

THE COMPARATIVE ANALYSIS ON PROBLEM OF MARKETING ACTIONS CLASSIFICATION FOR THE PURPOSE OF TAX LAW IN THE PERSPECTIVE OF EUROPEAN AND POLISH LEGAL SYSTEMS. THE CONTEXT OF SUBSTANTIAL LAW AND LEGAL THEORY.

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Abstract: The primary point of article is to outline some common principles for the European Union Member States in the classification process of the marketing actions as legally eligible incurred income cost and in effect the tax deductible revenue. The paper is written for the purpose of presenting specific aspects of legal theory and the legal text interpretation as useful and effective tools in the process of solving earlier mentioned tax law problems. The article is mostly based on comparative analysis of the European Union Countries tax law as well as provides the classic examples of the classification conflict between representation and advertisement. In addition authors of the article intend to present the entire issue on the example of Polish law regulations. The work mainly emphasizes on issues related to the law interpretation and the language logic in the context of analyzing the legal regulations of European tax systems, which could successfully facilitate the process of understanding European Union Countries key legal institutions in the subject matter.

Keywords: taxes, marketing actions, tax deductible revenue, incurred income cost, legal theory, interpretation of law, European tax law, Polish tax law

1. The introduction

The instant progress of political and economic integration between European Union Member States causes that the increasing number of entrepreneurs decides to begin conducting business activity in other Member State than their home country¹. In addition, it cannot be forgotten that the basic aim in expanding business activity to the territories of other member countries is to maximize expected incomes. To achieve this purpose the entrepreneur cannot limit himself only to **increase revenue, but also he should realize that it is necessary to minimize the costs associated with conducted activity at every available field**². One of the most important tools, which helps in increasing the income are marketing actions that may be undertaken in various forms. It should be noted that this kind of actions, when performed usually requires the appropriate financial resources. Rational entrepreneur cannot remain indifferent to current legal regulations in the countries, where his or her business activity is conducted. It concerns above all the tax regulations, which creates principles of ranking expenses among obtained tax deductible revenue. At this point it is necessary to mention that international and European Union legislative activity in a notable degree caused standardization of the legal-tax order in European Union Member States. During the process of comparative law analyze, it is possible to derive certain common regularities at general level which could facilitate understanding of the principal system solutions, which are present in every modern country. Naturally it should be mentioned that considering such extensive territories even under the hard top-down imposed conditions of implementing consolidated regulatory standards, the local differences in applying and understanding law will always occur and it is necessary to contemplate such differences individually.

2. The definition of tax deductible revenue in perspective of Corporate Income Tax

Tax deductible revenues are the second, after revenue, element affecting the income as economic subject of taxation under the income tax. In the tax law, the concept of obtained income costs functions exclusively in income taxes. In European tax systems it will be British: Personal Income Tax, in German: Einkommensteuer, French: Impôt sur le Revenu des Personnes Physiques, in Poland, paid based on the personal income tax act³

(hereinafter referred as the Personal Income Tax Act) and British: Corporate Income Tax, in German: Körperschaftsteuer, French: Impôt sur les Sociétés, in Poland, paid based on the Income Tax Act⁴ from legal persons (hereinafter referred as the Corporate Income Tax Act). In most countries, the costs are defined in similar way as in the Polish law⁵. Legal construction of tax deductible revenue is currently one of the most complex regulation types in the field of corporate income tax. The legislative powers of different states usually do not specify all types of tax deductible revenue, which can be deducted from the income during the process of calculating the taxable base. In principle the legislator provides only a general definition supplemented by negative criteria.

If one should better understand the subject matter ought to consider much closer the concept of "costs". From an economic point of view, the cost is a usage of the production factors (raw materials, materials, machines, tools, etc.) and human work in certain closely determined period in the enterprise (company, unit). This usage is expressed in the financial measure⁶. Based on the Polish law, in practice the tax deductible revenue can be both costs of the raw materials consumption, transport costs, expenses on repairs, gas, electricity, rent (lease), expenses related with the office, advertisement and payments of different kinds (e.g. postal, bank), etc. In summary, all expenditure incurred in order to obtain profits will be the tax deductible revenue.

