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ACCIDENT AND MALPRACTICE LIABILITY OF PROFESSIONAL CORPORATION SHAREHOLDERS

Historically, the inability of professionals\(^1\) to incorporate their practices\(^2\) meant that each member of a professional group practice was jointly and severally liable for all tortious harm arising from services rendered by any other member or employee on behalf of the organization.\(^3\) During the past fifteen years, however, special professional corporation legislation has been enacted in every state.\(^4\) Most of these acts exempt all shareholders from liability for tortious harm arising from services rendered by any other shareholder or employee on behalf of the corporation.\(^5\)

\(^1\) Most state professional corporation acts use the term "professional" broadly to denote services performable only pursuant to a license granted by the state; however, many statutes deny use of their provisions to those who can legally incorporate under any other act. See, e.g., ARIZ. REV. STAT. ANN. §§ 10-902.5, 10-903.A (Supp. 1975); CAL. CORP. CODE §§ 13401, 13402 (West Supp. 1975). Physicians, dentists, lawyers, and accountants are the least likely to be able to incorporate under any other act. See cases collected in Willcox, Hospitals and the Corporate Practice of Medicine, 45 CORNELL L. REV. 432, 442-43 (1960); Wormser, Corporations and the Practice of Law, 5 FORDHAM L. REV. 207, 208-14 (1936). This note limits its discussion to these four professions because they are the prime beneficiaries of professional corporation legislation and because relevant information is lacking concerning other professions. Special account will be taken of physicians. They have utilized the professional corporation form far more than other professionals. See Hayes, Professional Corporations in Iowa — 1970-1972, 25 DRAKE L. REV. 161, 162 (1975) (Health care professionals utilize 90 percent of Iowa's professional corporations.) Furthermore, pertinent accident data is much more complete and recent for physicians than for any other profession.


\(^3\) Three forms of business organization were open to professionals wishing to engage in group practice. The only common one, the partnership, is always characterized by full and independent liability of each general partner for torts committed by any partner or employee of the partnership. See note 16 infra. The rarely used joint stock company is generally characterized by joint and several liability. H. HENN, HANDBOOK OF THE LAW OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 54 (1970). Only a minority of the states invariably impose joint and several liability on the occasionally employed business trust; a larger group imposes such liability where, as is likely in business trusts formed to provide professional services, full control is exercised by the beneficiaries. Id. at § 64.


\(^5\) See, e.g., ALA. CODE tit. 46, §§ 350, 359; tit. 10, § 21(41) (Cum. Supp. 1973). The statement in the text is based upon the author's examination of over forty of the state statutes. As in the Alabama legislation just cited, the most prevalent provision merely states that no change is intended. In such an absence of a positive provision, the incorporation by reference of all nonconflicting business corporation law means that the limited liability characteristic of business corporations also characterizes professional corporations. Although the shareholders are subject to no liability as a legal matter, their corporation is fully liable by virtue of the doctrine of enterprise liability. See James, Vicarious Liability, 28 TUL. L. REV. 161 (1954). Thus, each shareholder is, in effect, liable to the extent of his or her share in the corporation's assets. This de facto liability is called "limited liability," both in contrast to the broader legal standard of joint and several liability and because it is limited to each shareholder's share in the corporate assets.
This shift to limited tort liability warrants examination for several reasons. First, shareholder nonliability finds scant justification in the basic policy of the professional corporation acts in modifying traditional corporate qualities whenever necessary to preserve the public protection objectives of professional licensing laws, which for many years had been held to prohibit the formation of professional corporations.\(^6\) Reducing liability would seem to be discordant with the special responsibilities placed upon professionals by licensing laws.\(^7\) Second, the only apparent justification for retaining limited liability no longer exists. Professional corporation laws were enacted as a result of efforts by professionals to share in the federal tax advantages available to corporations.\(^8\) Because the drafters of the early acts knew that the Internal Revenue Service would oppose treating professional corporations as corporations

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\(^6\) The professional licensing acts were designed to protect the public from ignorance, incompetence, and imposition. See, e.g., Funk Jewelry Co. v. State ex rel. La Prade, 46 Ariz. 348, 50 P.2d 945 (1935); Willcox, supra note 1, at 445. But cf. Gellhorn, The Abuse of Occupational Licensing, 44 U. Chi. L. Rev. 6 (1976) (discussion of substantial abuses by professional groups); notes 75-78 and accompanying text infra (professionals’ abuse of monopolies granted by licensing acts). The courts presented a series of evils that would occur if professionals were permitted to incorporate. Among the destructive aspects emphasized were commercial exploitation, gross corporate misconduct unreachable by the licensing authorities, and diversion of professional loyalty from clients to employers under the influence of lay control and the profit motive. See, e.g., People v. Pacific Health Corp., 12 Cal. 2d 156, 82 P.2d 429 (1938), cert. denied, 306 U.S. 633 (1939). Parker v. Board of Dental Examiners, 216 Cal. 285, 14 P.2d 67 (1932); In re Cooperative Law Co., 198 N.Y. 479, 92 N.E. 15, 16 (1910). The dangers asserted through the years are discussed in Jones, supra note 2, at 354-55.

The modifications made in the state professional corporation acts to prevent these dangers while extending the business advantages of the corporate form can be grouped under five headings:

1. All acts limit the permissible scope of business activity to one or two complementary professions and investments. See, e.g., ALASKA STAT. § 10.45.240 (Supp. 1971); IOWA CODE § 496C.4 (Supp. 1975).

2. In order to ensure that no lay person can exert any control over professional decisions or derive any profit from the corporation, all acts place a series of restrictions on the issue, transfer, and voting of shares and on the qualifications of directors and officers. See, e.g., CAL. CORP. CODE §§ 13401(c), 13403, 13406, 13407 (West Supp. 1975).


5. Some acts impose personal liability on shareholders for the torts of employees. With respect to contractual debt, however, these acts also grant shareholders limited liability. See, e.g., ARIZ. REV. STAT. ANN. § 10-905 (Supp. 1974); ME. REV. STAT. ANN. tit. 13, § 708 (1974); OR. REV. STAT. ANN. § 58.185 (1975).

6 See Kurzner v. United States, 413 F.2d 97, 101, 106 (5th Cir. 1969); Note, supra note 7, at 777-78, 779-80, 784, 789.

7 See Jones, supra note 2, at 361; Note, Professional Corporations and Associations, 75 HARV. L. REV. 776, 788-90 (1962).
for tax purposes and because these acts departed substantially from the incidents of corporate form relevant to corporate tax treatment, retention of the corporate feature of limited liability was potentially a crucial factor in the impending legal struggle with the Service. Once this battle was won in 1969, limited liability was no longer essential to preserve the federal tax advantages originally sought by these acts. Finally, the malpractice crises affecting the various professions in the past few years have stimulated extensive debate over the appropriate scope of professional liability and have, in combination with recent federal tax relief for unincorporated professionals, accentuated the importance of liability differences between partnerships and corporations.

Part I of this note describes the various tort liability provisions

9 See United States v. Kintner, 216 F.2d 418 (9th Cir. 1954) (nonacquiescence of the Internal Revenue Service) (The court held that an association of physicians qualified as a corporation for federal tax purposes because the association agreement conferred sufficient corporate attributes on the association.); Galt v. United States, 175 F. Supp. 360 (N.D. Texas 1959); Shores, supra note 4, at 694; Note, supra note 7, at 784-85.

10 In federal tax law a business organization must have more corporate than noncorporate characteristics in order to gain corporate tax status. See Treas. Reg. § 301.7701-1.2(a), T.D. 6503, 1960-2 C.B. 409. Under this regulation, the restrictions discussed in note 6 supra would probably have been held by the Service to preclude corporate tax treatment for any professional corporation if the shareholders did not enjoy limited liability. See Kurzner v. United States, 413 F.2d 97, 104 (5th Cir. 1969); Note, supra note 7, at 783-84.

11 The 1965 amendments to the regulation cited in note 10 supra made it clear that the Service would oppose even those professional corporations possessing limited liability. See Treas. Reg. § 310.7701-1.2(a), 2(h), T.D. 6797, 1965-1 C.B. 553. But after several rounds of adverse litigation, Kurzner v. United States, 413 F.2d 97 (5th Cir. 1969); O'Neill v. United States, 406 F.2d 157 (10th Cir. 1967); Holder v. United States, 289 F. Supp. 150 (N.D. Ga. 1968), the Service conceded the issue. It stated that professional corporations would be taxed as corporations whether or not they had limited liability or any other corporate characteristics, if the state labeled them as corporations. T.I.R. 1019 (1969); Rev. Rul. 70-101, 1970-1 C.B. 278.

12 Compare the dissenting statement of Charles A. Hoffman in U.S. DEPT. OF HEALTH, EDUC. & WELFARE, SECRETARY'S COMM’N ON MEDICAL MALPRACTICE: REPORT 113, 121-25 (1973) [hereinafter cited as REPORT] (advocating reduced liability to ease ill effects of malpractice crises), with Wagner, At the Core: The Patient, TRIAL, May/June 1975, at 44 (advocating broad exposure to deter excessive levels of malpractice).

found in the professional corporation acts, focusing particularly on
the recently published Model Professional Corporation Supple­
ment.14 Part II compares how effectively these alternatives ac­
complish the goals of accident law in the professional corporation
setting. The inability of the preferred model provision to alleviate
the malpractice problem in any way as well as proposals for rein­
vigoration of the professional corporation act concept are dis­
cussed in Part III.

I. STATE AND MODEL TORT LIABILITY
PROVISIONS

The great majority of state professional corporation acts pro­
vide limited shareholder liability identical to that of shareholders
in typical business corporations.15 However, a few states subject
professional corporation shareholders to the joint and several lia­
bility traditionally applied to partners.16 Variations on each of
these two statutory approaches also exist,17 and a few states amal­
gamate both types by replacing joint and several liability with
limited liability if a specified amount of liability insurance is main­
tained.18

14 The Model Professional Corporation Supplement [hereinafter cited as "Model"] is a
project of the American Bar Association's Committee on Corporate Laws. It was approved
by the Committee after its second reading on June 25, 1976, and subsequently published for
comments in the BUSINESS LAWYER. See Professional Corporation Supplement to the
Model Business Corporation Act, 32 BUS. LAW. 289 (1976). A member of the Committee has
informed the author that few changes are contemplated before final adoption and promulga­
tion in 1977.

15 See note 5 supra.

16 See note 6(5) supra. None of these states appears to have construed the nature of this
liability authoritatively. Presumably, it would be closely analogous to the joint and several
liability of partners. Case law under sections 13-15 of the Uniform Partnership Act, which
now governs partner liability in forty-seven states, 6 UNIFORM LAWS ANN. 5 (Supp. 1975),
shows that partners are personally liable, either individually or in any combination the
plaintiff may choose, for tortious acts of the firm or any of its partners, agents, or employees
acting within the scope of their authority. See Phillips v. Cook, 239 Md. 215, 219-20, 223-24,
210 A.2d 743, 746, 749 (1965); Martinoff v. Triboro Roofing, 228 N.Y.S.2d 139, 141-42 (Sup.
Ct. 1962), Hardy & Newsome, Inc. v. Whedbee, 244 N.C. 682, 683, 94 S.E.2d 837, 838
(1956). There is considerable authority in partnership law that partnership assets must be
exhausted before the assets of individual partners can be attached. See Horn's Crane Serv.
v. Prior, 182 Neb. 94, 95, 152 N.W.2d 421, 423 (1967); Young v. Mayfield, 316 P.2d 162, 165
(Okla. 1957). By analogy, the professional corporation's assets would probably have to be
exhausted before the separate personal assets of the shareholders could be used to satisfy
the debt.

