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Incompetent Principals, Competent Third Parties, and the Law of Agency

ALEXANDER M. MEIKLEJOHN*

INTRODUCTION

The onset of mental incompetence is a common occurrence in the United States.¹ Given advances in life-sustaining technology, mental incapacity² is likely to become even more prevalent in the future. When a person becomes incompetent,³ a variety of important legal problems may arise. One such problem results if an agent⁴ continues to represent the incompetent despite, or even because of,⁵ his condition. This article addresses the question of how courts should treat transactions⁶ entered into by agents of incompetent principals.

According to traditional theory, agents should represent only competent people. Agency is a consensual relation; it is premised on the principal's

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1. See, e.g., Moses & Pope, *Estate Planning, Disability, and the Durable Power of Attorney*, 30 S.C.L. REV. 511, 513 (1979), (citing Schlesinger, *Drafting the Estate Plan to Cover Disability*, 7 INST. ON EST. PLAN. 73.201.1 (U. Miami 1973)).

2. For stylistic purposes, the terms "incompetence" and "incapacity" are used interchangeably throughout this article.

3. Whether a particular person is incompetent can be a very difficult question. See, e.g., Green, *Proof of Mental Incompetency and the Unexpressed Major Premise*, 53 YALE L.J. 271, 271 (1944) [hereinafter cited as Green, *Proof*]; Comment, *Mental Illness and the Law of Contracts*, 57 MICH. L. REV. 1020, 1027 (1959). See generally Green, *Judicial Tests of Mental Incompetency*, 6 MO. L. REV. 141 (1941) [hereinafter cited as Green, *Judicial Tests*]. This article, however, focuses not on the test for mental incompetence but rather on certain of its legal consequences.

4. This article does not consider problems arising from the agent's loss of capacity.

5. See *infra* note 13 and accompanying text.

6. This article addresses only those actions by agents that affect the property of their principals. For an argument that agents should be permitted to make decisions with respect to the persons of incompetent principals, see Note, *Appointing an Agent to Make Medical Treatment Choices*, 84 COLUM. L. REV. 985 (1984).

ability to understand and either approve or disapprove of the agent's acts.⁷ When the principal lacks that ability, the agent should have no authority.⁸ Most writers on the subject state that the general rules follow that logic: a person who is mentally incompetent cannot appoint an agent⁹ and cannot continue to be represented by an agent appointed before the onset of the incompetence.¹⁰

In a large number of cases, however, courts have upheld acts of agents representing incompetents.¹¹ The legislatures of nearly all the states, moreover, have now passed statutes permitting the creation of "durable" powers of attorney that either survive or come into existence only upon the principal's loss of competence.¹² A widespread perception that guardianship procedures

7. Seavey, *The Rationale of Agency*, 29 YALE L.J. 859, 863 (1920). Professor Seavey distinguishes between the agency relation and a class of relations created by operation of law. With respect to agency, he states:

That the relationship is consensual there can be no doubt. The law creates the power upon the voluntary act of the principal and he is the *dominus* during its existence. The agent's duty of obedience flows directly from the control which the cases recognize to be at all times in the principal. This control over the existence of the power implies the exercise of the will at the inception of the relationship, and, as the principal may create the power, so he may diminish, enlarge, or terminate it at will, subject, of course, to rules for the protection of third persons. On the other side, the duties of a fiduciary cannot be thrust upon an unwilling person, so that the relation cannot be created, nor can it continue to exist without the consent of both parties.

Id. (footnote omitted). "Agencies by necessity," by contrast, are classified among relations created by law and are unrelated to agency proper. *Id.* at 863-64. According to the doctrine of "agency by necessity," an incompetent is liable for necessities purchased on his behalf on the basis that the purchaser was his "agent." For commentary to the effect that an incompetent's obligation to pay for necessities is quasi-contractual, see Green, *The Operative Effect of Mental Incompetency on Agreements and Wills*, 21 TEX. L. REV. 554, 562 (1943) (citing 1 S. WILLISTON, *CONTRACTS* 751 (rev. ed. 1936); 3 W. PAGE, *CONTRACTS* 2814 (2d ed. 1920)); Weihofen, *Mental Incompetency to Contract or Convey*, 39 S. CAL. L. REV. 211, 238 (1966) (stating that "necessaries" include "all things reasonably necessary for support, maintenance and comfort, according to the person's condition and status in life"); Comment, *supra* note 3, at 1089-90.

8. Even according to traditional theory, however, authority that is coupled with an interest persists beyond the onset of the principal's incompetence. *E.g.*, *Johnson v. National Bank*, 320 Ill. 389, 394-95, 151 N.E. 231, 233 (1926) (power of attorney to confess judgment, given by debtor to creditor, not revoked by an adjudication of the debtor's incompetence) (citing 1 F. MECHEM, *A TREATISE ON THE LAW OF AGENCY* § 679 (2d ed. 1914)).

9. H. REUSCHLEIN & W. GREGORY, *HANDBOOK ON THE LAW OF AGENCY AND PARTNERSHIP* § 9A (1979) ("An insane person, at least when adjudicated incompetent, cannot ordinarily appoint an agent."); W. SEAVEY, *HANDBOOK OF THE LAW OF AGENCY* § 14B (1964) ("Persons whose insanity deprives them of capacity to consent cannot have an agent."); W. SELL, *AGENCY* § 16 (1975) ("If the purported principal, because of insanity or some other condition, lacks the capacity to give a legally effective consent, he cannot appoint an agent.").

10. H. REUSCHLEIN & W. GREGORY, *supra* note 9, § 45E; W. SEAVEY, *supra* note 9, § 48C; W. SELL, *supra* note 9, § 223.

11. Many of the cases are collected in Mukatis, *Does the Agency Die When the Principal Becomes Mentally Incapacitated?*, 7 U. PUGET SOUND L. REV. 105 (1983).

12. See ALA. CODE § 26-1-2 (Supp. 1985); ALASKA STAT. § 13.26.325 (1972); ARIZ. REV. STAT. ANN. § 14-5501 (1975); ARK. STAT. ANN. §§ 58-701 to -704 (Supp. 1985); CAL. CIV.

are unduly humiliating, expensive, and cumbersome has led to serious interest in such powers as vehicles for the care of incompetents.¹³ The *Uniform Probate Code* provides for durable powers¹⁴ and, under some circumstances,

CODE §§ 2400-2406 (West Supp. 1985); COLO. REV. STAT. § 15-14-501 (Supp. 1984); CONN. GEN. STAT. § 45-690 (1985); DEL. CODE ANN. tit. 12, §§ 4901-4905 (Supp. 1984); FLA. STAT. ANN. § 709.08 (West Supp. 1985); HAWAII REV. STAT. § 560:5-501 (Supp. 1984); IDAHO CODE §§ 15-5-501 to -507 (Supp. 1985); IND. CODE ANN. §§ 30-2-11-1 to -7 (Burns Supp. 1985); IOWA CODE ANN. §§ 633.705 to .706 (West Supp. 1984-85); KAN. STAT. ANN. §§ 58-610 to -617 (1983); KY. REV. STAT. § 386.093 (1984); ME. REV. STAT. ANN. tit. 18-A, § 5-501 (1981); MD. EST. & TRUSTS CODE ANN. § 13-601 (1974); MASS. ANN. LAWS ch. 201B, §§ 1-7 (Michie/Law. Co-op. Supp. 1985); MINN. STAT. ANN. §§ 523.07 to .08 (West Supp. 1985); MISS. CODE ANN. § 87-3-13 (Supp. 1985); MO. ANN. STAT. §§ 486.550 to .595 (Vernon Supp. 1985); MONT. CODE ANN. § 72-5-501 (1985); NEB. REV. STAT. §§ 30-2644 to -2672 (Supp. 1985); NEV. REV. STAT. § 111.460 (1983); N.H. REV. STAT. ANN. § 506:6 (1983); N.J. STAT. ANN. § 46:2B-8 (West Supp. 1985); N.M. STAT. ANN. § 45-5-501 (1978); N.Y. GEN. OBLIG. LAW § 5-1601 (McKinney 1978); N.C. GEN. STAT. §§ 32A-8 to -14 (1984); N.D. CENT. CODE §§ 30.1-30-01 to -05 (Supp. 1985); OHIO REV. CODE ANN. §§ 1337.09 to .092 (Page Supp. 1984); OKLA. STAT. ANN. tit. 58, §§ 1051-1062 (West Supp. 1984-85); OR. REV. STAT. § 126.407 (1984); 20 PA. CONS. STAT. ANN. §§ 5604, 5606 (Purdon Supp. 1985); R.I. GEN. LAWS § 34-22-6.1 (1984); S.C. CODE ANN. § 32-13-10 (Law. Co-op. Supp. 1984); S.D. CODIFIED LAWS ANN. §§ 59-7-2.1 to -2.4 (1978); TENN. CODE ANN. § 34-6-101 to -107 (1984); TEX. PROB. CODE ANN. art. 36A (Vernon 1980); UTAH CODE ANN. § 75-5-501 (1978); VT. STAT. ANN. tit. 14, § 3051 (Supp. 1984); VA. CODE § 11-9.1 (1985); WASH. REV. CODE ANN. § 11.94.010 (Supp. 1986); W. VA. CODE § 27-11-6 (Supp. 1985); WIS. STAT. ANN. § 243.07 (West Supp. 1985); WYO. STAT. § 3-5-101 (1985).

One state has a statute providing generally that the authority of the agent continues unless and until the principal is declared incompetent. ILL. ANN. STAT. ch. 110 1/2, § 11a-23 (Smith-Hurd Supp. 1985).

Two states have statutes providing that the authority of the agent continues unless and until a guardian is appointed for the principal. GA. CODE ANN. § 10-6-36 (1982); LA. CIV. CODE ANN. art. 3027 (West Supp. 1985).

13. See, e.g., Lombard, *Asset Management Under A Durable Power of Attorney—The Ideal Solution To Guardianships or Conservatorships*, 9 PROB. NOTES 189, 189-91 (1983); Moses & Pope, *supra* note 1, at 515-16.

14. UNIF. PROB. CODE §§ 5-501 to -505 (1984). The sections are identical to UNIF. DURABLE POWER OF ATTORNEY ACT §§ 1-5 (1984). The Code sections were promulgated

to assist persons interested in establishing non-court regimes for the management of their affairs in the event of later incompetency or disability. The purpose was to recognize a form of senility insurance comparable to that available to relatively wealthy persons who use funded, revocable trusts for persons who are unwilling or unable to transfer assets as required to establish a trust.

UNIF. PROB. CODE §§ 5-501 to -505 prefatory note (1984). A durable power of attorney is defined as

a power of attorney by which a principal designates another his attorney in fact in writing and the writing contains the words 'This power of attorney shall not be affected by subsequent disability or incapacity of the principal, or lapse of time,' or 'This power of attorney shall become effective upon the disability or incapacity of the principal,' or similar words showing the intent of the principal that the authority conferred shall be exercisable notwithstanding the principal's subsequent disability or incapacity, and, unless it states a time of termination, notwithstanding the lapse of time since the execution of the instrument.

Id. § 5-501. A durable power is not affected by the disability or incapacity of the principal:

All acts done by an attorney in fact pursuant to a durable power of attorney during any period of disability or incapacity of the principal have the same effect

for the persistence of a traditional power of attorney beyond the onset of the principal's incompetence.¹⁵

Neither the law relating to traditional agency relationships and incompetence nor the law relating to durable powers is well understood. The opinions in the cases involving traditional powers fail to explain adequately why some transactions are upheld and others are not, and there is very little case law to date concerning durable powers. This article attempts to rationalize the existing law and to anticipate and prescribe some features of future decisions in the area. Part I critically examines the current status of the law regarding transactions entered into on behalf of incompetents by holders of traditional agency powers.¹⁶ Part II argues that the traditional agency cases have certain implications for future decisions involving durable powers.

I. TRADITIONAL AGENCIES PER SE

In theory, at least, the principal's ability to control the agent provides a basis for the traditional agency relation that is clear and easily justifiable in policy terms. An agent's acts bind a competent principal because, through the agent, the principal exercises freedom of choice in economic matters.¹⁷ If an agent's acts are similarly to bind an incompetent principal, the basis for that authority should be equally clear and equally justified in policy terms. In the current state of the law regarding traditional agencies, however, the reason for the agent's authority is unclear. The most significant treatment of the problem in recent years has been in a series of federal cases¹⁸ and in

and inure to the benefit of and bind the principal and his successors in interest as if the principal were competent and not disabled.

Id. § 5-502.

15. Where a traditional power of attorney is in writing it continues to be effective as to any person who is unaware of the principal's condition:

The disability or incapacity of a principal who has previously executed a written power of attorney that is not a durable power does not revoke or terminate the agency as to the attorney in fact or other person who, without actual knowledge of the disability or incapacity of the principal, acts in good faith under the power. Any action so taken, unless otherwise invalid or unenforceable, binds the principal and his successors in interest.

