The cost of I2P non-compliance

Spend Matters™

TUNGSTEN NETWORK

a KOFAX company

Part 1

The Power of the Invoice

When did the humble invoice become so important? The invoice has always been a promise to pay for goods and services. But now, in the 21st century, the invoice has been elevated to more lofty heights.

The supplier invoice is a critical document in the trade cycle, and is used not just as a request for payment, but also as an accounting document for suppliers and buyers, and as evidence to support tax reclaims or payments to or from governments.

Organizations must therefore take appropriate steps to fulfill their accounting obligations and responsibilities, and audit and satisfy the legal and fiscal requirements of the authorities. Traditionally, invoices have been issued on paper, providing the regulatory authorities with sufficient detail to enable audit activities. However, in most jurisdictions, paper invoices and electronic invoices are now treated equally. With many countries having abolished paper invoicing through e-invoicing mandates, tax authorities around the world are increas ingly making compliance mandatory. In these three chapters we look at the cost of non-compliance.

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When you think of the billions of transactions that take place every single day in the B2B buying world, the possibilities for error during the buying, supplying, paying, and getting paid process, are manifold. At the same time, tax rules for B2B invoicing are different around the world, and regulations can change rapidly, especially now that governments are starting to get involved in invoice-to-pay (I2P) financial supply chains.

It costs time, money and business disruption if you don't get it right, and with increasing demands for compliance, non-compliance can be very damaging for both sides of the B2B transaction. In this guide, produced in conjunction with Spend Matters, Ruud van Hilten, SVP Country Compliance and Strategic Business Development at Tungsten Network looks at the true cost of I2P non-compliance and how, as your business grows, you can manage your compliance responsibilities.

So What Do We Mean By I2P Non-Compliance?

To be 'legally' compliant means we must act in accordance with local/national legislation or requirements: these might focus on how invoices are processed, transmitted, or stored. Then we have to be 'tax' compliant, where we must comply with the local/national tax laws and have that correctly reflected in our invoices.

It's a complex task for businesses, and getting it right is hard. Mandates are not harmonized across governments or regions, neither from a technical standpoint nor a legal one. Organizations are therefore more and more concerned with streamlining their processes to protect their business from the cost of non-compliance. And as the consequences of not getting it right can be severe, many organizations choose to outsource that responsibility to a third party, one that knows exactly how to get it right.

"Invoice-to-pay costs time, money and business disruption if you don't get it right, and with increasing demands for compliance, non-compliance can be very damaging for both sides of the B2B transaction."

The Issue With Compliance

As Ruud explains, "In order to understand the cost of e-invoice non-compliance, we have to understand compliance, and that means understanding not just the legal obligations of processing an e-invoice, but the tax implications and requirements too. And those requirements are different all over the world."

"First of all, we have to consider that any invoice is a living legal document, and as such is subject to audits. Buyers rely on its accuracy to settle with suppliers and to reclaim value-added tax in whatever local format that takes. So there is a taxation element to invoices that should be taken very seriously, because failure to do so runs substantial risk; invoice audit failure can result in monetary penalties or even criminal charges."

"Tax on the value of goods or services delivered to a customer, whether called VAT, GST or sales tax, depending on the region, must be reflected in the invoice - it's an obligation that every country has. The problem is that each tax regime differs; what a government requires a business to do can be hugely different depending on the region, and even inside of a region, like Europe, there are country differences between what makes up a compliant invoice."

"Companies have to consider whether their invoices satisfy the requirements of their local tax office, specifically if they are domestic invoices; that is, to a buyer within their own country, or whether they satisfy the requirements of multiple countries' tax offices if they sell to different countries. There are so many variables."

A Problematic Landscape

The invoicing landscape is home to many variants and every organization must familiarize itself with the legal requirements of each country it deals with - or find someone who can. Whether wilful or genuine, errors pose a significant threat not just to businesses, but also to governments.

"It's no secret that tax evasion and tax avoidance takes place," says van Hilten, "and they can create significant tax deficiencies for countries in terms of the tax they receive compared to what they should receive (a so-called VAT Gap). This shortfall leaves a country with less money to invest in the likes of education, infrastructure and healthcare. In the EU alone this equates to over €165 billion. Countries are missing out on a staggering amount of money, and clearly they need to find ways of curtailing that, so in recent years governments have invested more in technology that can help them get a better grip on tax payable — the business case is a no-brainer!"

