Powers of Attorney: Analyzing Differences between Federal/State Statutes of Limitations and an Agent's Authority and Duty

By Brian P. Corrigan

A recent decision, *Stauffer v. Internal Revenue Service*,[1] presents an opportunity to review an important difference between the limitations periods in the Internal Revenue Code (IRC) and New York Civil Practice Laws and Rules (CPLR) applicable to persons under a mental disability who have appointed an agent through a power of attorney (POA). Specifically, while a mentally disabled person/principal may be excused from acting within certain time limitations imposed by state law, this is not true under the IRC, even if the agent has no legal duty to act on behalf of the principal. Thus, a principal's interests may be harmed due to the inaction of the agent, yet the agent had no duty to take that action. The *Stauffer* decision also allows an opportunity to review the difference drawn between an agent's authority and duty where an agent's inaction caused, or is alleged to have caused, a loss to the principal.

The Statutes of Limitations

New York State Law

The so-called "insanity toll" at CPLR § 208 serves to protect parties who cannot protect their legal rights due to their general inability to function in society.[2] Thus, for those who lack the ability and capacity, due to a mental affliction, to pursue their lawful rights, this toll will relieve them of the strict time restrictions otherwise imposed by the applicable statute of limitations.[3]

Significantly, under New York law, if another person holds a POA to act on behalf of the mentally disabled person, the existence of that agency relationship does not deprive the disabled principal of the protections of the tolling statute.[4] In other words, if an agent is merely *authorized* to act on behalf of the principal – and *could* act – with respect to the particular matter, this fact does not create an exception to the tolling provisions at CPLR § 208. The opposite, however, is the case under IRC § 6511.

Internal Revenue Code

The timeliness of a taxpayer's refund claim is governed by IRC § 6511(a). The applicable limitations period will, however, be tolled if the taxpayer is "financially disabled."[5] The IRC defines a financially disabled taxpayer as one who "is unable to manage his financial affairs by reason of a medically determinable physical or mental impairment . . . which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than 12 months."[6]

Significantly, the IRC provides the following exception to the protections of that tolling provision. "An individual shall not be treated as financially disabled during any period that . . . [any] person is *authorized* to act on behalf of such individual in financial matters."[7] We now turn to the relevant facts of the *Stauffer* decision.

Stauffer v. IRS

In 2005, Father executed a durable POA appointing Son as agent. Son requested the POA to assist Father in the management of his finances because he was elderly and mentally ill. The POA granted Son broad powers, including the authority to "prepare, execute and file in [Father's] behalf . . . any and all income tax declarations and returns . . . and to represent [Father] before the Internal Revenue Service . . . with respect to any claim or proceeding having to do with [his] tax liabilities."[8]

Father died in 2012 and Son was named personal representative of his estate. In that capacity, Son filed Father's tax returns for the years 2006 through 2012 and the 2006 return reported a tax overpayment and asserted a refund claim. The IRS denied the claim for the 2006 tax refund as untimely. On behalf of the estate, Son argued the refund claim was timely because Father's financial disability tolled the statutory period to file a claim pursuant to IRC § 6511(h)(1).

The district court ruled in favor of the IRS finding, *inter alia*, that, as of 2005, Son was authorized under the POA to act on behalf of Father in financial matters for purposes of IRC § 6511(h)(2)(B). On appeal to the First Circuit, Son argued that the exception to the tolling provision (IRC § 6511(h)(2)(B)) should only apply if someone (a) has the *duty* to file the financially disabled taxpayer's tax returns and (b) actual or constructive knowledge that the tax returns for a particular year have to be filed on behalf of the disabled taxpayer.

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The First Circuit observed that the key word for their analysis of IRC § 6511(h)(2)(B) is "authorized." The Court reviewed the definitions of "authority" in both *Black's Law Dictionary* and *Merriam-Webster's Dictionary* and found none of the definitions imply that the existence of a "duty" is a requisite for a person's authority. Thus, if the Court were to adopt the Son's "duty" and "constructive knowledge" requirements, it would be interpreting the term "authorized" in IRC § 6511(h)(2)(B) beyond its plain and unambiguous meaning, which it could not do.

