Competitive Advantages of Sales Tax Automation for Retailers

More retailers are trending toward automation to keep up with customers, compliance

Consumer confidence is on the upswing and there is a renewed energy around retail's future. Forbes hails 2018 as the year of retail renaissance, echoed by Deloitte's prediction that the industry is poised for transformative change. Ecommerce is certainly at the center of this change. Growing at a rate of 23% year over year, US retail ecommerce sales are expected to exceed $461 billion in 2018.[1]

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The ease and speed of ecommerce and mobile commerce mean consumers have more choices readily available. Competition is fierce and the pressure is on to keep customers happy and engaged. So, it's not surprisingly that 77% of retail CEOs are concerned about keeping up with the digital demands of their tech-savvy customers.[2]

A third of retail CFOs say they'll overcome this by automating more business processes this year.[3] It's a smart move. Highly automated businesses are six times more likely to have an annual revenue growth of 15% or higher.[4] Sales tax automation may not seem like the obvious choice to drive this growth, but for many retailers it can have a big impact on ecommerce success. By automating sales tax, you can be more responsive to customers and confidently go after new markets or sales channels without putting undue risk on the business .

Why sales tax is harder to get right for ecommerce sellers

The retail tax landscape has become increasing complex, making compliance more difficult. Last year, there were close to 40,000 tax rate and rules changes in US tax jurisdictions alone. Getting sales tax right in this inconstant environment requires extra vigilance. Applying incorrect rules, exempting taxable goods and services, or not using the proper forms and certificates can get you in trouble.

As a seller, it's your job to know the rules and apply sales tax where appropriate. With 16,000 taxing jurisdictions and millions of tax rules in the U.S. alone, this is a daunting task no matter how big or small your business.

"There are so many laws out there that change daily, monthly, yearly," says Heather Gravelle, tax manager for Furniture Row, a national home furnishings retailer. "We needed to outsource sales tax to make sure we were compliant."

Tax automation can alleviate undue burden or uncertainty around getting sales tax right. Choosing the right technology partner is key. SaaS solutions like Avalara are a great fit for retailers who operate in multiple states or online because they integrate with your online shopping carts and ecommerce systems so you can instantly and accurately apply tax rates and rules specific to any sale in any location.

Furniture Row uses Avalara's tax automation software to reduce liability. "It supports what we need as far as staying compliant with all of those states, jurisdictions and cities."

[1] *Statista 2018*
[2] *PricewaterhouseCoopers, 2016 Global CEO Survey*
[3] *2018 Retail Compass Survey, BDO*
[4] *Today's State of Work: At the Breaking Point, ServiceNow*

Nexus definitions are expanding, putting retailers at risk

12 states have or have proposed "economic nexus" laws, which require you to collect and remit sales tax on remote sales based solely on revenue or number of sales transactions. These states are Alabama, Indiana, Maine, Minnesota, North Dakota, Oklahoma, Rhode Island, South Dakota, Tennessee, Vermont, Washington and Wyoming.

As retailers grow, they are more likely to trigger nexus, a "physical presence" in a state that creates an obligation to collect and remit sales tax. As such, you need to pay closer attention to where customers and partners are located and ensure point of sale, ecommerce systems and shopping carts are set up to calculate the correct tax in each state and jurisdiction in which you have nexus.

Many states have expanded their nexus laws, which means activities you do every day such as advertise online, store inventory in warehouses, or use drop shippers or fulfill order using third parties could obligate your business to collect sales tax in states where those activities take place.

Additionally, 12 states have or have proposed "economic nexus" laws, which require you to collect and remit sales tax on remote sales based solely on revenue or number of sales transactions. These states are Alabama, Indiana, Maine, Minnesota, North Dakota, Oklahoma, Rhode Island, South Dakota, Tennessee, Vermont, Washington and Wyoming. The thresholds of economic nexus can be quite low. In South Dakota for example, $100,000 in annual sales or 200 separate transactions will give you economic nexus in the state.

Having to comply with state-mandated nexus laws can businesses beyond the threshold of managing sales tax manually. At this point, automation becomes a much more attractive – and necessary–solution for many sellers.

"We were collecting sales tax in three states where we had nexus," explains Susan Smith, finance director for Natural Health Trends, a global ecommerce and direct seller of premium personal care, wellness and nutrition products. "Then we started to collect tax on behalf of our distributors and that put us in almost every state. That was not something we wanted to take on in-house."

Smith says the company doesn't worry about calculating the right sales tax or preparing and filing individual returns for multiple jurisdictions with Avalara's software. "It's done for us. And we know it's correct."

[3] *Peisner Johnson*

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“As we grew, our affiliates created a presence for us in new states. Some states charge sales tax on freight, others don’t and each state has its own product taxability definitions and rules. “We wanted to be ready and comply properly. But we couldn’t be a tax expert in every state.”