3. The eligibility criteria in the classification process of incurred costs as the legal tax deductible revenue

At ranking economical efforts, which were incurred in order to obtain profits, as eligible expenditures that the legislator legally recognized and allows to write off in the given tax year as obtained income costs, there is no consolidated position in tax systems of the European Union Member States. Generally European countries define in similar way the tax deductible revenue. In this field a matter, which is the most variable in the European tax orders is the definition of expenses catalogue, which are legally valid to classify as possible to deduct from the revenue. The main cause of earlier mentioned differences is frequent usage of this legal construction by member states to conduct own socioeconomic policy. In the context of legislative technique, Member States applying the general clause, which specifies what kind of expenditure are suitable to deduct, supplemented by positive enumeration of exact cases, when these given costs classes even if incurred directly in connection with the revenue will not be classified, as the expense eligible to deduction. Additionally, towards every state individually, one should consider the factor of tax law appliance practice (by the administrative authorities and national courts), especially in the form of rich judicial decisions subjecting the earlier mentioned general clause to interpretation. It is also possible that in certain member states, for example in France⁷, these authoritative interpretations of the administrative authorities in the tax issues will decide almost entirely, what cost is suitable for a deduction and which is not.

Fundamentally, in every European taxation order the general rule, which has a key role in the classification of economic cost as tax deductible revenue, is a test of causal nexus between the

¹ See: Hall. S. Scott, *International Finance*, New York 2004 y., p. 148

² See: Stephen A. Lind, Stephen Schwarz, Daniel J. Lathrope, Joshua D. Rosenberg, *Fundamentals Of Business Enterprise Taxation*, New York 2002 p. 685 and next.

³ A bill on Personal Income Tax from 26.07.1991. Dz.U. of 1991 Nr 80, pos. 350, with changes.

⁴ A bill on Corporate Income Tax from 15.02.1992. Dz.U. of 1992 Nr 21, pos. 86, with changes.

⁵ See: M. Pawlik, *Nowe pojęcie kosztów uzyskania przychodów*, [in:] Monitor Podatkowy 2/2007, p. 13.

⁶ See: Jacek Kulicki, *Podatek dochodowy od osób fizycznych 2002 Tom II*, Warsaw 2002 y., p. 106.

⁷ See: K. Purski [in:] ed. B. Brzeziński, J.P. Tarno, *Sądowa kontrola decyzji podatkowych w Republice Francuskiej – podstawowe zasady*, Wolters Kluwer business, Warsaw 2011 p. 336 and next.

income and costs incurred for the purposes of paid activity. The income is reduced exclusively by objectively incurred costs (associated with paid activity). Summing up, to legally classify the given cost to the tax deductible revenue group, the costs must be incurred in order to obtain the income. This is a positive criterion. Another factor will be fulfillment of the negative criterion, i.e. the cost which meets a positive criterion, cannot be qualified to the legally not-recognizable group of the economic cost by the legislator for obtained revenue. Therefore, concluded that not all incurred expenses in order to obtain the income or keep the income are eligible to be classified as tax deductible revenue. Polish legislation in this exact field does not deviate from the European standard. Polish regulation of the income taxes, implement the restricted list of expenses, which despite the fact that are incurred in order to obtain the income or to keep or protect the income source, cannot be tax deductible revenue, for instance entertainment expenses or on individual needs of the taxpayer. Detailed list of such expenses presents the Article 16 of the Corporate Income Tax and Article 23 of the Personal Income Tax.

4. The costs in legal and economic sense in Polish tax law

Real costs in the economic meaning are one of the elements that shape the legal taxation subject for the purpose of income tax. From this point of view a principle of statutory appointing legal rules, which concerns the costs, guaranteed by the Article 217 of the Polish Constitutions is so essential. It simply does not give to the legislator possibility to delegate the prerogatives in this matter to the executive authority. It is so crucial because without this principle executive power could easily diminish the economic liberties of the individuals. It should be also noticed that the amendments conducted in the legislation in this sphere have vital importance for taxpayers because they creates area of freedom in disposing financial resources as well as have a direct impact on the tax amount⁸.

