



Federation of Small Businesses
The UK's Leading Business Organisation



Small businesses and online trading

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Introduction

In less than two decades a large proportion of commercial activities have moved online, and the UK is now the largest global per capita e-commerce market.¹ Online trading has definitely empowered those small businesses that are able to find new markets, sell new products, try new business models and compete on an equal footing with larger businesses. But to what extent does our membership benefit from these new opportunities? This report sets out how our members are trading online, how they are using the internet economy, and what obstacles they are encountering.

The details given in this report are based on an online survey carried out in June 2011 by 1,633 members of the FSB 'Voice of Small Business' Panel. The members of this panel are broadly representative of the wider FSB membership. The study was undertaken by Research by Design on behalf of the Federation of Small Businesses.

We believe that there is a lot of potential for small businesses to increase their sales and develop

their business through e-commerce. In order to promote the active use of online trading by small businesses and let them share in the benefits of the Digital Single Market and beyond, the FSB makes the following recommendations:

- **Broadband** infrastructure will be the key to the further development of e-commerce. Therefore, we ask the Government to keep the National Broadband Strategy under review and to make a clear commitment to deploying universal superfast broadband across the UK.
- Small businesses frequently rely on the Post Office for the **delivery** of their products. We are concerned that the Post Office's planned restructuring will change the services currently being provided. Any post-office strategy needs to take into account not just financial sustainability but the need to safeguard a valued public service.
- Small businesses trading online are often the victim of 'card-not-

present' fraud. The banks should work with businesses on **security** issues and on reducing the risks of this type of fraud. Action Fraud should become a hub for internet security information and e-crime prevention for small businesses.

- There are still barriers of a legal and fiscal nature when conducting business within the EU. To make sure small businesses can benefit from the **Single Market**, we urge the Government to stick to the pledges made in their 'Let's Choose Growth' policy and to be constructive in negotiations on the removal of barriers in the Single Market.

1. *The Connected Kingdom*, Boston Consulting Group 2010.

Selling goods and services online

Almost all small firms now use the internet for their business.² However, half (50 per cent) of FSB members are either interested in selling goods and/or services online or are already doing so; half do not sell online, mainly because it is not appropriate for their particular business.

Given that we are living in a mature e-commerce market, this picture of half the members being interested in selling online and half not selling online may not change dramatically. But with better access to broadband this figure could improve, although some business activities, such as building, will never be suitable for online selling. However, there will be a lot of scope for growth in small businesses trading online, with regard to both turnover and finding new markets.

In 2010 business-to-consumer e-commerce contributed £60 billion to the UK economy.³ Our own survey suggested that those firms whose profitability had increased in 2009 were more likely to have used the internet for business purposes.⁴ Internet businesses seem to

weather the economic storm better than offline traders.

Currently, of those members trading online, a quarter claim that this generates at least half of their business turnover. It is expected that the internet economy will grow by 10 per cent per year, reaching 10 per cent of GDP by 2015.⁵ This is good news for small businesses that use online trading; there will be scope for increasing their profitability.

2. *The ICM-FSB 'Voice of Small Business' Annual Survey 2009.*

3. Interactive Media in Retail Group.

4. *The ICM-FSB 'Voice of Small Business' Annual Survey 2009.*

5. *The Connected Kingdom*, Boston Consulting Group 2010.

Websites as shop floors

The vast majority (91 per cent) of FSB members who trade online do this through their own company website. However, more than a quarter (28 per cent) sell their goods or services via third-party websites. A number of members who are using their own websites complement this with the use of a third-party website. Some members host third-party websites themselves or have personalised order journeys for customers on their website.

Members use mainstream third-party websites such as Gumtree, Amazon and e-Bay. Some providers offer a 'shop' rather than an account, which illustrates the trend of the internet becoming a second shop floor.

"We also have an e-Bay shop."

Members use many different specialised third-party websites, such as websites for flower delivery services, camping bookings, property, wholesale and online booking agencies.

"We are a hotel, so we use specialist third-party websites, e.g. AVIVO, Red Funnel, Expedia, Island Breaks, lastminute.com."

The internet is often used as an advertising tool. Members advertise on online web directories or via YouTube, or they have links on free listing websites and take part in online forums. They use social media such as LinkedIn, Facebook and Twitter to promote a product or a service. It is an inexpensive way of meeting customers. Social media are also a tool for online networking between businesses.