– Bob Ramano, VP of Finance, Life is Good

Online sales channels can take retailers offline with tax compliance

More than half of Americans prefer to shop online and now spend 36 percent of their shopping budget on Internet purchases.[5] Taxing those online sales, however, remains a gray area – one that has cost states $26 billion in uncollected sales tax revenue and put undue risk on retailers to navigate state by state rules around whether or not to collect tax on remote sales.

Resolution may finally come in June when the U.S. Supreme Court rules on *Wayfair v South Dakota*. This landmark case will decide if the *Quill* physical presence standard still stands or if states can require online sellers to collect sales tax on all out-of-state purchases.

Until then, it’s important to note that all but eight states enforce some form of expanded nexus laws requiring out-of-state sellers to collect and remit sales tax on Internet and catalog purchases.[6] Amazon now collects sales tax in all 45 states with a state sales tax. If you sell through online affiliates or marketplaces like Amazon, eBay, and Etsy or use third-party fulfillment services like Fulfillment by Amazon (FBA) or drop shippers, be sure you understand how they impact your sales tax liability.

“When we built out our affiliate program, states were already beginning to consider this sufficient presence to create sales tax collection responsibilities,” says Bob Romano, VP of Finance for Life is Good, a national apparel manufacturer and retailer. “As we grew, our affiliates created a presence for us in new states. Some states charge sales tax on freight, others don’t and each state has its own product taxability definitions and rules. We wanted to be ready and comply properly. But we couldn’t be a tax expert in every state,” explains Romano.

That’s where tax automation pays off. It’s an extra layer of protection built-in to your ERP or ecommerce system that allows you to make strategic business decisions like adding new sales channels without worrying if they’ll impact your ability to be tax compliant.

Product taxability can be problematic for some retailers

Most tangible products are subject to sales tax in the U.S. However, product taxability rules and rates vary widely from state to state and change frequently. If that wasn’t bad enough, certain goods and services fall into a nebulous category called “sometimes taxable” where use can make a difference in how an item is taxed. This can make sales tax compliance particularly difficult for affected retailers.

[5] *Statista*
[6] *Multistate Associates*

“Certain states view functional products differently than fashion products when it comes to tax,” explains Scott Cohn, who served as VP of ecommerce for five years for Chinese Laundry, a popular brand of women’s footwear. “Different types of boots, for example. Some, like rain boots, could be considered functional, while others are purely fashion. Trying to figure out how all of that breaks down is cumbersome.”

That was a key decision to Chinese Laundry employing Avalara’s sales tax compliance solutions. “They help us figure out how each state charges tax on those various subsets of the products we sell.”

Different states tax these categories in different ways. So, while you may be tax compliant in one state or a set of states, selling in new states or introducing nexus could open you up to more liability. It’s a major challenge facing retailers, admits Cohn. “The only way to manage this would be to have a massive in-house team. Or do it systemically with software.”

The payoff of automating sales tax

For retailers, the research, calculations, filing, and reporting required for sales and use tax compliance is time consuming and resource-intensive. A Wakefield Research study found that companies employ six people on average to manage sales and use tax compliance, who spend upwards of 460 hours per year solely on sales tax-related activities. The study also found that 62% of those companies have hired additional staff to manage sales tax within the last five years and even with additional staff, time spent on sales tax compliance increased by more than 250 percent.

Automation allows retailers to be more agile and efficient in all areas of their business, including tax compliance. A survey of Avalara customers found that retailers who used Avalara’s tax automation software cut the time they spend managing sales and use tax by more than half. Avalara customers were also 90 percent less likely to overcharge customers sales tax and were twice as likely to passed audits without penalty.

Avalara manages sales and use tax compliance for more than 20,000 companies including top retail brands like Reebok, Bed Bath and Beyond, Dylan’s Candy Bar, AutoZone and 3,000 other leading retailers. More than 98% of the companies that implement Avalara’s software are still customers Avalara customers today.

If you aren’t automating sales tax with Avalara, what can we do to change that?

About Avalara

A privately held company, Avalara was founded by a team of tax and software industry veterans to fulfill a vision of delivering an affordable, scalable sales tax solution. Thus making what was not economically feasible in the past for mid-sized business not only affordable, but more accurate as well – all with the latest and most innovative technology available. From Bainbridge Island, close to Seattle, Avalara’s knowledgeable staff works tirelessly to help customers put the hassles of sales tax compliance out of mind. Avalara’s mission is to transform the tax process for customers by creating cost-effective state-of-the-art solutions. The company does so through integrated on-demand, Web-based software services that provide transparent transactions, accurate tax compliance, painless administration and effortless reporting.