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TRADE COMPLIANCE

Insurance can save the day

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AN IMPORTER CONTACTS HIS supplier in Spain and asks the company to produce coffee mugs to meet the specifications and samples he has provided.

The supplier agrees to produce the goods, and the importer orders 50,000 white coffee mugs with five red stripes.

When the shipment arrives, the importer is shocked to discover that the coffee mugs are red with five white stripes.

Now what?

As just-in-time deliveries are becoming the trend among most shippers, little or no time can be factored in to correct an order should the delivered goods not comply with the buyer's specifications.

In addition, buyers are making more complex demands, and this is resulting in increasingly stringent purchase orders and terms of sale.

Importers of most retail products have a need for trade compliance insurance to supplement broad-form cargo insurance, according to Richard W. Bridges, account executive, Roanoke Trade Services Inc., Boston.

"As profit margins continue to erode, most of the national chain department and 'membership' stores are deliberately placing more of the risks upon the supplier, so as to minimize any unforeseen expenses," Bridges said.

Trade compliance insurance can turn a contingent transaction into an asset by guaranteeing that the seller of the goods will be paid regardless of whether the buyer accepts them.

Here is how it works.

Trade compliance insurance is a term that includes not only insurance but a series of detailed inspections that the goods must pass before being considered for the coverage.

The importer sends all documents, including the purchase order and the accepted sample or written specifications, to an inspection company agreed upon by underwriters. The purchase order details the color shades and a sample showing the exact colors and quality of the mugs.

The inspection company determines when the goods are to be manufactured and sets up a time to inspect. An in-process, random sampling inspection is performed to determine if the goods are being processed to all the specifications as set forth in the order documents and sample.

Should the goods not pass this inspection, the manufacturer is required to fix the discrepancy or the goods may be accepted by the importer as-is. This acceptance then voids any coverage that may have applied to the shipment.

After the goods are produced, the inspector then performs another random sampling to again determine whether the goods have been produced to specification. Again, the assured is given the option to accept the goods as-is, thus voiding coverage.

After both inspections are completed, a certificate of compliance is released by the inspection company.

The random sampling, which involves checking about one item per 100, has proven to be 85% effective in catching all discrepancies. However, there still exists a 15% chance that all or a portion of the goods may be discrepant when they arrive at the consignee.

If the buyer then discovers that the mugs have been manufactured with the wrong shade of red, the assured can again accept as-is or file a claim for loss incurred as a result of this error.

The shipper is then paid for the cost that would have been realized in the sale of the goods without the aggravation, delay and expense of return shipments and re-orders.

As the transaction matures, underwriters agree to decrease the level of inspections and insurance rates based upon the loss history.

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Currently, Intercargo Insurance Co. offers the most flexible program for large users, Bridges, of Roanoke Trade, said.

Reinsured by the A-plus rated XL Capital subsidiary, Brockbank, Intercargo has aligned itself with global partners. Roanoke has aligned itself with various inspection agencies, which provide the inspection scheduling.

Intercargo rates this coverage in the same manner as marine cargo insurance. Depending on volume and commodity types, rates range from 35 cents per $100 to 60 cents per $100 based upon a valuation of 90% landed cost, or selling price.

Deductibles range from $2,000 to $5,000 to eliminate nuisance claims. All inspection costs are the responsibility of the assured.

Inspectorate Groupe, Intertek Testing and SGS are a few examples of companies that can provide these inspections.

Combined with broad-form cargo insurance, Bridges said the program gives a clear advantage over competitors who are with out trade compliance and provides the lender with an alternative to asset-based lending.

Therefore, as the shipper grows, uninhibited by the low ceiling of an asset-based line of credit, the lender can share in this growth without the risk of default.

Bridges said trade compliance is used to effectively cover the types of goods that may be inspected using a standard sampling plan known as Mil. Std. 105E. Typically, these are manufactured goods shipped in full container load increments, such as textiles and apparel, housewares, furniture, sporting goods, electronic products and office supplies.

The program is not designed for one-of-a-kind goods or foodstuffs. Computer chips, automobiles, bulk fuels and heavy machinery are not eligible.

Unlike most brokers, Roanoke Trade Services designs the cargo policies it issues.

"Off-the-shelf policies are typically not used, as no two shippers are alike," Bridges said.

Direct shippers like John Deere and Victoria's Secret rely on its customized coverages to protect all of their cargo exposures as well.

Broad form or broker forms are those that are customized by the broker to cover the exact exposures of the assured, as opposed to a policy created by an insurance company to cover the average shipper.

Given that cargo insurance is truly a specialized coverage, Bridge said,

Roanoke has developed The Learning Center, a series of internet-based training programs designed to educate the shipper and forwarder about the unique risks associated with transporting goods and Customs clearance.

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