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Current Challenges Facing Retail Sector

or how to effectively implement the on-line sales channel for a conventional shop

E-commerce Report 2011

pwc

This Report was compiled in collaboration with our clients to whom I would like to extend my thanks for their commitment and their important contribution on the e-commerce market.

I would also like to thank the group of our PwC experts who contributed most to the development of this report.

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Introduction

I present you with a practical guide of the Report on the e-commerce market, compiled by PwC experts. The Report offers a comprehensive discussion of both challenges facing the implementation of the on-line sales channel as well as business and legal, accounting and tax issues arising in e-commerce.

Chapter I focuses mostly on the on-line channel implementation strategy. It confirms that perceiving it as a simple continuation of traditional sales is faulty as it requires taking into account the specificity of the virtual world. The entire sales process, from offering the product to the customer through its delivery becomes a challenge to business and it requires an innovative approach. Previous management techniques turn out to be ineffective as they prevent the business from attaining optimum benefits from the operation of the on-line sales channel. Chapter I also offers you remarks on, among others, the technical concepts of developing e-shop websites, including the most important issues for potential customers.

The legal part of the Report concentrates on the entrepreneur – consumer relations. A specific characteristic of e-commerce is that the buyer is unable to see the goods before purchasing them. Thus, the consumer's rights and entrepreneur's obligations have been defined in a particularly detailed way. On the one hand, the Report presents a catalogue of rights vested in the consumer, regarding – among others – concluding agreements or returning goods. On the other, it discusses the obligations of the entrepreneur in regards to informing the consumer of the transaction terms or personal data protection of e-shop users.

The following chapter is an overview of potential problems that may arise from running an e-shop in the area of accounting. The subjects discussed include the timing of revenue recognition, return of goods by the buyer or introduction of loyalty programmes. All these subjects can be approached differently, which requires that e-shops develop their own relevant accounting policies.

The final part of the Report concerns e-shopping from a tax perspective (i.e. in terms of VAT and income tax). In regards to VAT, we focus on the moment of the tax obligation in different purchasing and payment situations, including customer's refusal to accept the goods ordered.

Furthermore, the income tax review includes such issues as recognition of costs arising due to implementation of a new sales channel, allocation of costs related to on-line order sales or the settlement method for the goods returned. In the part regarding Corporate Income Tax, the Report also presents information on operating the cross-border on-line channel, i.e. in collaboration with foreign entities or by offering goods abroad.

You should remember that the e-commerce market in Poland is new and relatively poorly recognised. However, rapidly growing turnover volumes as well as increasing number of on-line sales customers indicate that undoubtedly this will be the market of the future. Therefore, engaging in this market is of key importance for entrepreneurs.

Agnieszka Ostaszewska
Partner, Commerce and Consumer Goods Leader

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On-line sales channel: innovation or necessity?

On the one hand, if the Internet sales are introduced very early, before others do this, it may turn out that this change is going to be like every innovation – you never know what the effects would be like. There have been a lot of pioneers of e-commerce on the market who failed to develop the business but who "released" many talented professionals on the market. On the other hand, if the decision is taken too late, the fight for the position on the market may be inevitable.

José Bonito
Customer Management Director
Makro Cash and Carry Polska S.A.

The pace of development of Poland's information society and ever growing number of Internet users who surf the web looking for information on products and services make on-line sales channel implementation more a necessity than just innovation.

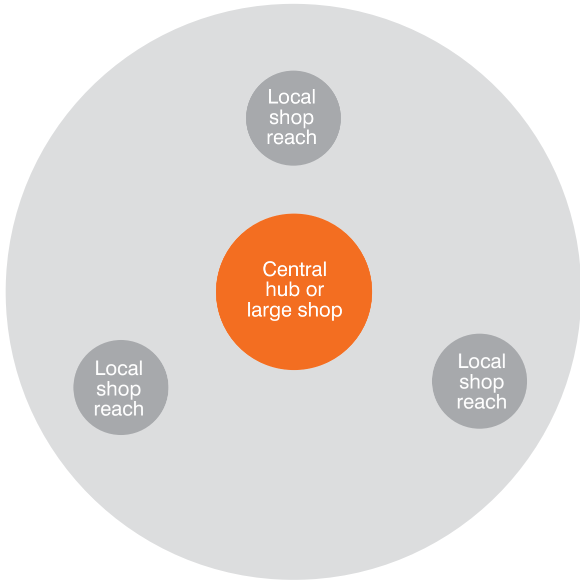
In Poland, 96% of enterprises and more than 63% of households already have unlimited access to the Internet[1]. Among enterprises, 65.5% declared in 2010 that they had their own website, while 9.9% of them (as compared to 7.1% in 2009) admitted their website was aimed at ordering or booking goods or services on-line.

The value of the Polish e-commerce market is growing and was estimated in 2010 at more than PLN 15.5 billion, with 24 million Internet users[2].

[1] Społeczeństwo informacyjne w Polsce [Information Society in Poland]. Results of statistical research from 2006–2010, Central Statistical Office in Szczecin.

[2] Internet Standard, Commerce Report.

On-line shop reach



Source: PwC UK Study

Statistics clearly show that on-line presence is becoming a necessity rather than a way to stand out in the market. The development of the virtual world provides enterprises with new opportunities to present and offer their products and services.

The most important business benefits of implementing the on-line sales channel include:

- Business development by extending the customer base, which means winning customers that cannot be reached by traditional shops and taking customers interested in on-line shopping over from competitors not offering the on-line functionality. Possibly, the Internet offers business growth potential by providing access to an extremely wide audience, which is impossible with other sales channels.

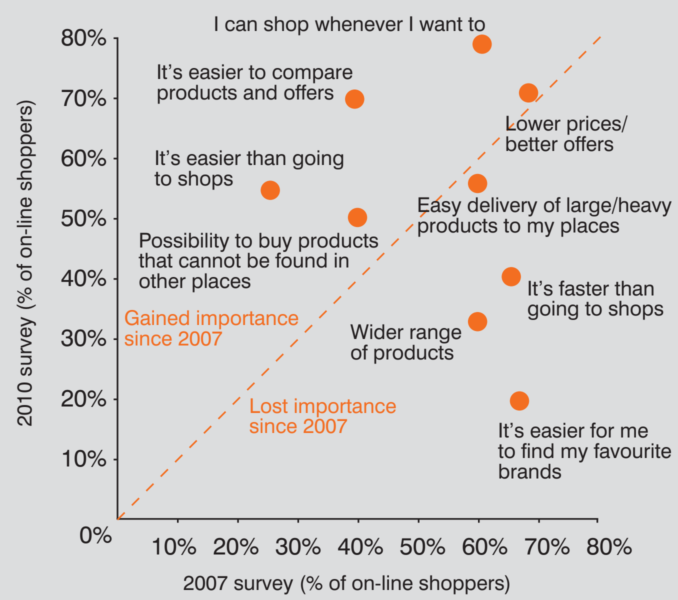
Internet is inevitable. It is a wave, a trend that cannot be fought against but requires adaptation to the evolving situation. It is harder and harder to distinguish a TV set from a computer as more and more TV sets offer web browsing capabilities. The question is when will these two devices become one? Almost 700,000 people in Poland have no TV sets at home, and they watch news and movies using the Internet.

Adam Ołowiańczyk
Media Saturn Holding Polska Sp. z o.o.

What do we associate e-commerce with? With the "fast-cheap-reliable" principle. Only e-commerce can meet all the three requirements combined.

Michał Grom
E-commerce Services Sp. z o.o.
(empik.com, smyk.com, empikfoto.pl, ...)

What factors make you shop on-line?



Source: PwC UK Study

- Improvement in customer service level by better meeting customer needs. The on-line sales channel enables to meet growing customers' requirements related to non-stop shop availability. The need was confirmed in a survey conducted by PwC in the United Kingdom, which has been holding regular surveys of customer on-line shopping behaviours since 2007. The survey showed that the possibility to shop whenever you want to is becoming an increasingly important reason for shopping on-line.
- Better management of existing customers. e-Business leaders perceive the web not only as an additional sales channel: e-commerce can support the entire customer retention cycle. The Internet is an unlimited source of gathering customer information on their behaviours and preferences. In an on-line shop, we can trace the customer's navigation on the site and their interest in specific sections of it or the way they combine products. We can also ask the customer to provide their opinion, which on-line shoppers are more willing to do than customers at traditional shops.

Moreover, the on-line sales channel can help us test new products and new marketing techniques.

How to effectively implement the on-line sales channel to a conventional business?

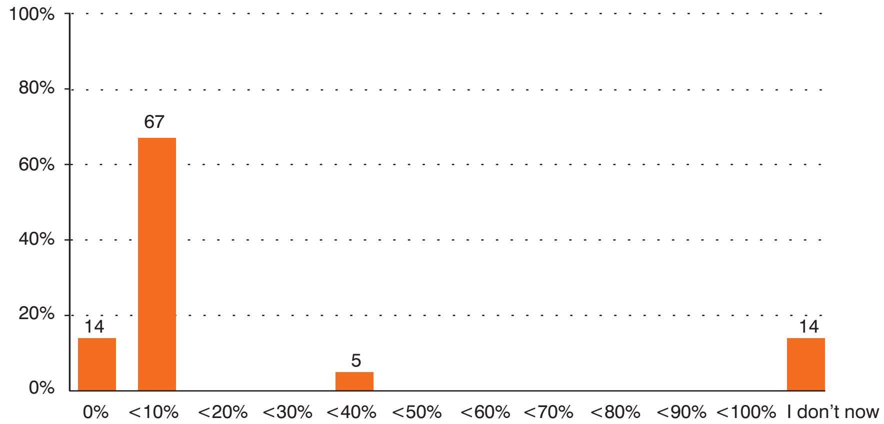
A survey conducted by PwC in the Netherlands showed that most companies operating traditionally in retail fail to use the potential of on-line sales channels due to a lack of strategic approach to their implementation.

A very important thing when implementing the on-line channel is to do it in such a way as to avoid damaging the traditional channel that we have. That is why internal cooperation is so important when compiling a consistent commercial offering.

Adam Ołowiańczyk
Media Saturn Holding Polska Sp. z o.o.

1. Reasonable on-line channel implementation strategy is one of the key success factors

What is the percentage share of on-line shop turnover in 2009?



Source: PwC Netherlands study

The survey PwC conducted in the Netherlands among entities operating traditionally in the retail sector shows that as the on-line channel is perceived a necessity, its implementation is carried out in a hurry, as a result of which strategic planning aspects seem to be overlooked. As a consequence, the on-line channel becomes a simple imitation of the traditional path in terms of the range of products offered, prices and promotional campaigns, with no regard to its specificity. Such an approach results, in among others the fact that on-line sales channels provide much lower revenue than traditional channels.

1.1. Strategy development should be started with definition of strategic goals for the on-line sales channel

Implementation of the on-line sales channel involves the organisation's core processes. Thus, it is worth taking some time at the planning stage to define the goals the organisation sets for the new distribution channel. A precise definition of these goals enables the selection of the relevant Internet presence model that best meets the organisation's requirements and determines the scope of changes that the organisation needs to face as a result.

In order to define a list of goals set for the on-line channel, providing answers to the following questions may prove helpful:

- What do the Internet and related technologies mean for the business?
- What type of Internet presence would be considered: presentational or transactional?
- How does the implementation of the on-line sales channel fit in the current competitive strategy? Do you have to change the elements of the previous strategy?
- How does using the Internet fit in the current IT systems strategy?
- What benefits would be expected from implementing the on-line sales channel?

The strategic goals defined should be further elaborated upon in the context of three principal aspects of a new sales channel implementation: brand growth, geographical market growth and extension of customer base.

Brand growth

Depending on the strategy adopted, the on-line sales channel may meet the goals consisting in existing brand growth, its repositioning or developing a new brand and launching an entirely new brand on the market. Each time, this will be a strategic decision for the implementation of which the on-line sales channel will become a tool, not a starting point.

Geographical market growth

In the context of market growth, it should be decided whether the aim is to further penetrate the current market or to grow it geographically. This should partially determine the look and feel of the website, its functionalities and the marketing strategy. The decision also predetermines any possible changes to the supply chain organisation.

Customer base extension

In regards to the customer base, the basic strategic decision is to define goals towards the target customer group. It has to be decided whether the new on-line sales channel will be used to offer our product to customers with the same profile as our current customers or whether what we aim at is to extend the customer base outside the currently dominating profile. The decision will provide for further product range, price and marketing strategies.

1.2. Integrate or separate?

Having both the traditional and on-line sales channels, it should be decided whether they should operate as independent structures or be functionally integrated.

It is hard to decide whether to integrate or separate as between these two extremes there is a plethora of possibilities and configurations out of which the organisation is to choose the appropriate model.

