to set reasonable estimates of spending by residents and non-residents across all categories. These estimates also helped inform adjustments for each category.

Potential sales calculations are based on average statewide spending by merchandise category and the population of the county, then adjusted by the level of income in Cottage Grove. Specifically, potential sales result from county population, state per capita taxable sales, and the index of income (see sidebar and Appendix B).

The following section details the initial and adjusted trade area calculations for all merchandise categories. The sections labeled “Analysis with Adjustments” lists the final estimate of sales generated by non-residents. A rationale for adjustments and conclusions is also included.

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:

$$(T \div PMn) \times PO \times (YWC \div YMn) = \text{potential sales}$$

T = Total Minnesota taxable sales for a merchandise category

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

PO = 2020 population of Cottage Grove (38,839)

YWC = Per capita income of Washington County residents (\$72,273)

YMn = Per capita income of Minnesota residents (\$58,834)

TRADE AREA ANALYSIS BY MERCHANDISE CATEGORY

The following pages provide detailed analysis by merchandise category.

Vehicles and Parts

13.1 percent of total taxable retail and service sales

The 7 **businesses** in this retail category include repair parts, snowmobiles, boats, trailers, and recreational vehicles. *Sales of cars and other on-road vehicles are not included in this category since they are subject to a different tax.*

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$32.54 |
| -Potential sales | \$26.69 |
| = \$ variance | \$5.85 |
| = as % of potential | 21.9% |

Unadjusted Trade Area Analysis

| | |
|--------------------------------------|---------|
| Potential taxable sales to residents | \$26.69 |
| Surplus | \$5.85 |
| Total | \$32.54 |
| Surplus percentage | 18.0% |

Analysis with Adjustments

| | |
|---|---------|
| Capture rate of Cottage Grove residents | 80% |
| Residents' \$ share | \$21.48 |
| Non-Residents' \$ share | \$11.07 |
| Total | \$32.54 |
| Non-resident share per group | 34.0% |

Analysis for Vehicles and Parts

Extension's trade area analysis estimates that the city has a surplus in this category. Based on this surplus, Extension estimated about 34%, or one-third of all sales in this category were to non-residents. And the local capture rate of 80% highlights the strength of this category within the city retails sector.

Furniture Stores

N/A percent of total taxable retail and service sales

These N/A **businesses** sell furniture, beds, carpeting, window coverings, kitchenware, and wood-burning stoves.

(\$Millions)

Actual taxable sales
Potential sales
= \$ variance
= as % of potential

Unadjusted Trade Area Analysis

Potential sales to residents
Surplus
Total
Non-resident share per group

Analysis with Adjustments

Capture rate of Cottage Grove residents
Residents' \$ share
Non-Residents' \$ share
Total
Non-resident share per group

Analysis for Furniture Stores

Categories suppressed by the Department of Revenue are included in Misc. Retail category

Electronics and Appliances

0.6 percent of total taxable retail and service sales*

These 9 **businesses** primarily include household-type appliances, sewing machines, cameras, computers, and other electronic goods.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$1.44 |
| -Potential sales | \$11.92 |
| = \$ variance | (\$10.49) |
| = as % of potential | -87.9% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|-----------|
| Potential sales to residents | \$11.92 |
| Surplus | (\$10.49) |
| Total | \$1.44 |
| Non-resident share per group | -729.6% |

Analysis with Adjustments

| | |
|---|--------|
| Capture rate of Cottage Grove residents | 11% |
| Residents' \$ share | \$1.29 |
| Non-residents' \$ share | \$0.14 |
| Total | \$1.44 |
| Non-resident share per group | 10.0% |

Analysis for Electronics and Appliances

Taxable sales are significantly lower than expected in the electronics and appliances category. The category accounts for less than 1% of all retail and service taxable sales and resulted in a nearly \$10 million deficit. Extension set the non-resident share at 10% as a floor in this category to account for some shopping from non-residents in this category.

