

## Memorandum

To: Revenue Interim Committee  
From: Finn McMichael, Tax Policy and Research  
Date: 11/13/2025  
Subject: Department of Revenue's Sales Tax Model

### Overview of Montana's Sales Tax Model

To generate sales tax revenue estimates, the Department of Revenue developed a sales tax revenue estimation model based on data from the U.S. Census Bureau's Economic Census of Businesses, the U.S. Department of Labor's Consumer Expenditure Survey, and taxable sales ratios from other state's sales tax reports (specifically South Dakota). Based on industry data, the sales tax model projects revenue for sales taxes that exclude particular industries or services, such as food sales or medical services. The sales tax model also projects future sales tax revenue based on forecasted consumer spending growth and patterns. Finally, the sales tax model provides revenue estimates based on various sales tax rates that are proposed in legislation.

To generate its revenue estimates, the department's sales tax model follows a four-step process. In the first step, historical total sales data from the 2022 Economic Census of Businesses is used to provide taxable sales estimates for each of Montana's economic sectors, such as retail sales, construction services and accommodation and food services. Most sales taxes are designed to not tax intermediate sales between businesses, but only final sales to consumers, so the model attempts to account for this by specifying a percentage of the total sales that are estimated to be taxable, using taxable sales reports from other states. These percentages are referred to as taxable sales ratios and vary between sectors and types of goods and services. Next, the historical sales data is projected forward using estimated growth and changes to consumer spending patterns, based on the Consumer Expenditure Survey. Finally, the specified tax rate, non-compliance and vendor allowance rates are applied to the adjusted taxable sales to provide the final revenue estimate. The current version of the model assumes a 5% non-compliance and 1.5% vendor allowance.

In the end, the revenue amounts provided by the revenue model are estimates and are subject to several assumptions and limitations. One the primary assumptions made by the model is that consumption spending patterns by residents of Montana are comparable to the spending patterns of the United States as a whole. This assumption is due to the lack of state level consumer spending pattern data. Another assumption is that industry sales do not change significantly over a short amount of time. This assumption is necessary, as industry sales data from the Economic Census are only released every five years and must be projected forward.



## Sales Tax Revenue Estimates for SB 558 from 2025 Legislative Session

SB 558 proposed to create a statewide general sales tax of 4% for the use of reducing property taxes for school funding. The sales tax portion was modeled after South Dakota's sales tax, which is broad based, meaning it taxes most final goods and services, with a few exclusions (food, housing, healthcare, education). These exclusions were applied to the department's sales tax model, and taxable sales ratios from South Dakota sales tax data were used to estimate the taxable sales by industry and resulting tax revenue. The resulting tax revenue estimates from the department's sales tax model, for this type of 4% general statewide sales tax is \$1.5 to \$1.7 billion per year for the next few years.

If you have any additional questions, please don't hesitate to give me a call at (406) 444-2715.