AN ANALYSIS OF THE CLASSIFICATION OF ADVERTISING COST FOR TAX PURPOSES

Amoré Diederichs
22345469

Dissertation submitted in partial fulfilment of the requirements for the degree *Magister Commercii* in Accounting at the Vaal Triangle Campus of the North-West University

Supervisor: Veruschka Pelser-Carstens
Co-supervisor: Lerike Jacobs
Prof Pierre Lucouw

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DECLARATION

I, Amoré Diederichs declare that ***An analysis of the classification of advertising cost for tax purposes*** is my own work and that all the sources I have used or quoted have been indicated and acknowledged by means of complete references.

Signature: _____

Date: _____

ACKNOWLEDGEMENTS

I would like to express the deepest appreciation to my supervisor Mrs Veruschka Pelser-Carstens, for her aspiring guidance, invaluably constructive criticism and friendly advice. I am sincerely grateful to Mrs Lerike Jacobs, Prof Pierre Lucouw, Mr André Swart and Mrs Marie Preston for sharing their truthful and illuminating views on issues related to this study.

I want to express my gratitude towards the staff of the NWU Vaal School of Accounting for their motivation through the course of my study. Furthermore I would also like to acknowledge with much appreciation Prof David Levey and Mrs Aldine.Oosthuyzen for editing and formatting my study.

A special thanks to my family and friends. Words cannot express how grateful I am to my mother and father for all the sacrifices that you have made on my behalf. Thank you to my dearest friend Ashley who urged me to strive towards my goal.

Lastly I would like to thank my Heavenly Father for giving me this opportunity.

ABSTRACT

Advertising plays a distinct role in economies around the world and, in this regard, diverse countries have been investigated in this study including the BRICS countries. It focused on the classification of advertising cost for tax purposes. Research questions posed by this study are answered through the development of a classification process that may assist with the classification of advertising cost for the purpose of taxation.

It has been established that guidelines for the classification of advertising cost as capital or revenue of nature are needed to correctly classify advertising cost for tax purposes. Furthermore, the determination of when advertising cost will be regarded as capital of nature is required.

The study used a mixed method research approach, involving a literature review of case law and income tax acts as well as an analysis of annual financial statements.

Findings from this research indicate a growing trend in revenue generated from advertising in South Africa; proving the importance of the advertising market in the economy. Guidelines for the classification of advertising cost for tax purposes were established by using principles from national and international case law.

Keywords: Advertising, Capital, Expense, Income Tax Acts, Revenue

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LIST OF ABBREVIATIONS

AME:	African Media Entertainment Limited
BRIC:	Brazil, Russia, India, China
BRICS:	Brazil, Russia, India, China, South Africa
FICCI:	Federation of Indian Chambers of Commerce and Industry
GAAP:	Generally accepted accounting principles
Hosken:	Hosken Consolidated Investments Limited
IAS:	International Accounting Standards
IFRS:	International Financial Reporting Standards
IRS:	Internal revenue Services
JSE:	Johannesburg Stock Exchange
Kagiso Ltd:	Kagiso Media Limited Limited
Naspers:	Naspers Limited
SARS:	South African revenue Services
TAA:	Tax Administration Act (28/2011)
Tax:	Taxation
The Act:	Income Tax Act (58/1962)
TV:	Television

CHAPTER 1
INTRODUCTION, PROBLEM STATEMENT AND OBJECTIVES OF THE STUDY

1.1 INTRODUCTION

Consumers are furnished with information through advertisements and advertisers are willing to spend a great deal of money on advertising their products (Backman, 1968:2). Advertising is commonly referred to as an endeavour to persuade consumers to feel a positive attitude towards a product or institution in order to ensure the purchase of such product which will then have an increased sales effect or create loyalty to that institution (Welukar & Harichandan, 2011:4). Advertising is, however, not a process by which gullible consumers are persuaded to buy goods and services they do not want (Backman, 1968:2). Economists are of the opinion that advertising is essential to ensure a specific sales rate (Akanbi & Adeyeye, 2011:117). Economists first drew attention to the intangible capital characteristics of advertising costs 52 years ago (Telser, 1961:194). An intangible asset may be referred to as an asset without physical substance that meets all other requirements of the definition of an asset as required by the International Financial Reporting Standards (IFRS), paragraph 4.4 of the Conceptual Framework.

While researchers accentuate the intangible capital characteristics of advertising costs in academic literature, advertisers accentuate the intangible capital characteristics of advertising costs through court cases. This is illustrated in the instance where one of the principles focused on in Commissioner of The South African Revenue Services v George Forest Timber Company Ltd (1924), was that of expenditure related to obtaining or generating an income yielding structure. The court explained that expenditure related to obtaining or generating an income yielding structure must be capital of nature. This statement has been investigated over the years by numerous researchers such as Telser (1961:194) and Hirchey (1982:375). However,

these investigations have proven inconclusive in respect of the determination and understanding of when advertising cost should be classified as capital of nature. Moodley (2011:57) therefore recommends that this topic should be further researched in order to establish classification guidelines.

The aim of the study was to understand the differentiation between and classification of advertising expenditure of a capital and of a revenue nature. This differentiation is crucial to establish when an expenditure, which is revenue related, will be deductible against income because this will not be the case if the expense is of a capital nature. Advertisers will therefore benefit from establishing classification guidelines.

A short overview of the basics of capital versus revenue of nature is presented in order to highlight the need for establishing classification guidelines. References to the Income Tax Act (58/1962) (hereafter The Act), the Tax Administration Act (28/2011) (TAA) and related case law, rules, regulations and practice notes are made.

1.1.1 Capital versus revenue

In accordance with section 11(a) of The Act, cost incurred that is capital of nature is a prohibited deduction. Moodley (2011:42) argues that the determination of the nature of cost incurred is thus an important factor in determining taxable income. McCann and Holmes (2010:1) states that the classification of costs as capital of nature is complex. Battersby (2008:41) posits that the line between the classification of advertising cost as capital or revenue of nature is unclear. Incorrectly recognising advertising cost as capital or revenue will not only have an impact on the taxable income, which will then directly influence the tax liability payable to SARS, but may also cause the misinterpretation of the TAA, that may lead to fines and penalties. Antecedent studies related to similar topics have addressed the issue, advancing different arguments and opinions (Peles, 1971:1032). Arguments and opinions, from Akanbi and Adeyeye (2011:117), Moodley (2011:57) and Telser (1961:195), include the notion that the intangible asset qualities that advertising cost may have, as well as the reasons for the classification of

advertising as capital or revenue, are important. This also highlights the importance of determining the relationship between advertising and future profits.

These arguments and opinions have moreover led to various court cases. In Bourke's Estate v The Commissioner for the South African Revenue Services (1991), The Commissioner For The South African Revenue Services v African Oxygen Ltd (1963), Sub Nigel Ltd v The Commissioner For The South African Revenue Services (1948) and Vallambrosa Rubber Co Ltd v Farmer (1910), the principle established indicates that cost spent to generate or obtain an income producing structure must be capital of nature since it is invested to earn future profits.

From principles established by the abovementioned court cases, it is clear that there are no clear classification guidelines. To emphasise the importance of understanding principles established in court cases, more such cases related to this topic will be discussed in detail during the progression of the study. By analysing these court cases, guidelines may be established to answer the problem statement posed in this study. This is discussed in paragraph 1.2.

1.2 PROBLEM STATEMENT

Antecedent studies have not yet resolved the question related to the classification of advertising as an expense or capital asset (Moodley, 2011:57). Determining the understanding of the principles given in The Act regarding the classification of advertising cost as capital or revenue of nature is important, since the incorrect interpretation of The Act will have a direct impact on the tax liability. Furthermore, this might lead to violations in terms of the TAA. This proves problematic for capital deductions and amortisation of advertisement cost as a capital asset.

Williams (2011:207) noticed that The Act requires the classification of an amount as capital or revenue for the purpose of income and expenditure or losses. The interpretation of The Act by Williams (2011:208) led to the conclusion that section 11(a) of The Act contains provisions related to the

deduction of expenditure and losses; however, only if such expenditure or losses are capital of nature. Hence the requirements set out in section 11(a) lead to questions being asked related to the classification of advertising costs.

A gap in academic literature on the classification of advertising cost as capital or revenue of nature exists. The vagueness and different ways of interpreting the sections of The Act with respect to advertising cost, may prove to be reason for the lack of understanding and erroneous application of the provisions of The Act that lead to violations of the TAA.

The gap in academic literature and the different principles established by court cases have left the following questions unanswered:

- When can advertising cost be seen as capital of nature?
- Can advertising cost be classified as an asset or intangible asset?
- Is there a link between advertising costs and long term benefits arising from advertising? (Darral, 1976:345)
- Does advertising cost have long term benefits? (Hassens, 2011:2)

Guidelines for the classification of advertising cost as capital or revenue of nature are therefore needed. Furthermore, the determination of when advertising cost will be seen as capital of nature is required.

1.3 OBJECTIVES

The following objectives were consequently formulated for the study:

1.3.1 Primary objectives

The study investigates

- When may advertising cost for tax purposes be classified as capital or revenue of nature?

The aim of the study is therefore to determine when advertising cost will be classified as capital or revenue of nature.

1.3.2 Secondary objectives

In accordance with the primary objective of the study, the following secondary objectives are formulated:

- To establish guidelines for the classification of advertising cost
- To determine the role of advertising in the South African economy.

1.4 RESEARCH DESIGN AND METHODOLOGY

1.4.1 Research design

The purpose of the analysis in this study may be described as an exploration of classification of advertising cost as capital or revenue of nature, as well as the evaluation and explanation of the outcomes of various court cases, to assist in understanding the sections 11(a) read together with section 23 of The Act, related to advertising costs.

The study comprises a literature review, including applicable case studies. An analysis of data will be performed with the use of financial records from companies listed on the Johannesburg Stock Exchange (JSE).

1.4.2 Research methodology

Rajasekar *et al.* (2013:5) explain research methodology as a methodical technique to solve a problem and to achieve research objectives. A qualitative research methodology approach, by means of a literature study and empirical study, known as a mixed methods study, was adopted for this research.

In order to achieve the research aim, the following objectives form part of the research methodology:

- Setting guidelines to use when classifying advertising as capital or revenue of nature
- Analysing the financial statements of JSE listed companies to determine the growth of advertising income in South Africa. This was done to emphasise the importance of advertising cost
- To deduce whether advertising cost can be classified as an asset

- To conclude how the treatment of advertising cost should be approached.

An investigation was conducted to determine when and why it is possible to establish advertising cost as capital or revenue of nature as well as the justification for advertising cost not having any capital allowance, according to The Act.

1.4.3 Literature review

The literature review was primarily conducted on primary and secondary sources and includes a comparison of the applicable legislation from South Africa, the BRICS and Commonwealth countries as well as the United States of America. It furthermore includes a comparison of the applicable court cases on advertising cost from South Africa, the BRICS and Commonwealth countries as well as the United Kingdom (UK) and the United States of America (US). Secondary data sources include relevant textbooks, journal articles, newspaper articles, financial statements and the internet. These sources are used to briefly describe the development of advertising and the growth thereof. In addition, the literature review was used in the process of establishing guidelines for the process of classifying advertising as capital or revenue of nature.

1.4.4 Empirical review and mixed method approach

The empirical review was conducted in such a manner as to determine the gap between literature, empirical literature reviews, legislation and court cases on advertising cost for tax purposes. Christie *et al.* (2000:10) explained that "the research methodology of qualitative case studies is process orientated and does not deal with cause and effect relations, but with underlying causal tendencies" and further stated that case study research is a way of comprehending the dynamics present in a management situation. Burns (2000:460) is of the view that following a case study approach ensures an exploration that discovers the comprehensive and meaningful factors of real life phenomena.

Case studies were used in this research to establish the classification of advertising cost as capital or revenue of nature by uncovering similarities in court cases and the accounting legislation of various countries related to this topic. The aim of this case study was to address the significant gap in the understanding of the nature of advertising cost in South Africa.

As an alternative to the conventional empirical review and literature study, a mixed method approach was used. This approach focused on textual analysis and on critiquing legislation referring to advertising cost for tax purposes, as well as on textual criticism of financial statements from JSE listed companies.

Information related to the growth of advertising income of JSE listed companies, specifically trading in the media, entertainment and broadcasting sectors, was analysed and interpreted. This was done to emphasise the importance of advertising cost.

1.5 ETHICAL CONSIDERATIONS

Questionnaires were not implemented, but a literature review and case studies were used in this study. An Ethics Approval Application Form obtained from http://www.nwu.ac.za/library/documents/manualpostgrad.pdf, was completed. The North West University's Guidelines for Ethical Research as set out in the Manual for Postgraduate studies are applicable to this study.

1.6 LAYOUT OF THE STUDY

This study comprises seven chapters, summarised below:

Following on Chapter 1, **Chapter 2** reviews the research methodology.

Chapter 3 provides a literature review on advertising cost. This chapter commences by briefly providing the history and development of advertising cost in the BRICS countries, the United Kingdom, the United States of America and some of the Commonwealth countries. An analysis and interpretation of advertising as an asset or intangible asset within the South African context is also undertaken. Furthermore, the development and role of advertising in South Africa are discussed.

In **Chapter 4,** the provisions of the South African Tax Act related to advertising are discussed. The income tax acts of the BRICS countries, the United Kingdom, the United States of America and some of the Commonwealth countries related to advertising are also discussed.

In **Chapter 5,** court cases from the BRICS countries, the United Kingdom, the United States of America and some of the Commonwealth countries, relating to the classification of advertising cost, are analysed and reviewed. The principles established in South African court cases are used as guidelines in this chapter.

Chapter 6 commences by analysing and interpreting the financial records of JSE listed companies, with the focus falling on companies trading in the media, entertainment, and broadcasting

In **Chapter 7** a comprehensive discussion and interpretation of the criteria relating to the classification and understanding of advertising cost, in correspondence with the information found in the previous chapters is provided. Pertinent information and conclusions from the previous chapters are summarised.

