# How Retail's Revolution is Driving New Tax Challenges

The radical transformation of e-commerce is making tax compliance more complex than ever. In the United States, e-commerce sales rose by 9.2% in the second quarter of 2021. That's after huge spikes of more than **30% growth** per quarter from Q2 2020 to Q1 2021 during the height of COVID-19 lockdowns.

This is only the beginning.

In the coming months and years, changing consumer habits resulting from the pandemic and ongoing digitization of retail will continue driving expansion of online sales and digital marketplaces. At the same time, new legislation will accelerate the adoption of new business models and force companies to reimagine supply chains to reduce tax risk.

The business-to-business (B2B) space that once relied on long sales cycles, deep relationships and organization-to-organization contact is now embracing the direct-to-consumer (DTC) revolution. In fact, B2B e-commerce sales rose by 18.2% in 2020 and are expected to grow 18.7% from 2021 to 2028. Marketplace businesses should fare well. They offer analytics on buyer trends, product categories, geography and other key data points that enable more effective DTC selling of products that were once transacted via B2B. These paradigm shifts will allow a new class of companies to tap into the consumer market.

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Shifts are also taking place in business development strategy. Retailers and e-commerce players are embracing mergers and acquisitions (M&A) to quickly grow their businesses, scale their brands and enter new markets. M&A can offer rapid entry into new business lines or geographies where existing brands have yet to find penetration, but it comes with significant logistical challenges, such as integrating technologies, tax compliance and minimizing risk. These seismic changes in the e-commerce ecosystem have huge implications for businesses — with one of the most important being the complex and ever-changing indirect tax environment.

In this e-book, we'll explain the macroeconomic trends driving change, why these paradigm shifts will bring new tax complexities, and how businesses can manage indirect tax compliance and use it as a competitive advantage.

# Trends Driving Change

There are powerful influences driving changes in the e-commerce market. Among the most significant include:

**Mass adoption of e-commerce and changing consumer interests.** The consumer economy has gradually but inevitably been shifting toward e-commerce for years. Then came the pandemic, which accelerated the transformation. While most consumers had already engaged in at least some e-commerce activities before COVID-19, pandemic lockdowns and safety concerns drove this concentration way up, even among the most skeptical and least digital-savvy consumers.

The widespread adoption of remote work, an increasingly globalized workforce and the temporary decline of traditional entertainment gave rise to new hobbies and consumer interests. Matthew Kenneally, Vice President of Global Channel and Alliances at SAP, argues that these changes made e-commerce more appealing to the average consumer while simultaneously creating new needs for goods and services to facilitate changing lifestyles. While this presents opportunities to increase revenue, he cautions that many organizations will find themselves at a disadvantage due to ineffective technology solutions that can't meet rising demand.

> "The global pandemic has accelerated many companies' plans to invest in scalable customer experience solutions. Many users are relying more on B2B and B2C solutions than ever before."
>
> **- Matthew Kenneally**, Vice President of Global Channel and Alliances at SAP.

Brands that previously made a limited investment in e-commerce now must adapt to the digital ecosystem, engage more directly with consumers online and increase their participation in digital marketplaces. At the same time, hybrid physical-digital experiences like curbside pick-up and buy online, pick up in-store (BOPIS) have risen in popularity.

**Channel expansion.** A rapidly expanding ecosystem of digital platforms has created a wide range of fresh opportunities for businesses to reach new customers online and pull them into a marketplace experience. Social channels like Facebook, Instagram and TikTok have engaged users across demographics. Emerging platforms like connected TV offer the opportunity to integrate the online retail experience with a television-like ad experience, bringing even more users into e-commerce spaces.

**Reduced marketing costs.** The explosion of consumer channels has created many lower-cost marketing options that appeal to smaller businesses. Brands that once relied on (or couldn't afford) television commercials, billboards or print ads can now launch digital campaigns at a fraction of the price. The democratization of marketing allows new brands to scale quickly and even target their desired audience.

**Around-the-clock operations.** Unlike brick-and-mortar retail, e-commerce is a 24/7 global business. Websites, e-stores and marketplaces don't close down at the end of the business day. E-commerce tends to follow people's daily routines, and while shopping does dip overnight, transactions continue to take place at all hours. To avoid backlog, e-commerce retailers must prepare to operate around the clock with shipping, inventory management and customer service.

**Supply chain challenges.** Pandemic-era labor scarcities and lockdowns led to supply chain shortages, delaying the shipment of everything from semiconductors to appliances to furniture. These challenges make cross-border trade particularly difficult, requiring retailers to navigate a new level of logistics.

