

# When High-Priced Celebrity Lawyers Are Tax Deductible

By Robert W. Wood



Celebrities often pay higher legal fees than the norm. In some cases, this is because of the type of lawyer they need, the type of legal matter they are pursuing (or defending), or both. Winona Ryder's shoplifting charge racked up far larger legal fees (not to mention public interest) than the typical shoplifting case. The fact that she paid her lawyer more than the customary fee for such a defense should make the tax impact of these fees of greater interest.

Perhaps everything about celebrities is of greater interest. Celebrity lawyers become quasi-celebrities themselves. Several television programs are devoted to celebrity legal matters, on Court TV, E!, and even more traditional networks. Several news channels have their own brand of legal tabloid broadcast. Fox News Channel's show is hosted by former prosecutor and former San Francisco first lady Kimberly Guilfoyle.

The phenomenon of high legal fees and high interest in the legal woes of celebrities is not restricted to criminal cases of the likes of Winona Ryder, Robert Blake, or telephone-brandishing supermodel Naomi Campbell. The latter represents an avid consumer of legal services, after several telephone-wielding misunderstandings, and an expensive breach of confidentiality suit against London's *Daily Mirror*. This suit was filed over photos of the model leaving a drug treatment center. When she lost, the British court system (where the loser always pays the winner's costs) required Campbell to bear the *Mirror's* legal fees of £350,000, plus her own legal fees.

Fortunately for her, the decision was overturned in 2004, awarding Campbell £3,500 in damages, and refunding her £350,000 in fees. Although Campbell's total fees are not known, the *Mirror's* total legal fees are thought to exceed £1,000,000. Models may prove profitable for lawyers. Danish supermodel May Andersen was arrested in April after allegedly hitting a flight attendant on a flight from Amsterdam to Miami.

Martha Stewart's case also deserves mention. The domestic doyenne paid legal fees all out of proportion to her crime, an obstruction of justice charge arising out of the sale of Imclone stock. News reports had her selling 75,000 shares of Martha Stewart Living Omnimedia, Inc. to pay legal fees (raising \$4.67 million).<sup>1</sup> Then SEC filings revealed that she sought reimbursement (as an officer and director) for \$3.7 million of fees.<sup>2</sup> The \$3.7 million figure applied to Stewart's successful defense on a single criminal count, the charge that she tried to lift her own company's share price in 2002 by declaring that she was innocent of insider trading. That charge was dismissed.

Then there's the granddaddy of all celebrity legal fiascos, the Michael Jackson molestation trial. Although Jackson's year-long residence in Bahrain put him less in the spotlight, his acquittal on child molestation charges came at a price. Some estimates put the King of Pop's legal expenses as high as \$20 million. Such stratospheric numbers should prompt the celebrities, their advisors, and perhaps the tabloid-devouring public to ask: When Winona Ryder, Martha Stewart, Naomi Campbell or Michael Jackson pay such whopping fees, are they deductible and if so, how?

Whether incurred in the criminal or civil context, such bloated legal fees raise significant tax issues. Deductibility is ultimately controlled by a question of nexus to the conduct of a trade or business or to income-producing activity. In the case of celebrities, where connections between income and publicity are symbiotic, it is surprising that these questions rarely get asked.

### Deductibility of Legal Fees

Given the societal omnipresence of lawyers and their fees, it may seem surprising that the Internal Revenue Code does not expressly provide for the deductibility of legal fees. Instead, legal expenses (like many other expenses of various types) are deductible as "business expenses," if

they are paid or incurred in a trade or business. Similarly, if the legal fees are paid or incurred pursuing investment activity (generally something that is intended to produce a profit, but that does not rise in activity to the level of a *bona fide* trade or business), the legal fees will be deductible as investment expenses.

Deductions for trade or business expenses are much more useful than deductions for investment expenses, because of various percentage limitations and arcane tax rules such as the alternative minimum tax. For that rea-

tion. And, in either case, they must be current expenses rather than capital expenditures.

### Problems With Personal Expenditures

All expenses that arise in connection with personal, living or family expenses are not deductible.<sup>3</sup> Deductions for professional fees have generated substantial controversy in this area of the tax law. Taxpayers often attempt to show a close nexus between legal expenses and a trade, business or investment activity. Yet, virtually any settle-

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son, much of the tax law surrounding the deductibility of legal fees concerns the line between trade or business expenses on the one hand and investment expenses on the other. Fees paid for tax advice occupy a preferred status (amen!). Fees for tax advice are *always* deductible as investment expenses, even if related to divorce or some other personal matter.