17 See, e.g., MINN. STAT. ANN. § 319A.10 (Supp. 1975) (nullifying all personal vicarious
liability and granting limited liability); ME: REV. STAT. ANN. tit. 13, § 708 (1974) (retaining
joint and several liability if the shareholder is personally involved in a professional relation­
ship).

18 See, e.g., COLO. REV. STAT. ANN. § 12-36-134(g) (1974); S.D. COMPIL. LAWS ANN. §
In the model provisions the liability of each individual for accidents arising from the rendition of professional services as an employee on behalf of a professional corporation is determined by the tort law standards normally applicable to an individual professional.\textsuperscript{19} The corporation is liable to the same extent as the employee if the accident arises from services within the employee's apparent authority.\textsuperscript{20} But with respect to shareholder liability, the Model offers standardized language for each of the three main alternatives: limited liability;\textsuperscript{21} joint and several liability;\textsuperscript{22} and joint and several liability unless the corporation has provided adequate security for financial responsibility, in which case all shareholders gain limited liability status.\textsuperscript{23}

\textsuperscript{19} Professional Corporation Supplement to the Model Business Corporation Act, supra note 14, at 302, § 11(b):
Every individual who renders professional services as an employee of a professional corporation shall be liable for any negligent or wrongful act or omission in which he personally participates to the same extent as if he rendered such services as a sole practitioner . . . .

\textsuperscript{20} Id. § 11(c):
Every corporation whose employees perform professional services within the scope of their employment or of their apparent authority to act for the corporation shall be liable to the same extent as its employees.

\textsuperscript{21} Id. § 11(d) (Alternate 1):
Except as otherwise provided by statute, the personal liability of a shareholder of a professional corporation shall be no greater in any respect than that of a shareholder of a corporation organized under the . . . Business Corporation Act.

\textsuperscript{22} Id. § 11(d) (Alternate 2):
Except as otherwise provided by statute, if any corporation is liable under the provisions of subsection (c) of this section, every shareholder of the corporation shall be liable to the same extent as though he were a partner in a partnership and the services giving rise to liability had been rendered on behalf of the partnership.

\textsuperscript{23} Id. § 11(d) (Alternate 3):
(1) Except as otherwise provided by statute, if any corporation is liable under the provisions of subsection (c) of this section, every shareholder of that corporation shall be liable to the same extent as though he were a partner in a partnership and the services giving rise to liability had been rendered on behalf of the partnership, unless the corporation has provided security for professional responsibility as provided in paragraph (2) of this subsection and the liability is satisfied to the extent contemplated by the insurance or bond which effectuates the security.

(2) A professional corporation, domestic or foreign, may provide security for professional responsibility by procuring insurance or a surety bond issued by an insurance company, or a combination thereof, as the corporation may elect. The minimum amount of security and requirements as to the form and coverage provided by the insurance policy or surety bond may be established for each profession by the licensing authority for the profession, and the minimum amount may be set to vary with the number of shareholders, the type of practice, or other variables deemed appropriate by the licensing authority. If no effective determination by the licensing authority is in effect, the minimum amount of professional responsibility security for the professional corporation shall be the product of . . . dollars multiplied by the number of shareholders of the professional corporation.

The model provisions fail to specify whether the corporation must post security before injury, notice of injury, suit, or judgment in order to gain limited liability. The earliest point is preferable in order to prevent corporations from obtaining limited liability after an accident but before liability has been established. See Colo. Rev. Stat. Ann. § 12-36-134(g) (1974). The Colorado Act, which specifies the minimum level of insurance, has less flexibility than the model provisions, which permit other forms of security and allow licensing authorities considerable discretion in setting the amount of security required.
II. COMPARATIVE ACHIEVEMENT OF ACCIDENT LAW GOALS

Determining which of these tort liability alternatives is preferable requires comparison of how well each option accomplishes the goals of accident law. In making that determination this note employs the schema of accident law developed by Professor Guido Calabresi.\(^{24}\) Calabresi posits two fundamental goals: minimizing accident costs and doing so in a fair way.\(^{25}\) The first goal he subdivides into three subgoals: minimizing the number and severity of accidents; minimizing the social costs of accidents that do occur; and optimizing the costs of achieving the subgoals.\(^{26}\) The goal of fairness seeks to ensure that the mechanisms used to minimize accidents and their social costs do not deviate unduly from other social and ethical values.\(^{27}\)

A. Minimizing the Number and Severity of Accidents

Calabresi discusses two methods of minimizing the number and severity of accidents. The first method, market deterrence, leaves achievement of accident minimization entirely to market forces.\(^{28}\) In theory, bargaining in a perfectly competitive market between risk-averse buyers and sellers possessing total rationality and costless knowledge of all accident costs\(^{29}\) will reduce the number and severity of accidents to the optimal point.\(^{30}\) The real market is less


\(^{25}\) ACCIDENT COSTS, supra note 24, at 24.

\(^{26}\) Id. at 26-28.

\(^{27}\) Id. at 24. The fairness goal "requires that our many goals not specifically dealt with under cost reduction be adequately handled by the proposed system." Id. at 24 n.1. See Cramton, Driver Behavior and Legal Sanctions: A Study of Deterrence, 67 MICH. L. REV. 421 (1969).

\(^{28}\) ACCIDENT COSTS, supra note 24, at 68-69; Primary Accident Costs, supra note 24, at 432; Calabresi also calls this method general deterrence.

\(^{29}\) Optimal Deterrence, supra note 24, at 657, 660-61; Transaction Costs, supra note 24, at 67-68. Pertinent costless knowledge includes knowledge of the risk of injury, risk of negligence by either party, cost of the injury to either party, alternative methods of preventing or reducing the injury or negligence, and the costs of those methods.

\(^{30}\) Transaction Costs, supra note 24, at 67-68. See ACCIDENT COSTS, supra note 24, at 70. The optimal point is reached when the cost of achieving greater safety exceeds the savings in accident costs that are achieved thereby. See Transaction Costs, supra note 24, at 68. Thus, as accident costs increase, their number and severity decrease, both through bargaining and as a result of decisions to forego purchasing a good or service with high accident costs or to substitute one with lower accident costs. ACCIDENT COSTS, supra note 24, at 73.
than perfect, however, for competition is imperfect, knowledge of accident costs and safety techniques is costly, and people often act irrationally.\(^{31}\) As these distortions increase, the utility of the market approach decreases.

The other method, collective deterrence, encompasses all accident minimization decisions made on some societal level and enforced without regard to market forces.\(^{32}\) Collective deterrence also operates imperfectly, due to the economic impracticability of and societal aversion to thoroughgoing regulation.\(^{33}\)

Personal fault, the dominant principle of liability in accidents arising from the rendition of professional services,\(^{34}\) combines elements of both methods of deterrence. It does so by initially depending upon the myriad standards of liability collectively established by juries and then leaving each person free to decide in the marketplace whether having accidents is worth the price of these collectively imposed costs.\(^{35}\)

1. Deterrent Incentives—Both limited liability and joint and several liability are purely market-incentive forms of deterrence. Neither enlarges the scope of liability; both merely increase the number of sources for payment of the liability.\(^{36}\) In each the corporation is held fully liable once an employee is found liable under the personal fault standard for a work-related accident.\(^{37}\) Joint and


\(^{32}\) *Accident Costs*, supra note 24, at 95.

\(^{33}\) *Id.* at 76-77, 108-11; *Primary Accident Costs*, supra note 24, at 431.


\(^{35}\) *Optimal Deterrence*, supra note 24, at 660. The deterrent incentives from accident costs apply to all persons, not just potential defendants, because a verdict for the defendant in effect makes the injured plaintiff liable by not reallocating the cost. *Primary Accident Costs*, supra note 24, at 442 n.20.

In addition to the immediate cash award from a verdict or settlement, the accident costs that generate deterrent incentives include the professional's fear of losing business because of a tarnished reputation or a restricted license. *See Ohio Rev. Code Ann.* § 4731.22(B)(2), (6) (Page Supp. 1975) (negligent practice as ground for license restriction or revocation); Statement of George Northup, in *Report*, *supra* note 12, at 106; *Comment, supra* note 34, at 632, 683. This element of deterrence may decrease if there is a considerable increase in the percentage of professionals sued due to the malpractice crises. *See Brook, Brutoco & Williams, The Relationship Between Medical Malpractice and Quality of Care*, 1975 *Duke L. J.* 1197, 1217.

\(^{36}\) *See James, supra* note 5, at 161-63; notes 17-23 and accompanying text *supra*.

\(^{37}\) *See James, supra* note 5, at 161, 210; notes 5, 17-23 and accompanying text *supra*. In nonprofessional corporations the whole award is almost always paid by the corporation without any indemnification by the negligent employee. Fleming, *The Role of Negligence in Modern Tort Law*, 53 *Va. L. Rev.* 815, 834 (1967); *James, Accident Liability Reconsidered: The Impact of Liability Insurance*, 57 *Yale L.J.* 549, 556-57 (1948). Although this phenomenon does not by itself increase deterrent incentives, it may increase their effectiveness by
several liability goes a step further by making each shareholder fully and independently liable as well. Because jointly and severally liable shareholders risk their entire personal wealth as well as their shares in the corporate assets, this form of liability creates greater financial incentives than does limited liability to reduce the number and severity of accidents and does so to the extent that the combined assets of the culpable employee and corporation fail to satisfy the award.

The likelihood that these combined assets will be insufficient is greatest where professional liability insurance is not present. Many professionals carry little or no liability insurance, and their number appears to be rising as professionals react to extreme increases in the cost of such coverage in recent years. In this situation long run inadequacy of assets to cover liabilities is likely despite the significant amount of protection provided by the combined assets of the employee and the corporation.

focusing them on one person, the corporation, which is better able to reduce accidents. See James, supra note 5, at 172. This phenomenon appears to be largely absent in professional corporations because the professional employees usually carry their own insurance. See Roddis & Stewart, The Insurance of Medical Losses, 1975 DUKE L.J. 1261, 1291. To that extent, the enterprise liability imposed by limited liability and joint and several liability creates greater accident minimization incentives only where the employee's inability to satisfy the award forces the corporation to contribute its assets. In professional corporations these incentives are effectively spread to the shareholders to the extent of their share in the corporate assets because professional corporations are almost invariably close corporations in which shareholders are intimately involved as professional staff, officers, and directors. See Treas. Reg. § 301.7701-2 (h)(2), T.D. 6797, 1965-1 C.B. 553; Note. supra note 7, at 783-95; note 6(2) supra.