The decision should depend on the goals that have been defined for the on-line sales channel and the operational capacity of our organisation. In addition, the decision-making process should be based on an analysis of possible synergies in specific sales channel integration options. Focussing on fundamental issues, it should be decided to what extent the basic areas of new channel management, operating processes and brand management should be integrated.

New channel management

An answer to the question whether the function should be integrated within the business or separated depends on the organisation's business model and the management's attitude towards the on-line channel. Companies that see their future as dependent on their presence on the Internet or in general as following a multi-channel strategy will, in most cases, strive to consistently manage the channels. However, businesses concentrated more on traditional sales can appoint a separate team to manage the on-line activities.

Both solutions have their pros and cons. An integrated management team will certainly reconcile strategic goals between the two channels better, using synergies and the knowledge acquired thanks to the new channel. On the other hand, an independent team will be more focused on the new channel requirements, avoiding conflict between the two distribution paths. Of key importance when making the decision and implementing it is to select the proper competences of people responsible for managing the channel or channels. Given the stage of development of the Polish e-commerce market, the availability of specialists experienced in introducing the organisation to the on-line sales channel may be limited, while the specific nature of the business makes managers historically responsible for traditional channels not competent enough to manage on-line channels.

The feedback that we get from customers shopping at Alma24.pl enables us to enhance processes in the traditional shop in terms of the expected product quality, range of products or their organisation on shelves, for instance.

Stanisław Krzaklewski
Alma Market S.A.

Can on-line channel implementation have a positive impact on the off-line channel? Our experience shows that these two channels will always interfere. Yves Rocher conducted a survey in Belgium, showing that 20–30% of customers who saw products on-line came to buy them at a regular shop.

Jakub Kuśpit
Yves Rocher Polska Sp. z o.o.

Questions that might support the decision-making process:

- Do current managers have enough knowledge and experience to be able to manage the new sales channel?
- Are current managers able to assess e-commerce initiatives with entirely different indicators than in the traditional channel?
- To what extent will the operations be integrated?
- Will we offer on-line sales under the same brand as in the traditional channel?
- Is there a risk of a serious conflict arising between the channels?

Operational processes

Separation of operational processes enables the organization to create a new, unique model of operation adjusted to the specific requirements of the on-line channel, but prevents economies that are available when the operational processes are integrated.

A decision on the level of integration of operations largely depends on the IT systems owned by the organisation and on its physical infrastructure. When the traditional and on-line channels are harmonised effectively, integration of operational processes can provide significant economies as compared to the two channels being managed separately. Savings can mainly be expected in terms of labour costs, stocking and delivery costs.

Labour costs in the traditional sales channel would be related to such duties as checking information about products, comparing information, availability monitoring, filling in customer registration forms, orders or complaint forms, and provision of after sales services that can be largely transferred to the customer in the on-line channel. For customers who are fluent Internet users this is a solution that they accept to be able to shop or arrange complaint issues at a time they find convenient from home, without the need to visit the shop during its working hours.

Economies related to stocking result from the lack of necessity to keep extensive stocks of rarely purchased products as the requisition for such products is made on-line. The possibilities to model product range availability and receipt policies in specific channels are extensive and will be strongly contingent upon the sector. However, it may be stated beyond doubt that so-called luxury products or slow-moving goods can be offered in the range without the need to keep expensive stocks. Delivery-related savings can be obtained as a result of using a traditional point of sale as a point of delivery of goods ordered on-line or as a storage to locally serve on-line channel customers.

Integration of operations resulting in sharing costs between both channels enables the building of cost advantages over shops that operate only virtually, and facilitates reaching customers who prefer to collect their goods personally.

Moreover, integration of customer service systems and sales systems enables gathering information on the demand and needs of our customers in all the channels we serve. The Internet provides unprecedented capabilities of monitoring customers' behaviours; how they navigate on the website, what information they look for, at which stage they abandon their "shopping carts". What is more, the Internet community, to a much wider extent than the traditional customer population, like to share their opinions and comments, especially given that providing feedback on-line is not as time-consuming as filling in questionnaires in shops.

Questions that might support the decision-making process:

- Can the existing sales system be easily adjusted to the requirements of the on-line channel?
- Are the existing IT systems sufficient to provide a platform for building e-commerce capabilities?
- Is any of the sales or IT systems offering competitive advantage?

Brand

A decision to integrate or separate the brands is determined by the flexibility and willingness to build trust. If a brand that is known from traditional distribution in the on-line channel is used, the brand becomes immediately reliable, the interest in the brand rises, which is followed by an increase in revenues. This results from the physical presence of a traditional shop where customers can, for instance, return the goods or file a complaint, which makes them feel less anxious about finalising the transaction. In Poland, this may be especially important due to the current stage of development of the Internet society. Still, there are many customers who are afraid to shop on-line, and especially to shop on-line for valuable products. In addition, traditional sales channels in selected sectors, such as furniture, provide the customers with the possibility of seeing the product before the purchase despite the fact that the entire transaction may later be finalised on-line.

It is worth noting that a decision to integrate a brand leads to a cross-exchange of customers between the two channels, which enables offering them additional on-line services. These may be comparison tools that enable a simple comparison of product features, community forums or expert advice who present how to assemble a product or possible product applications, and finally the possibility to extensively present products using various multimedia tools (videos, arrangements, etc.).

However, it should be taken into account that a decision to integrate the brand in sales channels may eventually reduce the flexibility of the on-line channel. For example, with the same brand, the price in the new channel should be similar to the prices in the traditional points of sale, otherwise customers can become confused and can object. What is more, it will be more difficult to adjust the offering to the needs of a different customer segment without infringing upon the brand's integrity.

Questions that might support the decision-making process:

- Can the existing brand be easily transferred on-line?
- Would the on-line offering be significantly different from the traditional one in terms of assortment and the target market segment?
- Would on-line prices have to be different than prices in traditional points of sale to meet the benchmarks set by the competitors?
- Do traditional and on-line channels combined foster building trust better than the on-line channel alone?

To sum up, when implementing an on-line distribution channel, one should start with answering the question of how the electronic media in the business model are supposed to be used and then define the operating goals for the new channel based on that. The final step is to plan implementation by determining the level of integration between sales channels. Such a process flow will ensure that the decisions made will support the organisation's strategy in the long term, and the form of implementation will provide for the expected benefits.

The importance of trust depends on the sector where the shop operates. For foods, where reliability is paramount, it is better to stick to your traditional brand.

Stanisław Krzaklewski
Alma Market S.A.

Price comparison tools offered by on-line shops are a corporations' nightmare. There are two ways to avoid posting "shop" prices in comparison tools: either enter the market with your own brands, or start selling on-line under a different brand.

Krzysztof Szymański
Castorama Polska Sp. z o.o.

People who manage and create on-line sales channels need to "feel the Internet" and understand the consumer's behaviours. The consumer feels anonymous on-line and thus acts less predictably.

Krzysztof Szymański
Castorama Polska Sp. z o.o.

One of the main problems in implementing on-line sales in an organisation that has so far operated only traditionally is to adjust the organisational structure and to change the way of thinking about business.

Stanisław Krzaklewski
Alma Market S.A.

2. How to adjust organisational structure to the new reality?

2.1. Organisational structure

The on-line sales channel fosters an organisational structure that concentrates on customer relations, and thus is a structure that goes beyond groups of products. It is accepted that the higher the importance of the on-line channel for the organisation, the more fundamental changes to its structure are required.

However, the scope of changes would depend on the decision whether to integrate the sales channels or not and – most importantly – on the management function. The higher the integration, the stronger the interdependencies and the need to cooperate, which implies the need to establish interdisciplinary teams instead of units that have so far operated in the traditional sales channel. Where no integration is assumed, changes to the structure can be limited to establishing new functions that would serve the new sales channel somewhat independently from each other.

For an organisation implementing an integrated on-line sales channel with a shared brand, the necessary modifications to the organisational structure include:

- establishment and continued improvement of the organisational structure focussed on performing CRM functions,
- establishment of new functions or extension of competences of employees who have the knowledge and experience in individual operational areas,
- change of the organisational culture to a more flexible and open to change. The Internet is a very dynamic medium that constantly evolves and where customer behaviours are not easily predictable. Effective competition requires keeping the pace with the current trends or even setting trends.

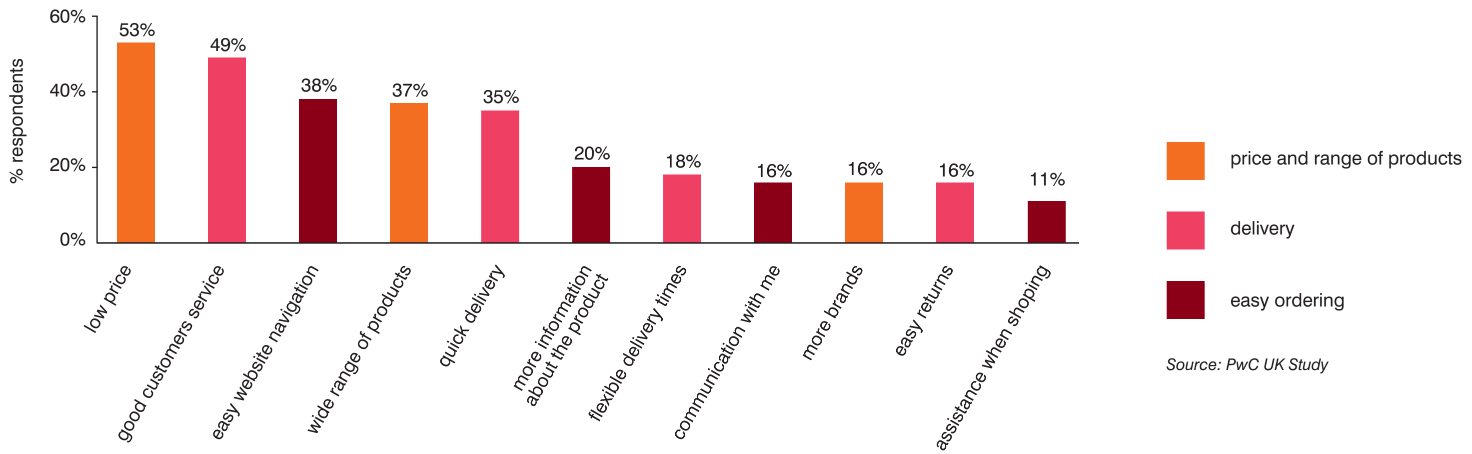
There also appears an issue of allocating new responsibilities to functions already operating in the organisation. Policy regarding the issue indicates the organisation's approach to e-commerce. For example, allocating key new channel development competences to the IT function may indicate a limited on-line presence strategy (e.g. only a website for information purposes) or a plan to create a simple continuation of the traditional sales. Establishment of an independent function, however, confirms the organisation's pursuit of wider and more innovative presence on-line.

2.2. Competences

As stated before, competences necessary to build an on-line sales channel are not consistent with the management of operations in the traditional channel. e-Business forms an environment that enables customers to freely compare prices, reduces the complexity of transactions and facilitates access to information.

Given increased competition, the ability to acquire, configure and use key competences in this area becomes of paramount importance. In order to make the new channel implementation successful, relevant competences should be provided already at the initial stage of the project. This will enable to plan a relevant strategy for the on-line channel in the initial stage of the project. The consequences if the stage is missed were described in the strategy part, indicating that following traditional channel solutions automatically may significantly reduce the benefits and opportunities provided by the implementation.

Reasons to shop at the same on-line shop, 2007 (UK)



Source: PwC UK Study

Added value services such as a forum, presence in social networking services or advice to customers are not a big burden for the organisation but at the same time they constitute a good way of contacting the most committed customers.

Stanisław Krzaklewski
Alma Market S.A.

Analogically, running an operational on-line shop itself requires competences that are absent in an organisation that have so far traded in the traditional distribution channel. These are:

Competences in building websites for on-line shops: usability

One of the core criteria for choosing an on-line shop is – in addition to prices and service level – the functional character of the website, called "usability". This is confirmed by the survey conducted by PwC in the United Kingdom.

According to Jakob Nielsen, one of the first promoters of the concept, usability is made up of five elements:

- learnability – how easy it is for users to accomplish basic tasks the first time they encounter the system,
- efficiency – once users have learned the website, how quickly can they perform tasks?
- memorability – when users return to the website after a period of not using it, how easily can they re-establish proficiency?
- errors – how many errors do users make, how severe are these errors, and how easily can they recover from the errors?
- satisfaction – how pleasant is it to use the website?

Competences in terms of usability are unique for Internet businesses and because of the importance of the above website parameters, it is necessary to acquire these competences for an on-line launch project.

The stable and strong brand of a "brick-and-mortar" company is a very useful asset in the process of e-commerce implementation. The traditional stores are very helpful in building the trust on the Internet.

