1987

Municipal Liability under 1983: A Legal and Economic Analysis

Larry B. Kramer

Alan O. Sykes

LARRY KRAMER
ALAN O. SYKES

MUNICIPAL LIABILITY UNDER §1983: A LEGAL AND ECONOMIC ANALYSIS

Corporations are a legal fiction representing a network of legal, usually contractual, arrangements. "Corporations" thus do not act, do not make contracts, sell property, or commit torts; their agents do. For convenience, we sometimes describe the acts of such agents as acts of the corporation. But if an agent commits a tort and the tort is said to have been committed by the corporation (meaning that damages will be paid out of the corporate treasury), the corporation's liability is necessarily vicarious.

Vicarious liability may be imposed on any number of theories. At common law, corporate vicarious liability typically rests on the doctrine of *respondeat superior*, which holds principals liable for torts committed by their agents within the scope of employment.[1] In *Monell v. Department of Social Services*,[2] the Supreme Court held that the doctrine of *respondeat superior* is inapplicable to municipal corporations in suits brought under 42 U.S.C. §1983. "Instead," the

Larry Kramer and Alan O. Sykes are Assistant Professors of Law, The University of Chicago.

AUTHORS NOTE: We are grateful to Albert Alschuler, Walter Blum, Richard Craswell, David Currie, Daniel Fischel, Fred McChesney, Geoffrey Miller, Richard Posner, Geoffrey Stone, David Strauss, and Cass Sunstein for their helpful comments. Special thanks are due to Stephanie Dest for her indefagitable research assistance. Financial assistance for this paper was provided by the Lynde and Harry Bradley Foundation and by the Olin Foundation.

[1]See Keeton, Dobbs, Keeton & Owen, Prosser and Keeton on the Law of Torts 501-08 (5th ed. 1984).

[2]436 U.S. 658 (1978).

0-226-46440-7/88/1987-0006$01.00

Court explained in a much quoted passage, "it is when execution of a government's policy . . . , whether made by its lawmakers or by those whose edicts or acts may fairly be said to represent official policy, inflicts the injury that the government as an entity is responsible under §1983."[3]

Like the "scope of employment rule" or the "independent contractor rule" at common-law, the "policy rule" of *Monell* limits the circumstances in which a municipal employer may be held liable for tortious acts committed by agents or employees. Unfortunately, the Court in *Monell* did not define the concept of policy: elaboration of the policy rule was left to future litigation.[4] The result has been confusion about the limits of municipal liability under §1983. The factual patterns in which issues of §1983 municipal liability arise are extremely diverse, involving everything from employment decisions to licensing decisions to police misconduct. Even a small sampling of the numerous lower court decisions applying *Monell* reveals the absence of any clear understanding of what policy is or means.[5] Recent Supreme Court decisions have only added to the confusion. In each of the last three Terms, the Court agreed to hear cases for the purpose of elaborating the policy requirement, but was unable to put together a majority in any.[6]

That such uncertainty remains and indeed is growing suggests that a reexamination of the policy rule is in order. The policy rule has been extremely difficult to apply coherently, and there is no reason to continue the exercise. The *Monell* Court read the language and legislative history of §1983 erroneously. Rather than define the precise limits of liability, Congress intended to create a federal common-law tort remedy for deprivations under color of state law of federally protected rights. That conclusion raises the question how the federal courts should exercise their common-law power in determining the scope of municipal liability. We contend that this

[3]*Id.* at 694.

[4]*Id.* at 695.

[5]See, *e.g.*, Spell v. McDaniel, 824 F.2d 1380 (4th Cir. 1987); Nahmod, Civil Rights and Civil Liberties Litigation: The Law of Section 1983 ch. 6 (2d ed. 1986).

[6]The cases are City of Oklahoma City v. Tuttle, 471 U.S. 808 (1985); Pembaur v. City of Cincinnati, 475 U.S. 469 (1986); and City of Springfield v. Kibbe, 107 S.Ct. 1114 (1987). The Court recently heard argument in City of St. Louis v. Praprotnik, No. 86-772, which raises a question suggested by *Pembaur:* whether a municipality is liable under §1983 for unconstitutional actions taken by non-policymaking municipal employees acting within the scope of delegated authority when these actions are not subject to further *de novo* review.

question cannot be answered without due regard for the economic consequences of municipal liability, and that economic analysis may be dispositive. We conclude that *Monell's* policy rule—which has the effect of immunizing the municipality where there is no policy and making it strictly liable where there is policy—is economically inefficient.[7] We suggest the adoption of a negligence rule for the imposition of municipal liability, requiring the plaintiff to show tbat the municipality (*i.e.*, municipal officials who supervise the tortfeasor) failed to take reasonable (*i.e.*, cost-effective) measures to avert the tort, or, alternatively, the adoption of conventional *respondeat superior.* With respect to cases in which the individual tortfeasor enjoys immunity, we tentatively conclude that immunity ought also to extend to the municipality.

I. A Reexamination of Municipal Liability Under Monell

A. THE POLICY RULE

The Court's post-*Monell* efforts have produced two competing views of what constitutes "policy" for purposes of municipal liability under §1983, neither of which has been accepted by a majority of the justices.

One view, developed in Part IIB of Justice Brennan's opinion in *Pembaur v. City of Cincinnati*[8] (a part joined only by a plurality[9]), focuses on the status of the decisionmaker. This view conceptualizes "policy" as encompassing decisions that are made by persons designated to speak the last word for the municipality. A second view, implicit in Justice Rehnquist's plurality opinion in *City of Oklahoma City v. Tuttle*[10] and elaborated in Justice Powell's dissent in *Pembaur*,

---

[7]This paper uses the term "efficiency" in the Hicks-Kaldor sense: liability rule A is more efficient that liability rule B if the members of society who prefer A to B can compensate the members of society who prefer B to A and remain better off themselves, whether or not such compensation is actually paid. This notion of efficiency underlies applied "cost/benefit" analysis as it is generally practiced and is the concept of efficiency typically employed in economic analyses of tort law. See generally Landes & Posner, The Economic Structure of Tort Law (1987).

[8]475 U.S. 469 (1986).

[9]In *Pembaur*, Justice Brennan delivered an opinion for six justices in Parts I and IIA, for four justices in Part IIB, and for five justices in Part IIC. Justices White, Stevens, and O'Connor each wrote separate opinions disagreeing with particular aspects of Justice Brennan's analysis. Justice Powell dissented, joined by Chief Justice Burger and Justice Rehnquist.

[10]471 U.S. 808 (1985).

emphasizes the nature of the decision and the process by which it is made. This view limits "policy" to formal rules, usually of general applicability, established through careful deliberation.

Pembaur highlights the difference between these views. In that case, county police officers sought entry to plaintiff's medical clinic to execute a capias (a form of arrest warrant) for two witnesses thought to be at the clinic. When plaintiff refused to allow them to enter, the officers contacted their supervisor, who advised them to call the prosecutor for instructions. The prosecutor commanded them to " 'go in and get [the witnesses],' " a command subsequently held to violate the Fourth Amendment. The liability of the county turned on whether this order constituted "policy" under *Monell.* The evidence showed that county police had never before used force to gain access to a third-person's property while serving a capias, that the police handled such matters on a case-by-case basis, and that the practice of the county police department was to refer such matters to the county prosecutor and follow his instructions.[11]

Justice Brennan concluded that the prosecutor's order constituted policy under *Monell.* He understood the policy rule as intended "to distinguish acts of the *municipality* from acts of *employees* of the municipality, and thereby [to] make clear that municipal liability is limited to action for which the municipality is actually responsible."[12] Decisions by some municipal employees are acts "of the municipality" while other decisions are merely acts "of employees of the municipality." Liability depends entirely on who makes a decision: "where the decisionmaker possesses final authority to establish policy with respect to the action ordered," the decision can fairly be said to represent a decision of the municipality itself and the imposition of liability is not vicarious.[13]

Justice Powell argued in dissent that the plurality's view constituted nothing less than a partial overruling of *Monell.* By focusing exclusively on the status of the decisionmaker, "local government

---

[11]475 U.S. at ___, 106 S.Ct. at 1294–96.

[12]*Id.* at ___, 106 S.Ct. at 1298.

[13]*Id.* at ___, 106 S.Ct. at 1298–1300. Justice Brennan did not explain how it is possible to determine who is a policymaker without first determining what makes something "policy," although he did distinguish between policymaking power and discretion (apparently including discretion to make unreviewed decisions). *Id.* at ___, 106 S.Ct. at 1299–1300. The Court may clarify the distinction in City of St. Louis v. Praprotnick, No. 86-772.

units are now subject to *respondeat superior*, at least with respect to a certain class of employees, *i.e.*, those with final authority to make policy."[14] Justice Powell argued that the Court should focus on the characteristics of the decision at issue. Thus, for Justice Powell, "policy" is established "when a rule is formed that applies to all similar situations—a 'governing principle [or] plan.' . . . When a rule of general applicability has been approved, the government has taken a position for which it can be held responsible."[15] In rare instances, a rule not of general applicability may constitute municipal policy according to Justice Powell, but only if that rule was formulated through a properly deliberative process.[16] Because the prosecutor's order was directed to the specific case only and was "an off-the-cuff answer to a single question," it did not constitute policy for purposes of §1983.[17]

Both the plurality and the dissent in *Pembaur* read *Monell* as holding that municipalities cannot be vicariously liable under §1983, and both reason that municipal liability is direct rather than vicarious only when a tort is committed pursuant to policy. The argument in *Pembaur* thus turns on whether a particular definition of policy successfully limits municipal liability to situations where the municipality is directly responsible for the tort or whether it has the effect of imposing liability vicariously.

Justice Powell is surely correct when he characterizes Justice Brennan's approach as imposing a form of vicarious liability: the municipality must pay for the wrongful acts of certain of its employees. But exactly the same thing can be said of Justice Powell's approach. The only difference between the two formulations is that Justice Powell would impose vicarious liability only if the employee whose acts are to be attributed to the municipality expressed himself in general terms or chose his course of action carefully.

The problem is that municipal action is always—can only be—carried out by persons employed by the municipality. Municipal liability is necessarily vicarious, and there is no such thing as "policy" that can make a municipality directly rather than vicariously responsible for a constitutional tort. "Policy" is merely a conclusion

---

[14] 475 U.S. at ___, 106 S.Ct. at 1308.

[15] *Id.* at ___, 106 S.Ct. at 1309.

[16] *Id.* at ___, 106 S.Ct. at 1309.

[17] *Id.* at ___, 106 S.Ct. at 1310.

about which activities by which municipal employees should be vicariously attributed to the municipality for purposes of §1983. It is therefore senseless to try and define policy as the Court has done, as something that distinguishes acts "of the municipality" from acts of "employees of the municipality."

But *Monell* did not hold that all forms of vicarious municipal liability are improper. *Monell* held only that "a municipality cannot be held liable *solely* because it employs a tortfeasor—or, in other words, a municipality cannot be held liable under §1983 on a *respondeat superior* theory."[18] Thus, the proper question is not whether we can define policy in such a way as to prevent imposing vicarious liability, but whether we can define policy in such a way as to prevent imposing a particular form of vicarious liability—*respondeat superior.*

This refinement does little to solve the problem of defining "policy." There are several semantically plausible definitions of policy.[19] The problem is to choose which of these definitions best serves the purpose underlying the "policy" concept as it is used in the context of §1983 municipal liability. But *Monell* tells us only that municipal liability must rest on more than *respondeat superior*, and all of the competing definitions of policy satisfy this requirement. For example, Justice Brennan's approach in *Pembaur* is more than *respondeat superior*, because the municipality is not liable for acts by every municipal employee; it is *respondeat superior* "plus," with the plus factor being the limitation to those employees who make policy. Similarly, Justice Powell's approach limits the scope of *respondeat superior* to a particular kind of act by policymaking employees. Indeed, every definition of policy that in any way limits the ordinary scope of *respondeat superior* will satisfy *Monell* by not imposing liability "*solely* because [the municipality] employs a tortfeasor."[20] It is, therefore, not surprising that courts have had difficulty implementing *Monell's* policy rule. By limiting municipal liability to acts pursuant to "policy" without saying anything more than policy is something different from *respondeat superior*, the Supreme Court

[18]436 U.S. at 691; see also *id.* at 692 & n.57.

[19]Consider, for example, the different dictionary definitions cited and relied upon by the Justices. *Compare Pembaur*, 475 U.S. at ____, 106 S.Ct. at 1299, n.9 (opinion of Brennan, J.) *with id.* at ____, 106 S.Ct. at 1309 (Powell, J., dissenting) and City of Oklahoma City v. Tuttle, 471 U.S. 808, 823 n.6.

[20]436 U.S. at 691.

established a vague category susceptible to many plausible definitions.

Should the policy rule therefore be abandoned? The Court in *Monell* deliberately chose not to elaborate the meaning of policy, and it may be that the reasoning which led the Court to reject *respondeat superior* suggests ways of refining the policy rule. Reexamining *Monell*, however, demonstrates only that the Court's reasons for rejecting the use of *respondeat superior* under §1983 were mistaken.

B. MONELL

Monell offered two propositions to support its conclusion that Congress did not intend municipalities to be liable under §1983 unless a tort resulted from action pursuant to municipal policy. First, the Court suggested that this limitation was implicit in the language of §1983. Second, it contended that the application of *respondeat superior* to municipalities would be inconsistent with §1983's legislative history.

1. Monell's *Analysis of the language of §1983*. Section 1983 holds liable "[e]very person who, under color of [state law] subjects, or causes to be subjected" any person to the deprivation of a federally protected right.[21] *Monell* overruled the holding of *Monroe v. Pape* that municipal corporations are not "persons" within the meaning of this language.[22] At the same time, the Court found significance in the phrase "subjects or causes to be subjected." According to the Court, "that language cannot be easily read to impose liability vicariously on governing bodies solely on the basis of the existence of an employer-employee relationship with a tortfeasor. Indeed, the fact that Congress did specifically provide that A's tort became B's liability if B 'caused' A to subject another to a tort suggests that Congress did not intend §1983 liability to attach where such causation was absent."[23]

---

[21]In its entirety, §1983 provides: "Every person who, under color of any statute, ordinance, regulation, custom, or usage, of any State or Territory, subjects, or causes to be subjected, any citizen of the United States or other person within the jurisdiction thereof to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured in an action at law, suit in equity, or other proper proceeding for redress." 42 U.S.C. §1983 (1982).