CHAPTER 2
RESEARCH METHODOLOGY

2.1 INTRODUCTION

According to Rajasekar *et al*. (2013:2), there are six prime objectives of research that should be kept in mind when the appropriate research methodology is selected for a study. The six steps will be applied in this study as follows:

- The first objective is to discover new facts. In this study new facts that were discovered were used in setting guidelines for the process of classifying advertising cost as capital or revenue of nature.
- The second objective is to verify and test important facts. In this study, important facts, such as the recognition of advertising as an asset for accounting purposes, are verified.
- The third objective is to analyse an event, process or phenomenon to identify the cause and effect relationship. In this study court cases, tax acts and financial records are analysed to help identify the relationship between the growth of advertising and the classification of advertising cost as capital or revenue of nature for tax purposes.
- The fourth objective is to develop concepts and theories to understand problems. In this study, new concepts and theories take the form of establishing guidelines to assist in the classification process of advertising cost as capital or revenue of nature for tax purposes.
- The fifth objective is to find solutions for problems. In this study an attempt was made to find a solution for the research problem.
- The final objective is to overcome or solve the problems occurring in our everyday life. In this study, attempts to reach this objective were made by establishing guidelines to be used to identify when advertising cost should be classified as capital or revenue of nature, for tax purposes.

After taking into account the six suggested objectives, this chapter attempts to give a detailed description of the research methodology that was applied for the purpose of this study. Research methods are discussed in the following paragraph, with a focus on qualitative, quantitative and mixed method research methods.

2.2 RESEARCH METHODS

Research methods may be divided into three groups:

- qualitative research methods
- quantitative research methods and
- a mixed method approach.

Quantitative research is described by Teddlie and Tashakkori (2009:6) as comprising systems that are related to the collection, examination, explanation and presentation of numerical information. Burns (2000:388) posits that qualitative research is not based on empirical fact. She outlines that qualitative methods venture to clarify and grasp certain definitions, interpretations and the validity of phenomena, whereas quantitative research is based on the calculation of phenomena. Paragraph 2.2.1 gives an overview of qualitative research.

2.2.1 Qualitative research

Maxwell (2012:3) explains that there is no specific design to follow in qualitative research. As Hancock *et al*. (2007:4) state, qualitative research strives to enlarge the comprehension of certain phenomena but they argue it is inaccurate to say that results found from a qualitative study are not generalisable even though qualitative research does not perform random sampling but, rather, uses a specific part of the population.

Trochim (2002:223) posits that there are many different methods that can be used when a qualitative approach is adopted for a research study. She further points out that the methods that may be used are restricted by the researcher him- or herself. Hancock *et al*. (2007:10) also explain that there are various

ways of conducting qualitative research. Qualitative research methods focus on the analysis and interpretation of case study materials, life stories, interviews, personal experiences, introspective analysis, interactional data, visual texts and historical documents (Taylor, 2005:106). Hennik *et al*. (2011:16) refer to qualitative research as having a basic objective that may be described as acquiring a comprehensive understanding of fundamental reasons, beliefs and motivations with regard to the solution of the research question and the achievement of research objectives set out in the study. As Burns (2000:11) indicates, qualitative research is based on the identification of the significance of subjective phenomena.

2.2.2 Quantitative research

Hennik *et al*. (2011:16) are of the opinion that the main objective of quantitative research is to quantify data and deduce results, applying them to a broader population, while the outcome is based on the analysis of data to establish patterns and to determine averages from the data that were collected in the process. Quantitative research methods include descriptive statistics, normal distribution and statistical significance in analysis of variance and meta-analysis (Burns, 2000:41).

Burns (2000:390) notes that quantitative research is not based on reviewing previous research and developing the researcher's own opinion on the topic; it is, rather, based on new findings as a result of data analysis. Quantitative research is best suited for deductive studies that test a theory or hypothesis and pose a narrow research question (Borrego *et al*., 2009:54). A research problem is usually developed when the data are collected, depending on the information required by the research question, after which data are analysed and the results are used to answer the research question (Borrego *et al*., 2009:54).

Newman and Benz (1998:2) propose that without taking the differences of a theoretical nature into account, quantitative research approaches usually indicate that there is a general similarity that can be agreed upon. A qualitative research approach is used when a hypothesis is tested to confirm

the validity of such hypothesis (Newman & Benz, 1998:3). Quantitative research may be referred to as having an empirical nature (Anderson, 2006:3) since data is collected, analysed and interpreted to test the hypothesis or suggest possible solutions for the research question.

Table 2-1 is used to summarise the differences and similarities between qualitative and quantitative research. The differences between these two methods may also be regarded in some ways as strengths and weaknesses. Table 2-1 will be used in the determination of weaknesses that the study may face and of how these weaknesses will be overcome by combining the two research methods in paragraph 2.2.

Table 2-1: Summary of differences between qualitative research and quantitative research

Qualitative	Quantitative
Gives information relating to "Which beans are worth counting?"	"Counts the beans"
Focus of the study is broad and based on the interpretation of the researcher	Focus of the study is narrow and based on factual data
Outlines significances and is discovery oriented	Determines connections between data and hypothesis
Makes use of examinations and associations	Uses instruments
Does not have a sample size; rather seeks information	Has a sample size that is unique to each study

Table 2-1: Summary of differences between qualitative research and quantitative research (continued)

Has subjects that are studied	Has participants that partake in the study
Has a research question	Has a hypothesis
Researcher is part of the procedure	Researcher does not form part of the procedure
Interprets information	Measures data
The literature study does not have to be carried out first; it may be performed during the progression of the study or at the end of the study	The literature study has to be undertaken at the beginning of the study
Research questions focus on: • What? • How? • Why?	Research questions focus on: • What quantities? • Weight of relation?
Aims to develop a new theory or build on an existing hypothesis	Experiments with a hypothesis or examines a hypothesis
Subjective	Empirical
The method can be described as recognising, interpreting and comprehending different phenomena and hypotheses	The method may be described as managing decreasing data in an accurate manner

Source: Adapted from Anderson (2006:3)

Table 2-1 gives a brief explanation of the most easily identifiable differences between qualitative and quantitative research. The comparison of the differences contributes to the reasons for using the research methodology followed in this study. Furthermore, it enables the achievement of the objectives as set out in Chapter 1.

Johnson and Christensen (2008:34) and Lichtman (2006:7) explain that qualitative research may be described as a chronological report that refers to opinions and describes phenomena in a contextual way. Johnson and Christensen (2008:34) and Lichtman (2006:7) furthermore explain that quantitative research is described as being a statistics based report which focuses on the comparison of statistical data. From the comparative summary provided in Table 2-1, it is evident that qualitative research and quantitative research do not share a great number of similarities. These two research methods differ in multiple ways, such as qualitative research being more subjective as opposed to qualitative research being objective.

2.2.3 Mixed method approach

Many researchers are of the opinion that qualitative and quantitative research methods should be kept separate and not mixed (Howe, 1988:10). Johnson and Onwuegbuzie (2004:14) aver that the on-going dispute between researchers about these two research methods causes new researchers to choose between these methods instead of staying true to the method of preference. Johnson and Onwuegbuzie (2004:16) consider that the use of a mixed method research approach will result in less flawed results and suggest that the reason for the use of such an approach may rather be seen as combining the best of both qualitative research and quantitative research in order to achieve feasible results. It may thus be assumed that the main reason for combining both research methods is to aim for the best possible ways to reach the best possible solutions for the problems posed in the study.

The mixed method methodology approach is relatively new (Teddlie & Tashakkori, 2009:7). Mixed method methodology is basically a combination of both qualitative and quantitative research methods. This method aims to solve

the research problem without encountering any limitations as well as achieving the research objectives set out in the study (Tashakkori & Creswell, 2007:4). The approach is a venture to combine different research approaches, in order to answer questions posed in the study without it being necessary to limit the researcher's options (Johnson & Onwuegbuzie, 2004:17).

Table 2-1 summarises the key differences between qualitative research and quantitative research. These were identified and taken into account before a research method was selected for the purpose of this study.

Table 2-2 identifies the weaknesses of this approach which may influence this study. The ways in which the said limitations will be addressed, to obviate interference with the study, are also described in Table 2-2. In other words, Table 2-2 is used to indicate the limitations that have been identified, as well as the solutions that are used to overcome these.

Table 2-2: Limitations posed by the mixed method research approach

Limitation	Solution
Due to the nature of the methodology both research approaches are used which is therefore time consuming	By the use of strict deadlines this limitation is overcome
Data needs to be transformed to allow integration	Due to the objectives of the study, results from both empirical research and literature research are easily able to be combined to establish a possible solution for the research problem

Source: Own research

As identified in Table 2-2, there are only two limitations that may cause some imperfections in this study; however these may be overcome by strict planning and good integration skills. Suggestions are made.

- Numbers may be accompanied by literature, images and chronological events to ensure a less puzzling and more comprehensible study.
- Literature may be accompanied by numeral results to strengthen theories or results.
- The strengths of both qualitative research and quantitative research are combined.
- A theory can be developed and tested by the researcher.
- With the combination of both qualitative research and quantitative research, a more complete insight which contributes to finding the best possible solution for the research problem, is offered.
- This approach results in a better conclusion due to both literature and empirical evidence being used, which means less factors are overlooked when determining a suitable conclusion.
- The strengths of one research method may be employed to overcome the limitations of the other research method.

2.3 APPLIED RESEARCH METHODOLOGY

In order to develop an impression of the knowledge required for this study it is essential to take previous research on this topic into account so as to understand research problems posed in previous research as well as possible solutions (Kumar *et al*., 2005:43). Chapter 1 of this research indicates that a mixed method approach will be followed. This has been selected to ensure that the research problem is solved in the best way possible without coming across the limitations that would have been encountered if only the qualitative research method or quantitative research method had been used.

A qualitative research approach is used in this study in combination with a quantitative approach, as opposed to just a quantitative approach. The latter would merely focus on the misconceptions related to the understanding, treatment and classification of advertising cost for tax and accounting purposes. A qualitative approach offers an appropriate way of understanding the reasons for the misconceptions and of finding possible solutions for the

problems highlighted by this study. The research structure that is followed in this study is explained in paragraph 2.4, by making use of six research steps.

2.4 RESEARCH STRUCTURE

Six research steps are followed in this study in order to ensure that the research process is approached in a well-structured manner. These steps are illustrated in Diagram 2-1, which is used to visually illustrate the flow of the research process in this study to achieve the research objectives set out in Chapter 1.

Diagram 2-1: Research process

Source: Rajasekar et al. (2013:2)

The following paragraphs indicate how the six steps have individually been applied to this study in order to conduct the research in an organised manner.

2.4.1 Construction of problems

Brewer and Hunter (2006:39) explain that a research problem should not only be perceived as a problematic, grey area, but as an opportunity that may offer new views and perceptions of certain phenomena. The problem that was

established for the purpose of this study emerged from a lack of knowledge and research relating to the classification of advertising cost as well as the possible recognition of advertising as an asset for accounting purposes.

2.4.2 Establishing research objectives

The research objective was established in the first chapter of this study in a meticulous, all-inclusive, transparent and practical manner.

2.4.3 Planning the study

The study was planned in a methodical manner incorporating both mentioned research methods; it may therefore be described as a mixed method approach. The study plan described in Chapter 1 focuses on the background, motivation of the topic's actuality, and the problem statement. It also concentrates on the objectives that should be achieved on the completion of the study and the research method that was used to conduct the study.

2.4.4 Methods of data collection

Data were collected for this study by means of:

- analysing court cases from South Africa on the classification of advertising cost
- analysing international court cases on this topic
- literature review of academic articles on the said topic
- analysing accounting records and information of JSE listed companies to gather information on the growth of advertising income (see paragraph 2.9)
- literature review of newspaper articles, internet articles, dictionaries and textbooks
- analysing national and international legislation to assist with realising a possible solution for the research problem posed in Chapter 1 and to achieve the objectives set out in Chapter 1.

2.4.5 Statistical analysis

Statistics obtained from JSE listed companies that trade in the media, entertainment and broadcasting markets were used to clarify the role and growth of advertising in the South African economy. These statistics were used to support the importance of classifying advertising into capital or revenue of nature.

2.4.6 Explanation of results

The results are analysed in Chapter 5 where possible solutions derived from the findings are discussed and weighed against alternatives. Advantages and disadvantages of the possible solutions are assessed.

2.5 CONCLUSION

The most suitable research approach for this study, a mixed method approach, was determined after taking the differences between qualitative and quantitative research, as set out in Table 2-1, into account. By using this approach the strengths of both types of research are combined to ensure that the best possible solution may be found for the problem statement.

The qualitative research entailed analysis of international tax acts. A comparison of them was undertaken to identify their similarities and differences regarding the tax treatment of advertising cost. Court cases were interpreted to assist in developing guidelines for the purpose of classifying advertising as capital or revenue for tax purposes. The limitations faced by using a mixed method approach were overcome by applying solutions to these problems, as indicated in Table 2-2.

Quantitative research was performed by analysing and interpreting the financial records of companies listed on the JSE that trade in the media, entertainment and broadcasting markets.

CHAPTER 3
ANALYSIS AND INTERPRETATION OF ADVERTISING COST AS AN ASSET OR INTANGIBLE ASSET

3.1 INTRODUCTION

The limited amount of antecedent studies related to the classification of advertising cost, as stated by Moodley (2011:57), leads to a misinterpretation of whether advertising should be classified as either revenue or capital of nature. The determination of advertising cost as an asset or intangible asset forms part of the foundation for constructing guidelines in the classification process.

The classification of advertising cost as capital or revenue of nature is important, since disclosing the correct tax payable or receivable is crucial for an entity in order to avoid fines and penalties as prescribed in the TAA. Elements that form part of the TAA structure and which may be affected by the wrongful classification of advertising cost are administrative non-compliance penalties, understatement penalties, dispute resolutions and tax liabilities and payments.

The BRICS countries, the United Kingdom, the United States of America as well as some of the Commonwealth countries have been selected for the purpose of this study. The reason is to ensure that jurisdictions from across the globe are being used and analysed to ensure a more comprehensive view of the tax treatment of advertising cost and the possibilities of the classification of advertising cost as capital or revenue of nature.