"In that regard, governments have started to place themselves inside the financial supply chain, within the flow of invoices from supplier to buyer. In many countries plans have been launched that force the supplier to register invoices before they go to the buyers to be settled. Italy is one example - it's no longer the case that we can simply send an invoice and expect to get audited a few years later. In essence, you are audited before you complete the transaction."

"By deploying technology, they can force the behaviors of buyers and suppliers. From a tax-due perspective it's a very logical thing for a government to do, but from a business point of view, it can seem very intrusive. The objectives for governments to impose a mandate are often in total opposition to the objectives of companies to drive their digital agenda. And companies have to plan for this: maybe the IT department isn't ready to integrate with that technology, or maybe you didn't budget for it. Complying with these regimes is difficult enough in one country, even more so if you are dealing with tens of country regimes."

Non-Compliance Is Not An Option

The problem is, if you don't comply, you risk penalties. And in some countries, a supplier can't even invoice a buyer, because the government will reject the invoice. "Firms that have offshored their AP to lower-wage countries, for example, often find themselves moving it back into their own areas to better satisfy these regimes. But these mandates are not set out to drive efficiencies for the company. When we follow just what the government requires us to do, the efficiencies you've built up in your cost-savings initiatives can deteriorate, because of extra time and money investment. So it's fair to say that what's good for government isn't always good for business. On the other hand, this movement from governments can stimulate greater digitization, which is a positive. However, that requires a business to partner wisely and not make the mistake of trying to implement these mandates in house."

The Hidden Consequence Of Mandates

When a government imposes a mandate, you can guarantee it will not be a one-off. "Governments will look for continuous improvements, maybe other areas of taxation they can pull in, and will drive you to constantly do more as a business to satisfy the compliance agenda. Often they will bring other pieces of information in to be part of the invoice, for example Tax Deducted/Collected at Source, as is the case in India where the income tax requirement has been added as an obligation for compliant invoicing. You can suddenly be in a position where your systems have to be able to output this and you must adapt your processes to fit”.

Of course, there is also an element of reporting to comply with government legislation in terms of revenues and accounts, and all can be done online. That component is also starting to move into invoicing, in so-called “hybrid mandate models” - so there’s a convergence of worlds in some countries: reporting can take the dominant role in some, and e-invoicing in others.

“The point is,” says Ruud, “you have to stay on the ball with all the different obligations, and make sure your back-end systems are ready to comply. There’s a lot of ambiguity around taxation and it’s something none of us likes, because unlike developing a new product, or implementing a new system, this change comes from the outside, and is beyond our control.”

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Part 2

Where’s the harm?

The landscape is unstable as more countries emerge from the relief programmes put in place to keep their businesses afloat during Covid. This instability is felt particularly by the sector of the economy most susceptible to fluctuations - SMEs.

“While not always the case, most large corporations will have a tax team, because enterprises are subject to a lot of scrutiny and there is significant pressure to make sure the business complies,” says van Hilten. “But what happens with the backbone of any economy — the SMEs?

“Most governments with mandates offer a portal that you can connect with manually to enter your invoices. So the technology, albeit not very elegant, is available - but in the real world of the SME, no-one wants to, or has the resource to, key-enter invoices into a government portal. It’s not part of their core job. In addition, these portals are rarely designed for ease of use. For companies that send high invoice volumes, governments usually offer a facility to connect finance systems directly to the government platforms using APIs or other technologies, which is fine if you have a solid tax and IT team at your disposal that understands what they need to do, what’s coming, and can plan ahead.”

“For those that have no in-house capability to do that, or to plan for it, it’s almost certainly going to affect their operations and their IT budget. Even if they have already rationalized their vendor base, or digitized their procurement process, mandates are still disruptive and expensive. How you submit information to the government in a prescribed file format and how you receive information back from the government needs to be project-managed. And you may need to review some projects you already had planned. Compliance with mandates can therefore be a rather painful exercise, particularly for smaller firms that may not have the IT capacity in place to comply.”