[22]See *Monell*, 436 U.S. at 664–89; Monroe v. Pape, 365 U.S. 167, 187–92 (1961).

[23]436 U.S. at 692.

The Court does not explain why the municipality "causes" the constitutional tort only if the tort is committed pursuant to official policy. The practical effect of the policy rule is to limit vicarious liability to cases in which high-level municipal employees participate in the tort. But even if there is reason to treat the acts of high-level employees differently from the acts of lower-level employees, that reason has nothing to do with causation and thus nothing to do with the language upon which the Court focused. The municipality has not "caused" the tort more in one situation than in the other.

More importantly, the Court was wrong to suppose that the language of §1983 conveys such subtle limitations on liability. That language, which was proposed and debated as §1 of the Civil Rights Act of 1871, was borrowed from §2 of the Civil Rights Act of 1866.[24] The wording was given little thought or attention by its drafters, who were primarily concerned with the more controversial provisions of sections two through four.[25] For similar reasons, §1 was largely ignored during the bitter and extensive floor debate concerning the 1871 Civil Rights Act.[26] Supporters said only that §1 was to be "liberally and beneficently construed" by the courts.[27] The only opponent of the Act to address §1 in any detail was Senator Thurman, and his chief complaint was that its language was vague and raised more questions than it answered.[28]

The reason so little attention was paid to the wording of §1 is suggested by a colloquy between Senators Thurman and Edmunds about another provision of the Act at a later point in the debate: Edmunds (who sponsored the 1871 Act) responded to Thurman's charge that the Act omitted certain essential safeguards by stating that these need not be included by Congress since they were already

---

[24]Adickes v. S.H. Kress & Co., 398 U.S. 144, 162–63 (1970); Cong. Globe, 42d Cong., 1st Sess. app. at 68 (1871) [hereinafter Globe] (statement of Rep. Shellaharger); Nahmod, note 7 *supra*, at §1.03.

[25]For the history of the Civil Rights Act of 1871, see Fairman, VII History of the Supreme Court of the United States ch. 3 (1987); Comment, 46 U. Chi. L. Rev. 402, 407–17 (1979); see generally Globe, note 24 *supra*.

[26]See Globe, note 24 *supra*, *passim*; *Monell*, 436 U.S. at 665.

[27]Globe, note 24 *supra*, app. at 68 (statement of Rep. Shellabarger); see also *id.* at 800 (statement of Rep. Perry). Similar statements are collected and cited in *Monell*, 436 U.S. at 684–85 & n.45.

[28]Globe, note 24 *supra*, app. at 216–17.

provided by the common law.[29] In other words, the language of §1983 was not intended to define fully the extent of liability, which would be determined by the courts through common-law adjudication.[30]

2. Monell's *analysis of §1983's legislative history.* The holding in *Monell* does not rest solely on the Court's textual argument. Indeed, the Court relied "[p]rimarily"[31] on a second proposition: that the limitation of municipal liability to action pursuant to official policy is mandated by the legislative history of the Civil Rights Act of 1871, in particular, the debate over the so-called "Sherman amendment."

The history of the Sherman amendment, which was twice modified by conference committees before being passed, is recounted in great detail in *Monell.*[32] The relevant portion of that history is the House debate in which the first conference report was rejected.[33]

---

[29]See Globe, note 24 *supra*, at 771. Senator Thurman responded that common-law doctrines should not be read into a statute. *Ibid.* See also the colloquy between Senators Sherman, Edmunds, Thurman, and Frelinghuysen in which Senator Sherman explains that an amendment to his proposed amendment is unnecessary because the common-law already contains such a provision. *Id.* at 707.

[30]In addressing other questions under §1983, the Court has recognized that the statute should be "read against the background of tort liability." Monroe v. Pape, 365 U.S. 167, 187 (1961). *Accord* Carey v. Piphus, 435 U.S. 247, 258 n.13 (1978); Imbler v. Pachtman, 424 U.S. 409, 418 (1976). See also Nahmod, Section 1983 and the "Background" of Tort Liability, 50 Ind. L. J. 5 (1974); Comment, 46 U. Chi. L. Rev. 935, 939 (1979); Comment, 37 U. Chi. L. Rev. 494, 507–08 (1970).

[31]See *Pembaur*, 106 S.Ct. 1292, 1298 (1986).

[32]See *Monell*, 436 U.S. at 665–83.

[33]Globe, note 24 *supra*, at 755; see also *Monell*, 436 U.S. at 703–04. The bill which became the Civil Rights Act of 1871 was proposed as H.R. 320 by Representative Shellabarger on March 28, 1871. Globe, note 24 *supra*, at 317. Senator Sherman introduced his amendment immediately prior to the vote in the Senate. *Id.* at 663, 686. As proposed, the Sherman amendment would have added a provision to the Act making any inhabitant of a municipality liable for damage inflicted within municipal boundaries by any persons "riotously and tumultuously assembled" for the purpose of depriving the victim of federally protected rights. *Id.* at 663. Under the Senate's rules, no discussion of the amendment was allowed and it passed without debate. *Id.* at 704–09.

The House refused—also without debate—to acquiesce in the Sherman amendment by a vote of 45–132 and requested a conference on this and several other amendments made by the Senate to H.R. 320. *Id.* at 725. Despite the overwhelming rejection of the Sherman amendment by the House, the Senate voted not to recede and agreed to confer. *Id.* at 727–28. The conferees submitted an alternative version of the Sherman amendment to the Senate the very next day. The debate over this proposal, which modified the original proposal to give the victim an action against the municipality itself, was thus the first open debate in Congress on the merits of the Sherman amendment.

This report proposed adding to the 1871 Act a section that would provide victims of injuries inflicted by "any persons riotously and tumultuously assembled together" an action for damages against the municipality in which the injuries were inflicted. The municipality, in turn, was given an action for indemnity against the wrongdoers.

As explained in *Monell*, the Representatives who voted against this proposal—in particular, the moderate Republicans who held the balance of power in the House[34]—did so because they thought that it was unconstitutional.[35] Congress sought in the 1871 Act to stop groups such as the Ku Klux Klan from using violence to prevent individuals from exercising their constitutional rights. The Sherman amendment went beyond the Act's provisions for federal intervention and sought by imposing liability to compel municipalities to assist the federal government in this effort. Opponents of the Sherman amendment contended that, while Congress could create federal mechanisms for enforcing constitutional rights, it could not obligate state and local governments to allocate their resources to the task.[36]

This understanding of the limits of federal power was consistent with then-existing Supreme Court precedents such as *Collector v. Day*[37] and *Prigg v. Pennsylvania*.[38] In fact, the moderate Republicans

---

The Senate agreed to the conference report by a vote of 32–16, essentially identical to the 38–24 vote that had approved Senator Sherman's initial proposal. *Id.* at 707, 779. The House again voted the amendment down, this time by the somewhat closer margin of 74–106. *Id.* at 800. A second conference was held and the amendment was drastically altered: the second conference version did not mention municipalities; it imposed liability on individuals who knew that a wrong was to be committed and had power to prevent it but failed to act. *Id.* at 801, 802, 819–20. This version easily passed both Houses of Congress. *Id.* at 804, 808, 831. It is currently codified as 42 U.S.C. §1986.

[34]See Comment, note 24 *supra*, 46 U. Chi. L. Rev., at 414–20.

[35]*Monell*, 436 U.S. at 669–83.

[36]Globe, note 24 *supra*, at 795 (statement of Rep. Blair). This position was espoused by all of the Republicans who spoke against the Sherman amendment. See *id.* at 791 (statement of Rep. Willard); *id.* at 793 (statement of Rep. Poland); *id.* at 795 (statement of Rep. Burchard); *id.* at 799 (statement of Rep. Farnsworth).

[37]*Collector* held that the federal government could not tax a state court judge because this would enable the federal government to cripple or destroy the "means and instrnmentalities employed [by the states] for carrying on the operations of their governments." 11 Wall. 113, 125–126 (1871).

[38]*Prigg* held that, while the Fugitive Slave Clause empowered Congress to enact legislation for the return of escaped slaves, Congress could not require state officers to execute such legislation but must provide federal means of doing so. 16 Pet. 539, 615–16 (1842).

whose votes defeated the first conference report cited and discussed these cases as the source of their opposition.[39]

Although the Sherman amendment had nothing to do with §1 of the 1871 Act, Justice Brennan found the reasons for its rejection pertinent to the imposition of municipal liability under §1983. He argued that *respondeat superior* imposes an obligation on employers to prevent their employees from committing torts that is much like the obligation to prevent Klan violence imposed on municipalities by the Sherman amendment.[40] It follows, therefore, that "creation of a federal law of *respondeat superior* would have raised all the constitutional problems associated with the obligation to keep the peace, an obligation Congress chose not to impose because it thought imposition of such an obligation unconstitutional."[41]

This reasoning proves too much. Justice Brennan asserts that *respondeat superior* under §1983 would have raised the same constitutional objections as the Sherman amendment because it too imposes an obligation on municipalities. But if all such obligations suffer the same constitutional infirmity, why was it not also unconstitutional for Congress to impose an obligation to obey the Constitution on individual state officers? The only difference between requiring an individual officer not to violate the Constitution and requiring a municipality to insure that its employees do not violate the Constitution is that the individual officer is made responsible only for his own behavior, while the municipality is made responsible for the behavior of agents. But that distinction has

---

[39]See, *e.g.*, Globe, note 24 *supra*, at 795 (discussing *Prigg* and Collector v. Day) (statement of Rep. Blair); *id.* at 793 (discussing Collecter v. Day) (statement of Rep. Poland); *id.* at 799 (discussing Collecter v. Day) (statement of Rep. Farnsworth).

[40]436 U.S. at 693–94.

[41]*Id.* In a footnote, Justice Brennan added that the Sherman amendment was the only form of vicarious liability presented to Congress and concluded that "combined with the absence of any language in §1983 which can easily be construed to create *respondeat superior* liability, the inference that Congress did not intend to impose such liability is quite strong." 436 U.S. at 693 n.57. On the contrary, any such inference depends on erroneous assumptions. The nature of the liability to be imposed by the Sherman amendment was significantly different from *respondeat superior*, and its rejection eannot reasonably be interpreted to say anything at all about the question. The Sherman amendment would have made the municipality liable for unlawful acts committed by anyone—citizens, employees, or strangers—within municipal boundaries. Although a few states and England may have had similar "riot acts," see Globe, note 24 *supra*, at 760–61 (statement of Sen. Sherman); *id.* at 792 (statement of Rep. Butler), this was an unusually severe form of viearious liability. *Respondeat superior*, on the other hand, was an alrcady long-established and unexceptionable common-law rule. See City of Oklahoma City v. Tuttle, 471 U.S. 808, 835–39 (1985) (Stevens, J., dissenting).

nothing to do with the constitutional principles that made the Sherman amendment objectionable. Indeed, the cases relied upon by the opponents of the Sherman amendment—*Collector v. Day* and *Prigg v. Pennsylvania*—involved federal efforts to impose duties on individual state officials. The Sherman amendment's opponents were able to make their argument only by claiming that municipalities were identical to individual officers as regards the principle of dual sovereignty recoguized in these cases.[42]

Thus, if Justice Brennan is right—if Congress would have found the imposition of a duty on municipalities to prevent their employees from violating the Constitution subject to the same objections as the Sherman amendment—then Congress would have also opposed the imposition of an obligation to obey the Constitution on individual state officials. Yet everyone agreed that §1983 was intended to do just that.[43] The moderate Republicans whose votes defeated the Sherman amendment voted in favor of §1983.[44]

These votes can, however, be reconciled. The opponents of the Sherman amendment distinguished between imposing an entirely new obligation on a state officer, and requiring a state officer to discharge obligations already imposed by state law in accordance with the Constitution. The federal government could not add to the duties imposed on state agents by state law an additional duty to prevent Klan violence, but the federal government could require state agents to discharge duties the state had already placed on them in accordance with the Constitution.[45] In other words, the argument that the federal government had no power to impose obligations on state agents did not include the obligation to obey the Constitution in the pursuit of ends established by state law.

---

[42]See, *e.g.*, Globe, note 24 *supra*, at 795 (statement of Rep. Blair): "It was held also in the case of Prigg v. Pennsylvania (I speak from recollection only) that it was not within the power of the Congress of the United States to lay duties upon a State officer; that we cannot command a state officer to do any duty whatever, as such; and I ask gentlemen to show me the difference between that and commanding a municipality, which is equally the crcature of the State, to perform a duty."

[43]*Monell*, 436 U.S. at 682–83; see, *e.g.*, Globe, note 24 *supra*, at 334 (statement of Rep. Hoar); *id.* at 365 (statement of Rep. Arthur); *id.* at 367–68 (statement of Rep. Sheldon); *id.* at 385 (statement of Rep. Lewis).

[44]*Compare* Globe, note 24 *supra*, at 522 *with id.* at 800.

[45]This distinction was drawn by a number of opponents to the Sherman amendment. See, *e.g.*, Globe, note 24 *supra*, at 794 (statement of Rep. Poland); *id.* at 795 (statement of Rep. Blair); *id.* (statement of Rep. Burchard); *id.* at 799 (statement of Rep. Farnsworth). *Cf.* Levin, The Section 1983 Municipal Immunity Doctrine, 65 Georgetown L. J. 1483, 1520–31 (1977).

This distinction may sound hollow to the modern ear. After all, requiring a state officer not to violate the Constitution while performing duties imposed by state law is still imposing an obligation—the obligation to obey the United States Constitution. In both cases, a state officer is being required by the federal government to act in a particular way. The distinction may be justified, however, by the difference in degree of intrusion by the federal government into the operation of state government. In any event, and however weak or strong the distinction may appear today, it was recognized and accepted by the members of the Forty-Second Congress.

What this means, moreover, is that the constitutional objections to the Sherman amendment have no bearing on whether a municipality may be liable under §1983 on a *respondeat superior* theory. Under *Collecter v. Day* and *Prigg v. Pennsylvania*, it was thought that Congress could not impose obligations on individual state officers. But there was no constitutional impediment to holding such officers liable if they violated the Constitution while performing tasks delegated to them by the state. For purposes of *Collector v. Day* and *Prigg*, there was no distinction between individual and corporate agents of the state.[46] Thus, by analogy to these same cases, Congress could not impose affirmative obligations on municipalities. However, still reasoning by analogy, there would have been no constitutional impediment to holding municipalities liable for constitutional violations committed by municipal employees performing tasks delegated to the municipality by the state.

