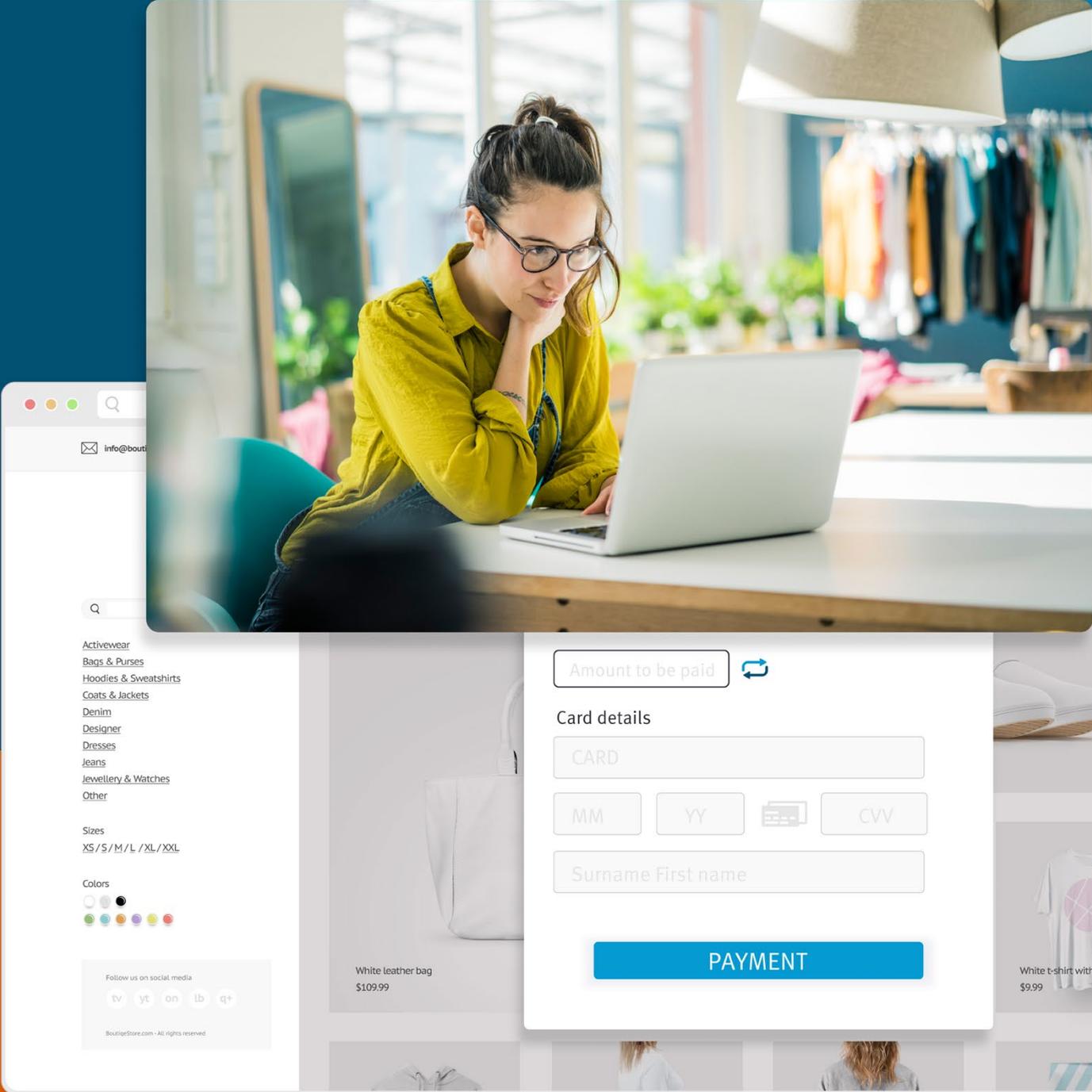


SOLVING TOP TAX COMPLIANCE CHALLENGES FOR SHOPIFY BUSINESSES

Expert-sourced tips to help
keep your business in the clear



Executive summary

Who this guide is for:

Ecommerce merchants and businesses that currently have stores on Shopify or plan to do so in the future.

