

Corporate Form Limits Damages Due Doctors

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Practice Area: Health Law

In a case recently decided by the Utah Supreme Court, a group of anesthesiologist shareholders achieved a hollow victory in their breach of contract dispute with a hospital.

Although the group “won” its suit, the Court determined damages had to be based on income lost to the professional corporation, which did not include the lost income of the shareholder/employed anesthesiologists.

Anesthesiologists Associates of Ogden, a Utah professional corporation, includes six anesthesiologists who covered St. Benedict’s Hospital under two separate service contracts – one for general surgical anesthesia and one for obstetrical anesthesia. When the group notified St. Benedict’s that it intended to discontinue obstetrical anesthesia, the hospital terminated both contracts. The group sued for breach of contract.

After finding that the hospital breached the contract, the trial court determined damages to be the lost income of the professional corporation, less the expenses it saved – including the anesthesiologists’ incomes – in not having to perform its contract obligations. The court awarded Associates damages of \$14,883.

Associates successfully argued before the court of appeals that, due to the unusual nature of professional service corporations, the income of the shareholder/employed anesthesiologists should be included in the damages due. The court of appeals reversed the trial court decision and found that the total damages amounted to more than \$1 million.

The Utah Supreme Court reinstated the trial court decision that damages were limited to what the corporation, not the physicians, lost as a result of the breach of contract. While acknowledging that professional corporations like those formed by physicians, attorneys and engineers are organized and operate somewhat differently than other kinds of corporations, the Court determined that those who choose to enjoy the advantages of a corporate form must endure the disadvantages as well.

Generally, corporate law holds that damages to a corporation from breach of contract are limited to the losses incurred by the corporation in not performing the contract, with such losses reduced by the “savings” incurred in not having to pay employees to perform the required contract services. The Court determined that this principle applies to a professional corporation that chooses to pay out all of its income as if it were a partnership.

The language of the Court contains a message to physicians who choose a professional corporate form:

"Unfortunately, Associates' argument confuses the corporation with its shareholder employees. The hospital's only contractual duty was to Associates; it had no duty under the contract to provide the salaries of the individual doctors, who were paid by the corporation out of the corporation's gross profits. This action was brought against the hospital by Associates, a professional corporation. The hospital contracted with none of the individual doctors, and none of the doctors whose salaries were lost through the hospital's breach were parties to this action."

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