II. Methodological Issues in Interpreting §1983: Toward a Common-Law Foundation for Municipal Liability

What follows from the conclusion that *Monell*'s analysis is unsound? Does the inadequacy of its reasoning imply that *respondeat*

[46]This was Representative Blair's argument cited *supra* at note 42. This conclusion is also consistent with the prevailing legal theory, which held that a municipal corporation is merely an agent of the state to which some of the duties of governing have been assigned. See, *e.g.*, Shearman & Redfield, The Law of Negligence §§116–22 (2d ed. 1870); Dillon, The Law of Municipal Corporations §§29–39 (1872); Cooley, Constitutional Limitations, 211 (1868); Cooley, General Principles of Constitutional Law 344–45 (1880).

Interestingly, Justice Brennan relied on the identity between individual and corporate agents in Part I of *Monell* to explain why the objections to the Sherman amendment did not support the conclusion that municipalities could never be liable under §1983. See 436 U.S. at 682; Mead, 42 U.S.C. §1983 Municipal Liability: The Monell Sketch Becomes a Distorted Picture, 65 N.C. L. Rev. 517, 535–36 (1987).

superior should be fully applicable to municipalities? Other commentators and one Justice have reached this conclusion, arguing that if the language and legislative history of §1983 do not preclude municipal liability on a *respondeat superior* theory, then the fair assumption is that it was intended to apply to suits under §1983.[47] These commentators note that the doctrine of *respondeat superior* was used against municipalities in 1871 and argue that the members of the Forty-Second Congress were familiar with common-law principles and presumably intended them to apply.

This is a conventional method of statutory construction. Courts often assume that if the language and legislative history of a statute are silent on a question, the legislature intended to incorporate then-prevailing rules of law. Hence, it is certainly plausible to interpret §1983 to incorporate nineteenth-century principles of *respondeat superior.*

The argument is plausible, but incomplete. To be sure, municipal corporations sometimes incurred liability under *respondeat superior* at the time §1983 was enacted.[48] But more commonly, municipal corporations were insulated from liability by various immunity doctrines not applicable to private corporations. For example, municipal corporations were not liable for wrongs committed by municipal employees performing "governmental" rather than "corporate" (we would now say "proprietary") activities.[49] This limitation on municipal liability is significant here because, while the classification of municipal activities as "corporate" or "governmental" was often controversial,[50] the vast majority of §1983 claims probably

---

[47]See, *e.g.*, *Pembaur*, 475 U.S. at ____, 106 S.Ct. at 1303 (Stevens, J., concurring in part and concurring in the judgment); Mead, note 46 *supra*, at 538–42; Blum, From Monroe to Monell: Defining the Scope of Municipal Liability in Federal Courts, 51 Temp. L. Q. 409, 413 n.15 (1978); Comment, 47 Brook. L. Rev. 517, 552–57 (1981); Comment, note 30 *supra*, 46 U. Chi. L. Rev. at 952–55; Comment, 64 Iowa L. Rev. 1032, 1045–52 (1979); Note, 7 Hofstra L. Rev. 893, 917–21 (1979).

[48]See Cooley, The Law or Torts 619–27 (1879) (citing cases); Dillon, note 46 *supra*, at §§752–802 (citing cases); Shearman & Redfield, note 46 *supra*, ch. 8 (citing cases). See also *Pembaur*, 475 U.S. at ____, 106 S.Ct. 1292, 1303 (1986) (Stevens, J., dissenting); City of Oklahoma City v. Tuttle, 471 U.S. at 834–36 (Stevens, J., dissenting); Mead, note 46 *supra*, at 527; Blum, note 47 *supra;* Comment, note 30 *supra*, 46 U. Chi. L. Rev. at 956–61.

[49]See Dillon, note 46 *supra*, at §§753–55, 764, 778–80; Cooley, note 48 *supra*, at 619–20; Shapo, Municipal Liability for Police Torts: An Analysis of a Strand of American Legal History, 17 U. Miami L. Rev. 475, 478–79 (1963); Note, 30 Am. St. Rep. 376 (1892) (citing cases); see also Owen v. City of Independence, 445 U.S. 622, 644–47 (1980).

[50]See Dillon, note 46 *supra*, §766 at 724.

involve municipal functions that were traditionally classified as governmental.[51]

The "governmental functions" immunity apparently was not available if the wrongful act "was expressly authorized by the governing body of the corporation, or where, without such special authorization, it . . . has been ratified by the corporation."[52] This is rather similar to the policy rnle of *Monell.* Consequently, and somewhat ironically, proponents of the view that §1983 should be interpreted consistently with common-law principles in use when it was enacted may find themselves reaffirming the policy rnle after all. In any event, advocates of this interpretation of §1983 must explain why municipalities can no longer rely on the common-law immunities.[53]

Simply posing this question suggests another: why should liability under §1983 depend upon—or have anything to do with—the common law of 1871? Why, in other words, should congressional silence on the issue of municipal liability be interpreted to incorporate and freeze then-existing common-law rules?[54]

---

[51]Levin, note 45 *supra,* at 1521 n.156.

[52]Dillon, note 46 *supra,* §770 at 728 & n.2 (citing cases). See also Cooley, note 48 *supra,* at 621; Shearman & Redfield, note 46 *supra,* §120 at 148. Shearman and Redfield went farther than this and asserted in 1869 that the distinction between governmental and corporate activities had been "entirely repudiated." *Ibid.* However, they did not support this assertion with any authority, and, in light of the cases cited by Dillon, Cooley, and others, it appears that Shearman and Redfield were trying to shape rather than describe law. Although inaccurate at the time, Shearman's and Redfield's assertion subsequently became the law in most states. See note 54 *infra.*

[53]In Owen v. City of Independence, 445 U.S. 622 (1980), the Supreme Court held that the common-law "governmental functions" immunity is not available to municipalities sued under §1983. Tracing the source of this doctrine to the principle of sovereign immunity, the Court explained: "the municipality's 'governmental' immunity is obviously abrogated by the sovereign's enactment of a statute making it amenable to suit. Section 1983 was just such a statute. By including municipalities within the class of 'persons' subject to liability for violations of the Federal Constitution and laws, Congress—the supreme sovereign on matters of federal law—abolished whatever vestiges of the State's sovereign immunity the municipality possessed." *Id.* at 647–48 (footnote omitted). This is *ipse dixit.* The fact that Congress could have abrogated this municipal immunity does not mean that it did so. In precisely the same way, Congress could have abrogated the traditional common-law immunities of individual officials. Yet the Supreme Court has held that Congress did not abolish these immunities in enacting 1983. See notes 64–68, 76–86 *infra* and accompanying text.

[54]The rules of municipal liability in the states have undergone profound changes in the last 117 years as a product of both judicial and legislative efforts. See Prosser & Keeton, note 1 *supra,* at 1051–52; Shapo, note 49 *supra.* See also Owen v. City of Independence, 445 U.S. at 680–82 (Powell, J., dissenting).

The language and legislative history of §1983 say nothing about a great many issues in addition to municipal liability that arise under the statute. To name only a few, the statute and its legislative history do not indicate what defenses are available,[55] who bears the burdens of pleading and persuasion,[56] what kinds of damages are recoverable,[57] or whether exhaustion of state remedies is required.[58] Surely Congress must have been aware that cases under §1983 would raise many issues not answered by the text. The legislative history suggests an explanation for Congress' silence on these issues. Supporters of the 1871 Act wanted a federal remedy for injuries associated with the denial under color of state law of federally protected rights. Once the existence of a remedy was established, however, the Act's supporters were content to allow the courts to develop its boundaries as part of the federal common law of torts. Thus, on the few occasions when opponents pointed to the omission of particular details from the Act, supporters answered that such provisions were "not necessary because the common law gives a remedy."[59]

One can, of course, read these references to the common law as evidence that Congress thought it was incorporating then-existing common law into the statute. Far more likely, however, is the conclusion that Congress intended the federal courts to shape and develop this tort as part of the general common law. It was the heyday of *Swift v. Tyson*;[60] the existence of an evolving common law and of federal judicial power to share in its development was a given. Indeed, some members of Congress apparently understood §1983 as nothing more than a grant of federal jurisdiction over common-law tort actions that had previously been heard exclusively

[55]See, *e.g.*, Tenny v. Brandhove, 341 U.S. 367, 376 (1951); Pierson v. Ray, 386 U.S. 547, 554–55 (1967).

[56]See, *e.g.*, Gomez v. Toledo, 446 U.S. 635 (1980).

[57]See, *e.g.*, Memphis Community School District v. Stachura, 106 S.Ct. 2537 (1986); Smith v. Wade, 461 U.S. 30 (1983); City of Newport v. Fact Concerts, Inc., 453 U.S. 247 (1981); Carey v. Piphus, 435 U.S. 247 (1978).

[58]See, *e.g.*, Patsy v. Bd. of Regents, 457 U.S. 496 (1982).

[59]See Globe, note 24 *supra*, at 707 (statement of Sen. Sherman); see also *id.* at 771 (statement of Sen. Edmunds); notes 24–30 *supra* and accompanying text.

[60]16 Pet. 1 (1842).

by state courts.[61] Thus, while the issue is not free from doubt, the sounder view is that—as with the Sherman Act and the federal habeas corpus statute—Congress intended not only to allow the common law to inform §1983, but also to permit the common-law interpretation of the statute to evolve with the rest of the common law.

The Supreme Court has sometimes said that it does not have common-lawmaking powers under §1983.[62] Where the language and legislative history do not make congressional intent clear, the Court has said, §1983 should be interpreted by assuming that the "members of the 42d Congress were familiar with common-law principles . . . and that they likely intended these common-law principles to obtain, absent specific provisions to the contrary."[63] Notwithstanding such statements, the Court has seldom hesitated to abandon historical inquiry into congressional intent in favor of its own analysis of sound public policy.

Consider the cases on official immunity.[64] The language and legislative history of §1983 do not indicate whether state officials may assert immunities, and the Court has engaged in an official-by-official analysis of whether immunity is available. In its early encounters with this question, the Court simply asked whether there was an analogous tort immunity at common-law and assumed that if Congress had wished to abrogate that immunity it would have said so.[65] But the Court did not adhere to this approach in subse-

---

[61]Senator Thurman began his remarks in opposition with the statement that §1 of the 1871 Civil Rights Act "creates no new cause of action. Its whole effect is to give to the Federal Judiciary that which now does not belong to it—a jurisdiction that may be constitutionally conferred upon it, I grant, but that has never yet been conferred upon it." Globe, note 24 *supra*, app. at 216. See also Butz v. Economou, 438 U.S. 478, 502, n.30 (1978), quoting District of Columbia v. Carter, 409 U.S. 418, 427–28 (1973).

[62]See, *e.g.*, Malley v. Briggs, 475 U.S. 335, ____, 106 S.Ct. 1092, 1097 (1986); see also Wood v. Strickland, 420 U.S. 308, 316 (1975).

[63]City of Newport v. Fact Concerts, Inc., 453 U.S. 247, 258 (1981). See also, *e.g.*, Malley v. Briggs, 475 U.S. 335, ____, 106 S.Ct. 1092, 1097 (1986); Briscoe v. LaHue, 460 U.S. 325, 330, 334 (1983); Pierson v. Ray, 386 U.S. 547, 553–55 (1967) ("Congress would have specifieally so provided had it wished to abolish" common-law doctrines).

[64]The pattern described here is not limited to the issue of official immunity but ean be found in the Court's solution to other questions not resolved by the language or legislative history of §1983. See Kreimer, The Source of Law in Civil Rights Actions: Some Old Light on Section 1988, 133 U. Pa. L. Rev. 601, 611 (1985). See, *e.g.*, cases cited at notes 55–58 supra.

[65]See, *e.g.*, Tenny v. Brandhove, 341 U.S. 367, 376 (1951); Pierson v. Ray, 386 U.S. 547, 554–55 (1967).

quent cases. In some cases, the Court ignored or disregarded the common law and resolved the question of immunity solely on the basis of policy considerations such as whether liability would have an undue chilling effect on decisionmaking.[66] In other cases, the Court examined the common law to see whether it provided immunity, and asked whether the considerations supporting the common-law rule likewise warrant immunity under §1983.[67] In still other cases, the Court discussed both common-law and public policy considerations, without explaining how these considerations are related.[68] In none of these subsequent cases did the Court limit its examination of the common law to the period before 1871.

The inconsistency between these cases and statements that §1983 should be presumed to incorporate common-law doctrines well-established in 1871 is striking. Whatever it may say, the Court does not adhere to the common-law as it stood in 1871. Nonetheless, the Court continues to deny that it can make—and has been making—federal common-law pursuant to §1983. This reticence is unnecessary. Congress left all but the most basic questions of liability unresolved when it enacted §1983. It anticipated that the common law would fill the gaps and in no way suggested that the Courts should not depart from the common-law as it existed in 1871.[69]

---

[66]See, *e.g.*, Procunier v. Navarette, 434 U.S. 555, 561–62 (1978); Harlow v. Fitzgerald, 457 U.S. 800 (1982).

[67]See, *e.g.*, Imbler v. Pachtman, 424 U.S. 409, 424–25 (1976).

[68]See, *e.g.*, Malley v. Briggs, 475 U.S. 335 (1986); Tower v. Glover, 467 U.S. 914 (1984); Wood v. Strickland, 420 U.S. 308, 318–22 (1975); Scheuer v. Rhodes, 416 U.S. 232, 242–49 (1974). In *Malley* and *Tower*, the Court did explain that the " 'initial inquiry is whether an official claiming immunity under §1983 can point to a common-law counterpart to the privilege he asserts,' " and that if such a privilege is found to exist, " 'the Court next considers whether §1983's history or purposes nonetheless counsel against recognizing the same immunity in §1983 actions.' " *Malley*, 106 S.Ct. at 1095 (quoting *Tower*, 467 U.S. at 920). Although this tells us the order in which to ask questions about history and policy, it does not explain what in "§1983's history or purposes" will trump the common-law or why. Nor does this description explain the cases in which history but not policy or policy but not history was relied upon.

