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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FIRST APPELLATE DISTRICT

DIVISION FIVE

FILED
Court of Appeal-First App. Dist.
DEC 11 2000
RON D. BARROW, CLERK
BY ______________ DEPUTY

PAUL HOFFMAN, as Co-executor, etc., et al.,

Plaintiffs and Appellants,

v.

KATHLEEN CONNELL, as Controller, etc.,

Defendant and Respondent.

A090985

(Sonoma County Super. Ct.No. SCV217934)

In *Hoffman v. Connell* (1999) 73 Cal.App.4th 1194 (sometimes hereafter *Hoffman*), this court ruled that the executors of the estate of Constance T. Cummings did not have to pay California estate taxes of property which Cummings did not own. Following that decision, the executors filed a motion in the trial court seeking attorney fees under the private attorney general statute: Code of Civil Procedure[1] section 1021.5. The trial court declined to award any fees reasoning that the executors had not satisfied the requirements of that section. The executors now appeal claiming the trial court abused its discretion when it denied their request for fees. We agree and will reverse.

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1 Unless otherwise indicated, all further section references will be to the Code of Civil Procedure.

I. FACTUAL AND PROCEDURAL BACKGROUND

Although we have seen this case before, we must briefly recount the factual and statutory background in order to put the parties' arguments into context.

Constance T. Cummings was the income beneficiary of a testamentary trust established by her deceased husband Robert. The trust was set up as a "QTIP" trust under federal tax law. (See 26 U.S.C. § 2056(b)(7).) QTIP stands for "qualified terminable interest property." (26 U.S.C. § 2056(b)(7)(B)(i).) The term refers to property which (1) passes from the decedent, (2) in which a surviving spouse has a qualifying income for life, and (3) to which an election is made on the decedent's federal tax return. (26 U.S.C. § 2056(b)(7)(B)(i)(I) through (b)(7)(B)(i)(III).) Property that qualifies as QTIP property is excluded from the decedent's gross estate for purposes of federal estate taxes. (26 U.S.C. § 2056(a) & (b)(7)(A)(i).) However QTIP property so excluded must then be included in the surviving spouse's estate for federal tax purposes when he or she dies. (See 26 U.S.C. § 2044(a).)

As a general rule, there is no estate tax in California. This policy is set forth in Revenue and Taxation Code section 13301 which provides, "Neither the state nor any political subdivision of the state shall impose any gift, inheritance, succession, legacy, income, or estate tax . . . on the estate or inheritance of any person . . . by reason of any transfer occurring by reason of a death." This general rule is subject to an exception which is contained in Revenue and Taxation Code section 13302. It states, "Notwithstanding the provisions of Section 13301, whenever a federal estate tax is payable to the United States, there is hereby imposed a California estate tax equal to the portion, if any, of the maximum allowable amount of the credit for state death taxes, allowable under the applicable federal estate tax law, which is attributable to property located in . . . California. However, in no event shall the estate tax hereby imposed result in a total death tax liability to the State of California and the United States in excess of the death tax liability to the United States which would result if this section were not in effect."

The "federal estate tax" described in Revenue and Taxation Code section 13302 is set forth in 26 United States Code section 2001. It provides, "A tax is hereby imposed on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States." The "credit for state death taxes" described in Revenue and Taxation Code section 13302 is set forth in 26 United States Code section 2011(a) which states, "The tax imposed by section 2001 shall be credited with the amount of any estate, inheritance, legacy, or succession taxes actually paid to any State . . . in respect of any property included in the gross estate . . . ."

The interaction between Revenue and Taxation Code section 13302 and the federal tax statutes we have quoted results in what the parties describe as a "pickup" tax; i.e., California picks up and imposes an estate tax equal to the credit which the federal tax law allows. Revenue and Taxation Code section 13302 does not impose a burden in addition to that which ordinarily would be imposed by the federal estate tax. Instead, a portion of what would otherwise be paid to the federal government is paid to the state.

When Cummings died in 1995, her executors filed federal and California estate tax returns that differed in the way they treated the property that had been placed into the QTIP trust. The federal return included the value of that property. The state return did not.

The state Controller believed the executors should have paid estate taxes on the trust property and issued a $173,134.78 notice of tax deficiency. Cummings' executors disputed the deficiency and filed a complaint to have it declared invalid. The trial court rejected the executors' arguments and ruled the deficiency was proper. The executors then filed an appeal to this court.