Compliance For Business Continuity

Of course if you don’t comply, there are penalties. These aren’t just in the form of fines or fees. If you don’t, or can’t, comply with an e-invoicing mandate, you simply can’t send invoices to your buyers to get paid, and at some point, your cashflow will break. “If you are just doing business in one country with local firms,” explains van Hilten, “then you may be able to manage it, but if you are the leader of an organization doing business in multiple countries and regions, this requires real planning. You need to look at a more continuous solution, because compliance mandates will continue to be implemented and they have a tendency to become more complex and with shorter deadlines. “If you plan to do it all in-house, you’ll need to get your ERP system adapted to connect to the government portal. The tech is available, and a good IT department can work with the government APIs to do that. But the question isn’t if you want to do it yourself — it’s more should you do it yourself? And for an SME the question is more pertinent – can you afford to do it yourself?” The answer to both those questions is no!

Why You Shouldn’t Take An In-House Approach

“This is an extremely complex exercise,” warned van Hilten. “And it’s expensive. Should you undertake this yourself, aside from all the requirements to understand the intricacies of the
various mandates and regimes, and foresee changes ahead, governments will continue to update and change legislation, the obligation to comply will become more and more stringent and you’ll have to be ready to make more and more changes. Not to mention the time and resource it takes.

The best advice is to outsource the elements you can to a third party that specializes in automation of trading documents, like invoices, and that can connect with governments quickly on your behalf. There’s more to compliance than just creating compliant invoices, you want to create efficiencies, because government mandates in themselves don’t drive any digitization in the supply chain or automate any processes, what they do is give the government what it needs.”

“If you work with a third party, it’s advisable to find one that will do more than just comply with regulations. A specialist with all the right instruments in its toolbox will enrich and add value to your invoices and improve the invoice data. As a buyer this means you can run a more efficient P2P or AP process, and as a supplier you can rest assured you’ll get paid on time. Equally important is to work with someone that can give you transparency. Governments have added a whole new layer of approvals and scrutiny to the process: you need to be able to see where your invoice is in the flow, whether it's approved, or whether you need to resubmit — and do it quickly. Otherwise your cashflow is at risk."

How to Avoid Non-Compliance

The mildest consequence of non-compliance is that you'll be in the bad books of the tax authority, and they will probably audit you more often, which can be costly and disruptive. Audits are not easy things; they force you to free up resource and take time away from your normal business operation. And as Ruud says, "once you are in their bad books — you'll stay there for some time". To avoid this, there are two key things to remember:

1. Make sure you don't get caught by surprise - make sure it's on the radar of your tax team and plan for it.

2. Don't even try to do it yourself – do not go down the rabbit hole of doing it once then having to continue to do it for a long time to come.

Then there are the penalties, which can run into significant amounts of money, and that comes on-top of the increased scrutiny. "The worst case scenario is criminal damage," van Hilten advises. "It can affect your reputation, your public image, your customers, and your suppliers. In some countries, non-compliance is seen as tax evasion and can be considered a federal crime. Of course not all non-compliance is wilful, but the law is often nebulous and it's easy for people to make mistakes. "But whatever the cost of non-compliance," he says, "it will
always disrupt your business. You're just better off getting it right the first time.

Part 3

Taking the right action

How To Ensure Invoice Compliance:

1. Use a third-party provider – regardless of who that is.

2. Choose a real specialist with diversified service levels – one that the largest companies on the planet, as well as some of the smaller ones, have put their trust in.

3. Find a provider that has tax experts in-house and collaborates with other experts to be on the front foot of legislation.

4. Identify an expert that has the ability to turn a validation project into a business value project through the added efficiencies of a network ecosystem.

5. Make sure that network is safe and secure, and can ease the accounts payable process with higher visibility, greater insights and speed.

What You Need From Your Compliance Partner

"First of all," explains van Hilten, "you need to find a provider that understands exactly how different government systems and mandates work, their requirements and the consequences of not meeting them. You need a specialist that is very well versed in transmitting trading documents, like invoices, and has expertise in archiving these documents properly — as with all government mandates, there is usually a requirement to store documents compliantly as well as create them. It's an area that is subject to significant legislation."