Building Materials

22.4 percent of total taxable retail and service sales*

These 7 **businesses** sell lumber, hardware, paint, wallpaper, tile, hardwood floors, roofing, fencing, ceiling fans, lawn equipment, and garden items.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$55.51 |
| Potential sales | \$55.64 |
| = \$ variance | (\$0.13) |
| = as % of potential | -0.2% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|----------|
| Potential sales to residents | \$55.64 |
| Surplus | (\$0.13) |
| Total | \$55.51 |
| Non-resident share per group | -0.2% |

Analysis with Adjustments

| | |
|---|---------|
| Capture rate of Cottage Grove residents | 75% |
| \$49Residents' \$ share | \$41.63 |
| Non-residents' \$ share | \$13.88 |
| Total | \$55.51 |
| Non-resident share per group | 25.0% |

Analysis for Building Materials

Building materials is a large category in Cottage Grove, accounting for over 22.4% of all retail and service taxable sales. Actual sales were almost equal to that of potential sales estimates. Extension set the non-resident share of taxable sales at 25% to account for some portion of non-resident spending in this competitive retail landscape and to allow for some leakage of Cottage Grove residents purchasing these goods outside of the city.

Food and Groceries

10.5 percent of total taxable retail and service sales

The **10 businesses** in this merchandise group include grocery stores, delis, bakeries, and butcher shops that sell food to be prepared at home. Liquor stores are also included in this group.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$25.91 |
| - Potential sales | \$37.35 |
| = \$ variance | (\$11.44) |
| = as % of potential | -30.6% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|-----------|
| Potential sales to residents | \$37.35 |
| Surplus | (\$11.44) |
| Total | \$25.91 |
| Non-resident share per group | -44.1% |

Analysis with Adjustments

| | |
|---|---------|
| Capture rate of Cottage Grove residents | 58% |
| Residents' \$ share | \$21.51 |
| Non-residents' \$ share | \$4.40 |
| Total | \$25.91 |
| Non-resident share per group | 17.0% |

Analysis for Food and Groceries

Extension's trade area analysis estimated a moderate deficit in the food and liquor category in this category. Extension set the non-resident share at 17%, primarily to allow for some reasonable portion of out-shopping by Cottage Grove residents. The Cottage Grove capture rate remains at a reasonable 58% in this category where customers often remain loyal to local operations even though competition abounds with many nearby groceries and specialty food retailers throughout the metro area.

Health and Personal Items

1.3 percent of total taxable retail and service sales

Stores selling prescription drugs, food supplements, vision supplies, cosmetics, and hearing aids are among the 7 **businesses** included in this merchandise group.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$3.20 |
| Potential sales | \$5.00 |
| = \$ variance | (\$1.81) |
| = as % of potential | -36.1% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|----------|
| Potential sales to residents | \$5.00 |
| Surplus | (\$1.81) |
| Total | \$3.20 |
| Non-resident share per group | -56.5% |

Analysis with Adjustments

| | |
|---|--------|
| Capture rate of Cottage Grove residents | 50% |
| Residents' \$ share | \$2.53 |
| Non-residents' \$ share | \$0.67 |
| Total | \$3.20 |
| Non-resident share per group | 21.0% |

Analysis for Health and Personal Items

As a percent of total retail and service sales, the health and person stores is a somewhat smaller category, accounting for 1.1% of taxable retail and service sales in the city. Taxable sales are less than would be expected, resulting in a \$1.8 million deficit. Extension set the non-resident share at a modest 21%, which translates into a 50% capture rate of local resident spending and allows for some amount of spending from commuters inside and outside the city boundaries.