One of the main objectives of this chapter was to resolve the question found in paragraph 1.2 and the research objective as found in paragraph 1.3 of the study. The question that was focused on, for this chapter, is related to the possibility of recognising advertising as an asset or an intangible asset for accounting purposes. Furthermore, an overview of advertising in the

abovementioned countries is given in order to understand the role of advertising and what the term "advertising" means. The role, development and history of advertising in these countries are important elements that have an influence on how advertising cost should be classified. Further insight, into the development of advertising in the BRICS and other mentioned countries, is presented in order to understand the significance of the role that advertising plays not only in the South African economy but in economies globally.

3.2 THE BRICS COUNTRIES

The original acronym BRIC stands for Brazil, Russia, India and China, and originated in 2003 (Armijo, 2007:8). According to Gordhan of the South African Info Newsgroup (2011:1), South Africa was added to the BRIC equation In April 2011changing the acronym to BRICS. South Africa attended its first BRICS summit as a full member of the group of emerging economies. Carmody (2012:223) is of the opinion that South Africa's inclusion in the BRICS initiative is an indication of the growing impact that South Africa has on a global scale.

According to Ashley and Gilleard (2013:2), the information and knowledge related to methods of tax collection in the different BRICS jurisdictions will be shared among the five different countries. The BRICS countries' tax systems, however, differ from one another. In the opinion of these authors, the differences in the tax systems offer a learning opportunity for the members of the BRICS countries, which propose to enhance the tax systems in such a way as to benefit the people living in the BRICS countries. This is consequently also the reason for this study referring to the BRICS countries. The BRICS integration seeks mutual cooperation not only in political structures but also in other areas; some of these are international taxation, tax evasion, tax avoidance, tax administration and the exchange of tax information between the BRICS countries (Stuenkel, 2013:1).

The BRICS countries were therefore used in this study to compare the tax treatment of advertising cost in the various jurisdictions. The aim of the comparison was to establish similarities and differences regarding the tax

treatment of advertising cost in these tax systems, which was utilised in the process of classifying advertising cost as capital or revenue of nature.

Together with the BRICS countries, the Commonwealth of Nations Organisation is used to determine the similarities and differences in the treatment of advertising cost in the member countries' various tax acts. The Commonwealth of Nations Organisation is discussed in paragraph 3.3.

3.3 THE COMMONWEALTH COUNTRIES

According to the official website of the British Monarchy (2014), the organisation known as the Commonwealth was established 83 years ago. The organisation is voluntary and consists of 53 independent countries; the head of the Commonwealth organisation is currently the reigning British monarch, Queen Elizabeth. The 53 members of the Commonwealth, their estimated populations as well as the year in which they became an official member of the Commonwealth countries and the status of the countries may be seen in Table 3-1.

The lack of availability of some of the Commonwealth countries' Income Tax Acts led to some countries being omitted from the study and consequently from the tax analysis. The countries that have been omitted are also indicated in Table 3-1.

Table 3-1: Commonwealth members

Country	Date on which they became official members	Status	Population (2014/2013)	Used in this study
Antigua and Barbuda	1981	Realm	90,117	Used
Australia	1931	Realm	23,344,735	Used
The Bahamas	1973	Realm	37,7544	Omitted
Bangladesh	1972	Realm	157,220,520	Omitted
Barbados	1966	Realm	284,544	Used

Table 3-1: Commonwealth members (continued)

Country	Date on which they became official members	Status	Population (2014/2013)	Used in this study
Belize	1981	Republic	333,433	Used
Botswana	1966	Republic	2,030,376	Used
Brunei	1984	Monarchy	418,626	Used
Cameroon	1995	Republic	22,396,025	Omitted
Canada	1931	Realm	35,163,430	Used
Cyprus	1961	Republic	1,142,177	Used
Dominica	1978	Republic	72,084	Used
Fiji	1970	Republic	883,763	Used
Ghana	1957	Republic	26,042,191	Used
Grenada	1974	Realm	10,6119	Omitted
Guyana	1966	Republic	802,918	Used
India	1947	Republic	1,255,720,200	Used
Jamaica	1962	Realm	2,790,427	Used
Kenya	1963	Republic	44,611,813	Used
Kiribati	1979	Republic	102,719	Omitted
Lesotho	1966	Monarchy	2,084,352	Omitted
Malawi	1964	Republic	16,456,639	Omitted
Malaysia	1957	Monarchy	29,768,915	Used
The Maldives	1982	Republic	345,256	Used
Malta	1964	Republic	429,339	Used
Mauritius	1968	Republic	1,245,897	Used

Table 3-1: Commonwealth members (continued)

Country	Date on which they became official members	Status	Population (2014/2013)	Used in this study
Mozambique	1995	Republic	25,965,554	Used
Namibia	1990	Republic	2,317,853	Omitted
Nauru	1968	Republic	10,379	Omitted
New Zealand	1931	Realm	4,512,546	Used
Nigeria	1960	Republic	173,611,131	Used
Pakistan	1947	Republic	183,753,942	Used
Papua New Guinea	1975	Realm	7,357,050	Omitted
Rwanda	2009	Republic	11,865,106	Used
St. Kitts and Nevis	1983	Realm	54,310	Omitted
St .Lucia	1979	Realm	182,675	Used
St. Vincent and the Grenadines	1979	Realm	109,630	Omitted
Samoa	1970	Republic	191,257	Omitted
Seychelles	1976	Republic	93,033	Omitted
Sierra Leone	1961	Republic	6,128,647	Used
Singapore	1965	Republic	5,399,200	Used
Solomon Islands	1978	Realm	564,522	Used
South Africa	1931	Republic	52,914,243	Used
Sri Lanka	1948	Republic	21,250,333	Used
Swaziland	1968	Monarchy	1,258,121	Used
Tanzania	1961	Republic	49,483,005	Used
Tonga	1970	Monarchy	105,745	Used

Table 3-1: Commonwealth members (continued)

Country	Date on which they became official members	Status	Population (2014/2013)	Used in this study
Trinidad and Tobago	1962	Republic	1,341,063	Used
Tuvalu	1978	Realm	10,837	Used
United Kingdom		Realm	63,134,171	Used
Uganda	1962	Republic	37,828,742	Used
Vanuatu	1980	Republic	25,35740	Omitted
Zambia	1964	Republic	14,540,846	Used

Source: Official British Monarchy website (2014:1), World Population Review (2014) & Department of Statistics Singapore (2013).

Countries joined the Commonwealth from as early as 1931, as listed in Table 3-1. The first members of the Commonwealth were Australia, Canada, New Zealand and South Africa. The newest member of the organisation according to the official British Monarchy website (2014) is Rwanda, officially recognised as a member in 2009. The country with the smallest population that is part of the Commonwealth organisation is Nauru with an estimated population for 2014 of 10,379, while the country with the largest population is India, with an estimated population for 2014 of 1,255,720,200. Taking the data gathered in Table 3-1 into account it may be observed that the Commonwealth includes countries around the world with different population sizes, varying political statuses and differing geographic locations.

According to the official website of The Commonwealth (2014:1) the 53 countries that form the organisation are from around the globe and comprise not only wealthy countries, but rather a mixture of some of the countries in the world which are wealthiest and some of the most poverty stricken countries. The Commonwealth membership is made up from some of the world's

smallest countries as well as from countries regarded as leading nations (The Commonwealth, 2014:1).

The Commonwealth Association of Tax Administrators is currently the biggest tax administration organisation in the world, boasting 49 members that form the movement, of which South Africa is one (The Commonwealth Association of Tax Administrators, 2014:1). The above document points out that the movement is celebrating their 36th birthday this year (2014).

The history of advertising costs in South Africa as well as the development of advertising cost in the BRICS countries and some of the Commonwealth countries is discussed next.

3.4 ADVERTISING COST

Advertising is unavoidable in the modern world, whether it is television advertising, billboards, newspaper adverts or internet pop up advertisements, promoting a wide spectrum of products and services available to the consumer. An overview of the history of advertising in the BRICS and some of the Commonwealth countries as well as the United States of America is carried out. The purpose of this overview was to obtain an indication of the importance of advertising in the financial sector, whether national or international, to assist the study in understanding the role that advertising plays in an industry. This was with a view to assisting in the classification process of whether to relegate advertising cost to capital or revenue of nature.

3.4.1 Defining advertising cost in South Africa

The meaning of the word "advertising", which originates from the Latin word "advertere", is "to turn the mind towards" (Danesi, 2008:6). Since advertising is a complex concept, various definitions have been developed by researchers. According to Wanoff (2007:23) "advertising consists of all the activities included in presenting to an audience a non-personal, sponsor identified, paid for message about a product or organisation". Gardner (1975:40) remarks that "advertising is the means of mass selling that has grown up parallel with and has been made necessary to mass production".

The American Marketing Association Dictionary (2014:1) defines advertising as "The placement of announcements and persuasive messages in time or space purchased in any of the mass media by business firms, non-profit organizations, government agencies, and individuals who seek to inform and/or persuade members of a particular target market or audience about their products, services, organizations, or ideas".

Welukar and Harichandan (2011:2) are of the opinion that the ever changing trends and developments in the current market demonstrate positive results related to sales and awareness. These result in increased profits in a more competitive atmosphere amongst organisations, with the effect being an increase in the importance of advertising as a prime component in the business plan of an organisation, in order to achieve product or institution awareness and to improve sales. The importance of advertising in the modern world is crucial for the success of a business as stated by Calderon (2010:1), with continuing growth and increasing importance of the spectrum of different forms of advertising such as television, billboards, print and radio (Schwartz, 2013:1), it is important for tax purposes to determine the nature of classification thereof.

To ensure an unambiguous perspective on how advertising should be classified for tax purposes, it was necessary to gain an overview of the development of the role of advertising in South Africa, followed by an overview of the same in the other members of the BRICS countries and some of the Commonwealth countries as well as the United Kingdom and the United States of America.

3.4.2 Development and role of advertising in South Africa

Traces of early advertising have been found in many parts of the world, including ancient Greece, Egypt and China (Bose, 2011:1), ranging from papyrus advertisements to paintings on walls. The development and role of advertising is explained in the following paragraphs to obtain an idea of the importance of the role that advertising plays in any national economy. The Advertising Standards Authority of South Africa states that advertising should

be factual, communicative and true, without overstepping any South African law. With this statement in mind, it is clear that advertising plays a major role in this country's economy since there are certain rules and regulations related to advertising. However, it is not possible to accurately quantify or describe the scope of the role that advertising plays in South Africa. Nonetheless, a perspective on the significance of advertising here may be gained by the amount of hits received on Google when simply searching for Advertising in South Africa, which amounts to about 170 000 000 (Date of access: 28 Nov. 2014.).

Bearing the above in mind, it may be further assumed that advertising will result in tax implications that will then in turn influence the economy. It is therefore of great importance to classify advertising correctly for tax purposes (Milner, 2013:1).

3.4.3 International development and role of advertising within the BRICS countries

It is relevant to the study to understand the development that advertising has undergone in order to identify the role of advertising in modern day economies around the world. It is necessary for the purpose of the study to acquire an understanding of this role to simplify the classification process which has been mentioned.

Kamat (2012:1) is of the opinion that advertising originated in America and that some of the first advertisements in India were published in the early nineteenth century, their main use being to inform communities about births, deaths and dates upon which ships would arrive.

Greater insight is required in terms of the role of advertising as well as the development of advertising in other countries around the globe in order to investigate possible adjustments that could be made to those sections in The Act that deal with advertising cost and the treatment thereof. As indicated, this section focuses on advertising in the BRICS and some of the Commonwealth countries, as listed in Table 3-1, as well as the United Kingdom and the United

States of America. The development and the role of advertising is now explained, beginning with the BRICS countries.

Brazil

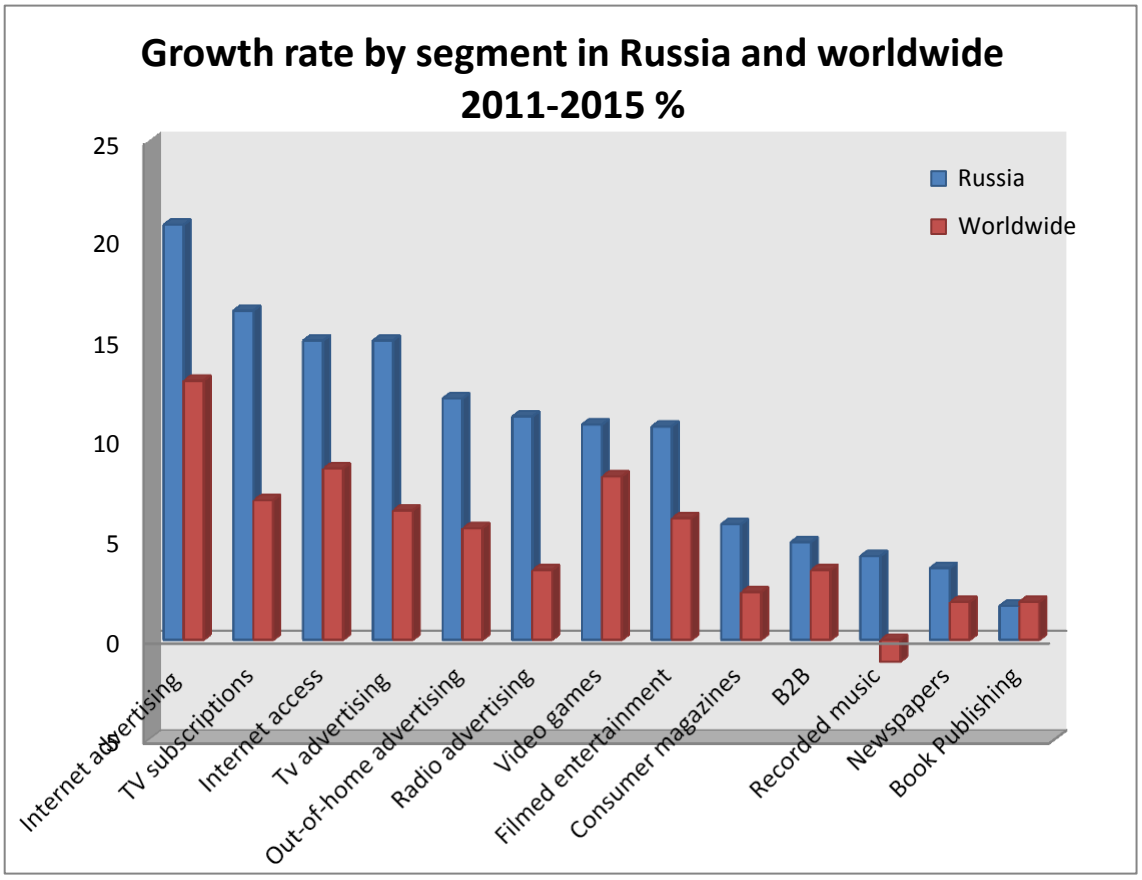
Rocha *et al*. (2003:1) state that regulations regarding advertising in Brazil were introduced into Brazilian law in the 1960's. Advertising in Brazil is changing due to the advent of the internet and modern day advertising, which are encroaching on the more traditional advertising methods (Mello, 2012:1).