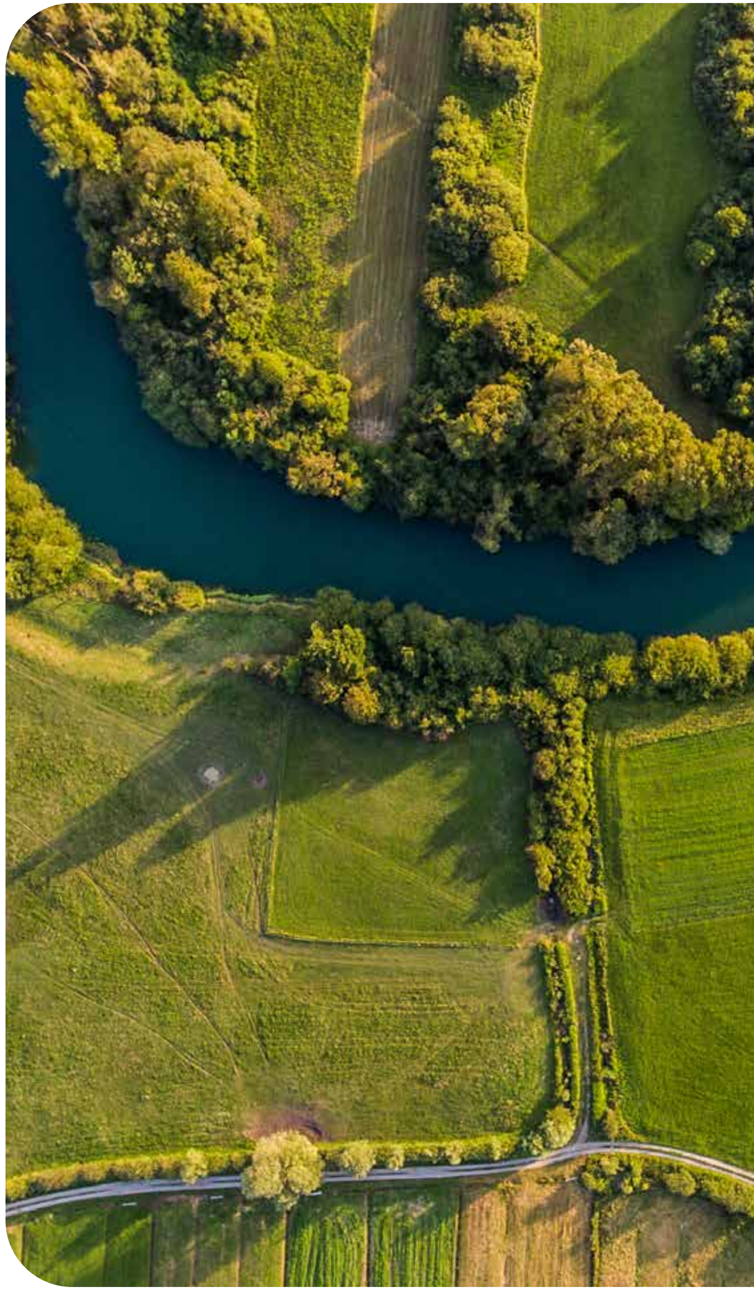
# The Tax Challenges of Change

What is the end result of all this change across the e-commerce ecosystem? The answer is: challenges, particularly in indirect tax compliance. Let's take a closer look at some of the difficulties facing retailers as a result of recent industry transformations.

**Cross-border tax risks.** E-commerce vastly expands the geographic area in which retailers can sell their products, but along with that expansion comes a new set of burdens. Retailers source and sell into new markets, but each has their own unique tax code.

> Retail and direct-to-consumer manufacturers have to worry about how much they're selling in each state, both in terms of revenue and number of transactions. There are hundreds of new jurisdictions that have popped up, new tax collecting entities like local towns as well as changing taxes, environmental fees, sales tax, non-traditional taxes and tax holidays.
>
> **- Peter Olanday**, Director of Retail Consulting at Vertex.

Let's not forget international tax laws including import, export and sales and use tax requirements which have made tax compliance a complex logistical and regulatory endeavor.



**"Ensuring compliance with fast-changing local tax laws is essential for retailers to thrive,"** Olanday says. This is especially true for new and emerging retailers who have scaled quickly but don't have the internal finance infrastructure to manage international tax codes in-house. This complexity will increase exponentially as retailers add new markets for sourcing and distribution.

**Modernization and digital transformation.** The current high-growth climate for e-commerce is creating new demands for retailers to implement modern technology and infrastructure. Most will need to quickly integrate new systems and tools in order to sustain their growth, create new scaled efficiencies, and support new marketers and products. This includes evaluating, integrating, and adopting tools for automation, digital marketing, customer communication, enterprise resource planning, procurement and marketplace creation. It requires migrating services and data to the cloud to enable all of these new functions. Tax technology must support the modern e-commerce tech stack so retailers can estimate, forecast, extract and pay appropriate local taxes to remain in compliance with various tax codes.

**Complexity.** Even the most integrated e-commerce experience demands input and contributions from multiple stakeholders. Sellers, shippers, manufacturers and distributors must all align to deliver consistent, seamless service. M&As only add to this complexity with multiple, different sources of data, and no single source of truth.