Gas/Convenience Stores

3.6 percent of total taxable retail and service sales

This merchandise group covers **8 businesses** selling convenience items at a store that also sells fuel.

| | (\$Millions) |
|----------------------|-------------------|
| Actual taxable sales | \$8.91 |
| -Potential sales | \$11.93 |
| = \$ variance | (\$3.03) |
| = as % of potential | -25.4% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|-------------------|
| Potential sales to residents | \$11.93 |
| Surplus | (\$3.03) |
| Total | \$8.91 |
| Non-resident share per group | -34.0% |

Analysis with Adjustments

| | |
|---|--------|
| Capture rate of Cottage Grove residents | 50% |
| Residents' \$ share | \$5.97 |
| Non-residents' \$ share | \$2.94 |
| Total | \$8.91 |
| Non-resident share per group | 33.0% |

Analysis for Gas/Convenience Stores

Cottage Grove has a sizeable deficit in the gas and convenience store category, netting about 75% of the potential sales calculations. Extension set the non-resident share at a 33% to account for non-resident spending when traveling through on major thoroughfares and for commuters into the city for work. This amounted to a 50% capture rate for Cottage Grove residents allowing for some leakage for those working, traveling and shopping outside the community.

Apparel/Clothing

2.7 percent of total taxable retail and service sales

This merchandise group includes **10 businesses** selling new clothing and accessories, jewelry, shoes, bridal items, clocks, and luggage.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$6.67 |
| Potential sales | \$5.48 |
| = \$ variance | \$1.19 |
| = as % of potential | 21.6% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|--------|
| Potential sales to residents | \$5.48 |
| Surplus | \$1.19 |
| Total | \$6.67 |
| Non-resident share per group | 17.8% |

Analysis with Adjustments

| | |
|---|--------|
| Capture rate of Cottage Grove residents | 55% |
| Residents' \$ share | \$3.00 |
| Non-residents' \$ share | \$3.67 |
| Total | \$6.67 |
| Non-resident share per group | 55.0% |

Analysis for Apparel/Clothing

Extension's trade area analysis estimates that the city brings in nearly \$1.2 million more in taxable sales than expected. With 10 businesses in this category, Cottage Grove clearly has a few stores in this category competitive with other nearby shopping areas. However, with this nearby competition in close proximity, Extension set capture rate at 55%, which translated into a 55% non-resident share to allow for about half of resident spending to leave the community.

Leisure Goods

0.0 percent of total taxable retail and service sales

The 5 **businesses** in this merchandise group sell sporting goods, books, music, hobby items, fabrics, and toys.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$0.00 |
| Potential sales | \$9.45 |
| = \$ variance | (\$9.44) |
| = as % of potential | -100.0% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|------------|
| Potential sales to residents | \$9.45 |
| Surplus | (\$9.44) |
| Total | \$0.00 |
| Non-resident share per group | -417174.0% |

Analysis with Adjustments

| | |
|---|--------|
| Capture rate of Cottage Grove residents | 0% |
| Residents' \$ share | \$0.00 |
| Non-Residents' \$ share | \$0.00 |
| Total | \$0.00 |
| Non-resident share per group | 10.0% |

Analysis for Leisure Goods

Extension's trade area analysis estimates that the city has a \$9 million deficit in this minor category which is focused on specialized retail. Extension set the non-resident share at 10% as a floor in this category. As a result of the small total amount of taxable sales in this category, it is relatively safe to assume that almost the entirety of spending by Cottage Grove residents in this category leaks outside of the city.

General Merchandise Stores

20.2 percent of total taxable retail and service sales*

The **4 businesses** in this category sell general merchandise and are unique because they have the equipment and staff needed to sell a large variety of goods from a single location. This includes department stores, superstores, dollar stores, and variety stores.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$49.98 |
| potential sales | \$50.04 |
| = \$ variance | (\$0.06) |
| = as % of potential | -0.1% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|----------|
| Potential sales to residents | \$50.04 |
| Surplus | (\$0.06) |
| Total | \$49.98 |
| Non-resident share per group | -0.1% |

Analysis with Adjustments

| | |
|---|---------|
| Capture rate of Cottage Grove residents | 75% |
| Residents' \$ share | \$37.48 |
| Non-Residents' \$ share | \$12.49 |
| Total | \$49.98 |
| Non-resident share per group | 25.0% |

Analysis for General Merchandise Stores

This is one of the largest categories in Cottage Grove, accounting for over 20% of all retail and service sales in the community. In 2020, Cottage Grove actual sales in the general merchandise category were in line with the calculated potential sales. Extension estimated non-residents in this category accounted for roughly 25% of all sales, capturing about 75% of Cottage Grove resident spending in this category.