UNIF. PROB. CODE § 5-504(b) (1984). A number of states have adopted similar provisions. *See, e.g.,* COLO. REV. STAT. § 15-14-502 (Supp. 1984).

16. Traditional agencies play important roles in many transactions. Professors Reuschlein and Gregory note that "[t]oday, most of the world's work is performed by agents." H. REUSCHLEIN & W. GREGORY, *supra* note 9, § 1. They list various types of agents, including factors, brokers, employees of individual proprietors, employees of trustees of business trusts, partners, and participants in joint ventures or joint stock companies. *Id.* The problem of the principal's incompetence could arise with respect to an agent in any of those categories.

17. Seavey, *supra* note 7, at 863.

18. *See* United States v. Manny, 645 F.2d 163 (2d Cir. 1981); United States v. Price, 514 F. Supp. 477 (S.D. Iowa 1981); United States v. Estate of Dean, 80-2 U.S. Tax Cas. (CCH) ¶ 13,358 (S.D. Ind. 1980); Silver v. United States, 498 F. Supp. 610 (N.D. Ill. 1980); Estate of Watson v. Simon, 442 F. Supp. 1000 (S.D.N.Y. 1977), *rev'd on juris. grounds sub nom.*, Estate of Watson v. Blumenthal, 586 F.2d 925 (2d Cir. 1978); Campbell v. United States, 657 F.2d 1174 (Ct. Cl. 1981); Estate of Pfohl v. Commissioner, 70 T.C. 630 (1978).

the *Uniform Probate Code*.¹⁹ This part contains first a description of the rules adopted in the cases and in the code, second an argument that the rules are unsatisfactory, and third a proposal for an alternative set of rules.²⁰

A. Recent Developments

1. The Cases

In the federal cases, with one exception,²¹ the courts approved a series of essentially identical transactions in which traditional powers of attorney were put to strikingly effective use on behalf of incompetent principals. The events leading up to *Campbell v. United States*,²² the last case in the series, demonstrate the potential value of a traditional agency power, and the opinion sets forth the rules that the cases adopted.

In 1965, Lionel L. Campbell was sixty-two years old and in good health. During that year, he gave his son (“Campbell Junior”) ‘a full and universal power of attorney’ authorizing Campbell Junior ‘to do any and every act, and exercise any and every power’ that Campbell could do or exercise through

19. See *supra* note 15.

20. The proposed rules and most of the cases concern situations in which agents have already entered into transactions on behalf of incompetent principals. They address the rights and liabilities of the principals and third parties arising out of those transactions. They do not address the question of whether an agent should continue to represent an incompetent principal. In cases in which courts have been asked that question, they have answered in the negative. In *Capital Nat'l Bank v. Stoll*, 220 Cal. 260, 30 P.2d 411 (1934), for example, a father who was 87 years old gave his son the authority to run his business until the date of the final distribution of his estate. *Id.* at 262-63, 30 P.2d at 412-13. The father then became incompetent, *id.* at 263, 30 P.2d at 413, and the court upheld a judgment restraining the son from interfering with his property. *Id.* at 266, 30 P.2d at 414. The court acted under a statute that it quoted as follows: “Unless the power of an agent is coupled with an interest in the subject of the agency, it is terminated, as to every person having notice thereof, by: 1. Its revocation by the principal; 2. His death; or, 3. His incapacity to contract.” *Id.* at 264, 30 P.2d at 413 (quoting CAL. CIV. CODE § 2356).

In *Gertison v. Hull*, 64 Pa. D. & C. 192 (1947), the holder of a power of attorney sought a declaratory judgment to the effect that the power was entitled to “full faith and credit in accordance with its terms.” *Id.* at 192. The court, which had appointed a temporary receiver to assume charge of the principal’s assets pending a decision on guardianship, denied the requested declaratory relief. *Id.* at 194-95.

In *Fulton Nat'l Bank v. Haldeman*, 29 Pa. D. & C. 331 (C.P. 1936), the court declared a power of attorney null and void as of the date on which the principal was held to be unable to take care of her property. *Id.* at 335. It also ordered the agent to file an accounting of his handling of the principal’s affairs, and noted that it would have such further authority as might be necessary to secure the transfer of the principal’s property from the agent to the principal’s guardian. *Id.* at 335-36. Since there was no evidence of any transaction entered into by the agent after the declaration of the principal’s incompetence, the effect of the judgment was prospective only.

21. See *United States v. Estate of Dean*, 80-2 U.S. Tax Cas. (CCH) ¶ 13,358 (S.D. Ind. 1980).

22. 657 F.2d 1174 (Ct. Cl. 1981).

any other person."²³ He evidently remained in good health for the next eleven years, but on December 9, 1976, he suffered a cerebral hemorrhage and became incompetent. The court stressed that, as of then, Campbell Junior could not be certain how long his father's incapacity would last.²⁴

The next day, however, Campbell Junior exercised the power of attorney. Intending to act as his father's agent and using his father's funds, he purchased a "flower bond" issued by the United States Treasury.²⁵ The face amount of the bond was \$200,000, and it was to mature on November 15, 1998. The court's statement of the facts omits both the amount Campbell Junior paid and the manner in which the purchase money was previously invested. The court did state that the bond was purchased at a "substantial discount."²⁶ Other information in the opinion suggests that the price was about \$155,000.²⁷ The bond was not particularly attractive as a long-term investment; the discount at which it was purchased was probably due to the fact that it bore interest of only 3.5% per year. If Campbell died at any time in the near future, however, the transaction would turn out to be extremely advantageous to his successors because the bond could be redeemed at its face value plus accrued interest in payment of federal taxes on his estate.²⁸ If those taxes amounted to \$200,000, for example, they could be

23. *Id.* at 1175.

24. *Id.* at 1177.

25. *Id.* at 1175.

26. *Id.*

27. The plaintiff claimed, apparently without contradiction, that "as of December 7, 1979 the approximate market value of \$106,000 of the face amount of the bond was \$81,885." *Id.*

28. In *Estate of Watson v. Blumenthal*, 586 F.2d 925 (2d Cir. 1978), the court provided the following explanation of the legal framework authorizing the issuance of flower bonds:

Treasury bonds in general and Flower Bonds in particular are issued under the authority given Congress in Article I, Section 8, Clause 2, of the Constitution 'to borrow Money on the credit of the United States.' Flower Bonds derive from the Second Liberty Bond Act, 31 U.S.C. § 752, and more particularly Section 20 of the Act, 31 U.S.C. § 754b, which was amended, 56 Stat. 189 (1942), so as to permit 'under such regulations and upon such terms and conditions as the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury may prescribe [bonds to] be receivable by the United States in payment of . . . taxes.' Regulations were adopted to permit certain bonds issues to be redeemed at par for purposes of paying federal estate tax. These issues are called Flower Bonds because in effect they bloom at the time of the death of the owner, prior to which, particularly because they bear low interest, they sell at a substantial discount on the open market. The Treasury Department could not issue Flower Bonds after March 3, 1971, because of a statutory repeal, 31 U.S.C. § 757c-4, but a number of issues made in the 1940s and '50s with maturity dates in the 1970s, '80s and '90s are outstanding, purchasable on the open market and ready to 'bloom' upon the owner's death. In connection with each issue here involved, the Treasury's Bureau of the Public Debt issued 'offering circulars' that set forth the conditions for the redemption of the bonds. Although the language of each of the offering circulars varies somewhat, they all require ownership or actual own-

paid in full simply by using the bond.²⁹ If the federal estate tax liability were less than \$200,000, the tax savings would be proportionally reduced but by no means eliminated. The bond and others like it were called "flower bonds" because they "bloomed" when the taxes on the estates of their owners came due.³⁰

Campbell died on January 2, 1977, twenty-three days after his son's purchase of the bond. His federal estate tax liability was later determined to be \$103,219, and the executrix of his estate sought to redeem the bond at its face amount to that extent. The United States refused to accept any part of the bond at its face amount on the ground that it did not belong to Campbell because his incompetence terminated the power of attorney and therefore the purported purchase was ineffective.³¹ The executrix filed suit in the Court of Claims for damages, claiming, among other things, the difference between \$103,219 of the face value of the bond and the market value of that amount,³² and the court held that she was entitled to recover.³³ The case was remanded to the trial division for a determination of damages. Although the report does not indicate the amount of the eventual tax savings, it appears, based on the figures in the opinion, that the estate probably saved approximately \$20,000.³⁴ Campbell Junior's exercise of the power of attorney thus turned out to be extremely advantageous to his father's heirs.

ership by the decedent at the time of his death. The circulars incorporate the regulations now appearing at 31 C.F.R. § 306.28, which also set forth, Subparagraph (b), as the requirements for redemption of bonds under this section that (1) the decedent must have owned the bonds at the time of his death, and (2) the bonds must constitute a part of his estate.

Id. at 927 (footnotes omitted).

29. Under those circumstances, the tax savings would not amount to \$45,000 because, as one of the flower bond courts explained:

Flower bonds redeemed at par in payment of estate taxes must be valued in the gross estate for federal estate tax purposes, at par, including interest accrued to the date of death. [1976] 1 Fed. Est. & Gift Tax Rep. (CCH) para. 4220.05; *Estate of Pfohl v. Commissioner*, 70 T.C. 630, 632 (1978). In effect, the Treasury, which would redeem at face value on maturity in any event, suffers whatever financial loss is attributable to having redeemed prior to maturity, decreased by the additional estate tax collected on the stepped up value of the bonds redeemed.

United States v. Manny, 645 F.2d 163, 164 n.1 (2d Cir. 1981).

30. *Estate of Watson v. Blumenthal*, 586 F.2d 925, 927 (2d Cir. 1978).

31. *Campbell*, 657 F.2d at 1175.

32. *Id.*

33. *Id.* at 1178.

34. The United States claimed that Campbell's estate tax liability was \$103,219 (the calculation was presumably based on the idea that no part of the bond could be redeemed at face value in payment of estate taxes). The plaintiff claimed that, as of December 7, 1979, the market value of \$106,000 of the face value of the bond was \$81,885. *Id.* at 1175. Assuming that figure was correct, as of the same date the market value of \$103,219 of the face value of the bond was \$79,737. The tax savings would have been the difference between \$103,219 and \$79,737, or \$23,482, less the additional tax resulting from inclusion of the bond in Campbell's estate.

The other flower bond cases involved purchases under similar circumstances³⁵ that were, with one exception,³⁶ upheld by the courts.

Under the flower bond cases, the principal's inability to consent to the agent's acts does not necessarily terminate the agency. The results of the cases may very well be in accordance with what most people would want and expect. Yet if the rule of the cases were simply that, in accordance with most people's expectations, the agency relationship has momentum that carries it beyond the onset of the principal's incompetence, the courts would have to uphold actions that most people would probably not want to see upheld. The Court of Claims in *Campbell* did not adopt such a rule. Instead, it set forth a view according to which the consequences of the principal's incompetence would vary according to the nature of the incompetence.

The opinion first distinguished between declared and undeclared incompetence.³⁷ Within the category of undeclared incompetence, the court drew a further line between a condition that precludes recovery and one that does not.³⁸ The effect of a judicial declaration of incompetence, according to the court, is to terminate the authority of a previously appointed agent.³⁹ The opinion is less clear with respect to clearly permanent incompetence, but suggests that it has the same consequence.⁴⁰

The legal effect of undeclared and potentially reversible incompetence, on the other hand, is only to make a transaction entered into by a previously appointed agent voidable by the incompetent or his or her "heirs, devisees, or personal representatives."⁴¹ In order to personally exercise his right to avoid, of course, the incompetent would have to recover. The court did not say whether the incompetent's successor(s) would have a right to avoid if the incompetent recovered before dying. The right to avoid, in any event, belonged only to the incompetent and his successor(s); in *Campbell* itself,

35. Estate tax savings presumably resulted from the purchases in the other cases as well, but the only opinions that contain information regarding the probable amounts of the savings are those in *Silver v. United States*, 498 F. Supp. 610 (N.D. Ill. 1980) and *Estate of Pfohl v. Commissioner*, 70 T.C. 630 (1978). In *Silver*, bonds whose face value was \$20,000 were sold, after the government's refusal to accept them in payment of estate taxes, for \$15,650. 498 F. Supp. at 611. In *Pfohl*, bonds having a par value of \$96,000 were reported in the decedent's estate tax return at a fair market value of \$73,320. 70 T.C. at 631.

36. See *United States v. Estate of Dean*, 80-2 U.S. Tax Cas. (CCH) ¶ 13,358 (S.D. Ind. 1980).

37. *Campbell*, 657 F.2d at 1176.

38. *Id.* at 1177.

39. *Id.* at 1176.

40. The court quoted with approval language from *United States v. Manny*, 645 F.2d 163 (2d Cir. 1981), that construed certain provisions of the *Restatement (Second) of Agency* as "depriving agents of capacity only where the incapacity of their principals is known to be permanent from the outset." 657 F.2d at 1177.