"We don't sell online at all as we are service-based, but we do promote online and this is important as we can be found."

"We are a pub with accommodation, so selling services is more about using the net to get people to phone and book."

"We are an architectural practice, and whilst we have a web presence and social media – we only advertise online and do not sell our services online."

Most online traders can be found in the retailing and wholesale sectors, and in the hospitality sector (hotels, restaurants, bars and catering). The construction sector hardly uses the internet at all to sell its products or services. In some sectors, online presence attracts customers but the actual business transaction is concluded offline, for example in the property sector.

Markets

The internet shrinks borders and is a major tool for finding new clients. Most of those who trade online do so within the UK (97 per cent), but around four in 10 trade in other EEA (European Economic Area) countries and in the Republic of Ireland. Nearly a third trade online with North America and Canada and a quarter with Australasia. A tenth trade online with the Middle East and with South/Central America.

Online trade could be the vehicle and trigger for cross-border trade. Although the focus of many policies is intra-EEA trade, selling online is not confined to Europe and is global by definition. Firms clearly export more to the EEA, but there exists the potential to target markets in the Far East as well. Currently, only 15 per cent of those trading online are selling to Asia.

FSB members have more online customers in the EEA, but they are clearly open to customers in the whole world.

“Our B&B is located here in the UK – but guests come from all over the world to stay here!”

“We have online customers in every country in the world!”

At the opposite end of the scale, members say their online presence increased sales in their specific postcode area. So the picture of where online clients are is mixed, but the internet clearly makes it possible to find new customers and increase sales.

Trading online and overseas

Whereas some businesses merely stumble upon orders in their inbox that happen to come from abroad, others actively seek to attract customers from other countries. For example, they ‘localise’ their website. Among those trading online outside the UK, a third have undertaken specific measures to increase online sales to this market.

For example, they have changed the settings of their account with a third-party platform to accommodate foreign customers, or they have created an account with a third-party platform in another country. Some also adapt their own website to suit the customer’s country of residence. Language problems are sometimes countered by means of translated websites and terms and conditions, and some businesses use multilingual staff to handle customer care in another language.

Barriers to trading online

Among those trading online (or operating a business with online potential), four in 10 identify problems that can hamper online trading within the UK.

The most serious barriers are the cost of **developing and maintaining a website** and **lack of IT skills**.

“I am short-staffed due to the recession and already overstretched; therefore I have insufficient time to get online trading up and running.”

Some members are not sure how to start selling online, and said that the following would be helpful:

“A course on how to go about selling by this method.”

“A decent but simple web-building tool.”

Another important barrier to online trading is **broadband speed**. This

is less of a problem in London, the South-East and the East Midlands. However, members in the South-West scored highest on broadband speed being a barrier to selling online. This is a problem for the tourist trade in particular, which is an important sector in this region.

Our latest report on broadband⁶ shows that small businesses believe they would be able to make better use of services such as online trading should they have access to superfast broadband. For 9 per cent of small businesses, current generation broadband is not available across any of their sites, for 22 per cent it is not available at at least one of their sites, and for those that do have current generation broadband, 26 per cent have speeds up to 2Mbps, acting as a significant barrier to things such as e-commerce

Not only broadband speed but also **guaranteed postal delivery services** are vital to the development of e-commerce. Sixteen per cent of members say that poor delivery services have prevented them from

trading online. In some areas of the UK the Post Office is the lifeline of small internet businesses. However, as Post Office Ltd moves towards a new model, 2,000 local post offices will offer a reduced service, with fewer products and services (including some parcel services) than sub-post offices currently provide. This will hold back small businesses that use the internet as a (second) shop floor. These are highly dependent on the Post Office because most courier companies are not yet geared up to serving small companies. Small online traders cannot guarantee regular parcels being sent out, which prevents them from getting better deals with couriers, and the costs of couriers become too high.

“We are unable to get reliable and cost-effective courier services. They have been terrible and have caused us to stop our online trading.”

6. *Small Businesses and Infrastructure: Broadband* FSB 2011.

Security is a significant barrier to the development of online commercial activities. Businesses cite security issues as one of the top five most significant barriers to the development of their online commercial activities. Around one tenth (11 per cent) of members say that the 'risk of card fraud or security failure' prevents them from trading more online.

