



# MEMO STATE OF MIND



Taking goods on consignment lets retailers keep their options open, conserve capital, and cut down on credit-line complications.

BY ROBERT HOBERMAN

In our security-dominated lifestyle, where completing a simple transaction usually requires a username and password, facial recognition, or some other form of technology, it is almost refreshing to see that the memo — a practice nearly as old as the jewelry industry itself — is alive and well.

The memo is a simple agreement, typically between a wholesaler and retailer. There is minimal paperwork involved; the arrangement is largely based on time and trust. In an industry as deeply rooted in tradition as the jewelry business, it's common for people to have worked with each other's firms and/or families for generations. It's not unusual for extraordinary quantities of precious stones and jewelry to change hands based on a memo and a handshake.

In the most basic form of this deal, the supplier leaves items with a retailer, who does not pay for them until they sell. Often a long-term, interest-free arrangement, the memo is about as sophisticated as the aforementioned handshake and just as binding.

## STAYING FLEXIBLE

While memos aren't flawless (see sidebar), they have certain advantages, particularly on the retail end. Accepting goods on memo can improve a business's cash management. It enables retailers to expand their inventory without paying for it until it sells, and thereby conserve capital. Without the memo, the retailer would need to spend that capital on inventory, often with no guarantee that the items would sell within a reasonable time period. Typically backed by generous terms, the opportunity to offer an expanded merchandise lineup without an additional cash outlay is an attractive one — especially since memo goods are often at a higher price point than a retailer would usually purchase for stock.

Consider, too, that prices for precious stones and metals are dynamic and often fluctuate based on market conditions and changing consumer preferences. What may have been highly fashionable in the spring may no longer be desirable in the fall, so the retailer might need to sell it at a discount or return it. Should prices substantially drop, retailers with goods on memo can renegotiate before buying them. Conversely, if prices rise, having memo items based on a lower price can increase the retailer's profit margin.

## THE FINANCE ANGLE

Another bonus is that memo does not impact the retailer's tax liability, and actually helps its credit profile. It's not usually necessary to disclose memo goods on financial statements, and there is no limit to the number of such goods a retailer may accept. Since the items are not the property of the consignee — i.e., the retailer — they are not recorded as a purchase and are therefore not an accounts-payable liability.

A similar principle applies when it comes to securing a loan or line of credit. Lenders trained to calculate risk tend to frown on those who take on extra accounts payable and tie up too much working capital in inventory. However, goods on memo are excluded from the credit-line application process, as they belong to the supplier until sold.

The memo method also lets retailers avoid the interest expense of a bank-based credit line, making cash available for other, more pressing needs like expansion or meeting payroll. Banks will charge interest on all amounts owed, and typically require a personal guarantee and credit check as well to determine if the applicant is a worthy risk. This process is time-consuming, and the end result frequently does not meet the retailer's credit needs. In contrast, memo items are interest-free and do not require a personal guarantee, as the parties can rapidly make deals based on trust, reputation, and a mutual willingness to build a thriving business relationship.

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## MITIGATING THE RISKS

When using memo, the wholesaler or manufacturer assumes a fair amount of risk. A memo may begin with a short-term agreement that the parties can extend as needed, but keeping track of items and getting paid once they sell can be challenging and time-consuming. This makes accurate record-keeping critical.

The longer an item remains on memo, the greater the risk. Hazards such as theft, loss, or damage from fire or natural disasters become increasingly likely over time. Similarly, if a retailer holding memo goods declares bankruptcy, obtaining restitution can be difficult. Under these circumstances, a supplier may have limited recourse, as most memos offer little or no protection. Claims from other creditors such as government entities and banks may take precedence, and the memo goods themselves may even be used to pay them back.

Miscommunications are another potential issue. Seemingly simple agreements can get complicated, and misunderstandings can strain or ruin relationships when memos go awry. While there are some generally accepted rules of conduct for memos across the jewelry industry, terms and conditions can vary. Putting terms and item descriptions in writing and making certain that both parties realize their responsibilities can help prevent future problems.

Experts such as independent accounting firms and lawyers with jewelry industry experience can provide guidance in crafting the right memo for your business needs. As with many business arrangements, clear communication and mutual understanding of each party's obligations from the beginning can help ensure a positive long-term experience.

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