41. 657 F.2d at 1178.

for example, it could be exercised by neither the party who sold the bond to Campbell Junior nor the United States.⁴²

Under the voidability rule, ratification of the purchase by Campbell or his successors was not required to bind the seller or make Campbell the owner of the bonds; they were his, subject to his right of avoidance. The court nevertheless added that the estate, by submitting the bond for early redemption, had ratified the transaction.⁴³ Where a transaction is voidable rather than void, the logical effect of an affirmance is to terminate the power of avoidance. The opinion does not indicate clearly whether the submission simply ended the estate's right to avoid. The court may have thought instead that the affirmance constituted a ratification that made the transaction enforceable independent of the voidability rule.

The court was careful to emphasize that it was applying the foregoing rules in a case in which the purchase was made the day after the principal became incompetent and less than a month before he died. It reserved judgment as to what the result would be "if the purchase was not made until a substantial time after the decedent became comatose, during which period a guardian could have been appointed, or if the decedent had survived the purchase for an extended time."⁴⁴ In the other flower bond cases,⁴⁵ the opinions did not include that limitation.

2. The Uniform Probate Code

Section 5-504(b) of the *Uniform Probate Code* provides that the incompetence of a principal who has executed a written power of attorney does not revoke the power as to the attorney in fact or other person who, without actual knowledge of the principal's condition, deals in good faith with the agent. The agency is apparently effective without regard to either the nature of the principal's condition or the nature of the transaction.⁴⁶ The comment to the section does not contain a detailed explanation of the theory underlying the persistence of the power despite the principal's incompetence.

B. *The Problematic Nature of the Flower Bond and Code Rules*

In many cases, the flower bond and code rules would produce just results. In many others, however, they would lead to unfair outcomes. The problematic nature of the rules stems from the fact that they do not follow from

42. The court stated that the transaction was voidable and could be disaffirmed, on Campbell's death, only by his successors. It was explicit in denying the government's right to disaffirm; it was not explicit in denying the same right to the seller. *Id.*

43. *Id.*

44. *Id.*

45. See *supra* note 18.

46. UNIF. PROB. CODE § 5-504(b) (1984). For the text of the section, see *supra* note 15.

a careful analysis of the policy considerations that bear on situations in which agents purport to represent incompetents. They are, moreover, not required by the relevant cases. This section of the article first explores the policy background and then examines the rules against that background and the cases that are thought to justify them.

1. The Policy Background

In a series of articles published during the 1940's, Milton D. Green reviewed the law of mental incompetence in cases involving contracts and wills.⁴⁷ He argued that the opinions in the cases were not explicit about the policies on which the holdings were based, and set forth what he believed those policies to be. He concluded that, in general, it was appropriate for the courts to base their decisions on those policies, rather than on the ideas discussed in the opinions.⁴⁸ The articles remain the most comprehensive, and probably the most authoritative, treatment of the law of mental incompetence and consensual transactions.

Green argued that, in cases in which incompetents executed wills or made contracts, two social policies were in conflict. The two policies were, in his terminology, security and equality.⁴⁹ The policy of security, meaning the security of transactions, dictated that transactions involving incompetents should be enforced. The policy of equality, meaning equality of distribution,⁵⁰ dictated that incompetents should not be bound by transactions into which they entered. Thus, according to Green, the legal consequences of mental incompetency

are dependent upon which of the two conflicting public policies involved the court deems paramount when considered in connection with the circumstances of the case under advisement. One policy is to protect the incompetent or his dependents. The other is to uphold the security of trans-

47. See Green, *Public Policies Underlying the Law of Mental Incompetency*, 38 MICH. L. REV. 1189 (1940) [hereinafter cited as Green, *Public Policies*]; Green, *Judicial Tests*, *supra* note 3; Green, *supra* note 7; Green, *Proof*, *supra* note 3.

48. Green argued that the courts purported to apply a test for mental incompetence that focused on capacity to understand transactions, but that they actually applied a test in which the fairness of the transaction often played a major role. He conceded that the use of the latter test ran "counter to the ideas of freedom of contract and testatorial absolutism." Green, *Proof*, *supra* note 3, at 309. Yet he defended the test and advocated its frank recognition as likely to lead to "greater certainty and predictability in this beclouded area of the law." *Id.*

49. Green, *Public Policies*, *supra* note 47, at 1205-12.

50. According to Hobbes: "Justice of Actions, is by Writers divided into *Commutative*, and *Distributive*. . . . Commutative therefore, they place in the equality of value of the things contracted for; And Distributive, in the distribution of equal benefit, to men of equal merit." T. HOBBS, *LEVIATHAN* 115 (Oxford Univ. Press 1947), quoted in F. KESSLER & G. GILMORE, *CONTRACTS, CASES AND MATERIALS* 440 (1970).

actions. These policies are at war with each other. If full recognition is given to the former the instrument will be held utterly void. If full recognition is given to the latter the instrument will be held valid.⁵¹

In the years following the publication of Green's articles, other commentators adopted similar views.⁵²

The policy background for cases involving incompetents, however, is more complex than it appears in Green's picture. First, incompetents' interests do not always militate in favor of invalidation of transactions. Second, the interests of those who deal with incompetents vary in terms of legitimacy in a way that Green did not describe, and, to the extent that they are legitimate, do not always militate in favor of enforcement of transactions.

With respect to incompetents, Green did qualify his generalization that a protective policy leads to invalidation of transactions. He acknowledged that there are certain transactions that leave the incompetents' interests essentially unaffected.⁵³ An incompetent's interests are not directly involved, for example, in an amendment of an inter vivos trust of which he is not a beneficiary,⁵⁴ or in a withdrawal of funds from a savings account trust with the result that his estate plan is altered.⁵⁵ In cases involving such transactions, Green demonstrated that the policy of protection of the incompetent's family or dependents plays a major if not decisive role.⁵⁶ His analysis is comprehensive except insofar as it omits the possibility of a compelling claim of reliance by a person in neither of those categories.⁵⁷

Green failed, however, to take account of the possibility that an incompetent can have a positive interest in the enforcement of a transaction. If an incompetent enters into a transaction and then recovers and freely affirms it, his interest in independence militates in favor of enforcement, rather than avoidance.⁵⁸ If there is no such affirmance, but the transaction is beneficial

51. Green, *supra* note 7, at 589.

52. See, e.g., Weihofen, *supra* note 7, at 228; Comment, *supra* note 3, at 1025-26.

53. Green noted the distinction between transactions that affect the principal and those that do not, as well as an area of overlap in cases in which wills are products of undue influence. Green, *Public Policies*, *supra* note 47, at 1216-19.

54. See, e.g., Estate of Head v. Taute, 94 N.M. 656, 615 P.2d 271 (Ct. App. 1980).

55. See, e.g., Bishop's Estate, 30 Pa. D. 149 (O.C. 1920).

56. See Green, *Proof*, *supra* note 3, at 298-306.

57. Such a claim would exist, for example, in the following situation. The incompetent amends an inter vivos trust to provide income for a beneficiary who is unaware of the incompetent's condition, assuring the beneficiary that the amendment will remain in effect for a certain number of years. In reliance on the amendment, the beneficiary purchases real estate, assuming a mortgage that he can only pay off if he receives the trust income.

58. For an argument that incompetents' interests in liberty do not receive sufficient protection, see Alexander & Szasz, *From Contract to Status via Psychiatry*, 13 SANTA CLARA LAW. 537 (1973). When the affirmance is by the guardian or conservator of an incompetent, the latter's interest in liberty is not at stake, but the policy favoring the security of transactions still militates in favor of enforcement. As Aaron Twerski points out with reference to ratification

to the incompetent, his economic interest militates in the same direction.⁵⁹ In either case, by holding the transaction to be valid, a court can at once protect the incompetent and further the policy of security.

With respect to the interests of those who deal with incompetents, Green failed to take account of a critical factor. He made no distinction between a person who attempts to take advantage of an incompetent and one who deals with an incompetent with neither knowledge nor reason to know of his condition. The distinction is important because the interests of the person who acts in good faith are entitled to recognition, whereas the interests of the person who acts in bad faith may appropriately be disregarded. In agency cases in particular, others are likely to deal with incompetents in good faith. The seller of the bond in *Campbell*, for example, probably had neither knowledge nor reason to know of Campbell's condition at the time of the sale. If courts generally fail to recognize the legitimate interests of those who deal with incompetents, they are, therefore, particularly likely to reach unjust results in agency cases.

Assuming that a person deals with an incompetent in good faith, and that his interests are therefore entitled to recognition, those interests may or may not be furthered by enforcement of the transaction. If the transaction is advantageous to him, enforcement will be beneficial; if it is disadvantageous, he has an interest in being able to withdraw. Where the incompetent cannot make an overriding claim of reliance,⁶⁰ that interest should be protected. Recognition of the competent person's right to withdraw would

in general:

Agency is an indispensable tool for the completion of the vast majority of business transactions. When one purports to be an authorized agent and his agency is confirmed by the purported principal, there should be no further attack on the bona fides of the relationship. The entire transaction undertaken by the agent has now been stamped with regularity. It ought not be recalled at the whim of either party.

Twerski, *The Independent Doctrine of Ratification v. The Restatement and Mr. Seavey*, 42 TEMP. L.Q. 1, 14 (1968).

59. See Virtue, *Restitution from the Mentally Infirm* (pts. 1 & 2), 26 N.Y.U. L. REV. 132, 291 (1951). Virtue examined "approximately eight hundred and thirty cases dealing with contracts attacked for mental infirmity." *Id.* (pt. 1) at 140. She reported:

In a significant number of the cases, upholding the contract did not produce a result adverse to the interest of the lunatic, but on the contrary either protected his interests or carried out his wishes; as where the contract was for an attorney to obtain restoration to legal sanity; or where the alleged incompetent made a gift *inter vivos* to obtain support or to the objects of his love and affection. Avoiding the contract and protecting the lunatic, therefore, are not necessarily equivalent. In the entire group of enforced contracts, not less than half were cases in which upholding the contract protected the lunatic, or in which the person whose mental infirmity was in issue had no real interest in the outcome of the litigation.

Id. at 141-42 (footnotes omitted).

60. Such a claim of reliance would exist where, for example, the incompetent spent and could not recover the consideration he received from the competent party.

further a policy of fairness; he would not be held in the absence of consideration for his promise.

Protection of the competent party's interest in withdrawal is, admittedly, not generally favored in the literature on the contracts of incompetents. Most commentators who have addressed the point take the position that the incompetent's promise, even though voidable, serves as consideration for the competent party's promise.⁶¹ To simply accept that generalization, however, is to neglect to ask whether there is any reason for enforcing the promise of the competent party.⁶² According to Green, the earlier cases involving promises made by incompetents held them to be void on the basis of a combination of the subjective theory of contracts and the concept of the mind and body as separate entities. Since a contract required a meeting of the minds, and since an incompetent had a body but not a mind, he could not make a contract.⁶³ If he entered into an agreement with a competent person, his promise would neither bind him nor serve as consideration for the competent person's promise.

Green viewed a later transition in the cases to a rule of voidability as an advance that was tied to an abandonment of the mind-body duality as a basis for decision and the substitution of the policy of protecting incompetents:

[M]any of our modern courts have adopted a new theoretical basis for invalidating the contracts and wills of mental incompetents. They regard the mental incompetent as one of a class who is in an obviously disadvantageous position with his contemporaries in society and therefore cast a cloak of protection about him by permitting him, or his legal representative, to avoid his contract.⁶⁴

Green's language suggests that the policy of protecting incompetents always justifies permitting them to avoid contracts while refusing to let competent parties do so. It suggests, that is, that an incompetent's voidable promise should indeed serve as consideration for a return promise by a competent person.

If all cases involving contracts of incompetents were cases in which they were taken advantage of by competent people, a rule of voidability would be justifiable in policy terms. Where the competent party has dealt with the incompetent in good faith, however, the policy of protecting incompetents is, without more, irrelevant, because the competent party has done nothing against with the incompetent needs protection. Only in a case in which the

61. See, e.g., A. CORBIN, CORBIN ON CONTRACTS § 146 (1963).

62. For an argument that the object of a study of consideration should be to discover why the courts enforce certain promises and refuse to enforce others, see *id.* § 110.

63. See Green, *Judicial Tests*, *supra* note 3, at 143-45; Green, *supra* note 7, at 558-59.

64. Green, *Judicial Tests*, *supra* note 3, at 145.

competent party either tries to or does take advantage of the incompetent does the need for protection arise simply on the basis of the incompetent's condition. While it may be appropriate to hold both parties to the transaction for some other reason, it is inappropriate to hold the competent party while permitting the incompetent to avoid. To adopt this position is not necessarily to return to either the subjective theory of contracts or the conception that the mind and body are separate entities. It is only to recognize that when an incompetent purports to make a promise he does not make the kind of choice⁶⁵ to which the law should, without more, give effect.⁶⁶

2. The Rules in Light of Policy and Precedent

Neither the set of rules announced in the flower bond opinions nor the Code rule is fully responsive to the range of legitimate interests that are potentially involved when an agent acts on behalf of an incompetent principal. The cases that are thought to justify the flower bond rules, moreover, fail to do so.

