



Alerts

Estate Held Liable for \$1.2 Million Based on Failure to Timely File Estate Tax Return Due to Attorney's Brain Cancer

January 21, 2015

Lawyers for the Profession® Alert

Specht v. U.S., 2015 WL 74539 (S.D.Ohio 2015) (January 6, 2015)

Brief Summary

This decision is not the legal malpractice case itself, but the underlying case that gave rise to the legal malpractice claims against the estate's attorney. A district court in Ohio held that an estate was liable for \$1.2 million in late filing penalties and interest relating to its estate tax return, despite the executor's having relied on an attorney who was suffering from brain cancer and who erroneously failed to file the return. The attorney was an experienced trusts and estates practitioner, and the executor was unaware of her illness. As a result of the malpractice, the attorney voluntarily relinquished her law license and was declared incompetent.

Complete Summary

Plaintiffs filed this case on behalf of the estate of Virginia Escher, seeking to recover the sum of \$1,198,261.38 in penalties and interest, which the IRS imposed upon the Escher estate as a result of its failure to timely file its estate tax return and to pay the tax owing in a timely fashion. The legal question for the court was simple: Whether plaintiffs' failure to timely file the estate tax return and to timely pay the taxes was due to reasonable cause and not willful neglect. The factual circumstances were, however, both fairly complex and sad.

Virginia Escher (decedent) died at the age of 92. Her estate was worth approximately \$12.5 million. Plaintiff Janice Specht (Specht), decedent's cousin, was asked to be the executor. Specht, then 73, was a high-school-educated homemaker who had never served as an executor, held no stock, and had never been in an attorney's office. Specht selected the decedent's attorney, Mary Backsman (attorney), to assist her. The attorney had over 50 years of experience in estate planning, but unbeknownst to Specht, was privately battling brain cancer. The attorney deceived Specht (whether intentionally or unintentionally), as to the status of an extension regarding the filing of the estate's tax returns. That deception eventually led to malpractice claims and the voluntary relinquishment of the attorney's law license. The attorney was ultimately declared incompetent and subject to a guardianship over her person and estate. The legal malpractice was settled three years before this decision, although the amount was not disclosed.

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In this case, plaintiffs argued that "reasonable cause" existed for the failure to timely file and pay estate taxes, because their failure was due to their reliance on the attorney. The United States government maintained that courts have recognized a non-delegable nature of the duty to make timely filings of tax returns and have held that reliance on counsel is not sufficient to constitute reasonable cause for the failure to timely file or pay.

After reviewing the facts and circumstances, the court noted that reasonable cause is not defined in the Internal Revenue Code. However, Treasury Regulations require the estate to demonstrate that it "exercised 'ordinary business care and prudence' but nevertheless was 'unable to file the return within the prescribed time.'" *United States v. Boyle*, 469 U.S. 241, 246 (1985), quoting 26 C.F.R. § 301.6651(c)(1). In *Boyle*, the U.S. Supreme Court held that "[t]he failure to make a timely filing of a tax return is not excused by the taxpayer's reliance on an agent, and such reliance is not 'reasonable cause' for a late filing under Section 6651(a)(1)." *Boyle*, 469 U.S. at 248. In *Boyle*, the court recognized a distinction between a taxpayer who "has relied on the erroneous advice of counsel concerning a question of law," and a taxpayer who has retained an attorney to attend to "an unambiguous, precisely defined duty to file" a return by a certain time. *Id.* at 250. Although a taxpayer may reasonably rely on advice received from an attorney "on a matter of tax law ... one does not have to be a tax expert to know that tax returns have fixed filing dates and that taxes must be paid when they are due." *Id.* at 251.

In addition to the reasonable cause requirement, the court noted that to escape penalties under Section 6651 of the Code, the estate was also required to meet the heavy burden of proving that the late filing and payment did not result from willful neglect. *Boyle*, 469 U.S. at 245. Willful neglect is "a conscious, intentional failure or reckless indifference." *Id.* However, mere carelessness is enough for a taxpayer to be denied a refund based on the exceptions in Section 6651 of the Code. *Id.* at 245 n. 4 ("[a] taxpayer seeking a refund must therefore prove that his failure to file on time was the result neither of carelessness, reckless indifference, nor intentional failure.").

Here, Specht was aware that the estate's federal tax return needed to be filed and paid nine months after decedent's death; that the tax liability was approximately \$6 million; and that the estate would need to sell certain stock to cover the tax liability. Specht further understood that the deadline was important, and that missing the deadline would result in consequences. In the months prior to the estate tax deadline, Specht received numerous notices from the probate court informing her that the estate was missing deadlines. After the deadline, Specht received additional notices from the court warning that the attorney had failed to file an accounting, numerous calls informing her the attorney was incompetent, letters from the Ohio Department of Taxation informing her the state tax return was delinquent, and a warning from another lawyer informing her that she needed to hire another attorney.

The court concluded that serving as the executor of a probate estate is clearly not an easy task, which is why Specht trusted an attorney to guide her through the process. While the court found it difficult to hold that plaintiffs were ultimately responsible for the attorney's malpractice, that was what binding precedent required. The court noted that in light of the attorney's malpractice, the State of Ohio refunded the late filing and payment penalties for Ohio estate taxes without the estate filing a refund suit, and that it was unfortunate that the United States did not follow the State of Ohio's lead.

Significance of Opinion

This decision and the legal malpractice action stemming from it are significant because they underscore the importance of an attorney having plans in place to ensure that his or her cases are taken over by counsel who can preserve the clients' rights in the unfortunate event that the attorney becomes sick, disabled or dies. See also *Cabrera v. Collazo*, 979 N.Y.S.2d 326 (2014) (attorney's death not an excuse for allowing statute of limitations to expire).

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