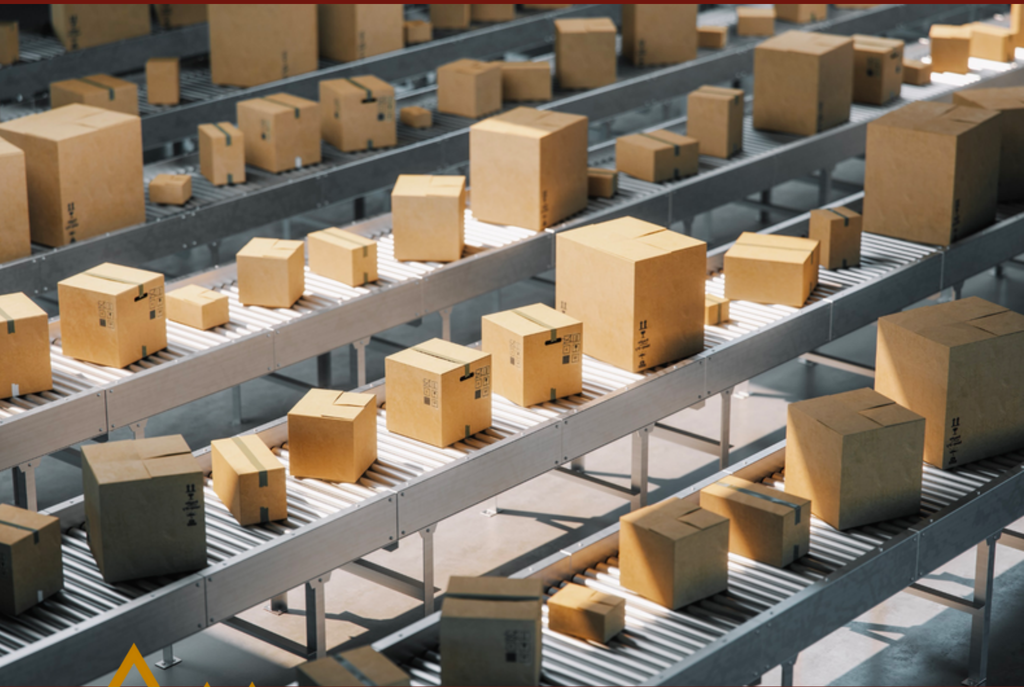
7 Accounting Struggles eCommerce Sellers Face

AND HOW TO OVERCOME THEM



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About the Author

Monica Roca-Quesada is an accounting professional with over 25 years of experience. Throughout her career, Monica has implemented financial systems and controls for large Fortune 500 companies such as Carnival Cruise Lines as well as helped dozens of small to mid-sized businesses and CPAs across the United States as a fractional CFO and Advanced Certified QuickBooks ProAdvisor.

INTRODUCTION

7 Accounting Struggles eCommerce Sellers Face

eCommerce is one of the fastest growing industries, with statistics forecasting online shopping revenue will reach $1.7 trillion in the U.S. alone by 2027. This makes sense given that there are an estimated 12 to 24 million eCommerce sites globally, with new entrants creating online storefronts each day.

Despite the growing consumer demand and popularity of eCommerce, all businesses won't see success and long-term growth. In fact, eCommerce businesses have a failure rate of 80% to 90%. Does this surprise you?

Whether you are considering opening your first eCommerce business or are trying to find effective strategies to stay afloat, understanding the common accounting struggles eCommerce businesses face can help you achieve long-term growth and avoid becoming part of the 90% of businesses that fail.

Misreporting Sales Tax

#1

The first area that eCommerce sellers struggle with is sales tax. Following the Wayfair vs South Dakota Supreme Court case, states may now impose sales tax on purchases from out-of-state sellers, even if there is no physical presence in the state. This means that all eCommerce sellers, such as Amazon FBA sellers and Shopify sellers, need to be tracking the sales made in each state.

Receiving a sale from another state doesn't always mean you need to file and pay sales tax in those states. Most states impose a nexus, which is a threshold that sellers must exceed before they are required to remit sales tax. Each state has a different nexus level, making it important to know each state's rules.

Determining if nexus has been met is only the first challenge when it comes to sales tax for eCommerce sellers. In fact, collecting and remitting sales tax is another challenge. Some platforms, like Amazon and Walmart, are considered marketplace facilitators, meaning they collect and remit sales tax on your behalf. However, other platforms, like Shopify, place the burden on you as an eCommerce business owner.

Taking on High Interest Cash Advances

#2

Making your first inventory purchase can be costly, especially when volume discounting is involved. The average cost of starting an eCommerce business is between $5,000 and $10,000. Do you have this kind of cash on hand? If not, you may need to seek outside investments to raise the needed capital to make your first inventory purchase.

One of the most common funding strategies that eCommerce sellers pursue is high interest cash advances. This type of financing can be secured through credit card companies that allow a cardholder to immediately withdraw cash. However, the interest rates are stiff with this financing method, reaching as high as 30%.

High interest cash advances are a common mistake made by eCommerce sellers. Let's say you take a cash advance of $5,000 with a 25% APY. Even if you are able to sell enough to pay back the $5,000 after six months, you will still be paying $625 in interest. Instead of using high interest cash advances, you should look into outside investments, such as through financial institutions or private investors.

A loan or line of credit through a financial institution reduces the interest rate you are charged and comes with more flexible terms, such as a three-year payback period. This not only reduces stress surrounding paying off the balance, but also contributes toward building a strong credit history for your eCommerce business.