In particular, you'll find this guide helpful if your Shopify store sells at high volume, internationally, or across state borders.

What you'll find inside:

Dealing with taxes is a universal pain point. For Shopify merchants trying to navigate growth, expansion, and evolving regulatory pressures, it's only getting more painful. This guide is designed to contextualize these challenges and offer real solutions. Learn the what, why, and how of an effective tax compliance strategy on Shopify that leverages the latest technology and innovation, with guidance from industry experts.

Featured voices:

Blake Oliver, *Founder and CEO, Earmark*

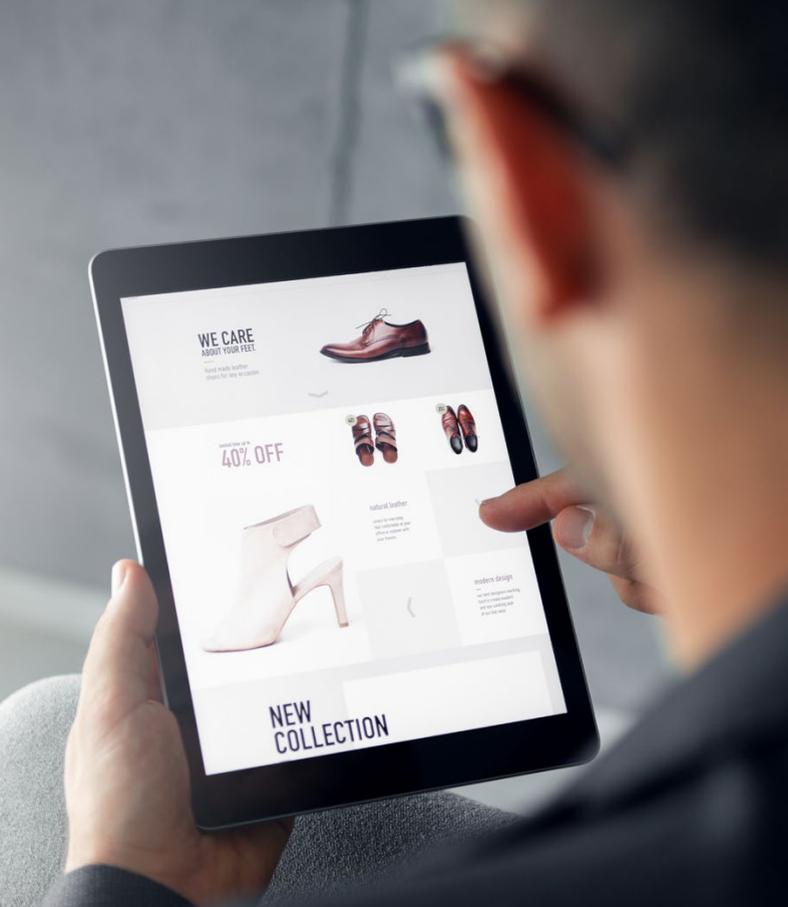
Vinny O'Brien, *Ecommerce Consultant, Vinny&Co Consulting Limited*

Linda Bustos, *Owner, Ecom Ideas*

Jeremy Horowitz, *Managing Partner, Because Ventures*

Kunle Campbell, *Founder, Conscious Commerce*





The evolution of tax complexity

Let's turn the clock back 10 years. In those days, online sellers operated in a fairly casual environment. Businesses were typically responsible for collecting and remitting sales tax only in states where they were actually located. Laws were simpler, and ecommerce was still emerging as a dominant force. Fast-forward to today, and the landscape is significantly more complex.

There is a lot to keep track of, and the stakes are high. Failure to comply can lead to a host of negative and disruptive consequences, including financial penalties, legal risks, and reputational damage. But the good news is that powerful tools and techniques are emerging to help you confidently streamline and automate ecommerce tax management.

Major shifts have reshaped tax compliance for digital sales, compelling businesses that sell online to think more deeply about their current and future practices.