José Bonito
Customer Management Director
Makro Cash and Carry Polska S.A.

It is really difficult to get on-line content. A good idea is to define obligations regarding on-line content already at the stage of agreements with suppliers.

Entering social media requires a good specialist and good regulations. The service is frequently outsourced.

Krzysztof Szymański
Castorama Polska Sp. z o.o.

Competences in creating on-line service content and scope of information

Competences in creating on-line service content and scope of information are understood as the ability to provide the customer with knowledge about the product, service and the company in a way that is transparent on the one hand, and on the other – enables saving time. The more types of customer in the customer base, the harder it becomes. Because customer attrition is explained by insufficient description of products and low comparability, richness of information is certainly a success factor of a sales channel. However, such competences require knowledge of both data availability and issues related to copyright, and of customers' requirements regarding information.

Competences in on-line marketing

Despite the fact that most traditional organisations hold their marketing campaigns also on the Internet, having a transaction-supporting website opens a gamut of new possibilities, especially in terms of image building and presence in the social media. This type of marketing is highly complex and the probability of having such competences in the traditional sales channel seems low.

Competences regarding on-line transactional processes, in particular the payment process

High competences in the area reduce sales costs and increase the efficiency of transactions. Also, an order monitoring function enables tracking of the entire delivery process, which enhances the customer experience. Integration of transactional processes with back-office operations enables the customer to check product availability and to select an alternative, which enhances cross-sales and up-sales.

Competences in terms of active customer support regarding any possible aspects, both before and after the transaction

Such an ability is directly related to satisfaction, thus it is important to offer support to the customer automatically by e-mail right after the transaction. This communicates to the customer the high level of customer service and confirms the reasonableness of choosing the on-line channel.

2.3. Detailed supply chain solutions can be decisive to the new sales channel's cost efficiency

What makes on-line sales channels so special is the fact that time flies "faster" on the Internet than in a traditional sales cycle. To gain competitive advantage, companies care more and more about the product lead time, the packaging, labelling and delivery of the product. The time of order delivery has a significant impact on the sales result. E-commerce also requires much greater involvement in relations between the seller, suppliers and customers who are connected by the Internet. The relations provide for such a level of interaction that has never been attained in the traditional sales channel. All the elements make designing a supply chain organisation for the on-line sales channel even more challenging.

The supply chain refers to the flow of physical goods and the related information from the source to the customer. The main activities in the supply chain are as follows:

- Production planning/supply planning,
- Purchasing,
- Resources management/stock controls,
- Distribution,
- Sales forecasting.

When a company decides to develop the on-line sales channel, a key decision needs to be made to select the relevant supply chain model. The solution depends on many factors and the character of the business. Of importance here are the structure and location of suppliers, range of products, product storage requirements, importance of delivery time, area of business and many more.

Cooperation with suppliers

The challenges that businesses starting up on-line sales are facing are at the same time challenges to their suppliers. Today's on-line business is characterised by high customer expectations towards product availability. This means that competitive advantage is gained by those entrepreneurs who can effectively build supplier – seller relations.

The supplier cooperation model depends on what product range the enterprise is selling and what the business' area of operation is. Also, an important element that determines the model is whether the target customer buys goods from one or multiple suppliers in a single transaction. Of key importance is the fact whether the company sells concurrently in the traditional sales channel, too.

Cooperation with the suppliers can have one of the following three forms:

- Delivery to the seller's warehouse of such a quantity of goods as the seller expects to sell within a specific time period

The model is characteristic of shops that sell a wide range of low-price products from multiple suppliers. A typical example are on-line shop chains offering foodstuffs and hardware goods. Such a range of products requires almost immediate product availability for order picking and sending to the customer. The biggest challenge in such a method of selling on-line is to maintain the optimum stock levels through short- and mid-term delivery planning.

In the food industry, this is especially relevant for fresh products. In this model, relations with suppliers are based not only on internal sales planning but also on shared forecasting of demand for specific products from the seller's range. Having the supplier prepared for specific quantities of products enables the supplier to reduce warehousing costs, thus reducing acquisition prices for the seller.

- Delivery to the seller's warehouse of such a product quantity as to meet the requirements arising from orders placed by target customers

The model is used most often in such sectors where the product range is highly differentiated and the purchase of a single product is of a significant value. For example, the model is typical for the construction industry where keeping large amounts of differentiated products means high costs of freezing capital and warehousing. Swift deliveries in this model are possible if the supplier has consolidated stocks for many customers or is highly flexible in manufacturing or obtaining a given range of products from the supplier's stock.

- Delivery directly to the end customers, without using the seller's warehouse

A direct delivery model, also called "drop shopping", is one of the logistic models available when outsourcing supply chain services. It applies when the goods are delivered directly to the end customer by a supplier cooperating with the seller. This model consists in the seller's acquiring customers, gathering orders and sending them to the supplier who arranges goods delivery itself. The model requires the closest cooperation between the seller and the supplier. This is a consequence of the fact that it is the supplier who bears responsibility and controls all the logistic activities on behalf of the seller. This refers to elements such as proper labelling of products, keeping delivery promise or accepting money from the end customer.

Therefore, in the direct delivery model, of key importance is the proper selection of and close cooperation with the supplier.

In selecting a model that will best match an on-line sales channel, the following questions should be answered:

1. What range of products will be sold in the on-line shop?
2. What are the relations with the suppliers?
3. How precisely the sales levels can be forecasted?
4. What delivery times will our customers accept?

Entering the on-line sales channel is facilitated if we have good relations with our suppliers as they are more willing to accept shorter lead times, and thus the need to keep higher stocks.

Krzysztof Szymański
Castorama Polska Sp. z o.o.

Promoting our Tesco on-line service, we emphasise such advantages of on-line shopping as time efficiency but also quality of products provided (in particular frozen food, which requires proper transport conditions).

Grzegorz Juszczyk
Tesco (Polska) Sp. z o.o.

For Yves Rocher, a great aid in implementing on-line sales was long-standing previous mail order sales. Building on the mail order channel, we could use the payment systems already in place, and our effective delivery system.

Jakub Kuśpit
Yves Rocher Polska Sp. z o.o.

Of particular importance in the white and brown goods sector is to provide the customer with support in the form of a website containing product information so that the on-line shopper can make the right choice.

I believe that establishing an effective on-line sales channel with a product-presenting website may also strengthen sales in the traditional channel.

Adam Ołowiańczyk
Media Saturn Holding Polska Sp. z o.o.

Picking orders

Various business models and strategies also determine the way the supplier picks the orders.

If on-line sales is a new method of selling, in addition to the traditional channel, enterprises often use synergies between the two channels and pick orders using stocks kept for the purposes of traditional sales. In such a case, the synergies of scale enable companies to reduce the necessary stock levels, however, it requires the planning functions in both business areas to be integrated. Such a model is typical of large retail chains selling fast moving consumer goods.

A solution that may be used when picking an order made up of products from different suppliers is called “cross docking”. It is a situation where the goods delivered to the warehouse are immediately handled and picked with other ordered items and almost immediately shipped to the end customer. This enables to avoid warehousing, which reduces total costs in the supply chain. This enables companies to avoid warehousing, which reduces total costs in the supply chain. However, it requires precise synchronisation of all the processes related to receiving and dispatching goods.

Delivery

Deliveries to end customers are one of the main challenges facing on-line sales channels. Deliveries have to take into account of the nature of the business, its scale and type of products sold. The existing delivery models include own transportation or outsourcing transportation services, including the most popular form of outsourcing: courier deliveries. An increase of the share of this delivery method explains a reduction in the prices of such services, in particular for companies signing long-term agreements, and – which is of key importance – short delivery times and high effectiveness. Some logistics companies even take some tasks over such as contacting the customer to set up a delivery time or packing the goods.

It is paramount to select the proper model of deliveries as it impacts the price of products on the one hand, and thus customer acquisition, and on the other – the quality of customer service.

Questions that may help in selecting an appropriate delivery model:

1. What range of products will be available through the on-line sales channel?
2. What geographical area is covered by the delivery service?
3. What is the average value of orders delivered?
4. Do the goods transported require any specific transportation conditions?

Customer service

A key success factor in the entire process of placing orders by customers and order delivery performance by the seller is to provide for a proper organisation of the customer service process itself. The task of establishing on-line customer service seems quite difficult given the fact that Internet users expect similar customer service quality as in traditional points of sale. In case of an on-line shop, interaction is excluded, however, on-line customer service needs to be given a human angle, and by creating appearances of control, communication of both good and bad information is a key to success.

The company should have a mechanism in place that enables quick response to any queries or complaints on the products and services offered. Customer service is thus performed in many various ways, including e-mail, instant messengers or hotlines.

The range of possibilities available for organising customer service is extensive. The basic decision is whether customer service processes in the traditional and on-line distribution channels are to be integrated, and to what extent. There are solutions on the market that enable the customers to freely choose communication channels irrespective of where the transaction was concluded (point of sale or on-line), the are also models where after sales service is provided through the channel in which the purchase was made.

Finally, the forms of offering customer service can vary, too. There are models where customer service desks are no longer present at points of sale but are moved to the Internet or exactly the opposite: the entire after sales service is offered in the traditional channel even if the transaction was made on-line.

A decision on which model to select depends on a multitude of aspects, including most of all the needs of our customers and their fluency in using the Internet, the extent to which IT systems are integrated (the full integration model enables viewing orders and tracking their statuses irrespective of the place the goods were purchased in) and, finally, on the range of products we sell and on the level of integration of our sales channels. If they are separated, every channel needs to model customer service processes independently, at least in the area visible to the customer.

There is no single successful solution in e-commerce. However, you have to remember that if we promise something to the customer, we need to keep that promise.

Michał Grom
E-commerce Services Sp. z o.o.
(empik.com, smyk.com, empikfoto.pl, ...)

II.
IT implementation

3. Where to start implementing IT systems

Implementation of the on-line sales channel has an impact on the basic operating processes of the business, thus it often entails large and extensive implementation of IT systems. A company that is getting ready to launch e-commerce services should – in line with the change of its business strategy, and in particular the on-line channel development strategy and the existing IT systems potential – conduct an analysis of the extent of implementation.

Answers to key questions regarding channel strategies:

- What do the Internet and related technologies mean for the business?
- What type of Internet presence would be considered: presentational or transactional?
- How does the implementation of the on-line sales channel fit in the current competitive strategy?
- Do the elements of the previous strategy need to be changed?
- How does the Internet fit in the current IT systems strategy?
- What benefits would be expected from implementing the on-line sales channel?

and regarding the existing IT systems potential:

- Can the existing sales system be easily adjusted to the requirements of the on-line channel?
- Are the existing IT systems sufficient to provide a platform for building e-commerce capabilities?

and estimation of the sales transaction volume will enable a company to draft an initial scope of implementation.

As every organisation with its supporting IT systems is different, if there is an initial vision of the scope of implementation, it has to be analysed which model would be used to implement the on-line transactions platform.

The key question is:

- Whether to choose a standard solution – provided as a service by a partner (e-commerce platform), out of the box software package or whether to customize and develop the existing solution using one's own resources?

Each of the options has their strengths and weaknesses. Selecting an e-commerce platform will enable a sooner launch, not only because of the standard IT solutions used and ready-made infrastructure but also because of the possibility to use the knowledge and experience of the partner that often also provides e.g. graphic layouts or content management functionalities. However, it should be agreed before implementation which functionalities are offered as a standard. Usually, platforms provide the most popular functionalities, and their development entails additional expenses.

Implementation of a standard platform usually requires less capital investment at the beginning, however, you should be aware of possible higher cost of maintenance at later stages.

For example, in case of shops with a monthly revenue of several hundred thousand zloty, it is possible to negotiate a fixed fee for which the provider will commit to provide a relevant availability level or a specific number of hours allocated for development. Such a service is an interim step before the implementation and maintenance of the company's own solution.

Implementation of a software package will enable a larger functional extent and wider adjustment possibilities as compared to e-commerce platforms provided as services. However, it entails longer preparation time and higher implementation costs, and usually higher maintenance costs. Typically, package solutions offer a full scope of functionalities enabling on-line channel operation, from marketing through sales and customer service to order processing. Such a solution, usually offering the possibility of tailoring the platform to the company's individual needs, enables the company at the same time to take advantage of the business knowledge used in it.

Implementation of a customized solution provides the largest potential of adjusting it to the needs and specific character of the company's sector, however, it requires the largest technical knowledge and usually also an own team dedicated to developing and maintaining the platform. Companies decide to build their own solutions if they need large-scale platforms or if they operate in a specific sector provided that their resource management system or financial system can be extended to include an on-line channel functionality. Implementation of a customized solution can be based on both open-source and commercial packages. However, in case of the latter products, it should be established whether and how the application's standard source code can be modified.