38 See note 16 and accompanying text supra.

39 These additional incentives are composed entirely of the likelihood that some shareholder will be required to pay part of an accident award out of personal resources. The less direct financial elements of accident minimization incentives, such as loss of reputation, are absent because there is no functional difference between shareholders in a limited liability corporation and those in a joint and several liability corporation. See note 37 supra.

40 Among physicians liability insurance has been viewed as indispensable. See Hoffman, supra note 12, at 124. Surveys performed in the early 1970's attempting to establish the percentage of lawyers carrying professional liability insurance placed it between 50 and 80 percent. See sources cited in Note, Improving Information on Legal Malpractice, 82 YALE L.J. 590, 601 n.47 (1973) [hereinafter cited as Legal Malpractice]. For accountants the fraction carrying liability insurance was estimated at 75 percent in the early 1970's. See Shear, Professional Liability Problems Among Architects, Engineers, Lawyers, and Accountants, in U.S. DEP'T OF HEALTH, EDUC. & WELFARE, THE SECRETARY'S COMM'N ON MEDICAL MALPRACTICE: APPENDIX 637, 642 (1973) [hereinafter cited as APPENDIX with citations to individual studies].

41 Hanahan, Malpractice, ATLANTIC MONTHLY, April 1976, at 6; Dixon, 'Going Bare' May Be Hazardous to Your Fiscal Health, J. LEGAL MED., March 1976, at 23.

42 The degree of protection depends upon the distribution of accident liability costs and the available assets of professional employees and their corporations. Accident liability cost data is extremely fragmentary except for physicians, for whom the average claim payment in 1970 was $10,600 and the estimated paid claim frequency was between 1.4 and 2.2 per 100 physicians with approximately 40 percent of the claims resulting in some payment. See Steves, A Proposal to Improve Cost to Benefit Relationships in the Medical Professional Liability Insurance System, 1975 DUKE L.J. 1305, 1312-13, 1315. These figures were derived from a universe of insured physicians but should be fully applicable to uninsured physicians as well because it is unlikely that physicians willing to take the risk of practicing without
The great majority of professionals carry professional liability insurance to protect their personal wealth. The statistical chance that one of the awards made in 1970 of over $100,000 (3 percent of all awards) would be made against one of the 8 percent of insureds carrying less than $100,000 in insurance would be substantially below 0.24 percent because only 23 percent of the awards over $100,000 were made against only one insured and because physicians in the handful of states in which high judgments are prevalent carry higher amounts of insurance. Compare Rudov, Myers & Mirabella, supra note 42, at 13, 15, with Steves, supra note 42, at 1312 n.32.

43 See notes 40-41 supra.

44 The statistical chance that one of the awards made in 1970 of over $100,000 (3 percent of all awards) would be made against one of the 8 percent of insureds carrying less than $100,000 in insurance would be substantially below 0.24 percent because only 23 percent of the awards over $100,000 were made against only one insured and because physicians in the handful of states in which high judgments are prevalent carry higher amounts of insurance. Compare Rudov, Myers & Mirabella, supra note 42, at 13, 15, with Steves, supra note 42, at 1312 n.32.

45 Many physicians, for instance, have increased coverage from the minimum $25,000/$75,000 policy to $100,000/$300,000 or higher (The first figure represents the maximum policy coverage per claim, while the second indicates maximum policy coverage per year.). Nonetheless, the dramatic increases in claim frequency and severity are likely to create a fear of inadequacy. The experience of physicians in California provides the best...
several liability is likely to impose additional incentives, chiefly in
the relatively small class of cases where insurance is absent, but
also to some indeterminate degree where normal levels of insur-
ance are present.

2. Conversion of Deterrence into Fewer Accidents—It is axioma-
tic that joint and several liability cannot more effectively achieve
the goal of minimizing accidents than limited liability unless its
additional incentives are actually converted into the marketplace
into fewer accidents. Arguments have been advanced for the con-
tradictory propositions that the personal fault system substantially
reduces the frequency of professional accidents and that it does
not have this effect. Only if the first proposition is true can joint
and several liability be expected to have a favorable impact upon
accident rates of professional corporations. Unfortunately, the
empirical data is insufficient to validate either contention. It can
be shown, however, that market distortions reduce to insignificant
proportions the class upon which joint and several liability would
have its intended effect and that on this class it operates quite
inefficiently.

a. Transfer—In an imperfect market it is generally best to
confine the allocation of accident costs as closely as possible to
those involved in the accidents. Because these persons are usu-
ally under the greatest pressure to convert cost incentives into
fewer accidents and have easiest access to the necessary accident
cost information, they are likely to be the most efficient at minimiz-
ing accidents. To a considerable extent, however, both classes
associated with professional accidents avoid these incentives by
transferring accident costs allocated to them onto others less able

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example. About 10 percent of that state's physicians faced liability in 1975. Compare Rudov, Myers & Mirabella, supra note 42, at 1, 13-15 (40 percent of claims result in some payment), with Brook, Brutoco & Williams, supra note 35, at 1197 (claim rate of 25 per 100 physician policy years in California in 1975). Prior to 1970 the figure was less than half as high. See id. In California there were thirteen awards greater than $1 million in a recent 28 month span and an increase in awards greater than $300,000 from five in 1970 to thirty-five in 1975. Linster, supra note 42, at 101. Nationwide, the average jury award in medical malpractice cases reached almost $350,000 in 1974 compared to $100,000 in 1970. The Doctors' New Dilemma, Newsweek, Feb. 10, 1975, at 41 (source: Jury Verdict Research, Inc.). Individual judgments have exceeded $4 million. The Patient Becomes the Plaintiff, Time, Mar. 23, 1975, at 62. Cf. Suing Your Lawyer, Time, May 23, 1975, at 93 ($500,000 award against a lawyer).


47 See, e.g., Brook, Brutoco & Williams, supra note 35, at 1220-22.

48 Id. at 1222.

49 See notes 50-102, especially note 83, and accompanying text infra.

50 Primary Accident Costs, supra note 24, at 439. In accident law transfer occurs to the extent that accident costs are allocated so that no person involved in the accident-prone activity carries the burden of these costs. Id. at 440. Transfer is not necessarily undesirable. however, since the transferee may actually be better able to improve safety. Id.
or willing to achieve greater safety, thereby dissipating much of the additional deterrent market incentives provided by joint and several liability.\(^{51}\)

The first element of the professionals' ability to transfer accident costs is professional liability insurance. Because the cost of insurance varies according to the rudimentary categories of geographical location and professional specialty rather than on the basis of individual accident experience,\(^{52}\) insured professionals, including those with greater than average accident costs, are able to treat their accident costs as a fixed cost of doing business.\(^{53}\) Since this fixed cost is the same for all insured professionals within the same broad risk category, consumer price resistance is the only impediment to the transfer of these costs.

Consumers, however, have shown little price resistance. This is in part due to longstanding and largely successful efforts by professionals to eliminate price competition between themselves.\(^{54}\) The substantial inelasticity of professional fees also contributes heavily to the lack of price resistance. Demand for most professional services is rather unresponsive to price variation,\(^{55}\) and professionals have vigorously prosecuted as illegal encroachments upon their services are rather unresponsive to price variation,\(^{55}\) and professionals have vigorously prosecuted as illegal encroachments upon their

\(^{51}\) See notes 52-85 and accompanying text infra.

\(^{52}\) See Steves, supra note 42, at 1319-20; Kendall & Haldi, The Medical Malpractice Insurance Market, in APPENDIX, supra note 40, at 533-34, 551-52, 556-57; Legal Malpractice, supra note 40, at 604 n.59. Unintended experience rating may occur, as when an insurer's refusal to continue insuring a particular professional forces a switch to a more costly insurer.

\(^{53}\) See Roddis & Stewart, supra note 37, at 1283-84; N.Y. Times, Oct. 25, 1976, at 22, col. 2 (A.M.A. study finding that the average cost of an office visit was 96 cents (34 percent of total increase in cost of office visit) higher than if malpractice rates had remained at 1973 levels). It has been suggested that the ability of physicians to pass on liability insurance costs is limited by the fact that physicians are prohibited from charging more than the "usual and customary" fees to the substantial number of patients whose fees are paid in part by health insurance plans. Steves, supra note 42, at 1327. See note 65 infra (insurance statistics). But the Blue Cross and Blue Shield plans are controlled by physicians, and the "usual and customary" level is quite responsive to the wishes of physicians. See Havighurst, Health Maintenance Organizations and the Market for Medical Services, 35 LAW & CONTEMP. PROB. 716, 768-69 (1970).

Even if these insurance costs were not transferable, professionals might treat them as though they were. Thus, the purchasers of auto liability insurance view it as a fixed cost of driving and take little cognizance of being placed in a higher risk category so far as changing their driving behavior is concerned. See ACCIDENT COSTS, supra note 24, at 65; Vickrey, Auto Accidents, Tort Law, Externalities, and Insurance: An Economist's Critique, 33 LAW & CONTEMP. PROB. 464, 470, 475 (1968).

\(^{54}\) See notes 73-78 and accompanying text infra.

\(^{55}\) See with respect to health care services, Havighurst, supra note 53, at 768; Mechanic, Problems in the Future of Organized Medical Practice, 35 LAW & CONTEMP. PROB. 233, 236 (1970); Reder, Medical Malpractice: An Economist's View, 1976 Am. B. Foundation Research J. 511, 558. In the legal profession one need only note its grip on the expertise and connections necessary to deal successfully with the burgeoning volume of regulatory and adminitative law. See also Schuchman, Ethics and Legal Ethics: The Propriety of the Canons as a Group Moral Code, 37 Geo. Wash. L. REV. 244, 253 (1968). Certified public accountants have their indispensability assured by the legal requirements of annual financial audits.
allocated areas of monopoly power, those cheaper substitutes that would increase price elasticity.56 Other factors, such as casualty insurance,57 tax deductions,58 and the nature of the professional relationship,59 also diminish price elasticity. Finally, the minor responsiveness that does exist is relatively insensitive to the accident cost component of professional fees, both because that component is small proportionally60 and because professional services tend to be nonstandardized with little price comparability.

Another important source of low price resistance is the ability of consumers to disguise or transfer the accident costs imposed on them. The various types of health insurance exemplify this process. Because health insurance premiums rarely vary with the health costs of the individual insured except indirectly with age, the additional benefit to any single health care consumer from additional use of insurance benefits is far greater than that individual's additional cost.61 Consequently, those within each risk category are encouraged to increase their own usage even if they realize that ultimately their own costs will also rise.62 The disregard for health care costs that drives up usage also tends to cause disregard of the accident cost component of health care costs.63

56 Carlson, Health Manpower Licensing and the Emerging Institutional Responsibility for the Quality of Care, 35 LAW & CONTEMP. PROB. 849, 850-51, esp. 851 n.7 (1970); Note, Legal Ethics and Professionalism, 79 YALE L.J. 1179, 1182 (1970). See also Pitts, Group Legal Services: A Plan to Huckster Professional Services, 55 A.B.A.J. 633 (1969); Note, Lay Divorce Firms and the Unauthorized Practice of Law, 6 U.MICH. J.L. REF. 423 (1973). The quarterly publication, UNAUTHORIZED PRACTICE NEWS, is devoted exclusively to reporting bar efforts to repel incursions upon its traditional areas of activity. For many years organized medicine staunchly opposed the prepaid group practice of medicine. See Havighurst, supra note 53, at 717, 739; Note, The Role of Prepaid Group Practice in Relieving the Medical Care Crisis, 84 HARV. L. REV. 887, 954-60 (1971). With regard to the monopoly power of professionals, see notes 73-79 and accompanying text infra.

