The Impact of the Political Landscape on International Trade

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Does your supply chain team feel like the front-line soldiers in the trade wars?

The good news is: you're not alone.

The bad news is: you're not alone.

Trade compliance and logistics have always been tightly interwoven, and the most successful companies understand how to manage both disciplines to avoid risk and take advantage of opportunities. But this fact has never been truer than it is right now, due to the extraordinarily volatile environment organizations find themselves in, especially in the United States when dealing with the fallout of President Trump's approach to trade policy. To understand the extent of the impact, here's a quick look at most (but not even all) of the changes that the new policies have brought:

- US pulled out of TPP (Trans-Pacific Partnership) negotiations in January 2017.
- US entered NAFTA re-negotiations with Canada and Mexico. Resulted in negotiation of the USMCA (United States-Mexico-Canada Agreement), which has been signed, but not ratified in any of the three countries.
- Section 232 Steel/Aluminum Case
  - 25% on Steel/10% on Aluminum on nearly every country
  - Retaliatory duties from all countries (5%-140%)
- Section 301
  - 25% on Chinese Goods, with multiple "Lists" and exclusions to manage
  - Retaliatory duties from China
- Section 232 Automotive Case
  - Published in Federal Register 5/30/18
  - Private report submitted by Commerce to President with Secretary's recommendation on 2/17/19
  - President Trump announced on 5/18/19 that he would "negotiate" with countries harming US security interests to reduce trade imbalance
- Removal of India and Turkey from GSP (Generalized System of Preferences) program
  - Announced 3/4/19
  - Turkey removed 5/17/19; India removal effective 6/5/19
- Section 301 Action on EU: helicopters and other items per WTO ruling
  - 300 items
  - Proposed duty rate not known until after WTO hearing held later this summer

As can be seen just from the number of bullets in the preceding list, there's a lot for trade compliance teams to stay on top of these days. First and foremost, they are the people within a company responsible for knowing what's happening or about to happen. That may sound easy, but it isn't always, because sometimes announcements about new duties or how a new regulation will be handled operationally by Customs is announced at the very last minute.

Secondly, the trade compliance department is most often the one with the data that can help to quantify the impact to the organization of any given change, such as a new duty. With so many HS numbers subject to so many increased duties, possible exclusions, and changes in preferential treatment happening all at the same time, it takes careful analysis of historical reporting to report accurately on the total cost of these changes and when they will be felt.

Finally, trade compliance teams are finding themselves under additional pressures to manage these changes and still remain compliant. Products have to be re-classified with new (or secondary) HS numbers, past declarations have to be re-filed with Customs to pay additional duties or get a refund back, and in some cases, the very act of filing a declaration has become more time-consuming. In the US, for example, when goods are subject to a Section 301 or 232 duty, a secondary HS number in chapter 99 must be reported on the entry line along with the regular tariff number. And if a product has both a Section 301 and a 232 duty, the importer has to know the correct order to report those HS numbers in. Each country has its own regulations, all of which trade compliance teams are spending time learning quickly and trying to ensure are being followed.

On top of this new more-demanding "day job," compliance professionals are helping their companies with the task of constantly re-evaluating their supply chains. The possible changes they may need to make are either "micro" in nature or "macro."

An example of when many US importers made micro changes was at the end of 2018. President Trump had been threatening for some time that the 10% duty rate on "List 3" of the Section 301 goods would move to 25% effective 1/1/19. In order to avoid such significant increased duty payments on orders planned to land early in 2019, many companies moved up their planned ship dates. By the time it was officially published on December 16 that the rate would not move to 25% on January 1 after all, most of those goods were either en route or too late to change the ship date again.

Making changes of this sort is not something that a company's trade compliance team handles alone, even if they are the department with the original knowledge to say "Houston, we have a problem!" Multiple departments need to get involved to assess if moving up orders is both desirable and even possible. The company needs to include sourcing/purchasing teams, logistics, financial, and distribution at a minimum to weigh in. The additional costs that can be incurred to bring in freight earlier than desired, such as off-loading/on-loading, cost-of-capital for paying invoices earlier than planned, possibly warehouse rental/temporary labor costs may not make the duty savings worth it. And it's also possible that the supplier may not be able to ship early.

Macro changes, when a company looks to change an entire supply lane or vendor/manufacturer, are even more complex. In addition to involving all these same parties, the organization and many of those same other internal teams will need to work with their third-party providers to manage the changes. For example, before moving sourcing from China to Indonesia just because the duty is lower, the logistics team needs to assess their carrier contracts for comparative rates, transit times, and even if the shipping lanes are supported in the first place.

Sourcing teams may need to work with other third-party providers such as a testing lab to ensure that a new supplier can have their goods tested to meet the regulatory requirements of the various agencies in the import country. Sometimes that may require months to find a new provider to work with in a new country — months of close inter-departmental collaboration to ensure successful outcomes.

With these significant changes, importers are looking at other ways to avoid or mitigate these costs. The starting point must be visibility. Times like these require significantly more robust reporting tools to look at the "Then," the "Now," and the "Next."