A large challenge when implementing an on-line sales channel in Poland is to provide effective traffic management on the website. The Polish Internet market is still young, and the level of website positioning services or effective affiliation systems services varies greatly from what is offered in Western Europe, at least in the cosmetics sector. Lack of experience of companies which extend their traditional distribution channels with on-line sales is taken advantage of by companies offering low quality quasi-e-commerce services at extremely high prices. This proves there are still no reliable e-commerce practices, which can effectively prevent start-up companies from selling on-line.

Jakub Kuśpit
Yves Rocher Polska Sp. z o.o.

What to pay attention to

Irrespective of the model chosen, it is important to provide clear graphic layout and intuitive navigation, both for the customers and back-end functions.

It should be noted that service clarity for the customer also refers to making payments. Therefore, it is worth to consider the forms of payment and – when deciding to work with a particular payment platform – chose the platform that best matches the on-line services.

In case of e-commerce platforms or package solutions, of importance is also the ability to integrate with stock keeping systems or – depending on the sector – with other core systems.

Equally important is to verify how the platform has been developed over the years and what the opinions of its users are, and whether it will allow for (and to what extent) enhancements in the future.

It is also particularly vital to analyse whether the platform enables easy management of promotional campaigns and other sales-driving elements that are specific to our sector.

In all the scenarios, and in particular when implementing the company's own solution using open-source software, one should remember to protect the service not only against the loss of sensitive data but also against the risk of losing income, e.g. as a result of service downtime, or against reputational risk, e.g. swapping of data. When implementing a customized solution, the need to monitor security updates continuously should be considered.

In case of a customized solution, special attention needs to be paid to the architecture design so that it can meet not only the current expectations but also enable development to the largest extent possible.

To sum up, starting implementation, one needs to be aware of the current and future business needs, the team's potential and the IT systems in place. Focussing on one of the proposed implementation models will enable a company to make a decision to look for appropriate business partners or to develop its own team.

III.
Legal aspects

E-commerce in consumer goods in Poland is regulated by a range of Acts[3], resulting in many cases from the implementation of EU legislation[4]. These regulations influence the content of agreements concluded with consumers and impose some obligations on entrepreneurs in terms of actions preceding transaction conclusion. Consumer's general rights to return and complain about goods were regulated in detail. This part of the report is aimed at brief presentation of the legal aspects regarding on-line consumer sale[5]. Also, the chapter provides an overview of regulations concerning personal data processing.

4. Consumer agreements concluded on-line

4.1. Offer, information obligations

In accordance with the general principles of the Civil Code, an entrepreneur making an on-line offer, including an offer posted on a website, should inform the other party clearly and comprehensibly of:

a) the technical actions constituting the agreement conclusion procedure,

b) legal effects of the confirmation by the other party of offer receipt,

c) principles and methods of recording, protecting and making the content of the agreement accessible by an entrepreneur to the other party,

d) technical methods and means used for detecting and correcting errors in the data entered that must be made available by an entrepreneur to the other party,

e) languages in which the agreement may be concluded,

f) codes of conduct complied with by the entrepreneur and on their availability in an electronic form.

Importantly, these principles are not applicable to conclusion of agreements via e-mail or similar means of individual remote communication.

Additional information-related obligations are imposed by the Act of 2 March 2000 on the protection of certain consumer rights and on the liability for damage caused by a dangerous product (hereinafter: Distance Sales Act), which provides that the entrepreneur is obliged to inform the consumer, using means of remote communication, and at the moment of offering to conclude an agreement at the latest, of:

a) first name and surname (trade name) and the domicile (premises) of the entrepreneur and of the body which registered the entrepreneur's business activity as well as of the number under which the entrepreneur was registered,

b) relevant characteristics of the subject matter of the agreement,

c) price or remuneration covering all its components, in particular customs duties and taxes,

d) conditions for price or remuneration payment,

e) costs, time limit and method of delivery,

f) right of withdrawal from the agreement within 10 days along with information on exceptions,

g) costs arising from the use of means of remote communication where they are calculated differently than according to a regular tariff,

h) period during which the offer or information on price or on remuneration remains binding,

i) minimum period of time for which the agreement for permanent or periodic services may be concluded,

j) place and procedures for lodging complaints,

k) right to terminate the agreement.

The above information is usually provided in the form of regulations (by-laws) posted on websites.

[3] Polish legal acts regulating e-commerce include in particular:

1. Civil Code of 23 April 1964 (Journal of Laws No 16, item 93, as amended) (hereinafter: "Civil Code"),
2. Act of 18 July 2002 on providing services by electronic means (Journal of Laws No 144, item 1204, as amended),
3. Act of 2 March 2000 on the protection of certain consumer rights and on the liability for damage caused by a dangerous product (Journal of Laws No 22, item 271, as amended),
4. Act of 27 July 2002 on specific terms and conditions of consumer sale and amendments to the Civil Code (Journal of Laws No 141, item 1176, as amended),
5. Act of 18 September 2001 on electronic signature (Journal of Laws No 130, item 1450, as amended),
6. Private International Law of 4 February 2011 (Journal of Laws 11.80.432) (hereinafter: "PIL").

[4] Community law acts regulating issues concerning e-commerce include:

1. Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market (hereinafter: "Directive on electronic commerce"),
2. Directive 99/44/EC of 25 May 1999 on certain aspects of the sale of consumer goods and associated guarantees,
3. Directive 85/374/EEC of 25 July 1985 on the approximation of the laws, regulations and administrative provisions of the Member States concerning liability for defective products,
4. Council Directive 85/577/EEC of 20 December 1985 to protect the consumer in respect of contracts negotiated away from business premises,
5. Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts,
6. Directive 97/7/EC of 20 May 1997 on the protection of consumers in respect of distance contracts,
7. Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 (Rome I),
8. Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters.

[5] The Report excludes legal issues related to the provision of services by electronic means subject to the Act of 19 July 2002 on providing services by electronic means (Journal of Laws No 144, item 1204, as amended).

The regulations (by-laws) should be formulated clearly, comprehensibly and should be easily readable so that the customer can make an informed decision when purchasing goods and services. Moreover, the company has to confirm all the above information in writing at the moment when performance starts at the latest. Failure to comply with the obligation provides the consumer with a prolonged time for withdrawal from the agreement. The period then is 3 months from the date of goods handover (normally the period is 10 days – read more in section 5.1).

Also, the legal regulations oblige the company to notify the consumer immediately, however not later than within 30 days from the agreement conclusion date, of the inability to perform the agreement due to product unavailability. In such an event, the company should return the entire amount paid by the consumer.

In addition, in a situation where the company is unable to perform due to even temporary inability to provide the goods with ordered properties, the company, if stipulated in the agreement, may provide substitute goods. Such substitute performance is treated a performance of the same quality, the same purpose, at the same price or remuneration. The company, however, has to inform the consumer in writing of the right to refuse substitute performance and withdraw from the agreement. In case of withdrawal costs of return of the goods are borne by the company.

4.2. Agreement terms and conditions

Agreements concluded with consumers in e-commerce transactions are subject to general provisions of the Civil Code, including the provisions on unlawful contractual provisions (so-called abusive clauses). Therefore, general terms of sale drafted by companies may not model the consumer's rights and obligations in a way that is inconsistent with good practices or that grossly infringes the consumer's interests. Provisions that are non-compliant with the above requirement shall not be binding upon customers.

The Civil Code lists a number of clauses that – in case of doubts – are deemed unlawful agreement provisions. Examples of such provisions include:

a) excluding or significantly limiting the company's liability for non-performance or improper performance of an obligation;

b) making the conclusion, the content or the performance of the agreement contingent upon the conclusion of another agreement unrelated directly to the agreement that includes provision in question.

The generally available record of clauses deemed by courts as unlawful is held by the Office of Competition and Consumer Protection. Additional strengthening of the protection of customers purchasing goods on-line results from the provisions of the Distance Sales Act which provides, among others, for:

a) right of the customer to withdraw from the agreement without stating the reason within 10 days from goods handover (read more in section 5.1);

b) prohibition to make a reservation that the customer is allowed to withdraw from the agreement upon payment of determined remuneration (compensation);

c) prohibition to impose on the customer the obligation to pay the price or remuneration before the goods are delivered (this refers to situations where pre-payment is the only available form of payment);

d) the obligation to provide the customer with the right to lodge complaints in a way that does not cause excessive difficulties or costs for the customer.

We live in a globalised word and almost all elements from the global strategy of the company may be implemented on a local level. Are there any local law regulations which may hinder implementation of the global strategy? I think that such regulations should be treated as challenges demanding from us for more involvement rather than the real restrictions.

José Bonito
Customer Management Director
Makro Cash and Carry Polska S.A.

5. Consumer's rights to return and complain about goods

Polish law provides consumers with the right to withdraw from the agreement under no specific reason and protects the consumer's interests if the goods purchased are inconsistent with the agreement or defective. These rights are provided for in regulations on distance sales and in other legal acts. Below, we present an overview of key rights vested in consumers when shopping on-line.

The multichannel approach is currently the essential factor in targeting clients in the traditional sales. It is not enough at present to be "brick-and-mortar", you should be brick-on-line.

José Bonito
Customer Management Director
Makro Cash and Carry Polska S.A.

5.1. Withdrawal from agreement – return of goods

The consumer's right to withdraw from the agreement was provided for in the Act on Distance Sales. The Act provides that a consumer who makes a purchase using means of remote communication has the right to withdraw from the agreement without stating the reason to do so.

The period for withdrawal is 10 days from goods handover and shall be prolonged to 3 months if there is no confirmation of information that the entrepreneur was due to provide to the consumer at goods handover (read more in section 4.2). However, if the information is confirmed after the said period starts, the period for consumer's withdrawal from the agreement is again reduced to 10 days. Therefore, the consumer should make a relevant statement in writing and send it to the entrepreneur before the lapse of the 10-day period.

Withdrawal from the agreement concluded remotely shall result in the agreement being deemed not concluded. As a consequence, the entrepreneur is released from any obligations, and what the parties provided to each other should be returned unaltered, unless alteration was necessary within the limits of regular management. Entrepreneurs are also obliged to return costs of goods delivery to the consumer, which was emphasised in the decisions by the Office of Competition and Consumer Protection (the consumer is only obliged to cover the costs of return delivery). The return should be made immediately, and the deadline to do so is 14 days.

If the consumer has made any pre-payments, the consumer has the right to receive statutory interest on the pre-paid amount from the date of pre-payments being made.

It is worth noting that withdrawal from the agreement is also effective with respect to a credit or loan agreement concluded by the consumer if the performance was to be fulfilled with the use of the credit or loan granted under an agreement between the creditor and the entrepreneur. In such an event, the creditor is obliged to return the costs incurred by the consumer related to the conclusion of the agreement, excluding preparatory fee and expenses related to any possible establishment of loan repayment security. The consumer shall not be able to withdraw from the agreement, unless the parties agreed otherwise, in the following cases:

a) provision of services if performance started, with the consumer's consent, before the period for withdrawal from the agreement without giving reasons lapsed,

b) contracts concerning audio and video recordings as well as data recorded on data carriers, once the original packaging is removed by the consumer,

c) contracts concerning performance for which the price or remuneration depends solely on price fluctuations on the financial market,

d) performance with characteristics specified by the consumer in his order or directly connected with the consumer's person,

e) performance which by reason of its nature cannot be returned or the subject of which is susceptible to quick deterioration,

f) supply of press,

g) services in the field of games of chance and betting.

Withdrawal from the agreement may also occur when the entrepreneur fails to inform the consumer in writing of the consumer's right to refuse substitute performance. Then, the cost of goods return is incurred by the entrepreneur.

The consumer's withdrawal from the agreement entails the entrepreneur's obligation to confirm in writing the return of the goods.

5.2. Entitlements when consumer goods are non-conformant with the agreement

In accordance with the Act of 27 July 2002 on specific terms and conditions of consumer sale and amendments to the Civil Code (hereinafter referred to as “Consumer Sale Act”), the seller is liable for the inconsistency of the goods with the agreement. Inconsistency is assessed as at the day of goods handover date. In the event of the inconsistency discovered within six months of handing over the goods, the inconsistency is deemed to have existed at the time of handing over.

The consumer goods are also deemed inconsistent with the agreement in case of an incorrect installation or activation, if the goods are installed or activated under the sales agreement by the seller or a person for whom he is responsible or by the buyer according to the instructions manual received at the time of sales.

The law provide for a number of cases where consistency of the goods with the agreement is assumed. This occurs in the following situations:

a) the features of the consumer goods are agreed individually, the goods comply with the description provided by the seller or have features of the sample shown to the buyer or features of the pattern and if the goods are suitable for the purpose specified by the buyer at the conclusion of the agreement, unless the seller raised any objections to such an application of the product,

b) the goods are suitable for the purpose for which products of this kind are usually used and if its features correspond to features typical for this kind of products,

c) goods fulfil the expectations towards the product of this kind, based on assurance of the seller, manufacturer or his representative, made in public.