Therefore, the Court held that a person may be considered "authorized to act on behalf of [a financially disabled taxpayer] in financial matters" for purposes of IRC § 6511(h)(2)(B) even if that person has no affirmative obligation to act on the taxpayer's behalf. Thus, interestingly, the result is that the principal (Father) sustained a loss due to the agent's (Son's) inaction, yet the agent's inaction may not have been a breach of any legal duty.[9]

Authority vs. Duty under New York Law

For powers of attorney, the New York General Obligations Law codifies the agent's fiduciary obligation to the principal. As to whether an agent has the duty to act, the statute provides: "The agent may be subject to liability for conduct or *omissions* which violate any fiduciary *duty*."[10]

Thus, applying New York law to the facts of *Stauffer*, if Father's estate asserted a claim for the lost tax refund against Son, as former agent under the POA, while the omission may be clear, what about the violation of the fiduciary duty element?

By statute, "[a]n agent acting under a power of attorney has a fiduciary relationship with the principal" and included among the fiduciary duties is acting "in the best interest of the principal."[11]

Under New York law, does an agent have a duty to use his or her authority under a POA at the first sign of a principal's cognitive decline or inability to handle financial matters?

Matter of Carl R.P.

This question was addressed in *Matter of Carl R.P.*,[12] in the context of a proceeding for the appointment of a guardian for Claire, an 81 year old woman. Claire lived with her daughter who was her agent under a POA. Claire's son, Carl, petitioned for guardianship. Carl alleged that his sister's—the agent's—failure to use her authority under the POA to assume control of Claire's assets, and make all financial decisions, was a breach of fiduciary duty. Thus, Carl alleged, this advance directive was void and a guardian was necessary.

The facts showed that while Claire's spending could be considered extravagant (some months approaching $15,000), it did not amount to financial irresponsibility. Even though Claire had significant memory defects and could not identify the current season, the President of the United States or the names of all of her five children, she had sufficient understanding as to how her money was being applied. Further, the court evaluator, who conducted an investigation of Claire's banking records, found no evidence of the agent misappropriating Claire's money.

The Court acknowledged that Claire's functional limitations may warrant the appointment of a guardian, but the sufficiency of the advance directives, specifically the POA, supported the denial of the guardianship petition.

As to the allegation that the agent was violating her fiduciary duty by not using her authority under the POA to take control of Claire's finances, the Court held that, if that argument were adopted:

> the court would be creating a new duty for fiduciaries which does not currently exist. Children holding powers of attorney, at the first sign of cognitive decline, would be compelled to use these documents to deprive their parents of total control over their finances and the dignity and respect that go along with that control, or face the prospect of having their parents' advance directives declared void. Counsel cites no case or statute that would warrant the creation of such a duty. Nor can he show anything in the law that prevents a child from maintaining the appearance of his or her parent's continued authority over his or her finances for as long as possible.[13]

One of the main objectives for the court in a guardianship proceeding is to make available to persons with incapacities the least restrictive form of intervention which assists them in meeting their needs but, at the same time, permits them to exercise the independence and self-determination of which they are capable.[14] Thus, the *Carl R.P.* decision—arising from a guardianship proceeding—reflects an appropriate sensitivity to the dignity of the principal (especially in the context of the parent-child relationship) when it comes to balancing the incapacities and the abilities of the principal in assessing the duties of the agent.

If an agent believes the principal to be capable of handling his/her affairs and does not intervene, but that belief is mistaken, is the agent answerable for any resulting damages to the principal on a breach of fiduciary duty claim? Alternatively, what if the principal is uncooperative and combative towards the agent making any assistance difficult or impossible to provide?

There is little authority on these issues and any such determination will likely be driven by a fact sensitive analysis hinging largely on the good faith of the agent. On the one hand, an agent is not the guarantor or insurer of the principal's acts or omissions and the *Carl R.P.* precedent supports affording the principal appropriate deference. On the other hand, by countersigning the New York Statutory Short Form Power of Attorney, the agent expressly acknowledges that he/she read the POA, recognizes the legal relationship established with the principal and that the agent's legal responsibilities continue until the agent resigns or the power is terminated or revoked.

Returning to the tolling statute in the IRC, if a mentally impaired parent's/principal's desire to retain control over his or her finances impedes the child's/agent's ability to exercise authority over those matters, will that fact support the application of the IRC tolling protections? This issue was addressed in *Plati v. United States*.[15]

Plati v. United States

In 2004, Mother executed a durable POA under Massachusetts law appointing Son as her agent. Son was authorized to, *inter alia*: "prepare, sign and file all tax returns, local, state, federal and foreign; to represent me before the Internal Revenue Service or before any other governmental agency for any purpose . . . ."[16]

In 2009, the IRS denied a refund claim made in that year for income tax withheld for Mother in tax year 2004. The IRS Appeals Office denied an appeal which argued for a suspension of the limitations period because of Mother's financial disability. Even though the Appeals Office acknowledged receipt of the required proof of the existence of Mother's medical condition, it referred to the 2004 POA authorizing Son to act as Mother's agent and, therefore, her failure to meet the criteria for having a financial disability under the IRC.