Miscellaneous Retail

11.8 percent of total taxable retail and service sales

91 businesses are part of this group, including florists, used merchandise stores, pet supply stores, and other retailers.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$4.10 |
| Potential sales | \$13.48 |
| = \$ variance | (\$9.38) |
| = as % of potential | -69.6% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|----------|
| Potential sales to residents | \$13.48 |
| Surplus | (\$9.38) |
| Total | \$4.10 |
| Non-resident share per group | -228.7% |

Analysis with Adjustments

| | |
|---|--------|
| Capture rate of Cottage Grove residents | 24% |
| Residents' \$ share | \$3.28 |
| Non-residents' \$ share | \$0.82 |
| Total | \$4.10 |
| Non-resident share per group | 20.0% |

Analysis for Miscellaneous Retail

Extension's trade area analysis estimates that Cottage Grove had over a \$9 million deficit in the miscellaneous retail category. Extension set the non-resident share to 20% despite this deficit since general merchandise is very competitive in the metro and some miscellaneous retail such as antique shops in the community would reasonably have a large draw.

Amusement and Recreation

0.7 percent of total taxable retail and service sales*

The 11 **businesses** in this group include casinos, bowling lanes, water parks, amusement parks, arcades, bingo halls, golf courses, ski slopes, marinas, dance or fitness centers, recreational clubs, ice rinks, swimming pools, roller rinks, etc.

| | (\$Millions) |
|----------------------|--------------------|
| Actual taxable sales | \$1.77 |
| Potential sales | \$12.60 |
| = \$ variance | (\$10.84) |
| = as % of potential | -86.0% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|--------------------|
| Potential sales to residents | \$12.60 |
| Surplus | (\$10.84) |
| Total | \$1.77 |
| Non-resident share per group | -613.5% |

Analysis with Adjustments

| | |
|---|--------|
| Capture rate of Cottage Grove residents | 10% |
| Residents' \$ share | \$1.24 |
| Non-residents' \$ share | \$0.53 |
| Total | \$1.77 |
| Non-resident share per group | 30.0% |

Analysis for Amusement and Recreation

Extension's trade area analysis estimates that the city has a significant deficit of potential sales in this category of over \$10 million. In this case and considering the large deficit, Extension set the non-resident share at 30 percent to account for roughly a 10% capture rate of Cottage Grove spending in this category due to the proximity to other metro area communities and attractions.

Accommodations

N/A percent of total taxable retail and service sales

These N/A **businesses** provide lodging or short-term accommodations for travelers, vacationers, and others. Included are hotels, motels, lodges, bed & breakfasts, campgrounds, fraternities, boarding houses, and dormitories.

(\$Millions)

Actual taxable sales
Potential sales
= \$ variance
= as % of potential

Unadjusted Trade Area Analysis

Potential sales to residents
Surplus
Total
Non-resident share per group

Analysis with Adjustments

Capture rate of Cottage Grove residents
Residents' \$ share
Non-residents' \$ share
Total
Non-resident share per group

Analysis for Accommodations

Categories suppressed by Department of Revenue show up in the Misc. Retail category

Eating/Drinking Establishments

15.8 percent of total taxable retail and service sales

These 43 businesses sell food at full-service or limited-service establishments. The group includes cafeterias, bagel shops, ice cream parlors, snack bars, food service contractors, caterers, lunch wagons, and street vendors. It also includes bars, taverns, and nightclubs.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$39.08 |
| Potential sales | \$58.56 |
| = \$ variance | (\$19.48) |
| = as % of potential | -33.3% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|-----------|
| Potential sales to residents | \$58.56 |
| Surplus | (\$19.48) |
| Total | \$39.08 |
| Non-resident share per group | -49.8% |

Analysis with Adjustments

| | |
|---|---------|
| Capture rate of Cottage Grove residents | 33% |
| Residents' \$ share | \$19.54 |
| Non-residents' \$ share | \$19.54 |
| Total | \$39.08 |
| Non-resident share per group | 50.0% |

Analysis for Eating/Drinking Establishments

The eating and drinking category—which includes all bars, restaurants, and other food service—is a significant category with \$39 million in taxable sales and has a significant deficit at nearly \$20 million. The community is surrounded by a lot of other dining options and competition from nearby communities with a wide mix of types of dining, pulls residents out of Cottage Grove. Combining this competition with local commuting patterns, Extension estimated a capture rate of 33% for Cottage Grove resident spending in this category.