Research results obtained by Avas Digital and GlobosatQualiBest (2011), from approximately 1 300 Brazilian internet users, indicate the growing tendency of online video advertising to be accepted by internet users (Acir, 2011:2). This research enhances the idea of increased modern advertising methods by focusing on video advertising as a fast growing form of advertising in Brazil.

Russia

According to Seferova (2006:2) advertising is a reflection of the modern mind-set that is constantly changing as a result of technology and the development of society. Seferova (2006:2) describes the advertising market of Russia as young, full of promise and gradually enlarging.

Yakvleva *et al*. (2011:2) report that according to PwC's Entertainment and Media Outlook 2011-2015, Russia has been found to be one of the fastest growing markets in the world. Predictions made by PwC indicate that Russia's media market will continue to grow in the future. The abovementioned report also illustrated the predicted growth of the Russian media market and compared it to the predicted growth of international media markets, as illustrated by Graph 3-1.



Graph 3-1: Estimated growth rate by segment in Russia and worldwide 2011-2015 %

Source: PwC Entertainment and Media outlook (2011:3)

In Graph 3-1 it may be observed that Russia's media market is expected to keep on expanding in the future. The growth of this market affords an indication of the growing importance of advertising, which further contributes to the necessity of correct classification of advertising for tax purposes.

The estimated growth rate of advertising by segment in Russia is also illustrated in Graph 3-1. This is compared to the worldwide norm; the comparison is made to demonstrate the dramatic growth of the advertising industry in Russia. The advertising market is divided into the thirteen most prominent segments of advertising in Russia.

In order to understand the said dramatic growth of this market it is necessary to understand the many reasons behind it. The key reasons for such rapid growth are provided and explained in Table 3-2.

Table 3-2: Reasons and explanations for growth in the Russian advertising market

Reason	Explanation
6th Largest economy in the world	This statistic means there are many markets in the economy that need to advertise their products and services, providing major advertising incentives.
Host of the 2014 Winter Olympics	Russia was the host of the 2014 Winter Olympic games, not only attracting foreign investors to the country but official sponsors of the games who had major advertising campaigns running before and during the games.
Growing oil and natural gas industry	The growth in the oil and natural gas industry brings economic development.
Large country	Russia is a geographically large country; because of this retailers go to extra lengths to ensure that all consumers are reached, causing strategically enlarged marketing campaigns.
Growing urban middle class	The urban middle class population of Russia is increasing; which may be regarded as a key attraction for investors to enter the Russian market.
Digital and mobile advertising	The lack of good infrastructure in Russia caused Russian advertisers to rapidly incorporate technology in their marketing strategies.
Traditional media	The continued growth of traditional Russian media is one of the factors in the fast growing advertising market of this country.

Table 3-2: Reasons and explanations for growth in the Russian advertising market (continued)

Russian tradition	Building successful advertising campaigns around Russian traditions and values gives cause for more increasingly integrated advertising.
Strong local competitors	Consumers in Russia find it hard to trust foreign markets and companies due to the history of Russia.

Source: Moorman (2014:1)

A combination of factors influences the growth in the Russian advertising market, with some of these factors being described in Table 3-2, such as the fact that Russia is the 6th largest economy in the world. As indicated in Table 3-2, there are many factors affecting this growth. This is an indication of the importance of advertising, which again emphasises the fact that the incorrect classification of advertising cost for tax purposes does have an influence on the economy of a country.

India

During the 1950's, the Indian Society of Advertisers and the Society of Advertising Practitioners were formed in India (Kamat, 2012:1). Research done by the Federation of Indian Chambers of Commerce and Industry (FICCI) (2012) indicates that advertising in India is developing at a rapid and effective pace. The development thereof increases the importance of the role that advertising plays in the Indian economy. During the 1960's and 1970's there was no reason for Indian entities to advertise, since advertising costs were not deductible for tax purposes (Ciochette, 2004:4).

Ciochette (2004:4) further states that during the 1980's, the Indian advertising market grew substantially due to the opening up of the Indian economy. This caused a spurt in the growth of alliances with foreign advertising agencies and the advent of more Indian advertising agencies. In the 1990's, the advertising

market in India continued to grow at a rapid pace, resulting in the need for sizable budgets for advertising agencies, due to the competitive multinational market in which they now found themselves. The Indian advertising market has continued to flourish due to continually changing technology, advertising methods, globalisation, consumer needs and products.

China

Between 1949 and 1979 there was basically no market for advertising in China since the government exercised control over most of the media. Due to the country's economic reform in 1979, the advertising industry in China grew exponentially – in an almost explosive way (Lee, 2009:4). Table 3-3 affords an indication of the most popular media in China and the medium used, as well as the language in which the media is available. This further justifies the study by way of determining the importance of advertising in China. As illustrated in the Table, nine out of the total 11 media have an English and a Chinese version, while three are Chinese only media and another three are English only media. Owing to the inclusion of English media it may be assumed that the media are not only intended for the people of China but also for foreign users. Table 3-3 is used to show the most important media in China and to understand popular Chinese advertising methods.

Table 3-3: Popular media in China

Media	Medium	Language
Beijing Evening News	Newspaper	Chinese
China Daily	Newspaper	English
GuanZhou Daily	Newspaper	Chinese
GuanZhou Morning Post	Newspaper	English
South China Morning Post	Newspaper	English
Ximin Evening News	Newspaper	Chinese

Table 3-3: Popular media in China (continued)

Media	Medium	Language
China News Service (CNS)	News Agency	English & Chinese
Asia Times	News Web Site	English & Chinese
CCTV-1	Entertainment TV	English & Chinese
Hong Kong Standard	Newspaper	English
RTHK Radio 4 Music	Entertainment radio	English

Source: adapted from Mondo Times 2009

From the information provided in Table 3-3 it may be assumed that advertising in China has increased substantially and embraced different advertising methods since 1979 and that it now forms a major part of its economy, Bittner (2008:9) also emphasises the growth of advertising in China since the 1970's.

The research that has been done in this study on advertising cost within the BRICS countries is limited. In order to overcome this limitation, reference is made to the United Kingdom, the United States of America and two of the Commonwealth countries: Australia and Botswana. The inclusion of Australia is due to the many similarities in the treatment of South African VAT and Australian VAT (Visser, 2014:1) A comparison of the likenesses of their Income Tax Act and the South African Act is made in Chapter 4. In addition, Botswana is discussed in more detail than the other Commonwealth countries, since it is one of the fastest growing countries in the world (Koppisch, 2002:1) as well as one of South Africa's nearest neighbours. Information on advertising cost, from these selected countries, was extensive.

The United Kingdom

Advertising agencies were first founded in the United Kingdom before the formalised concept was known in other parts of the world. Advertising in the

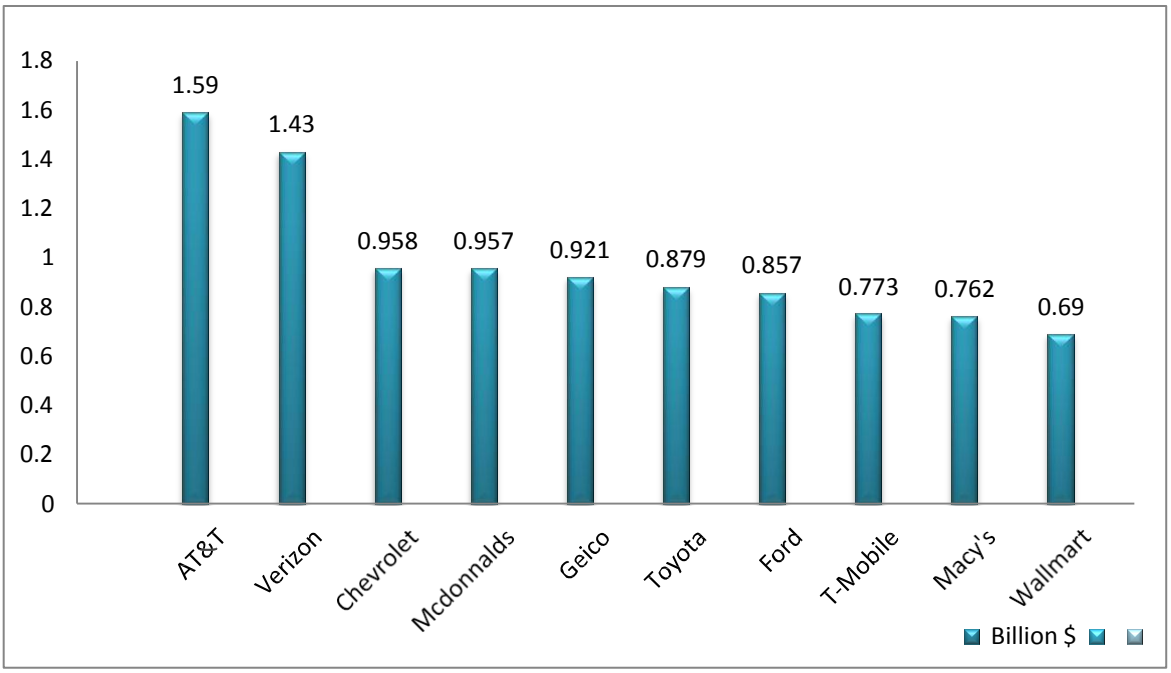
United Kingdom during the 1970's and 1980's steered the world of advertising (Northover, 2008:1).

Modern advertising is resulting in more competitive advertising around the world. Research has indicated, that owing to its increased importance, it is clear that it is an ever evolving element of the economy, and with this in mind the classification of advertising as capital or revenue becomes even more important**.**

The United States of America

Northover (2008:1) is of the opinion that the US advertising demand is the biggest in the modern world and therefore US advertising agencies dwarf others in the world. According to Crouse (2010:1), the first US advertising agency was founded by Volney Palmer during 1841 in Philadelphia, in agreement with Crouse (2010:1) Volney Palmer unknowingly altered the economy of America by introducing the first advertising agency to the Americans. Certain methods of advertising originate from the USA such as radio advertising, television commercials and internet advertising (O'Barr, 2010:1).

The United States of America contains many companies that spend large amounts of money on advertising campaigns in order to achieve brand awareness. AdAge.com (2013) compiled a list of the 100 United States of America leading advertisers of 2013. Graph 3-2 illustrates the top ten, by indicating the amount of money spent on advertising by the various companies during 2013.



Graph 3-2: Top 10 advertisers in the United States of America for 2013

Source: AdAge.com (2013)

As established in Graph 3-2, while the brand that has the highest advertising spend in the United States of America is AT&T, all of the top ten advertisers in the United States of America spend large amounts of money to gain the exposure that they need to ensure the success of their brands. According to Luden (2013:1), the fastest growing method of advertising in the United states of America is advertisements on mobile phones and tablets (mobile advertising) which showed a remarkable 81% growth rate during 2013; internet advertising is the second fastest growing advertising method in the United States of America with a growth rate of 16%. Multiple advertising agencies in the United States of America ensure a massive inflow of advertising revenue. The advertising agency with the highest growth in revenue produced by advertising is Google: it reported advertising revenue of $46 039 000 000 for 2012 which increased to $55 519 000 000 in 2013 (Financial Statements).

Certain similarities between the history and development in the abovementioned countries may be identified. Firstly, it is clear that advertising worldwide is revealing growth and the market for advertising is burgeoning, to

make consumers aware of products and services available to them. Secondly, it is easily identifiable that the technology spurt of the 20th century has exercised a major influence on traditional advertising methods, impacting not only on producers but also consumers. Thirdly, the fact that technology is improving at a rapid pace is causing internet advertising, mobile advertising and other new methods of advertising to reveal international growth.

Commonwealth Country: Australia

According to Davidson (2014:1), the advertising market in Australia indicated a slowing down trend due to the weakening of the Australian dollar. However, there are indications that this negative trend in the advertising market is coming to an end as some Australian companies are showing an increase in the current year's advertising revenues (Murdoch, 2014:1). Taking this into consideration, it is clear that advertising and the economy of a country are closely interrelated since it is evident that the advertising market was negatively affected by the weakening in the economy. Advertising in Australia did not only prosper from convincing Australians through creating brand preferences; it also influenced the individuality of Australian consumers by offering choices (Crawford, 2008:1). Crawford (2008:3) asserts that in the early 1920's, advertising was a fairly new concept in Australia, which, in order to convince consumers of its relevance, forced advertisers to engage in a great deal of detailed planning in order to integrate advertising with cultural standards.

Commonwealth Country: Botswana

According to the Botswana Media Sustainability Index (2009:11) growth was as expected for the future financial periods. The independence of media in that country is threatened by a law which ensures that all journalists must be registered with the government of Botswana (Botswana Media Sustainability Index, 2009:11).

According to Koppisch (2002:1), Botswana has the fastest growing economy in the world since 1966 Boesler (2012:1) also listed Botswana as one of the hottest economies in the world. As Botswana's economy is still in its growing

and development phase, it may be assumed that the growth and development of the advertising industry in Botswana will accompany that of the economy. Having a young economy, Botswana is still struggling to attract foreign investors but the government is aiming to improve market aspects to overcome this problem as stated in the *Botswana Government Gazette* (2014:1). If the factors that are limiting Botswana's attraction to such investors are overcome, the advertising market should display tendencies of growth if these investors launch advertising campaigns to reach consumers.

In order to achieve the research objectives of this study, it is necessary to determine if advertising may be recognised for accounting purposes as an asset or intangible asset. By applying the definitions and recognition criteria of an asset, paragraph 3.5 aims to determine if advertising may be recognised as an asset or intangible asset.