65. An agency case can arise only if the principal, while competent, made a choice to be represented by his agent. If the principal intended that the agent's authority should continue despite his incompetence, that choice will be frustrated if the agent's acts are not given effect. Even in the absence of an applicable durable power statute, there is an argument for giving effect to the agent's acts in order to carry out the principal's original decision to be represented. To appoint an agent who cannot be effectively supervised, however, is to make the kind of choice that should be enforced only where there has been compliance with standardized formalities that fulfill both cautionary and evidentiary functions. See Langbein, *Substantial Compliance with the Wills Act*, 88 HARV. L. REV. 489, 491-96 (1975) (discussing formalities for wills). In the absence of legislation prescribing such formalities for grants of authority other than powers of attorney, those grants should not be durable, either to bind the principal or to serve as consideration for promises by third parties. For a case in which an oral grant of authority that was probably meant to be durable was not given effect, see *Fischer v. Gorman*, 65 S.D. 453, 274 N.W. 866 (1937), discussed *infra* note 95.

66. Professor Corbin maintained that an incompetent's voidable promise serves as consideration for a return promise. See A. CORBIN, *supra* note 61, § 146. His sole citation, however, was *Atwell v. Jenkins*, 163 Mass. 362, 40 N.E. 178 (1895), which is explicable on other grounds. In *Atwell*, Hoes, who was insane, committed an offense in Massachusetts and engaged Jenkins to handle his defense. Hoes sent a telegram to Atwell, asking him to wire \$400 to Jenkins. Atwell forwarded \$400 of his own funds, whereupon Jenkins performed services worth at most \$60, and the prosecutor entered a *nolle prosequi* on the basis of Hoes' insanity. Atwell sued Jenkins to compel him to return \$300 of the funds he had received. *Id.* at 362-63, 40 N.E. at 178-79. The court, speaking through then Judge Holmes, upheld a judgment for Jenkins. *Id.* at 364, 40 N.E. at 180. Holmes' theory was that Atwell's advance had been to Hoes, pursuant to a loan agreement; Hoes' voidable promise to repay was consideration for Atwell's promise to lend. Because his promise was enforceable, Atwell was not entitled to an immediate refund from either Hoes or Jenkins. *Id.* at 364, 40 N.E. at 179. The case thus appears to stand for the proposition that a promise voidable by reason of the promisor's insanity serves as consideration for a return promise. The result, however, can be explained on the ground that the transaction was apparently fair and was relied on by Hoes. See *infra* text accompanying notes 109-15. At the end of the opinion, moreover, Holmes suggested that the true basis for the holding might have been part performance: the court expressed "no opinion as to the law in case of a bilateral contract wholly unexecuted on both sides." *Atwell*, 163 Mass. at 364, 40 N.E. at 180.

a. The Flower Bond Rules

The flower bond courts' view is unsatisfactory both with respect to declared and irreversible incompetence and with respect to undeclared and reversible incompetence. The idea that the agent's acts should be void in cases of declared and irreversible incompetence is admittedly consistent with the conception of agency as a consensual relation. It can, however, easily lead to results that are contrary to the interests of the incompetent and/or the third party.

With respect to declared incompetence, the rule is inappropriate in two respects. First, a principal whose incompetence has been judicially declared may recover. If he does, and then affirms a transaction entered into by his agent during his incompetence, the policies of liberty and the security of transactions militate in favor of enforcement of the transaction as much as they would if his incompetence had been undeclared. Second, even in the absence of such an affirmation, the change in the policy calculus that a declaration of incompetence dictates fails to justify automatic invalidation of the transaction. Despite the declaration, the third party may be unaware of the principal's condition.⁶⁷ Even if the declaration notifies the third party, however, the only logical response on the part of a court is to give less than usual consideration to his interests. To automatically invalidate all of the agent's acts is potentially to deprive the principal of the benefit of favorable transactions, thereby disregarding his interests along with those of the third party.⁶⁸

67. Professor Weihofen argues that the status of public records of incompetency proceedings does not justify the use of a rule of constructive notice to the public:

Any rule that gives conclusive effect to a judicial proceeding and deems all members of the public to have 'constructive notice' of such proceedings demands a system of records that enables people to acquire actual knowledge. Court records of adjudication are of course public, but few states have a system for centralizing such records. A person dealing with another whose competency he wishes to check may examine local court records and find nothing; yet the other party may have been adjudicated in some other county.

Weihofen, *supra* note 7, at 214.

68. Virtue takes the position that the "contracts of an adjudicated incompetent under active guardianship should be treated as void, except where handled through the guardianship." Virtue, *Restitution from the Mentally Infirm* (pts. 1 & 2), 26 N.Y.U. L. Rev. 132, 291, 319 (1951). She points out earlier, however, that "each court confronted with the contract of an incompetent examines the controversy for itself, with more real attention to the nature of the infirmity and the fairness of the contract than is given the legal status of the allegedly incapacitated party." *Id.* (pt. 1) at 147 (footnote omitted). She also acknowledges that enforcement of certain transactions can benefit an incompetent. *See supra* note 59.

Weihofen argues that the appointment of a guardian does not necessarily mean that all contracts of his ward should be held to be void:

[The guardian] has all the power and discretion he needs to discharge his duties if the ward's contract is voidable. To hold it void, and thus allow the healthy party to avoid (as he may if 'void' is to be taken literally), does not in any way

Although the *Restatement (Second) of Agency*⁶⁹ and some secondary authorities⁷⁰ support the position taken by the flower bond courts, the agency cases do not require it. The cases involving principals who were declared to be incompetent fall into two categories. In the first category, courts have been asked to rule on the prospective effects of declarations rather than on the consequences of transactions that have already taken place. The prospective decrees have been to the effect that the agents' authority is terminated, but the opinions can be nothing more than dicta with respect to particular transactions.⁷¹ In the second category, courts have in fact invalidated transactions. In each of the cases, however, the decision is explicable otherwise than by reference to the declaration.⁷² In neither category, therefore, do the decisions require that courts invalidate transactions simply on the basis of the principals' legal status.⁷³ In at least one case, moreover, a

aid the guardian in his duties; it reduces rather than augments his discretion. It also reduces the discretion that the court has under the voidable rule to weigh the equities and tailor the remedy to the facts of the particular case. Thus cases declaring void an adjudicated incompetent's contract to retain an attorney, entered into without his guardian's consent, could better reach the same result by holding that the guardian had power to affirm or disaffirm.

Weihofen, *supra* note 7, at 229.

69. The *Restatement's* general provision with respect to the principal's loss of capacity is to the effect that it terminates the agent's authority. RESTATEMENT (SECOND) OF AGENCY §§ 120, 122(1) (1957). A declaration of the principal's incompetence terminates the agent's authority even where the power was purportedly durable: "P authorizes A to sell Blackacre for not less than \$5000, the authority to continue for one year and not to terminate upon P's death or incapacity. P is adjudicated incompetent without A's knowledge. A's authority to sell Blackacre is terminated." *Id.* § 122 illustration 1. If the principal recovers and affirms the transaction, he is still not bound. *Id.* § 84(2). Thus: "[p]urporting to act for P, judicially declared to be insane, A buys clothes from him. P is declared sane and affirms. He is not liable on the contract, although he may be subject to restitutional liability or to liability upon a new contract." *Id.* § 84 illustration 6.

70. See, e.g., E.W. HUFFCUT, *THE LAW OF AGENCY* § 71(2) (2d ed. 1901); Mukatis, *Does the Agency Die When the Principal Becomes Mentally Incapacitated?*, 7 U. PUGET SOUND L. REV. 105, 108 (1983).

71. See, e.g., *Capital Nat'l Bank v. Stoll*, 220 Cal. 260, 30 P.2d 411 (1934); *Fulton Nat'l Bank v. Haldeman*, 29 Pa. D. & C. 331 (C.P. 1936). For discussion of these cases, see *supra* note 20.

72. See *Joost v. Racher*, 148 Ill. App. 548 (1909) (the court, having notice of the principal's condition, refused to deal with the agent; the effect of notice is discussed *infra* text accompanying notes 94-98); *Witherington v. Nickerson*, 256 Mass. 351, 152 N.E. 707 (1926) (self-dealing by agent; agent's self-dealing is discussed *infra* text accompanying note 98); *Evans v. York*, 217 S.W.2d 749 (Mo. Ct. App. 1949) (same); *In re Sellers' Estate*, 154 Ohio St. 483, 96 N.E.2d 595 (1951) (agent's action was of essentially testamentary significance and no legitimate interests militated in favor of enforcement; transactions of testamentary significance are discussed *infra* text accompanying notes 91-93); *Harrington v. Bailey*, 351 S.W.2d 946 (Tex. Civ. App. 1961) (transaction was possibly not authorized by the power of attorney and was unfair to the principal; the case is discussed *infra* note 118).

73. Professor Mukatis states that "the great weight of authority holds that an adjudication of incompetency terminates or suspends the authority of the agent regardless of knowledge or notice." Mukatis, *Does the Agency Die When the Principal Becomes Mentally Incapacitated?*, 7 U. PUGET SOUND L. REV. 105, 108 (1983). The cases he cites in support of his proposition,

court declined to invalidate a transaction entered into by an agent acting for a principal who had been declared incompetent.⁷⁴

however, do not sustain it. First, he cites *Joost v. Racher*, 148 Ill. App. 548 (1909), and *Harrington v. Bailey*, 351 S.W.2d 946 (Tex. Civ. App. 1961), both of which are explicable on other grounds. See *supra* note 72.

Second, he cites several other cases that at best include dicta supporting the proposition and at worst are simply irrelevant: *Hart v. Feely*, 109 F. Supp. 3, 5 (M.D. Pa. 1953) (the principal's guardian was an indispensable party, the joinder of whom ousted the court's jurisdiction); *Emporium v. Boyle*, 7 Alaska 80 (1923) (the power that was at issue was not an agency power because it was exercisable for the benefit of its holder rather than its grantor, see *W. SEAVEY, supra* note 9, § 11C); *Jackson v. Hall*, 139 Kan. 852, 32 P.2d 1055 (1934) (same); *Renfro v. City of Waco*, 33 S.W. 766 (Tex. Civ. App. 1896) (the suit was against a third party, not in order to set aside a transaction entered into by the third party and the principal's agent, but rather on the basis that the third party made an improper payment to the agent in the course of performing under an existing contract).

Third, he cites *Millman v. First Fed. Sav. & Loan Ass'n*, 198 So. 2d 338 (Fla. Dist. Ct. App. 1967), which is inconsistent with the proposition. For an analysis of the case, see *infra* note 74.

74. In *Millman v. First Fed. Sav. & Loan Ass'n*, 198 So. 2d 338 (Fla. Dist. Ct. App. 1967), the principal, while competent, established a savings account in his name and that of his stepdaughter whereby the two held funds jointly and with rights of survivorship. While still competent, he gave his wife a power of attorney enabling her to withdraw funds from the account. He was thereafter declared incompetent, and the court's order was recorded in the appropriate public record. *Id.* at 339. About two weeks later, his wife withdrew all the funds from the account and, about six weeks after that, he died. His stepdaughter sued the bank, claiming that the withdrawal was illegal and that she was therefore entitled to the funds. *Id.* The court held that the bank was not liable. *Id.* at 341.

According to the opinion, there were at least two grounds for a contrary result. First, the court stated that under the common law of the state an adjudication of the principal's incompetence would revoke the authority of his agent. *Id.* at 340. Under the state's common law rule, the declaration of the principal's incompetence meant that his wife was no longer his agent, that the payment to her was improper, and that the bank was liable. The court's response to that argument was that the contract between the principal and the bank took the case out of the general rule regarding incompetence. The principal's savings book provided in part:

[A]ny payment made in good faith to any person producing the book, either before or after the death of the account holder, shall be a valid payment to discharge the [bank] in the absence of prior receipt by the [bank] of written notice that the book has . . . fallen into the hands of unauthorized person or persons.

Id. The bank's ignorance of the principal's condition meant, in the eyes of the court, that the payment was made in good faith within the meaning of the contract, and was therefore a discharge of the bank's obligation.

The court could have come to a different conclusion about the contract. According to the opinion, Florida law provided as follows:

After the judgment adjudicating a person to be mentally incompetent is filed in the office of the county judge, such person shall be presumed to be incapable, for the duration of such incompetency, of managing his own affairs or of making any gift, contract, or any instrument in writing which is binding on him or his estate. The filing of said judgment shall be notice of such incapacity.