57 I.R.C. §§ 162(a), 213. See Roddis & Stewart, supra note 37, at 1284.

58 Once an individual or organization establishes a relationship with a professional, the individual or organization is usually reluctant to terminate the relationship. Confidence takes precedence over cost.

60 As a percentage of national health care costs, the cost of professional liability insurance to all health care providers was estimated to be less than 0.5 percent during 1970 and a maximum of 1.5 percent in 1975. See Steves, supra note 42, at 1317. Physicians spent 1.3 percent of their gross income on professional liability insurance in 1970 and approximately 6.7 percent in 1976. Id. at 1318. As a fraction of the typical office visit cost, the percentage is somewhat higher. Cf. N.Y. Times, supra note 53 (A.M.A. study implying figure of about 15 percent). The cost of professional liability insurance in other professions is a significantly lower percentage of fees. Cf. Legal Malpractice, supra note 40, at 600-01 nn.46, 50 (average individual annual cost of about $130 for professional liability insurance for 55,000 lawyers in 1969).


63 See ACCIDENT COSTS, supra note 24, at 65.
This is not transfer as technically defined, but it has an even more adverse effect on incentives to minimize accidents because it causes the incentives to evaporate rather than to be shifted to another class. Fringe benefit health insurance, common in the United States, carries this phenomenon one step further by disguising the fact that the employees pay for the insurance by foregoing higher wages.

Social welfare programs, primarily Medicare and Medicaid, produce transfer of costs in the classic sense. Because the government pays the cost of covered services, the beneficiaries have almost no economic incentives to minimize accidents. Further, in practice governmental assumption of these health costs has dissipated their deterrent power as market incentives.

The absence of price resistance enables professionals to pass on all of their insurance and accident costs that do not exceed policy limits. Since typical policy limits are sufficient to satisfy all but very large awards, jointly and severally liable shareholders are insulated almost completely from personal liability where the negligent employee is insured. The absence of price resistance also enables uninsured professionals to pass on most of their accident costs. By charging the same fees as insured professionals, uninsured professionals recoup the cost of insurance each year and,

64 See note 50 supra.
65 In 1973 private health insurance plans met 75.3 percent of all personal health expenditures for hospital care and 48.5 percent for all physician's services. STATISTICAL ABSTRACT, supra note 42, at 72. It should be noted that these figures include employee contribution plans as well as those paid for by employers.
66 The employer treats the insurance costs as a wage item, whereas the employees treat it as an employer cost since they never see it being deducted from their paychecks.
67 In 1973 government expenditures for personal health care were 36.6 percent of total expenditures for personal health care. Medicare and Medicaid accounted for 22.8 percent of that total. Preliminary figures for 1974 show an increase to 37.6 percent and 25.0 percent, respectively. Total dollar value of these public expenditures was $30 billion in 1973, and preliminary figures for 1974 show an increase to $34 billion. STATISTICAL ABSTRACT, supra note 42, at 70.
68 Costs such as diminished physical capacity and pain remain uncompensated to the extent not borne by governmental rehabilitation and relief programs.
69 For instance, in Medicare and Medicaid the federal government originally cast itself as a disinterested third-party payment fund. See Stevens & Stevens, Medicaid: Anatomy of a Dilemma, 35 LAW & CONTEMP. PROB. 348, 408 (1970). The inability inherent in this system of nonsupervision to police the quality of care soon led to unbearable levels of fraud by health care providers. In order to combat fraud, the federal government took the extraordinary step of freezing physician fees under Medicaid in 1969, id. at 412-14, but in 1976 the amount of health care provider fraud in the two programs was estimated to be $3.9 billion per year, approximately 15 percent of the cost of the two programs. Compare Billions in Medicaid Ripoffs: Can Anyone Stop It?, U.S. NEWS & WORLD REPORT, March 22, 1976, at 18, with STATISTICAL ABSTRACT, supra note 42, at 70. Even where the government has attempted to use its buying power as a lever to reduce the number and severity of accidents, it has imposed collective regulation rather than market incentives and thereby has eliminated the potential deterrent superiority of joint and several liability pro tanto. 42 U.S.C. § 1320c-c(19) (Supp. 1975) (mandatory peer review program required by all health care providers applying for Medicare or Medicaid payments).
70 See notes 43-45 and accompanying text supra.
therefore, over time should be able to pass on at least the average cost of accidents with the same freedom with which insured professionals pass on accident costs not exceeding their policy limits.\(^71\) When coupled with the available assets of the negligent employee and corporation, transfer thus enables shareholders whose employees are uninsured to obtain insulation from all but extremely high awards.\(^72\)

Beyond the levels just indicated, the degree of transferability cannot be determined. Its contours can, however, be suggested by professional monopoly power. One basis of this monopoly power is the mandatory licensing laws, which allocate to each profession certain areas of legal monopoly by erecting barriers to entry.\(^73\) Despite competition at the fringe of each allocation\(^74\) and fairly low entry barriers to some professions,\(^75\) the classic cartel powers granted to professionals in the form of licensing laws and self-regulation have often been abused to reduce intraprofessional

\(^{71}\) This phenomenon is possible because insurance offers protection against only two contingencies, liability sooner than average and liability greater than average, Accident Costs, supra note 24, at 48, and because each variation in insurance cost according to geographical location, functional risk, or policy coverage causes insurance to approximate that much more closely the results of the market without any insurance, id. at 48-49. See note 72 infra. Of course, this method of transfer will not work for all since some will face liability sooner or greater than average. But even these individuals may be able to borrow against future savings.

\(^{72}\) The average premium for $25,000/$75,000 professional liability insurance for all physicians in 1975 was $984. Steves, supra note 42, at 1319. Since the average liability frequency in 1975 was about five occurrences of liability per 100 physician policy years, see note 42 supra, nearly $20,000 could be saved between each occurrence of liability if rates remained constant. Liability risk varies greatly by geographical location and specialty, and thus the $984 average varies from $273 in New Hampshire to $3,348 in California, id., and from $6,648 in New Hampshire to over $77,000 in California for the highest risk class of surgeons at a policy level of $1 million/$3 million, id. at 1319-20. This variation means that employees in specialties or in states with higher liability experience will be able to save much greater amounts. Consequently, just as the $20,000 average savings roughly equals the increase in average liability between 1970 and 1975 (based on the 14 percent rate of annual increase reported in note 42 supra), so the savings of each employee in each risk category would roughly equal the insurance costs for professionals in the same state and risk category at locally prevalent risk levels. See note 71 supra. Indeed, the elimination of broker's fees and other overhead costs should enable uninsured professionals to save more than the average amount.

\(^{73}\) Barron, Business and Professional Licensing—California, a Representative Example, 18 STAN. L. REV. 640, 643-44 (1966); Lave & Lave, supra note 62, at 260; Comment, Occupational Licensing: An Antitrust Analysis, 41 MO. L. REV. 66 (1976).

\(^{74}\) Elson, Canon 2—The Bright and Dark Face of the Legal Profession, 12 U. SAN DIEGO L. REV. 306, 308 (1975); Schuchman, supra note 55, at 253; Wormser, supra note 1, at 217.

\(^{75}\) For years there have been many lawyers with only marginally profitable practices, a situation intimating the absence of unduly high entry barriers. See Note, Legal Ethics and Professionalism, 79 YALE L.J. 1179, 1180-81 (1970). But even within law there have been entry barriers to the most prestigious jobs. Id. Organized medicine, on the other hand, has restricted entry successfully for many years. See Kessel, Higher Education and the Nation's Health: A Review of the Carnegie Commission Report on Medical Education, 15 J. LAW & ECON. 115 (1972); Kessel, The A.M.A. and the Supply of Physicians, 35 LAW & CONTEMP. PROB. 266 (1970).
competition and thereby produce monopoly profits. Among the obvious examples are the anti-information and anti-advertising policies of the professions and the adjudicated antitrust violations of organized medicine and law. Another basis of professional monopoly power is the absence of price elasticity as previously discussed.

The power to charge excessive fees naturally includes the power to transfer accident costs by concealing them in the fee structure used. The magnitude of this power can only be approximated because of the difficulty of eliminating other factors. But estimates of $1.5 billion per year in excessive legal fees and between $1 and $7 billion of "defensive medicine" charges designed to minimize malpractice claims and liability suggest that limitations on the

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76 Elson, supra note 74, at 308; Havighurst, supra note 53, at 739; Kessel, Higher Education, supra note 75, at 119; Comment, Bar Association Minimum Fee Schedules and the Antitrust Law, 1974 DUKE L.J. 1164 (citing estimate by Group Legal Institute of California of $1.5 billion of excess legal fees per year).

77 Barron, supra note 73, at 654-56, 664. See Havighurst, supra note 53, at 768; Note, supra note 75, at 1182; cf. Kessel, Transfused Blood, Serum Hepatitis, and the Coase Theorem, 17 J. LAW & ECON. 265, 285 (1974) (noting that lack of hospital advertising reduces the information flow important in reducing the incidence of serum hepatitis); Roemer, Controlling and Promoting Quality in Medical Care, 35 LAW & CONTEMP. PROB. 284, 288 (1970) (stating that many ethical strictures are really designed to control competition).

The organized bar has engaged in efforts to restrict the flow of information about legal services in violation of constitutional free speech rights. See, e.g., United Trans. Union v. State Bar, 401 U.S. 576 (1971) (upholding right of union to recommend that its members hire specified Illinois attorneys to handle their Federal Employment Liability Act actions in Michigan in order to assure competent counsel at no greater than a 25 percent contingent fee); UMW, District 12 v. Illinois State Bar Ass'n, 389 U.S. 217 (1967) (reversing on first amendment grounds an injunction that prevented union from maintaining salaried legal staff to assist its members in asserting their legal rights); Brotherhood of Ry. Trainmen v. Virginia ex rel. Virginia State Bar, 377 U.S. 1 (1964) (reversing injunction that prevented union from channeling most of the legal work of its members to specific lawyers through recommendations). The A.B.A. has recently amended its canon of ethics to liberalize the permissible limits of lawyer advertising. Code Amendments Broaden Information Lawyers May Provide in Law Lists, Directories, and Yellow Pages, 62 A.B.A.J. 309 (1976), but the Department of Justice has nevertheless filed an antitrust action against the A.B.A. in the belief that the modified restrictions continue to violate the Sherman Act, United States v. American Bar Ass'n, 5 TRADE REG. REP. (CCH) ¶ 45.076 (N.D. Ill. 1976).

