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5 Ways to Increase the Business Value of Trade Compliance

New research confirms that most companies dramatically undervalue the role of trade compliance in driving business benefits. Here are 5 ways for companies to leverage trade compliance for financial improvement.

Trade Compliance: Severely Undervalued

The value and importance of effective trade compliance is severely underestimated at most companies. Trade compliance initiatives have traditionally been positioned as risk reduction or staff productivity projects. Based on our conversations with companies over the past 3 years, we find that few companies have examined and quantified the financial benefits that their trade compliance group brings to their company or assessed fully where the greatest opportunities are for driving further improvement.

This is a huge opportunity waiting to be tapped, as many companies are sitting on millions of dollars of potential financial improvement opportunities. These are the findings of benchmark research by Aberdeen across hundreds of corporations, along with Aberdeen's in-depth analysis of five companies' real trade data in conjunction with Global Data Mining, LLC, a trade data analysis specialist.

Vendor Checklist

Features to consider when evaluating trade compliance solutions:

√ Data mining and executive reporting capabilities

√ Enterprise-wide database support for trade compliance

√ Preferential trade agreement support

The 3 Barriers to Strategic Trade Compliance

The increase in global sourcing and selling activity has put relentless pressure on trade compliance professionals to keep pace with increased international transactions. Consumed with daily fire-fighting and administrative duties, most staffs have not had the time to examine their corporate-wide trade data in a strategic fashion.

Moreover, the trade compliance department is one of the least automated parts of most enterprises. Working off mountains of spreadsheets or aging databases and systems that vary across regions and business units, trade compliance professionals simply have not been properly armed with the tools to analyze their trade data and prioritize improvements. Other companies abdicate most of the trade compliance responsibility to their brokers and freight forwarders, further diluting their ability to use trade compliance data strategically.

A third barrier is the lack of effective cross-functional global trade organizations. Aberdeen's May 2007 research across 214 companies finds that **69% plan to put in place or enhance a cross-functional**

global trade team to improve performance. Without cross-functional oversight and implementation capabilities, it is nearly impossible for trade compliance professionals to induce their operations counterparts to take action on trade compliance savings opportunities. Alignment among product design, manufacturing, sourcing, logistics, and finance is required. In fact, past **Aberdeen research has shown that companies with cross-functional alignment and automation are 2X more likely to have reduced total landed cost than their peers.** Leading companies are setting up Global Trade Centers of Excellence to drive these cross-functional actions.

"It's been a struggle to get this kind of information to our executives."

~ Trade data analysis participant

Quantifying the Savings Opportunities

To quantify trade compliance's trapped business value, Aberdeen and Global Data Mining analyzed the actual trade data from 5 enterprises for their U.S. imports. As Table 1 shows, **these 5 organizations collectively had $261.2 million in direct compliance-related savings opportunities.**

Table 1: Potential Savings for 5 Companies Studied

Company	Revenue	Savings Opportunity	Top Compliance-Related Potential Savings Areas
Aerospace & Defense Company	$31 billion	**$1.67 million**	1. Potential duty savings from new sourcing opportunities 2. Self-filing savings 3. Potential duty savings from existing supply base
Apparel & Accessories Company	$3 billion	**$161.5 million**	1. Potential duty savings from existing supply base 2. Potential duty savings from new sourcing opportunities 3. Free trade zone savings
Electronic Components Company	$12 billion	**$90.5 million**	1. Potential duty savings from existing supply base 2. Inconsistent application of trade agreements 3. Self-filing savings
Transformers & Power Conversion Company	$5 billion	**$3.1 million**	1. Potential duty savings from existing supply base 2. Self-filing savings 3. Potential duty savings from new sourcing opportunities
Semiconductor Company	$13 billion	**$4.6 million**	1. Free trade zone savings 2. Self-filing savings 3. Potential duty savings from new sourcing opportunities

Source: Aberdeen Group and Global Data Mining, June 2007

By analyzing the trade data, we also found that these companies' trade compliance departments had **already collectively saved their companies over $100 million** since 2001 through trade agreements and other special programs over what straight duties would have been.

The study participants found the ability to step back and take a strategic look at savings opportunities using their actual trade data to be useful both in identifying areas to investigate further as well as to educate their executives on the business value of trade compliance expertise.

- Said one participant, ***"This is going to get a lot of people's attention ... from the CFO on down."***
- Another participant responded, ***"This is staggering information."***

In the study, the potential savings opportunities were identified at a transaction, commodity code, and factory location level; the data then could be sorted to stack rank the opportunities by business value. In many cases, most of the savings could be gained by focusing just on the top 10-20% of identified opportunities.

The potential savings opportunities are just that – potential. There may be sound business reasons for not pursuing all the opportunities, including specialized capabilities by certain suppliers or country risk concerns that prevent maximum duty savings. But by analyzing data in this way, companies can quickly understand decision tradeoffs and zero in on strategies to lower compliance-related costs by millions of dollars.

Top Savings Opportunities

Five compliance-related savings categories were identified in the study:

- **Inconsistent application of trade agreeements:** These are opportunities related to a company's import entries that could have been eligible for trade agreements and other special programs but were not taken. Other import entries with the same manufacturing location (MID) and 10-digit HTS (Harmonized Tariff Schedule) code had the agreements applied to them. To recover these savings, companies can apply to U.S. Customs and Border Protection for a readjustment of their duties. In total, more than $17 million in potential missed classifications were identified across the 5 participants.

  This analysis also identified shipments where trade agreements probably should not have been taken. For instance, should an organization really bear the additional risk burden of using a trade agreement for a $33 shipment?

