

# **Retailers Break New Ground With Open Account Trade Programs**





*Not only will retailers benefit by successfully reducing costs on each link of the payment chain, but their customers will as well.*

**D**esperately seeking alternatives to letters of credit with flexible payment processing.” It’s not your usual personal ad, but it certainly sounds like a request that would be made by today’s large retailers. From the thousand-store discount chain sourcing from hundreds of vendors in Asia, to the European boutiques on Rodeo Drive, reliance on a single method of payment for international transactions has become increasingly unpopular.

In the words of a senior logistics manager at a *Fortune* 500 retail organization, “There is no question that we need to streamline our operation and reduce the paperwork associated with letters of credit.” The owners of a successful chain of bridal stores express a similar need. “In a nutshell, we need to find more than one way to manage our international buying activities.” In both cases, the companies solved their problems by switching to an open account trade program that works in tandem with their letter of credit (LC) structure and electronic data interchange (EDI) systems — and they found exactly what they were “desperately seeking.”

each other can reduce the time and cost associated with LC and documentary collections by taking advantage of the open account trade process in which a provider not only effects payment for open account purchases, but also streamlines the reconciliation process.

This is how it works. The buyer presents purchase order information to the seller and the open account trade program service provider (provider) by sending an electronic purchase order message. The seller then presents commercial documents (shipping and any required documents) to the provider that contain the information the buyer needs to ensure the transaction qualifies for payment. The provider reviews those documents against the buyer’s predefined examination elements. Following this match-up process, the provider sends an electronic message containing details of presentation to the buyer, who, in turn, determines if/when payment is to be made. The buyer then communicates the pay decision to the provider, who pays the seller.

### **Why Open Account Trade Payments?**

Implementation of an open account trade program can provide tangible benefits for both buyer and seller. Buyers are able to decrease banking and internal processing costs, and reduce working capital.

### **What are Open Account Trade Programs?**

Buyers and sellers who regularly conduct business with



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Sellers are able to decrease internal costs and their savings per transaction can be significant — as much as 80 percent in some instances.

Whether making purchases from 12 or 1,200 vendors, consider the following issues to help determine the benefits of an open account trade program:

- Does the company have established relationships with quality vendors? Although open account trade is an ideal payment solution for buyers that have established relationships with their sellers, this payment method is primarily for long-term relationships with well-capitalized vendors. Accordingly, newer or smaller vendors may continue to use LCs and migrate to open account trade at a later date dependent upon the comfort level and need of both parties.
- Has the retailer made a significant outlay for EDI technology and now wants to leverage the investment? Whether the payment method is open account trade or LC, EDI technology can process both payment methods.

## Putting the Program to Work

A successful pilot program would consist of 1) identifying a limited number of vendors that would yield the largest dollar volume of purchases and 2) selecting the countries that are representative of the vendor population. A sampling of 20 or 30 vendors in as few as

four countries (e.g., Guatemala, Hong Kong, Taiwan and the United States) could be the first phase of a pilot program. When fully implemented, the program would comprise a much greater proportion of the company's import volume.

For example, a general merchandise retailer with nearly 1,500 store locations has more than 10,000 transactions per year in its program. This multi-billion dollar retailer of department stores has a direct mail and an online business, as well, and anticipates that the company and its vendors will realize cost savings of \$3.5 million in the first full year of operation.

In the words of a senior treasury officer from the retailer, "With our open account trade program we get savings on every level: first by reducing the volume of paperwork; second by reducing the need to utilize our credit lines; and third by decreasing our costs for reconciling and settling thousands of international purchase orders. Furthermore, because we can implement [the open account trade program] over our existing letter of credit processes, there is no need to reinvent and relearn our internal processes."

## Optimizing Banking Relationships

The move from an LC to an open account trade relationship is a complex undertaking that can affect both the company and its vendors. For this reason, program initiators should look to their bank for expert assistance and guidance on structuring and implementing the program. Keep in mind

## The Benefits of Open Account Trade Processing

- **A streamlined payment process** — Payment is affected upon receipt of instructions to pay, not upon receipt of documents conforming to the terms and conditions of an LC.
- **Reduced dependence on trade credit lines** — As the open account trade program expands to more vendors, trade credit lines can be reallocated efficiently.
- **Better basis for price negotiation** — This results from the accelerated receipt of payments and the substantial savings vendors realize from switching to the program.
- **Internal processing efficiencies** — Processes continue to evolve and improve as the open account trade program is rolled out to the vendor population.
- **Room for both payments methods** — The open account trade program operates within the same integrated payment platform as the letter of credit.

that the ability to ensure a speedy adoption, for both the company and its vendors, will directly affect profitability.

It is also beneficial to work with a bank that has an on-the-ground presence in the countries where the program operates. Vendors look to these banking resources to assist with transactions and as a possible source of financing in the absence of the LC.

Finally, while reduced costs are important, retailers should remember that they are initiating a long-term relationship; so be sure the package is wrapped in world-class service delivery with a provider that has a historic commitment to providing trade services.

## Looking Forward

Regardless of the mechanisms used for conducting international trade, the critical aspects of document handling and the

provision of information will continue to be the universal requirements for any international payment service. Both areas have great potential for redesign using current and developing technology.

And although technology will continue to play a significant role in expediting document preparation, merely facilitating document preparation or information flow does not provide a true value-added service. There is an equally critical need to have the information verified, consolidated and relayed in a useable format. ▀

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