In this guide, we'll take a deep dive into tax compliance for sellers on one of the world's largest ecommerce platforms: **Shopify**. You'll find research-driven insights, illustrative examples, and expert tips from our own team as well as some of the top voices in digital selling.

Chief among these shake-ups was the 2018 U.S. Supreme Court decision in *South Dakota v. Wayfair, Inc.*, which ruled that states can require out-of-state sellers to collect and remit sales tax on transactions even if the seller does not have a physical presence in the state.

This is your guide to helping keep your Shopify business in the clear, long-term, as you grow your business and scale your sales.

Today, ecommerce merchants who sell in the United States must be aware of varying economic nexus thresholds, while international ecommerce sales carry their own set of stipulations, such as VAT obligations and digital service taxes. In general, the rate of change in tax codes and regulations around the world has accelerated greatly.

By 2027, about

23%

of total retail sales will happen online.

(Shopify)



Blake Oliver

Founder and CEO,
Earmark



Why has tax compliance grown so complex?

The Wayfair decision turned the world of ecommerce taxation upside down, transforming a simple physical presence rule into a maze of economic nexus requirements for online sellers.

Pre-Wayfair, you only collected sales tax where you had physical presence. Now, economic activity alone triggers tax obligations across multiple jurisdictions. Businesses have to track sales volumes across states, register in new jurisdictions when they exceed thresholds, and keep up with constantly changing compliance requirements.

The impact has been dramatic, and the cost of manual compliance is unsustainable. But many businesses – particularly smaller ones – still struggle with multistate registration, varying remittance schedules, and complex exemption rules.

As tax authorities worldwide move toward electronic systems, technology adoption isn't optional – it's essential for survival. For online sellers to succeed in this new landscape, they need compliance strategies and technology solutions that can scale with their growth. The future of ecommerce tax compliance is digital, and that future is already here.

The growth of Shopify for ecommerce

Since being founded in 2006, Shopify has grown into a cornerstone of the modern ecommerce world. Consider these platform statistics, courtesy of [Backlinko](#):

More than **2 million merchants** use the Shopify platform, which hosts upwards of 4.5 million live websites.

Shopify has merchants in **175 countries** around the world.

It took Shopify seven years (2013) to first surpass **\$1 billion in gross merchandise volume**. In 2023 alone, Shopify processed about **\$235 billion in ecommerce sales**.

Shopify merchants had a total of **675 million buyers** in 2023.



Its intuitive interface, customizable storefronts, and robust app ecosystem make Shopify an attractive choice for businesses of all sizes.

For stores and merchants with an eye on growth and scalability, there are a range of helpful features available, such as flexible infrastructure and omnichannel capabilities.

But with growth and scale come a number of practical challenges, and tax compliance ranks highly on that list. While the Shopify platform has several built-in tools to help you seamlessly run your store and manage basic tax obligations, larger or growing businesses often require additional support and specialization.

The intricacies of tax compliance don't need to be intimidating. We're here to help. Avalara has been a proud longtime partner of Shopify, providing tax calculation services for Shopify Plus customers since 2015. More recently, Avalara became one of the first partners on the Shopify Tax Platform for further integration and simplicity.

The following sections will explore how taxes work natively within Shopify and how to navigate numerous scenarios that warrant added support.



Understanding taxes on Shopify

Shopify's built-in tax features provide a solid foundation for handling basic sales tax needs, including automatic tax calculation based on location, tax overrides for specific products, and default settings for common scenarios. These tools are often sufficient for businesses with straightforward operations, such as single-state sales or nontaxable products. However, understanding the limits of Shopify's native capabilities is key for assessing when additional compliance solutions may be needed as your business grows or becomes more complex.

It's important to take a big-picture view of your ecommerce business and its future. Even if some or all of the above conditions apply right now, will that be true in one year? Five years?

Let's explore some of the specific challenges that might prompt a deeper look at your tax compliance strategy.