- **Potential duty savings from existing supply base:** This is the savings that would be accrued if sourcing were shifted to maximize trade

Shifting the sourcing mix across existing suppliers to maximize trade agreement use could save more than **$150 million** for the 5 companies studied.

agreements and other special programs from a company's *existing* suppliers (e.g., suppliers from which a company already currently sourced some product with the same 10-digit HTS code). For the study participants, changing the sourcing mix across their existing suppliers could collectively drive more than $150 million in potential savings.

Maximizing the use of preferential trade agreements is becoming an increasingly important strategy to remain price competitive. In fact, Aberdeen's May benchmark research finds that 48% of respondents have initiatives to improve their use of preferential trade agreements in 2007.

- **Potential duty savings from new sourcing opportunities:** This is the savings that would be accrued if sourcing were shifted to new suppliers in *new* countries to maximize trade agreements and other special programs. These proposed new countries are already shipping product with the same 10-digit HTS code into the U.S. Our study identified more than $62 million in potential savings for the 5 participants. [Note that some of this savings may overlap with the savings opportunities identified from changing the import mix from the existing supplier base.]

  In a number of instances, the study found that China had duty rates on participants' imports but that other low-cost countries had regional trade agreements that dropped enforced duty amounts to $0. This is one reason a growing number of companies are expanding their low-cost country sourcing strategies beyond China. Aberdeen benchmark research finds that India and Vietnam are the top 2 new sourcing locations companies are considering.

For 3 of the companies studied, using U.S. foreign trade zones could result in a collective net savings of **$17 million**.

- **Potential foreign trade zone (FTZ) operating savings:** This is the potential return on investment from operating a warehouse or distribution center in a U.S. foreign trade zone. FTZs allow companies to effectively reduce duties, merchandise processing fees, and broker fees. When properly executed, they also increase the velocity of the supply chain. After deducting for the administrative, consulting, and software costs involved in setting up and running an FTZ, the net savings identified was $17 million across 3 of the participants. (Two of the study participants had $0 of FTZ potential.)

  Aberdeen benchmark research finds that 36% of respondents say they are investigating in 2007 how to use more global duty deferral programs like U.S. foreign trade zones, Mexican Maquiladoras, European processing under customs control, bonded warehousing, or other free trade zones.

- **Potential self-filing savings:** More companies are moving to self-filing trade documentation using web-enabled software. For the 5 study participants, more than $13 million of potential self-filing savings was identified. The savings calculation was based on an average broker fee of $75 an entry that could be reduced to a cost of $20-$35 per entry under a third-party web-based self-filing service. Companies can set up their own software and internal filing process to lower costs even more.

Savings Opportunities beyond the Compliance Department

Trade data analytics can also be used to pinpoint savings opportunities far beyond direct duty and compliance-related administrative cost reductions. To demonstrate this, Global Data Mining and Aberdeen also analyzed the participants' trade data to determine savings potential from early payment invoice discounts and from international parcel shipping freight audit.

Trade compliance professionals can use their trade data to help their finance and procurement counterparts identify which suppliers to approach for early payment discounts and the magnitude of the savings. In the study, trade data was sorted by dollar value imported per supplier and a 2% cash discount was applied for early payment. (Aberdeen's supply chain finance research has found that many companies have been able to negotiate 2-3% cash discounts with international suppliers in return for faster payment.) In the case of one participant, $2.9 million in savings could be achieved by negotiating a 2% cash discount with just the company's top 7 international suppliers. In total, if the 5 study participants moved all their international suppliers to 2% cash discounts, a whopping $224 million of savings would be achieved.

Trade data analysis revealed that study participants could achieve an additional **$224 million** of savings with cash discount programs.

We also ran an analysis for a participant on small parcel shipping savings. According to this company's trade data, it could save $461,469 on its international parcel shipments if it used a contingency-based firm for third-party freight audit, assuming a reasonable recovery rate of 3%.

Another savings area can be found in improving inventory velocity by creating a more automated and visible trade compliance process. Companies that currently have import or export compliance automation are 40% more likely to have increased customs clearance speed over the past 2 years than their peers, according to Aberdeen benchmark research. C-TPAT compliance and the use of foreign trade zones can also improve supply chain velocity. It is common for companies to calculate that each day of lead time reduction equates to a million dollars or more in inventory savings.

Recommendations for Action

Companies need to treat trade compliance data as a strategic asset. Analysis of existing trade data can drive more informed decisions and targeted improvement strategies. Below are some recommendations based on our research findings:

- Create an annual summary detailing how the trade compliance department is *already* saving the company money through trade agreements and other special programs over what straight duties would have been.

- Analyze trade data to determine how sourcing strategies or product design plans can be improved to minimize duties, such as by applying preferential trade agreements or by engineering subcomponents that will have lower importation rates.
- Consider increasing the use of global duty deferral programs like U.S. foreign trade zones.
- Assess the feasibility of using a self-filing service or managing a self-filing process internally.
- Increase trade compliance automation to reduce misclassified entries, achieve staff productivity improvements that can lead to headcount stabilization, enable execution of preferential trade agreement and other duty reduction programs, and improve supply chain velocity.

For more information on this or other research topics, please visit www.aberdeen.com

Related Research	
Global Trade Management Strategies: Surviving Growing Complexities in 2007, May 2007 *New Strategies for Financial Supply Chain Optimization*, November 2006	*Global Supply Chain Benchmark Report*, June 2006 *The CFO's Agenda for Global Trade Benchmark Report*, September 2005

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