Id. at 341 (quoting FLA. STAT. § 394.22(10)(a) (1951) (repealed 1971)). The principal's daughter interpreted that provision to mean that the bank had notice of the principal's condition as a result of the filing of the order, and its payment to his wife was therefore not in good faith within the meaning of the contract. *Id.* at 340-41. The court refused, for two reasons, to accept that argument. First, it read the contract as meaning that only actual knowledge would make the bank liable. *Id.* at 341. Second, it read the statute narrowly, so as to make the constructive

With respect to irreversible incompetence, the flower bond rule may be relatively unimportant because it will be applied infrequently. In the few cases in which courts decide to adopt it, however, it could produce unfortunate results. The rule, by definition, becomes relevant only when a court is satisfied that the principal has no chance to recover. Judges will seldom reach that conclusion with any degree of assurance.⁷⁵ Even where a court has so decided, however, the application of the rule is without justification and potentially harmful to the incompetent. In theory, justification might be found in the idea that those responsible for an incompetent who cannot recover should be encouraged to use guardianship as the vehicle for his care. Courts are probably less receptive now than they were in the past to the idea that they should encourage the use of guardianships.⁷⁶ Even if a court accepts that idea, however, it should reject a rule that voids transactions entered into before the earliest time at which a guardian could be appointed,⁷⁷ and deprives the principal of the benefit of favorable transactions.⁷⁸ The interests of both the principal and the third party are potentially adverse to

notice argument available to the principal's estate but unavailable to his daughter. *Id.* In so doing, it ignored the fact that the daughter was, according to the savings account book, his successor with respect to the funds. See Langbein, *The Nonprobate Revolution and the Future of the Law of Succession*, 97 HARV. L. REV. 1108, 1112 (1984) (noting the testamentary nature of savings account trusts).

The second basis for a contrary holding was that, apart from the common law of agency and the contract, the statute regarding the declaration meant that the transaction was not binding on the principal's daughter. The court's narrow reading of the statute, however, made that argument unavailable to her. *Millman*, 198 So. 2d at 341.

The relevant Uniform Commercial Code provision, which became effective in Florida after the transaction, resolves the issue in favor of the bank:

A payor or collecting bank's authority to accept, pay or collect an item or to account for proceeds of its collection if otherwise effective is not rendered ineffective by incompetence of a customer of either bank existing at the time the item is issued or its collection is undertaken if the bank does not know of an adjudication of incompetence. Neither death nor incompetence of a customer revokes such authority to accept, pay, collect or account until the bank knows of the fact of death or of an adjudication of incompetence and has reasonable opportunity to act on it.

FLA. STAT. ANN. § 674.4-405(1) (1980).

75. In recent years many commentators have asserted that courts should not attempt to evaluate incompetents' chances of recovery for the purpose of determining appropriate medical treatment. See, e.g., Note, *Appointing an Agent to Make Medical Treatment Choices*, 84 COLUM. L. REV. 985, 995 (1984).

76. A court recently observed that the Florida statute providing for durable powers of attorney had "the beneficial effect of avoiding the time, expense and embarrassment involved in having to establish guardianships for incompetent persons." *In re Estate of Schriver*, 441 So. 2d 1105, 1106 (Fla. Dist. Ct. App. 1983).

77. In *Campbell v. United States*, 657 F.2d 1174 (Ct. Cl. 1981), for example, had Campbell's incompetence been clearly permanent, the rule would have made his son's purchase of the bonds ineffective even though, according to the court, it took place before a guardian could be appointed. *Id.* at 1177-78. For the facts of the *Campbell* case, see *supra* text accompanying notes 23-24.

78. See Weihofen, *supra* note 7, at 229.

the rule, and neither the *Restatement (Second) of Agency* nor the agency case law requires it.

The rule of voidability that the flower bond courts adopted for cases of undeclared and reversible incompetence is inappropriate because it fails to distinguish between third parties who have tried to take advantage of incompetent principals and those who have acted in good faith. While a rule of voidability makes sense where the third party behaved improperly, it is not appropriate where he acted in good faith.

Although the rule announced in the flower bond cases was couched in broad terms, and was applied in situations involving their parties who acted in good faith, it is by no means required by the holdings. In none of the cases did either the seller of the bonds or the principal attempt to withdraw from the transaction. The results therefore mean only that the agent's act is effective where neither the third party nor the principal challenges it. The cases can be understood as products of the voidability rule, but they are also explicable on other grounds.⁷⁹ Nor is the rule required by the decisions that the courts purported to follow.⁸⁰

79. The transactions were executed and almost undoubtedly fair. See *infra* text accompanying notes 109-15.

80. Cases supporting a rule of voidability would be cases in which third parties' interests in withdrawal and enforcement were disregarded, while incompetent principals' interests in withdrawal and enforcement were protected. The group of cases cited by the flower bond courts does not fit that description. Only six of the cases involved transactions entered into by agents. Two of the six are irrelevant because they involved no claims that the principals were incompetent. See *Martin v. Judd*, 60 Ill. 78 (1871); *Wing v. Lederer*, 77 Ill. App. 2d 413, 222 N.E.2d 535 (1966). Another is inconsistent with a rule of voidability in that the court upheld the third party's interest in enforcement of the transaction. See *Merritt v. Merritt*, 43 A.D. 68, 59 N.Y.S. 357 (1899) (also cited *infra* notes 111, 113). The other three appear to support the rule in part in that they resulted in denials of third parties' requests for enforcement. In all three, however, there were alternative grounds for the results. See *Estate of Dierks v. Commissioner*, 40 T.C. 539 (1963) (third party was aware of the principal's condition; the case is discussed *infra* note 95); *Dann v. Sands*, 38 A.D.2d 661, 327 N.Y.S.2d 222 (1971) (self-dealing by agent; agent's self-dealing is discussed *infra* text accompanying note 98); *In re Berry's Estate*, 69 Misc. 2d 397, 329 N.Y.S.2d 915 (Surr. Ct. 1972) (same).

Of the cited cases not involving agents, two are simply irrelevant. See *Estate of Dreyer v. Commissioner*, 68 T.C. 275 (1977) (involving a question of whether a decedent's estate could renounce an interest in property); *Dean v. Estate of Atwood*, 221 Iowa 1388, 212 N.W. 371 (1927) (involving no claim of incompetence).

In two others, the competent parties' interests in enforcement were protected on the basis of ratifications by recovered incompetents. See *In re Kroll's Estate*, 8 Misc. 2d 133, 169 N.Y.S.2d 495 (Sur. Ct. 1957); *Gaston v. Copeland*, 335 S.W.2d 406 (Tex. Civ. App. 1960).

Four cases are inconsistent with the voidability rule in that the courts enforced transactions at the behest of competent parties in the absence of ratifications. See *Kevan v. John Hancock Mut. Life Ins. Co.*, 3 F. Supp. 288 (W.D. Mo. 1933); *In re Gensicke's Estate*, 237 N.W. 333 (Iowa 1931); *Blinn v. Schwarz*, 177 N.Y. 252, 69 N.E. 542 (1904); *Neill v. Pure Oil Co.*, 101 S.W.2d 402 (Tex. Civ. App. 1937).

Five cases offer apparent support for the rule but should be understood as based on other grounds. See *Luhrs v. Hancock*, 181 U.S. 567 (1901) (transaction was executed and apparently fair; fairness of the transaction is discussed *infra* text accompanying notes 109-15); *Atwell*

b. The Code Rule

The Code's rule under which a traditional power of attorney continues to be effective as to third parties who are without actual knowledge of the principal's condition is preferable to the flower bond rules in that it protects the interests of innocent third parties and makes no distinctions among varieties of incompetence. The Code addresses only powers of attorney, however, and the rule makes dispositive the state of mind of the third party without reference to any other features of the transaction. Under the Code the principal would be bound, for example, where a contract was made and the third party discovered the principal's condition before making any change of position in reliance. Particularly if the contract were unfair to the incompetent, there would be no policy basis for enforcing it, yet the Code would require that it be upheld. In failing to take account of the interests of the principal, and in being overly solicitous of the interests of the third party, the Code provision is too simplistic to govern adequately the use of powers of attorney or serve as a model in cases involving other agency relationships.

C. Alternative Rules

The shortcomings of both the flower bond and code rules could be avoided by the use of a different set of rules that is more responsive to the interests of the parties and better reflects what the courts actually do in agency cases. Under the alternative rules, the first question a court would ask is whether the agent's act has been ratified, either by the principal following recovery or by someone entitled to act on his behalf at a time when he was still

v. Jenkins, 163 Mass. 362, 40 N.E. 178 (1895) (same; for a statement of the case see *supra* note 66); *Ortelere v. Teachers' Retirement Bd.*, 25 N.Y.2d 196, 250 N.E.2d 460, 303 N.Y.S.2d 362 (1969) (competent party had notice of incompetent's condition; the effect of notice is discussed *infra* text accompanying notes 94-98); *Finch v. Goldstein*, 245 N.Y. 300, 157 N.E. 146 (1927) (same); *Bennett v. Romos*, 151 Tex. 511, 252 S.W.2d 442 (1952) (transaction was executed and apparently fair; executed and fair transactions are discussed *infra* text accompanying notes 109-15).

In three cases, courts more nearly applied the voidability rule. See *Reeves v. Hunter*, 185 Iowa 958, 171 N.W. 567 (1919) (the court permitted the incompetent to disaffirm the transaction mainly on the basis that he was under guardianship; the effect of guardianship is discussed *supra* note 68); *Verstandig v. Schlaffer*, 296 N.Y. 62, 70 N.E.2d 15 (1946) (incompetent's estate was permitted to avoid the transaction only if it could restore the status quo ante; restoration of the status quo is discussed *infra* notes 94); *Moore v. New York Life Ins. Co.*, 266 N.C. 440, 146 S.E.2d 492 (1966) (incompetent's estate was permitted to avoid a transaction that turned out to be disadvantageous to it; disadvantageous transactions are discussed *infra* text accompanying notes 116-18).

incompetent.⁸¹ The answer to that question will determine whether others need to be asked.

1. Ratification

If a court finds that an agent's act has been freely affirmed by an appropriate person, as a general rule it should treat the act as effective to bind the principal. An appropriate person is the principal if he has recovered, someone entitled to represent him if he is still incompetent,⁸² or, under

81. An alternative starting point is the idea that some periods of incompetence are so brief that they should not affect the agency relation at all. The *Restatement* states that "[v]ery brief periods of insanity caused by the temporary mental or physical illness of the principal do not destroy the power of a previously appointed agent to act in his behalf." RESTATEMENT (SECOND) OF AGENCY § 122 comment d (1957). Seavey appears to agree. He states that the principal need not have an active mind at the time the agent acts; he or she can, for example, go to sleep without depriving the agent of authority. W. SEAVEY, *supra* note 9, § 48C. Sell states that "very brief periods of insanity will not terminate the agent's authority even though the principal could not then appoint another agent." W. SELL, AGENCY § 223 (1975). This position makes sense in light of the fact that perfect control by the principal is probably impossible in all agency relationships. Incompetence that is so brief as to leave the situation essentially unchanged should not affect the agent's authority because it does not significantly increase the risks that the principal undertook when he entered into the relation. The scope of a rule to that effect would remain narrow if it were applied only when the incompetence lasted for at most a few hours.

This article does not advocate an exception for very brief insanity even where, on the whole, it creates relatively little interference with the principal's control over the agent. While the principal undertakes a certain amount of risk in appointing an agent, he probably does not undertake the particular risk of inability to control the agent because of lack of capacity, even for a brief period. In addition, it would often be very difficult for a court to evaluate the importance of the risk of brief incompetence in relation to the overall amount of risk that the principal initially assumed.

82. The range of acts that a guardian or conservator could ratify would only be as great as the scope of his authority to act directly, rather than through an agent. For an argument that the scope of a guardian's authority is unduly limited, see Comment, *The Effect of Guardianship on Estate Plans*, 65 MICH. L. REV. 1613 (1967). For a case in which the court concluded that a conservator ratified a contract see *Bankers Trust Co. v. Martin*, 51 A.D.2d 411, 381 N.Y.S.2d 1001 (1976). In *Bankers*, the principal gave a power of attorney to the bank at a time when he was, as far as the evidence in the case indicated, competent. *Id.* at 412, 381 N.Y.S.2d at 1003. At a point not specified in the opinion, the bank was appointed his conservator. Acting under the power of attorney, it then made a contract for the sale to the defendants of a parcel of his real estate. The defendants refused to complete the sale, claiming that the principal was incompetent when the contract was made. *Id.* at 412, 381 N.Y.S.2d at 1002-03. The court upheld a grant of summary judgment requiring the defendants to pay damages for breach of the agreement. *Id.* at 414, 381 N.Y.S.2d at 1004. Even if the principal was incompetent when the bank acted in its capacity as agent, the agreement might nevertheless be "ratified and approved by the incompetent person upon recovering his competency or by a duly authorized person on behalf of the incompetent." *Id.* at 412, 381 N.Y.S.2d at 1003 (citations omitted). The bank, as conservator, was a duly authorized person:

In this case the record shows that the bank as conservator ratified the contract.