Despite this dividing line, one point is painfully clear: you get *no* deduction for legal expenses of a personal nature. Unless you can show (to the satisfaction of the IRS or a court if it comes to that) that your legal fees are connected to the operation of your trade or business, or at least to an investment or profit-making activity, you receive no tax deduction. That means the legal expenses of a divorce, of a dispute over a fistfight at the local pub, or the costs of defending a rape or paternity charge, yield no deduction because these are personal expenses. Yet, as you might suspect, what is considered “personal” and what qualifies as either an investment or business expense can be debated.

Celebrities may be in a unique position when it comes to legal fees, because few personal decisions are not in the public eye. Few are therefore devoid of economic consequences. In Michael Jackson’s case, the question of personal vs. business/investment applied to the expenses of a messy criminal sex charge may seem rhetorical. Before we turn to what is considered personal and the inevitable though often fuzzy line between personal and business, let’s focus first on some basics about what is considered a business or investment expense.

Interestingly enough, although a trade or business expense might be likened to a gold-plated deduction (whereas an investment expense is merely silver or bronze), many of the same rules apply. Legal fees in both cases must be ordinary, necessary and reasonable. Similarly, legal fees in both cases must be paid or incurred during the tax year for which you are seeking a deduc-

tion or judgment payment which arises out of a business will be treated as deductible. But, just what “arises out of a business” can be debated.

For example, legal fees incurred in connection with a divorce, separation or decree for support, by either party, are not deductible.<sup>4</sup> The origin of the claim, not its consequences, is key. In the seminal case of *United States v. Gilmore*,<sup>5</sup> legal fees and associated expenses of divorce litigation were held to be nondeductible personal expenditures even though an adverse decision would destroy the taxpayer’s business. That meant the husband was truly fighting for the life of his business in the divorce. The origin of the claim was the divorce litigation rather than its potential consequences to the business, no matter how draconian those consequences seemed to be. Thus, the legal expenses were held to be nondeductible personal expenditures.

Most tax advisors have assumed that legal fees relating to sexual harassment, gender or race discrimination, wrongful termination, and a variety of other claims made against an officer or employee of a company are deductible by the company. The conclusion may turn on whether there is an express indemnity obligation under applicable law, under any instrument of corporate governance, or under any employment contract. Virtually all harassment or discrimination cases arguably arise out of some personal activity that could, at least under one reading of the facts, be considered outside the course and scope of employment. Thus, the line between deductible and nondeductible in this context can be a thin one.

*Kelly v. Commissioner*<sup>6</sup> involved a personal (nondeductible) vs. business (deductible) distinction, where a taxpayer sought to deduct fees paid in defending a sexual assault charge. Kelly had been charged with criminal sexual assault, and he sought to deduct his legal fees as a business expense. The Tax Court found these legal costs to be nondeductible, noting that the sexual harassment

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charges arose out of Kelly's personal activities, not out of any profit-seeking activities.

The court distinguished *Clark v. Commissioner*,<sup>7</sup> another tax case involving the legal costs of a sexual assault charge. In *Clark*, the taxpayer had been wrongfully accused of assault with intent to rape during the course of his employment. The court found the expenses deductible, because Clark had been working within the course and scope of his employment, and had not committed the rape of which he was accused. The Tax Court in *Kelly* found that sexual assault activity was not within the course and scope of the defendant's employment, nor was it conducted for a legitimate business purpose. The Tax Court found that Kelly's pursuits were purely personal.

Some taxpayers find themselves claiming that expenses are necessary to protect their business reputation, and this argument is occasionally made even outside the rarefied world of show business. For example, an attorney recently argued that it was necessary to settle a dispute with clients to avoid negative publicity, and that this settlement payment therefore was a valid business expense. In *Robert E. Kovacevich et ux. v. Commissioner*,<sup>8</sup> the attorney was named in a lawsuit by a client as a result of the lawyer's representation of another client. The lawsuit alleged fraud, not malpractice. The attorney eventually settled the case and sought to deduct the payment as a business expense.