Repair and Maintenance

2.2 percent of total taxable retail and service sales

The **17 businesses** in this group restore machinery, equipment, and other products. The group does not include plumbing or electrical repair services but does encompass auto repair, cameras, televisions, computers, copiers, appliances, lawn mowers, specialized equipment, small engines, furniture, shoes, guns, etc.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$5.55 |
| Potential sales | \$12.41 |
| = \$ variance | (\$6.86) |
| = as % of potential | -55.3% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|----------|
| Potential sales to residents | \$12.41 |
| Surplus | (\$6.86) |
| Total | \$5.55 |
| Non-resident share per group | -123.7% |

Analysis with Adjustments

| | |
|---|--------|
| Capture rate of Cottage Grove residents | 40% |
| Residents' \$ share | \$4.99 |
| Non-residents' \$ share | \$0.55 |
| Total | \$5.55 |
| Non-resident share per group | 10.0% |

Analysis for Repair and Maintenance

At 2.2 percent of total taxable sales, repair and maintenance is a relatively small category in Cottage Grove at just over \$5.5 million in actual sales. The large deficit that exists in this category, and the share of total spending coming from non-residents at approximately 10% estimates around a 40% capture rate for Cottage Grove resident spending in this category.

Personal Services/Laundry

3.3 percent of total taxable retail and service sales

The **140 businesses** in this merchandise group include barber shops and beauty parlors, death care services, laundry and dry-cleaning services, and a wide range of other personal services, such as pet care (except veterinary), photofinishing, temporary parking, and dating services.

| | (\$Millions) |
|----------------------|--------------|
| Actual taxable sales | \$27.01 |
| Potential Sales | \$11.52 |
| = \$ variance | \$15.50 |
| = as % of potential | 134.5% |

Unadjusted Trade Area Analysis

| | |
|------------------------------|---------|
| Potential sales to residents | \$11.52 |
| Surplus | \$15.50 |
| Total | \$27.01 |
| Non-resident share per group | 57.4% |

Analysis with Adjustments

| | |
|---|---------|
| Capture rate of Cottage Grove residents | 75% |
| Residents' \$ share | \$8.64 |
| Non-residents' \$ share | \$18.37 |
| Total | \$27.01 |
| Non-resident share per group | 68.0% |

Analysis for Personal Services/Laundry

This category includes businesses that typically serve a local market, such as barbers, hair salons, and dry-cleaning operations. Not unlike the health and personal store category in Cottage Grove, the city is disproportionately strong in this category with 140 businesses and a \$15.5 million surplus. Clearly the community has a niche which draws in non-residents. Extension set the non-resident share at 68%, which translates in a 75% capture rate.



Retail (Non-Store) and Other Services

This section includes taxable sales attributed to North American Industrial Classification System categories 511-813 released by MN Revenue.

| | |
|---|--------------|
| | (\$Millions) |
| Actual taxable sales | \$11.45 |
| % of total taxable retail and service sales In Cottage Grove | 4.6% |

Analysis with Adjustments

| | |
|------------------------------|--------------|
| | (\$Millions) |
| Residents' \$ share | \$7.22 |
| Non-residents' \$ share | \$4.24 |
| Total | \$11.45 |
| Non-resident share per group | 37% |