Upon proper application to the Supreme Court, a judgment was granted approving and confirming the proposed sale to appellants and directing the conservator to convey the real property to appellants in accordance with the terms and conditions of the contract.

Id. at 413, 381 N.Y.S.2d at 1003. An alternative basis for the decision is that the transaction was partly executed and apparently fair. See *infra* text accompanying notes 109-15.

certain circumstances, his successor in interest.⁸³ The court should take care to establish that any affirmance by the principal was in fact freely made when he was competent. It should also hold the transaction to any standards of substantive fairness that apply to other transactions of the same kind. Having done so, however, and having concluded that the agent's act would have been effective immediately had it not been for the principal's incompetence, it should enforce the transaction. Had Lionel Campbell recovered and freely affirmed his son's purchase,⁸⁴ for example, the purchase should have been enforceable on that basis alone.

The *Restatement (Second) of Agency* is in accord with this position, at least with respect to affirmances by principals who have recovered from undeclared incompetence.⁸⁵ Ratification has also found acceptance in the case law, although it has not become well established as an independent basis for upholding an agent's action. Of the courts deciding flower bond cases in favor of taxpayers, five took the position that the estates of the decedents had ratified the purchases,⁸⁶ while the sixth declined to adopt that idea.⁸⁷ All of the cases could probably have been decided the same way on other grounds.⁸⁸ In the earlier agency cases, the ratification principle is

83. The rules with respect to ratification by the incompetent's successor(s) in interest should probably not be different from those that apply where the transaction is entered into directly between an incompetent and a competent party. For a summary of those rules, see Weihofen, *supra* note 7, at 232-34.

84. For a summary of the facts in *Campbell v. United States*, 657 F.2d 1174 (Ct. Cl. 1981), see *supra* text accompanying notes 23-34.

85. The *Restatement* includes a comment stating that "[e]ven where there is a pronounced mental incompetency, there may be ratification of previously executed transactions during lucid intervals." *RESTATEMENT (SECOND) OF AGENCY* § 122 comment d (1957). The Institute's semantics are not completely consistent. See *id.* § 82 comment a. The *Restatement's* commitment to the ratification rule is nevertheless clear:

Purporting to act for P, who is mentally incompetent, but not judicially declared to be incompetent, A buys a diamond ring from T, who knows of P's condition. Later, P acquires full capacity and tells T that he will keep the ring. He is subject to liability for the purchase price of the ring.

Id. § 86 illustration 5. See also *id.* § 84 comment c, § 100 comment d. The Institute does not offer guidance with respect to the effect of an affirmance by someone other than the principal, except to say that, in general, ratification can be effected by a duly authorized agent. *Id.* § 87 comment c, § 93(3). The *Restatement* expressly declines to take a position as to "[t]he power of an executor or administrator to ratify acts done in the lifetime of and for the decedent." *Id.* § 84 comment e.

86. See *United States v. Price*, 514 F. Supp. 477, 480 (S.D. Iowa 1981); *Silver v. United States*, 498 F. Supp. 610, 612 (N.D. Ill. 1980); *Estate of Watson v. Simon*, 442 F. Supp. 1000, 1002-03 (S.D.N.Y. 1977), *rev'd on juris. grounds sub nom.* *Estate of Watson v. Blumenthal*, 586 F.2d 925 (2d Cir. 1978); *Campbell v. United States*, 657 F.2d 1174, 1178 (Ct. Cl. 1981); *Estate of Pfohl v. Commissioner*, 70 T.C. 630, 636 (1978).

87. See *United States v. Manny*, 645 F.2d 163, 169 (2d Cir. 1981).

88. The transactions were executed and almost undoubtedly fair. See *infra* notes 109-15 and accompanying text.

frequently approved in dictum⁸⁹ There are, moreover, three cases in which it functioned, at a minimum, as an alternative basis for upholding the agents' actions.⁹⁰

2. Balancing Interests

In the absence of a valid ratification, a court should begin with the idea that, because the principal could not consent to the agent's action, it was simply ineffective. The court should then decide, based on the nature of the transaction, whether it should nevertheless be enforced against either the third party alone or both the third party and the principal. A balancing of the interests involved may dictate that some form of enforcement is appro-

89. For example, in a frequently cited case the court stated:

[T]he insanity of the principal, or his incapacity to exercise any volition upon the subject, by reason of an entire loss of mental power, operates as a revocation, or suspension for the time being, of the authority of an agent acting under a revocable power. If, on the recovery of the principal, he manifests no will to terminate the authority, it may be considered as a mere suspension. And his assent to acts done during the suspension may be inferred from his forbearing to express dissent when they came to his knowledge.

Davis v. Lane, 10 N.H. 156, 159 (1839) (citations omitted).

90. In *San Francisco Credit Clearing House v. MacDonald*, 122 P. 964 (Cal. Dist. Ct. App. 1912), the principal gave a power of attorney to one of his two partners in business. The partnership, which owed the principal \$19,000, was dissolved. At a time when the principal's condition was such that any contract made by him personally would have been voidable, *id.* at 966, his former partner exercised the power of attorney to make a settlement with the third partner respecting the latter's share of the debt to the principal. The third partner executed a note for \$4,000, payable to the principal, in exchange for a release of the principal's claim for any amount in excess of that sum. The principal then recovered and assigned the note to the plaintiff "as trustee and for the purpose of collection." *Id.* at 965. The court held that the \$4,000 note was enforceable on two grounds. First, the transaction was not void but rather voidable by the principal, who did nothing to avoid it. Second, the principal's endorsement and assignment of the note were sufficient to constitute ratification. *Id.*

In *Bankers Trust Co. v. Martin*, 51 A.D.2d 411, 381 N.Y.S.2d 1001 (1976), the court said that the principal's conservator ratified a contract made by it under a power of attorney at a time when, for purposes of the opinion, the principal was incompetent. For a fuller explanation of the case, see *supra* note 82. For an alternative explanation of the result, see *infra* text accompanying notes 109-15.

In *Bishop's Estate*, 30 Pa. D. 149 (1920), the principal, who had a savings account, gave her cousin a power of attorney authorizing withdrawals from the account. The principal subsequently had "a stroke of apoplexy," *id.* at 150, after which her cousin withdrew funds from the account and used them to pay her medical bills and household expenses until she died. Over the period of about 14 months during which the withdrawals took place, the principal "was irrational at times and at others knew what was going on about her." *Id.* The court found that she was aware of and approved the withdrawals. *Id.* At her death, the principal left all the money in the bank account to three legatees. One of the legatees argued that her illness revoked the power of attorney and that, consequently, all funds withdrawn after its onset should be returned to the account, the cost of her care being "borne proportionally by all the personal estate." *Id.* The court upheld the withdrawals, saying that "it would seem that the right to continue [them] even after her stroke, necessarily followed, in that, with knowledge that she was being supported from funds withdrawn from this account, she did not demur." *Id.* at 151.

prate. In the course of its analysis of the transaction, the court's first question should be whether it had any significant effect on the principal during his life.

Acts of agents not affecting their principals should seldom be given effect. The policy of protecting the incompetent does not come into play in a case in which his interests are not at stake. Only if other policies, such as protection of deserving members of the incompetent's family⁹¹ or fairness to third parties who assert compelling claims of good faith reliance,⁹² militate strongly in favor of enforcement should transactions be upheld. In general, what little case law there is on the point seems consistent with this view.⁹³

In a case in which the interests of the principal are at least potentially at stake, the first question the court should ask is whether the third party was aware of the principal's condition at the time of his entry into the transaction.

91. See Green, *Public Policies*, *supra* note 47, at 1216-19.

92. For an example of such a claim of reliance, see *supra* note 57.

93. In *First Nat'l Bank v. Oppenheimer*, 23 Ohio Op. 2d 19, 190 N.E.2d 70 (P. Ct. 1963), the principal set up an inter vivos trust that provided, inter alia, for a particular disposition of the trust property on his death. He retained the right to revoke the trust in whole or in part by means of an instrument in writing signed by him and delivered to the trustee during his lifetime. *Id.* at 20, 190 N.E.2d at 71. He then executed a will purporting to revoke that part of the trust dealing with the disposition of the property after his death, and handed the will to his brother with instructions that it be delivered to the trustee. *Id.* He later became incompetent, and while he was in that state his brother carried out his instructions. The court held that the delivery was ineffective to revoke the trust. *Id.* at 24, 190 N.E.2d at 75. The result was that at least part of the property held by the trustee poured over into a trust for various members of the principal's family, but the opinion does not indicate what percentage of the estate that part was, how the other part was disposed of, or what the disposition would have been had the revocation been effective. The decision is understandable in light of the absence of evidence that the revocation would have produced a disposition of the property that was preferable in policy terms.

In *In re Berry's Estate*, 69 Misc. 2d 397, 329 N.Y.S.2d 915 (Sur. Ct. 1972), the principal gave a power of attorney to her niece, and later had a "cerebral accident," after which she remained in a comatose or semi-comatose condition until her death. The day after she became ill, her niece, acting under the power of attorney, deposited \$109,000 of the principal's funds in a Totten trust account in the name of the principal in trust for the niece's mother. *Id.* at 397, 329 N.Y.S.2d 915-16. After the principal died, her other distributees and their assigns argued that the principal was incompetent when the deposit was made, which meant that the niece's authority under the power of attorney was then suspended or revoked and the deposit was ineffective. *Id.* at 397-98, 329 N.Y.S.2d at 915-16. The court concluded that, as a matter of law, their argument was valid. *Id.* at 400, 329 N.Y.S.2d at 918. The decision is logical because the feature of the transaction that was in dispute was the provision for the disposition of the property after the principal's death and there was no showing that the niece's mother was a particularly deserving recipient.

There are two alternative explanations for the result. First, as the court pointed out in *United States v. Manny*, 645 F.2d 163, 168 (2d Cir. 1981), the niece's action was very close to, if not an example of, self-dealing. The effect of self-dealing is discussed *infra* text accompanying note 98. Second, to the extent that the deposit changed the principal's estate plan, it should have been ineffective because the act of making a will is not delegable to an agent. W. SEAVEY, *supra* note 9, § 13. An agent can execute a will for the principal according to his instructions, *id.*, but the niece in *Berry* was not carrying out the principal's directions when she made the deposit in trust for her mother.

If the answer to that question is yes, the court should hold that the transaction is voidable at the request of the incompetent or his successors, but not at the request of the third party. If the answer to that question is no, the court should examine the transaction further before deciding whether it should be enforced.

If the third party knew or had reason to know of the principal's incompetence at the time of his entry into the transaction, he should be bound even while the principal has a right of avoidance. A third party may in fact believe in good faith that the agent's actions are effective in spite of the principal's condition, but to make an exception to the rule of voidability in such a case would be to permit the third party to act in disregard of basic legal principles of which he should be aware. Moreover, assertions of good faith might well be difficult to controvert even if false. When a court is completely convinced of the third party's good faith, it can mitigate the effects of the voidability rule in various ways,⁹⁴ but it should not abandon the rule.

This position finds support in the cases. Probably because third parties who know they are dealing with agents of incompetents seldom enter into transactions that favor the incompetents, the cases have not involved efforts by the third parties to avoid the transactions. They have, however, involved claims that the incompetent principals were not bound, and the courts have upheld those claims.⁹⁵ Even where the third parties have apparently acted

94. In most jurisdictions, for example, the courts can condition the incompetent's right to avoid on his restoration of any benefits received from the competent party. See Weihofen, *supra* note 7, at 235; Comment, *supra* note 3, at 1083. For a case in which the court ordered restoration of the status quo for the benefit of a third party who knew of the principal's condition but still believed in good faith that the agent had authority, see *Lanahan v. Clark Car Co.*, 11 F.2d 820, 825 (3d Cir. 1926). In *Lanahan*, the court found that the principal was, at the time of the transaction, "wholly incapable either to transact or be consulted about business matters," *id.* at 822, but it did not rely on that fact in concluding that the agent's actions were without effect. *Id.* at 824.

95. In *Estate of Dierks v. Commissioner*, 40 T.C. 539 (1963), while the principal was comatose his attorney entered into a settlement with the Internal Revenue Service. The representatives of the Service with whom the attorney dealt were aware of the principal's condition, and the court held that the attorney's action was ineffective. *Id.* at 543. There was no evidence in the case that the settlement was unfair to the principal.

In *Davis v. Lane*, 10 N.H. 156 (1839), the principal's wife, who held a general power to transact business for him, made an assignment to a third party of a note owed to him in the amount of \$50 and received in exchange a release from a note for \$46 and a note for \$4 or \$5. At the time of the transaction, the third party was aware that the principal was "entirely senseless and [that] no hopes were entertained of his recovery." *Id.* at 156. After the principal died, his administrator sued to collect on the note that his wife had assigned to the third party, and the court held that his estate could recover. *Id.* at 162.