The lawyer (who also deducted the cost of his Rolls Royce) claimed that it was necessary for him to make payment on the lawsuit to avoid bad publicity. The IRS did not dispute the deductibility of the payment to settle the fraud suit. The sole question was whether the payment was deductible as a business expense or was rather an investment expense (meaning an itemized deduction). The lawyer claimed that he paid the settlement not out of a concern with his ultimate liability, but rather to protect his business and personal reputation. The lawyer had been continuously engaged in the private practice of law for a number of years. Personal client relationships a lawyer may have are arguably separate and apart from corporate goodwill.<sup>9</sup>

Although the Tax Court recognized that Kovacevich was engaged full-time in the business of practicing law, the court inquired whether this settlement was really attributable to his trade or business. The court found that it was not. Because Kovacevich was an employee of his professional corporation, the Tax Court found that he could only deduct these expenses as a miscellaneous itemized deduction.

The Tax Court was not persuaded that a desire to protect one's business reputation entitled one to a full business expense deduction, and the Ninth Circuit agreed.<sup>10</sup> Kovacevich attempted to rely upon *Marks v. Commissioner*.<sup>11</sup> The court in *Marks* found that the settle-

ment payment was made to protect the defendant's business rather than his personal reputation. The motivating concern in *Marks* was that bad publicity would have hurt the business, rather than him personally.

Cases such as *Marks* suggest that a taxpayer is entitled to consider the benefits and burdens of publicity. This may beg the question, of course, whether an entertainer might be benefited or burdened by a wave of publicity, whether that publicity is nominally bad or good.

## Crime and Punishment

Because criminal charges brought against a person generally involve personal matters, the cost of such legal representation may well be nondeductible. In some cases, the crime alleged to have been committed arises in the context of the defendant's profession or business. The cases denying deductions for legal expenses in connection with criminal representation have typically referred to the lack of a nexus between the crime which was alleged to have been committed and the defendant's business.

For example, a management consultant was not allowed to deduct legal expenses incurred in defending a charge against him for fraudulently selling securities, since he was not in the business of selling securities.<sup>12</sup> The degree of nexus required is well-illustrated by *Commissioner v. Tellier*,<sup>13</sup> in which the Supreme Court allowed a deduction for an unsuccessful criminal defense. The case involved a securities dealer convicted of violating the 1933 Securities Act and mail fraud statutes in conducting his business. The *Tellier* decision overturned several lower court cases, and made irrelevant the success or failure of the defense of the criminal charges.<sup>14</sup>

If the nexus between the trade or business and the alleged crime is not strong, the deduction will be denied. For example, the mere fact that a defendant's business will be destroyed if he is convicted of a crime is not a strong enough nexus to sustain deductibility for the attendant legal costs.<sup>15</sup> Indeed, even though a conviction may disqualify a defendant from engaging in a business or profession, if the claim does not arise out of the business or profession to begin with, the legal fees will not be deductible.<sup>16</sup>

## As Investment Expenses

Some taxpayers have argued that legal fees incurred in defending against a criminal prosecution should be deductible as expenses incurred in connection with investment activities, even though they may not rise to the level of an active conduct of a trade or business. In *Accardo v. Commissioner*,<sup>17</sup> Anthony Accardo was prosecuted under the RICO Act for charges involving racketeering in labor unions, including accepting kickbacks and commissions involving employee welfare benefit plans. Accardo was acquitted, and deducted the legal fees he incurred in his defense. He argued that the legal fees

were deductible, since the indictment sought a forfeiture judgment and Accardo sought to conserve and maintain income-producing assets.

The Tax Court nevertheless held that Accardo's legal fees were not deductible, finding his situation no different from that of any other defendant in a criminal or civil trial. Under the origin of the claim test, the claim against Accardo arose in connection with his income-producing assets. A desire to preserve income-producing assets was not sufficient to sustain a deduction for the legal fees Accardo paid in his defense. Legal fees paid with respect to a purely personal matter are not deductible, even if the legal fees have an effect on capital preservation. The applicable Treasury Regulations state that

[a]n expense (not otherwise deductible) paid or incurred by an individual in determining or contesting a liability asserted against him does not become deductible by reason of the fact that property held by him for the production of income may be required to be used or sold for the purpose of satisfying such liability.<sup>18</sup>

### Legal Fees in Disciplinary or Malpractice Proceedings

The cost of disciplinary or licensing proceedings against a person in connection with his business or profession may be deductible. The question is whether the conduct stems from the taxpayer's business rather than from his personal activities. The nature of the suit or legal proceeding against the person is controlling: *i.e.*, whether it stems from professional or business actions, or personal actions.