In some cases, the seller’s liability for inconsistency of the goods with the agreement is excluded. The liability is eliminated if the buyer has knowledge of such an inconsistency or reasonably he should have knowledge thereof. The same applies to any inconsistency arising from a defect of the material supplied by the buyer. Where the goods are inconsistent with the agreement, the buyer has specific rights the use of which is conditional upon notification of the seller of the inconsistency within a period of two months of discovering thereof. The buyer’s claims become time-barred after one year from the buyer’s discovery of the inconsistency of the consumer goods with the agreement, however, not before the expiry of two years of handing over of the goods. If the seller is notified of the inconsistency of the consumer goods with the agreement, the period of prescription is interrupted. The expiry of the two-year period of seller’s liability for the inconsistency of the consumer goods with the agreement and the one-year consumer’s claims time-barred period do not jeopardise the performance of relevant rights if at the time of concluding the agreement the seller had the knowledge of the inconsistency and failed to advise the buyer of that fact.

The list of buyer’s rights if the consumer goods is found inconsistent with the agreement and the order of their performance is as follows:

1. The buyer may require to have the goods restored to the condition stipulated by the agreement, i.e. to have it repaired or replaced free of charge by a new item, unless the repair or replacement are not feasible or entail excessive expenses – if the seller who receives the above demand from the buyer fails to reply to such a demand within 14 days, the demand is deemed justified;
2. Further, the buyer may demand an appropriate price reduction or terminate the agreement if:
   - the buyer cannot request to have the good repaired or replaced;
   - the seller is unable to satisfy such a claim in due time;
   - the repair or replacement would expose the buyer to significant inconvenience.

The agreement can be terminated, however, only if the inconsistency of the consumer goods with the agreement is material.

The main factors influencing the choice of the seller on-line (in particular in terms of electronic goods) is security, trust and price. A strong physical shop brand and multiple branches, complementarity of after sales support and guarantee foster trust and build competitive advantage as compared to shops that operate exclusively on-line.

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In case of companies that have a chain of franchised outlets, an additional challenge when going on-line is to persuade the franchisees that an additional channel would not affect their franchise sales.

Jakub Kuśpit
Yves Rocher Polska Sp. z o.o.

5.3. Guarantee

The Consumer Sale Act introduces a requirement to provide the buyer with a free warranty for the goods purchased. The provisions of the said Act exclude the application of warranty regulations set forth by the Civil Code.

The Act does not specify, however, who is to provide the warranty. It may be provided by the seller but more often it is provided by the manufacturer, importer of the goods or another entity obliged to perform such warranty services. The market practice is dominated by warranties provided by the manufacturer. In such a case, the seller performs the role of a messenger or the warrantor's proxy. The warranty is offered in the form of a statement by the warrantor in the warranty document or advertisement applicable to the consumer goods. The statement determines in a clear, understandable, not misleading way the warrantor's duties and obligations and the buyer's rights in case the features of the goods sold fail to correspond to the features described in the statement.

If it is the seller who is giving the warranty, the seller hands out a warranty document to the buyer together with the consumer goods. The warranty document should contain basic data necessary to pursue a claim under the warranty, and in particular:

a) name and address of the warrantor or his representative in the Republic of Poland,

b) length and territory of the warranty.

Moreover, the document should contain a statement that the warranty does not exclude, limit or suspend the buyer's rights arising from the inconsistency of the goods with the agreement.

In order to pursue their rights under warranty, the buyer should deliver the goods at the warrantor's expense to a place indicated in the warranty document or to the place where the goods were handed over with the warranty document. However, the circumstances in a given situation may suggest the removal of a given defect in the place where the goods were located at the moment of the discovery thereof.
The warrantor has to perform the obligations stipulated in the warranty document in a relevant time and deliver the goods to a relevant location to the buyer at the warrantor's expense. Upon a significant repair or replacement of the goods under the warranty provided, the warranty period starts anew from the moment of the delivery of the goods free of defects or return of the repaired goods. In other cases, the warranty period is extended by the time when the buyer was unable to use the goods due to the defect.

5.4. Exclusion of implied warranty rights

The implied warranty rights for physical and legal defects of goods provided for in the Civil Code are not applicable to consumer sale.
The protective role is provided by the concept of inconsistency of the good with the agreement (read more in section 5.2)[6].

[6] The Act on consumer sales overtly excludes the applicability of implied warranty provisions of the Civil Code in such cases.

6. On-line shoppers' personal data protection

6.1. Introduction

Offering on-line sales is inevitably related to the processing of personal data of customers who place orders. If the scope of the data gathered enables identification of the person to whom the data pertain, the provisions of the Act of 29 August 1997 on Personal Data Protection will apply (Polish Journal of Laws of 2002 No 10f1, item 926) (hereinafter: PDPA). In practice, it can be assumed that the scope of customer data gathered in relation to sales will always enable such identification, and thus the processing of the data will be subject to the PDPA.

The basic obligations of the entity processing personal data for its own purposes, which determines the means and purposes of such processing, i.e. the personal data controller within the meaning of the PDPA, are as follows:

a) having a legal basis authorising personal data processing,

b) using technical and organizational measures to protect the personal data being processed, appropriate to the risks and category of data being protected,

c) providing the persons whose personal data is being processed with certain information,

d) registration of the data filing systems with the register held by the Inspector General for Personal Data Protection (hereinafter: GIODO).

6.2. Legal basis for personal data processing

The basic prerequisite for authorising data processing is the consent of the person to whom the personal data pertain. However, the law provide for situations where personal data processing is permitted without the need to obtain the consent, including situations where processing is necessary for the performance of an agreement to which the data subject is a party, or in order to take steps at the request of the data subject prior to entering into an agreement. Thus, the said provision waives the obligation to obtain a consent for the purposes of the conclusion and performance of a sale agreement concluded on-line.

The need to obtain the consent may arise where sales is performed using a system that requires prior establishment of a fixed account and provision of personal data. The right to process personal data in relation to the performance of an agreement is not extended to the processing of data for the purposes of opening such account (the account itself does not oblige the user to make any purchase). Therefore, it is necessary to obtain a consent, the subject of which would be to provide authorisation to process data for the purposes of account creation and maintenance. The consent should be obtained prior to the commencement of personal data processing.

6.3. Obligation to protect data

The basic aim of the provisions regulating personal data processing is to provide protection against unauthorised access to data, their deletion or involuntary change. With regard to the above, the PDPA contains only a general provision imposing an obligation to implement appropriate technical and organizational measures to attain the said aims. Its proper performance requires an individual review of the conditions in which the business operates. The protection measures adopted should be presented in the documentation required by the law describing the method of data processing, i.e. in the Security Policy and Instruction on the management of IT systems used for personal data processing. In addition, the data controller should hold a register of persons authorised to carry out the processing of personal data and appoint an administrator of information security, and perform other obligations arising under PDPA.

With regard to personal data processing in IT systems, more detailed provisions are specified in the Regulation of 29 April 2004 on personal data processing documentation and technical and organisational conditions to be fulfilled by devices and computer systems used for personal data processing (hereinafter: the Regulation).

The Regulation provides for a range of requirements and specifies some functionalities that should be included in the system used for personal data processing, such as a requirement that the system should enable keeping records of the date when the data were registered for the first time in the system or information on recipients to whom the data have been disclosed. Given the complexity of the issue, the problem of ensuring data security is only hinted upon in this publication, and the actual solutions should be prepared in the context of specific circumstances and relevant provisions of the law.

In pursuit of profits, companies sometimes decide to invest in e-commerce. It is not a problem to launch an on-line shop. The problem is to have a carefully considered concept and a clear strategy that illustrates the goals the business wants to achieve. Yet, some companies fail to understand what they are working on.

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(empik.com, smyk.com, empikfoto.pl, ...)

6.4. Information obligation

The personal data controller is obliged to provide a data subject from whom the data are collected with information on the controller's name and address, the purpose of data collection, the right of access to personal data and to amend them. In addition, the controller should specify whether the provision of data is voluntary or obligatory. The provision does not apply if the data subject already has the above information.

6.5. Obligation to register the personal data file

In accordance with the PDPA, data controllers are obliged to register their personal data filing systems with GIODO. The obligation is applicable to customer data files held in relation to on-line sales.

The registration is performed on an administrative notification form. Personal data processing in a file is allowed only upon notification of the filing system for registration with GIODO. In case of the so-called sensitive[7] data, processing may be commenced only when the filing system is registered. Any changes to information notified at registration are to be notified to GIODO within 30 days of introducing such change.

6.6. Personal data processing with subcontractors

If personal data processing is performed by third parties, it is necessary to confer personal data processing in accordance with Article 31 of PDPA. Given the broad definition of the "data processing" term, which includes all the operations performed on personal data (such as collection, recording, keeping, compiling, altering, making available and deleting), the obligation to appropriately confer data processing may arise in many situations (e.g. when using an externally provided call centre services serving customer queries or hosting services for the server where the personal data filing system is held, with a specialised provider).

The processing should be conferred in writing. It may be performed through a separate dedicated agreement and as part of a framework agreement providing for the principles of commercial cooperation. In accordance with the Act, it is necessary to include provisions that specify the scope of data to be processed by the third party provider and the purpose of the processing operations. As the data controller is liable for the data processor's compliance with the provisions of PDPA, the agreement should also include provisions authorising the data controller to control the method of data processing by the service provider.

6.7. Using personal data for marketing purposes

In accordance with the PDPA, the data controller is authorised to process personal data for the purposes of direct marketing of own products or services. The authorisation is vested in the controller irrespective of the purpose for which the data were originally collected. However, it should be emphasised that some limitations on the means that can be used for marketing purposes result from the Act of 18 July 2002 on providing services by electronic means (hereinafter: APSEM). In accordance with the APSEM, pursuing marketing activities using electronic mail or any others means of electronic communications such as text messaging or multimedia messaging service (MMS), requires prior separate consent[8]. Such a consent may not be presumed from a statement of will having another contents. Practically, this means a necessity to take such a consent out of the website regulations and introduce a separate tick box to confirm the consent.

It is to be highlighted that the right to advertise is limited to own services and products. If the shop owner intends to use the data for marketing third party products and services, it is necessary to prepare an additional (separate) consent clause.

[7] Personal data revealing racial or ethnic origin, political opinions, religious or philosophical beliefs, religious, party or trade-union membership, as well as the processing of data concerning health, genetic code, addictions or sex life and data relating to convictions, decisions on penalty, fines and other decisions issued in court or administrative proceedings.

[8] If there is no such consent, the information sent is considered prohibited commercial information (so-called spam).

IV.
Accounting matters

From the accounting perspective, the operations of on-line shops are not much different from traditional forms of business. However, there are some accounting matters that may become a practical challenge for the management of a company that is starting up its operations in the form of an on-line shop. These areas include recognition of revenue, accounting for goods returned, loyalty programmes, website costs or expenses incurred for the establishment of a new distribution channel.

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7.1. Revenue recognition

One of the most important issues regarding revenue recognition is establishing when the revenue should be recognised. In case of transactions performed via on-line channel, it is usually not difficult to measure the revenue. This should be the fair value of the consideration received or receivable, most often corresponding to the net sale price.

The moment of revenue recognition is dealt with in the International Accounting Standard 18 "Revenue" (IAS 18).

When the sale transaction is performed on-line it should not be difficult to meet the requirements of reliable revenue measurement, probability of obtaining economic benefits and reliable measurement of costs incurred in respect of the transaction. Usually, all the above requirements are met at the moment of shipping the delivery to the customer. However, it may be problematic to establish when significant risk and rewards of ownership were transferred to the buyer. Is the requirement met at the moment of shipping the goods to the buyer (when an invoice is issued or a receipt is printed and the transaction is recorded in the company's financial system), or is it not until the buyer receives the goods or after the lapse of the period when the buyer can make an unconditional return of the good?

There is no clear answer to these questions as the answer largely depends on the character of the transaction and on the provisions of the agreement concluded between the seller and the buyer at the moment of placing the order, which are often included in the regulations stipulating the terms and conditions of on-line sales.

Let us have a look at the issue of recognising revenue from a transaction performed on-line.

Form of payment and goods receipt

Example 1

An on-line shop performs a sale transaction; the customer selects to pay at delivery performed by a courier company. Should the on-line shop recognise revenue at the moment of shipping the goods to the customer? In order to answer the question, we need to take a look at the provisions of IAS 18 and the requirements that need to be fulfilled so that the company may recognise revenue in its books of account. When are the risk and rewards associated with the goods sold transferred to the buyer?