78 American Medical Ass'n v. United States, 317 U.S. 519 (1943) (affirming violation of Sherman Act by A.M.A. in conspiring to obstruct the business of a group health organization by coercing A.M.A. members to refuse employment by the organization and consultation with its employees); Goldfarb v. Virginia, 421 U.S. 773 (1975) (affirming violation of Sherman Act by integrated state bar and private county bar association through promulgation and enforcement of minimum fee schedules). See Kessel, Price Discrimination in Medicine, 1 J. LAW & ECON. 20 (1958); Rayack, Restrictive Practices of Organized Medicine, 13 ANTITRUST BULL. 659 (1967); Comment, supra note 76; Comment, The American Medical Association: Power, Purpose, and Politics in Organized Medicine, 63 YALE L.J. 937 (1954); Note, supra note 75, at 1182.

79 See notes 55-60 and accompanying text supra.

80 See Comment, supra note 76, at 1164.

81 See Reiger, The View from HEW on Federal Involvement in the Malpractice Situation, J. LEGAL MED., June 1975, at 19 (reporting HEW official's estimate of $2-7 billion per year in the use of defensive medicine); Wolfe, The Real Victim, TRIAL, May/June 1975, at 26, 30.
power to transfer accident costs are rather negligible in both professions. This is particularly true for professional corporations, because they appear to be composed of wealthier professionals who probably possess greater than average market power. Some less wealthy, uninsured professionals with little market power undoubtedly form professional corporations sometimes motivated by the prospect of limiting their liability despite the unavailability of the tax advantages which usually prompt incorporation. Although the prevalence of wealth, insurance, and market power among professionals presently restricts the size of this class rather severely, it is the only one upon which joint and several liability is likely to have a significant effect. Statistically, shareholders in this class clearly risk personal liability unless they react to market incentives by acting more safely in their employee capacity. Analysis of the impact of consumer and professional ignorance, and other primary distortion to the market, suggests, however, that joint and several liability incentives will be inefficient even in this situation.  

b. Ignorance—In order to convert market incentives efficiently into fewer accidents, those faced with the incentives must know, at a relatively low cost, the risks and costs of injuries and negligence as well as the methods and costs of reducing them. Consumers of professional services are typically ignorant of the

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It has also been argued that defensive medicine does not exist. See Brook, Brutoco & Williams, supra note 35, at 1218, 1220. As argued in Mechanic, Some Social Aspects of the Medical Malpractice Dilemma, 1975 DUKE L.J. 1179, 1189-92, the conflict in opinion is probably largely due to the concomitance of the definition of defensive medicine in terms of medically unjustifiable procedures and the absence of agreement as to what procedures are justifiable. In the absence of agreement, defensive medicine becomes a function of subjective intent, and it is known that many physicians admit to engaging in what they view as defensive medicine. See Bernzweig, Defensive Medicine, in APPENDIX, supra note 40, at 38. Even if the amount of defensive medicine is only $1 billion per year, the low end of the estimates, it equals the total amount of health care provider professional liability insurance premiums paid in 1975. See Steves, supra note 42, at 1317 n.59. In other words, physicians appear to be able to pass on not only the cost of their insurance but also an equivalent amount of unnecessary costs to avoid having to pay more for insurance.

See note 42 supra.

More than 80 percent carry professional liability insurance. See note 40 supra. It is likely that a fair number of the uninsured have substantial wealth and market power because the income of incorporated physicians is higher than the national average. See note 42 supra.

If it is assumed that such employees earn half of the average income and that the corporation has no liquid assets, the fund generated in a physician professional corporation according to the sources in note 42 supra would be $30,000, whereas the likelihood of liability greater than $30,000 in a corporation of five professional employees would be about 8 percent in 1976. In addition, the smaller chances of very large liability become more important as the available assets dwindle. Although, outside the health care professions, those who are not wealthy and have little market power are less likely to render services in matters where large sums of money are at stake, these practitioners may also be more likely to cut corners. Cf. Note, supra note 73 (discussing problems of solo practitioners).

See notes 86-102 and accompanying text infra.
risk of injury and even more ignorant of the subsidiary risk that negligence, whether their own or the professional’s, will cause the injury. One of the chief sources of consumer ignorance is the nature of the professional relationship. Those receiving professional services typically surrender their judgment to the professional’s diagnosis, recommendation, and treatment, thereby becoming highly dependent. Partially because the professional often fails to reciprocate by admitting relative incompetence in a specific area or explaining the assessment of the problem and risks of various types of treatment, the consumer’s dependency may become so total as to culminate in somewhat of a psychological paralysis.

Another important source of consumer ignorance is the disorganized way in which professional services are purchased. In theory the personal fault system lends itself to reliable generalizations on the basis of the myriad case-by-case determinations of the proper standard of conduct. These generalizations could be used by consumers to avoid risky procedures and incompetent professionals and to pressure professionals for safer procedures. But consumers have never organized in such a way so as to collect this information. Rather, they continue to rely almost entirely on the professional’s judgment.

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86 See Havighurst & Tancredi, “Medical Adversity Insurance” — A No-Fault Approach to Medical Malpractice and Quality Assurance, 1974 Ins. L.J. 69, 73; Mechanic, supra note 81, at 1186-87; Peterson, Consumers’ Knowledge of and Attitudes Toward Medical Malpractice, in APPENDIX, supra note 40, at 658. Most individuals would be shocked to discover that they face nearly a 10 percent chance of sustaining injury each time they are admitted to a hospital and that about 30 percent of those injuries are due to the negligence of the health care provider. That only 6 percent of those negligently injured file a claim of any sort suggests that ignorance prevails. See Pocincki, Dogger & Schwartz, The Incidence of Iatrogenic Injuries, in APPENDIX, supra note 40, at 50. Few individuals are aware that 50 percent of the legal malpractice awards involve the simple failure by the lawyer to file suit or papers within the applicable statute of limitations or court-imposed deadline. See Legal Malpractice, supra note 40, at 599 n.41. Unsophisticated investors are unable to judge the adequacy of accountants’ work on corporate financial statements.

87 See Lave & Lave, supra note 62, at 742; Comment, supra note 34, at 645.


89 See Wolfe, supra note 81, at 27.

90 This paralytic dependency on the professional’s judgment may be illustrated by the case of the steelworker with a broken leg who, told to report back to the hospital in four days for an examination of the cast and further x-rays, lost his leg because he failed to report back earlier even though the foot became blue. See Wecht, Medicine: A Commercial Enterprise?, TRIAL, May/June 1975, at 39, 40.

91 Primary Accident Costs, supra note 24, at 442-44. The extent of ignorance about whether either party has been negligent may also be judged from the fact that the immense costs of administering this case-by-case system, see Brook, Brutoco & Williams, supra note 35, at 1208 (less than 20 percent of each premium dollar returned to patient who has won a claim), stem largely from the cost of discovering whether the conduct of either party caused the accident or was substandard. See Dietz, Baird & Berul, The Medical Malpractice Legal System, in APPENDIX, supra note 40, at 101, 154; Keeton, Compensation for Medical Accidents, 121 U. Pa. L. Rev. 590, 594 (1973); Legal Malpractice, supra note 40, at 593.

92 See Kessel, supra note 77, at 281, 285, 289; Legal Malpractice, supra note 40, at 594; cf. note 158 infra (substantial amount of unnecessary surgery).
The substantial lack of knowledge of the causes and costs of professional accidents that plagues professionals themselves underlies consumer ignorance and also forms an independent obstruction to accident minimization through market incentives. Despite extensive training and the use of sophisticated technology and procedures, most professional judgments are inherently imprecise. Overcoming imprecision creates additional complexity in professional skills, which in turn increases the difficulty of satisfying legal standards of sound practice. This is particularly true in medicine, where the development of powerful drugs and new surgical techniques with low tolerance for error has increased the potential efficacy of medical treatment as well as the risks of additional injury. This complexity and instability makes identification of risks and utilization of safety techniques more costly and may render collective attempts at detailed standard setting impracticable even at excessive costs. The atomistic organizational structure of the professions and the absence of economic incentives to minimize accident costs further inhibits compilation of the data necessary to identify precisely the nature and actuarial costs of risks and development of appropriate accident minimization.

93 See Bernzweig, Getting to the Root of the Problem, TRIAL, May/June 1975, at 58, 59; Brook, Brutoco & Williams, supra note 35, at 1209; Havighurst & Tancredi, supra note 86, at 94; Mechanic, supra note 81, at 1181; Comment, supra note 34, at 631.


95 See Brook, Brutoco & Williams, supra note 35, at 1209; Mechanic, supra note 81, at 1181-82.

96 See Havighurst & Tancredi, supra note 86, at 94.

97 Lawyers and accountants practice in firms more frequently than other professionals. Nonetheless, nearly half the nation's attorneys practice alone. STATISTICAL ABSTRACT, supra note 42, at 163. Law partnerships average five practicing attorneys. Id. In Michigan there were in 1974 only twenty-one firms with more than twenty active lawyers. 3 MARTINDALE-HUBBELL LAW DIRECTORY (1975 ed.), despite the fact that the state had roughly 8,000 practicing lawyers. STATISTICAL ABSTRACT, supra note 42, at 162. In 1970 only 15 percent of the nation's physicians practiced as members of a medical group. Carlson, supra note 56, at 854, 856 n.24, 861.

98 See notes 40-84 and accompanying text supra.

99 Professionals do come into contact with organizations—such as professional schools, insurers, licensing boards, professional associations at city, county, state, and national levels, hospitals, and courts—of sufficient size and number to allow compilation of the necessary data base. But usually these contacts are tenuous, or the organization has little interest in minimizing accidents. Thus, insurers have not gathered comprehensive accident data on malpractice claims. Wolfe, supra note 81, at 30; Legal Malpractice, supra note 40, at 590, 598-99. See Reiger, Resolution Sought for Malpractice Crisis, J. LEGAL MED., June 1975, at 35, 36. Courts and regulatory bodies are interested almost exclusively in licensing and discipline. REPORT, supra note 12, at 51-52; Wolfe, supra, at 27; Legal Malpractice, supra note 40, at 595. Professional trade organizations have typically concentrated their efforts on improving the social and financial status of their memberships rather than on collecting information necessary to reduce unnecessary losses associated with their members' services. See notes 83-86 and 91 and accompanying text infra; REPORT, supra, at 51-52; Legal Malpractice, supra, at 595. But see Kendall & Haldi, The Medical Malpractice Insurance Market, in APPENDIX, supra note 50, at 545-46; Legal Malpractice, supra note 40, at 608 n.82.
tion techniques. Further, the minimal correlation between the negligent act and the amount of injury may prevent development of techniques for selectively avoiding the most severe injuries, which are the only ones capable of providing professionals with significant market deterrent incentives.

One of the great problems with respect to joint and several liability is that those subject to its additional incentives are no more capable of overcoming the existing ignorance about professional accidents than are those not subject to joint and several liability. As a result, jointly and severally liable shareholders are restricted to more effective application of present knowledge instead of being able to use their financial incentives to develop new knowledge. This may reduce the number and severity of accidents somewhat, but it can hardly be commensurate with the additional incentives placed upon them. The extreme inefficiency of market incentives in the professional context appears to assure that even those shareholders whose employees and corporations have few assets and little market power are unable to utilize market incentives with any efficiency to reduce the number and severity of professional accidents. Consequently, the additional accident minimization to be gained by use of joint and several liability is negligible in all but a few instances.