The number of shoppers placing an order with Shopify merchants has increased by

47.7% since 2020. *(Backlinko)*



Vinny O'Brien

Ecommerce Consultant,
Vinny&Co Consulting Limited



What are the key priorities for Shopify merchants right now?

If 2024 was a year of efficiency gains, 2025 needs to supplement this with a real growth strategy. Without any surprises.

Understanding increased compliance and regulatory challenges should be key focus areas for brands seeking growth.

Many struggle to handle the correct setup for handling domestic and international tax requirements including reporting requirements. Bad data in, bad data out. This limitation curtails going after opportunity.

Shopify has excelled over the last number of years in presenting a self-serve environment. Tax handling is something they have not mastered. Natively, they struggle to simplify a few things:

1. Understanding the requirement
2. Implementing the right setup confidently and accurately
3. Creating simple reporting

Getting this wrong is not acceptable in 2025. Increased regulatory scrutiny can carry fines where reporting requirements are not met. Operationally too, many brands limit their growth strategy because compliance at scale is not made easy by back-end processes.

Finally, there is the small matter of customer experience. Efficient operations lead to excellent customer experiences. This is where smart brands win.

Avalara has a strong reputation for providing global setup options for ambitious brands. Their Shopify integration combines domain expertise with simple integration where data flows accurately and confidently, allowing you to focus on growth.

Challenges and roadblocks in tax compliance

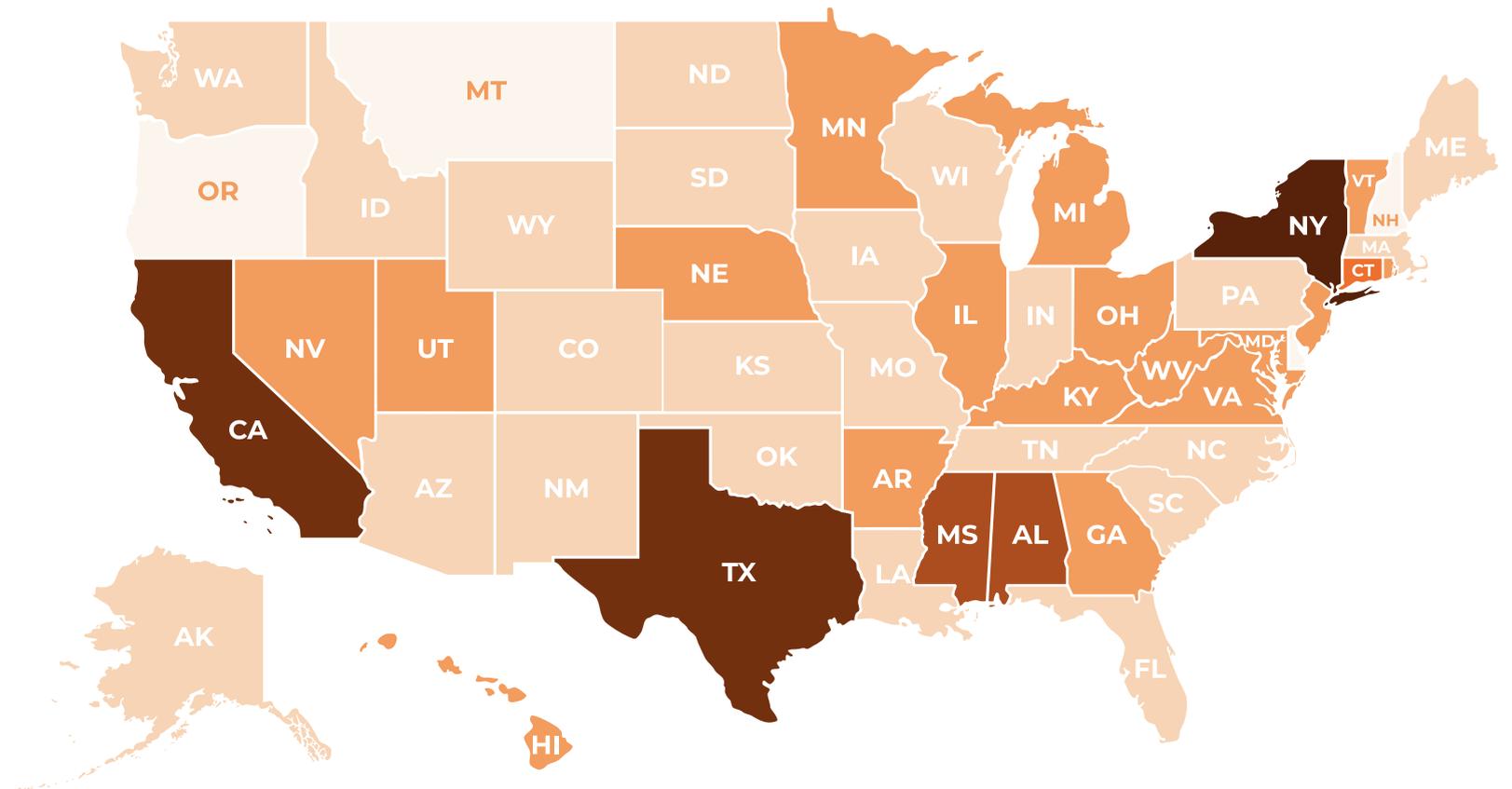
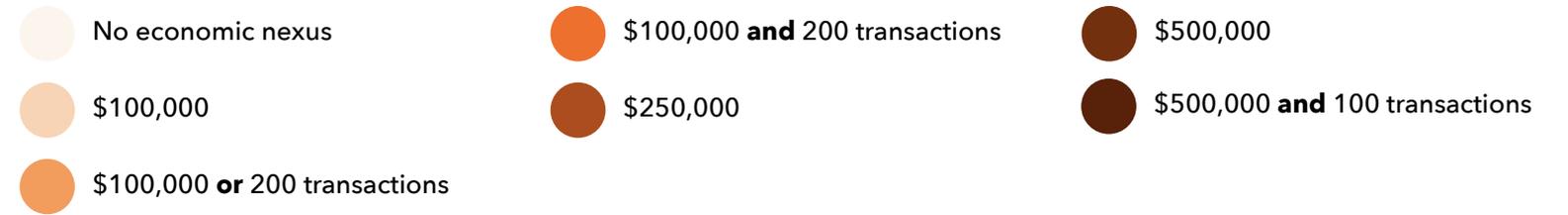
Navigating tax compliance as a Shopify merchant can feel like walking a tightrope – balanced and manageable until growth, new markets, or changing regulations hit like a stiff gust of wind. While Shopify equips merchants with powerful tools to build and scale their businesses, the complexities of tax compliance often extend beyond its default capabilities.