[69]*Cf.* Kreimer, note 64 *supra*, at 630. In Smith v. Wade, 461 U.S. 30 (1983), the Court held that a plaintiff could recover punitive damages against state officials who acted with reckless indifference to plaintiff's federal rights. Both Justice Brennan's opinion for the Court and Justice Rehnquist's dissent included extensive discussion of nineteenth-century common-law authorities. In a separate dissent, Justice O'Connor came close to advocating this approach to interpreting §1983. She agreed that it made sense to look to the common-law as it existed in 1871 "when there was a generally prevailing rule of common law, for then it is reasonable to assume that Congressmen were familiar with that rule and imagined that it would cover

III. An Introduction to the Economic Analysis

The conclusion that *Monell* is unsound and that the rules of municipal liability should be developed as part of the federal common law obviously does not establish who should incur liability when a municipal employee commits a tort. Should liability be imposed on the employee, the municipality, or both? We now turn to familiar tools of economic analysis to explore this problem.[70]

Put simply, economic analysis asks how to design a liability rule that will maximize the net economic value of municipal activity—the excess of its economic benefits over its economic costs. This inquiry, in turn, requires attention to three components of economic value. The first component is the efficiency of the precautions or deterrent measures that result under alternative liability rules. This is really a rather simple notion: liability rules create incentives to take precautions against accidental injuries and stand as a deterrent to intentional harms. These precautions and deterrent measures produce benefits in the form of a reduction in the number and magnitude of injuries, but they also impose costs on the individuals and institutions subject to liability. Economic analysis undertakes to identify the net gain from precautions or deterrent measures under alternative liability rules and, other things being equal, prefers the rule for which the excess of benefits over costs is at a maximum.

---

the cause of action they were creating." But, she continued, "when a signifieant split in authority existed, it strains credulity to argue that Congress simply assumed that one view rather than the other would govern. . . . Once it is established that the common law of 1871 provides us with no real guidance on this question, we should turn to the policies underlying §1983 to determine which rule best accords with those policies." *Id.* at 93.

[70]A number of recent papers analyze rules of vicarious liability from the economic perspective, but do not directly address the liability of municipalities. See Kraakman, Corporate Liability Strategies and the Costs of Legal Controls, 93 Yale L. J. 857 (1984); Kraakman, Gatekeepers: The Anatomy of a Third-Party Enforcement Strategy, 2 J. L. Econ. & Org. 53 (1986); Landes & Posner, Joint and Multiple Tortfeasors: An Economic Analysis, 9 J. Legal Stud. 517 (1980); Sykes, The Economics of Vicarious Liability, 93 Yale L. J. 1231 (1984) [hereinafter The Economics of Viearious Liability]; Sykes, The Boundaries of Vicarious Liability: An Economic Analysis of the Scope of Employment Rule and Related Doctrines, 101 Harv. L. Rev. 563 (1988) [hereinafter The Boundaries of Vicarious Liability]. Some of the principles developed in this literature apply directly to the public sector, but others do not—as discussed below, the imposition of viearious liability on governmental entities raiscs several difficult issucs that do not arise in the private sector. Economic issues relating to municipal liability are addressed briefly in Kornhauser, An Economic Analysis of the Choice Between Enterprise and Personal Liability for Accidents, 70 Calif. L. Rev. 1345 (1982).

A second component of economic value is the effect of alternative liability rules on scale of activity. Actors in the marketplace—individual or corporate, public or private—are limited in their ability to carry on activities by the resources available to them. Damages payments consume resources and thus tend to affect the scale of activity of those who are liable for damages (as well as those to whom they are paid). Other things being equal, economic analysis will prefer the liability rule that adjusts everyone's scale of activity so that the marginal benefit of an increase in scale is equal to its marginal cost—if such a rule exists.

The third component of value is the effect of different liability rules on the efficiency of risk bearing. Some individuals or organizations are better able to bear risk than others because, for example, they can better diversify the risk or can more easily lay it off on a superior risk bearer (such as an insurance company). Other things being equal, economic analysis will prefer the liability rule that allocates risk to institutions that are close to risk neutral and that shifts risk away from risk-averse individuals.

The importance of these considerations to the choice of liability rules seems self-evident.[71] The real question is whether the economic analysis is dispositive, or whether other, non-economic considerations also require attention. For example, economic analysis makes no allowance for purely distributional objectives like the provision of compensation to injured persons without regard to the effect of compensation on prevention, scale of activity, and risk bearing. Arguably, the pursuit of compensation for its own sake should not play an important role in the common-law jurisprudence of §1983. The legislative history of §1983 makes abundantly clear that Congress enacted §1983 to deter state officials from depriving state residents, particularly the newly freed slaves and Southern Republicans, of federally protected rights; there was no talk of enacting this statute to provide needed compensation to victims of constitutional torts.[72]

---

[71]The congruence between the economic theory of liability and the common law of torts has been well documented, see, *e.g.*, Landes & Posner, note 7 *supra;* Posner, Economic Analysis of Law (3d ed. 1986), including the considerable congruence between economic efficiency and the common law of vicarious liability, Sykes, The Economics of Vicarious Liability, note 70 *supra.*

[72]See Globe, note 24 *supra, passim;* see also Developments in the Law, Section 1983 and Federalism, 90 Harv. L. Rev. 1133, 1142–52 (1977).

Nonetheless, some readers may find our analysis incomplete as a normative basis for policymaking due to the omission of express attention to "compensation" or some other conceivable policy objective. In any event, the issues that we address are by all accounts central to—if perhaps not exhaustive of—the policy debate.[73]

IV. Rules of Official Immunity

The vicarious liability of employers in the private sector is almost always joint and several with their employees. With very few exceptions, plaintiffs cannot reach the employer of the tortfeasor unless they can also establish the tortfeasor's individual liability. Of course, the individual liability of the injurer is not sufficient to allow the plaintiff to reach the injurer's employer—rules like the scope-of-employment rule and the independent contractor rule act as limitations on the scope of the employer's vicarious liability. Thus, depending upon the circumstances in which an employee commits a tort, the employee may be liable alone or the employer may be jointly and severally liable with the employee, but liability on the employer alone is extremely uncommon.

The existing rules of liability that apply to municipalities and to their employees under §1983 are often parallel. A plaintiff may seek damages from an employee who committed the tort. But, as in the private sector, the liability of the employee may not be sufficient for municipal liability since the plaintiff cannot recover from the municipality without also satisfying the policy rule of *Monell.* In these cases, the policy rule functions like the familiar limits on vicarious liability mentioned above.

Another class of §1983 cases finds little parallel in the private sector. Rules of official immunity sometimes allow public officers to escape individual liability under §1983. But *Owen v. City of Independence*[74] provides that municipalities cannot raise official immunity as a defense to their own liability. As a result, municipalities

[73]There is, of course, much more that could be said about the role of economics in developing legal rules. See, *e.g.*, Dworkin, Is Wealth a Value, 9 J. Legal Stud. 191 (1980); Kronman, Wealth Maximization as a Normative Principle, 9 J. Legal Stud. 227 (1980); Posner, The Value of Wealth: A Comment on Dworkin and Kronman, 9 J. Legal Stud. 243 (1980); Posner, Utilitarianism, Economics, and Legal Theory, 8 J. Legal Stud. 103 (1979).

[74]445 U.S. 622 (1980).

may incur liability under §1983 even if the individual tortfeasor is immune. Here, too, of course, the municipality's liability is contingent on the plaintiff's ability to satisfy *Monell*'s policy rule.

Our analysis will not question the efficiency of these rules of immunity where they apply. The doctrine of official immunity raises a number of difficult legal and economic issues,[75] but we shall assume that rules of official immunity are immutable and direct our inquiry to how the rule of vicarious liability should be designed given the existing rules of immunity. We must digress briefly, therefore, to sketch the limits of official immunity.

Certain classes of individual defendants are "absolutely" immune from damages actions under §1983. Specifically, absolute immunity has been conferred upon state legislators when acting in a legislative capacity,[76] upon judges when not acting in the clear absence of jurisdiction,[77] and upon prosecutors when acting as advocates in the criminal process.[78]

Otherwise, all public officials can assert a defense of qualified immunity under §1983.[79] At first, this qualified immunity had both a subjective and an objective element; an official could be held liable for committing a constitutional tort if the official "knew or reasonably should have known that the action he took . . . would violate the constitutional rights of the [plaintiff], or if he took the action with malicious intention to cause a deprivation of constitutional rights or other injury. . . ."[80] Because this formulation,

---

[75]See, *e.g.*, Epstein, Private Law Models for Official Immunity, 42 L. & Contemp. Probs. 53 (1978).

[76]Tenny v. Brandhove, 341 U.S. 367 (1951); see also Lake Country Estates, Inc. v. Tahoe Regional Planning Agency, 440 U.S. 391 (1979) (absolute immunity for regional legislators acting under authority of interstate compact).

[77]Stump v. Sparkman, 435 U.S. 349 (1978); Pierson v. Ray, 386 U.S. 547 (1967).

[78]Imbler v. Pachtman, 424 U.S. 409 (1976). In both *Imbler*, 424 U.S. at 430–31, and *Pembaur*, 475 U.S. at ___, 106 S.Ct. at 1295 n.2, the Supreme Court expressly reserved judgment on whether a prosecutor is entitled to absolute immunity when he acts as an administrator or investigator rather than as an advocate.

[79]Although the Supreme Court has not issued a blanket holding that all state and local officials are entitled to at least qualified immunity, it has extended such immunity to every public official who has sought it. See, *e.g.*, Pierson v. Ray, 386 U.S. 547 (1967) (police officers); Scheuer v. Rhodes, 416 U.S. 232 (1974) (executive officials); Procunier v. Navarette, 434 U.S. 555 (1978) (prison officials); O'Connor v. Donaldson, 422 U.S. 563 (1975) (mental hospital administrators); Wood v. Strickland, 420 U.S. 308 (1975) (school board members).

[80]*Id.* at 322. Although the Court in *Wood* limited its holding to school board members, subsequent cases relied upon *Wood* as a general statement of the qualified immunity test. *E.g.*, Procunier v. Navarette, 434 U.S. at 562–63; see also Harlow v. Fitzgerald, 457 U.S. 800, 815, n.25 (1982).

particularly its subjective element, made it difficult for public officials to obtain summary judgment, the Court revised the qualified immunity standard in *Harlow v. Fitzgerald.*[81] *Harlow* eliminated the subjective element and made the objective element more favorable to defendants. Government officials now enjoy immunity from liability for civil damages "insofar as their conduct does not violate clearly established statutory or constitutional rights of which a reasonable person would have known."[82] Public officials have a duty to follow clearly settled law, but are immune from suit if their actions were of uncertain legality under an objective standard when they were taken.[83] Qualified immunity is also referred to as "good faith" immunity: acts that satisfy the *Harlow* test are said to be acts in "good faith"; acts that do not meet the test are said to be in "bad faith."

As noted, municipalities cannot claim the same immunity as their officials under §1983.[84] This is true whether that immunity is absolute or qualified.[85] The vast majority of municipal liability cases, however, involve acts by officers who are entitled only to good faith immunity.[86]

---

[81]457 U.S. 800 (1982).

[82]*Id.* at 818. See also Davis v. Scherer, 468 U.S. 183 (1984).

[83]*Cf.* Mitchell v. Forsyth, 472 U.S. 511, 530–35 (1985); Bennis v. Gable, 823 F.2d 723, 732–33 (3d Cir. 1987); Llaguno v. Mingey, 763 F.2d 1560, 1569 (7th Cir. 1985). See generally Nahmod, note 5 *supra*, at §8.06.

[84]Owen v. City of Independence, 445 U.S. 622 (1980).

[85]Reed v. Village of Shorewood, 704 F.2d 943, 953–54 (7th Cir. 1983); Hernandez v. City of Lafayette, 643 F.2d 1188, 1194–1200 (5th Cir. 1981).

[86]Prior to the Supreme Court's decision in *Lake Country Estates*, 440 U.S. 391 (1979), local—as opposed to state—legislators were given only qualified immunity. See, *e.g.*, Thomas v. Younglove, 545 F.2d 1171 (9th Cir. 1976); Lane v. Inman, 509 F.2d 184 (5th Cir. 1975); Curry v. Gillette, 461 F.2d 1003 (6th Cir.), cert. denied, 409 U.S. 1042 (1972); Nelson v. Knox, 256 F.2d 312 (6th Cir. 1958). In *Lake Country Estates*, which dealt with the immunity of regional legislators acting under an interstate compact, the Court left the issue of local legislators' immunity open; Justice Marshall noted in dissent that, as a practical matter, the Court's reasoning resolved the question in favor of absolute immunity. 440 U.S. at 408–09 (Marshall, J., dissenting). Since that decision, a number of courts of appeals have held that local legislators are entitled to absolute immunity. See, *e.g.*, Aitchison v. Raffiani, 708 F.2d 96 (3d Cir. 1983); Reed v. Village of Shorewood, 704 F.2d 943 (7th Cir. 1983); Hernandez v. City of Fafayette, 643 F.2d 1188 (5th Cir. 19981); Bruce v. Riddle, 631 F.2d 272 (4th Cir. 1980). See generally Nahmod, note 5 *supra*, at §7.05. Nonetheless, these cases are relatively rare. Also rare are cases in which a plaintiff sues a municipality for the act of a municipal judge or a local prosecutor. The combined number of cases in all three of these categories does not compare to the number of eases filed against police officers and other municipal officials who have only good faith immunity.

V. The Scope of Municipal Liability for "Bad Faith" Acts by Municipal Employees

Setting aside for the moment any consideration of "good faith" acts, and assuming that a cause of action against the individual official for bad faith acts is efficient,[87] we now examine whether the policy rule of *Monell* is an economically sensible criterion for the imposition of vicarious liability on municipalities. We conclude it is not. The application of common-law agency principles, including the doctrine of *respondeat superior*, would likely produce improvement. Moreover, we contend that a negligence-based approach to municipal liability for bad faith acts might do better still.