In *Matthiessen & Wiechers Ref. Co. v. McMahon's Adm'r*, 38 N.J.L. 536 (1876), the principal owed a refining company \$11,000. While competent, he made an oral agreement with the company under which he was to transfer to it certain goods in exchange for a release from the debt. Because the agreement was not in writing and the consideration for the transfer of the goods was more than \$30, the principal's promise was, when made, unenforceable under

in good faith and the transactions have been apparently fair or even beneficial to the incompetents, the courts have refused to enforce them at the behest of the third parties.⁹⁶ When courts have found themselves to be third parties with notice of the condition of incompetent principals, they have set appropriate examples by refusing to deal with agents.⁹⁷ Where agents have dealt with themselves, knowing that their principals were incompetent, courts have refused to enforce the transactions.⁹⁸

Each of the flower bond cases involved a situation in which, in all likelihood, the third party was without notice of the principal's incompetence. In such a case, neither the principal nor the third party can be regarded as having done anything improper, and the law's basic goal should be to treat the two in an even-handed fashion. Having begun with the idea that the absence of consent on the part of the principal means that the transaction

the statute of frauds. After he made the bargain, the principal became incompetent, and the general superintendent of his business, who held a power of attorney, delivered the goods to the refining company. At or before the time of the delivery, the company knew or should have known of the principal's condition. *Id.* at 543. If effective, the delivery would have been at once part performance of the agreement and the last step in making it enforceable. The court held that it was ineffective, first because it was not authorized by the power of attorney and second because of the principal's condition. It then stated that, if it were wrong with respect to the first point, the second point could decide the case. *Id.* at 536, 547.

In *Fischer v. Gorman*, 65 S.D. 453, 274 N.W. 866 (1937), the principal executed deeds to real and personal property in favor of two of her good friends and neighbors. She kept the deeds in her possession, but told her maid where they were stored. When the maid was told that the principal could not recover, she was to deliver the deeds to the grantees. Some months later, the principal had a stroke, and the maid delivered the deeds the next morning, *id.* at 455-56, 274 N.W. at 867-68, at a time when the principal was without capacity to contract. *Id.* at 462, 274 N.W. at 871. The principal died early that afternoon. *Id.* at 455-56, 274 N.W. at 868. There was no showing that she ever changed her mind about the gifts, or that her affection for the grantees lessened. On the contrary, there was testimony indicating that, after her stroke, she still cared for them. *Id.* at 460, 274 N.W. at 870. The court nevertheless held that the delivery was ineffective, *id.* at 463, 274 N.W. at 872, emphasizing the transfer's potentially serious consequences for the principal:

In the instant case, the principal must have retained sufficient of her faculties not only to understand the nature of the particular transfers, but also to comprehend that such transfers would divest her of all title to her property, and that such divestiture would remain absolute even though she regained her health.

Id. at 459, 274 N.W. at 870. For an alternative basis for the holding, see *infra* text accompanying notes 116-18.

In *Wallis v. Manhattan Co.*, 2 Hall 495 (N.Y. Super. 1829), the court held that a bank should have honored a power of attorney given by one of its depositors even though it knew him to be incompetent. The decision is understandable in the light of the court's impression that it had to treat the agent's act as either completely effective or completely ineffective, even in a case in which the third party was aware of the principal's condition. *Id.* at 500.

96. See *Lanahan v. Clark Car Co.*, 11 F.2d 820 (3d Cir. 1926); *Estate of Dierks v. Commissioner*, 40 T.C. 539 (1963); *Davis v. Lane*, 10 N.H. 156 (1839).

97. See *Sullivan v. Dunne*, 198 Cal. 183, 244 P. 343 (1926); *Joost v. Racher*, 148 Ill. App. 548 (1909); *Chase v. Chase*, 163 Ind. 178, 71 N.E. 485 (1904).

98. See *Dann v. Sands*, 38 A.D.2d 661, 327 N.Y.S.2d 222 (1971); *In re Berry's Estate*, 69 Misc. 2d 397, 329 N.Y.S.2d 915 (Surr. Ct. 1972) (in which the agent dealt not with herself but with her mother).

should not be enforced, the court should then ask whether the circumstances are such that enforcement is nevertheless appropriate. In the latter event, the cause of action for enforcement should be available to both parties, rather than to the incompetent alone.

Although much of the literature regarding the contracts of incompetents supports the use of a rule of voidability even where the third party acts in good faith,⁹⁹ there is authority for the contrary. The *Restatement (Second) of Contracts* sets forth a general rule of voidability,¹⁰⁰ but also provides that "if the other party did not know of the incompetency at the time of contracting he cannot be compelled to perform unless the contract is effectively affirmed."¹⁰¹ While that language would not have permitted the sellers in the flower bond cases to withdraw after the bonds were delivered, it does recognize the idea that, for at least some period of time, the transaction is binding on neither party. A review of all of the cases in which competent parties have dealt with incompetents without notice of their condition is beyond the scope of this article, but there is at least one case in which the court recognized the inequity involved in binding the competent party alone and refused to do so. In *Rattner v. Kleinman*,¹⁰² the competent party agreed to purchase from the incompetent and her husband a parcel "of citrus fruit land in the valley of the Rio Grande." The price was \$44,000, \$12,000 of which was paid in cash and \$32,000 of which was in the form of promissory notes. The buyer refused to pay according to the notes, the incompetent and her husband sued, and the buyer sought to cancel the transaction and

99. See, e.g., Weihofen, *supra* note 7, at 231.

100. The *Restatement's* language is as follows:

(1) A person incurs only voidable contractual duties by entering into a transaction if by reason of mental illness or defect

(a) he is unable to understand in a reasonable manner the nature and consequences of the transaction, or

(b) he is unable to act in a reasonable manner in relation to the transaction and the other party has reason to know of his condition.

(2) Where the contract is made on fair terms and the other party is without knowledge of the mental illness or defect, the power of avoidance under Subsection (1) terminates to the extent that the contract has been so performed in whole or in part or the circumstances have so changed that avoidance would be unjust. In such a case a court may grant relief as justice requires.

RESTATEMENT (SECOND) OF CONTRACTS § 15 (1979).

101. *Id.* comment d. The *Restatement* suggests, however, that before exercising his right to withdraw from the contract the competent party must give those responsible for the incompetent a chance to have a guardian appointed, presumably so that the guardian can effectively affirm the contract. Thus:

A, an incompetent not under guardianship, contracts to sell land to B, who does not know of the incompetency. A continues to be incompetent. On discovering the incompetency, B may refuse to perform until a guardian is appointed, and if none is appointed within a reasonable time may obtain a decree cancelling the contract.

Id. illustration 2.

102. 36 S.W.2d 249 (Tex. Civ. App. 1931).

recover the \$12,000 already paid.¹⁰³ The court held that, upon proof of the incompetence of one of the sellers, the buyer would be entitled to rescission:

It will be noted that no such doctrine is promulgated that, while the insane person may obtain equitable relief, the sane vendee, without notice of the insanity of the vendor, can obtain no relief. Such doctrine is monstrous and utterly untenable. The evidence as to the sanity of Mrs. Kleiman at the time and subsequent to the execution of the deed should have been heard, and proof made of such insanity. If her condition was unknown to appellant at the time the deed was executed, he is entitled to a rescission of the contract and a judgment for payments already made by him on the land.¹⁰⁴

Cases like *Rattner*, in which the competent party is bound to perform over a period of years, are particularly appropriate for the application of a rule that lets him withdraw in the absence of a ratification. Yet the reason for the rule, though less dramatically evident, is present in any case in which the incompetent can withdraw.

The position of the *Restatement (Second) of Agency* is consistent with that of the *Rattner* court. Under the *Restatement*, the principal's undeclared incompetence makes the agent's acts ratifiable.¹⁰⁵ Where a transaction is such that it can be ratified, withdrawal by the third party before an affirmance by the principal prevents the affirmance from serving as ratification.¹⁰⁶ The Institute's reason for adopting that rule was that it is inappropriate to hold the third party where he receives no consideration for his promise.¹⁰⁷ The problem has not been addressed directly in cases dealing with representation

103. *Id.* at 250.

104. *Id.* at 251.

105. *See supra* note 85 and accompanying text.

106. The *Restatement's* language is as follows: "To constitute ratification, the affirmance of a transaction must occur before the other party has manifested his withdrawal from it either to the purported principal or to the agent, and before the offer or agreement has otherwise terminated or been discharged." RESTATEMENT (SECOND) OF AGENCY § 88 (1957).

107. The Institute argued that the rule

seems obviously fair where the other party to the transaction realizes that the principal is not bound by it, since he should not be required to remain in indecision until a possible ratification. Unless one receives consideration or executes a sealed instrument, he is not bound by agreeing to be bound; if the other party to a transaction with an agent knows that the agent has no power to bind the principal, he gets nothing in return for his promise. But even when he refuses to perform for other reasons, believing himself to be bound, it is not unfair to hold that a subsequent affirmance comes too late to be ratification. If the other party believes that the agent is authorized and is led into the transaction by the misrepresentation of authority on the part of the pseudo agent, admitting that the initial transaction has some validity, it is at least voidable by him as in any transaction entered into as the result of a misrepresentation. It is true that after an affirmance he cannot rescind since the affirmance gives him what he expected. But until ratification has cured the defect, the fact that he is not aware of his right to withdrawal should not deprive him of the right to do so.

Id. § 88 reporter's notes. For the text of the section, see *supra* note 106.

of incompetents. Where agents of competent principals have acted beyond their authority, however, third parties have been permitted to withdraw.¹⁰⁸

After initially regarding the transaction as enforceable against neither party, the court, upon balancing the parties' interests, may find a reason for enforcing it against both of them. The process of weighing interests is not one in which courts will be able to follow hard and fast rules. There is, however, an approach to the problem that they could logically use and that can explain many of the results in the cases. In determining at what point, if any, both parties should be bound, a court should take into account both (1) the fairness of the transaction viewed as an exchange and (2) any reliance of either party on either performance or the prospect of performance by the other. Any fiduciary obligation owed by the third party to the principal should be taken into account in evaluating the fairness of the transaction. If the transaction is fair when viewed as an exchange, any showing of substantial reliance by either party provides a basis for enforcement. Where the transaction is executed, a presumption of reliance may very well make sense. If the transaction is not fair when viewed as an exchange but rather disadvantageous to one party, it should be enforced only if the other party can show reliance that more than makes up for that disadvantage.

The *Restatement (Second) of Contracts* is in accord with the view that, where the transaction is fair, enforcement may be justified.¹⁰⁹ That view is also amply supported in the agency cases, both where the transaction is completely executed and where it is only partly executed. In the category of completely executed transactions that the courts have enforced, the flower bond sales are conspicuous examples. In each case, the price paid for the bond was almost certainly fair. In none of the cases was there any clear evidence of a significant change of position by either party in reliance on the transaction, but such changes very likely took place, particularly on the part of third parties. If the complete execution of a transaction gives rise to a presumption of such changes of position, the transactions in the cases were correctly held to be enforceable. In each case, the court's language concerning voidability was dictum because the seller of the bond made no effort to withdraw from the transaction.

108. Note, *Rescission by Third Party Prior to Principal's Ratification of Agent's Unauthorized Action*, 2 VAND. L. REV. 100 (1948).

109. Under the *Restatement*, the incompetent's power of avoidance "terminates to the extent that the contract has been so performed in whole or in part or the circumstances have so changed that avoidance would be unjust." RESTATEMENT (SECOND) OF CONTRACTS § 15(2) (1979). For the text of the entire section, see *supra* note 100. A review of the non-agency cases addressing the problem is beyond the scope of this article, but the principle of the subsection provides an explanation for the result in *Atwell v. Jenkins*, 163 Mass. 362, 40 N.E. 178 (1895). The case involved a loan that was apparently fair and that was relied on by the incompetent. For a statement of the facts, see *supra* note 66.

In the category of fair but only partly executed transactions, requests for enforcement have also met with a favorable response. In one case involving a mortgage executed by an agent for an incompetent principal the court upheld the transaction;¹¹⁰ in two similar cases, courts held that mortgages could be enforced if certain evidence were produced in future proceedings.¹¹¹ In one of the latter cases, the court required nothing more than evidence of the competence of the principal at the time of the execution of the agent's power of attorney.¹¹² In the other, the court required proof that the third party was without notice and supplied the full consideration referred to in the mortgage.¹¹³ In a case in which the principal and his agent owned a firm that was run by the agent while the principal was, for the purposes of the decision, incompetent, a party who delivered goods to the firm was held to be entitled to recover the price of the goods.¹¹⁴ In a case in which the agent

110. See *Watkins v. Hagerty*, 104 Neb. 414, 177 N.W. 654 (1920).

111. See *First Nat'l City Bank v. Gonzalez & Co. Sucr. Corp.*, 308 F. Supp. 596 (D.P.R. 1970); *Merritt v. Merritt*, 43 A.D. 68, 59 N.Y.S. 357 (1899).