Thus, a deduction for legal fees incurred by a lawyer in defending a legal malpractice case would be allowed. However, legal fees paid by a doctor in defending a bribery conviction which ultimately resulted in a loss of a medical license would not be. Despite its professional consequences, the doctor's conduct would not lead to a deduction, because the bribery was a personal offense.<sup>19</sup> On the other hand, if the doctor had bribed a medical device supplier, that should lead to a different result.

Sometimes, it is difficult to determine whether a deduction for legal fees is appropriate based on the business nature of the suit, or whether the genesis of the suit really is personal. For example, in *McDonald v. Commissioner*,<sup>20</sup> a lawyer was denied a deduction for amounts paid to settle a threatened lawsuit to contest a will that made several bequests to the lawyer. The court reasoned that, although the suit might threaten the lawyer's profession, the origin of the claim was personal. Similarly, in *Solomon v. Commissioner*,<sup>21</sup> an accountant was denied a deduction for expenses resulting from the settlement of a lawsuit against him for misappropriation of his father's funds. The court determined that the matter was personal in nature rather than related to the accountant's trade or business.

Sometimes the IRS will seek to dissect a transaction into minute pieces in order to deny deductions

where it would seem that purely personal activities are being pursued. In *Peters, Gamm, West & Vincent, Inc. v. Commissioner*,<sup>22</sup> the Tax Court considered charges brought by the SEC against Peters, a partner in an investment firm. Although the firm was not named in the case, charges against Peters were pursued and ultimately resulted in significant legal fees. The firm paid the legal fees, and the question was whether they were deductible.

Ultimately, the Tax Court agreed with the IRS that deductions by the corporation should be disallowed, and that the payment should be considered constructively paid by the investment firm to Peters and, in turn, paid by Peters to the lawyers. That meant that Peters, not his firm, could deduct the fees. Unfortunately, the legal fees were deductible by Peters only as investment expenses under § 212 rather than as trade or business expenses under § 162. That produced an alternative minimum tax problem.

Even judges can have legal expenses. In Revenue Ruling 74-394,<sup>23</sup> a judge was allowed to deduct defense costs against charges of misconduct in office. Politicians can incur legal expenses too. In Revenue Ruling 71-470,<sup>24</sup> a public official was allowed to deduct defense costs against a voter recall. Nevertheless, the Service has successfully litigated a number of cases where legal expenses have been disallowed.

### Ordinary and Necessary Expenses?

The requirement that legal fee expenses be ordinary, necessary and reasonable in order to be deductible, applies under both § 162 (trade or business expenses) and § 212 (investment expenses). The "ordinary and necessary" requirement has generated substantial confusion. Generally speaking, an expense is "ordinary" if a businessperson would commonly incur it in the particular circumstances involved.<sup>25</sup> Taxpayers frequently confuse the "ordinary" requirement with the notion that the particular expenses must arise over and over again, and hence would be ordinary in the common usage of that word as a synonym for "recurrent."

The courts have not been restrictive in their interpretation of the ordinary and necessary requirement. In fact, the Supreme Court has noted that an ordinary expense may be extremely *irregular* in occurrence. A lawsuit affecting the safety of a business may happen once in a lifetime. Yet, even if legal fees are high, the expenses are ordinary, because we know from experience that payments for such a purpose are the common and accepted means of defense against attack.<sup>26</sup>

Just as the "ordinary" requirement has been liberally interpreted, the "necessary" requirement has been given wide berth. It is not necessary to inquire whether the taxpayer really *had* to incur a particular expense, such as taking a client to lunch, if incurring such an expense was appropriate or helpful.<sup>27</sup> Moreover, with attorney fees,

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there may be even greater latitude in determining when something is “necessary.” Some courts have looked not to whether the employment of an attorney is appropriate or helpful, but to an even more watered-down standard.