A. THE SIGNIFICANCE OF THE CHOICE BETWEEN PERSONAL LIABILITY AND VICARIOUS LIABILITY

It is perhaps tempting to assume that the choice between vicarious liability (a regime in which employers and employees are jointly and severally liable) and personal liability (a regime in which only employees are liable) is always important on the premise that a judgment against the employee under personal liability will have little or no impact on the employer. Recent work on the economics of vicarious liability, however, suggests that the choice between vicarious liability and personal liability has no economic consequences if two conditions prevail: (1) the employee has sufficient assets to pay any conceivable judgment against him in full (perhaps with the aid of insurance or contractual indemnification from the employer), and (2) the transaction costs of employment contracts that include terms to allocate liability between the employer and the employee are small.[88] The intuition that underlies this proposition is quite simple.[89]

Suppose that a rule of personal liability prevails, so that only the employee incurs liability for the employee's torts. In negotiating

---

[87]The assumption that the cause of action against the individual employee is efficient implies that economic welfare is greater when the cause of action is allowed that when it is barred. Without this assumption, potentially difficult second-best issues complicate the analysis.

[88]See Sykes, The Economics of Vicarious Liability, note 70 *supra*, at 1239–43.

[89]The analysis assumes that there are no systematic errors in the assignment of liability or the computation of damages under either personal liability or vicarious liability: in either regime, expected liability is equal to the actual costs suffered by injured parties.

an employment agreement, the employer and the employee can nonetheless include provisions that allocate the risk of liability judgments against the employee between the employer and the employee. Perhaps the employer will agree to assume some or all of the risk of liability, or perhaps the employee will agree to bear this risk in exchange for higher wages or other benefits. The precise terms of this agreement will depend upon each party's attitude toward risk-bearing, upon the need to create proper incentives for the employee, upon each party's bargaining power, and so on.

Now suppose that the liability rule is changed to vicarious liability. The employer and the employee must renegotiate their employment agreement to take account of the fact that judgments may now be rendered against the employer. The total amount paid to the plaintiff by the employer and the employee remains the same, however, for if employees can pay adverse judgments in full under personal liability, all judgments will be satisfied under either liability rule. That being true, the renegotiated employment agreement under vicarious liability *can* exactly replicate the division of liability agreed to by the employer and the employee under personal liability.

Moreover, if the second condition above is met, if the transaction costs of replicating the division of liability and all other terms and incentives contained in the employment agreement negotiated under personal liability are small, then the employment agreement under vicarious liability *will* tend to replicate the preferred agreement under personal liability.[90] At least the change to vicarious liability is unlikely to have any systematic or predictable effect on the employment agreement.

Whichever rule prevails, then, injured parties are fully compensated, the incentives facing employees are likely to be the same,

---

[90]Of course, the analysis works in reverse if the liability rule changes from vicarious liability to personal liability, thus establishing the equivalence of the two regimes. Formal models of bargaining developed by game theorists typically embody an assumption—known as the "independence of irrelevant alternatives"—that leads directly to this result. See, *e.g.*, Nash, The Bargaining Problem, 18 Econometrica 155 (1950); Sykes, The Economics of Vicarious Liability, in Two Essays in the Economics of Law (unpublished Ph.D. dissertation 1987). One can also show that if employees can pay all judgments in full under personal liability and the transaction costs of contracting are negligible, then any employment agreement that is Pareto optimal from the perspective of the employer and the employee under personal liability is also Pareto optimal from their perspective under vicarious liability. *Ibid.*; Kornhauser, note 70 *supra*.

and the ultimate allocation of risk (in contrast to the initial allocation created by the legal rule) is likely to be the same. It follows that the efficiency of resource allocation is invariant to the liability rule.

This analysis seems at first to be equally applicable to employment relationships in the public and private sectors. One need only assume that the employer and the employee each have preferences among the alternative employment agreements that jointly determine, along with each party's bargaining power, the terms of their agreement. Then, if the mutually preferred employment agreement under one liability rule can be reconstructed at little cost under the other rule, the choice between the two rules is unlikely to have any systematic effect on the terms of the employment relationship or the resulting allocation of resources.

This conclusion is at odds with recent literature on governmental liability and immunities. This literature implies that, even if employees are able to pay judgments against them in full, and even if the transaction costs of employment agreements are low, a rule of personal liability will have a perverse effect on the incentives and productivity of government workers.[91] Employees in the public sector, the argument runs, perform tasks that benefit the public as a whole, not just themselves or the organization that employs them. Personal liability, by contrast, is a cost that is borne entirely by the employee. Personal liability thus encourages overcautious behavior or inaction by the employee: while the employee enjoys all the benefits associated with his reduced exposure to civil liability, the costs of excessive caution or inaction fall on the public as a whole. Proponents of this argument conclude, therefore, that personal liability is undesirable, and implicitly assume that the adverse effects of personal liability will not be eliminated by contract (for example, by the use of indemnity agreements). They recommend greater immunity for government employees, coupled with expanded governmental liability.

This analysis is flawed. All employers, public or private, face incentive problems. It is usually too costly for employers to observe the behavior of each employee at all times, and thus impossible to

[91]See, *e.g.*, Mashaw, Civil Liability of Government Officers: Property Rights and Official Accountability, 42 L. & Contemp. Probs. 8, 26–28 (1978); Schuck, Suing the Government (1983); Schuck, Suing Our Servants: The Court, Congress, and the Liability of Public Officials for Damages, 1980 Supreme Court Review 281.

design an incentive structure that perfectly harmonizes the behavior of employees with the interests of the employer. The result is the familiar problem of "agency costs," the costs of shirking, of imprudence, of overcaution, of inaction, and so on. To a large extent, these costs fall on the employer whether the employer is public or private.

Because employees' incentives are seldom perfectly aligned with employers' interests, the imposition of personal liability on an employee may lead to an exercise of caution that is excessive from the employer's perspective:[92] the employee will perceive benefits from excessive caution in the form of reduced exposure to liability, while the costs of excessive caution—decreased productivity—fall, in the first instance, on the employer. The employer can respond to this problem by altering the employee's incentive structure to encourage him or her to perform more desirably. For example, if a truck driver for Sears is personally liable for his or her motor vehicle torts, Sears can discourage overcautious driving by rewarding the driver for timely deliveries or penalizing late deliveries. Similarly, if a policeman for the City of Chicago is personally liable for the unintended use of excessive force, the City can try to discourage timidity or inaction in the pursuit of suspects by rewarding policemen with distinguished arrest records or penalizing policemen whose arrest records suggest ineffectiveness.

Of course, some incentive problems are more difficult than others. It may be easy to determine when a delivery is late, but quite difficult to ascertain when police conduct is timid. Thus, in our hypotheticals, Sears may find it easier to remedy the incentive problem than the City of Chicago (though Chicago can always ameliorate the problem by indemnifying its policemen). But that observation is irrelevant: the fact remains that it is in the interest of any employer, public or private, to utilize whatever cost-effective incentives are available to eliminate the undesirable consequences of personal liability.

Moreover, as explained above, the ultimate allocation of risk—and the attendant set of incentives facing employees—will not be

[92]This problem may not arise if personal liability attaches only to harms that the employee intends to cause. Because the employee need only refrain from deliberate misconduct to avoid liability, he or she has no incentive to become overcautious. Consequently, there may be no adverse effect on employee productivity. The possibility of frivolous lawsuits predicated on intentional misconduct, however, might induce overcaution even under these circumstances.

affected by the choice between personal liability and vicarious liability so long as judgments would be paid in full under either liability rule and the transaction costs of contracting are low enough to permit the employment agreement that would prevail under personal liability to be reconstructed under vicarious liability (or vice-versa). Under these conditions, the initial locus of liability simply does not affect the mutually preferred set of contractual incentives,[93] including the ultimate division of liability between the employer and the employee.

To be sure, the incentives contained in the employment contract may not be socially optimal. In the public sector, for example, poor performance by governmental employees may impose considerable costs on members of the general public while imperfections in the political process insulate public agencies from any substantial pressure to eliminate these costs. Consequently, employment agreements in the public sector may work poorly at motivating employees to serve the public interest. But such problems with the performance of public sector employees are not affected by the choice between personal liability and vicarious liability when employees are able to pay adverse judgments in full and the transaction costs of contracting are low—the terms of employments agreement, including the existence or non-existence of indemnification agreements and the like, will be the same under either regime. Of course, these two conditions may not be satisfied, in which case the choice between personal and vicarious liability can have significant effects on resource allocation, problems to which we now turn.

B. THE EFFICIENCY OF VICARIOUS LIABILITY WHEN THE EMPLOYEE IS JUDGMENT-PROOF

Municipal employees are often unable to pay adverse judgments in full. Judgments in §1983 cases are frequently quite large; amounts

[93]The concept of "incentives" here is quite broad. For example, suppose that a vicariously liable employer decides to establish a training program to instruct employees on precautions against accidents. The employer finds the program desirable because its cost is less than the reduction in his expected liability. Would the training program also be desirable under personal liability? If employees can pay judgments against them in full, the answer is yes. Employees can finance the program through a reduction in wages, and it is advantageous for them to do so because the cost is again less than the reduction in their expected liability. Unless transaction costs prevent the employees from bargaining for the program, then, it will be established whatever the liability rule.

in excess of several hundred thousand dollars are not uncommon.[94] Plainly, such judgments will usually exceed the personal assets of municipal employees.[95]

The fact that municipal employees are often judgment-proof may have profound effects on resource allocation. It can affect the scale of municipal activity; the degree of supervision, training, and other incentives that discourage constitutional torts; the productivity of municipal employees; and the efficiency of risk allocation. To understand these effects, and their implications for the choice between personal and vicarious liability, it is instructive to begin by examining the inefficiencies that arise when employees are judgment-proof under a regime of personal liability.

1. *The inefficiencies of personal liability. a) The private sector.* In the private sector, the inefficiencies of personal liability for torts when employees are judgment-proof may be readily identified. Under such circumstances, a rule of personal liability allows the business enterprise to "externalize" costs of doing business by passing off all or part of the losses occasioned by the commission of a tort onto the victim.[96] One result of cost externalization is that the incentive to exercise care to avoid the occurrence of torts may be inadequate, either for the employer or the employee. Alternatively, even though

[94]*Cf.* Nahmod, note 5 *supra*, at §4.03.

[95]Of course, municipal employees exposed to the risk of large judgments under a rule of personal liability may seek employment agreements that provide indemnification. Indeed, some municipal employees are indemnified by their state governments. See, e.g., N.Y. Pub. Off. Law §18 (McKinney 1984). Municipalities will be reluctant to provide indemnification for "bad faith" behavior that consists of knowing, intentional torts by the employee; the attendant moral hazard would likely be unacceptable. E.g., *id.* at §18(4) (b) (excluding indemnification for "intentional wrongdoing or recklessness"). But many bad faith acts that give rise to liability are merely negligent—the failure of a policeman in the heat of the moment to abide by the strictures of the Fourth Amendment, for example, or the unwitting failure of supervisors to provide constitutionally required process before discharging a subordinate. Employees may succeed in obtaining indemnification for liability that arises from such behavior. By agreeing to indemnify employees, the municipality (or its state government) in effect imposes vicarious liability on itself by contract. Any judgment will generally be satisfied in full, and, as suggested above, the choice between personal liability and vicarious liability likely becomes a matter of indifference. The "policy rule" of *Monell* has no practical effect.

[96]This discussion assumes that the tort is "caused" by the employment relationship in the following sense: If the employment relationship dissolves and the employee remains unemployed, the probability of the tort is reduced to zero. Under this assumption, the tort is properly viewed as a cost of production for the business enterprise. See Sykes, The Boundaries of Vicarious Liability, note 70 *supra*.

a judgment-proof employee does not bear the full cost of the injuries that he causes, the prospect that a judgment could render him bankrupt may motivate the employee to exercise an inefficiently high level of care if he is risk averse. If the employer cannot eliminate this incentive for excessive care except through indemnification—potentially very costly to the employer—the employer may decide simply to tolerate the excessive level of care.

In addition, if either employees or prospective injured parties are risk averse, the allocation of risk under personal liability may be inefficient. Risk allocation could be improved if the risk of injury were shifted to a more efficient risk bearer such as an insurance company or, in many cases, the employer.

Finally, in a competitive market, the added profitability that results from cost externalization attracts new entry and encourages the expansion of existing firms until the prevailing price falls to the level of private marginal costs. Because the externalization of liability implies that private marginal costs are below social marginal costs, the resulting scale of business activity is excessive.[97]

Despite these inefficiencies, the externalization of liability can prove worthwhile from the perspective of the employer and the employee. The resulting increment in expected profits to the business enterprise can be divided between the employer and the employee (in the form of higher wages) to make them both better off at the expense of the injured party whose judgment goes wholly or partially unsatisfied. For this reason, rational profit-maximizing or utility-maximizing employers and employees will often enter employment agreements that do not provide the employee with indemnification and that expose the employee to a risk of bankruptcy.

b) The public sector. To a considerable extent, the inefficiencies and incentives for liability externalization that arise in the private sector under a rule of personal liability also arise when the employer is a municipality. But there are important differences as well.

Consider first the incentive to externalize liability. As explained above, cost externalization is often profit-maximizing for a private firm. With the possible exception of certain independent, proprietary government entities, however, municipal agencies are not usually motivated by the desire to maximize profits.

[97]But see note 113 *infra*.

Yet municipalities (or, more accurately, municipal officials) are to some extent motivated by a desire to provide public services at minimum cost. Most elected officials confront demands for both increased levels of public services and lower taxes. Although the response to these pressures may be somewhat unpredictable and imperfect, opportunities for cost reduction are likely to be explored. The externalization of liability is one such opportunity.

Of course, any costs that are "externalized" will fall to a large extent on citizens of the municipality—the voters. For a variety of reasons, however, voters may not act as an effective check on liability externalization and the inefficiencies that may accompany it even if they bear the brunt of the externalized costs. Injuries caused by municipal employees may be relatively low-probability events about which most voters are poorly informed, and which consequently do not have much influence on voting. Moreover, even well-informed voters probably view the problem of injuries caused by municipal employees as unimportant by comparison to other issues, and thus of little moment in deciding how to vote. By contrast, the tax assessment is all too familiar to most voters, many of whom will reward officials who minimize it.

Finally, and perhaps most importantly, the costs of uncompensated injuries may fall disproportionately on segments of the population with limited political power. The costs of police misconduct, for example, may fall primarily on the poor, on minorities, and on individuals with prior convictions, while the costs of compensating such injuries through tax revenues will be more broadly dispersed. The result may well be that a majority of the electorate, even if well-informed, will prefer liability externalization despite the attendant inefficiencies.