In most cases, the on-line shop should recognise revenue at the moment of the customer's acceptance of the delivery from the courier. Then, the risk and rewards associated with the goods sold are transferred to the buyer. Similarly, only at the moment of receiving the goods purchased does the buyer become the owner of the goods. Obviously, a lot may depend upon specific provisions of the sale agreement set forth in the on-line shop regulations.

However, neither the fact that the courier delivery is insured, nor that the customer has already paid for the goods, should influence the moment of revenue recognition as until the customer receives the delivery, neither the risk and rewards related to the goods are transferred to the customer. Any possible insurance for products damaged in the shipping is not paid to the buyer, which only confirms the conclusion above.

Establishing the moment of revenue recognition usually poses no difficulty in retail trade. The customer receives the goods at the shop together with a transaction confirmation in the form of an invoice or a cash register receipt and this is when sales is recognised – the transfer of risk and rewards to the buyer is concurrent with the transfer of the ownership of the goods or with physical delivery of the goods. However, the situation may be different in the on-line distribution channel. An on-line shop should develop its own accounting policy specifying in detail the matter of revenue recognition depending on, among others, the method of delivery, in accordance with the applicable on-line shop regulations and in reference to the requirements necessary to allow revenue recognition as set forth in IAS 18. In practice, this may mean the need to control at the end of the reporting period which deliveries were not collected by the customers and to adjust the previously recognised revenue and costs if they were recognised automatically, when an invoice or a cash register receipt has been issued.

7.2. Returns

A frequent practice of on-line shops is to enable customers to return the goods unconditionally within e.g. 14 days from the receipt of the goods by the buyer. This results, among others, from the specifics of e-commerce, where the buyer is unable to physically check the goods before purchasing and delivery. A question therefore appears whether the possibility to make such a return has any implications for revenue recognition or whether it might impact the financial result at the moment of sale, before the lapse of the period in which the customer can return the goods.

Returns are nothing specific to the on-line channel: in traditional shops, more and more often customers can return the goods without stating the reason to do so, provided that the goods are intact and will be fit for further sale.

In accordance with IAS 18, an example of a situation where a business incurs an insignificant ownership-related risk is retail sale enabling reimbursement if the customer is dissatisfied with the goods purchased. In such cases, revenue is recognised at sale provided that the seller can reliably estimate the probability of return of goods in the future and will recognise the liability related to the returns in its report, based on the previous experience and on other relevant considerations.

At the end of the reporting period, the on-line shop should review historical return levels. e.g. as compared to total sales in a given period, and establish whether the level of returns requires the establishment of a provision for probable returns.

If it turns out that the level of returns established based on historical data (or other available information such as a faulty product lot or information from companies running a similar business) is significant for the financial statements, a relevant provision should be established up to the value of the margin (after adjustment of, respectively, recognised revenue and value of goods sold) that the shop may lose if customers decide to return the goods.

7.3. Loyalty programmes

A relatively popular form of encouraging customers to repeat purchasing are rebates and loyalty programmes. When a specific good or service is purchased, the customer is awarded loyalty points by the business, which may be exchanged at the following transaction for rewards such as free or discounted goods and services.

The accounting consequences of awarding points to the customer, enabling their exchange for free or discounted goods have been dealt with in the International Financial Reporting Interpretations Committee Interpretation 13 “Loyalty programmes” (IFRIC 13).

According to the interpretation, the company recognises loyalty points as a separate element of the sale transaction for which they are awarded (“initial sale”). The fair value of the proceeds received or receivable in relation to the initial sale should be allocated to the loyalty points and to other elements of the sales transaction (value of the goods sold or service rendered).

The proceeds allocated to the loyalty points are measured by reference to their fair value, that is, the amount for which the loyalty points could have been sold separately. A company may measure the fair value of loyalty points by reference to the fair value of awards that one may receive in exchange for the points. The fair value of these awards takes appropriate account of the amounts of rebates and incentives that would be offered to customers who did not collect loyalty points and the proportion of loyalty points in relation to which the business can reasonably expect to remain unused.

If the business provides the awards itself, then it recognises the proceeds allocated to loyalty points as revenue at the moment of the redemption of points and after the obligation to provide awards is fulfilled. The amount of revenue recognised is based on the number of loyalty points redeemed for awards as compared to the total number of loyalty points the redemption of which can be expected.

When we opened the on-line channel, we faced a question of how to solve the problem of payment for goods when customers can refuse to accept part of the order at delivery. Tesco chose the model of payment by cards only, both credit and debit cards. The customer will be able to make a prepayment on-line (the amount will be blocked and then charged in the appropriate amount at delivery) or to pay at delivery (the deliveryman will have a card terminal at delivery).

Grzegorz Juszczyk
Tesco (Polska) Sp. z o.o.

Example 2

Year 1

Purchase of goods by customers in year 1 of the value of PLN 1,000,000. Customers receive 200,000 points in a loyalty programme. The fair value of goods for which a single point can be redeemed is PLN 1. The amount already includes the estimated rebates that would be offered to customers who do not collect loyalty points.

The initial evaluation of the redemption of points awarded in the loyalty programme shows that half of the points is not used by the customers.

Initial revenue allocation

- *The total proceeds should be allocated to both elements of the agreement, i.e. to the initial sale transaction and points awarded to customers. The allocation should be based on the fair value of points.*
- *The fair value of points is calculated as follows:*

200,000 points x PLN 1 (fair value of goods for which points can be redeemed) x 50% (expected proportion of the redemption of points) = PLN 100,000.

As a result, the fair value of points accumulated by customers in year 1 amounts to PLN 100,000. The amount should be recognised as deferred revenue.

- *The remaining value of PLN 900,000 (PLN 1,000,000 – PLN 100,000) should be recognised as revenue from sale of goods.*

Year 2

- *Out of the pool of points awarded in year 1, 120,000 points are used in year 2, and the business changes its estimations as to the number of points that will be redeemed from 50% to 75%.*

Further postings (year 2)

- *The business re-estimated the points redemption rate from 50% to 75%. This means that the business expects redemption of 150,000 points awarded in year 1 (200,000 points awarded in year 1 x 75%).*
- *120,000 points were redeemed through the end of year 2. The revenue should then be recognised in reference to points redeemed in year 1 in proportion to the expected redemption level as illustrated below:*

– Share of redeemed points: 120,000/150,000 = 80%

– Deferred revenue in year 1: PLN 100,000

– Opening balance revenue to be recognised in year 2: 80,000 (PLN 100,000 x 80%).

To summarise, an on-line shop which awards loyalty points should recognise such a transaction appropriately. In accordance with IFRIC 13, part of the revenue being an estimated fair value of the points awarded should be deferred and recognised only upon redemption of the points awarded.

7.4. Website costs

The success of the on-line distribution channel largely depends on the functionality of its website. In order to provide for its sufficient functionality, appropriate – and sometimes significant – investments are required to launch the on-line channel.

A company can make internal investments in the development and operation of its own website, providing access to internal or external users. A website designed to be made accessible to external users may be used for different purposes such as promotion and advertising of the company's own products or services, sales of products and services and provision of electronic services. Meanwhile, a website designed for internal users can be used for posting information on the company's policies, customer data and for searching for information.

A developed website is recognised as an intangible asset only when in addition to the general requirements provided for in IAS 38 (probability of future economic benefits and ability to reliably measure the cost of the asset) the business meets the requirements of IAS 38.57 (referring to development works). The fulfilment of the requirement to demonstrate how the website will generate probable future financial benefits should be feasible mainly in a situation where the website can generate revenue, for instance, direct revenue resulting from the possibility of submitting orders via the website.

If the website was developed exclusively or mainly for the promotion or advertising the company's own products or services, the company will not be able to demonstrate that the website would generate probable economic benefits and thus all the expenses incurred in relation to the development of such a website are recognised as costs at the moment of incurring.

In order to help the management to establish the method of recognising website costs, the Standing Interpretations Committee (SIC) issued in 2002 interpretation SIC 32 "Intangible Assets – Website Costs" (SIC – 32).

The interpretation recognises the following stages of website development:

a) planning – includes undertaking feasibility studies, defining objectives and specifications, evaluating alternatives and selecting preferences;

b) application (software) and infrastructure development – includes obtaining a domain name, purchasing and developing hardware and operating software, installing developed applications and stress testing;

c) graphical design development – includes designing the appearance of web pages;

d) content development – includes creating, purchasing, preparing and uploading information, either textual or graphical in nature, on the website before the completion of the website's development. This information may either be stored in separate databases that are integrated into (or accessed from) the website or coded directly into the web pages.

The company's own website developed, with access for internal or external users, constitutes an intangible asset developed by the company that is subject to the requirements of IAS 38 "Intangible Assets".

The table on the right, constituting an appendix to SIC – 32, summarises the stages of website development with the relevant accounting treatment.

Stage/nature of expenditure	*Accounting treatment*
Planning	
• undertaking feasibility studies • defining hardware and software specifications • evaluating alternative products and suppliers • selecting preferences	Recognise as an expense when incurred in accordance with IAS 38.54
Application and infrastructure development	
• purchasing or developing hardware	Cost capitalisation in accordance with IAS 16
• obtaining domain name • developing operating software (e.g. operating system and server software) • developing code for the application • installing developed applications on the web server • stress testing	Recognise as an expense when incurred, unless the expenditure can be directly attributed to preparing the website to operate in the manner intended by management, and the website meets the recognition criteria of IAS 38.21 and IAS 38.57(a) (i.e. probability that future economic benefits will flow to the entity, possibility to reliably measure the cost of the asset and the technical feasibility of completing the intangible asset so that it will be available for use or sale)
Graphical design and development	
• designing the appearance (e.g. layout and colour) of web pages	Recognise as an expense when incurred, unless the expenditure can be directly attributed to preparing the website to operate in the manner intended by management, and the website meets the recognition criteria of IAS 38.21 and IAS 38.57(a) (i.e. probability that future economic benefits will flow to the entity, possibility to reliably measure the cost of the asset and the technical feasibility of completing the intangible asset so that it will be available for use or sale)

Stage/nature of expenditure	*Accounting treatment*
Content development	
• creating, purchasing, preparing (e.g. creating links and identifying tags), and uploading information, either textual or graphical in nature, on the website before the completion of the website's development. Examples of content include information about an entity, products or services offered for sale	Recognise as an expense when incurred in accordance with IAS 38.69(c) to the extent that content is developed to advertise and promote an entity's own products and services (e.g. digital photographs of products). Otherwise, recognise as an expense when incurred, unless the expenditure can be directly attributed to preparing the website to operate in the manner intended by management, and the website meets the recognition criteria of IAS 38.21 and IAS 38.57(a) Cost capitalisation in accordance with IAS 16
Operating stage	
• updating graphics and revising content • adding new functions, features and content • registering the website with search engines • backing up data • reviewing security access • analysing usage of the website	Assess whether it meets the definition of an intangible asset and the recognition criteria set out in IAS 38.18, in which case the expenditure is recognised in the carrying amount of the website asset
Other	
• selling, administrative and other general overhead expenditure unless it can be directly attributed to preparing the website for use to operate in the manner intended by management • clearly identified inefficiencies and initial operating losses incurred before the website achieves planned performance (e.g. false-start testing) • training employees to operate the website	Recognise as an expense when incurred in accordance with IAS 38.65-70

In the context of establishing the on-line distribution channel, it is especially important to allocate the expenses incurred to specific stages and to collect appropriate documentation to confirm that specific expenditure categories are relevant for a specific stage. For stages quoted in SIC – 32 items b) to d), proper documentation should also confirm that a given expenditure item can be directly attributed to preparing the website for use to operate in the manner intended by management.

To summarise, the management of the company embarking upon developing its own website with the use of which goods are to be sold should be aware that not all the expenses incurred for the development of such a website can be capitalised in the light of the applicable regulations. Relevant documentation of specific stages should enable capitalisation of a part of related expenses, and thus it is worth to consider – already at the investment planning stage – how to classify the expenditure incurred for the development of the website.

One should remember that driving sales through on-line presence is not limited to having a corporate website or an on-line shop. If we want to build corporate image, we should never forget about the power of social media, including Facebook. Frequently, it is entering the social media that mainly stimulates on-line sales. A great advantage of it is the fact that the on-line community builds itself. However, this entails great responsibility. Presence in the social media requires the company to be swift in responding to customer questions and comments as these, left unreplied, may cause a wave of negative comments and deteriorate the brand image in a very short time.

Jakub Kuśpit
Yves Rocher Polska Sp. z o.o.

7.5. Expenses for establishing a new distribution channel

When the company decides to launch on-line sales as a channel to support traditional sales, it will be necessary to invest in the development of a new concept of sales and supply chain operations, and to incur expenditures on new IT systems and a website.