These are examples of challenges faced by Shopify merchants that can often require a great deal of effort and energy to address:

Varying economic nexus thresholds

Each state and country has its own sales tax rules. Some require collection after a set number of transactions, while others base it on revenue thresholds (or both). Monitoring and managing these thresholds can be daunting.

Thresholds legend



Sample scenario: A Shopify merchant in Arizona expands its online sales nationwide, unknowingly surpassing California’s \$500,000 sales threshold and New York’s \$500,000 threshold without registering or collecting taxes.

International tax complexity

Selling globally introduces new layers of compliance. For instance, many countries require the collection and remittance of value-added tax (VAT) or goods and services tax (GST). These taxes are consumption-based, applied at each stage of the supply chain, and vary by country.

For example, the European Union requires VAT registration in the customer's country once sales exceed a specific threshold, while Australia mandates GST collection for all goods under AUD 1,000. Grappling with varying rates, registration requirements, and reporting obligations can be challenging without proper systems, especially as cross-border sales grow.

Additionally, calculating customs duties and import taxes for international transactions is a time-consuming responsibility for ecommerce businesses. It requires staying up to date with constantly changing tax rules, trade regulations, and country-specific tariff codes, often across hundreds of jurisdictions.

VAT (value-added tax): A tax applied at each stage of production or distribution based on the value added to a product. Common in Europe and other regions, it's ultimately paid by the end customer.