The "Then"

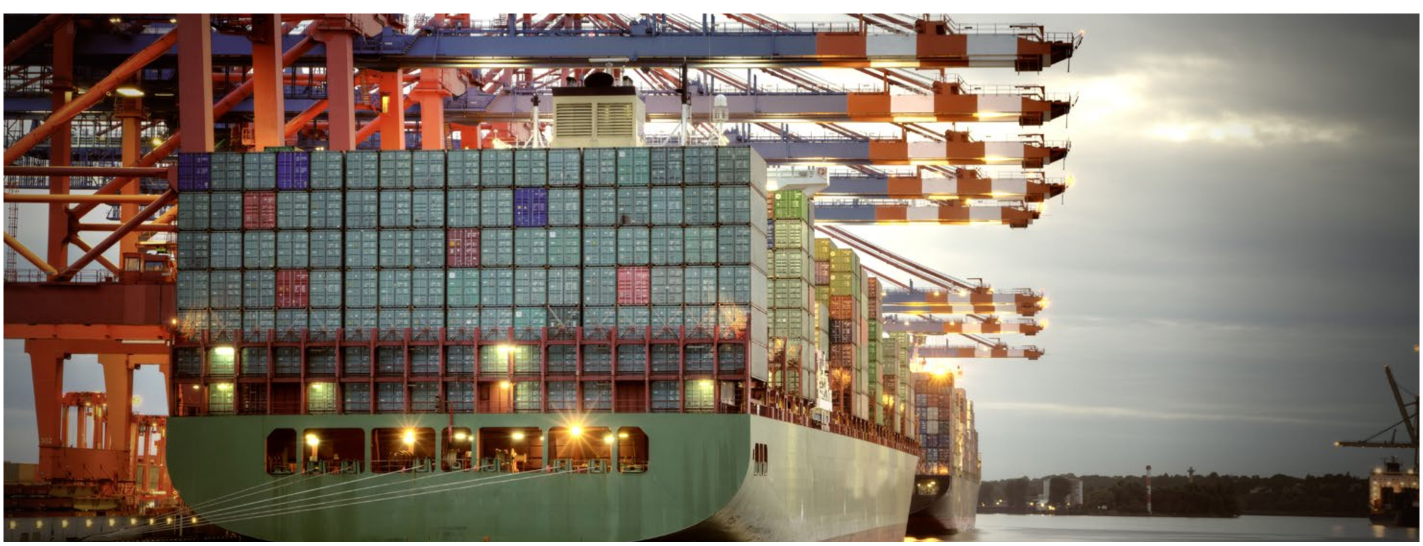
- Baseline import reporting to understand what your company's normal volumes have been — duties, values, countries, HS numbers
- Need to know export volumes too in order to understand opportunities for programs like Drawback and Foreign-Trade Zones
- Should have ability to see data normalized across all countries your company is doing business in, to be able to compare apples to apples

The "Now"

- Ability to drill down to specific changes based on new duties incurred recently, for example to specific HS numbers
- Trend reports to identify recent impact of increased duty spend
- Need to be able to see what impact would be to all goods from a given country losing preferential duty status
- Need to be able to quantify financial cost of proposed new duty to given group of HS numbers, etc.

The "Next"

- Tools to hypothesize changes to supply chain and measure impact to duty spend
- "What If" scenario creation utilizing actual historical import data as baseline data to consider different options
- Ability to see duty impact with current, updated tariff content to allow users to refresh scenarios on an on-going basis



Once a company has used a tool like this, the trade compliance and supply chain teams are in a good position to work together to decide on next best steps. As suggested, sometimes, companies will make major changes in supply chain sourcing approaches, but these can be very time-consuming and not always viable options. Some other key opportunities for mitigating the cost impacts that importers are using more and more are:

- **Duty deferral programs, such as the Foreign-Trade Zone program in the US**
  - Zones allow importers to hold imported goods without paying duties until they ship into commerce.
  - Zones also allow for export of goods without ever paying for duties, completely avoiding the payment of these elevated duties.
  - The higher one's total duty payments, the better the ROI on participating in the program.
- **Duty Drawback**
  - Drawback is a program under which an importer may receive a refund for the majority of duties paid at import when goods are exported.
  - Not all these new duties are eligible, and the requirements of the program require careful management, but with such high duties being paid, it's a program saving many companies millions of dollars annually.
- **Closer analysis of Entered Value**
  - Since each of these new duties is an ad valorem rate, importers are looking at ways to ensure that the value of the goods is as low as is possible and still compliant.
  - Some things being looked at are use of the First Sale program and identification of deductions, such as freight costs, depending upon what Incoterms were used in the purchase of the goods.

As with the micro and macro changes, though, each of these solutions requires importing companies to understand the full impact of implementing a new program of this sort throughout their organization. Ultimately, there **are** opportunities to avoid some of these impacts, but excellent communication across the entire corporate and wider supply chain structure is critical to achieving success.

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