The new concept is related to the pursuit of an appropriate model of functioning of the company, the implementation of such an appropriate model and its later monitoring. Very often, companies decide to hire consultants who are experienced in implementing new distribution channels. The expenses incurred by companies at the stage of development and implementation of such a concept are significant, which raises a question whether it is reasonable to recognise such expenditures as costs of the financial period if they refer to the future operations of the business.

Guidelines regarding expenditures for research and development are dealt with in the International Accounting Standard 38 “Intangible assets” (IAS 38).

Companies expend their resources or incur liabilities for the purchase, development, maintenance and improvement of intangible assets such as scientific and technical knowledge, design and implementation of new processes or systems. Establishment of a new distribution channel may be an example of such type of expenditure.

Not all the expenses, however, for the establishment of a new distribution channel meet the development work criteria and criteria for capitalisation of development work costs. If a given item fails to meet the criteria, then such costs are recognised as an expense when they are incurred.

In order to be able to determine whether a given intangible asset developed by the company meets the capitalisation criteria, the entity needs to divide the asset development process into the research stage and development stage.

Development works, the costs of which can be capitalised in accordance with IAS 38, include design, development and testing of selected solutions in terms of new or improved materials, devices, products, processes, systems or services.

In case of implementation of a new goods distribution concept in the on-line channel, most expenses related to its development, in line with the provisions of IAS 38, should be recognised by the business as costs of the financial period in which the cost was incurred. IAS 38 provides a range of criteria that are to be met so that costs can be capitalised as costs of the development stage, including availability for use or later sale or probability of generating future economic benefits.

For example, development of a supply chain concept in relation to the introduction of the on-line sales model, consisting in the formulation and selection or relevant internal processes and pursuit of optimal solutions, will be classified as research works, and thus the costs of this stage should not be capitalised. At the same time, when the entity decides to choose a relevant concept and undertakes implementation efforts, such efforts will most probably be considered development works. If the company can evidence that the development works it undertook will meet the capitalisation criteria (identifiably, control and economic benefits), the costs incurred in relation to the works can be capitalised. If works pertain to the existing IT systems but only to the extent to which the works improve system functionality, by e.g. enabling the operation of a new distribution channel, then they are capitalised when the criteria set forth in IAS 38 for capitalisation of further costs are met.

It is of key importance for proper classification of costs and presentation of the business’ financial results to know which criteria need to be met to enable capitalisation of part of the costs incurred for the establishment of a new distribution channel.

V.
Tax issues

This part discusses the most frequent issues related to fiscal regulations, which appear when a company launches an on-line sales channel. The issues are based on information we received during interviews with our clients.

8. VAT aspects

Introducing the on-line sales does not simplify the taxpayer's obligations relating to value added tax (hereinafter: "VAT") with respect to accounting and documentation areas. What is more, fulfilment of the statutory obligations can often be more burdensome than in case of traditional sales due to the fact that the obligations may differ depending on the details of the transaction.

8.1. On-line sales and tax obligation

On-line sale of goods can be performed in a number of ways differing with the moment of payment for the goods ordered.

For VAT purposes, such type of sales will be considered "mail order sales". However, depending on the arrangements regarding the payment date, the moment of VAT obligation as well as other VAT consequences may differ.

Payment directly to the seller's bank account after goods delivery

The first of the possible situations is a situation where the buyer of goods (e.g. who bought them from an on-line shop) makes payment after delivery directly to the bank account of the seller (thus without the intermediation of the mailman or courier).

In the case in question, general principles of recognition of VAT tax obligations provided for in Article 19(1) of the Act on value added tax apply. Therefore, the tax obligation will arise at the moment of goods handover. However, if the sale should be confirmed with an invoice (e.g. when the sale is performed for the benefit of businesses), the tax obligation under Article 19(4) of the VAT Act will arise on the date of invoice issuance, however, not later than on the seventh day from goods handover. As in the trade practice the VAT invoice is attached to the delivery shipped to the buyer, the tax obligation will therefore arise on the day the invoice is issued.

It should also be noted that the above principles also apply to situations where the transaction itself is concluded on-line (e.g. using an auction service), however, the receipt of the goods purchased and payment of the price is made in cash at the seller's premises.

Cash on delivery

A form of payment that is sometimes used in on-line commerce is "cash on delivery". In such cases, the buyer pays for the goods purchased only upon delivery, however, the payment is not transferred directly to the seller's bank account but made through a mailman or a courier and packing.

The VAT Act provides for such situations a specific moment for the occurrence of the tax obligation, under Article 19(13) item 6 of the VAT Act. In accordance with the provision quoted, in case of a mail order performed on "cash on delivery" terms, the tax obligation arises at the moment of the seller's receipt of the payment.

Interestingly, the legislator referred to the above situation using the expression "za zaliczeniem pocztowym" (English: "cash on post delivery"), thus ignoring the market practice of using not only post services but also courier services to deliver orders. For the latter services use the expression "za pobraniem" (English: "delivery upon collection"), not "za zaliczeniem pocztowym". It seems, though, that this is an oversight of the legislator and not a deliberate measure that preconditions the moment of tax obligation occurrence on the choice of the operator who delivers a given transaction.

The above proposition is also confirmed by the opinions of tax authorities which stated on many occasions, interpreting the tax law, that in the situation in question, the specific moment of tax obligation occurrence is determined by the form of delivery performance (handover of goods upon payment), and not by the type of operator performing the delivery.

Payment before shipping

Irrespective of the above forms of payment, the on-line sales practice witnesses most often payments before the shipping of goods. Therefore, the seller is obliged to recognise the amount paid as an advance payment, which – as a consequence – gives rise to a tax obligation with regard to the payment received at the moment it is received. In accordance with Article 19(11) of the VAT Act, if part of the due payment is received before the handover of the goods of performance of services, and in particular if the seller receives a pre-payment, an advance payment, a downpayment or an instalment, the tax obligation arises at the moment the part of the payment is received.

Although it is hard to perceive any payment equalling the total amount due to the seller as an advance in standard terms, this is irrelevant for the classification of the payment for VAT purposes as such an advance payment.

Customer's refusal to accept goods purchased

Sometimes, in case of on-line sales, situations may occur where the goods ordered are sent to the buyer with the sale confirmation document (receipt/invoice), however, the customer refuses to accept the goods referring to the current circumstances (withdrawing from the agreement). A question arises then whether the seller is obliged to account for the VAT indicated in the invoice/receipt issued for the customer, as the regulations oblige the seller to pay the tax arising under the document issued.

It seems, however, that in such a situation (refusal to accept the goods) the invoice does not enter the trade and thus (despite the invoice being issued) the VAT tax obligation does not occur. As a consequence, the seller is obliged to cancel the document issued as it does not practically document any sales transaction.

9. Corporate Income Tax (CIT) aspects

9.1. Allocation of costs related to on-line order sales

From the perspective of income taxes, the extension of business for an additional Internet channel does not entail any particular changes of the method of reporting income for tax purposes. Both the qualification and the moment of recognition of sales revenue or cost of goods sold do not differ than in the traditional sales where the general principles are used.

The important aspect may only be the qualification of so-called costs recognised close to the year end, related in particular to the allocation of costs to the proper tax year.

The proper allocation of costs close to the tax year end results directly from the regulations of the CIT Law. The Polish tax legislator obliges taxpayers to allocate to the closing year all the costs incurred already in the subsequent year, before the approval of the financial statements for the year ended as long as these costs are considered as direct costs. Obviously, as it is often the case with tax provisions, the CIT Law does not define precisely which types of costs can be considered so-called direct costs. However, the practice of the tax authorities indicates a rather narrow interpretation of the term: the direct costs are the ones that can be directly connected to specific income (individual sales).

In case of businesses of retail sales to consumers, it is hard to find any direct costs except for the traditional cost of goods sold. Therefore, the problem of cost allocation close to the year end remains purely theoretical.

However, if an additional distribution channel is implemented in the form of on-line sales, an additional category of expenses appears, not very important in traditional trade (with some exceptions): costs of services related to the shipping or delivery of goods to the place indicated by the ordering party. Such services, depending on how they are settled, can be either connected every time with a sales transaction made (and then should be considered as direct costs) or constitute one accumulated periodic (monthly or weekly, depending on the scale) charge for services performed by shipping and/or courier companies (and then should be considered as indirect costs), which are not subject to allocation mentioned above.

To sum up, if you decide to enter the on-line channel and purchase additional categories of services connected to sales, you need to consider the possibility of correct settlement with service providers close to the year end.

At present every consumer needs to be treated individually. Acting on the Internet allows for customization of the Clients' offers. However, you have to be very careful not to violate one's privacy during the observation of the Clients' behaviors on the Internet used for offers customization.

José Bonito
Customer Management Director
Makro Cash and Carry Polska S.A.

9.2. Settlement of returns for CIT purposes (practical issues related to reverse corrections)

An additional problem related to the recognition of costs at the turn of tax years results from potential returns of the goods previously purchased. Naturally, this is an issue that has been present before on-line sales became popular. The topic of proper settlements of goods returned is what we also face in traditional retail sales. However, compared to traditional sales, in case of on-line sales, the scale of the problem increases, as does the related risk. Here, the customer cannot evaluate the goods until he makes a purchasing decision and the goods are delivered.

So what is the risk about? There are no clear tax regulations that would precisely indicate how to correctly recognise/allocate to the proper year the returns of goods that were purchased by customers in the previous years.

Moreover, contrary to the cost allocation described above, the CIT Law does not regulate the revenue corrections. However, the tax authorities present their approach in this respect quite often. The tax authorities in particular in recent years have taken a stance that revenue corrections of, among others, returns of previously purchased goods should be recognised in the year when the related revenue was recognised. They argue that the revenue as such does not create a new transaction and, therefore, it should be connected to the original transaction.

However it is hard to question this standpoint to some extent, taxpayers for whom the corrections resulting from on-line sales will be significant, may face the additional burdensome administrative obligations.

9.3. Recognition of costs related to new system implementation for CIT purposes

In addition to costs directly related to the implementation of the on-line sales system, the costs of payments for using the software, rental of servers, adjustment of the database to local needs and conditions, translation and on-going technical support may be also incurred. Each one of these costs requires individual assessment for tax purposes.

Payment for the performance of services related to the implementation of the on-line channel may, as a rule, be recognised as tax deductible costs provided that the taxpayer can prove their connection with the business activity pursued and that such costs were not disallowed in tax provisions (such as costs of representation). It is important for a company recognising tax costs related to the implementation of a website that it obtains obvious benefits from the website operations by, e.g. posting advertisements of products sold by the company, posting information on the promotional campaigns currently held, on the properties of the services offered, etc. Therefore, an expense incurred by the group of which the company is a part of will not be a tax deductible item if the website presents, for instance, content other than the company's business operations.

The connection between the expenses incurred and the income generated should be properly documented for tax purposes, in the form of, among others, a cooperation agreement, reports provided, projects implemented, etc.

Proper qualification of the cost incurred determines the moment of its recognition for tax purposes. In accordance with the CIT Law, the costs related to the implementation of on-line sales as so-called "indirect costs" are deductible as on the date when incurred. However, if they relate to a period that exceeds the tax year and it is not possible to determine which part of them is connected to the given tax year, they shall be recognised as tax deductible costs in proportion to the length of the period to which they relate. In a situation where parties decide to sell the copyrights for use of software, such payments take the form of licence fees. In such a case, the payments for licence fees should be recognised for tax purposes, as a rule, when incurred. Nevertheless, a company that pays the agreed licence fees is charged with other tax obligations as discussed below.

In the situation where the sale of the copyrights for use of computer software or licences for use of computer software which has a value exceeding PLN 3,500 and that will be used for more than a year within the purchasing company's business operations, such sale entails a different method of recognition of tax expenses. In such case, in accordance with the CIT Law, the copyright purchased should be recognized as the intangible assets subject to depreciation, while the expenses incurred for their purchase should be recognised as tax deductible costs by means of depreciation write-offs[9]. However, if the agreement clearly does not provide for the transfer of copyrights, or the company is not provided with a licence or technical know-how, then no intangible assets should be recognized, and the cost for tax purposes should be recognised on an on-going basis when incurred[10].

[9] Cf. tax ruling issued by the Director of the Tax Chamber in Katowice dated 26 November 2010, ref. No IBPBI/2/423-1146/10/JD.

[10] Cf. tax ruling issued by the Director of the Tax Chamber in Katowice dated 11 February 2010, ref. No IBPBI/2/423-1394/09/BG.

9.4. New technology implementation vs. possible tax benefits

Implementation of new technologies, also in IT areas, is clearly promoted by the Polish legislator. As an example, the CIT Law provides for a tax relief for the companies who purchase intangible assets in the form of technical know-how.

A taxpayer who implements new technologies in the enterprise may deduct from the tax base up to 50% of expenses incurred for acquisition of new technologies.