112. *First Nat'l City Bank v. Gonzalez & Co. Sucr. Corp.*, 308 F. Supp. 596, 603 (D.P.R. 1970). There is authority to the effect that in civil law jurisdictions the incompetence or death of the principal affects the agency only if the third party has notice of the principal's condition. Seavey, *supra* note 7, at 893. The author of this article has found no case in either Puerto Rico or Louisiana in which a transaction was upheld that would not also have been upheld under the rules proposed in the article.

113. *Merritt v. Merritt*, 43 A.D. 68, 73-74, 59 N.Y.S. 357, 361 (1899).

114. *Jurgens v. Ittmann*, 47 La. Ann. 367, 16 So. 952 (1895). In *Jurgens*, the third party sued to recover the price of the goods and the estate of the principal moved to dismiss on the ground that the principal was insane when they were sold. *Id.* at 368, 16 So. at 952-53. The trial court rendered judgment in favor of the third party, *id.* at 368-69, 16 So. at 953, and the Louisiana Supreme Court affirmed. *Id.* at 374, 16 So. at 955. The prices charged for the goods were fair, *id.* at 371, 16 So. at 953, and the case is thus one in which a series of fair, partly executed transactions was enforced. There are two possible alternative explanations for the result. First, the court suggested, but did not say, that the transactions were ratified by the curator who was appointed to care for the principal and/or by his estate. *Id.* at 371, 16 So. at 954. The conduct to which the court referred was inaction rather than action. *Id.* For a general discussion of whether inaction can constitute ratification, see RESTATEMENT (SECOND) OF AGENCY § 94 reporter's notes (1957). Second, the principal and his agent were partners, and the court said that the partnership remained in existence despite the principal's incompetence. *Jurgens*, 47 La. Ann. at 371, 16 So. at 954. The court's reasoning on the latter point is open to question. According to the opinion, one of the statutes dealing with the termination of partnerships in Louisiana provided

that if the partnership has been contracted without any limitation of time one of the partners may dissolve the partnership by notifying his partners that he does not intend to remain any longer in the partnership; provided, nevertheless, the renunciation to the partnership be made *bona fide*, and it does not take place unseasonably.

Id. at 372, 16 So. at 954 (quoting LA. CIV. CODE art. 2885). A partner's loss of capacity would mean that he was no longer capable of giving notice, and thus could logically result in the termination of the partnership. Another statutory provision stated, however, that a partnership would terminate when one of the partners was declared incompetent. *Id.* (quoting LA. CIV. CODE art. 2876). If the latter provision controlled, partnership law meant that the undeclared incompetence of a partner left the relation unaffected. Because the principal was declared incompetent after the goods were sold, the partnership was still in existence at the time of the

made a contract for the sale of a parcel of the incompetent principal's real estate, the apparent fairness of the transaction provides an alternative basis for the holding that the contract was enforceable.¹¹⁵

The cases involving unfair transactions are consistent with the idea that the courts should refuse enforcement in the absence of good faith reliance that more than makes up for the unfairness, although none of them has involved unfairness to the third party. In two cases of attempts by attorneys in fact to complete inter vivos gifts of the property of their principals, the courts found the attempts to be ineffective.¹¹⁶ One of the cases involved third parties who were aware of the principal's incompetence, and its holding is consistent with the application of a rule of voidability.¹¹⁷ In the other case, however, there was no evidence that the third party was aware of the principal's condition and the court nevertheless construed narrowly the grant of authority to the agent. The result was that the gift was not given effect.¹¹⁸

sales and could account for their validity.

Modern partnership law, at least as set forth in the Uniform Partnership Act, is that "[o]n application by or for a partner the court shall decree a dissolution whenever . . . [a] partner has been declared a lunatic in any judicial proceeding or is shown to be of unsound mind" UNIF. PARTNERSHIP ACT § 32(1)(a) (1969). The Act does not say how a court should treat a transaction entered into by one partner while the other is incompetent.

115. See *Bankers Trust Co. v. Martin*, 51 A.D.2d 411, 381 N.Y.S.2d 1001 (1976). The other basis for the decision was that the transaction was ratified. The case is discussed *supra* note 82.

116. *Fischer v. Gorman*, 65 S.D. 453, 274 N.W. 866 (1937) (discussed *supra* note 95); *Harrington v. Bailey*, 351 S.W.2d 946 (Tex. Civ. App. 1961) (discussed *infra* note 118).

117. *Fischer v. Gorman*, 65 S.D. 453, 274 N.W. 866 (1937) (discussed *supra* note 95).

118. In *Harrington v. Bailey*, 351 S.W.2d 946 (Tex. Civ. App. 1961), the principal was the owner of a biblical manuscript written in Hebrew on goatskin. In 1952, he told his sister that he wanted A. & M. College to have the manuscript, and also dictated to her a note to that effect, placing the note with the manuscript. He made "some effort" to have an official of the college come to his home and pick up the manuscript, but did not succeed and it remained in his possession until 1956. *Id.* at 947. During 1956, he delivered the manuscript to his sister. She testified that the delivery to her was a result of his fear that someone would steal the manuscript from him, and the court pointed out that he later stated to a witness that he was going to give the manuscript to the college. In 1957, he was declared to be of unsound mind. In 1959, his sister, who had been appointed his guardian, delivered the manuscript to the college. *Id.* at 947-48. The opinion refers to no evidence either that the college was aware of the principal's condition at the time of the delivery or that it made any change of position in reliance on the delivery. The court held that the sister's authority was only to hold the manuscript for safekeeping, and therefore no gift resulted when she transferred it to the college. *Id.* The holding is consistent with the principal's intent in a narrow sense; his immediate reason for giving the manuscript to his sister may very well have been to protect it. The decision is, however, inconsistent with the intent he expressed in 1952, and in his conversation with the witness, that the college should have the manuscript. There is, moreover, no positive indication in the case that he intended to keep it in his possession until his death; rather, the available evidence indicated that in 1952 he was frustrated in his intention to make an inter vivos gift. Had the court wanted to sustain the gift, it could have found that the delivery was authorized because it was in accordance with his overall intention. Since the transaction was unfair to the principal when viewed as an exchange and the college showed no reliance upon it, however, a balancing of the interests involved leads to the conclusion that the decision is correct. An

II. DURABLE POWERS—THE IMPLICATIONS OF THE CASES INVOLVING TRADITIONAL POWERS

When a legislature passes a statute providing for durable powers of attorney, it expresses a policy judgment that is fundamentally at odds with traditional thinking about agency. The vacuum that the principal's incompetence traditionally created is filled by the choice that he made, while competent, to be represented by an agent even when unable to consent intelligently to the agent's acts. In theory, courts could simply carry out the legislative policy in favor of giving effect to that choice, and enforce all acts of holders of durable powers. In cases in which the transactions would be upheld even if the powers were not durable, that will very likely be the nature of the judicial response. Transactions that are ratified or that are appropriate in the light of public policy will probably be held valid.

In cases in which neither ratification nor public policy militates in favor of enforcement, however, the courts will be faced with an uncomfortable choice. If they read the statutes literally, they will enforce transactions that they, and probably most people, do not want to see enforced. If they are determined not to enforce those transactions, they will be hard put to find intellectually honest bases for their decisions. In a case involving an unfair transaction, for example, a court could probably say with complete accuracy that neither the legislature nor the principal would consider enforcement appropriate. In such a case, however, the language of the statute and the power of attorney will both call for enforcement. The cases dealing with traditional powers suggest that the judicial response will be to take account of the nature of the transaction even if it means disregarding that language.

The cases to date that have involved the exercise of durable powers are few in number and by no means definitive. They do suggest, however, that the nature of the transaction will continue to play a critical role. Courts have enforced transactions that would have been enforced even if done by the holders of traditional powers.¹¹⁹ The only case in which the transaction

alternative explanation for the result that is inconsistent with the set of rules proposed in this article is that the principal was declared to be incompetent before the manuscript was delivered to the college. See *supra* note 72 and accompanying text.

119. In *In re Estate of Schriver*, 441 So. 2d 1105 (Fla. Dist. Ct. App. 1983), the court permitted the holder of a durable power to exercise the principal's right of election to take against her husband's will, in which she was left nothing, without addressing the question of whether she was competent at the time of the election. In light of the strong public policy in favor of protecting a surviving spouse, the decision is not surprising.

In *In re Estate of Head*, 94 N.M. 656, 615 P.2d 271 (Ct. App. 1980), the court indicated in dictum that a wife could exercise a power of attorney for her husband to amend a trust so as to eliminate the interest of a woman raised by the two of them but unrelated to them by blood. *Id.* at 663, 615 P.2d at 278. The apparent result of the amendment was to increase the share in the trust property of each of the couple's natural daughters. The dictum is understandable, if not necessarily justifiable, in light of the fact that the principal's interests were not affected and the transaction benefitted his natural family.

would have been unenforceable had the power been traditional is one in which there was a legitimate reason, apart from the nature of the transaction, for denying enforcement.¹²⁰ In other cases, however, courts have indicated that they will continue to take account of the nature of the agents' actions and perhaps to find less than straightforward ways to avoid giving them effect. In *Roybal v. Morris*,¹²¹ for example, the attorney in fact sued to set aside a deed given by the principal to the principal's daughter. There was no evidence that the principal was incompetent, but he was unable, because of age and infirmity, to testify at the trial. The court rejected the daughter's motion to dismiss for failure to join an indispensable party, namely the principal, on the basis that the plaintiff was acting as his attorney in fact. It indicated, however, that it might not have been willing to permit that kind of representation if the suit had been potentially disadvantageous to the principal:

Under circumstances wherein a party who has given a power of attorney, is subsequently alleged to have become incompetent, and the agent under the power of attorney asserts legal claims which if successful will divest his principal of property—the trial court has a duty to inquire into the present status of the mental condition of the principal and, if necessary, appoint a guardian *ad litem* to protect and represent the present interests of the [principal] in the litigation.¹²²

The court's willingness to let the attorney in fact represent the principal was thus expressly made dependent on the effect of the representation on the principal's interests.

Identification of all the ways in which courts will avoid enforcing transactions of which they do not approve is probably impossible. The cases, however, suggest at least three potential methods of avoidance. First, in any case in which the agent's interests were even arguably furthered, the transaction can be invalidated as a breach of his fiduciary obligation.¹²³ Second, the court may be able to construe the power of attorney narrowly to come to the conclusion that the agent's action was not authorized.¹²⁴ Third, the court might so construe the statute as to make it simply inapplicable. In *United States v. Price*,¹²⁵ one of the pro-taxpayer flower bond cases, the

120. In *Creasy v. Henderson*, 210 Va. 744, 173 S.E.2d 823 (1970), the principal's sister held a durable power of attorney permitting her to make a "proper" sale of the principal's real estate. *Id.* at 749, 173 S.E.2d at 828. The court refused to approve a sale to the attorney in fact's daughter for about half the value of the property on the legitimate grounds that it was not authorized by the power of attorney and it amounted to a breach of her fiduciary obligation. *Id.* at 749-50, 173 S.E.2d at 828.

121. 100 N.M. 305, 669 P.2d 1100 (Ct. App. 1983).

122. *Id.* at 312, 669 P.2d at 1107.

123. *E.g.*, *Creasy v. Henderson*, 210 Va. 744, 749, 173 S.E.2d 823, 828 (1970).

124. *E.g.*, *Welke v. Wackershauser*, 143 Iowa 107, 120 N.W. 77 (1909) (in which a general, nondurable power of attorney with respect to real estate was held not to authorize a gratuitous conveyance).

125. 514 F. Supp. 477 (S.D. Iowa 1981).

court suggested that Iowa's durable power of attorney statute, which tracked the language of the Uniform Act, might be applicable only if the principal's incompetence were permanent.¹²⁶ If that construction were generally adopted, the statutes would be effective in only a narrow range of cases.

CONCLUSION

In cases involving traditional agency powers, courts should continue to give prospective instructions to the effect that the incompetence of the principal terminates the relation. Where an agent has already acted, however, the judicial response should be based on a careful evaluation of all the legitimate interests involved in the transaction. It should not be based on the idea that transactions entered into by or on behalf of an incompetent are, or necessarily should be, voidable. A court's analysis of the various interests involved in the transaction should be explicit. More open discussion of those interests would lead to a better understanding of the ways in which they bear on enforceability.

In cases involving durable powers, courts should respect the legislative judgment that a need for such powers exists, as well as the choices of principals to be represented by agents. No court should assume, however, that either a legislature or a principal contemplated enforcement of an unfair transaction or series of transactions entered into by the holder of a durable power. The fairness of any given transaction can be no less relevant where the power is durable than where the power is traditional. Explicit discussion of that factor, moreover, would be just as valuable in the durable power cases as in those dealing with nondurable powers.

126. *Id.* at 481.