B. Minimizing the Social Costs of Accidents

Although accident costs are in the first instance borne by those involved, they are often spread to society through loss of work and

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100 See Roemer, supra note 77, at 289, 295. The organizations with which professionals do come into contact have failed to be concerned adequately with reducing accidents. REPORT, supra note 12, at 51-52; Brook, Brutoco & Williams, supra note 35, at 1215-17; Havighurst & Tancredi, supra note 86, at 96; Leiser, Hospital Administrators: Passing Muster?, TRIAL, May/June 1975, at 42; Mechanic, supra note 55, at 235-36; Parker, Periodic Recertification of Lawyers: A Comparative Study of Programs for Maintaining Professional Competence, 1974 UTAH L. REV. 463, 464, 467; Roemer, supra note 77, at 289-90, 294; Warren, The Discipline of Physicians, J. LEGAL MED., Sept./Oct. 1974, at 23, 26; Wolfe, supra note 81, at 27; Note, Legal Specialization and Certification, 61 VA. L. REV. 434, 435 (1975); Legal Malpractice, supra note 40, at 595.


101 See Mechanic, supra note 81, at 1181.

102 Usually, the shareholders are also the employees. See note 37 supra. The inefficiency of joint and several liability does not mean that no reduction in the level of accidents occurs as a result of its imposition. But efficiency is so low that the incentives may not be worth imposing if accident minimization is the only goal to be achieved thereby. Of course, joint and several liability may be more useful to other goals, such as minimizing the social costs of accidents after they occur. See note 111 and accompanying text infra.
reliance upon social welfare programs. The reduction of these societal costs forms Calabresi's second subgoal. He identifies two methods of achieving this objective. One, loss spreading, is based upon the assumption that accident costs will be less burdensome on individuals if spread among people and over time. This is accomplished primarily through public and private casualty and liability insurance. The second method, called "the deep pocket" by Calabresi, utilizes the further assumption that accident costs become less burdensome to society when assumed by those least likely to suffer painful economic or social dislocation from the imposition of those costs and depends for its realization upon mechanisms such as enterprise liability and the progressive income tax.

1. Conceptual Superiority of Joint and Several Liability—The personal fault system does not seek to minimize the social costs of accidents. It demonstrates this blindness to minimizing the overall burden by holding negligent defendants liable or leaving the costs on plaintiffs when negligence is not proved, without consideration of the relative economic position of either party. On the other hand, joint and several liability, as well as limited liability, does tend to diminish the likelihood of social and economic dislocation to injurer and injured alike by spreading the loss to additional payment sources and increasing the fund available for compensating the injured individual. The larger fund minimizes the victim's dislocation, while the spreading of the loss to additional sources reduces the burden on the injurer. In any given professional corporation joint and several liability creates a broader asset base and a larger potential fund than that available with limited liability. Consequently, it is in theory the superior minimizer of dislocation to both injurers and injured and hence of societal accident costs as well.

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104 Accident Costs, supra note 24, at 27, 39.
105 Id. at 39-40, 46-49.
106 Id. at 40.
107 Id. at 53-54.
108 In practice the personal fault system rarely operates by itself. Usually it operates in conjunction with the loss spreading devices of casualty and liability insurance. Accident Costs, supra note 24, at 24-26, 289-309. For conceptualization of the problems dealt with here, however, the personal fault system must be considered separately from its adjuncts.
109 See Optimal Deterrence, supra note 24, at 657.
110 In this context loss spreading combines with the deep-pocket method. Professional corporations are likely both to have assets sufficient to avoid dislocation if the loss is placed upon them (deep pocket) and to be able to spread the losses among the consumers of their services.
2. Practical Superiority of Joint and Several Liability—In practice the superiority of joint and several liability over limited liability as a method of minimizing the social costs of accidents varies with the adequacy of the assets of the corporation and the professional actually at fault. Where these assets are sufficient to satisfy any foreseeable tort awards, the two types of liability are virtually indistinguishable since the additional asset base and larger potential fund of joint and several liability need not be utilized. But where these assets are insufficient, joint and several liability is superior because it produces a greater fund for the victim while spreading the source of the funds in order to reduce dislocation to the injurer.

With respect to the goal of minimizing social costs, the likelihood that the combined assets of the negligent employee and corporation will be insufficient is quite small. But the use of joint and several liability to minimize social costs in these rare cases is more easily justified than its use to minimize the number and severity of accidents because in the latter situation the incentives of joint and several liability are largely dissipated by ignorance of how to use them, whereas no such inefficiencies occur in the minimization of social costs.

C. Choosing the Optimal Method of Minimizing Accidents and Their Social Costs

Optimization involves a cost-benefit analysis aimed at achieving the greatest reduction in accidents and in their social costs at the lowest possible administrative cost. This analysis is difficult because the subgoals of deterrence and cost spreading conflict with each other as do the two methods of deterrence. Often the only practical method of optimizing costs is delegation, the allocation of costs to that class of persons most likely to reach the optimal distribution in the marketplace.

111 Indeed, the likelihood is no greater than that with respect to minimizing the number and severity of accidents. See notes 42, 45, 70-72, 80-82, 85 and accompanying text supra.
112 ACCIDENT COSTS, supra note 24, at 28.
113 Id. at 29, 93, 131-34; PRIMARY ACCIDENT COSTS, supra note 24, at 436-38.
114 PRIMARY ACCIDENT COSTS, supra note 24, at 438. Calabresi develops three cumulative criteria for making a sound delegation. ACCIDENT COSTS, supra note 24, at 143-52; PRIMARY ACCIDENT COSTS, supra note 24, at 439-40. The first criterion involves finding the optimal cost-benefit relationship between accident avoidance costs and administrative costs. For instance, if the cost of discovering that hospitals could avoid surgical accidents most cheaply would greatly exceed the cost of the additional accidents that would occur from leaving the avoidance incentives on physicians in general, the first criterion would suggest leaving the incentives with the less efficient but ultimately less costly physicians. The second criterion is avoiding a delegation to a class that can have little impact on reducing those accidents unless it is so much cheaper administratively to put the incentive on that class that it
Determining the optimal method of reducing the costs of accidents arising from the rendition of professional services is beyond the scope of this note.\textsuperscript{115} Here the inquiry is confined to the relative optimality of limited liability and joint and several liability. Joint and several liability appears to be optimal where the assets of the corporation and the professional at fault are clearly inadequate to meet anticipatable accident costs. In this situation the clear and important gains in reducing social costs\textsuperscript{116} more than counterbalance the inefficiency of joint and several liability in reducing the number and severity of accidents.\textsuperscript{117} But where assets are adequate, limited liability appears to be comparatively optimal because accidents and social costs are minimized efficiently without the wasteful psychological fear that may exist in joint and several liability situations. This shift in optimality from one type of liability to the other depending on the adequacy of the assets suggests that the third alternative model solution, which utilizes each given concept of liability where optimal, rather than a single concept exclusively, would be the optimal solution for all professional corporations.

\textbf{D. Fairness}

In applying Calabresi's schema to professional accidents, fairness may be viewed as a reasonable balance between the conflicting social goals of minimizing accidents and encouraging necessary and beneficial professional activities.\textsuperscript{118} Although Calabresi has used the concept of fairness primarily to demonstrate the unfairness of the whole personal fault and loss spreading system that dominates American accident law,\textsuperscript{119} fairness may also be used in a more limited, comparative manner to aid choosing between alternative elements within an existing accident law system. In this context the optimal model solution (the third alternative) would also be sufficiently fair if no overriding claim can be presented by the victim class for exclusive use of the additional safeguards of becoming the least expensive way despite the consequent inefficiency in accident reduction. Putting the costs of surgical accidents on farmers would be an example of this inoptimality, which Calabresi calls externalization. The third criterion requires delegation to the class most likely to be able to make bargains in the marketplace to correct mistakes in delegation.\textsuperscript{115} It is clear, however, that absolute optimality would require a fundamental restructuring of the market for professional services or much greater reliance upon collective regulation. \textit{See notes 164-171 and accompanying text infra.}

\textsuperscript{115} \textit{See Accident Costs, supra note 24, at 44; Fleming, supra note 37, at 824-25; James, supra note 37, at 558.}

\textsuperscript{116} \textit{See supra note 24.}

\textsuperscript{117} \textit{See note 27 and accompanying text supra.}

\textsuperscript{118} \textit{See sources cited in note 24 supra.}
joint and several liability or by the injurer class for the additional protection available to them through limited liability.

1. Joint and Several Liability—The argument for the greater fairness of joint and several liability rests on the belief that the public needs special protection from exposure to professional incompetence and imposition. Special protection has taken many forms including licensing requirements, regulatory boards, judicial and legislative prohibitions of professional corporations, and the development of a wide range of tort doctrines.

The public protection approach has severe limitations. Outside of the health care sector, the vast majority of professional service consumers are commercial clients in a position to judge the quality of services performed. In addition, since few physicians and barely half of the nation’s attorneys practice in firms, joint and several liability can affect only a small proportion of professionals. The widespread ignorance among professionals concerning the causes of accidents and the appropriate methods of reducing accidents contributes to the diversion of attention from reducing accidents to avoiding liability, thereby further diminishing the potential effectiveness of joint and several liability.

A more fundamental weakness in the public protection argument arises from the fact that joint and several liability fails to offer greater protection wherever the assets of a firm are sufficient to meet anticipatable accident costs. Since professional corporations normally have adequate assets in the form of liability insur-

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120 See note 7 and accompanying text supra.
121 Barron, supra note 73, at 643-44; Graves, Professional and Occupational Restrictions, 13 Temple L.Q. 334 (1939).
122 In addition to administering mandatory licensing systems, regulatory boards also oversee entrance requirements, standards of ethical conduct and disciplinary charges and hearings. See, e.g., Ky. Rev. Stat. Ann. §§ 317.400, .590 (1971). For a variety of reasons, these boards have been ineffective in improving performance. See Report, supra note 12, at 51-60; Brook, Brutoco & Williams, supra note 35, at 1215-17; Havighurst & Tancredi, supra note 86, at 96; Warren, supra note 100, at 26.
123 See note 2 and accompanying text supra.
124 Several doctrines easing the plaintiff’s case such as informed consent, res ipsa loquitur, and postponement of the statute of limitations, have been liberally applied against physicians. See Report, supra note 12, at 27-33; Dietz, Baird & Berul, supra note 91, at 122-52; Kessel, supra note 77, at 280; Kroll, The Etiology, Plus and Prognosis of Medical Malpractice, 8 Suffolk L. Rev. 598, 607-20 (1974); Roddis & Stewart, supra note 37, at 1299-1300. Architects, engineers, and accountants have lost the defense that formerly restricted liability exclusively to those with whom they had had a contractual relationship. See Gormly, Accountants’ Professional Liability—A Ten-Year Review, 29 Bus. Law 1205 (1974); Comment, Recent Statutory Developments Concerning the Limitation of Actions Against Architects, Engineers, and Builders, 60 Ky. L.J. 462 (1972). The exposure of lawyers is discussed in Comment, supra note 34, at 635-45.
125 See note 97 supra.
126 Id.
127 See notes 93-101 and accompanying text supra.
128 See note 39 and accompanying text supra.
ance, fairness does not require exclusive use of joint and several liability. Further, the phenomenon of defensive medicine may actually be producing a retrograde effect which the exclusive use of joint and several liability would fuel.\textsuperscript{129}

2. Limited Liability—The argument for the exclusive use of limited liability for professional corporations rests on two grounds. The first is that professional corporations are entitled to the same advantages afforded other corporations. However, not all shareholders of all other corporations have limited liability for all purposes.\textsuperscript{130} More importantly, limited liability is a legislative creation\textsuperscript{131} designed to stimulate the passive investment necessary for rapid industrialization and commercial growth.\textsuperscript{132} Professional corporations fail to produce these benefits, however, because passive investment in professional corporations is both impractical\textsuperscript{133} and severely restricted as a matter of law\textsuperscript{134} and because professional corporations are created not to foster commercial growth but to minimize taxes.\textsuperscript{135} Finally, where contractual debt far exceeds potential tort liabilities, as was true of the original beneficiaries of limited liability, limited liability is far less significant than it is in professional corporations, where potential tort liabilities far exceed contractual debt. This is because potential contract creditors can easily circumvent limited liability by requiring personal

\textsuperscript{129} This effect would occur if, as has probably happened, the addition of one dollar of liability would spawn greater than one dollar of additional cost for defensive medicine. See note 81 supra.