The pivotal issue in the appeal was whether Cummings "owned" the property that had been placed into the QTIP trust. Applying well established common law principles, we ruled Cummings did not "own" the trust corpus under the applicable statutes (she was only the income beneficiary), and therefore that

her estate was not obligated to pay tax on it. Having reached that conclusion, we were not required to address the various constitutional arguments the executors had made. We then remanded the case to the trial court and ordered it to enter a judgment in favor of the executors.

This court did not publish *Hoffman* initially. However the executors asked that the case be published noting the absence of any cases discussing whether QTIP trusts are subject to California estate tax. We granted the request and ordered the opinion published.

The Controller did not offer any opinion on the publication request in this court, but she did ask the Supreme Court to depublish the opinion. The Supreme Court denied the request.

When the case returned to the trial court, the executors filed a motion for attorney fees under section 1021.5. They argued that they had satisfied each of the requirements of that section. The trial court ruled the executors had not satisfied *any* of the requirements set forth in section 1021.5 and denied the executors' request for fees. This appeal followed.

II. DISCUSSION

The executors contends the trial court erred when it denied their request for attorney fees under section 1021.5.[2]

A party may be entitled to fees under section 1021.5 if "(1) the action has resulted in the enforcement of an important right affecting the public interest, (2) a significant benefit, whether pecuniary or nonpecuniary, has been conferred on the general public or a large class of persons, and (3) the necessity and financial

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2 Section 1021.5 states, in part, "a court may award attorneys' fees to a successful party against one or more opposing parties in any action which has resulted in the enforcement of an important right affecting the public interest if: (a) a significant benefit, whether pecuniary or nonpecuniary, has been conferred on the general public or a large class of persons, (b) the necessity and financial burden of private enforcement . . . are such as to make the award appropriate, and

burden of private enforcement make the award appropriate. [Citations.]" (*Planned Parenthood v. Aakhus* (1993) 14 Cal.App.4th 162, 169-170.) All three of these requirements must be satisfied. (*Los Angeles Police Protective League v. City of Los Angeles* (1986) 188 Cal.App.3d 1, 6.)

The trial court is normally in the best position to determine whether fees under section 1021.5 are justified and the court's ruling on that issue will not be reversed "unless the appellate court is convinced that it is clearly wrong and constitutes an abuse of discretion. [Citations.]" (*Planned Parenthood v. Aakhus, supra,* 14 Cal.App.4th at p. 170.) This standard of review is modified somewhat where, as here, "litigation has resulted in a decision by an appellate court, and there is a subsequent appeal from a fee award . . . ." (*Beasley v. Wells Fargo Bank* (1991) 235 Cal.App.3d 1407, 1415.) In that instance, the appellate court is in as good a position as the trial court to assess whether the litigation involved important public interests, or a significant public benefit has been conferred. (*Los Angeles Police Protective League v. City of Los Angeles, supra,* 188 Cal.App.3d at pp. 7-9.) We will apply this slightly modified standard of review in this case.

A. Importance of the Litigation

The first issue is whether the underlying litigation "resulted in the enforcement of an important right affecting the public interest . . . ." (*Planned Parenthood v. Aakhus, supra,* 14 Cal.App.4th at pp. 169-170.) Our Supreme Court has said this factor "directs the judiciary to exercise judgment in attempting to ascertain the 'strength' or 'societal importance' of the right involved." (*Woodland Hills Residents Assn., Inc. v. City Council* (1979) 23 Cal.3d 917, 935.)

Here, several factors indicate that the right enforced in the litigation was important. First, as we explained in the prior appeal, the Controller was, in effect, trying to impose an estate tax on property that Cummings did not own. That

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(c) such fees should not in the interest of justice be paid out of the recovery, if any."