Thus, in one case, legal fees were ordinary and necessary where engaging attorneys was an act a reasonably prudent man in the same circumstances might undertake.<sup>28</sup> Indeed, where legal fees are incurred to either bring or defend a lawsuit, it is hard to imagine the ordinary and necessary nature of the expense being questioned. The critical question is the *nature* of the lawsuit. The origin of the claims test applies with respect to legal fees, as it does with respect to the characterization of the underlying recovery.

### Reasonableness

The ordinary and necessary nature of legal expenses in this context is rarely questioned as long as the requisite nexus can be established between the lawsuit and the business or investment activity of the plaintiff or defendant. Nevertheless, there is still the question of the overall reasonableness standard. Most lawyers’ fees may not seem reasonable. Yet, generally, the reasonableness of a payment of legal fees will not be questioned. Since litigation is by its very nature adversarial, the reasonableness of a payment of legal fees to dispose of litigation or discharge a settlement or judgment is rarely questioned.

However, the issue has been considered in a few cases, and a portion of the claimed legal fee expenses were disallowed.<sup>29</sup> Contingent fee arrangements may result in quite large legal fee payments. Even so, the sheer size of the legal fees will not necessarily make the fees unreasonable. As long as the fee arrangement was the subject of an arm’s-length contract between the parties, the reasonableness of the resulting contingent fees should not be in dispute.<sup>30</sup>

### Celebrity Cases

For the typical celebrity criminal defendant – say Hugh Grant’s solicitation of prostitution charges, Robert Blake’s murder charge, or Winona Ryder’s shoplifting charge, the nexus between the conduct and the legal expense is likely to be purely personal, whatever the effects on the celebrity’s career.

Yet, in the case of Naomi Campbell’s breach of contract case, more analysis is needed. An invasion of privacy claim may be axiomatically personal. But, a defamation case may involve either personal or business reputation, and so may give rise to tax-deductible lawyers’ fees. Naomi Campbell’s legal fees arguably arose out of her contract with the *Daily Mirror*. While that deal may have involved solely what she perceived to be her privacy, the privacy of a public figure, this wasn’t an invasion of privacy suit but rather one for breach of contract. Establishing a business nexus with a breach of contract suit would be far easier than with an invasion of privacy suit.

Although it is awfully difficult to see legal fees relating to child molestation charges as business (or even investment) expenses, Michael Jackson may have at least some arguments to lessen the sting of \$20 million in legal bills. First, he was acquitted. Under *Commissioner v. Tellier*,<sup>31</sup> conviction versus acquittal is plainly not the linchpin of a deduction. Even so, it’s almost always easier to claim (and defend) a deduction after an acquittal.

Second, Jackson’s legal battle arguably arose (at least in part) out of his own foray into media spin and self-promotion. Jackson’s problems may not have *started* with the media, but they certainly got worse because of it. The now-infamous broadcast “Living with Michael Jackson” first aired in February 2003. This less-than-flattering documentary from British journalist Martin Bashir focused tremendous attention on Jackson’s proclivities, particularly his penchant for sleeping with young boys.

Because Jackson and his handlers surely thought that granting Bashir access was a smart public relations move, I’m guessing that Jackson incurred costs in allowing such access, which he treated as deductible advertising or public relations expenses. If I’m right about this, then there is a kind of chicken-and-egg phenomenon here. Arguably, the dominoes started to fall with the February broadcast of the Bashir documentary. Neverland Ranch was searched in November, Jackson was booked and charged (in December 2003), and the rest is history.

Once Jackson went public with his TV special and appeal, there is little doubt that his legal woes got worse. After the documentary, most observers say his profile with prosecutors went way up. If the prosecutors were smoldering charcoal briquettes, his media activities amounted to a liberal dose of lighter fluid. I’m not sure one can argue that the molestation charges and ensuing trial *arose* out of his business, and out of his media (mis)handling, but I’m also not sure one cannot.

Indeed, there is some evidence it was the media, and Michael’s (mis)management of it that set off the maelstrom. The primary prosecutor, Tom Sneddon, admitted that he pursued the case primarily because of his view that Jackson revealed so much in his TV saturation. At a minimum, perhaps one could bifurcate Jackson’s fees and expenses between those related to or arising out of the media blitz, and those caused by the underlying charge. Arriving at principled percentages may be difficult, but recognizing the dual nature of the expense and trying to apportion it makes perfect sense.