Some current concerns expressed by members in the survey were:

"Our e-bay shop was hacked into and the product references were altered."

"Our site is hacked continuously."

Fraud that occurs when either the card or the cardholder are not physically present (known as CNP, 'card-not-present', fraud) continues to be a big problem for small retailers. They are often a victim several times over and can lose thousands of pounds in the process.⁷ The FSB would like to see the banks engaging in more direct communication with small businesses on this type of fraud, and explaining that online authorisation does not guarantee payment.

There is no shortage of accessible guidance for small businesses on internet security, and we urge businesses to seek advice to ensure that they're protected. It is a positive move that the Action Fraud Reporting Centre will be taking reports of fraud and online crime. The intelligence that emerges from this can be used to combat fraud. Small businesses will need to be made aware of Action Fraud as an advice centre on e-crime issues.

The FSB has worked with a number of organisations including the Fraud Advisory Panel and the National Fraud Authority on advice and guidance for businesses on internet security, including protecting IT systems, security of mobile devices, e-crime and managing the risks involved in cloud computing. Our recent report on cloud computing highlights security as an important barrier to the use of online services. With more firms moving parts of their business online and using 'the Cloud', it is important that advice and guidance on security should be well targeted. The FSB will continue to play its part in raising awareness of the risks.

There are **other reasons** why businesses don't trade online. These might include: lack of storage space; preferring a personal approach to clients; having problems with insurance or payment collection; or the prohibitive cost of external assistance.

7. *Inhibiting Enterprise: Fraud and Online Crime Against Small Businesses* FSB (2009).

Barriers in the Single Market

For businesses, the online EU market is complex, costly and unpredictable, and the European online market is fragmented along national lines. We asked what would make it easier for small businesses to sell online to other countries. Two-thirds identified measures that would make trading within the EEA easier.

VAT is the biggest problem in cross-border transactions, and three in 10 claim that harmonised VAT rules throughout the EEA would help. They experience difficulty with reporting obligations and VAT rates. Online traders must register for VAT in every country in which their sales exceed a certain threshold. In addition, VAT rates vary from country to country.

“In addition to shipping, tax and legal issues are also a source of anxiety.”

A quarter state that **specialised advice services** for small businesses would be helpful. A number of

small businesses don't know how to go about selling online to other countries. Our report on exporting⁸ suggested that better promotion of available support and tailor-made information for small firms are considered the best measures for encouraging exporting by small businesses. This is thus also necessary for cross-border business that is conducted online.

A fifth of members say that recognition by all countries of **e-signatures, harmonised consumer rights** and an optional **Common European Sales Law** would make it easier to sell online within the EEA. These issues stem from the protection of national provisions in these areas. But if we want to ease cross-border online trade, there will have to be more harmonisation in those areas. For example, e-signatures are not always recognised in every EU country,⁹ and online businesses are confronted with different bodies of legislation. In 2007, the FSB calculated that it would cost a business £13,000 in legal and implementation fees to comply with a country's regulations.¹⁰

“The biggest barrier, in my view, are the varying levels of sales laws and regulations between EEA states. It's impossible for a small UK business to comply with every bit of selling legislation where jurisdiction may preside (such as France).”

The proposed Common European Sales Law is a positive step towards harmonisation. Combined with adequate online dispute resolution and alternative dispute resolution mechanisms, and with the review of the e-signatures directive, it may go some way towards easing legal barriers to online cross-border trade.

When trading online across borders, being able to trust a delivery service is even more important. For some, delivery costs are prohibitively high for trading within the EEA. This means that problems with **delivery**

8. *Made in the UK. Small businesses and an export-led recovery*, FSB 2010.

9. *Survey of e-commerce barriers within the EU*, Kommerkollegium 2011.

10. FSB Position Paper on Rome I.

need to be tackled to facilitate online cross-border trade. After all, infrastructure is the backbone of the internet economy. Our members indicated that the following would help:

“Lower shipping costs and guaranteed delivery services to the continent and the rest of the world.”

“Help with distribution channels.”

In addition to fears about delivery, **cross-border payments** are a major challenge for small firms. They indicated that the following would make their lives easier:

“Honest punctual payment practices in all EU countries.”