It is necessary to note that statutory definition of the costs differs in a considerable degree from the economic and accounting recognition⁹. Act from 29 September 1994 y. about accounting enables taxpayers, for accounting purposes, to establish the depreciation deduction (amortization) based on sole economic criteria. The period of amortizing fixed assets in this case depends exclusively on economical consumption of this asset. Such kind of write off undoubtedly will be, recognized from the economic and accounting point of view, as the cost associated with conducted activity. In accordance with tax law, to tax deductible revenues shall be ranked only the write off, which will not exceed the amount defined in particular statutes¹⁰. This is not only one, exclusive tax restriction, for instance among many other restrictions could be listed: leasing rent, business trips, loss in debts, fixed and rotational assets, penalties and sanctions, social insurance contributions. These expenses from the economic or accounting point of view are classified as the costs or extraordinary losses. In addition it is not possible to rank them, entirely or even in a small part, to the group of tax deductible revenue. These differences between the "cost" in economic or accounting categories and the "cost" in the context of tax law are significant in determining the factual profit and taxable base, so-called the revenue in field of tax law.

5. The marketing actions

Not only will the technical classification of particular action to specific legal category have an impact on the costs categorization. But also very important are the factors associated with sole interpretation of terminology, as well as studying the logic or semantic of the characteristic features of concrete names and assigning them a relevant designates. Therefore the indispensable condition of the correct interpretation of tax law

standards is to conduct this process not only based on substantive law and general principles, but also in accordance with strict procedural standards intended for applying the substantive law. In addition, it is necessary to be aware of characteristic features of specific factual situation, which is the subject of interpretation. Generally, all mentioned factors affects possibility to deduct the given costs.

Taking into account previous reasoning, it is possible to start to consider specific issues connected to the marketing actions on the example of advertising and representation. The Christmas season provides excellent examples for this process. Important matter from a practical point of view for companies could be the classification of gifts as tax deductible revenue. Such action may in the significant degree reduce the amount of income tax. On the basis of this example appears a relevant problem for the discussed subject matter. It is simply the difficulty of a finding what kind of actions are advertising and what representation. According to the Article 23 paragraph 1 pt. 23 act of the Personal Income Tax (appropriately Article 16 paragraph 1 pt. 28 act of the Corporate Income Tax), in Polish law the entertainment expenses, in particular for catering services, purchase of food and drinks, including alcohol beverages are not regarded as tax expenditures. Regarding the gift as a representation, even if there will be fulfilled positive criterion (one of two necessary premises which must be fulfilled altogether), the costs will be incurred in order to obtain the income, possibility to deduct will be excluded, because a negative premise will not be fulfilled (the representation is statutory excluded from the group of tax deductible revenue). However, it is possible to deduct the incurred expenditure for activities related with the advertisement.

Unfortunately, in the Polish law, both advertisement and representation are not legally defined in the tax acts. The part of Polish tax law doctrine submits that such definitions should be reconstructed on the basis of different than tax law regulations, which are created to regulate concrete activities like trade of individual things, for instance advertisement of tobacco products¹¹. However, the conception of giving specific meaning for terminology, which will be used for purpose of tax law from non-tax regulations, due to tax law special character and its functions as well as constitutional principles of trust to the state and laws or special strict procedures of restricting laws and imposing obligations do not seem to be right¹².

In the opposition to the above, the process of giving meaning to the tax law terminology should be conducted in regard to basic principle of the legal text linguistic interpretation, which constitutes that if in the act, clearly to words was not given a special meaning (e.g. through legal definitions or professional vocabulary) the interpreter must assume that the words has the meaning adequate to colloquial language¹³. Considering practically the term of advertisement, it will be necessary to start with dictionary meaning, where: advertisement [Latin] is, persuasive type of communication, which includes techniques and actions taken in order to draw attention on the product, service or idea; the primary advertisement functions was to provide information about goods and its purchase sources; at present the advertisement fulfills functions of: presentation, shaping the demand, creating and keeping markets; advertisement uses visual sources (publishing companies, newspaper announcements, posters, films, television, neon lights as well as packages, exhibitions, etc.) and audio acoustic (radio, street gigantophones, telephone information service, etc.¹⁴). Summing up, the aim of advertisement is to inform and encourage to use or to acquire the specific goods as well as

¹¹ See: R. Krasnodębski, *Wydatki marketingowe w świetle ustaw o podatkach dochodowych*, [in:] *Monitor Podatkowy* 11/2004, p. 20.

¹² See: B. Brzeziński [in:] ed. W. Nykiel, N. Sek, *Protection of Taxpayer's rights – European, International and Domestic Tax Law Perspective*, Wolters Kluwer business, Warsaw 2009 p. 21-31.

