



RISK NOTE

SUBJECT: Who is responsible for property on consignment?

In many organizations, but particularly in health care, capital funds are in short supply. Materials management staff are challenged on a regular basis to find better ways of managing expenditures. One way of doing this is to reduce expenditures on inventories of stock and supplies by way of a consignment arrangement. The following scenario demonstrates such an arrangement.

A large hospital arranged with a supplier of medical equipment to receive 50 heart valves. Each was valued at \$7,000. Rather than pay in advance the entire cost of \$350,000, the hospital and the supplier agreed that the stock would be inventoried monthly and the hospital would only pay for the heart valves they had used.

Before your organization considers entering into an arrangement like this, it is essential that you come to an understanding with the supplier as to who will be responsible for the equipment in the event that it is damaged before you pay them for it. Under a standard purchase order, title to the property wouldn't usually transfer until the equipment had been "purchased" by the hospital. The store of unused heart valves would continue to be owned by the supplier up to that point.

Under the Health Care Protection Program "Property Coverage Agreement" coverage for "all real property and personal property of every kind and description" is provided only for property that is "owned or leased by the Health Care Agency or for which the Health Care Agency has agreed to provide coverage". Since the consigned equipment is neither owned nor leased by the Health Care Agency, there must be a written agreement stating who is responsible for the consigned equipment and at what point the risk of loss passes from one party to the other. If it is the intent that the Health Care Agency be responsible for the equipment, the agreement must state that the Health Care Agency agrees to provide coverage otherwise the Health Care Protection Program is limited in its ability to respond should a loss occur.

A contract is the essential tool that informs both parties of their responsibilities and objectives. Such an agreement should be in writing and address the following points:

- Description of the goods being consigned
- Duration of the consignment agreement
- Who is responsible for the items and when the risk passes from one party to the other

- Insurance particulars at each stage
- Retail prices (what you will pay if you use the goods)
- Wholesale prices (what you will pay if the goods are damaged before you use them)
- Any special responsibilities with respect to maintenance (i.e. temperature, humidity, security etc.)

Common understanding will have the added benefit of helping you to maintain a good business relationship with suppliers in the event of an unforeseen mishap.

This type of consignment arrangement is not typical and is, in fact, more similar to one of bailment - where one party is entrusted to hold the goods of another for safekeeping. Consequently, we recommend that you have your agreement drafted, or at the very least reviewed, by your legal counsel. Remember that contracts provided by the supplier will not necessarily protect your interests.

We recommend that the supplier be responsible for insuring the property while it is in their control. If they have arranged the transportation they should be responsible for insuring the goods up to and including the point they are received and accepted in good condition at your site. Similarly, agree with the supplier as to who will be responsible for the property if it is being returned to them unused for any reason.

HCPP would be pleased to review contracts related to consignment arrangements from a risk management and insurance perspective upon submission of the draft form of contract to us.

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It should be clearly understood that this document and the information contained within is not legal advice and is provided for guidance from a risk management perspective only. It is not intended as a comprehensive or exhaustive review of the law and readers are advised to seek independent legal advice where appropriate. If you have any questions about the content of this Risk Note please contact your organization's risk manager or chief risk officer to discuss.