In her complaint to the United States Court of Federal Claims, Mother (through Son as her agent) alleged the IRS ruling was incorrect because it found Son had authority and control over Mother's affairs when, in fact, he did not. Specifically, Son pointed to the following:

- Despite her dementia, Mother insisted on keeping control of her financial matters;
- Mother would hide her bills if Son tried to pay them and it was not until 2011 that she accepted help paying overdue bills;
- On multiple occasions Son tried to set up visiting homemaker services for Mother which she refused; and
- Mother refused to transfer ownership of her house to Son until 2007, even though she was advised by an attorney to do so 6 years earlier.

Notwithstanding Mother's dementia and her insistence on keeping control over her financial affairs, the fact that Son was Mother's attorney-in-fact since 2004 was fatal to the attempt to qualify her as a "financially disabled" taxpayer and, thereby, entitled to the protections of the tolling provisions of the IRC. The Court held:

> The plaintiff does not dispute that [Son] was indeed *authorized* to act for [Mother] in her financial matters. Whether [Son] had difficulty in doing so does not change the application of the plain language of the statute.
>
> Because an individual was authorized to act on [Mother's] behalf with regard to financial matters during the relevant time period, I.R.C. § 6511(h)(2)(B) mandates that [Mother] not be treated as financially disabled during this period.[17]

Conclusion

While an agent may not have a legal duty to seize control of the principal's finances if the principal's cognition begins to decline and, further, may be relieved of acting on behalf of a mentally disabled principal within the otherwise applicable CPLR period given the "insanity toll" at CPLR § 208, the provisions of the IRC reviewed above stand in sharp contrast. As a practical matter, it is more likely that a mentally declining principal will have tax matters requiring attention than the need to sue someone. Nevertheless, if someone is simply authorized to act on the principal's behalf with respect to tax matters, the IRC tolling provisions will not apply, thereby presenting an opportunity for a loss to the principal. Indeed, the New York Statutory Short Form Power of Attorney authorizes an agent to handle "tax matters" which, like the POAs in both *Stauffer* and *Plati*, includes the power to prepare, sign and file tax returns for the principal and to represent the principal before the IRS and any other taxing authority.[18] Research does not reveal any New York decisions surcharging an agent under a POA for damages arising from a breach of fiduciary duty for failure to file a tax return on behalf of a disabled principal. Even so, given the strict application of the exception to the IRC tolling provision, agents, and attorneys advising agents, acting under a POA should pay special attention to this issue.

Endnotes

1. 939 F.3d 1 (1st Cir. 2019).
2. *See McCarthy v. Volkswagen of Am., Inc.*, 55 N.Y.2d 543, 548, 450 N.Y.S.2d 457, 459 (1982).
3. Although the person's insanity need not have been formally adjudicated at the time the action accrues, the mental disability must exist when the action accrues. *See Hammer v. Rosen*, 7 N.Y.2d 376, 379, 198 N.Y.S.2d 65, 66 (1960).
4. *See Bookstein v. Republic Ins. Co.*, 266 A.D.2d 113, 698 N.Y.S.2d 683 (1st Dep't 1999); *New York Found. for Sr. Citizens v. Rhea*, 2012 WL 6221086 (Sup. Ct., N.Y. Co. 2012).
5. IRC § 6511(h)(1)).
6. IRC § 6511(h)(2)(A).
7. *Id*. § 6511(h)(2)(B) (emphasis added).
8. The POA was executed in Pennsylvania while Father was living in that state and, therefore, the instrument was governed by Pennsylvania state law.
9. The Court also rejected the argument that the person authorized to act on behalf of the financially disabled taxpayer must have actual or constructive knowledge of the need to file tax returns in a specific year.
10. N.Y. GOL § 5-1505(2)(b) (emphasis added).
11. *Id.* § 5-1505(2)(a)(1).
12. 44 Misc. 3d. 1219(A), 997 N.Y.S.2d 97 (Table) (Sup. Ct., Suffolk Co. 2014).
13. *Id*.
14. *See* N.Y. MHL § 81.01.
15. 99 Fed. Cl. 634 (2011).
16. *Id.* at 635.
17. *Id.* at 641 (emphasis in original; footnote removed).
18. *See* N.Y. GOL § 5-1502M.