Analysis for Retail and Other Services

This group includes non-store retailers (such as direct selling operations), healthcare, waste management, rental/lease services, administrative support, and the performing arts. Some of these categories serve primarily a local market, whereas categories like 541 (professional and technical services) often serve a non-local market. This mix of business types is too diverse to run a trade area analysis for, but Extension estimated an aggregate 35 percent of these sales are to non-resident customers. The categories of sales are shown below:

| Category | Taxable Sales | % non-local | \$ non-local |
|-------------------------------|---------------|-------------|----------------|
| 454 RETL -NONSTORE RETAILERS | \$409,771 | 50% | \$204,885.50 |
| 517 INFO -TELECOMMUNICATIONS | \$2,709,435 | 40% | \$1,083,774.00 |
| 531 REAL ESTATE | \$2,313,582 | 40% | \$925,432.80 |
| 532 RENTAL, LEASING SERVICES | \$200,293 | 20% | \$40,058.60 |
| 541 PROF,SCIENTIFIC,TECH SERV | \$2,020,394 | 40% | \$808,157.60 |
| 561 ADMIN, SUPPORT SERVICES | \$3,020,805 | 30% | \$906,241.50 |
| 621 HEALTH -AMBULATORY CARE | \$779,741 | 40% | \$311,896.40 |
| TOTAL | \$11,454,021 | 37% | \$4,280,446.40 |

Construction, Manufacturing, Utilities, Wholesale Operations, Transportation, and Sales 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. These industries and services generate \$18.2 million in taxable sales, or 6.8 percent of total taxable sales in Cottage Grove. A significant portion of this amount would be subject to any new sales taxes, including a local option sales tax.

This category includes utilities that primarily serve a local market and are subject to a local option sales tax. The diversity of firm types included in this category makes it difficult to understand the customer mix of these businesses; however, Extension broke out each known subcategory with an assumption of whether customers paying the taxable sales were non-local:

| Category | Taxable Sales | % non-local | \$ non-local |
|-------------------------|---------------|-------------|---------------|
| CONSTRUCTION | \$688,529 | 50% | \$344,264.5 |
| MANUFACTURING | \$96,655 | 80% | \$77,324.0 |
| WHOLESALE | \$8,732,207 | 60% | \$5,239,324.2 |
| UNDESIGNATED/SUPPRESSED | \$8,700,830 | 30% | \$2,610,249.0 |
| Total | \$18,218,221 | 45% | \$8,271,161.7 |

Extension estimated that, overall, 44 percent of sales are to non-residents. This analysis assumes that some subcategories, such as manufacturing sell primarily (80 percent) to non-resident customers, whereas subcategories like construction split sales between resident and non-resident customers.

Analysis with Adjustments

| | (\$Millions) |
|------------------------|--------------|
| Residents' \$ share | \$10.02 |
| Non-residents \$ share | \$8.20 |
| Total | \$18.22 |
| Non-resident share | 45% |

APPENDIX A: RESEARCH ON THE EFFECTS OF A LOCAL OPTION SALES TAX

Policymakers are often concerned that enacting a local sales tax will result in a loss of consumer purchases to neighboring communities that have not adopted the tax.

The Minnesota Department of Revenue records the tax collected from a set of Minnesota jurisdictions that have had a local sales or use tax in effect for at least eight years. Most of these cities show continued sales growth. A comparison that includes 11 Minnesota cities adopting a 0.5 percent local option sales tax is offered below (refer to Figures 4, 5, 6, and 7).

Policymakers must determine the best allowable method to raise revenue from a variety of options. One option is raising property taxes, which is not directly related to a household's current income and raises the financial burden of low-income or retired homeowners. Sales taxes raise revenues based on household expenditures, which, in Minnesota, excludes the basic necessities of food and clothing. However, since sales tax raises revenues from non-residents who shop in Cottage Grove, resident contributions to tax revenues are significantly lower than a tax generated exclusively by local residents, such as a property tax. Policymakers must carefully consider these and other factors before making a decision about enacting a local sales tax.