Consequently, even though municipalities will rarely be motivated to externalize liability by the pursuit of "profit," powerful incentives to take advantage of the opportunity to externalize liability may nonetheless arise. The fact that liability externalization occurs in the public sector rather than the private sector warrants no presumption that it is efficient or otherwise in the overall public interest.

Given the incentive to externalize liability that may arise on the part of municipalities, then, will externalization lead to the same inefficiencies as in the private sector? The answer is yes, and no.

First, as in the private sector, cost externalization by municipalities and their employees may result in inadequate incentives to take precautions against wrongdoing. Employees may exercise inefficiently little care in performing their duties or, with respect to intentional harms, the level of deterrence may be inadequate.[98] Similarly, as in the private sector, the externalization of liability diminishes the incentives of municipalities to institute training, supervision and monitoring, or otherwise to dissuade wrongdoing through injury-contingent contractual penalties. On the other hand, it is conceivable that municipal employees may exercise inefficiently high levels of care due to the conjunction of risk aversion with personal liability, or to the fact that the burden of overcautious behavior falls on the general public and not on the employees. As noted, municipalities have an incentive to correct this problem, and the most obvious way to do so would be by indemnifying employees. But the costs of indemnification may be too high from the municipality's perspective (it requires forgoing the benefits of cost externalization), and effective alternatives to indemnification may not exist.

Although the problem of excessive care surely exists in the abstract, we doubt its significance with respect to "bad faith" constitutional torts. Many of these torts involve intentional harms, and others involve reckless behavior or other conduct that reflects complete inattention or indifference to constitutional requirements. It therefore seems unlikely that personal liability for such torts will often induce overcautious behavior or inaction, as the employee can avoid liability with minimal effort.[99] Rather, the problems of un-

---

[98]Bad faith constitutional torts may be either intentional or negligent. If a supervisor discharges a subordinate on the basis of race, for example, or a policeman deliberately brutalizes a suspect, the tort is plainly intentional. By contrast, if a policeman carelessly exceeds his authority under a search warrant, or a supervisor unthinkingly discharges an employee without an adequate hearing, the injury is not intentional but negligent or reckless.

[99]This is true of the factual issue on which §1983 claims are typically based as well as the question of immunity under *Harlow*. The factual component in §1983 cases invariably concerns intentional action by a state official, such as whether an official searched a plaintiff's home. The uncertain element in such cases is the legal effect of this intentional action and the official's knowledge of the law: should the official have known that he lacked probable cause to search? Until recently, claimed deprivations of due process were an exception to this rule and could be based on allegations that a government official acted negligently. Parratt v. Taylor, 451 U.S. 527 (1981). In Daniels v. Williams, 106 S.Ct 662 (1986), however, the Supreme Court overruled *Parratt* and held that injuries inflicted by governmental negligence do not violate the Due Process Clause. The Court reserved the question "whether

derinvestment in care and underdeterrence are probably far more serious inefficiencies of personal liability for these torts.

A second consequence of cost externalization that may arise in the public sector as well as in the private sector is inefficiency in risk allocation. The costs of injuries fall on the victim and the individual wrongdoer who, as in the private sector, are often risk averse. Here too, then, the efficiency of risk bearing can be improved by shifting the risk to a risk neutral (or less risk averse) entity. Of course, even a risk averse wrongdoer is an efficient "risk" bearer in cases involving intentional injuries[100] and, as noted,[101] many bad faith constitutional torts involve intentional misconduct. But if the wrongdoer is unable to pay judgments against him in full, the risk still falls on the risk averse victim in many cases, and risk allocation remains inefficient.

With respect to the third possible inefficiency of personal liability in the private sector, distortion in the scale of activity, the situation in the public sector is significantly different. As noted above, economic theory predicts that cost externalization in a competitive market will lead (other things being equal) to an inefficiently large scale of activity as prices fall below social marginal costs of production. No such prediction can be made about the effects of cost externalization on the scale of governmental activity for the simple reason that economists have no generally accepted theory of how the scale of public sector activity is determined in the first place.

If the scale of activity is determined by majority vote, for example, the preferences of the "median voter" might be decisive.[102] Whether the scale of government activity established by the "median voter" is efficient depends upon a variety of factors that determine how the costs and benefits of government activity are dis-

---

something less than intentional conduct, such as recklessness or 'gross negligence,' is enough to trigger the protections of the Due Process Clause." *Id.* at 667 n.3. As to "good faith" torts, see notes 122–32 *infra* and accompanying text.

[100]If the employee knows that particular behavior will produce an actionable injury with certainty, and knows that he can avoid the injury with certainty by refraining from the behavior in question, then the employee does not bear any "risk" if he incurs personal liability for such behavior. Such a deterministic relationship between the behavior and the existence of an actionable wrong is characteristic of most "intentional" misconduct. It follows that aside from any risk of exposure to baseless litigation, there is no inefficiency in risk allocation if the wrongdoer bears the full cost of any injury that he "intentionally" causes.

[101]See notes 98–99 *supra* and accompanying text.

[102]See, *e.g.*, Atkinson & Stiglitz, Lectures on Public Economics 299–326 (1980).

tributed among members of the voting public. If the benefits of government activity accrue to a minority of citizens but the costs are widely dispersed, for example, then the scale of activity determined by majority vote may be inefficiently small. The reverse possibility also exists.

To complicate matters further, direct majority voting only rarely determines the scale of government activity. More commonly, the scale of activity is determined by elected representatives and appointed bureaucrats who respond to complex and widely divergent incentives. A variety of theories have been advanced that directly or indirectly purport to explain the resulting scale of government activity—theories of budget-maximizing bureaucrats, theories of voters who "vote with their feet" by relocating to find a preferred mix of public services, and many others.[103] Some of these theories predict that the scale of government activity will tend to be inefficiently high while some predict the opposite; some yield no determinate prediction about the efficiency of scale.[104]

Assuming, therefore, that cost externalization by the public sector tends to increase the scale of government activity,[105] it is unclear whether the resulting increment in scale will enhance or worsen the efficiency of resource allocation. In some cases, cost externalization may cause government activity to expand from an already excessive base; in other cases, the expansion may offset conditions that would otherwise produce an inefficiently small scale of activity.

Thus, at least two of the inefficiences associated with a rule of personal liability when employees are judgment proof are found in the public as well as the private sector: the reduction of incentives to avoid committing torts and an inefficient allocation of risk. With respect to the third inefficiency in the private sector—an inefficient

---

[103]For a partial survey, see Mueller, Public Choice (1979).

[104]The Niskanen model of the budget-maximizing bureaucrat, for example, predicts overprovision of public services. Mueller, note 103 *supra*, at 156–63. The theory of public goods by contrast, implies some tendency for under-provision of public goods due to free-rider problems. See, *e.g.*, Malinvaud, Lectures on Microeconomic Theory 211–19 (1972).

[105]Whatever the details of the public choice process, it seems likely that an increase in the cost of government services to the public treasury will usually (though perhaps not always) lead voters or their representatives to economize on those costs through some reduction in the scale of government activity. Conversely, a reduction in the cost of government services to the public treasury will tend to produce an expansion in the scale of government activity.

increase in the scale of activity—no prediction can be made with respect to the public sector.

2. *The consequences of vicarious liability.* Under the common law of torts, the imposition of vicarious liability on employers usually occurs pursuant to the doctrine of *respondeat superior.*[106] *Respondeat superior* is a form of "strict" liability: the plaintiff need not show that the employer was negligent or otherwise culpable, and, once the employee's liability is established, the derivative liability of the employer follows without more.

In some cases, however, the employer cannot be held liable unless the plaintiff proves that the employer breached a duty to the plaintiff, for example, the limited duty of an employer to control the conduct of an employee acting outside the scope of employment.[107] Derivative liability on the basis of negligent failure to supervise a wrongdoer or otherwise to prevent a wrong is also quite common outside the employment relationship.[108] Strictly speaking, of course, such liability is not "vicarious" at all, as the derivatively liable party breached its own duty of care. For convenience of exposition, however, we refer below to two types of "vicarious" liability: strict vicarious liability and vicarious liability based on negligence.

More precisely, we understand "strict" vicarious liability to be the application to municipalities of the same common-law agency principles that govern the liability of private sector employers. The doctrine of *respondeat superior* is the most important of these principles.

A "negligence" approach to the liability of the municipality would, by contrast, require the plaintiff to prove that municipal employees with supervisory authority over the wrongdoer failed to adopt some cost-effective measure to avert the constitutional tort and that the absence of such a measure proximately caused the injury. For example, if the constitutional tort arose in connection with an illegal police search, the plaintiff might show that the police officers were inadequately trained or supervised or that the police department

---

[106]See generally Prosser & Keeton on the Law of Torts, note 1 *supra*, at 501–08.

[107]See Restatement (Second) of Torts §317 (1965).

[108]See Sykes, The Boundaries of Vicarious Liability, note 70 *supra*. For example, the version of the Sherman Amendment that was finally passed imposes liability on individuals who know that someone else will commit a constitutional tort and have power to prevent it but fail to act. See 42 U.S.C. §1986. There are many other examples.

neglected to establish reasonable internal policies to deter illegal searches.[109]

To some, the negligence approach might seem peculiar—the municipality escapes liability for the wrong of one employee, while it incurs liability for the wrong of a second employee. But upon reflection, the result is not peculiar at all.

Personal liability on the active wrongdoer operates directly upon his incentives, but not upon the incentives of supervisors. And, because of transaction costs (discussed below) or because the active wrongdoer is judgment proof, personal liability may produce little or no indirect pressure for cost-effective supervision. To generate such incentives under these circumstances, the scope of liability must be expanded.

One option would be to impose personal liability on the negligent supervisors. We reject that option, principally because it would involve potentially intolerable litigation costs. Specifically, although plaintiffs might reasonably be expected to explain how better training, monitoring, or supervision of the tortfeasor could have prevented their injury, it might be extraordinarily difficult for them to identify which supervisory officials were responsible—indeed, a colorable claim of negligence might be advanced against numerous officials at various stages of the hierarchy. A rule imposing personal liability on negligent supervisors would thus tempt plaintiffs to implead any number of municipal officials. Each might well want his own attorney, and the ensuing litigation over which official was the "negligent" one would consume considerable resources. Compounding the problem is the fact that supervisors themselves may be judgment proof, so that the imposition of personal liability upon negligent supervisors may still fail to create adequate incentives for supervision.

We therefore conclude that incentives for cost-effective supervision within the municipal hierarchy can be created more efficiently by a rule that imposes liability on the municipality rather than upon negligent supervisors individually. The more difficult question is whether those incentives should be created through a rule of strict vicarious liability for bad faith torts, or whether the victims of bad faith torts should be required to show that the tort

[109]Justice O'Connor adopted a variation of this approach in her dissent from the dismissal of the petition for certiorari in City of Springfield v. Kibbe, 107 S.Ct. 114 (1987).

also resulted from an act of negligence somewhere within the administrative hierarchy.

Either type of vicarious liability can ameliorate certain inefficiencies that arise under personal liability when municipal employees are judgment-proof. Take the problem of underinvestment in care by the employee or the employer or the problem of underdeterrence of intentional harms. If, as is almost certainly the case, fiscal pressures produce incentives for municipalities to minimize the cost of delivering municipal services, strict vicarious liability will motivate the municipality to adopt cost-effective measures to reduce the incidence of misconduct.[110] But much the same incentives for taking cost-effective measures to prevent misconduct will arise if vicarious liability is imposed on the basis of negligence, assuming that "negligence" is defined in accordance with the Learned Hand test as the failure to take cost-effective precautions.

Indeed, by singling out negligent supervisory officials and identifying the measures that they should have taken, a negligence-based approach to vicarious liability might be more effective than strict vicarious liability at motivating cost-effective monitoring, training, and similar measures: negligence cases would generate a body of information about required precautionary measures for the guidance of other municipalities.

The negligence approach also has disadvantages. First, it requires an expenditure of resources to litigate the issue of negligence, although the total number of lawsuits under a negligence regime will likely be smaller.[111] Second, and in contrast to strict vicarious liability, the negligence approach places the court in the position of second-guessing municipal officials about what measures should be taken to guard against constitutional torts, a process that may introduce significant error costs. Finally, although both strict vicarious liability and vicarious liability based on negligence will ameliorate the inefficient allocation of risk that results under personal liability, strict vicarious liability appears to do this better. Strict

[110]These measures may include greater supervision of employees, better training programs, improved penalty/reward incentives conditioned on the occurrence/avoidance of misconduct, and so on. If the transaction costs of such measures are high, however, shifting liability from the employee to the employer may actually increase the incidence of negligent or intentional harms. See Section I-C *infra*.

[111]See Landes & Posner, note 7 *supra*, at 65–66.

vicarious liability automatically redistributes the risk of loss from typically inefficient risk-bearers (victims[112] and municipal employees) to a typically superior risk bearer that can distribute the risk broadly among the taxpaying public. Under the negligence approach, by contrast, losses are redistributed only when the municipality is shown to have been negligent.

Yet another difference exists between the two approaches: they are likely to have differing effects on the scale of municipal activity. In the private sector, a potential advantage of either strict or negligent vicarious liability is that it increases the degree of cost-internalization by business enterprises whose judgment-proof employees cause injuries. Other things being equal, this improves resource allocation by encouraging businesses to operate at a more efficient scale. And, because there is less cost-internalization under a negligence-based approach to vicarious liability than under strict vicarious liability, the scale of private sector activity that results from vicarious liability based on negligence would be less efficient (other things being equal[113]) than the scale of activity that results from strict vicarious liability.

In the public sector, however, it is unclear whether greater cost internalization by municipal agencies would, other things being equal, improve or worsen resource allocation. The problem lies in the issue discussed above: the scale of municipal activity resulting from political and bureacratic decisions may be too large or too small. We simply have no way of knowing. Therefore, even if greater cost internalization would reduce the scale of activity, it is impossible to know whether such a reduction would be beneficial.[114]

---

[112] First-party insurance is not an entirely satisfactory method of risk redistribution, as the injuries caused by constitutional torts are often uninsurable in the first-party insurance market. Loss of public employment and loss of liberty and income due to unlawful confinement are illustrative of these uninsurable injuries.