# Rising to the Challenges

Yes, the new normal in retail is complex and fast-evolving. But many of today's companies leverage new tools to level the playing field. In many cases, automation provides a solution to the demands of an increasingly complex economy that requires 24/7 support. Sales automation allows retailers to continue selling at all hours without maintaining around-the-clock workforces. Tax automation helps minimize the cost and labor involved in navigating complex interstate and cross-border trade. Even with a strong, knowledgeable team, manual tax implementation is both difficult and time-consuming, and most importantly, error-prone.

Vertex is a great example of making tax compliance a seamless process. As a leading tax technology provider, Vertex not only offers tools that navigate the complex tax codes as they change, but it also integrates with popular business management software. For example, its integration with SAP helps a wide variety of enterprises improve tax compliance with reliable tax rules and rates, improved calculation and compliance, and exemption management.

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**Data is key.** In order for businesses to make informed decisions in an increasingly complex environment, they will need accurate, reliable tax analytics. Data is the key to making better tax decisions and reducing tax liability. An integrated end-to-end solution lets businesses use that data to deliver results. Such a solution allows retailers to streamline their operations based on a common set of up-to-date rates and rules while also reducing overhead costs by avoiding unnecessary data silos and unwarranted fees for duplicative tools and services.

With more accurate data, businesses can improve tax forecasting, which enables retailers to proactively reduce the amount of cash on reserve needed to guard against underpayment. Accurate estimation of required remittances will allow businesses to keep more capital liquid rather than holding it in reserve to address unanticipated tax penalties.

**Manage complexity.** Automation tools can also reduce the burden of managing multichannel sales. While many retailers will find it desirable to leverage as many channels as possible to reach a wider array of consumers, the individual burdens of managing taxation across these channels can be prohibitive. Unifying all channels under a single overarching tax engine can reduce the manual work required of tax and finance teams. That allows retailers to scale, embrace new channels quickly, and flexibly shift spending between channels without concern for overwhelming backend resources with new demand.

**Simplify M&As.** For businesses looking to expand their market through M&A, a holistic approach to tax automation can help ease the pains of integrating new businesses. Such an approach reduces complexity and creates a single unified tax solution rather than a wide range of disparate tools requiring their own individual integrations.

Holly Hamby, Tax Managing Director at Deloitte Tax LLP, says that integrated tax automation can be a huge boon for M&A development strategies in retail. "Companies in the retail space tend to acquire smaller businesses that align well with their growth strategy," Hamby says. "Having a standard technology solution, including indirect tax, allows you to be more nimble and minimize onboarding costs."

**The power of a unified tax engine.** SAP's Kenneally says that modern tax technology works best when partnered with the right strategy. "A holistic integration approach goes far beyond technical integration of applications by integrating both technology and business processes to deliver significant value to the business, helping them become an intelligent enterprise," he says.

Having a single tax engine that seamlessly integrates with all of a retailer's business systems provides a single source of truth for tax determination and compliance. This allows for a more consistent process and approach that reduces complexity and mitigates the risk of errors and excessive penalties. A fully integrated system of tax automation frees capital and resources to allocate to other strategic concerns, providing the flexibility needed to support all of the systems and platforms businesses rely on to scale.

# Simplify Tax Compliance For a Bright Future

Tax compliance is complex, and it's becoming even more challenging to stay compliant without the right technology. Consumer behaviors are evolving more rapidly than ever, and businesses are transforming operations to keep pace. They are entering new markets, selling on new platforms and launching new business lines — while looking to limit tax liabilities.

Tax technology is coming to the rescue. It helps businesses comply with ever-changing tax codes in jurisdictions all over the world. It removes manual tax calculations and makes it simple for companies to charge the right taxes for products and services. With tax compliance handled, companies have the freedom to experiment with new ways of reaching customers and making sales.

Nobody knows what the future of e-commerce will bring, but with the right tax compliance software and strategy, businesses can prepare accordingly.

Learn More

## About Vertex

Vertex Inc., is a leading global provider of indirect tax software and solutions. The company's mission is to deliver the most trusted tax technology, enabling global businesses to transact, comply, and grow with confidence. Vertex provides solutions that can be tailored to specific industries for major lines of indirect tax, including sales and consumer use, value added, and payroll. Headquartered in North America, and with offices in South America and Europe, Vertex employs over 1,200 professionals and serves companies across the globe.

Learn more about our Commerce Cloud integration with SAP.

Available on SAP Store

## About Retail TouchPoints

*Retail TouchPoints* and design: retail give all members of the retail world access to a vibrant community that combines insights, inspiration and opportunities to interact with their peers. We sit at the intersection of the art and science of retail strategy, providing granular data, high-value commentary, and aspirational success stories to help readers optimize customer experiences across all channels. Touching all facets of the retail ecosystem, including store experience and design, workforce management, digital marketing and engagement, and omnichannel optimization, our editorial content, multi-media resources and events take timely news and trends and transform them into tactical takeaways that meet the unique needs and priorities of our executive readers.

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