Quite apart from all this, there is the whole charitable activity and Neverland Ranch symbiosis. I see these as distinct, so let’s take the charitable issue first. Michael Jackson routinely gives money, time and energy to charitable causes, particularly those involving children. A cynic might say that he does this only to get close to the kids for his own ulterior motives.

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But, consider the possibility that the criminal charges arose solely (or primarily) because of his altruistic behavior. If it did, maybe the fees (or at least some portion of them) are deductible as out-of-pocket expenses incurred in connection with his charitable works. Although one gets no charitable contribution deduction for the value of one's services, out-of-pocket expenses should be deductible.

Bear in mind too that we are not talking about standards beyond a reasonable doubt. We're not talking about guilt or innocence here. His innocence was already established. We're only talking about tax arguments, and I think they can be made with a straight (non-surgically altered) face.

Then, take Neverland Ranch. It is a veritable amusement park and zoo rolled into one, not to mention a very valuable piece of property. With most, if not all, of the molestation alleged to have occurred on the ranch itself, and with its operation being so central to Jackson's persona and career, is the ranch *itself* a business? Is it an investment?

You see where I'm going here. I don't know if Mr. Jackson claims any tax deduction for the operation of the ranch apart from the inevitable property tax, but I'll bet he does. There is surely extensive security, and there are probably other expenses that are solely attributable to his career. Then, there are the costs of his charitable functions, the caterers, the clowns, the animal trainers, and so on. I have no idea how Jackson's tax lawyers and accountants treat the millions all this has to cost. I don't even know which entity or entities this is all run through.

I'm guessing, though, that as many zeros as are involved, someone *has* looked at these issues. I'm also guessing that Neverland Ranch and all its operations are not entirely funded with after-tax dollars. You may say that all of this has nothing whatsoever to do with the deductibility of legal fees incurred in Jackson's successful defense of his molestation charges. With the arguably close connection between the charges and the Ranch's operation (charitable, investment, hobby?), though, I'm not so sure.

### Trade or Business Nexus

To address the deductibility of legal fees in a case such as Jackson's, the key question is whether the origin of the case against him is personal or arises out of trade or business or investment activity. "Origin" sounds primal, and this sounds like a point easily resolved. After all, *United States v. Gilmore*<sup>32</sup> holds that if a case and corollary legal expenses have their origin in personal activity (a divorce, child molestation charges, etc.), the mere fact that grave business or investment consequences may flow from that case (as surely would have from Jackson's conviction) does not convert the origin of the claim from personal to business or investment.

In *Gilmore*, the subject of the litigation was a high-profile (and expensive) divorce that threatened to close the husband's car dealerships. The Detroit automakers had told Mr. Gilmore that if his wife got control of any of the dealerships they would not sell to her and would cancel Gilmore's dealer agreements. Notwithstanding the substantial business motives that the car dealer had to fight over his business assets, Gilmore's divorce expenses were held nondeductible by the U.S. Supreme Court.

Against this tough standard, Mr. Jackson's legal expenses seem plainly personal. It is hard to argue that the criminal charges against him can in any respect be viewed as connected to his business. Yet, as I've attempted to show, he may have colorable arguments for a potential bid to have the government share in his legal costs.

### Thriller?

Between the poles of authorities like *Gilmore* (personal) and *Tellier* (upholding business nexus), how do celebrity legal fees stack up? Like non-celebrities, the answer will depend on the facts. As with non-celebrities, the origin of the claim, not the effects it may have on the celebrity's business or investments, should control. In many cases, such as Hugh Grant's solicitation charge, Robert Downey Jr.'s drug charges or Robert Blake's murder trial, there is no argument that any portion of the legal fees is related to business or investment.

In some cases, though, I believe the standard for the deductibility of legal expenses may be somewhat lessened for celebrities. Put differently, I believe it may be easier for at least some celebrities to make connections between the genesis of legal expenses (rather than their mere effects) and their business or investment activities. Martha Stewart's considerable legal expenses arose out of her Imclone stock trading, surely an investment activity.

However, a portion of her legal expenses related not merely to investments, but rather to her trade or business. Managing the Imclone affair doubtless involved advertising and image consultants, as well as legal expenses legitimately related to Martha Stewart's omnipresent business. In any case, she won reimbursement for \$3.7 million in fees attributable to a business claim that she had attempted to lift the company's share price by proclaiming her innocence to the insider trading charge. This simple example should show that a huge part of the issue here can be allocations of legal bills. Much like the post-*INDOPCO*<sup>33</sup> bifurcation of legal bills between deductible and capitalized acquisition costs, celebrity legal bills may withstand a good deal of this.