[113] Of course, other things may not be equal. Greater cost-internalization by injurers under strict vicarious liability accompanies reduced cost-internalization by victims. But in some cases, it may be more efficient for victims to reduce the scale of their activities than for injurers to reduce the scale of their activities. See, *e.g.*, Shavell, Strict Liability vs. Negligence, 9 J. Legal Stud. 1 (1980). Yet the observation in the text with respect to the difference between the public and private sectors remains valid. Whatever the desirability of cost internalization by victims, the greater cost internalization by injurers under strict vicarious liability has some benefit in the private sector (perhaps offset by other costs), but may have no benefits whatsoever in the public sector.

[114] In other words, a "second-best" issue arises with respect to cost-internalization in the public sector that does not arise in the private sector. Technically, this "second-best" issue

To summarize: either strict vicarious liability or vicarious liability based on negligence is an improvement over personal liability with respect to the efficiency of deterrent and precautionary measures to reduce the incidence of constitutional torts. Both would also likely improve the efficiency of risk allocation, but strict vicarious liability is probably better than a negligence-based approach in this regard. Finally, the greater degree of cost-internalization produced by strict vicarious liability has highly ambiguous effects on resource allocation. It would almost certainly lead to a greater reduction in the level of municipal services than the negligence-based approach, but the efficiency of this reduction is questionable. We therefore reserve judgment on the choice between the two approaches for the moment, pending an exploration of transaction cost issues.

It seems clear, however, that either approach is superior to personal liability when employees are judgment-proof and the transaction costs of contractual incentives are low (as assumed throughout this section). The only possible disadvantage of vicarious liability arises from the possibility that, in some instances, the greater degree of cost-internalization under vicarious liability could inefficiently reduce the scale of municipal activity. Yet, it is also possible that the increased cost-internalization under vicarious liability would efficiently reduce the scale of municipal activity. Hence, it seems that the economic case for pockets of personal liability must rest on transaction costs, if the case can be made at all.

C. THE PROBLEM OF TRANSACTION COSTS

Although vicarious liability may ameliorate some inefficiencies of personal liability by eliminating cost externalization, it may result in other inefficiences if certain transaction costs of employment agreements are siguificant. One possible inefficiency associated with vicarious liability, whether strict or negligent, is that the employee's incentive to avoid the occurrence of the wrong may be diluted, or at least the costs of motivating the employee to avoid the wrong will increase.

---

also complicates the analysis of precautionary behavior and deterrent measures under the alternative liability regimes. In particular, although either strict vicarious liability or vicarious liability based on negligence will motivate cost-effective precautions and deterrent measures, what is "cost-effective" may depend upon the scale of activity, and thus may differ between the two regimes. We assume throughout the analysis to follow, however, that such differences do not weigh systematically in favor of one regime or the other.

Under vicarious liability, successful plaintiffs tend to collect their judgments from the deep pocket (the municipal defendant) even if the individual wrongdoer remains jointly and severally liable. But if employees do not bear the costs of their wrongdoing, their incentive to avoid misconduct will decline. The municipality can avoid this decline only by introducing contractual incentives that will motivate precautions against accidental harms and deter intentional harms.

Absent transaction costs to negotiating and enforcing such contractual incentives, a municipality could establish adequate alternatives to personal liability. For example, the municipality can preserve the incentive to avoid wrongdoing that is created by personal liability with a clause in the employment agreement requiring the wrongdoer to indemnify the municipality for the consequences of the wrongdoer's acts.

But the limited empirical evidence suggests that employers very rarely pursue indemnity actions against their employees even when they have a legal or contractual right to indemnity.[115] To some extent, the unwillingness of employers to pursue indemnity actions may reflect implicit risk sharing agreements motivated by the risk aversion of employees or the existence of alternative incentive devices that are superior to indemnity. In that case, the unwillingness of employers to seek indemnity would not evidence any inefficiency of vicarious liability. It is also possible, however, that indemnity actions are simply not worth the effort, because the costs of bringing them and pursuing recovery thereafter may exceed the anticipated recovery from an employee with limited assets.[116] Under these conditions, the reduction in the incentives of employees to avoid wrong-

[115]See The Economics of Vicarious Liability, *supra* note 70, at 1243, and sources cited.

[116]. If an employee's assets are too meager to justify the pursuit of indemnity by the employer under vicarious liability, then a prospective plaintiff under personal liability may also find it unprofitable to bring suit. If so, then the imposition of vicarious liability will not dilute the employee's incentives to avoid wrongdoing. For a variety of reasons, however, plaintiffs may find it worthwhile to file suit even if the employer does not. The plaintiff may have an emotional or dignitary interest in filing an action that the employer lacks. Alternatively, the employer may decline to pursue indemnity for fear that it will disrupt otherwise amicable relations with the workforce—an indemnity action that sends an employee into personal bankruptcy could send a signal to the workforce that the employer has little interest in the personal welfare of his employees, affecting morale and productivity adversely.

doing may not be outweighed by other benefits, and vicarious liability may be inefficient.

Moreover, even if the employer can maintain the same incentive to avoid wrongdoing that exists under personal liability through indemnity actions or some other device, vicarious liability requires the employer to incur the transaction costs[117] of doing so. Vicarious liability also adds an additional party to litigation, and may thus increase litigation costs significantly. Unless these costs are offset by some other benefit of vicarious liability, such as a reduction in the number of wrongs committed due to greater monitoring and supervision by the employer, vicarious liability will ultimately reduce economic welfare. More generally, the economic benefits of vicarious liability (if any) are greater, the smaller the transaction costs to the employer of creating effective incentives for employees to avoid wrongdoing.

1. *The nature and magnitude of transaction costs.* A variety of factors affect the transaction costs of establishing contractual incentives to prevent misconduct. One important factor is the observability of employee performance. It is usually quite inexpensive to deter misconduct that the employer can cheaply observe before a wrong occurs: the employer simply intervenes to correct misbehavior before it causes injury. If behavior is unobservable or costly to observe, by contrast, ex-post rewards or penalties contingent upon the occurrence or non-occurrence of a wrong may be the only options available to establish proper incentives. Such ex-post incentives, however, may be quite costly. Consider, for example, the possibility of requiring the employee to indemnify the municipality: because litigation and other costs of pursuing an employee's assets are often quite high relative to the value of the assets, indemnity will often be uneconomical.

The expected duration of the employment relationship is another factor that affects the transaction costs of establishing incentives to

[117]The absolute magnitude of transaction costs is often less important than their relative magnitude. For example, the absolute costs of negotiating and enforcing a collective bargaining agreement between a municipality and its police force may be considerable, yet the existence of the agreement and of the attendant opportunity to bargain carefully on a wide range of issues may enable the municipality and its police officers to agree upon training, monitoring, and other incentive mechanisms that cheaply and effectively dissuade constitutional violations by the entire police force.

avoid misconduct. If the employee anticipates a long association with the employer and cannot easily secure equally attractive alternative employment, the employer can incorporate effective incentives against wrongdoing into routine decisions about career advancement—decisions about promotions, firings, salary increases, and so on. Such decisions must be made anyway, and it costs very little to condition them in part upon an employee's history of wrongdoing. If, however, the anticipated duration of employment is brief, or if equally attractive alternative employment is easily available, incentives pertaining to career advancement will likely be ineffective.

A third factor affecting transaction costs is the extent to which various employees confront the employer with similar or distinct incentive problems. If a large number of employees perform similar functions and pose similar risks of malfeasance, a single system of incentives that applies to all of these employees may dissuade misconduct satisfactorily, and the employer may achieve considerable "economies of scale" with such a system. If each employee performs distinct tasks, by contrast, a costly process of customizing the incentives for each employee may be necessary.

Finally, the employer's knowledge of the risk of misconduct and the opportunities to avoid it will affect the magnitude of transaction costs. If the employee performs a highly skilled function that the employer understands poorly, it may be quite expensive for the employer to design and enforce effective incentives against misconduct. If the risk of misconduct involves behavior that is quite familiar to the employer, the cost of instituting incentives is lessened.

2. *Implications for the rule of municipal liability.* As noted at the outset, the factual patterns that give rise to constitutional tort claims are tremendously diverse. Consequently, it is difficult to generalize about the transaction costs of incentives to avoid these torts. Two examples may be instructive.

Example (i): Police activity is perhaps the most frequent target of constitutional tort actions. Most of this police conduct occurs on the streets and is difficult for police supervisors to observe before the tort occurs, a factor that increases the transaction costs of preventing it. On the other hand, most police officers are career employees who are deeply concerned about prospects for promotion, and who cannot move easily to equally remunerative alternative employment. Cheaply administered rewards and penalties built into

career advancement decisions, therefore, may be quite effective at inducing appropriate behavior. In addition, because the risk of misconduct is similar for every police officer, customized incentives are probably unnecessary. Finally, the nature of police misconduct is quite well understood by supervisory employees, making it easy to design training programs and police manuals that establish detailed guidelines for line officers to follow.

On the whole, therefore, the costs to the municipality of negotiating and enforcing reasonably effective incentives to dissuade constitutional violations by the police are probably modest. The use of costly incentive mechanisms such as indemnity suits against individual police officers is unnecessary, because training programs, careful supervision, and injury-contingent penalties relating to career advancement can probably suffice to prevent most misconduct.

It follows that the imposition of vicarious liability on the municipality is unlikely to dilute the incentives of police officers to avoid constitutional violations. On the contrary, vicarious liability will likely motivate municipalities to adopt a variety of cost-effective devices to reduce the incidence of police malfeasance. These devices may not be adopted in the absence of vicarious liability because police officers are often judgment-proof which, as explained above, allows municipalities to externalize the costs of constitutional violations and thereby dilutes their incentives to economize on the costs of injuries.

Example (ii): Hiring and firing decisions are also common targets of constitutional tort litigation. For concreteness, imagine a small municipality with a city attorney's office; the office has a small staff, and the city attorney is ordinarily responsible for hiring and firing members of the staff. The city attorney discharges a female staff attorney, purportedly because she is incompetent. The discharged employee claims, however, that she was fired because of her sex.

If—as seems quite likely—senior municipal officials (the mayor, the city manager, and so on) lack the expertise necessary to evaluate the legal skills of staff attorneys in the city attorney's office, it is difficult to imagine what type of monitoring or other supervisory measures they might cost-effectively employ to avoid invidious discrimination in the hiring and firing decisions of the city attorney. Any attempt to interfere in such decisions might simply undermine the ability of the city attorney to assemble the best possible staff.

Of course, vicarious liability will likely motivate the municipality to do what it can to avoid hiring a sexist city attorney, but such proclivities on the part of candidates for the position may be undetectable during the hiring process. And, while the municipality can always establish a policy of firing any city attorney who is successfully sued under §1983, even that sanction may be relatively ineffective if the city attorney can earn a comparable income in private practice.

Under these circumstances, the imposition of vicarious liability upon the municipality may not do much to ameliorate any problem of unlawful hirings and firings. Indeed, it may exacerbate the problem if its only effect is to insulate potential wrongdoers, like the city attorney in our hypothetical example, from personal liability. Vicarious liability may then be counterproductive.

These examples illustrate how transaction costs vary from job category to job category. And, depending upon the transaction costs of available contractual incentives, the imposition of vicarious liability may lead to an amelioration of serious inefficiencies that arise under personal liability or may actually worsen those inefficiencies.

We now return to an issue raised in the last section, whether a negligence-based approach to the imposition of vicarious liability upon municipalities is more or less efficient than strict vicarious liability. What follows suggests that the possible existence of significant transaction costs tends to support adoption of the negligence approach.

The transaction costs of contractual incentives are directly relevant to a negligence analysis. Under a negligence standard, the question is whether supervisory employees could have employed cost-effective measures to prevent the constitutional tort. Where the transaction costs of contractual incentives are high, cost-effective measures to prevent the tort may not exist, and thus negligence is less likely to be found. Where transaction costs are low, cost-effective measures to prevent the tort may well exist, and a finding of negligence is more likely. In short, the negligence approach tends to result in the imposition of vicarious liability in precisely those situations where transaction costs are lowest and the economic benefits of vicarious liability are greatest.

Strict vicarious liability, on the other hand, imposes vicarious liability whenever it is determined that the employee who committed the wrong was a servant of the municipality acting within

the scope of his employment, a condition that is almost always satisfied in constitutional torts cases. Thus, a danger exists that strict vicarious liability may at times reduce the incentives of municipal employees to avoid misconduct, or at least increase the costs of dissuading misconduct, with little or no offsetting benefits.[118]

For this reason, the negligence-based approach is perhaps the better alternative, although the choice is a close one. The negligence approach creates incentives for municipalities to adopt cost-effective measures to prevent constitutional torts, while preserving the incentives created by personal liability for individual employees to avoid misconduct when municipalities cannot substitute alternative incentives at reasonable cost or when municipalities have exhausted all reasonable measures to prevent misconduct.

One last issue requires attention. If vicarious liability is limited as under the negligence-based approach, there will be more cases in which the employee is held personally liable and must pay damages out of his own pocket. This observation brings the analysis full circle to an issue addressed earlier: whether personal liability inefficiently reduces the productivity of municipal employees by causing overcautious, self-protective behavior. If the transaction costs of contractual incentives to avoid misconduct are high—contrary to the assumption embodied in our prior discussion of this issue—the same may be true of the transaction costs of contractual incentives to discourage undue timidity or inaction by municipal employees. One must therefore inquire whether a rule of personal liability might create inefficiencies that cannot be averted by contract.

---

[118]Of course, strict vicarious liability is not necessarily inconsistent with an approach to vicarious liability that is sensitive to the transaction costs problem. The common-law of agency and torts creates categories of employment relationships, and imposes vicarious liability or not depending upon the category into which the employment relationship falls—*respondeat superior* applies to the master-servant category. One of the authors has argued elsewhere that this approach often (though by no means always) leads to vicarious liability when transaction costs of contracting are low and vicarious liability is relatively more efficient. See Sykes, The Economies of Vicarious Liability, note 70 *supra*, at 1259–79. In effect, then, an implicit (though more sweeping and categorical) negligence analysis appears to underlie the common-law categories.

As noted in the text, however, almost all constitutional torts are committed by servants under the common-law definition. The city attorney in our illustration, for example, almost certainly fits the definition of a servant, yet we are uneasy about vicarious liability under the hypothesized circumstances. We are therefore hesitant to embrace the common-law categories as an adequate solution to the problem of transaction costs.