\textsuperscript{130} See N.Y. BUS. CORP. LAW § 630 (McKinney 1963).

\textsuperscript{131} At common law no organization is entitled to limited liability. See Comment, The Validity of Limited Tort Liability for Shareholders in Close Corporations, 23 AM. U.L. REV. 208, 210 (1973) [hereinafter cited as Limited Tort Liability]. Until 1930 the shareholders of California corporations were subject to joint and several liability. Comment, Inadequate Capitalization as a Basis for Shareholder Liability: The California Approach and a Recommendation, 45 SO. CALIF. L. REV. 823, 832 (1972) [hereinafter cited as Inadequate Capitalization].

\textsuperscript{132} Limited Tort Liability, supra note 131, at 212; Inadequate Capitalization, supra note 131, at 833.

\textsuperscript{133} The capital requirements of most professional corporations are so low and the proportion of income from services so high that an equity investment in a professional corporation would earn almost nothing. Indeed, since the primary motivation for forming professional corporations was to secure more favorable tax treatment, see note 8 and accompanying text supra, the directors of a professional corporation would seek to minimize the amount of the corporation’s net income dividends payable.

Professional corporations are not materially different from many other close corporations with respect to passive investment because close corporation financing agreements are frequently conditioned on consent by the principal shareholders to become personally liable for the debt, W. CARY, CORPORATIONS 22-23 (1969). The proper solution, however, is not limited liability for all but greater exposure to tort liability on the part of shareholders in all close corporations, as both courts and commentators have suggested. See Walkovszky v. Carlton, 18 N.Y.2d 414, 420, 223 N.E.2d 6, 9, 276 N.Y.S.2d 585, 589-90 (1966); Inadequate Capitalization, supra note 131, at 830; Comment, Should Shareholders Be Personally Liable for the Torts of Their Corporations, 76 YALE L.J. 1190, 1196 (1967).

\textsuperscript{134} See note 6(2) supra.

\textsuperscript{135} See note 8 and accompanying text supra.
guarantees from shareholders on financing agreements, whereas potential tort victims cannot plan ahead to secure a waiver of limited liability. 136

The second argument for exclusive use of limited liability is that it would help decrease the present socially harmful overexposure of professionals to tort liability. 137 Professionals have in recent years witnessed a dramatic increase in potential tort liability as a result of the greater frequency and severity of claims, and the expanding catalogue of legal bases for such claims. 138 The magnitude of this increase is most evident in the medical profession, where between 1960 and 1974 medical malpractice insurance costs increased fifteen times as quickly as the substantial rise in health care costs 139 and where the cost of liability insurance is estimated to have reached $2 billion in 1976. 140 Increased exposure has in some respects harmed the relationship between health care providers and their patients. 141 The substantial losses of scarce medical services due to the time requirements of defending against claims have disrupted the health care delivery system, 142 while the use of defensive medicine has appreciably increased the costs of medical care without any corresponding medical benefits. 143

Professionals have used this argument successfully in winning legislative atrophication of the basis of liability 144 and claim sever-

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136 See Limited Tort Liability, supra note 131, at 208 n.3.
137 Advocates of reduced liability for health care providers point to two types of social harm. The first is that extremely large tort recoveries by a small minority of health care consumers excessively increase the cost of medical care to all consumers. See Hoffman, supra note 12, at 123; Linster, supra note 42, at 103; Perr, The Great JAILer Conspiracy—Malpractice, Torts, and the Middle Class, J. LEGAL MED., March 1976, at 16. The second is that overexposure to liability disrupts the trust and good will that must exist between the professional and the patient and therefore damages the quality of health care. See Hoffman, supra note 12, at 123; Keeton, supra note 91, at 598-600.
138 See Steves, supra note 42, at 1312-19; note 124 supra.
139 In 1970 the average premium rates for physicians other than surgeons stood at 540 percent of a 1960 base; for surgeons the figure was 940 percent. REPORT, supra note 12, at 13. This is an annual rate of increase of nearly 20 percent for both categories combined. Since 1970 these costs have been estimated to be rising at an annual rate of over 23 percent. See Steves, supra note 42, at 1316. Linear extrapolation through 1974 yields an increase of 1400 percent over the 1960 base, almost fifteen times the 95 percent increase in the cost of health care between 1960 and 1974. See STATISTICAL ABSTRACT, supra note 42, at 71.
140 Steves, supra note 42, at 1317 n.59.
141 See, e.g., REPORT, supra note 12, at 19; Havighurst & Tancredi, supra note 86, at 95; Hoffman, supra note 12, at 123. But cf. Brook, Brutoco & Williams, supra note 35, at 1221 (noting that changing social attitudes may be more important factors than malpractice litigation).
143 See note 81 and accompanying text supra.
144 Comment, An Analysis of State Legislative Responses to the Medical Malpractice Crisis, 1975 DUKE L.J. 1417. Legislatures have shortened statutes of limitations and modified exceptions to them. id. at 1429-36. They have also restricted the doctrines of informed consent. id. at 1436-42, and res ipsa loquitur, id. at 1426-29.
However, using joint and several liability to force one professional to assume part of another professional's liability has nothing to do with the amount of liability imposed, the reason for imposing it, or the likelihood that a claim will be made. It also has little to do with the use of medically unjustified procedures to avoid claims and liability. Consequently, elimination of joint and several liability among shareholders of professional corporations would have no meaningful impact on the exposure of professionals to liability. Even if such a result were possible, the societal goal of adequate compensation to those tortiously injured while receiving professional services would counsel strongly against exclusive use of limited liability in professional corporations.

Inasmuch as neither joint and several liability nor limited liability presents an overriding claim to being more fair in all situations, the amalgamation alternative of the model solution appears to be both optimal and fair. It is preferable to the exclusive use of either of the traditional types of shareholder liability. Indeed, its preservation of each type of liability in the circumstances in which it serves the two policies of encouraging professional activities and preventing and compensating injuries from those activities suggests that the model's utilization of three alternatives is an unnecessary deviation from the goal of greater uniformity aimed at by model legislation.

III. PROFESSIONAL CORPORATIONS AND PROFESSIONAL LIABILITY

Adoption of the third alternative model solution would have the salutary effect of foreclosing avoidance of liability as a motive for professional incorporation. But the relative rarity of corporate or shareholder liability assures that neither the model solution nor any existing shareholder liability provision can have any substantial impact upon the malpractice crises. Elimination of these crises in a fair manner might be aided, however, by modification of the professional corporation form. Indeed, the confluence of three factors—the decreasing usefulness of the professional corporation for tax and organizational purposes, the growing realization that the personal fault system is an extremely inefficient and inappropriate

145 Modifications include specific dollar limitations on total recovery by the claimant, id. at 1418-25, reduction in maximum contingent fee percentages, id. at 1442-47, requirements for reducing the award by the amount of collateral payments, id. at 1447-50, and elimination of ad damnum clauses in litigated complaints, id. at 1451-53.
method of minimizing professional accidents and compensating their victims, and the availability of serious proposals to alter the personal fault system in the context of professional accidents—suggests that the professional corporation may be an attractive vehicle for wide-ranging state experimentation with alternative professional accident law systems.

As noted earlier, professional corporations were originally formed and have been used primarily to gain the tax advantages given to corporations by the federal government. In recent years, however, these advantages have diminished, and future reform is likely to further reduce the tax differences between corporations and partnerships. Adoption of the third alternative model solution with respect to shareholder liability would also remove the socially undesirable use of incorporation as a technique for avoiding liability. Inasmuch as the professional corporation form may actually hinder the flexible operating structure desirable in professional practices, diminution of the nonorganizational benefits of incorporation has increasingly made the professional corporation a form without function. The corporate form is a vehicle of legislative policy and should be adaptable to new purposes if the professional corporation form no longer serves its original objective.

The inability of the personal fault system to deter professional negligence and compensate its victims has been demonstrated with particular persuasiveness in the area of medical accidents. The percentage of each dollar of professional liability insurance premium reaching successful medical malpractice claimants is lower than in any other area of personal injury litigation. Many claims

146 See note 8 and accompanying text supra.
147 See note 13 and accompanying text supra. Some courts have held that partners qualify as employees for purposes of employee deductions, thereby substantially reducing the differences between corporations and partnerships. See, e.g., Armstrong v. Phinney, 394 F.2d 661 (5th Cir. 1968) (finding that a five percent partner serving as resident manager of partnership’s ranch operation was an employee for purposes of I.R.C. § 119 deduction for value of meals and lodging supplied by the partnership and noting that the result would be the same under § 707(c) by virtue of its incorporation of § 61, which incorporates § 119).
148 A partnership agreement may be designed to secure as much centralization of management as exists in a corporation. See Brand v. Elledge, 101 Ariz. 352, 419 P.2d 331 (1966); Potter v. Brown, 328 Pa. 554, 195 A. 901 (1938); Frost, Some Comments as to Professional Corporation Statutes, 4 ARIZ. L. REV. 169, 170 (1963). Most states impose restrictions on professional corporations concerning multi-state practice, see note 6(4) supra, to which partnerships are not subject because they are treated as an aggregate of individuals. Further, the professional independence required by professional ethics laws and explicitly preserved by the various professional corporation acts may prohibit professionals from making full use of corporate management structures. See Note, supra note 7, at 781-82.
149 See REPORT, supra note 12, at 100; Havighurst, supra note 142, at 1234-36; Keeton, supra note 91.
150 REPORT, supra note 12, at 100; Brook, Brutoco & Williams, supra note 35, at 1208 (citing figure of 18-20 percent). Lawyers handling medical malpractice claims have estimated that these claims require about four times as many hours as other personal injury cases. Dietz, Baird & Berul, supra note 91, at 101.
never receive an adequate hearing because proper advocacy would cost more than the claim is worth or because evidentiary problems exist.\textsuperscript{151} Claims are never filed for hundreds of thousands of negligent incidents per year.\textsuperscript{152} Litigation is abrasive, produces economically and medically wasteful procedures, interruptions, and antagonisms, and utilizes a rather vague and unscientific standard of liability which produces arbitrary results.\textsuperscript{153} Further, its financial incentives to achieve greater safety are sloughed off by physicians and dissipated by patients.\textsuperscript{154}