¹³ See: A. Bielska-Brodziak, *Interpretacja tekstu prawnego na podstawie orzecznictwa podatkowego*, Wolters Kluwer business, Warsaw 2009 p.25,60.

¹⁴ See: word: reklama, <http://encyklopedia.pwn.pl/haslo.php?id=3966917>, 29.11.2010 y.

⁸ See: J. Małecki, [in:] A. Gomulowicz, J. Małecki, *Podatki i prawo podatkowe*, Warsaw 2010, p. 652.

⁹ See: M. Śliwarczyk, [in:] G. Dźwigala, Z. Huszcz, P. Karwat, R. Krasnodębski, M. Śliwarczyk, F. Świątała, *Ustawa o podatku dochodowym od osób prawnych. Komentarz*, Warsaw 2009, p. 272.

¹⁰ See: Jacek Kulicki, *ibidem.*, p. 105.

services. Advertisement takes different forms – starting from reliable information about product features, met mainly in the specialist press, ending at praising the product without reliable technical information about the good, what is often assigned to TV advertising. The Polish Ministry of Finance emphasized that action of advertisement certainly includes activities which are aimed to provide the knowledge about benefits and values of the company, carried out by spreading its logo¹⁵. At this point it is useful to present official opinion of the Tax Chamber Director in Warsaw, where the authority states that: Company which gives advertising gifts to the customers, can such expenses classify as tax deductible revenues. However, the entrepreneur must establish the causal nexus between incurred expense and obtained income from this specific activity. Additionally, one must remember that an advertisement is action of the business entity, which shapes the demand to given goods, services or brand, by encouraging as many potential customers as it is possible to purchase goods or services¹⁶. In conclusion it should be noted that an advertisement is the presentation of product in such a manner that it will be attractive for the future customers and has a potential to create the relation between it and the demand for product (the one that will be sold).

At this stage the term of representation should be closer analyzed and during this process emerges the picture of company activity which is aimed on gaining prestige and building positive company image. The Polish Ministry of Finance in the letter from 17th July 1995 y. stated that the term of representation means the grandeur, refinement in someone's lifestyle, associated with the position or social rank¹⁷. Other opinion states the Supreme Administrative Court (further referred as the NSA) in judgment from 6th May 1998 y. it is stated that: “used term - “the representation” (under the Article 2 paragraph 3 pt. 1 from the statute of Value Added Tax (VAT)) not only has to refer to “grandeurs, refinement”, but also refers to “good representing of the company” which includes: appropriate employees clothing, company decor, its logo, billboards, way of entertaining enquirers and contracting parties¹⁸. In turn, Provincial Administrative Court (further referred as the WSA) in Warsaw in judgment from 21st January 2009 y. emphasized that the term of representation also means taking various actions, which aim to facilitate and support establishing trade relations, also by building personal reports, where one of the main goals is to create entrepreneur image, as the affluent, trustworthy business partner¹⁹. Prima facie determining what the advertisement is and what is the representation may seem bright and clear, however it is deceptive conclusion. It might seem that these terms are stiff and there is no similarity between them. But looking at their designates and taking into account the multiplicity of different evaluation criteria of these terms, especially in relation to remaining non-linguistic factors, classifying concrete designate to appropriate term does not seem so obvious. To correctly conduct classification process of factual situation to corresponding legal term helpful will be to do abstract analyze of tax law acts and the purposes, that lies beneath the regulation in the context of the situation, which is the subject to this task. In the same moment the factual features of the given activity as well as the factual purpose and main effect of the activity caused in the real world should be considered in the same manner as previously (primarily what is relevant from the point of the tax law). Such specific proceedings could be called as rules of reason that in dubious situations may turn out to be helpful for the purpose of correct classification earlier mentioned terms. From the practical point of view, in unclear situation when ordinary principles of interpretation fails, firstly the purpose of the given legal-tax regulation should be recognized, (what the legislator wanted to achieve, the activity which he wanted to tax), secondly very important is to accurately recognize these circumstances in the context of factual event, including the

motives of the taxpayer activities and what significant features his action had, what effect it caused, what was his aim and whether if all this data is relevant from a legal-tax point of view.