Signing Revenue Based Financing Agreements

#3

Although you should always have confidence that your business is going to succeed, betting on your business isn't always the best idea. Similar to high interest cash advances, revenue based financing agreements can put your business in a tricky situation with no clarity into your cash flow.

A revenue based financing agreement is a contract between you and a third party, which is usually the platform you are doing business on, like Amazon, Shopify, or PayPal. In exchange for an upfront cash advance, the platform will deduct payments from your daily sales.

In the e-commerce world, revenue based financing agreements are being used daily. These agreements are not only expensive, but also difficult to deal with accounting-wise since they often don't come with set schedules.

All major e-commerce platforms have begun offering this financing method, looking attractive on paper until your business has no idea what to expect from a cash flow perspective. You could have dozens of transactions in any given month for these types of daily repayment financing. If the sporadic payments weren't trouble enough, interest rates can reach upwards of 10%.

This makes it difficult to strategically plan for growth, implement a budget, and truly understand where your business stands. As with cash advances, you should consider going the traditional route before signing a revenue based financing agreement.

Recording Wrong Inventory Costs and Prepayments

#4

Inventory is another accounting struggle for eCommerce sellers. When you place an order for inventory, the amount does not go directly to your income statement as an expense. Instead, the inventory cost goes to the balance sheet until the item is sold. With rising prices, it's important to keep track of the unit cost of each good, as the price can differ between items.

When the wrong unit cost is moved to the income statement, you not only have misreported cost of goods sold, but your ending inventory balance as well. Many eCommerce sellers can avoid this issue by working with an accounting professional or investing in inventory management software that tracks each product.

Moreover, shipping delays have caused another accounting issue for eCommerce sellers. Vendor prepayments are also not reported on the income statement. These costs go to the balance sheet as a current asset until the goods are received, when they will then be moved to inventory. Understanding the proper cut-off and placement of these transactions is important to generate accurate financials and tax returns.

Focusing on the Wrong Advertising

#5

Since most eCommerce businesses don't have a physical brick-and-mortar location, advertising is a major expense that can lead to unprofitable operations. Customer acquisition cost is one of the top expenses in eCommerce businesses, with studies suggesting an average CAC of $49.06. Of course, this average varies based on your industry and product selling price but expect to pay a decent amount on CAC.

One way to reduce your CAC is to improve your lifetime value, known as LTV. Lifetime value is how much money you have made from a customer over the course of your relationship. eCommerce sellers struggle when they focus solely on the initial interaction with customers and neglect to nurture the relationship to achieve higher LTV percentages.

Take a look at your income statement to see how much you spend on advertising. Are you taking advantage of free outlets, like creating a TikTok video or posting on Instagram? Utilizing both paid and free marketing channels can help you reduce the CAC and improve the LTV in your eCommerce business.

Neglecting to Analyze Profitability

#6

Sales do not equal profit. One of the challenges eCommerce business owners face is differentiating between sales and profit. Sales are everything you sell without factoring in any expenses. On the other hand, profit includes cost of goods sold, selling expenses, administrative expenses, general expenses, and occupancy expenses.

Analyzing profitability gives you insight into where you can cut costs to improve your margins. There are three calculations you should perform on a regular basis to analyze your eCommerce profitability.

1. Gross Margin – This calculation takes gross sales minus cost of goods sold, which are costs directly related to the sale of your principal product or service, like purchases. Then divide this number by revenue. This tells you how profitable you are before factoring in operating expenses.

2. Operating Margin – This metric takes your gross margin in dollars and subtracts operating expenses, like bank fees, office wages, and professional fees. Then, you divide the outcome by your gross margins in dollars.

3. Net Margin – This calculation compares the total income or loss for the period to sales. Net margin factors in other income and expense items that don't occur in the ordinary course of business, such as the loss from discontinuing a product line or interest income.

Many eCommerce sellers focus solely on making sales and neglect to consider operating expenses. By analyzing the profitability of the business, you can make informed decisions on which segments are underperforming and where actionable change is needed, setting you up for long-term success.

Foregoing App Integrations

#7

A common pitfall that eCommerce sellers face is poor app integrations. Technology has come a long way in the past decade, making it important to leverage these shifts to improve visibility, productivity, and efficiency in your eCommerce business. At a minimum, you should have app integrations to your accounting software, such as from bank and credit card accounts. This not only reduces a majority of the data entry burden but can also lead to more accurate records and real-time data.

Additionally, regardless of if you have a physical warehouse, it's important that you have an inventory tracking application that connects to your accounting software. This ensures that the correct amount of cost of goods sold and inventory is on the financial statements.

Many eCommerce sellers gravitate towards QuickBooks Online *for their general accounting software because of its cost-effectiveness and user-friendly features. If you are interested in learning more about which accounting software programs are best for your business, reach out to schedule a consultation. Nevertheless, without the right app integrations working in the background, you aren't properly positioning the accounting of your business for success.*

Overcoming These Challenges

The good news is that these common accounting struggles can be overcome, leading to a greater chance of avoiding being part of the 90% of eCommerce businesses that fail. To find viable solutions to these problems tailored to your eCommerce business, reach out to Agile Planners today.

Our team of experts has been helping eCommerce sellers navigate through accounting challenges, resulting in less stress, more transparency into financial health, and greater profitability potential.

Visit www.agileplanners.com today to learn more.

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