Each proposal to modify substantially the personal fault system attempts to rationalize the compensation system by predicting compensation on an adverse result or an iatrogenic injury\textsuperscript{155} alone rather than on an iatrogenic injury plus the capricious causal element of negligence. The plan supported by the American Medical Association achieves this improvement by mandating that all employers carry medical accident casualty insurance for their employees.\textsuperscript{156} Because this plan is designed to remove all market and collective forms of minimizing accidents,\textsuperscript{157} it would only be worthy of consideration in the unlikely event that medical accident rates could not be diminished.\textsuperscript{158} The Inouye-Kennedy proposal\textsuperscript{159} counterbalances the externalization of accident costs to a national insurance pool by imposing regulatory quality controls on participating physicians.\textsuperscript{160}

\begin{footnotes}
\item[151] See Dietz, Baird & Berul, supra note 91, at 153; Keeton, supra note 91, at 596.
\item[152] See Steves, supra note 42, at 1308-12; compare Statistical Abstract, supra note 42, at 80, 83, with Pocincki, Dogger & Schwartz, supra note 86, at 50.
\item[153] See Havighurst, supra note 142, at 1234-35; Hoffman, supra note 12, at 122-24; Mechanic, supra note 81, at 1188; Steves, supra note 42, at 1300. Hoffman’s criticism that the tort system is being applied much more harshly to physicians than other professionals appears to be justified, especially in light of the self-serving and primitive requirement in legal malpractice litigation that injury can only be proved by establishing that the plaintiff’s action or defense would have succeeded if the attorney had not been negligent. See Legal Malpractice, supra note 40, at 593.
\item[154] See notes 49-102 and accompanying text supra; cf. Brook, Brutoco & Williams, supra note 35, at 1220-22 (asserting that the threat of a malpractice claim has a minimal impact on improvement of performance); Havighurst, supra note 142, at 1243 (statement by Senator Inouye that physicians practice good medicine in spite of malpractice threats).
\item[155] Iatrogenic injuries are those produced inadvertently by the physician or treatment. See Pocincki, Dogger & Schwartz, supra note 86, at 51.
\item[156] See Havighurst, supra note 142, at 1241, 1243-44.
\item[157] Externalizing compensation costs by placing them on the victims’ employers eliminates market incentives because employers, who would enjoy tax deductions for the cost of the plan, are no more likely to press for cost control than they are under current medical casualty insurance plans which are deductible fringe benefits; it eliminates collective deterrence because employers, unlike the government, are unable to regulate physicians. See Havighurst, supra note 142, at 1243-44.
\item[158] Accidental injury due to the substantial amount of unnecessary surgery fostered by the fee-for-service system of health care, see Mechanic, supra note 55, at 245; Steves, supra note 42, at 1310, is one area where fairly quick gains in accident reduction could be made. Serum hepatitis from blood transfusions appears to be another such area. See Kessel, supra note 77; Steves, supra note 42, at 1309 n.19.
\item[160] Id. §§ 1704, 1731 (federalization of health care professional licensing and renewals).
\end{footnotes}
In contrast to this trade-off of reduced market for greater collective incentives, Professor Clark Havighurst proposes to increase market incentives while, if necessary, decreasing collective regulation. In his proposal health care providers automatically compensate patients for any of a limited list of specific adverse outcomes with a liability insurance program that utilizes extensive individual experience rating and deductible or co-insurance features in order to strengthen market incentives to avoid medical accidents. The additional costs of compensating a higher percentage of victims are expected to be covered by savings resulting from elimination of the administrative costs of determining fault. An independent variation of this plan devised by Professor Jeffrey O’Connell may affect but does not explicitly consider the problem of deterrence; it envisages voluntary contractual arrangements between physicians and patients in which both parties give up recourse to litigation in favor of no-fault compensation of specified adverse outcomes.

There are severe problems with both the collective and market approaches to minimizing professional accidents. The extensive political power of physicians and other health care providers and their longstanding opposition to governmental and internal regulation make it unlikely that new regulations will be strong enough to reduce accident rates substantially. Certainly, regulations recently imposed by some states as trade-offs for alleviation of the liability insurance crisis have been rather innocuous. Governmental regulation of professional activities almost invariably controls the inputs and processes rather than the outcomes of professional services delivery. Input and process controls, however, are difficult and expensive to apply and modify. Further,
their incompatibility with the historical professional desire for independence may produce a mentality of formal compliance without the desired byproduct of better performance.\textsuperscript{169}

On the other hand, the substantial market power of professionals that has been traced by this note suggests that combinations of individualized experience rating and deductibles or co-insurance would have to be very expensive, perhaps unrealistically so, to produce sufficient incentives among professionals to avoid accidents.\textsuperscript{170} This will continue to be true so long as the federal tax structure permits professionals to deduct liability insurance premiums and tort liability expenses.\textsuperscript{171} And if adverse outcomes prove to be unavoidable without large-scale changes in the technology and art of professional care, nontransferable market incentives might be a merely punitive measure devoid of social benefit.

Because professional corporation status is voluntary, any modification of the personal fault system would have to be made palatable enough to retain a professional corporation population sufficient for use in gauging the modification's success. Havighurst seeks to achieve acceptability by avoiding the abrasive waste of litigation, removing the emphasis on process in personal fault litigation, and reducing collective controls;\textsuperscript{172} the Inouye-Kennedy approach prefers reducing market incentives.\textsuperscript{173} Since neither proposal is likely to reduce the number of accidents without controls or incentives that are significantly greater than at present, the favorable trade-off may remain unachievable. The suitability of a voluntary mode of experimentation, as in the professional corporation, is also open to question in light of the probability that market deterrence alternatives would attract primarily those who thought they stood to gain from extensive experience rating because of their lower than average accident cost experience, while collective deterrence alternatives would attract primarily those whose unfortunate accident experience suggested that avoidance of all accident costs would be desirable. Such a phenomenon would detract from the validity of any conclusions drawn from the control group.

Nevertheless, experimentation remains imperative if the goals of equitably minimizing accidents and their social costs are to be

\textsuperscript{169} See notes 164-65 and accompanying text \textit{supra}.

\textsuperscript{170} See notes 54, 73-82 and accompanying text \textit{supra}. Potentially, a countervailing monopsony would be necessary to internalize accident costs. But this is not achievable with respect to professional corporations alone and therefore cannot be used to achieve internalization at politically acceptable levels of individualization.

\textsuperscript{171} See Havighurst, \textit{supra} note 142, at 1250 n.50. \textit{Cf. id.} at 1240 (noting that third-party payments make the practice of defensive medicine easier).

\textsuperscript{172} \textit{Id.} at 1238-40, 1249-50, 1267, 1278 n.133.

served. The professional corporation thus remains a fairly attractive vehicle for experimentation. Because the form is malleable and less useful to professionals than previously, little would be lost by requiring acceptance of an alternative accident law system as a condition of gaining or retaining professional corporation status. Because professional corporations account for a small percentage of professional services rendered, the relative merits of competing and problematical systems could be gauged in advance of any large-scale commitment. Because professional group practices appear to attract, in the health care sector at least, a greater than normal percentage of malpractice claims, professionals practicing in groups may be particularly willing to try an alternative.

IV. Conclusion

This note has examined the various shareholder tort liability provisions in the professional corporation legislation, including the nearly completed Model Professional Corporation Supplement. In light of the objectives of accident law, the preferable provision is the third model alternative, which makes each shareholder jointly and severally liable unless the corporation demonstrates financial responsibility for such harm, in which case no shareholder is liable in a shareholder capacity.

Because the personal fault system allows individuals in the marketplace to decide whether to pay the costs of negligently caused accidents or to act more safely, it might be thought that the additional liability potential from joint and several liability would make that form of liability preferable so far as the goal of deterring accidents is concerned. But the use of liability insurance, the relative wealth and market power of most professionals, and the lack of price resistance by consumers to noncompetitive fees assures that almost all professional accident costs are transferred to consumers and either dissipated by them or transferred to the government, whose insubstantial prevention regulations do not utilize shareholder liability for deterrence purposes. Further, in the rare instances in which professional corporation shareholders are not insulated from liability, their additional financial incentives to

174 In 1970 only 15 percent of the nation’s physicians practiced as members of a group. Carlson, supra note 56, at 854, 856 n.24, 861. But in the same year physicians practicing in groups (partnerships, associations, and professional corporations) were involved in 33.1 percent of the medical malpractice claims closed. See Rudov, Myers & Mirabella, supra note 42, at 16.
minimize accidents are largely ineffective because the shareholders are subject to the same ignorance about causes and costs of professional accidents and their prevention that makes it difficult for professionals and consumers to reduce the number and severity of professional accidents. Consequently, the theoretical deterrent superiority of joint and several liability is negligible in the actual context of professional accidents. Indeed, where the corporate assets are sufficient to meet reasonably anticipatable awards, joint and several liability may foster counterproductive practices, such as defensive medicine, rather than help to reduce accidents.

Because joint and several liability assures a larger number of sources and a larger fund for payment of negligently injured persons, it appears to be the preferable form of liability with respect to the accident law goal of reducing economic and social dislocation to both the victim and the injurer. But the widespread use of liability insurance and the wealth of professionals restrict the practical application of this feature of joint and several liability to very few instances.

Although joint and several liability is not effective in all situations and may be counterproductive in some, it is clearly the most effective type of liability where the available assets of the negligent employee and corporation are inadequate. Because the third alternative model provision utilizes joint and several liability in just these circumstances and retains limited liability in all others, it achieves the deterrence and social cost goals of accident law more effectively in the aggregate than does either limited liability or joint and several liability alone.

The final goal of accident law is fairness, which involves resolution of the conflicting social goals of encouraging professional activities and minimizing accidents. As compared to the preferred model provision, neither joint and several nor limited liability has any overriding claim of greater fairness which requires its exclusive use. Joint and several liability is not fairer because it is rarely needed and may be counterproductive in some situations. Limited liability is not fairer because professional corporations fail to offer the passive investment and commercial development which limited liability was designed to foster and because limited liability for shareholders cannot meaningfully affect the excessive malpractice liability that in recent years has impaired the delivery of professional services.

This note has also discussed the possibility of adapting the professional corporation form to help solve the malpractice crises, which stem in large part from the unfairness of the personal fault system. Several alternatives to the fault system in the professional
accident context that are worthy of careful consideration have been proposed. Although the politically powerful opposition of professionals to regulation and their substantial market power may make it difficult to make an alternative palatable on a voluntary basis, the pressing need for change and the decreasing usefulness of the professional corporation form for its original tax-minimizing function suggest that it may be an effective vehicle for experimentation with these proposed alternatives.

—Richard Tunis Prins