3.5 ANALYSIS OF THE RECOGNITION OF ADVERTISING AS A TANGIBLE ASSET AND AN INTANGIBLE ASSET IN SOUTH AFRICA

In accordance with the conceptual framework as per the International Financial Reporting Standards (IFRS), definitions of tangible assets and intangible assets differ slightly. It should be noted that this has a material impact on the accuracy of financial statements as well as on the interpretation thereof. The conceptual framework states that assets form part of the elements of financial statements (Deloitte, 2007:1). A comparative guide set out by Ernst and Young which provides guidelines on the difference in accounting treatment, comparing Generally Accepted Accounting Principles (GAAP) and the IFRS, states that the definition of assets is similar in both cases (2012:15).

In order to be able to determine whether advertising may be seen as an asset, one should first clarify, in terms of the conceptual framework as per the IFRS, what defines an asset and the applicable recognition criteria.

3.5.1 Assets and advertising

According to James (2009:20), accounting standards are used as the cornerstone for tax assessments. James (2009:20) further states that there is a vast difference between the accounting treatment and the tax treatment of an item. If the accounting treatment of advertising can be established it will form part of the bigger picture in the classification of advertising cost as capital or revenue of nature for tax purposes.

Paragraph 4.4 of the IFRS conceptual framework stipulates the definition of an asset. For an item to qualify as an asset it should be controlled by the entity in question, that is, a business entity, which includes any corporate or commercial establishment. Before the item does qualify it should have been acquired "as a result of a past event and the flow of future economic benefits from it should be probable (Australian Accounting Research Foundation, 1995:3). Not only must all the requirements be met but the recognition criteria for an asset have to be met as well (Clark *et al*., 2013:3). There are two:

- it should be probable that future economic benefits will flow to the entity
- it should have a reliably measurable cost.

If the requirements of the definition as well as the recognition criteria are kept in mind, it may be possible to classify advertising as an asset. The elements which form the definition of an asset in reference to the IFRS Conceptual Framework paragraph 4.4, are separately discussed to determine the possibility of advertising being classified as an asset.

Element number 1: Under the control of the entity

The first element of the definition of an asset is that the asset should be under the control of the entity in question (Weil *et al*., 2008:114). The argument can be advanced that advertising is under the control of the entity since it controls all the elements of placing the advertisement such as its nature (billboard, newspaper, radio or television advertising), the frequency of advertising, the geographical location of the advertising campaign and the target population.

Element number 2: As a result of past events

The second element of the definition of an asset is that the asset should be a result of a past event (Clark *et al*., 2013:3). Even though the entity exercises control over the advertising campaign, it should still be as a result of a past event since all the factors should be present before the definition can be met. In the case of advertising, the past event that might have occurred is the advertising contract as well as the implementation of that campaign.

Element number 3: Future economic benefits

The final element of the definition of an asset is that it should be "probable that future economic benefits will flow to the entity as a result of the asset" acquired (Vorster *et al*., 2009:12). This element is debatable, since the outcome of the advertising cannot be controlled, neither can the consumer; therefore it is impossible to determine the monetary value of economic benefits that will flow to the entity. However it is probable that economic benefits will flow to the entity in the form of cash generated, due to the awareness that has been created by the advertising campaign, even though the monetary value of the benefit is undeterminable. If only one new customer is attracted by an advertisement, a future economic benefit has been obtained.

The argument may be raised that the flow of economic benefits to the entity may not occur, but it is more probable that advertising will attract more customers and clients, which will cause an inflow of economic benefits. Advertising thus fulfils the element of the definition that relates to the flow of economic benefits from the asset in question.

Recognition criteria

For advertising cost to be classified as an asset, two criteria need to be met (Vorster *et al*., 2009:17). The first is that, as previously mentioned, advertising will cause possible future economic benefits to flow to the entity since the awareness generated by the advertising campaign will likely cause an influx of customers or clients. The inflow of economic benefits is not measurable in

monetary value, but it is possible to estimate such benefits. With this probable inflow as a result of advertising, it can be assumed that this cost meets the first recognition criterion.

The second that should be met is that the asset should have a reliably measured cost (Clark *et al*., 2013:3). With the cost of the asset (advertising) being the amount of money spent on the advertising campaign, it is clear that the cost of advertising is reliably measured; therefore advertising meets this criterion.

With the elements of the definition, as stipulated in paragraph 4.4 of the IFRS conceptual framework, in mind, it is possible that advertising in general can be regarded as an asset since it meets the definition of an asset and it adheres to both the recognition criteria. It is, however, possible for advertising not to qualify as an asset in a case where the specific transaction does not meet the requirements of the definition and the recognition criteria.

3.5.2 Intangible assets and advertising

According to the IFRS (IAS 38) an intangible asset may be described as an identifiable non-monetary asset (asset as defined in paragraph 3.5.1 that does not have a physical substance). It is further stated that an intangible asset can only come into existence if the item in question meets the definition of an asset and the recognition criteria for an intangible asset are also met.

In reference to IFRS (IAS 38 paragraph 21, 22 and 57) an intangible asset is identifiable as such if it meets one of the following criteria:

- The item is separable, dividable or able to be separated from the entity and sold on its own, transferred, licensed, exchanged or rented; either individually or accompanied by a related contract, identifiable asset or liability, regardless of whether the entity's intention is to do so; OR
- The item comes into existence as a result of contractual or legal rights: regardless of whether such rights are transferrable or separable from the entity or from other rights and obligations .

If advertising is to be measured against these two criteria it would most likely fall within the boundaries of the second criterion. If the first is to be analysed and applied to advertising, it is obvious that an advertising campaign, for example, will not be able to be separated from the business entity and sold on its own. An exception to this would occur if the business entity sells the rights to a brand or a product to another business entity; it may consider selling the advertising campaign together with the brand or product. This will be the case if advertising is part of the process of developing and registering a trademark. Even in the case where this event occurs, advertising may still not be perceived as an item that is able to be sold on its own. Advertising or an advertising campaign would not be able to be rented out or exchanged for another item since an advertising campaign is unique to each and every entity and would not be useable by another entity.

Advertising or an advertising campaign does however arise from contractual rights and agreements (Silkin, 2005:1), and it therefore meets the second criterion which states that for an item to qualify as an intangible asset it needs to arise due to contractual or other legal rights. Even though an advertising campaign arises due to contractual rights it cannot be separated from the entity in order to form an item that can be sold on its own. However the second criterion states that even though the item cannot be seen as separable or transferrable on its own, it may still qualify for being identified as an intangible asset.

For an intangible asset to be recognised IAS 38 paragraph 21 requires that two criteria have to be met:

- It has to be probable that future economic benefits that can expected to flow from the asset will cause an inflow into the entity; and
- The asset's cost can be reliably measured.

When the recognition criteria are applied to advertising or an advertising campaign it may be assumed that in line with paragraph 3.5.2 it can be expected that an advertising campaign will produce economic benefits due to the fact that advertisements aim to promote a product or service (Ashe-

Edmunds, 2014:1). The promotion of products or services will cause an inflow of economic benefits to the entity, which will flow to the entity itself in the form of customers; this in effect will cause higher revenues for the entity. It is thus accepted that advertising or an advertising campaign will meet the first recognition criterion for an intangible asset.

The second of the recognition criteria is that the cost that is attributable to the asset should be reliably measurable (Neuhausen & Schlank, 2007:253). The cost of an advertising campaign may indeed be reliably measured as the cost that was agreed upon by way of contract. In reference to IFRS (IAS 38) an intangible asset will always be recorded at its cost.

Since advertising meets both the requirements for recognition and the criteria for identification of an intangible asset it has been determined that advertising may be recognised as an intangible asset for accounting purposes.

For the purpose of this study it was assumed that advertising meets the requirements of the definition of an asset as well as the recognition criteria of an asset and an intangible asset; it will therefore be treated as such. Not all types of advertisements can be seen as assets. A clear distinction has to be made. In the case where the focus of the advertisement is short term and if it only has an economic value within the next business cycle, it will then be regarded as an expense. The definition and recognition of an expense is discussed in paragraph 3.5.4.

Advertising a winter sale or a special offer against a specific price will only be valid for a short term. Where the aim of the advertisement is to create general awareness without any price or terms and conditions being mentioned (for example, Coca Cola advertisements) it will then be recognised as an asset (Poole, 2014:2). In the case where advertising is classified as an asset it will have to be tested for impairments on a regular basis as prescribed in IAS 36.

In the case when advertising is recognised as an asset for accounting purposes and classified as capital of nature for taxation, elements such as depreciation and capital allowances will have to be considered, as will how these can be calculated.

Since assets lose their value over time they therefore has a limited useful life and depreciation is implemented to make provision for the loss of value (Vorster *et al*., 2010:69). According to accountingsimplified.com (2014:1), it is necessary to depreciate all assets in order to show the link between the asset and the economic value it has for the entity. If assets are not depreciated, this will give a misleading view of the entity's profitability.

Expenses of a capital nature cannot be deducted under s 11(a) or 23(g) of The Act as discussed in paragraph 4.6, Chapter 4. The Act does however make provision for capital allowance being deducted (Stiglingh *et al*., 2013:218). In the circumstances where advertising is classified as capital of nature, the relevance of a capital allowance being granted needs to be investigated.

Advertising may be recognised in three different ways, as established in paragraph 3.5: as an asset, an intangible asset or an expense, depending on the individual details of each scenario.

3.5.3 Expenses and advertising

An expense is defined in IAS 1, paragraph 4.33 of the conceptual framework. The definition consists of four elements:

- A decrease of economic benefits during the accounting period
- by way of an outflow of assets
- or increase in liabilities
- that has a decrease in equity as a result.

For an expense to be recognised it has to meet the recognition criteria of an expense. The cost of the expense needs to be reliably measurable and it needs to be probable that future economic benefits will flow to or from the entity as a result of the expense incurred.

Advertising cost meets the recognition criteria as previously discussed in paragraphs 3.5.1 and 3.5.2. However, in the case where it is recognised as an expense, there will be an outflow of economic benefits in the form of costs

incurred for the purpose of the advertisement. The definition of an expense may be applied to advertising cost if the cost is incurred for an advertisement with a short term benefit as mentioned in paragraph 3.5.2.

The elements of the definition of an expense may be applied to cost incurred for the purpose of advertising. Such a cost will lead to a decrease of economic benefits in the accounting period by the way of an outflow of assets; assets will flow from the entity by way of monies paid for the advertisement, the first and second elements of the definition thus being met. Advertising may create a liability by way of a debt incurred, resulting in an increase of numbers of creditors. A decrease in equity will be the result of more creditors and decreased assets due to payments made for advertisements.

The definitions of revenue, expenses and capital will be analysed from different sources to identify similarities and differences in the definitions. The definitions of revenue, expense and capital will advance the purpose of this study by way of ensuring that the distinctions between these three terms are clear and that they will not be confused.

3.6 REVENUE, EXPENSES AND CAPITAL

Definitions that should be clearly understood before attempting to establish the classification guidelines for the purpose of this study are: revenue, expense and capital. Various sources were used in order to obtain an unbiased view of the different ways in which these terms are defined. Definitions of these terms were analysed and summarised. Tables are used to analyse the definitions of the different terms and to illustrate the difference in these definitions. By the use of a Table format a comparison between the different definitions may easily be made.

3.6.1 Revenue

Various definitions of revenue may be found in textbooks, online dictionaries, dictionaries and articles. Table 3-4 summarises the analyses of definitions gathered concerning revenue for the above purpose.

Table 3-4: Summarised analysis of the definition of revenue

Revenue	Oxford Dictionary	Online Business Dictionary	IFRS
Definition	Income; Of an organization; Of a substantial nature.	Income generated; From sales or services; Or any use of assets; Before cost or expenses are deducted.	Gross inflow; Of economic benefits; From ordinary operating activities; Of an entity. [IAS 18.7]

Source: Own research

Table 3-4 provides an overview of the different definitions of revenue that were found in the individual sources used. The Oxford Dictionary (2014:1) also states that “revenue is usually shown as the first item in a profit or loss statement, from which all costs and expenses are deducted in order to establish the net income”. It is clear that the definitions from different sources all agree that revenue is income from ordinary operating activities.

3.6.2 Expense

Table 3-5 is used to summarise three of the many definitions of an expense that were found. The definitions in Table 3-5 were taken into consideration when developing the (proposed) guidelines for the classification process of advertising as capital or revenue of nature.

Table 3-5: Summarised analysis of the definition of expense

Expense	Oxford Dictionary	Online Business Dictionary	IFRS
Summarised definition of Expense	Cost incurred or required to acquire something.	Money spent. Cost incurred. In order to generate revenue. Representing the cost to do business.	Decrease in economic benefits during the accounting period. Resulting in an decrease in assets or an increase in liabilities. Resulting in decreased equity. (Conceptual framework 4.33.)
Summarised explanation of Expenses	-	Summarised and charged in the statement of financial position as a deduction from income before the calculation of tax.	Not related to distributions to equity participants.
Notes on Expenses	-	All expenses are costs, but not all costs are expenses e.g. costs incurred in the acquisition of an asset.	-

Source: Own research

Although the definitions of an expense stem from various sources, similarities do exist. The definitions as set out in Table 3-5 all stipulate that an expense is money spent to acquire something and that this occurrence results in a

decrease of income. If this definition should be applied to cost spent on advertising, the money spent would be the amount paid towards the advertisement, and this payment will lead to a decrease in income.

3.6.3 Capital

Many definitions of capital may be found when research is carried out on the topic; however, these definitions proved to have many similarities. Therefore only three sources have been used to compile table 3-6 from these sources, in line with those used in paragraph 3.6.1 and 3.6.2. The definitions of capital are crucial to this study since one of the research objectives, as stated in Chapter 1, is to determine if advertising may be classified as capital of nature; therefore it is important that there is a clear understanding of what capital entails. In this context, capital does not refer to the share capital of a company, but rather to an amount invested. The definitions are formulated in Table 3-6 so that similarities and differences between the three definitions may be easily identified.