As noted above, bad faith constitutional torts usually involve intentional harms or reckless behavior that reflect indifference to well-settled constitutional requirements. Most of these torts are easily avoidable, and few municipal employees need fear that they will accidentally commit them.[119] The likelihood of overcautious behavior under personal liability seems small, therefore, even when the transaction costs of contractual incentives against it are high.

In addition, the costs of any overcautious behavior under personal liability must be weighed against the costs of shifting liability to the municipality in circumstances where the municipality cannot cost-effectively create equivalent contractual incentives against misconduct. Especially where the danger of inducing overcautious behavior under personal liability is quite low, as is seemingly the case for bad faith constitutional torts, the balance would seem to favor personal liability.

In short, although a negligence-based approach to vicarious liability would assuredly insulate the municipality from liability in some cases, it does so in precisely those cases where vicarious liability is least likely to be beneficial, and where personal liability produces valuable incentives that may be lost or that will be costly to replicate under vicarious liability. Strict vicarious liability, as well as some of the alternatives proposed by other writers,[120] lacks this important quality.

D. THE POLICY RULE

Is the policy rule of *Monell* an economically sound basis for the imposition of vicarious liability upon the municipality? The above analysis suggests that the answer is no.

In Part I, we noted that the policy rule is somewhat unsettled and that recent Supreme Court decisions vacillate between two interpretations of "policy." One interpretation focuses upon the position of the wrongdoer in the municipal hierarchy; the tort was committed pursuant to "policy" only if the decision that led to the

[119]To the extent that overcautious behavior might be induced by a fear of baseless litigation, municipalities can avoid the problem by agreeing to assume the litigation costs of employees sued for constitutional violations, or at least the costs of employees who successfully defend themselves.

[120]See note 91 *supra*.

tort was made by a high-ranking municipal official in a policymaking position. The second interpretation focuses on the nature of the decision that led to the tort; the tort was committed pursuant to "policy" only if that decision amounted to or resulted from a rule of general applicability, formulated through a deliberative process. Neither of these understandings of the policy rule is economically satisfactory.

The view that requires the decisionmaker to be a policymaker with final authority in the municipal hierarchy obviously excludes the possibility of municipal liability for most torts caused by low-level employees. It does so even when training, monitoring, or injury-contingent contractual penalties provide a cost-effective means to avoid the tort or to reduce the incidence of such torts, and despite the fact that the municipality may lack the incentive to utilize these measures under personal liability. There is no apparent economic justification for this limitation.

Concomitantly, municipal liability for constitutional torts caused by high-level municipal officials may sometimes do little to reduce the incidence of these torts (or may even increase their incidence) because of the potentially high transaction costs associated with establishing contractual incentives to dissuade misconduct. The higher the official in the municipal hierarchy, the more likely that the official occupies a specialized and relatively autonomous position. As a consequence, other municipal officials will often lack the expertise to monitor or supervise the official effectively. In addition, because the duties of officials high in the municipal hierarchy are often unique, a costly process of negotiating customized contractual incentives applicable to only the one official will often be necessary.

Consequently, the transaction costs of contractual incentives against misconduct are probably, on average, relatively great for high-level municipal officials in policymaking positions. A rule of municipal liability that limits liability to torts caused by these officials may at times produce outcomes opposite to those that would result under the negligence-based approach that we advocate above.

The alternative interpretation of the policy rule, which emphasizes the nature of the decision that causes the constitutional tort, is no better. It is true that municipal liability for the consequences of rules of general applicability will perhaps motivate more careful deliberation over the formulation of these rules, and thus reduce the number of constitutional torts that result from them. But no

economic basis exists for limiting municipal liability so narrowly. To the extent that the incidence of constitutional torts can be reduced cost-effectively through training, monitoring, and injury-contingent contractual incentives, it should not matter whether the torts result from some generally applied rule.

In sum, the policy rule of *Monell*, in both of its present variations, is economically unsound as a rule of vicarious liability for bad faith constitutional torts. As noted, a number of commentators have suggested abandoning the policy rule in favor of *respondeat superior*.[121] Our analysis shows that such an approach would certainly be preferable to existing law. But a rule of "vicarious" liability based on the negligent failure of the municipality to take measures to prevent the tort is also economically superior to existing law, and is at least arguably superior to *respondeat superior* as well.

VI. The Scope of Municipal Liability for "Good Faith" Acts by Municipal Employees

Good faith torts arise from actions of municipal employees that are determined to be unconstitutional ex post but were not clearly unconstitutional ex ante. In many of these cases, municipal employees or their supervisors undoubtedly recognize that the behavior in question falls within a gray area of the law.[122] In other cases, however, the courts make new law or reverse old law and apply the change retroactively, with the result that behavior may ultimately be found unconstitutional even if it appeared certainly constitutional beforehand.[123]

As noted earlier, municipal employees enjoy individual immunity for good faith constitutional torts. But under *Monell* and *Owen*, municipalities incur liability for good faith torts committed pursuant to official policy.[124] Thus, in this class of cases, the policy rule of *Monell* does not simply determine whether a municipality is vicariously liable for a constitutional tort, it determines whether the tort is actionable at all.

---

[121]See authorities cited in note 47 *supra*.

[122]See *e.g.*, Mitchell v. Forsyth, 472 U.S. 511 (1985); Evers v. Custer County, 745 F. 2d 1196 (9th Cir. 1984); Walters v. City of Ocean Springs, 626 F.2d 1317 (5th Cir. 1980).

[123]See, *e.g.*, *Pembaur*, 475 U.S. 469; Owen v. City of Independence, 445 U.S. 622.

[124]See notes 74, 84–86 *supra* and accompanying text.

A. THE JUSTIFICATION FOR INDIVIDUAL IMMUNITY

The policy rationale for individual immunity is the familiar concern about self-protective behavior. Without immunity, the courts suggest, a fear of personal liability would cause municipal employees to become overcautious in the performance of their duties.[125]

This concern is legitimate where, for whatever reason, the municipal employer cannot be sued: If the law is unsettled, municipal employees cannot determine with confidence ex ante which of their actions may later be judged unconstitutional. To subject them to personal liability under these conditions may well encourage them to avoid taking actions that they believe create an appreciable risk of liability, with adverse effects on job performance and on overall social welfare.

Of course, as explained above, the municipality might eliminate this problem through indemnification agreements or other contractual incentives that motivate better job performance.[126] But the municipality may view indemnification as undesirable because it eliminates the cost externalization that accompanies the use of judgment-proof employees. And other incentives for improved job performance may operate quite imperfectly, especially if the quality of job performance is difficult or costly to observe. As a result, it is possible that municipalities will simply tolerate the adverse effects of personal liability on job performance. If so, personal liability could lead to serious inefficiencies.

By discouraging behavior of uncertain legality, of course, personal liability can also reduce the incidence of good faith constitutional torts. The benefits of this reduction in the number of torts, however, may well be outweighed by the inefficiencies of uncorrected self-protective behavior. It may then be economically desirable to provide individual immunity—at least so long as the employer is not amenable to suit.

---

[125]See *e.g.*, Imbler v. Pachtman, 424 U.S. at 424–29; Wood v. Strickland, 420 U.S. at 319–21; Scheuer v. Rhodes, 416 U.S. at 242–49. In addition to this policy rationale, the Supreme Court has sometimes justified the official immunity doctrine on the ground that the Forty-Second Congress would have explicitly abolished common-law tort immunities had it intended to do so. See *e.g.*, Tenny v. Brandhove, 341 U.S. at 376; Pierson v. Ray, 386 U.S. at 554–55. (1967). As we suggested in Part II, however, this is an incorrect way to interpret §1983.

[126]See notes 96–99 *supra* and accompanying text.

If the municipal employer can be sued, however, the case for individual immunity is considerably weakened, whether or not the transaction costs of contractual incentives are significant. Consider first the case of low transaction costs. As the analysis in Section V indicates, the choice between vicarious liability and personal liability has no economic importance if employees can pay judgments against them in full and the transaction costs of contractual incentives are low. Precisely the same analysis establishes that the choice between municipal liability with individual immunity and municipal liability without individual immunity has no significance if municipalities can pay judgments against them in full and the transaction costs of contractual incentives are low. Because most municipalities generally can pay adverse judgments, therefore, our prior analysis establishes that the rule of individual immunity will have no effect on resource allocation when transaction costs are low.

When transaction costs are high, individual immunity is still largely superfluous. For whether the employee enjoys individual immunity or not, successful plaintiffs will usually collect from the deep-pocket defendant (the municipality) rather than the employee. Hence, even if the problem of self-protective behavior makes it inefficient to place personal liability on the employee, a costly reallocation of liability to the municipality by contract is usually unnecessary. Alternatively, if it is efficient for the employee to bear some amount of liability, a costly employment agreement to accomplish that result will be necessary regardless of whether the employee enjoys personal immunity.

It follows that a rule of individual immunity has no impact if the municipality is amenable to suit. It does no harm, but neither is it essential to prevent self-protective behavior. If individual immunity serves some valuable purpose, therefore, that purpose must relate to cases in which the municipal employer is also immune. This conclusion contrasts starkly with the conclusions of other writers,[127] who argue that individual immunity is an important component of the liability regime, even when the municipality is subject to suit.

B. THE CASE FOR MUNICIPAL IMMUNITY

The remainder of our analysis will assume, as do the courts, that a serious problem of self-protective behavior would arise if personal

[127]See authorities cited in note 91 *supra*.

liability were imposed in cases involving good faith torts and that a rule of individual immunity is therefore efficient for such cases if the municipality is also immune from suit. We have established as well that if the municipality can be sued, the existence or nonexistence of individual immunity is largely a matter of indifference. The analysis is thereby considerably simplified, and only one question remains: should there be a cause of action against municipalities for good faith constitutional torts?

A review of cases involving good faith torts suggests that many of them involve actions which, ex ante, appear almost certainly to be legal. Cases in which changes in the law are applied retroactively are illustrative.[128] Obviously, the imposition of municipal liability for these actions will have little impact on the ex ante behavior of municipal employees and their supervisors. It will simply impose costs ex post that tend to reduce the scale of municipal activity, with highly ambiguous implications for economic welfare, while at the same time creating significant litigation costs.

To be sure, liability also redistributes the risk of associated injuries, and may therefore provide some risk-sharing benefits if municipalities are better risk bearers than injured parties. But risk sharing benefits alone rarely suffice to justify the imposition of civil liability, since civil litigation is ordinarily far more costly than alternative mechanisms for the redistribution of risk, such as social insurance schemes.

Other good faith constitutional tort cases involve actions that are known ex ante to fall within gray areas of the law.[129] If liability attaches in such cases, municipal employees and their supervisors may well perceive a substantial possibility of an adverse judgment in the event of litigation. This prospect, in turn, will induce some efforts to avoid actions of questionable legality altogether and to accomplish tasks by alternative means. The question is whether these efforts are efficient.

That question is quite difficult to answer. The prospect of liability will discourage actions that would ultimately prove constitutional as well as actions that would ultimately prove unconstitutional. In other words, a problem of self-protective behavior arises yet again as municipalities strive to avoid liability, with potentially adverse effects on the quality of municipal services. It is impossible to know

[128]See note 123 *supra*.

[129]See note 122 *supra*.

whether the inefficiencies of self-protective behavior by municipalities will exceed the efficiencies associated with a reduced number of constitutional torts. But the danger of self-protective behavior certainly weakens the case for the imposition of liability, and the distinct possibility arises that municipal liability for these good faith torts is also inefficient.[130]

This conclusion again contrasts markedly with the analysis of other writers,[131] who suggest that self-protective behavior is a problem that arises mainly under personal liability, and that it can be eliminated by expanded governmental liability coupled with immunity for individual officials. On the contrary, inefficient self-protective behavior is by no means unique to a regime of personal liability, and its emergence under vicarious liability may justify governmental immunity just as its emergence under personal liability may justify individual immunity.

In the end, because the efficiency of municipal liability for good faith constitutional torts is very much in doubt, a rule of municipal immunity for such torts is perhaps as attractive as any alternative. At a minimum, immunity would avoid some costly litigation, eliminate some inefficient self-protective measures, and protect municipalities in some cases against liability that cannot be anticipated at all ex ante and that consequently would impose considerable burdens on the municipal treasury ex post with no attendant reduction in the number of constitutional violations.[132]

VII. Conclusion

The rules presently governing the imposition of municipal liability in constitutional tort cases are hopelessly flawed. Contrary

[130]This analysis provides no support, however, for the policy rule of *Monell*, inasmuch as the risk of self-protective behavior is no smaller for "policy" decisions by high-level officials than for other decisions by municipal employees.

[131]See note 91 *supra*.

[132]A possible objection to immunity for good faith constitutional torts is that it would destroy the incentive for litigation over actions that fall within gray areas of the law, and thus perpetuate legal uncertainty. Municipal liability would create an incentive to litigate such actions and thereby promote the resolution of uncertainties. But the resolution of uncertainty is not in itself advantageous, as the costs of associated litigation may be great. Besides, the incentive to litigate is considerable even in the absence of municipal liability for good faith torts. Little would be lost, arguably, if "good faith" constitutional torts were no longer actionable.

to the analysis in *Monell*, there is no evidence in the Civil Rights Act of 1871 or its legislative history that the Forty-Second Congress intended to limit vicarious liability for the torts of municipal employees to actions that are taken pursuant to "policy." Instead, the historical evidence suggests that Congress intended to leave the standards for the imposition of vicarious liability to the federal common law.

More importantly, the "policy rule" of *Monell* serves no intelligible purpose. It is largely incompatible with the policy objectives that the Supreme Court itself invokes on occasion as the basis for the enactment of §1983, such as the effective deterrence of wrongdoing.

Thus, the Court, through its common-lawmaking authority, should adopt an alternative approach to municipal liability. We have developed an economic analysis that provides some support for the proposal by other writers that the policy rule be abandoned in favor of common-law agency principles, including the doctrine of *respondeat superior*, but our analysis suggests still other alternatives. With respect to the most egregious constitutional torts, those committed in "bad faith," a negligence approach to municipal liability is arguably as good or better from an economic standpoint than *respondeat superior*. And with respect to more innocent "good faith" torts, for which municipal officials enjoy individual immunity, the extension of immunity to the municipality is perhaps the best option.