Using the above analyses of advertisement and representation terms it is necessary to notice that advertisement as marketing action is used to raise the sales of given goods, so the specific goods are the main matter of advertisement, therefore giving earlier recalled gifts with company logos, as a small sample in order to enable for potential customers option to try out the goods, which in the effect creates the demand for this good, certainly can be categorized as advertisement. While, the representation regards the enterprise as certain functional integrity, thus the entire enterprise is represented and in opposition to that - not the individual product. This kind of action creates the image, renown, recognition, etc. of the enterprise. Analogically, the same action of giving gifts with company logo in the enterprise building, even if that gifts are the products of the company, but it is not aimed mainly on creating demand for this good quite and what more is generally aimed to create corporate image, certainly we will categorized as representation. From other hand, if goods are effectively advertised and indeed meet the customer requirements, also in some way are creating a positive corporate image, (as the producer of the good). But whether these actions consist on representation? It seems that the answer to such question must be negative, because described earlier results (and previously objectives – in the form of building corporate image) are carried out by the way, while the main purpose remains of course completely different.

6. The example of conflict on the interpretation field between advertisement and representation

At the beginning of this reasoning we should consider the categorization of occasional company decor e.g. Easter decorations or Santa Claus handing small gifts in the Christmas period. Holiday (Easter or Christmas) atmosphere is supposed to have a stimulating effect on customers and usually encourage them to purchase goods or service offered by the entrepreneur. Whereas it is not hard to recognize Christmas or Easter decorations as an advertisement and not the representation, because representation has generally the features of grandeur and refinement. The problem will appear with hired Santa Claus or Easter Bunny which walks through the shop and encourages for shopping, or gives sweets. At this point the interpreter must find for what purpose and what effect handing these gifts should cause? It is not without meaning what the Bunny has in basket, and Santa Claus in the bag. Concluding from the official statement of Tax Chamber Director in Poznan: “Expenses on advertising gadgets provided with the company logo or product logo (leather wallets, albums, basket gifts and other) up to the amount 100 PLN handed to contracting parties and potential customers may constitute the tax deductible revenue for taxpayer under to the Article 15 paragraph 1 of the Corporate Income Tax, because these are advertising, rather than entertainment expenses²⁰. In the same tone states another Tax Chamber Director in Poznan, the authority confirms that similarly to previous factual situation: “Giving small gifts during parties, exhibitions and similar actions sponsored by the company to potential, current or future customers as well as contracting parties on a large scale (gadgets), provided with the company logo has features of the advertisement, and expenses associated with it can be ranked among tax deductible revenues²¹. However, any shopping vouchers (at the assumption that we aren't acting as e.g. supermarket) about the value of 1000 PLN, handed by the Santa Claus or Bunny without a doubt must be categorized as representation. From the practical point of view, most safe for the taxpayer would be if the gifts will be small, marked with the company and preferably were related with the company activity, then there will be no doubt that the action will be categorized as the advertisement and therefore will be tax deductible revenue.

¹⁵ See: Biuletyn Skarbowy nb. 5/2007, p.12.

¹⁶ Director of Tax Chamber in Warsaw, IPPB5/423-432/09-6/JC.

¹⁷ Polish Ministry of Finance official statement from 17th July 1995 y. (POS/AK-722-702/95).

¹⁸ Ruling of Supreme Administrative Court from 6th May 1998 y. (III SA 1452/96).

¹⁹ Ruling of Provincial Administrative Court in Warsaw from 21st January 2009 y. (III SA/Wa 1597/08).

²⁰ Director of Tax Chamber in Poznań, ILPB3/423-34/09-2a/MC.

²¹ Director of Tax Chamber in Poznań, ILPB3/423-192/07-2/MC.

7. The conclusion

In the free market economy countries, where the entrepreneurs has to compete every day the marketing actions has key role to play. What more, nowadays it is bigger and bigger trend in the business that the entrepreneurs are building long-term and expensive marketing strategies, which are associated closely to rising financial resources. Therefore the tax regulations are so crucial and essential for every entrepreneur, and are directly connected to the advertisement and representation. Presented knowledge allow to categorize undertaken marketing actions, as advertisements or representation in the meaning of legal term and in turn gives the opportunity to qualify incurred economic costs as tax deductible revenue which simply will be reflected in higher profit.

Summing up, in dubious situations, when other methods seems to be insufficient, it is useful to utilize earlier described rules of reason, that will allow to state about the desired matters e.g. about gifts or holiday decorations character, and in consequence will allow to classify them whether as the representation and not tax deductible revenue or as the advertisement and the tax deductible revenues.

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