Table 3-6: Summarised analysis of the definition of capital

Capital	Oxford Dictionary	Online Business Dictionary	IFRS
Summarised definition of Capital	Wealth; in one of two forms: money or assets owned by an entity or individual; applied to start a company or investing.	Common definition: Wealth; in one of two forms; Money or assets; indicating the financial strength of an individual, entity or nation.	No definition for capital as per IFRS.
Summarised explanation of Capital	-	Accounting definition: Money; invested; to generate income	No explanation of Capital given. Only an explanation on equity.

Source: Own research

One of the trending factors that may be seen in the definitions of capital as illustrated in Table 3-6 are that the capital is either in the form of money or of assets. Another notable factor is that the capital should be available to be used for investment. The Online Dictionary divides the definition of capital into subcategories as opposed to the Oxford Dictionary, but core similarities of these definitions remain.

3.7 CONCLUSION

After the analysis and consideration of the different definitions of revenue, expenses and capital, the main factors from each definition may be used together to form an overall definitions of each of these terms. Revenue may therefore be defined as income produced from operating activities by an entity or income produced as a result from assets being held by an entity, while the definition of capital may be stated as money or assets that are classified as wealth and applied for the purpose of investing. An expense may be defined as the outflow of money in order to acquire an item, with the purpose being to generate revenue.

The literature above has revealed that advertising is increasingly coming into focus as an element of the economy, not only in South Africa but also in India, Russia, Brazil, China, some of the Commonwealth Countries as well as the United Kingdom and the United States of America. Owing to the increased importance of advertising in these different economies, it may be assumed that the tax treatment of advertising cost may have a substantial impact on the said economies. The correct classification of advertising cost as capital or revenue of nature is therefore an essential factor and due to the growth of the advertising markets in the different economies, the growing importance of the correct classification of advertising with regard to tax is also increasing.

One of the objectives of this chapter was to answer the question posed in paragraph 1.2 regarding the recognition of advertising as an asset or intangible asset for accounting purposes. By answering this question one of the primary research objectives has been achieved as set out in paragraph 1.3.1. A proposed solution to this question has been found in Chapter 3. In

reference to paragraph 3.5, it is assumed that advertising will be recognisable for accounting purposes according to the guidelines set out by IFRS as an asset or an intangible asset. After critically discussing whether advertising may be seen as an asset or intangible asset, it may be concluded that in some situations it may be possible for advertising to be classified as either an asset or intangible asset, depending on the specifics of the situation.

An advertising campaign can have a very limited useful life with short term economic benefits and this may be an indication of advertising being an expense. If advertising is regarded as an asset for accounting purposes, it should continuously be tested for impairment in accordance with the International Accounting Standard (IAS 36).

As indicated earlier, when advertising is recognised as an asset for accounting purposes it is crucial that it meet all three of the criteria set out by the definition of an asset as applied in paragraph 3.5.2. After the definition has been met, the recognition criteria must also be met before an item can be recognised as an asset. It was found in paragraph 3.5.3 that advertising may also be recognised as an intangible asset for accounting purposes, if it meets the definition of an asset and the recognition criteria of an intangible asset as set out in IAS 38.

Provisions in the Tax Acts related to advertising were analysed and compared and are reported in the following chapter. Tax acts from various countries around the world were used to obtain a broad idea of the different provisions made in these acts that relate to advertising cost.

CHAPTER 4
PROVISIONS IN SOUTH AFRICA'S TAX ACT AND INTERNATIONAL INCOME TAX ACTS RELATED TO ADVERTISING

4.1 INTRODUCTION

Chapter 3 outlined the importance of the role that advertising plays in economies around the world. It also emphasised the fact that this is a growing market with significant future potential. With the completion of the primary objective relating to the recognition of advertising for accounting purposes in Chapter 3, the focus of this chapter lies in determining how advertising cost is treated for taxation purposes. In order to achieve the objectives set out in Chapter 1 in paragraph 1.3, tax Acts of various countries around the world were scrutinised for sections that deal with this issue.

The emphasis in this chapter is on provisions made for advertising cost in the different income tax acts of BRICS countries, the United Kingdom, the United States of America and some of the Commonwealth countries. By analysing these acts, a deeper insight into the tax treatment of advertising was gained. As set out in the problem statement in Chapter 1, it was necessary to establish if advertising cost may be regarded as capital of nature. Section 11(a) of The Act clearly states that expenditure of a capital nature cannot be deducted. Section 11(a) further stipulates that items of a capital nature often have an enduring benefit and they may be linked to a once-off payment (SARS, 2008:4). The different provisions found in each act were analysed and used to establish the differences and similarities of the provisions found for advertising cost in the various acts.

Provisions that could be found in the Tax Acts of the BRICS and some of the Commonwealth countries as well as the United Kingdom and the United States of America were analysed and are discussed in this part of the study, for the purpose just mentioned.

4.2 BRAZIL

Article 54 of the Brazilian Income Tax Act (30 of 1964) provides for the tax treatment of advertising. In reference to article 54, advertising cost may be deducted from the taxable income if the cost is exclusively incurred for the operations of the enterprise. Criteria are set out in article 54, and are as follows:

Advertising cost should be related to:

- Income earned from salaried, unaffiliated or professional work or income from the acquisition of copyright on artistic work;
- Amounts paid to media companies, in relation to announcements or publications;
- Amounts paid to broadcasters or television companies, related to advertisements, leased hours, or programmes;
- Expenses paid to any company, including marketing companies, provided they are registered as payers of income tax and maintain regular financial upkeep

Only if the criteria set out in article 54 of the Brazilian Income Tax Act (30 of 1964) are met, is advertising cost allowed as a deduction.

4.3 RUSSIA

According to Ernst and Young, expenses are commonly deductible if they are in accordance with Russian law and regulations, are able to be authenticated and are economically justifiable (Nab, 2011:20). The latter refers to the economic logic of a transaction; for example, if an entity sells a product for R200 and the advertising cost relating to the sale of the product is R10, it is economically justifiable; however if the advertising cost related to the sale of the product was R199 it would not be economically justifiable. The Doing Business in the Russian Federation guide, set out by Ernst and Young, further states that it is possible to deduct expenses that are not part of the allowable deductions of the Tax Code of the Russian Federation; the process of

deducting these expenses is just more complex. The deductibility of unlisted deductions depends mostly on the justification of the transaction by way of proof of the purpose and nature of the transaction in the form of settlement, records and statements. Most methods are deductible as business expenses (Nab, 2011:21).

In article 264 of the Tax Code of the Russian Federation (1 of 1998), which deals with other outlays involved in the production of income or the sale of goods, under sub-section 28, details related to provisions for advertising cost are stipulated. In accordance with sub-section 28 of article 264 of the Tax Code of the Russian Federation (1 of 1998) expenditure incurred in the course of advertising products, services, acquired items or advertisements related to the taxpayers undertaking is deductible as an expense for tax purposes.

More detail is given in sub-section 28 of article 264 of the Tax Code of the Russian Federation (1 of 1998) about other types of advertising ventures. Advertising costs incurred in order to advertise trademarks and service marks are also allowed as a deduction. The promotion of a business's participation in presentations and showcases forms part of the article 264 deduction.

There is no indication of the possibility of advertising being seen as capital of nature; this may be because the advertising market in Russia has only recently started to grow, as previously stated in 2.4.2.

4.4 INDIA

Section 36 of the Indian Income Tax Act (43 of 1961) deals with the deduction of specific items. This section points out that expenditure which is not capital of nature and has been incurred by an entity is allowed as a deduction if three requirements are met:

- The deduction item is constituted by a central State or Provincial Act
- The entity has complied with the rules set out in sub section a and is informed by the Central Government in the official gazette for the purpose of this clause

- The expenditure in question is incurred for the objects and purposes authorised by the Indian Income Tax Act (43 of 1961) under which it is constituted or established.

In reference to section 37 of the Indian Income Tax Act (43 of 1961), expenses that are not specifically addressed in the said Act (43 of 1961) may be deducted for tax purposes if the following criteria are met:

- the expenses incurred are not of a capital nature
- the expenses have not been applied for personal use
- the expenses are completely related to the business and its operations.

Furthermore, section 37 explains that expenses incurred which are in any form unlawful or related to unlawful activities are disallowed as a business deduction for tax purposes. It provides further detail on advertising by stating that advertisements linked to and published by any political party are not allowed as a deduction.

4.5 CHINA

An expense incurred by a business that is fair and has been incurred for the purpose of trade is deductible when Corporate Income Tax is calculated (KPMG, 2008:4). An expense that is deductible includes costs, business expenses, certain losses and other expenses (KPMG, 2008:4). Article 27 of section 3 of the Corporate Income Tax Law of China (1 of 2007) refers to related expenses as expenses incurred that may be directly associated with the production of income. This article also lays down that ordinary and essential costs which are incurred through the normal course of business and production of income must be used when gains and losses are calculated for tax purposes.

There are two categories of expenses as outlined in Article 28 of section 3 of the Corporate Income Tax law of China (1 of 2007): revenue expenditure and capital expenditure. The deduction of the former is calculated over an extended period while expenditure of a revenue nature is deducted in the current tax period.

Section 3 Article 44 of the Corporate Income Tax Law of China (1 of 2007) provides for the deduction of advertising cost and promotional cost to the extent of an amount to be calculated at no more than 15% of the income derived from sales for the tax period. This provision may be overruled if the department of the State Council in charge of finance and taxation decides on a more appropriate deduction (KPMG, 2008: 21). In the case where advertising cost amounts to more than 15% of the income derived from sales, the excess amount may be brought forward and will then be deducted in subsequent tax periods.

4.6 SOUTH AFRICA

Advertising cost, as stated by Stiglingh *et al*. (2013:145), qualifies as a transaction under the general deductions formula as per the Act. This, however, contains some limitations and requirements. For advertising cost to qualify as a deduction it must, to some degree be connected to the advertising of a pre-existing business. Furthermore, it has to meet all the requirements set out in the general deduction formula.

Components of which the general deductions formula are composed, as per section 11(a) and 23(g) of the Act, are detailed in Table 4-1. The purpose of the table is to understand the different elements.

Table 4-1: Discussion of general deduction formula elements

Element	Discussion
Expenditure and losses	• Expenditure refers to money spent or the reduction of assets.
Actually incurred	• As long as the liability to pay an expense has been incurred it may be deductible
During the year of assessment	• The expense has to be deducted in the year in which it is incurred

In the production of income	• The expense must be closely connected to the income producing activity • Expenses incurred in one year can be deducted even though income is only generated in the future
Not of a capital nature	• If an expense is incurred to acquire a capital asset it is capital of nature
For the purpose of trade	• The expense must be incurred for specific trading purposes

Source: Stiglingh et al. (2013:131)

There are factors that have to be considered before an expense may be deducted under the general deductions formula as per section 11(a) read together with section 23(g). The relevant factors are set out in Table 4-1. The expenses should be "actually incurred during the year of assessment; they have to be incurred for the purpose of trade and in the production of income" Stiglingh *et al.* (2013:131). It is of crucial importance that the expense is not of a capital nature, since it will not be deductible under the rule of section 11(a) and 23(g). Determining when advertising costs could be seen as capital of nature therefore makes it important to comply with the provisions set out in The Act.

In order for a cost to be deductible, it should meet all the components of the general deductions formula. Stiglingh *et al.* (2013:146) add that as soon as an asset with an enduring benefit develops as a result of advertising, it will be seen as capital of nature and will therefore not be deductible as an expense, as made provision for by the Act, under the general deductions formula.

Clear guidelines and requirements are set out in the general deductions formula as to when certain expenses will qualify as a deduction. There is a relatively short section dedicated to the explanation of the deductibility of advertising cost. The lack of detailed explanations regarding advertising deductions is evident in some of the tax textbooks most frequently used by

university students and lecturers, two of these being *Silke: South African Income Tax* (Stiglingh *et al*., 2013:145) and *A Student's Approach to Income Tax* (Venter *et al*., 2011:123). Section 11(a) and 23(g) of The Act states that advertising cost is not deductible under the general deductions formula as set out in the Act when it is of a capital nature, but the factors that should be regarded when classifying advertising as capital of nature are mostly absent and obscure. The fact that these factors or guidelines are unclear may cause a misinterpretation of the Act, which will consequently cause difficulties when calculating tax for an entity.

4.7 THE UNITED KINGDOM

The Business Manual provided by Her Majesty's Revenue and Customs (2014:1) states that there are provisions made for the deduction of costs that can be linked to advertising, if the expenditure is current and related to the advertising of the entities' products or services. It is also stipulated that advertising cost incurred for the purpose of acquiring an advertisement with a permanent benefit as well as of a long lasting nature will not be allowed as a deduction.

Specific items are addressed by the Business Income Manual of Her Majesty's Revenue and Customs (2014:1), as summarised in Diagram 4-1. This divides the other expenses into two categories, and describes these in detail in order to provide a clear understanding of the deductions allowed and disallowed.

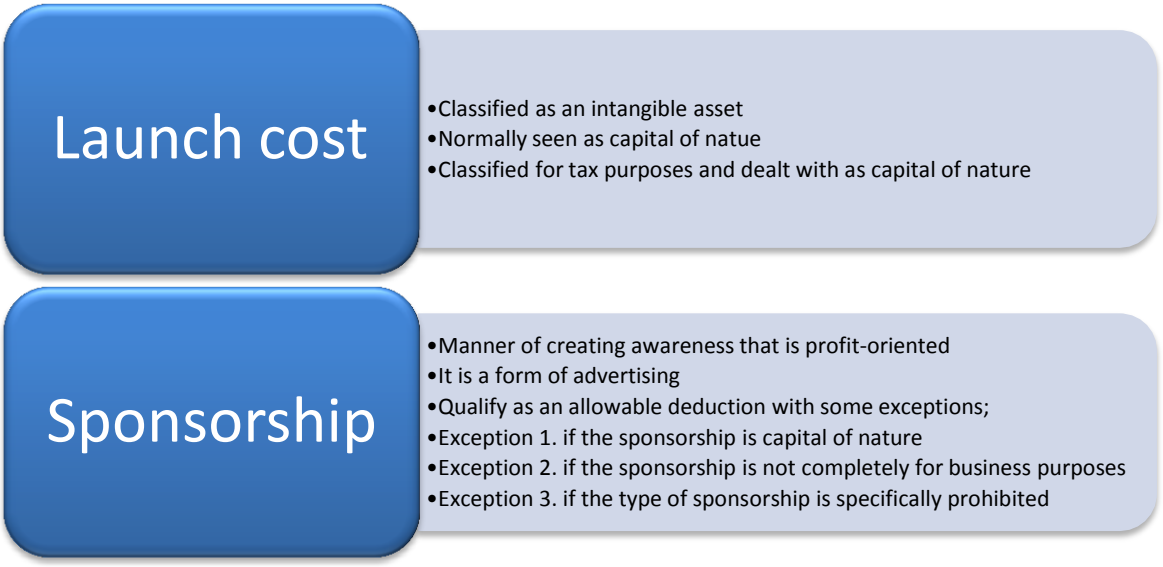


Diagram 4-1: Specific advertising items (The United Kingdom)

Source: Own Research

Diagram 4-1 briefly explains the specific advertising items; there are two groups: launch cost and sponsorship. As may be observed from Diagram 4-1, launch cost is usually seen as capital of nature and classified as an intangible asset while sponsorships lists three exceptions that are not allowed as a deduction; other than those three, all sponsorship cost will be allowed as a deduction.