So what does this mean? It means you need to find a partner that does e-invoicing for a living, and for whom it's not a side product. "At Tungsten," he says, "this is the core of our business: the organization, system and network are all built around, and built for, providing compliant e-invoicing as a service. "Your partner must be able to ensure all mandatory fields in your invoices are accurately populated and complete; these fields are often different for different countries. It is not good enough to look at mandatory fields only from an indirect tax perspective like VAT, there are often requirements for fields from other tax areas like income tax in India or corporate tax in Germany and France." Tungsten, for example, generates legally compliant e-invoices on behalf of suppliers across 54 countries. "Ideally, you also need someone that works with suppliers to generate invoices on their behalf, taking that workload and responsibility upon themselves to ensure compliance. This is more than just creating the data for a file."

Tungsten Network operates under a 'delegation of authority' which states they are empowered by the supplier to create their invoices for its customers. "Your partner should definitely be able to validate the invoice data sent by a supplier. It should make sure all components are accurate and compliant, from the invoice number to the validation of the sender; check whether it is an invoice or a credit note; make sure the invoice matches the requirements of the buyer and map prices to thresholds and appropriate approvals."

Where any check falls short, Tungsten will attempt to make an invoice compliant. Where it can't do this, it will reject the invoice back to the supplier, but within seconds rather than weeks. This means a supplier can resubmit quickly, eliminating the need for a credit note and having less impact on cashflow. "What we do," says van Hilten, "is create extra value for the customer, not just by validating the compliance of an invoice for the supplier, but by driving digitization for the buyer while giving the government what it requires. It's a much more efficient process."

How Tungsten Creates Extra Value

In such a vast and complex world of multi-government compliance requirements, firms offering e-invoicing services must stay ahead. "At Tungsten Network we stay on top of compliance through our team of tax experts. Unlike many other providers, we also collaborate closely with the specialist teams of one of the best consultancies in the world, PwC, to understand compliance demands, foresee changes and define best practices for every country in the world."

"As well as fulfilling legislative requirements, validating and archiving these legal documents, we provide full visibility of where an invoice is at any given time. All in all we drive a lot more value to both parties. Because of that, customers find that the benefits associated with outsourcing to a partner far outweigh the cost of non-compliance. The fact that Tungsten is networked creates advantages that others cannot. A supplier signing into the network can submit an invoice to any one of the buyers, and only needs to connect once. Any buyer connected to the network can receive invoices from its thousands of suppliers. So it's a 'connect-once, send-and-receive-many' platform, and that creates huge efficiencies."

"When you consider the ongoing cost of constant change, what governments come up with and what buyers require you to do, Tungsten estimates that it can be 70% cheaper to outsource than to do it in-house."

"As your business grows," van Hilten concludes, "compliance obligations grow too. It's more and more important to have a reliable and scalable means of managing your responsibilities. Luckily, responsibility can be outsourced alongside your legal obligations."

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Tungsten Network provides e-invoicing services to suppliers and buyers in every country in the world, unless government embargoes or other legal or local restrictions apply. Where electronic invoicing is mandated by the government, Tungsten Network (for the Tungsten Network e-Invoice-compliant countries) helps facilitate this obligation for the suppliers and buyers connected to its network.

Tungsten Network enables electronic invoicing from any supplier system to any buyer system in the business-to-business trading environment. It is independent of accounting and e-commerce systems, data standards, currency, geographical location and means of payment.

The primary objectives of the Tungsten Network service are to:

- **Eliminate the need for suppliers to send paper invoices**
- **Improve buyer invoice processing efficiency**
- **Reduce data entry errors in buyers' accounting systems**
- **Provide suppliers with surety of invoice delivery**
- **Provide an audit trail for buyers, suppliers, and tax authorities**
- **Enable quick and efficient invoice audit capabilities**
- **Facilitate mandatory electronic invoicing, in the jurisdictions where such an obligation has been imposed**

In supporting these objectives, the system has been constructed using robust processing and security components. Click below to find out more.

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This article was written in conjunction with Spendmatters.com