“Make it easier to collect late payments.”

“Make it easier to make and receive payments between British and other European banks.”

“Banks should offer speedy (i.e. under one month) settlement for ‘foreign’ cheque transfers.”

“The bank credit card payment fee should reflect the small margin on small-value products – at present the bank would take the entire margin for small-volume sales so there is no point in experimenting.”

“With a small gross margin, the fluctuations in the value of the pound to the Euro make trade very risky.”

“We need safer card sales. I avoid selling abroad due to the amount of fraud on cards.”

It is clear from the above that payment problems abound. Late payment and concerns about cost and security of payment are the most important issues.

Further barriers to cross-border online trade are linked to **intellectual property rights**. The two most pertinent problems are copyright levies in several countries and internet theft of intellectual property. Our recent survey on these matters¹¹ shows that copyright and design rights are the most commonly experienced areas of intellectual property theft. Almost a third were unable to solve their problem, claiming that the process was too complicated or expensive. For around a quarter of those experiencing intellectual property theft, the matter remains unresolved.

11. FSB ‘Voice of Small Business’ Survey Panel (October 2011).

Conclusion

The picture that emerges of online trading among FSB members is as follows:

Roughly half of FSB members are involved in selling online. They mostly do this through their company website, and the internet is often used as an advertising tool. Most of them trade within the UK, but around four in 10 trade in other EEA countries. However, selling online is not confined to Europe and members target other parts of the world as well. A third have undertaken specific measures to attract customers from other countries.

Whereas online trading is easy for some, others have indicated significant barriers to developing their business online. Having to design and maintain a website and a lack of IT skills are major barriers, as are slow broadband speed and the lack of guaranteed postal delivery services. Security issues are also a major obstacle.

The Digital Single Market is not barrier free either. VAT, lack of

specialised advice services, payment problems and concerns with intellectual property all impede online selling to customers abroad. Barriers of a legal nature were also mentioned, such as EU-wide recognition of e-signatures, and different consumer rights and contracts laws. Last but not least, the inability to ensure guaranteed delivery throughout the EU is of huge concern to small businesses exporting via the web.

So has the development of online trade empowered small businesses? It is clear that online trading has enabled small businesses to find new markets, sell new products and try new business models. However, the barriers mentioned above prevent small businesses from benefiting fully from the huge potential of national and international online trade. As long as these barriers exist, small businesses will be only partly able to compete on an equal footing with larger businesses.

Recommendations

In order to increase the active use of online trading by small businesses and to let them share in the benefits of the Digital Single Market and beyond, the FSB makes the following recommendations:

- **Broadband** infrastructure will be the key to the further development of e-commerce. Broadband access and speed and reliability of service are vital for small businesses that engage in selling online. For this reason we ask the Government to keep the National Broadband Strategy and related targets under review, to ensure that UK ambitions are kept in line with EC targets, so that UK enterprises are not at a competitive disadvantage compared to European counterparts, and to give a clear commitment to deploying universal superfast broadband across the UK. Recent announcements regarding funding commitments for broadband infrastructure are welcome, but the Government must ensure that these funds are allocated quickly and targeted at those areas to which the market will not extend.
- Small businesses form a loyal customer base and frequently rely on the local post office for the **delivery** of their products. We are concerned that Post Office Ltd's planned restructuring will change the services currently being provided. There is little public awareness or scrutiny of these plans, and customers have so far been given little opportunity to engage with Post Office Ltd on its strategy. Any post-office strategy needs to take into account not just financial sustainability but the need to safeguard a valued public service.
- Small businesses trading online are often the victim of 'card-not-present' fraud. The banks should work with businesses on **security** issues and on reducing the risks of this type of fraud. Businesses are paying for a service and the message that authorisation does not guarantee payment is hidden in the small print. Action Fraud should become a hub for internet security information and e-crime prevention for small businesses.
- There are still barriers of a legal and fiscal nature when conducting business within the EU. The Government has taken the lead in unleashing the Single Market with its 'Let's Choose Growth' policy. However, we have yet to see what they have done to reduce the cost of doing business in Europe. To make sure that small businesses can benefit from the **Single Market**, we urge the Government to stick to their pledges and be constructive in negotiations on the removal of barriers in the Single Market, such as VAT rules and the fragmented sales and consumer rules within the EU.



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