4.8 THE UNITED STATES OF AMERICA

Thorndike (2013:1) is of the opinion that the deduction of advertising cost for tax purposes is often a topic of debate in the United States of America.

Costs related to implements used for the purpose of the business may be deducted if such implements are disposed of within 365 days from the date of purchase. Amounts paid for implements used in the business with a useful life of more than one tax year should be depreciated according to the methods of depreciation as set out in the American Income Tax Act (Internal Revenue Services, 2013:1). If this statement is interpreted in such a way that advertising may be seen as an implement used for the purpose of the business, because it is used to generate more income for an entity by way of

attracting money spending customers, as discussed earlier in Chapter 3, it is clear that certain types of advertising would qualify to be depreciated, such as billboards, TV commercials and radio advertising, since the lifespan of these advertisements can easily stretch over a period longer than one year.

A provision is made for other expenses in the American Income Tax Act; these are referred to as "ordinary" and "necessary" expenditure. The provision for other expenses has three categories, which are illustrated in Diagram 4-2.

This diagram is used to visually represent the three categories into which the provisions for other expenses are divided. These three categories describe the circumstances in which one expense may be deducted as another expense.

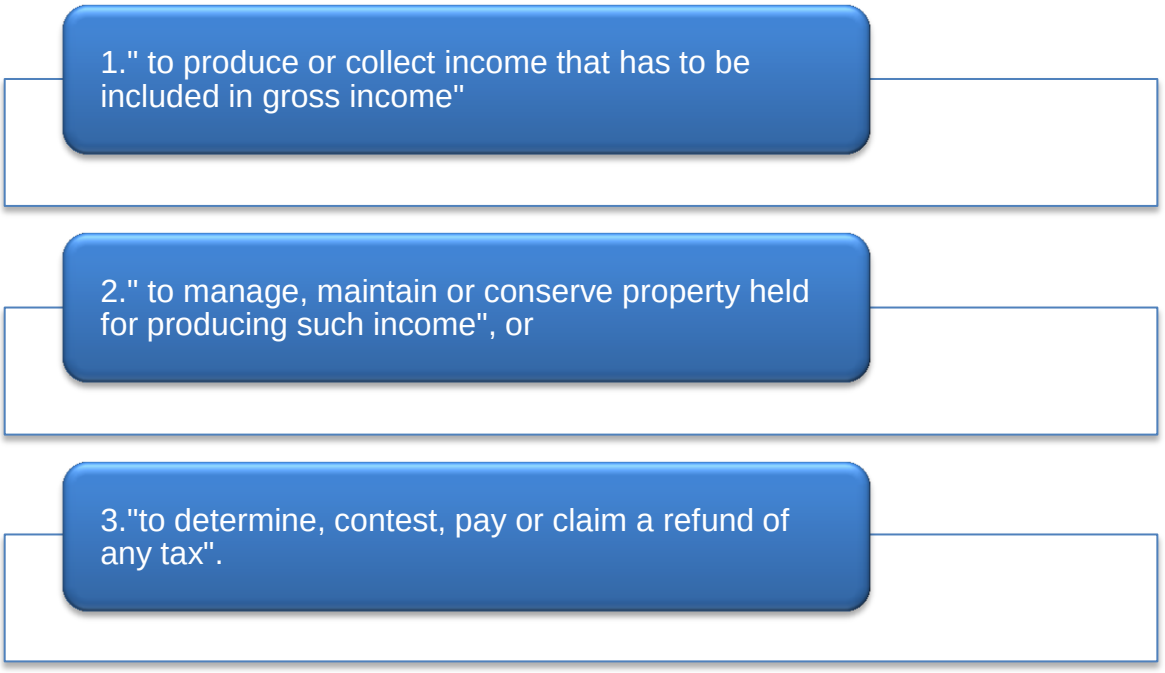


Diagram 4-2: Other expenses categories (The United States of America)

Source: The American Income Tax Act

Diagram 4-2 illustrates the three other expenses categories that will qualify as a deduction. If these are examined it becomes obvious that there is no specific deduction for advertising. However, it may occur that advertising falls

within the boundaries of the first of the three categories, since it may be argued that advertising plays a role in the production or collection of income that will be included in gross income. An itemised list is provided with expenses that can be classified as other expenses in interpretation note (Internal Revenue Services, 2013:1) but there is no mention of advertising cost. Nevertheless, assuming that advertising cost is a qualifying other expense, it will most likely be deductible under the first category.

A list of non-deductible expenses may be found under interpretation note 529 (Internal Revenue Services, 2013:1). Some of the items included in this are capital expenses, fines and penalties, personal expenses as well as bribes and kickbacks. Evidently, advertising cost is not listed on this list either and is thus assumed to be an allowable deduction.

The disallowance of the deduction of capital expenses as stated in interpretation note 529 (Internal Revenue Services, 2013:1) is explained as amounts spent to acquire capital items with a lifespan of more than one tax year. It also includes amounts spent in relation to increasing the value of existing property, or extending the useful life of another capital item. Such expenses are prohibited from being immediately deducted; however, provision for these expenses is made in the form of depreciation with the requirement being that the item, to which the expenses are related, is used for business purposes.

In general, it is stated that advertising expenses may be deducted if the expenses are reasonable. The aforementioned expenses should also be in direct relation to the business. Amounts related to advertising for goodwill purposes are also permitted as a deduction (Internal Revenue Services, 2013:1). In consulting the United States of America's Internal Revenue Service's resources and publications regarding advertising cost, the researcher has found that provisions made for advertising cost in the American tax system are not very detailed and descriptive regarding what specifically is included under advertising cost and what the criteria, for costs to qualify as advertising cost in order to be deducted, are. It is also unclear as to what is not included in advertising cost. The gap left by the lack of detailed

explanation may leave room for the misinterpretation of the American Tax Act; the gap is quite similar to the one that can be found in The South African Act. Paragraph 4.9 summarises the most important elements of the income tax acts related to tax treatment of advertising costs in most of the Commonwealth countries.

4.9 THE COMMONWEALTH NATIONS TAX ANALYSIS

An analysis of the tax acts of some of the Commonwealth countries was undertaken and illustrated in Table 4-2 in order to acquire a wider perspective on the various ways in which advertising cost is being managed worldwide, regarding its taxation. The intention here was to learn more about possible ways in which the provisions made in The South African Act may be adjusted to contain more detail on the treatment of advertising expenses.

The information derived from the different tax acts may be used to improve the provisions that are made in The South African Income Tax Act (58/1962). Countries that were omitted from the analysis of Commonwealth countries are:

- Bahamas
- Bangladesh
- Cameroon
- Grenada
- Kiribati
- Lesotho
- Malawi
- Namibia
- Nauru
- Papua New Guinea
- Samoa
- St. Kitts and Nevis

- St. Vincent and the Grenadines
- Seychelles
- Vanuatu

The above mentioned countries were omitted due to the unavailability of their Income Tax Acts for interpretation. The omission of the above mentioned countries was not a limitation for the study since they only represent 26.4 % of the Commonwealth countries.

Table 4-2 is a summary of key points derived from the tax acts of most of the countries which form the Commonwealth. This Table displays the sections in the various acts that may be linked to the deduction of advertising cost.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points

Country	Income Tax Act Name	Key points
Antigua and Barbuda	The Income Tax Act 1957 of Antigua and Barbuda	• Section 10(1) provides a list of allowable deductions if the costs have been incurred in the process of income production. • Section 10(1) (i) provides for other deductions that have not been specifically mentioned in section 10 or section 11. • Advertising is specifically addressed under sub section 10(2) (a)(ix). This section is dedicated to relief of hotel proprietors and stipulates that advertising, publishing and promoting the business related to the hotel prior to the start of such business will be classified as capital expenditure.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
Barbados	Income Tax Act 1989 of Barbados	• Division F section 10(1) (a) provides for the deduction of expenditure incurred in the production of income. • There is no specific mention of a deduction related to advertising cost.
Belize	Income and Business Tax Act 1999 of Belize	• Section 11(1) states that there will be an allowable deduction for any amount spent that is directly linked to the production of income by the taxpayer who is not an employed person. • Section 11 (2) indicates that the Minister may use his own discretion apply certain rules to this section 11.
Botswana	Income Tax Act 1995 of Botswana	• Section 39-50 provides for allowable general deductions if the cost incurred is directly applied in the process to produce income that will be taxable. • Paragraph 3 of the act outlines that when computing the taxable income of the taxpayer any amounts related directly to marketing should be deducted from gross income, while paragraph 3(g) specifically states that advertising and sales promotion expenses should be deducted.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
Brunei	Income Tax Act 13 of 1951 of Brunei	• Any expense that is attributed to the production of income that may be taxed by the taxpayer will be allowed as a deduction as per section 11(1). • Section 11B(1) states that costs related to an approved marketing project overseas and cost related to advertisements placed in the approved Brunei Darussalam publication for publicity overseas may be deducted. • The minister may as per section 11B (2) decide on a maximum amount of deductions related to section 11B (1).
Canada	Income Tax Act of 1985 of Canada	• Section 18(1) (a) indicates that deductions will be allowed for expenses incurred solely for the purpose of producing taxable income. • In reference with section 19(1) when income is calculated there will be no deduction allowed for advertising expenses incurred for advertising in a newspaper with the target being Canadian consumers, unless the advertisement is in a Canadian newspaper.
Cyprus	Cyprus Income Tax Law 2002 of Cyprus	• Section 9(1) provides for the deduction of expenses that are applied wholly for the production of taxable income for any person.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
Dominica	Income tax Act 37 of 1982 of Dominica	• Under section 39(2) taxable income will be determined after taking allowable deductions into account; deductions allowed need to be expenses solely incurred for the purpose of generating income that will be taxable.
Fiji	Income Tax Act 6 of 1974 of Fiji	• Section 38(x) (iv) which deals with company administration and management cost stipulates under sub section (C) that any amount related to marketing will be allowed as a deduction.
Ghana	Internal Revenue Act 592 of 2000 of Ghana	• Any amount spent in order to generate income by an individual will be allowed as a deduction in line with section 13, as well as any other deductions that are stipulated in section 114. • Section 114 deals with the rights of the Commissioner of Internal Revenue.
Guyana	Income Tax Act 17 of 1929 of Guyana	• Amounts directly related to the production of income that has been spent in the year before the current tax year will be allowed as a deduction as per section 16(1).
Jamaica	The Income tax Act 1985 of Jamaica	• Section 3(a) stipulates that expenses incurred in acquiring taxable income may be deducted from gross income.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
Kenya	The Income Tax Act 1973 of Kenya	• Under the guidelines provided by section 15(1) any cost incurred for exclusively for the production of taxable income, will be allowed as a deduction. • Section 15(2)(p) contains a detailed provision for the deduction of advertising expenses, which states that advertising cost may be deducted if it is in connection with the business to the extent that the Commissioner considers it reasonable, this expenditure includes any expenditure incurred with the intention to promote the sale of goods or services whether directly or indirectly.
Malaysia	Income Tax Act 53 of 1967 of Malaysia	• Section 39(l) (iv) prohibits the deduction of promotional samples.
Maldives	Business Profit Tax Act 2011 of Maldives	• Under the provisions made in section 10(a) no amount except amounts incurred for the purpose of generating taxable income may be deducted from gross income.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
Malta	Income tax Act 54 of 1948 of Malta	• Deductions are allowed for expenses incurred in the previous year of assessment if such expenses are exclusively incurred for the production of income (section 14(1)). • 14(1) (l) indicates that costs related to advertising may be deducted from gross income.
Mauritius	The Income Tax Act 1995 of Mauritius	• Section 67A stipulates that any entity carrying on a trade that is related to tourism or export activities is allowed to deduct double the amount of any expenses incurred on overseas marketing. This includes export promotions, participation in international trade fairs and overseas advertising. • As found in section 18(1) any amount incurred which is directly attributable to the production of gross income may be deducted.
Mozambique	Income Tax Act 1989 of Mozambique	• Income Tax Act was not found • Ferreira (2013:1) posits that the Mozambique Tax Act has provisions for specific deductions for every income schedule as well as global deductions.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
New Zealand	Income Tax Act 97 of 2007 of New Zealand	• DG7 (1) deals with expenditure relating to income earning use, and states that a person is entitled to a deduction to the extent to which the amount relates to business activities. • DV1(1) & (2) refers to a publicising superannuation fund and is applicable when a superannuation fund incurs costs in the processes of developing, advertising, promoting or advertising the fund. The fund is allowed a deduction for these types of expenditure.
Nigeria	Personal Income Tax Act 104 of 1993 of Nigeria	• All expenses incurred that can be directly attributed to the production of income will be regarded as a deduction (section 20(1))
Pakistan	Income Tax Ordinance 49 of 2001 of Pakistan	• Section 20(1) stipulates that any expense that is exclusively incurred for the purpose of business will be allowed as a deduction; the deduction however does not include expenditure in relation with the acquisition of a depreciable asset and intangible asset with a life of more than 1 year.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
Rwanda	Income Tax Act 16 of 2005 of Rwanda	• Article 21 provides for deductions for expenses if they are incurred for trade and linked to ordinary business; these should be supported by documentation, the expenses should result in a decrease of net assets and they should be incurred in the current tax period.
St. Lucia	Income Tax Act 1 of 1989 of Saint Lucia	• Section 37(2) deals with general deductions and stipulates that any amount related to the production of taxable income will be allowed as a general deduction.
Sierra Leone	Income Tax Act 2000 of Sierra Leone	• According to section 32(2) all amounts may be deducted if incurred for the purpose of generating taxable income.
Singapore	Income Tax Act 39 of 1947 of Singapore	• Any expense that is directly related to the producing of gross income, except amounts related to interest, may be deducted under section 14. • Section 11(b) provides for the deduction of advertising expenditure if the advertisement is placed in approved media.
Solomon Islands	Income Tax Act 1982 of Solomon Islands	• In order to determine the taxable income of an individual all expenditure incurred by the individual that is of such nature that it can be wholly attributed to the generation of taxable income as per section 18(1) should be deducted.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
Sri Lanka	Income Tax Act 10 of 2006 of Sri Lanka	• Section 25(1) provides for the deduction of expenses if related to the income generating activities of the entity.
Swaziland	The Income Tax Order 21 of 1975 of Swaziland	• No indication of general deductions or specific deductions for advertising could be found.
Tanzania	The Income Tax Act 2004 of Tanzania	• Subdivision D relates to deductions, section 11(2) stipulates that deductions will be allowed for expenses incurred exclusively for the purpose of generating taxable income. • Section 11(3) states that there will be no deduction for expenses that are of a capital nature. • The act provides for advertising cost under assets and liabilities, indicating that advertising cost will be included in incidental expenditure incurred for acquiring or realising an asset.
Tonga	Income Tax Act 10 of 2007 of Tonga	• Section 25 provides for deductions of expenses if incurred in the production of gross income.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
Trinidad and Tobago	Income Tax Act 34 of 1938 of Trinidad and Tobago	• No provision is made for general deductions; however the act provides for various specific deductions. • Under section 12(a) the act stipulates that any expense that is not directly related to the production of income may not be allowed as a deduction. • Section 10A(1) stipulates that if promotional expense is incurred for the purpose of generating taxable income it may be deducted, while section 10A(5)(a) indicates that advertising cost may be seen as promotional expense.
Tuvalu	Income Tax Act 5 of 1992 of Tuvalu	• Section 12 indicates that the taxpayer has the authority to treat expenditure as deductible cost if such expenditure is directly linked to the production of gross income.
Uganda	Income Tax Act 17 of 1929 of Uganda	• Section 22 provides for expenses derived from income being allowed as a deduction from gross income, and stipulates that expenses which are solely incurred for the purpose of producing income may be deducted under the provisions of this section.