action violated the applicable statutes. Numerous cases have held that fees under section 1021.5 can be awarded in litigation to enforce statutory rights. (See e.g. *County of San Diego v. Lamb* (1998) 63 Cal.App.4th 845, 853; *Hull v. Rossi* (1993) 13 Cal.App.4th 1763, 1768.) Second, the enforcement of important constitutional rights can justify an award of fees. (*Serrano v. Priest* (1977) 20 Cal.3d 25, 46, fn. 18.) It is at least plausible to view this case as vindicating the Constitutional principle that "an unlawful levy is a species of taxation without representation." (*City of Sacramento v. Drew* (1989) 207 Cal.App.3d 1287, 1304-1305.) Third, evidence in the record indicates that experts in taxation view the prior litigation (and our resulting published opinion) as having a significant impact on estate taxation. A law professor from Atlanta said he had incorporated a discussion of *Hoffman* into his nationwide lectures on estate planning to tax attorneys. An attorney from Santa Monica said he planned to discuss *Hoffman* in a tax treatise he was preparing for a leading legal publisher. A law professor from San Francisco said he represented a client who had incorrectly paid estate tax to California under circumstances identical to those in *Hoffman*, and that he intended to file for a refund. Two attorneys who worked for the federal Internal Revenue Service (IRS) contacted counsel for appellant and told him that "as a result of the *Hoffman* decision, the IRS's California offices would no longer allow a state death tax credit to estates for taxes paid to California attributable to QTIP property, that the Federal government would now insist on collecting that portion of the tax and that notices of deficiency would be issued as necessary." One of the attorneys estimated QTIP property is involved in approximately one out of five estate tax returns filed with the federal government. Fourth, while this appeal was pending, the Legislature passed, and the Governor signed, urgency legislation that is designed to overrule *Hoffman*.[3] (See Stats. 2000, ch. 363, §§ 1-5, as adopted

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[3] The Controller has filed a motion asking this court to take judicial notice of the legislative history of the newly enacted law. The motion is granted.

9/8/2000.) A case that causes the Legislature and the Governor to respond so swiftly can reasonably be characterized as important. Finally, as another court explained, "The fact we or some other appellate court decides to publish an opinion does not conclusively establish the underlying action 'vindicated an important right.' On the other hand, it is strong evidence on that question. . . . [W]here as here the reason for publication of the opinion is to announce a rule not found in previously published opinions the decision clearly vindicates a right and one deemed important enough to warrant publication." (*Los Angeles Police Protective League v. City of Los Angeles, supra,* 188 Cal.App.3d at p. 12.)

Viewing all of these factors together, we conclude the litigation in this case "resulted in the enforcement of an important right affecting the public interest . . . ." (*Planned Parenthood v. Aakhus, supra,* 14 Cal.App.4th at pp. 169-170.)

The Controller contends the right enforced was not important because of the unique nature of the federal and state tax statutes at issue. She notes that the executors did not pay a lesser tax as a result of the litigation, they only paid the same amount of tax to a different entity, i.e., the federal government instead of the state. The trial court based its decision on this issue on similar grounds stating the case was not important because "the bottom line is that there is no deprivation of any kind suffered by the public. The deprivation is suffered by the federal government and not by the citizens of California except as [the Controller] indicate[s], to lose tax dollars."

While the facts described by the Controller and the court are correct, they are not controlling on this issue. A case can be important even if its financial impact is minimal or neutral. Indeed, many cases have held a right to be important even if it does not involve financial gain. (See, e.g., *Friends of the Trails v. Blasius* (2000) 78 Cal.App.4th 810, 833 [upholding the importance of litigation that established a public easement.] We conclude the issue in this litigation was important even though it did not result in a monetary gain to Cummings' estate.

B. Significant Benefit

The second issue is whether "a significant benefit, whether pecuniary or nonpecuniary, has been conferred on the general public or a large class of persons . . . " (*Planned Parenthood v. Aakhus, supra,* 14 Cal.App.4th at p. 170.) Again, we conclude the answer is yes.

The benefit conferred by this litigation is plain: It required the Controller to change her policies and to comply with then applicable statutes which precluded the imposition of a pickup tax on QTIP property. Since the litigation resulted in a published opinion, that change will (or at least had the potential to[4]) benefit all the citizens of this state.

The broad range of persons benefited by this case is demonstrated by the fact that our opinion in *Hoffman* caused the federal IRS to change it policies. As we have explained, the IRS no longer allows a state death tax credit to estates for taxes paid to California attributable to QTIP property. The scope of the benefit is also demonstrated by evidence submitted by the Controller, showing that her office received 8,858 estate tax returns during the 1998-1999 tax year and that approximately 15 percent of them involved QTIP trusts. Thus, for that tax year alone, the opinion in *Hoffman,* had the potential to affect 1,328 estates. This is a large and significant number. Finally, the Controller admitted that California has lost at least $1.7 million dollars because of the decision in *Hoffman.* While the precise amount of money involved is not known, it is undisputed that it is a large amount. We conclude the litigation in this case provided a significant benefit to a broad range of persons.