GST (goods and services tax): A similar consumption tax that applies to goods and services, typically charged as a single rate at the point of sale. Popular in countries like Australia, New Zealand, and Canada.



Linda Bustos
Owner, Ecom Ideas



Why does tax compliance feel like such a moving target in ecommerce?

For fast-growing Shopify merchants, expanding to new geographies and third-party selling platforms adds complexity to tax compliance requirements, and the rules can change at any time – from both governments and tech platforms.

For example, in 2022 Etsy abruptly removed its tax tool for Canadian shops which applied the appropriate provincial and federal taxes to each Canadian sale, forcing sellers to build taxes into their top-line pricing and remit taxes using reverse calculation, midway through their fiscal years.

Platforms like TikTok may collect and remit sales taxes on your behalf and still push tax data into your Shopify, but this issue may be fixed by the platform any moment.

Governments may even announce temporary changes to sales tax, such as Canada's two-month GST holiday which left merchants scrambling to update retail and online systems to accommodate the various tax-exempt products on extremely short notice.

It's critical that merchants stay aware and nimble to navigate these nuances. Look for automated tax compliance solutions that handle the majority of real-time updates but that also have flexible APIs to handle any non-standard requirements that may emerge across your sales landscape.

Multi-platform coordination

Selling across multiple platforms and channels – such as Amazon, Etsy, eBay, and physical stores – can complicate tax compliance for Shopify merchants. Each platform handles taxes differently; for example, Amazon collects taxes as a marketplace facilitator, while Shopify requires merchants to manage their own tax setup. Tracking these variations across platforms can too easily lead to gaps, redundancies, or errors.

The need to monitor nexus thresholds, or international rates and requirements, also becomes more complicated when running a multi-channel approach.

Product taxability nuances

We've shared these quirky examples before: Did you know that in New York, tacos are taxable, but burritos aren't? Or that in Indiana, a Snickers bar is taxable, while KitKat and Twix aren't? Orange juice is taxed more than 300 different ways in the U.S. alone! These seemingly arbitrary delineations help illustrate the complexity of product taxability, which can vary based on a wide range of factors.

Products and services are taxed differently (or not at all) in different jurisdictions based on how they're categorized, or their intended use. Beyond food and beverages, these are just a few types of products that are subject to taxability nuances:

- Digital content
- Bundles
- Subscriptions
- Health-related products
- Event-triggered taxability (e.g., buy one, get one)

Although Shopify provides merchants with the ability to set up tax overrides and custom rules, they must be manually configured. As you might imagine, keeping track of all these details is an extraordinary challenge.



“We chose Avalara because we realized that they have the right expertise and could so easily connect with our Shopify platform. I recommend it as a solution that can help you automate your tax filings and tax calculations as well as being a technical solution that’s very easy to use and implement.”

Ann Masson, Chief Financial Officer, Iconic London



The cost of noncompliance

Why should ecommerce merchants take tax compliance seriously? Failing to stay in the clear can lead to a multitude of negative impacts for your business, including damage to customer trust and merchant reputation. But the most immediate and palpable risk of noncompliance is audits and fines.

A study conducted by NetReflector/Potentiate and Avalara found that:

- Audits required an average of **35 employee hours to respond**, with some audits exceeding 100 hours of staff time. For smaller businesses (SMBs), overseeing these audits cost an average of \$4,679, more than 200% higher than the cost for enterprise-sized businesses (ESBs), which average \$1,471 per audit.
- For some companies, **audits drag on for months**, compounding stress and resource drain.
- The top triggers for penalties are **sales tax rate or rule errors**, and **missing exemption certificates**.

Note: These results reflect the answers of respondents to a 2021 survey and not all businesses.

Exemption management

Nearly every seller encounters tax-exempt sales, whether due to non-taxable products, buyer exemptions like resale purposes, or other qualifying reasons. Every exempt sale requires collecting a valid exemption certificate, ensuring it's accurate, and keeping it organized for future audits. With varying rules across states and the need to track expiration dates, managing these certificates on your own can quickly become overwhelming, especially as your business scales.