Figure 4: Taxable retail and service sales by communities that began collecting a local option sales tax from 1999 to 2006

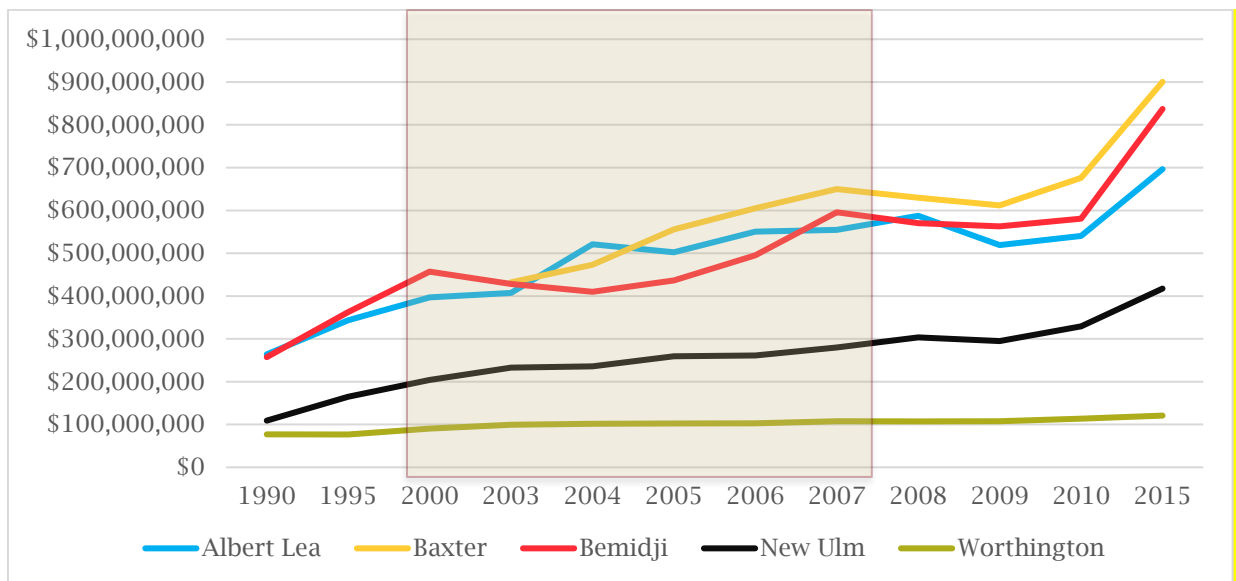


Figure 5: Data table for example communities, taxable retail and service sales (in millions)

| Town Name | 2015 Population | Year LOST | 90 | 95 | 00 | 03 | 04 | 05 | 06 | 07 | 08 | 09 | 10 | 15 |
|-------------|-----------------|-----------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Albert Lea | 18,356 | 2006 | \$264 | \$344 | \$397 | \$407 | \$521 | \$502 | \$551 | \$555 | \$588 | \$519 | \$541 | \$696 |
| Baxter | 8,065 | 2006 | | | | \$432 | \$473 | \$556 | \$605 | \$650 | \$630 | \$612 | \$676 | \$900 |
| Bemidji | 11,917 | 2005 | \$257 | \$362 | \$457 | \$428 | \$410 | \$437 | \$495 | \$596 | \$570 | \$563 | \$581 | \$837 |
| New Ulm | 13,594 | 1999 | \$109 | \$165 | \$204 | \$233 | \$236 | \$259 | \$261 | \$280 | \$303 | \$295 | \$329 | \$417 |
| Worthington | 11,283 | 2005 | \$77 | \$77 | \$91 | \$99 | \$102 | \$103 | \$103 | \$108 | \$107 | \$108 | \$114 | \$121 |

Figure 6: Taxable retail and service sales by communities that began collecting a local option sales tax between 2011- 2012

