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United States General Accounting Office
Washington, DC 20548

November 6, 2001

The Honorable Max Baucus, Chairman
The Honorable Charles E. Grassley
Ranking Minority Member
Committee on Finance
United States Senate

Subject: Update on State and Local Revenue Loss From Internet Sales

As you requested, we have examined the Census Bureau's estimates of e-commerce in 1999¹ to determine whether they would provide a basis for us to revise any of the results we presented in our 2000 report on sales tax losses from e-commerce.² In that report, we used a range of available private-sector forecasts of Internet and total remote sales as the basis for several scenarios illustrating the impact of such sales on state and local sales and use tax revenues. The scenarios showed that there is considerable uncertainty about the size of the impacts and how various assumptions about sales, compliance, and other factors contribute to that uncertainty. The purpose of this letter is to present our conclusions from a review of the Census estimates.

In summary, we found that Census' new e-commerce estimates do not provide a basis for revising the results in our 2000 report. Census' definition of e-commerce is broader than Internet sales.³ Because of the way firms provided information on their e-commerce sales to Census, Internet sales cannot be separated from the broader e-commerce sales at a level of detail that allows us to compare Census' results with the Internet sales estimates we used in our report.

In our 2000 report, we made a distinction between sales by businesses to other businesses and sales by businesses to individual consumers. Private-sector forecasters typically estimate these two categories of sales separately. The Census Bureau also makes separate estimates for broad categories of e-commerce. Census' estimate for manufacturers' value of e-commerce shipments is its estimate that is closest in concept to the estimates of business-to-business Internet sales that we used

¹See "1999 Multi-sector report," *E-Stats*, (Mar. 7, 2001), www.census.gov/estats.

²See *Sales Taxes: Electronic Commerce Growth Presents Challenges; Revenue Losses Are Uncertain* (GAO/GGD/OCE-00-165, June 30, 2000).

³"The Census Bureau's e-commerce measures report the value of goods and services sold online whether over open networks such as the Internet, or over proprietary networks running systems such as Electronic Data Interchange (EDI)." (See *E-Stats* (Mar. 7, 2001) www.census.gov/estats.) The Internet sales estimates we used in our 2000 report covered only sales transacted over the Internet.

in our report. Census' estimate of retail e-commerce is closest in concept to the estimates of business-to-consumer Internet sales that we used.

We cannot use Census' estimate for manufacturers' value of e-commerce shipments in 1999 to revise the business-to-business Internet sales estimates that we used for the scenarios in our report. The Census estimate includes transactions completed over Electronic Data Interchange networks, which have been widely used for years and were in use before the recent growth in Internet commerce. EDI can involve transactions over the Internet, but a large volume of EDI takes place over proprietary networks. Firms that responded to a Census questionnaire concerning e-commerce in 1999 did not report separate values for EDI transactions and Internet transactions. The respondents reported total on-line sales and indicated which type of computer network they used most frequently, but they did not provide a percentage distribution of sales that corresponded to the various networks. Moreover, Census' e-commerce estimates are disaggregated by broad manufacturing sectors. The estimates of Internet sales that we used in our 2000 study were reported at a different level of detail. We are unable to aggregate our 2000 estimates in a manner that would permit a comprehensive and accurate comparison to the Census estimates.

Census' new estimate of retail e-commerce does not provide a reason for us to revise the range of revenue loss scenarios that we presented in our 2000 report. The difference between Census' estimate and the high-end estimate that we used in our report is small relative to the margins of error associated with many of the assumptions that we needed to use in that study.⁴ Census estimates that U.S. retailers sold about \$27.3 billion in goods and services on-line in 2000. This number is higher than the \$24.8 billion figure that we used for the higher scenario in our study. However, the Census estimate includes export sales and sales by retailers to other businesses, which were not included in the sales estimates that we used and which would not be part of the U.S. business-to-consumer sales tax base that we were estimating. If the exports and sales to businesses were excluded from the Census estimate, it is likely that the estimate would not be significantly above the value that we used.

We based our conclusions in this letter on a comparison of the documentation for Census' e-commerce estimates and for Forrester Research's estimates of business-to-consumer and business-to-business Internet sales that we used in our 2000 report. We discussed the differences between Census' and Forrester's estimates with individuals who were involved in preparing both sets of estimates.

The Department of Commerce reviewed a draft of the correspondence and had no changes to suggest. We conducted our audit work in accordance with generally accepted government auditing standards between August and September 2001.

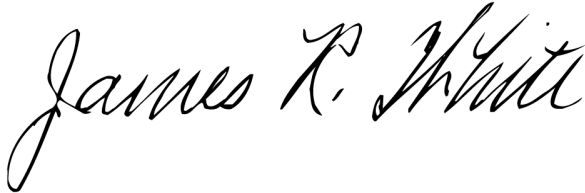
As arranged with your offices, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days after the date of this letter. At

⁴The fact that Census includes EDI in its definition of e-commerce does not have significance for this comparison of business-to-consumer sales estimates because EDI occurs between businesses, not between businesses and individual consumers.

that time we will be sending copies of this letter to interested congressional Committees and the Director, Bureau of the Census. The letter will also be available on GAO's home page at www.gao.gov.

If you have any questions, you may contact Jim Wozny or me at (202) 512-9110. In addition, Demian Moore and Tara Carter made key contributions to this letter.

Sincerely yours,

A handwritten signature in black ink that reads "James R. White". The signature is written in a cursive style with a large, prominent initial "J".

James R. White
Director, Tax Policy
and Administration Issues

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