Mistakes in exemption management are a common target for auditors, as even minor errors can result in penalties.

Refunds and exchanges

Shopify's native tools for handling partial refunds and exchanges often fall short in ensuring tax compliance. For partial refunds, the platform may not automatically adjust sales tax, leading to discrepancies between the original tax collected and the refunded amount. This issue becomes even more complex with multi-item orders, where it can be unclear how much tax to allocate to specific refunded items. Exchanges present additional challenges, especially when items of different values are involved.

Best practices for a tax-compliant future

In spite of all the pain points we just covered, tax compliance doesn't have to be a headache. By adopting future-focused strategies and leveraging automation, Shopify merchants can simplify processes, gain confidence in compliance, and focus more on growing their business.

Below are expert-recommended best practices to stay ahead and in the clear:



Monitor and manage economic nexus: Regularly track your sales activity to identify when you've surpassed economic nexus thresholds in specific states. This involves consolidating data from all sales channels and ensuring you register to collect taxes in any new jurisdictions where obligations arise.



Automate tax calculations: Use tools that provide real-time tax calculations based on precise factors like customer location, product category, and jurisdiction-specific rules. Automation reduces errors and helps ensure customers are charged the correct tax rates every time.



Stay updated on tax codes: Tax laws change frequently at both state and international levels. Employ systems that automatically update tax rules to keep your business compliant without requiring constant manual research and adjustments.

Avalara for Shopify removes the guesswork:

- Identifies product-specific tax rules across jurisdictions
- Regularly updates tax rates with real-time changes across 12,000+ jurisdictions



Jeremy Horowitz

*Managing Partner,
Because Ventures*

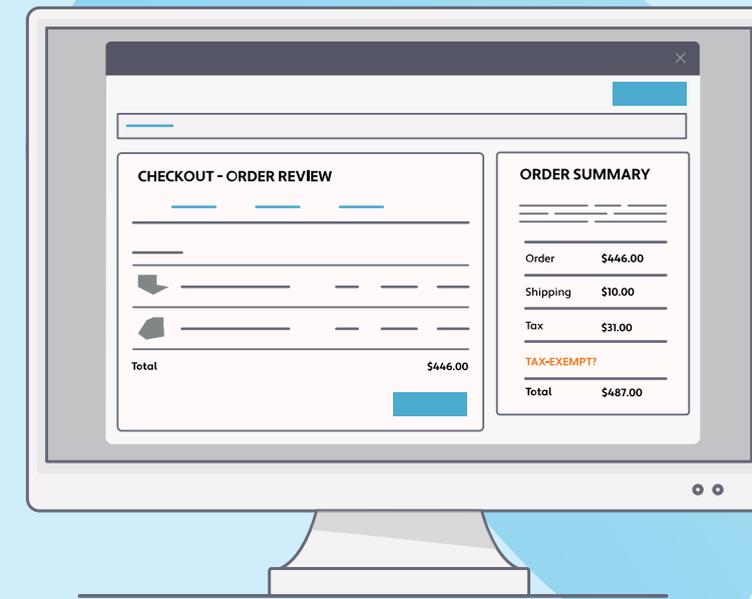


What's the biggest tax challenge for ecommerce businesses on Shopify?

The greatest tax challenge Shopify merchants have is not knowing all of the local, state, and municipal tax laws where they operate. It's just too much to monitor for a small to midsize businesses.

There are too many specific tax codes for a brand to keep track of. When you do and don't collect tax, how much to collect, and what you should remit. It's a massive data problem that brands won't have the internal expertise to handle.

At this point, solving this problem requires software to properly calculate, collect, and remit sales tax in every region a brand operates within.



Streamline cross-channel compliance: If you sell on multiple platforms, integrate them with a centralized system to unify tax data. This enables consistency in tax calculations and reporting, regardless of where a sale occurs, reducing compliance risks across channels.