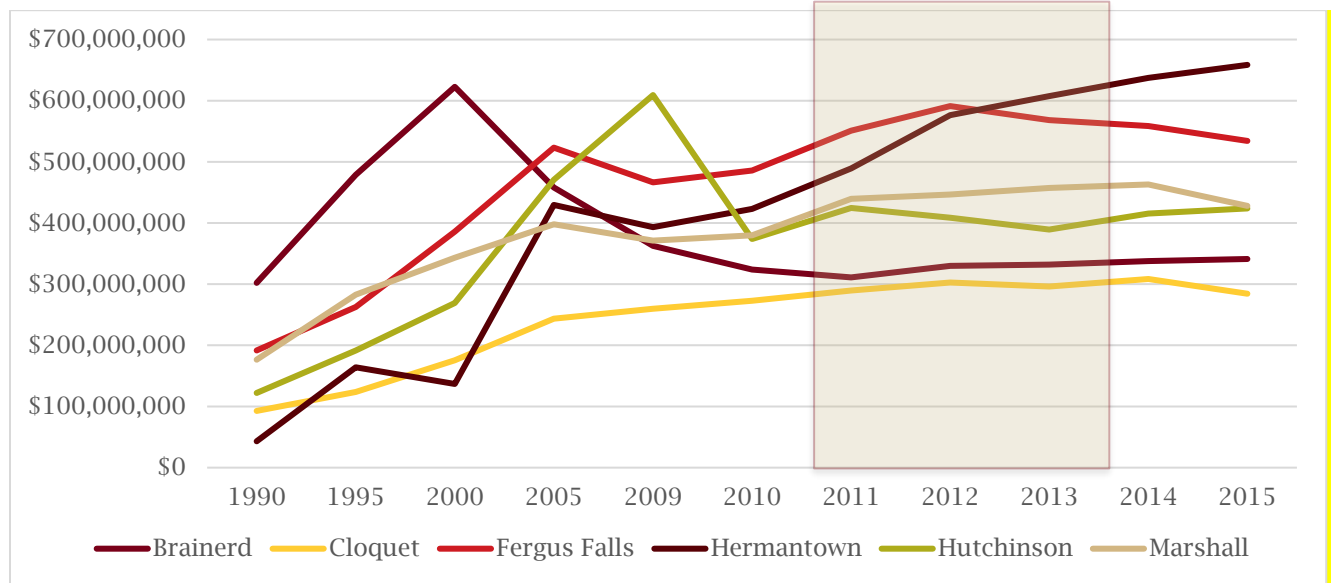


Figure 7: Data table for example communities, taxable retail and service sales (in millions)

| Town Name | 2015 Pop | Year LOST | 90 | 95 | 00 | 05 | 09 | 10 | 11 | 12 | 13 | 14 | 15 |
|---------------------|----------|----------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| <i>Brainerd</i> | 13,178 | 2011 | \$302 | \$479 | \$623 | \$458 | \$362 | \$324 | \$311 | \$330 | \$332 | \$338 | \$341 |
| <i>Cloquet</i> | 11,201 | 2011 | \$93 | \$124 | \$175 | \$244 | \$260 | \$273 | \$290 | \$303 | \$296 | \$308 | \$284 |
| <i>Fergus Falls</i> | 13,471 | 2011 | \$192 | \$263 | \$386 | \$523 | \$467 | \$486 | \$551 | \$591 | \$568 | \$558 | \$534 |
| <i>Hermantown</i> | 7,448 | 1996 - increase 2012 | \$43 | \$164 | \$137 | \$430 | \$393 | \$423 | \$489 | \$576 | \$607 | \$637 | \$659 |
| <i>Hutchinson</i> | 13,080 | 2011 | \$122 | \$191 | \$269 | \$471 | \$609 | \$374 | \$425 | \$409 | \$389 | \$415 | \$424 |
| <i>Marshall</i> | 12,735 | 2011 | \$176 | \$283 | \$343 | \$398 | \$371 | \$380 | \$440 | \$447 | \$457 | \$463 | \$428 |

APPENDIX B: 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 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 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 <https://www.revenue.state.mn.us/minnesota-tax-handbooks>

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 or county. It is the product of county population, state per capita sales, and the index of income (based on the county personal per capita income).

Actual sales

For this study, the Minnesota Department of Revenue's 2019 sales data for Cottage Grove 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 that 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. All sales reported by a business is attributed to that selected NAICS category. 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 underreport 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 county, 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 county. Whenever misreporting is discovered, the Minnesota Department of Revenue is contacted to clarify the situation.