Naomi Campbell's legal expenses related to her phone-bashing are plainly personal, whatever the effects. But, her expenses related to her *Daily Mirror* suit seem to relate to her contract with the tabloid. Despite the invasion of privacy tenor of the dispute and its focus on photos of the model exiting drug rehab, that contract arguably arose

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entirely out of her trade or business. Michael Jackson's legal fees may be a stretch, so much so that I expect some readers will think I've lost my marbles by mentioning some of the arguments I've suggested here. The truth is, I don't know enough about the allegations, about Jackson's business and investment entities, or even about his charitable work, to carry these arguments very far.

Yet, I suspect that at least some of his legal fees may arguably be deductible on some theory. That may make Jackson similar to dethroned investment banking star Frank Quattrone, to jailed and released (and now even more beloved) Martha Stewart, and to a host of other celebrity and non-celebrity users of legal services. Celebrity clients can be a boon to lawyers, but when you take the celebrity's tax posturing into account, sometimes taxpayers are footing at least part of the bill. ■

1. See *Martha Stewart Sells Shares for Legal Fees*, N.Y. Times, June 12, 2004.
2. See *Martha Stewart Starts Appeal*, CNNMoney.com, Mar. 17, 2005.
3. I.R.C. § 262.
4. Treas. Reg. § 1.262-1(b)(7).
5. 372 U.S. 39 (1963), *on remand*, 245 F. Supp. 383 (N.D. Cal. 1965).
6. T.C. Memo. 1999-69.
7. 30 T.C. 1330 (1958).
8. T.C. Memo 2003-161, *aff'd*, 177 F. App'x 561 (9th Cir. 2006).
9. See *Martin Ice Cream v. Comm'r*, 110 T.C. 189 (1998).
10. T.C. Memo. 2003-161.
11. 27 T.C. 464 (1956).
12. See *Price v. Comm'r*, T.C. Memo. 1973-65 (1973).
13. 383 U.S. 687 (1966).
14. See Rev. Rul. 66-330, 1966-2 C.B. 44 (1966) (indicating that whether the defense of a criminal action is successful or unsuccessful is irrelevant).
15. See *Hylton v. Comm'r*, T.C. Memo. 1973-262.
16. See *Patch v. Comm'r*, T.C. Memo. 1980-11.
17. 94 T.C. 96 (1990), *aff'd*, 942 F.2d 444 (7th Cir. 1991), *cert. denied*, 503 U.S. 907 (1992).
18. Treas. Reg. § 1.212-1(m).
19. See *Margoles v. Comm'r*, 27 T.C.M. (CCH) 319 (1968). For similar cases, see *Tinkoff v. Comm'r*, 120 F.2d 564 (7th Cir.), *cert. denied*, 314 U.S. 581 (1941); *Joseph v. Comm'r*, 26 T.C. 562 (1956).
20. 592 F.2d 635 (2d Cir. 1978).
21. T.C. Memo. 1974-127.
22. T.C. Memo. 1996-186.
23. 1974-2 C.B. 40.
24. 1971-2 C.B. 121.
25. See *Comm'r v. Chicago Dock & Canal Co.*, 84 F.2d 288 (7th Cir. 1936); see also *Comm'r v. Heining*, 320 U.S. 467 (1943).
26. *Welch v. Helvering*, 290 U.S. 111 (1933).
27. See *Lilly v. Comm'r*, 343 U.S. 90 (1952).
28. *Kanelos v. Comm'r*, 2 T.C.M. (CCH) 806 (1943).
29. See *Harvey v. Comm'r*, 171 F.2d 952 (9th Cir. 1949); *Michaels v. Comm'r*, 12 T.C. 17 (1949), *acq.*, 1949-1 C.B. 3.
30. See Treas. Reg. § 1.162-7(b)(2).
31. 383 U.S. 687 (1966).
32. 372 U.S. 39 (1963), *on remand*, 245 F. Supp. 383 (N.D. Cal. 1965).
33. *INDOPCO v. Comm'r*, 503 U.S. 79 (1992).