Collect and manage exemption certificates: Develop a streamlined process for collecting and validating exemption certificates from customers claiming tax-exempt status. Store these certificates securely and set up reminders for renewals to stay audit-ready and avoid penalties.



Leverage automated reporting and filing: Use automated tools to generate and file tax returns more accurately and on time. This reduces the risk of late filings, errors, and the associated fines, while saving valuable time for your team.



Conduct regular compliance audits: Periodically review your tax compliance processes to identify gaps or discrepancies. Audits can help you address issues proactively, ensuring that you're prepared in the event of an official review by tax authorities.



Work with domain experts: Partner with professionals or platforms specializing in tax compliance to access their expertise and ensure your processes are aligned with the latest regulations. Expert guidance can save time, reduce errors, and provide peace of mind as your business grows.

Managing exempt sales, made easier

Tax-exempt sales – like wholesale or resale transactions – add extra complexity. You're required to collect, validate, and store exemption certificates, which can quickly become messy and prone to errors, especially as you grow and sell in more markets. And when auditors come calling, missing or invalid certificates can mean costly penalties.

We recently introduced Avalara Exemption Certificate Management (ECM) to Avalara for Shopify through a subscription to help you. Here's how it helps:

Simplifies collection: Exempt customers can easily submit their exemption certificates directly through your Shopify store.

Automates validation: ECM checks certificates for accuracy, like missing details or signatures, so you're confident they're valid.

Organizes records: Cloud-based storage means your certificates are always accessible, neatly organized, and ready for audits.



Kunle Campbell

Founder, Conscious Commerce



Why is it important to work with tax compliance leaders in technology?

1. Save time and resources: Tax compliance involves navigating a web of complex regulations, endless paperwork, and recurring filings. Automating these processes with technology allows your team to focus on growing the business instead of getting bogged down by administrative tasks.

2. Avoid costly compliance pitfalls: Tax regulations differ across regions, whether it's sales tax in the U.S. or VAT in the EU. Noncompliance can result in unexpected penalties, audits, or disruption to your business. Working with compliance experts ensures that your ecommerce brand stays on top of these requirements.

3. Seamlessly enable cross-border ecommerce: Expanding your ecommerce business to new markets comes with opportunities and challenges. Navigating international tax laws, duties, and customs requirements can be complex, but with the right compliance support, cross-border ecommerce becomes a manageable and lucrative growth strategy.

4. Future-proof your business: While setting up tax compliance processes can feel complex at first, it's a long-term investment in your growth. A robust compliance infrastructure reduces errors, mitigates risks, and creates a scalable framework for future expansion.

5. Blend technology and expertise: Pairing technology with professional guidance delivers both efficiency and confidence. It's a strategic way to manage compliance at scale, without overloading your internal team.

By working with experienced technology and compliance partners, your ecommerce business can operate more efficiently, reduce risk, and focus on serving customers while confidently navigating the complexities of tax regulations.

About Avalara

Avalara makes tax compliance faster, easier, more accurate, and more reliable for 43,000+ business and government customers in over 75 countries. Tax compliance automation software solutions from Avalara leverage 1,200+ signed partner integrations across leading ecommerce, ERP, and other billing systems to power tax calculations, document management, tax return filing, and tax content access. Visit avalara.com to improve your compliance journey.

THE FUTURE OF TAX COMPLIANCE

Business growth is exciting. In the era of ecommerce, traditional barriers are being demolished; your expansion potential can feel limitless. Don't let tax compliance become an inhibitor to growth.

By understanding the landscape, anticipating challenges, and implementing best practices, businesses can confidently meet their obligations

while staying focused on scaling up and pursuing new markets. Technology and automation hold the key to forging ahead with efficiency and confidence.

Tax compliance may be complex, but it doesn't have to be overwhelming. With expert tools and trusted partners like Avalara, Shopify merchants can navigate the future of ecommerce with peace of mind.

Ready to simplify your tax compliance journey?
Learn more about Avalara for Shopify today.

Get started

Tax rates, rules and regulations change frequently. We hope you find this information helpful, however, this resource is for informational purposes only and does not provide legal or tax advice.