The Controller contends the benefit conferred by this litigation was not significant because of the nature of the tax statutes at issue. Noting that the result of *Hoffman* was to take money that would have been paid to the state and to

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[4] As we have explained, the Governor very recently signed legislation that was designed to overrule *Hoffman.* We state no opinion on the new legislation and whether it will lead to a result different from that reached in *Hoffman.*

redirect it to the federal government, the Controller contends this litigation was not significant because "benefits that would otherwise flow to California citizens, may be viewed as being redistributed to citizens of all states and to various foreign countries." The trial court based its decision on this ground, explaining that the executors did not "'[avoid] an unlawful levy'" as a result of the litigation. Once again, we reject this argument because it is premised upon the assumption that monetary benefit is required. This is simply incorrect. Section 1021.5 itself states that an award of attorney fees is warranted when "a significant benefit, *whether pecuniary or nonpecuniary*, has been conferred on the general public or a large class of persons . . . ." (Italic added.) The fact that the benefit here is nonpecuniary and may in fact result in less money flowing into the state coffers is simply irrelevant.

The Controller also suggests that the significance of this litigation is diminished by the recently enacted legislation that was intended to overrule our opinion in *Hoffman*. However, even if we were to assume that the new legislation does overrule *Hoffman* and will require that QTIP trusts in California be taxed differently, the fact remains that this litigation has *already* provided a significant benefit to a large number of persons. That benefit remains significant even if no more persons are affected. Furthermore, the fact that *Hoffman* triggered new legislation that is designed to allow California to tax assets that previously were subject to an illegal levy, could itself be viewed as a public benefit.

C. Necessity of Private Enforcement

The final issue is whether the "necessity and financial burden of private enforcement make [an award of fees] appropriate. [Citations.]" (*Planned Parenthood v. Aakhus, supra,* 14 Cal.App.4th at pp. 169-170.) This factor is satisfied "when the cost of the claimant's legal victory transcends his personal interest, that is, when the necessity for pursuing the lawsuit placed a burden on the plaintiff out of proportion to his individual stake in the matter." (*Woodland Hills Residents Assn., Inc. v. City Council, supra,* 23 Cal.3d at p. 941; internal citations

& quotation marks omitted.) When the successful party has no pecuniary interest in the outcome of the litigation, this requirement is fulfilled. (*Press v. Lucky Stores, Inc.* (1983) 34 Cal.3d 311, 321.)

Here, the executors had no financial interest in the outcome of the litigation. While the estate may have avoided paying interest on the tax deficiency that had been assessed, the estate did not "save" any taxes because of its victory. The benefit to the estate was the avoidance of an unlawful state levy. The estate paid the same total tax, but to a different entity, the federal government rather than the state. We conclude the cost of the executors' legal victory exceeded their personal interest.

The Controller contends the executors did have a financial interest in the outcome of this case because by winning, they avoided paying nearly $75,000 in interest that otherwise would have been due to California. Although the record is not clear on this point, this sum apparently represents the interest that would have accrued on the $173,134.78 notice of tax deficiency during the course of this litigation.

We reject this argument because it misconstrues the vantage point from which we must evaluate the executors' interests. As was stated by our colleagues in Division Four, "the inquiry looks forward from the outset of counsel's vital litigation decisions, rather than backward after judgment. This is because the purpose of section 1021.5 is to encourage public interest litigation by offering the 'bounty' of a court-ordered fee [citation], and the focus of that incentive is on the point in time when vital litigation decisions are being considered." (*Beasley v. Wells Fargo Bank, supra,* 235 Cal.App.3d at p. 1414.)

Here when the executors undertook this case, there would have been no interest due. The fact that interest may have accrued during the course of the litigation, and that the executors avoided paying that interest by winning, is simply irrelevant.

The Controller also suggests that the necessity requirement was not satisfied because the issues involved in the underlying litigation were not important. The trial court ruled similarly stating that "no one is denying the money had to be paid anyway. The equation doesn't add up to the kind of issue which should be considered societally important."

We reject these analyses because they focus on the wrong question. The correct inquiry is whether the financial burden to the estate outweighed its incentives in pursuing the litigation. As we have explained that requirement was satisfied here.

D. Conclusion

We conclude all the requirements for an award of attorney fees under section 1021.5 are present in this case. The trial court abused its discretion when it refused to award the executors their fees.

III. DISPOSITION

The order declining to award fees is reversed. The matter is remanded to the trial court so it can determine the amount of fees to which the executors are entitled. Appellants to recover costs on appeal.

Jones, P.J.

We concur:

Stevens, J.

Richman, J.*

*Judge of the Alameda Superior Court assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.

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