It should be noted here that the said deduction is independent from the general principles of the tax depreciation. Therefore, the company may obtain a tax benefit in the form of recognition as tax costs of up to 150% of the new technology value (i.e. in the form of depreciation write-offs and the tax relief).

The legislator introduced no limitations with respect to specific types of intangible assets or selected sectors of economy from the perspective of the tax relief. Our experience shows that the technological allowance is already used by many companies, mainly operating in the telecom sector (implementations of modern ICT network software); banking sector (modern banking systems, e-banking solutions); manufacturing (production processes; formulas and know-how, ERP systems) and IT and Internet sector (modern IT systems, Internet platforms, payment systems and modern customer communication channels).

However, the possibility to use the new technologies tax allowance depends on fulfilment by the company of a number of requirements. These are, among others:

- the technological know-how implemented at the enterprise and constituting an intangible asset may not have been used globally for more than 5 years;
- an opinion of an independent scientific authority is to be obtained on the innovativeness of the said technological know-how;
- the solution implemented should enable the company to release new or improved products or services;
- the company may not sublicense the new technology;
- the company may not obtain in any form a reimbursement of expenses incurred for the new technology, nor he can it operate in a special economic zone.

9.5. Withholding tax on payment for system implementation

Under the provisions of the CIT Law, the entities making payments for the benefit of non-residents relating to the revenue generated in Poland under copyright and related rights, as well as the know-how provided and other services, including consultancy and advertising services, are obliged to charge 20% withholding tax (“withholding tax”). As observed in the tax practice, the said payments also include payments for the acquisition of the right to use computer software[11]. Given the fact that the list of payments for the said services subject to withholding tax is not exhaustive, it should be noted that the tax obligation also covers remuneration for design development, its implementation, growth and maintenance.

It should be underlined that the tax regulations provide for a reduced rate or a withholding tax exemption with respect to payment of licence fees and other payments. In the light of the double tax treaties concluded by Poland and the country of the said payments beneficiary, only selected payments are subject to withholding tax, whereas the other liabilities are treated as business profits that are not taxable in Poland (unless the foreign contractor has a so-called “permanent establishment” in Poland, see below). However, application of a reduced tax rate resulting from the relevant double tax treaty or application of a tax exemption in accordance with such a treaty is possible provided that the beneficiary seat is properly documented for tax purposes. The application of a tax exemption or a reduced tax rate requires each time an analysis of the payment made in terms of the provisions of the double tax treaty concluded between Poland and the relevant state where the taxpayer has its place of residence.

[11] Cf. tax ruling issued by the Director of the Tax Chamber in Warsaw dated 21 May 2010, ref. No IPPB5/423-134/10-4/PS.

9.6. Running business outside Poland – risk of creating "a permanent establishment"

Conducting on-line sales provides the company with the possibility to easily target the customers also from markets outside Poland. For business and logistic reasons, however, opening the on-line channel to foreign customers may require the company to maintain branches (establishments, warehouses) in other countries that could hand the goods purchased to foreign customers or that could carry out other activities related to international customer service (e.g. receiving complaints).

Obviously, there is a question whether pursuing business operations in other country generates an income which is subject to taxation there?

The developing trade relations between entrepreneurs in different countries have already forced creation of some boundaries for business operations performed in other countries which determine whether the income from such business is subject to taxation in that country. These boundaries have been set by the concept of so-called "permanent establishment". In international tax law, a permanent establishment means, as a rule, fixed place of business through which the business of an enterprise is wholly or partly carried on (in particular, a permanent establishment may include an affiliate or an office).

This mainly refers to situations where the business of an entrepreneur being a resident of one country operated in other country is significant enough and permanently related to such country that the country wants to participate in the taxation of profits generated by the business[12].

Therefore, a permanent establishment occurs if all of the following requirements are met:

a) there is a place of business,

b) the place of business is fixed,

c) the place of business is used for carrying out all or at least part of the entrepreneur's business.

In practice, a place of business may mean any place (office, part of a site or space) located in other country that remains at the disposal of the company. Yet, it is irrelevant whether the company has any legal right to use the place (ownership, rental) or not (the place may be used illegally).

However, when assessing whether the place of business has a fixed character, the following issues should be taken into account: the time for which the place has lasted (in international practice, it is usually assumed that a place of business is of fixed character if it has been used for at least six months), and the intent to use it permanently for carrying out business operations. Finally, creation of a permanent establishment depends on the fact whether the company uses it to carry out all or part of his business operations.

Tesco is one of few companies in the food industry where on-line sales is profitable. The key to success in introducing the on-line channel in the UK was the simplicity of the system, low product prices but also effective use of the existing organisational structures, and in particular of the physical shops. Building on that experience, we are developing an on-line channel in Poland that will operate on the basis of the existing shops. We will deploy additional warehousing and administration facilities and the use of the existing structure's potential will enable us to increase sales in the existing shops. In our model, traditional retail and on-line sales will operate in synergy.

Grzegorz Juszczyk
Tesco (Polska) Sp. z o.o.

[12] Read more on "permanent establishment": "Umowy o unikaniu podwójnego opodatkowania. Komentarz" [Double Tax Conventions. A Commentary], edited by M. Zasiewska, A. Oktawiec. J. Chorązka, published by: Wolters Kluwer, Warsaw 2011, pp. 92–124.

The international tax law provides for situations where although a fixed place of business has been created by a foreign company (i.e. a resident of a different country) for his business operations in other country, no permanent establishment occurs. It was adopted that the term "permanent establishment" does not include the use or maintenance of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise in location of other country.

There will be no permanent establishment also in situations where the company maintains a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character. In practice, it may be quite difficult to establish which business could be considered preparatory or auxiliary and which business could not. The OECD Model Tax Convention (which constitutes a template for most contemporary international double tax treaties) recommends the following to be taken into account when making such a distinction:

- whether a given activity/scope of business constitutes a separate and independent element of a given business of an enterprise,
- whether the business carried out in the place of business corresponds with the company's core business,
- whether the business is carried out upon commission and for entities other than the parent company,
- whether the business is part of after sales service.

Given the above considerations, we can assume that, as a rule, having a place of business (branch) in another country to store the goods to be delivered to foreign recipients shall not create a permanent establishment and, thus, there will be no tax obligation in other state relating to income generating in this respect. However, undertaking the additional business using such a place of business should be assessed each time in detail in terms of the character (preparatory or auxiliary) of such activity as compared to the entrepreneur's regular business. It may be helpful in this respect, as in case of Poland, to obtain explanations (interpretations, information) from the given state's tax authorities.

9.7. Return of goods purchased abroad

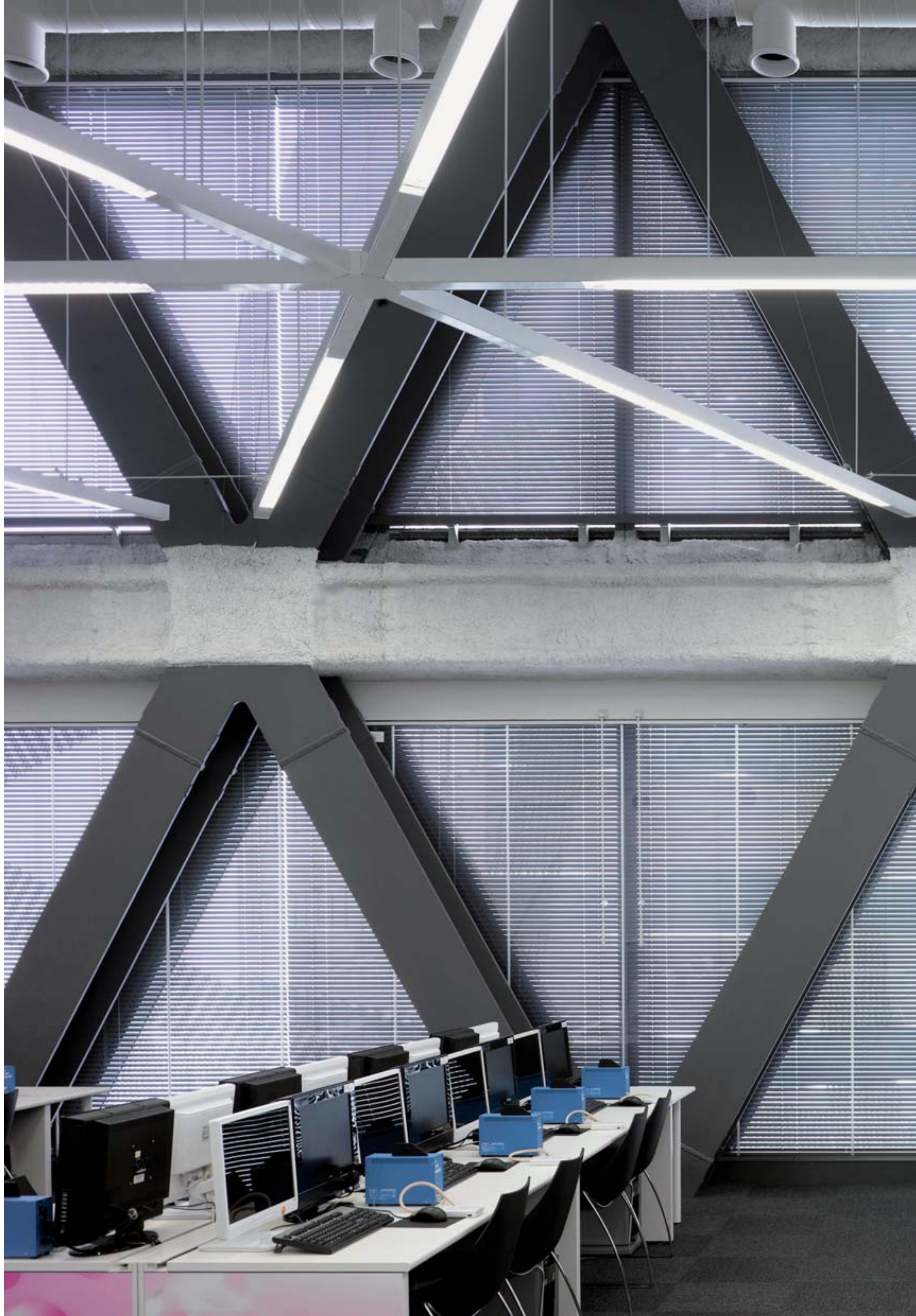
Running a business (not only through an on-line channel) which is targeted at customers from different countries may lead to a situation where customers purchasing goods in one country would return them in other country. In practice, such cases result from a specific sales and customer service policy adopted – it is a kind of a marketing tool: we provide the customer with free and easy access to our points of sale and after sales service.

Accepting the goods from a customer who bought the goods in other country shall not entail any tax consequences (except for the VAT where the movement of goods will constitute an intra-community supply of goods, which – when certain conditions are met – is taxed at a 0% rate) in a situation where the goods are then sent to the point where they were initially purchased (i.e. when we are only performing the role of an intermediate).

In practice, however, given the costs of shipping of the goods returned as compared to their value, the good received are retained in our stocks and are kept available for sale. In suchcase, it should be considered that the goods returned are actually purchased and the reimbursement for the return of goods constitutes the purchase price of the goods (therefore, in the future it will constitute tax-deductible costs when they are sold).

Unfortunately, the treatment of such a return as a purchase will result in an obligation to pay (by the purchaser) the civil law activities tax unless the value of the goods does not exceed PLN 1,000.

Practically speaking, due to unfavourable tax consequences of the situation described above, the development of the relevant procedures for receiving, warehousing and then shipping of the goods returned between points of sale located in different countries should be considered.



Concluding remarks

Is it worth to be on the Internet?
This is obvious.
The question is not "to be or not to be" but "how to be" on the Internet"?

José Bonito
Customer Management Director
Makro Cash and Carry Polska S.A.

The dynamic development of new technologies makes people transfer more and more aspects of their real lives to the virtual world. From booking movie tickets or making wire transfers through meeting people and making friends. Undeniably, commerce will also become increasingly present in the world wide web. This forces the presence of companies that do not want to lose their growing markets.

You can either ride the wave or get swept by it, said one of the customers, illustrating the growth of the e-commerce market. Within the last few years, the annual percentage growth of this sector in Poland was a two-digit number. This confirms the great potential of this part of the economy and its growing role in commerce in general. On the other hand, e-commerce is much different from the traditional channel, which requires new ideas and visions for growth. Obviously, companies that want to operate effectively in the global network need to overcome a multitude of obstacles and learn about the ways of presenting and advertising goods, as well as customers' expectations and preferences.

Despite multiple challenges and barriers, establishing an on-line sales channel seems a must today. We should remember that e-commerce is not only about technical networking solutions but most importantly it is a concept for growth and a brand recognisable to Internet users and existing in their awareness.

It seems that the key to success is to look at the on-line sales channel not as one of many ways of selling goods, but as an entirely new business area of invaluable importance in the future.

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