Table 4-2: Commonwealth countries tax act analysis, focusing on key points (continued)

Country	Income Tax Act Name	Key points
Zambia	Income Tax Act 32 of 1967 of Zambia	• Section 29 provides for general deductions, being expenses incurred wholly for producing income which is not of a capital nature. • Section 44 deals with deductions that are not allowed. Section 44(i) states that any expenditure related to advertising to the public whether capital of nature or not may not be allowed.

Source: Own research

Table 4-2 indicates the country, the tax acts and the key elements that can be identified in the tax acts which relate to the tax treatment of advertising cost. The provisions found in the Australian tax act that relate to the tax treatment of advertising cost are discussed in the following paragraph.

4.10 AUSTRALIA

The Australian Income Tax Assessment Act (38 of 1997) of Australia contains provisions for general deductions under Division 8; it also makes provision for promotion and advertising expenses in section 32. Division 8(1) states that an amount may be deducted as a general deduction if it is used in producing taxable income or it is incurred for the purpose of carrying on a trade with the aim of being able to produce taxable income. Section 32-5 deals with promotion and advertising expenses, and indicates that a loss or expense related to promotion and advertising may be deducted under certain circumstances; these are explained in the Income Tax Assessment Act (38 of 1997) and are summarised in Table 4-3.

Table 4-3: Circumstances stipulated in Section 32 (Australia)

a) When entertainment is provided if: it is provided to an individual due to a contractual obligation to supply the individual with products or services; and b) The loss or expense is incurred in the course of advertising or promoting the business, goods or services to consumers.	In circumstances a and b, the deduction will be allowed as per section 32-5.
c) Expenses related to an exhibition held of goods, services or the business in order to advertise or promote such goods, services or business to consumers.	In circumstance c, the deduction will be allowed as per section 32-5.
d) When entertainment is provided to promote or advertise goods, services or the business to consumers e) The same principle applies as in "d" however it results in certain consumers having a better chance to get benefits from the entertainment than other consumers.	In circumstance d, the deduction will be allowed as per section 35-2 but for circumstance e no deduction will be allowed under this section.

Source: Australian Income Tax Assessment Act (38 of 1997)

Table 4-3 describes the five special circumstances as stipulated in section 32 of the Australian tax act. The circumstances are described, as are the specific rules applicable to these circumstances.

Certain key points have been identified from the analysis of the various tax acts. These are shown in Table 4-4.

Table 4-4: Key points identified from tax act analysis

Country	Key Points
Brazil	• There are provisions made for the tax treatment of advertising cost • In order to deduct advertising cost there are three criteria that should be met
Russia	• There are provisions available for advertising cost • Advertising cost may be deducted if it is closely related to trade • Advertising cost related to presentations and showcases is deductible • There is no indication of the possibility of advertising cost being capital of nature
India	• There is not a specific provision for advertising cost • It is assumed that advertising cost is deductible under other deductions • Other deductions are disqualified if against the law • Advertisements published by political parties are not tax deductible
China	• There is a specific provision for advertising cost • The deduction of advertising cost is limited to 15% of sales income • Amounts more than the permitted 15% may be brought forward and deducted in succeeding tax periods • No mention of advertising as capital of nature

Table 4-4: Key points identified from tax act analysis (continued)

Country	Key Points
South Africa	• Provisions are made for advertising expenditure related to trade to be fully deducted • Advertising of a capital nature is not deductible • Lack of explanation regarding capital of nature in the case of advertising
Australia	• There is a provision for general deductions • A specific provision is made for promotion and advertising expenses being deductible in certain circumstances as set out in Table 3-5.
Botswana	• Provisions for allowable general deductions are available • Specific provisions are made for advertising expenses causing them to be deductible
United Kingdom	• There are provisions made for the deduction of advertising costs • The provision applies only if the cost is incurred for the advertisement of products or services • Long lasting advertisements as well as advertisements with permanent benefits are disregarded • Launch cost is seen as an intangible asset while sponsorships are regarded as an expense
United States of America	• There is no specific provision made for the deduction of advertising cost • Advertising cost may qualify as a deduction under other expenses if it is fair and reasonable

	• Advertising for the purpose of goodwill is allowed as a deduction

Source: Own research

Table 4-4 highlights some of the key points that have been identified as a result of the analysis of various income tax acts with the focus on the BRICS countries as well as the United Kingdom, the United States of America, Australia and Botswana.

4.11 CONCLUSION

The treatment and provisions made in the different tax acts of the BRICS countries, some Commonwealth countries as well as The United Kingdom and The United States of America have been examined and it is clear that some similarities exist related to the tax treatment of advertising cost as illustrated in Table 4-4.

The key element that is found from the information of the South African treatment of advertising is that advertising cost is fully deductible as an expense if it is in relation to the trade that is carried on by an entity. However, it will not be deductible if it is capital of nature. Furthermore, there is a lack of explanation regarding the situations when advertising is capital of nature. The provisions made for advertising in the United Kingdom are similar to those that can be found in South African law. Both allow advertising as a deduction if it is related to trade and both disallow advertising that is capital of nature. The information regarding advertising provisions in the United Kingdom also lacks clear guidelines as to when advertising is capital of nature.

While provision is made for advertising in the Russian law if the cost is closely related to income earning activities, no provision could be found in Indian law for this item. Russian law allows the deduction of advertising cost in relation to presentations and showcases; this specific deduction is only visible in Russian law. No indication as to whether advertising can be considered as capital of nature is found in Russian law.

The Chinese tax act makes provision for the deduction of advertising cost, but the deduction is limited to 15% of income derived from sales. If the cost is more than the allowed 15% it may be brought forward and deducted in the following tax periods. There is no indication in the provisions for advertising deductions of the capital nature of advertising. There is no specific deduction for advertising cost in the American tax law, but it is stated that advertising for the purpose of goodwill may be deducted. Advertising may qualify for a deduction under other expenses if it is fair and reasonable.

For advertising cost to be classified as revenue or capital of nature for tax purposes, it must be determined if it qualifies as an asset. The different factors and recognition criteria need to be met (Clark *et al*., 2013:3) in order for it to qualify as an asset. With the different methods of advertising existing in the modern economy, this proves to be a challenge; however, each advertising transaction should be individually handled when determining if it qualifies as an asset. In this chapter it was found that most of the BRICS countries, as well as most of the Commonwealth Countries, apply the principle that if an expense is related to the generation of taxable income it may be deducted and if an expense is capital of nature then it may not be deducted, as set out in section 11(a).

Chapter 4 contributed to achieving the solution to the problem stated in Chapter 1 of the study by way of determining key points in the tax treatment of advertising cost in various tax acts. The key elements identified may be used to make the classification process of advertising as capital or revenue of nature more accurate and understandable. With the analysis and interpretation of the various income tax acts reviewed in this chapter, it is clear that there are many different approaches regarding the tax treatment of advertising cost. South Africa could, in a combined effort, use these approaches to improve the details regarding the classification of advertising for tax purposes. Using the information gathered and discussed in Chapter 4, the study is now able to move forward in attempting to solve the research problem posed in Chapter 1.

Chapter 5 includes literature that was reviewed relating to court cases which might have an impact on the classification of advertising cost. The aim of Chapter 5 was to achieve the objective set out in Chapter 1, regarding the determination of the classification of advertising cost as revenue or capital of nature. Achieving this objective resulted in the study being one step closer to solving the problem statement set out in Chapter 1.

CHAPTER 5
ANALYSIS AND INTERPRETATION OF SOUTH AFRICAN AND INTERNATIONAL CASE LAW REGARDING THE CLASSIFICATION OF ADVERTISING COST

5.1 INTRODUCTION

An analysis and interpretation of national and international income tax law was performed in Chapter 4 to determine the different ways that advertising cost is handled as an expense. In Chapter 3, a background of the role that advertising plays around the globe was also provided. Chapter 3 focussed on achieving the research objective set out in in Chapter 1 relating to the recognition of advertising as an asset or intangible asset. It was determined that for this study it would be assumed that advertising may be seen as an asset or an intangible asset. Chapter 4 contributed to solving the problem set out in chapter one by way of identifying aspects of national and international tax acts that relate to the treatment of advertising cost.

Chapter 5 will provide the analysis and interpretation of national and international court cases that are applicable to the classification process of advertising as capital or revenue of nature. The aim of Chapter 5 is to successfully analyse and interpret the said case law.

Maples (2006:2) points out that income tax is not simple and that its complexity can be attributed to the complicated manner in which tax acts are planned and composed. Due to the lack of detail in the Income Tax Act (58/1962) regarding the deduction and classification of advertising cost as established in Chapter 4, it is important to seek alternative ways to interpret The Act.

Guidelines were devised using the principles established in the analysed and interpreted case law. It is anticipated that the guidelines that are established at the end of this chapter will contribute to solving the problem posed in

Chapter 1, by way of assisting the process of classifying advertising as capital or revenue of nature. The research objective of this chapter was that of establishing guidelines for improved accuracy of the classification process of advertising cost as capital or revenue of nature. South African case law is discussed first, followed by the discussion of international case law.

5.2 SOUTH AFRICAN COURT CASES

The following paragraphs include the analysis and interpretation of principles that have been established in South African court cases. The principles discussed were used in the given classification process. The principles discussed also formed part of the guidelines suggested to ensure greater accuracy of the outcome of the classification process.

5.2.1 Capital and capital of nature

According to Williams (2011:167) one of the attributes of income that has been identified in judicial resolutions is that proceeds of a capital nature do not qualify as income in reference to the definition of gross income as stipulated in The Act. However, in the case of The Commissioner for the South African Revenue Services v George Forest Timber Company Ltd (1924) it was stated that the common economic denotation of the term capital and "capital of nature" should be used as guidance since capital cannot be defined, and that the statement "of a capital nature" is also not clarified. According to the Sub Nigel Ltd v The Commissioner for the South African Revenue Services (1948) any cost that is incurred with the aim being to obtain an income earning structure should be capital of nature since it will result in future economic benefits. It may also be noted in the Sub-Nigel Ltd v The Commissioner for the South African Revenue Services (1948) case that the meaning of capital is unclear and a fixed definition is absent. In this instance it is asserted that defining what is classified as expenditure of a non-capital nature is beyond the bounds of possibility. This definition would form a benchmark for all related cases, but it is, however, not feasible to attempt such a definition.

It may be assumed that the difficulty experienced in determining a definite definition for capital or capital of nature has a direct impact on advertising for

tax purposes since these definitions are the cornerstone of classifying advertising cost. It may further be reasoned that the wrongful classification thereof will influence the total tax payable or receivable at the end of a period.

5.2.2 Fixed and floating capital

The difference between fixed and floating capital was first described by Smith (1776:294). The *Oxford Dictionary* (2014:1) defines fixed capital as "capital invested in fixed assets" while the definition of floating or working capital is "The capital of a business which is used in its day-to-day trading operations, calculated as the current assets minus the current liabilities". Definitions found in the *Business Dictionary* (2014:1) of fixed capital and floating capital are respectively “capital that is employed in assets of durable nature for repeated use over a long period" and “the cash available for day-to-day operations of an organization".

The Commissioner for the South African Revenue Service v George Forest Timber Company Ltd (1924), sheds further light on fixed and floating capital by referring to floating capital as capital used in the production process whereas fixed capital is described as remaining static even though it generates substance. The relevance of the aforementioned difference is questionable, since fixed capital is also prone to replacement, such as the case of machinery used in a production process that becomes outdated or vehicles that become obsolete. It is evident from these cases, amongst others, that even after dividing the definition of capital into fixed capital and floating capital, there is still room for error when categorising expenditure under these two categories.

In order for a cost to be labelled as fixed capital or floating capital, it was established in Bourke’s Estate v The Commissioner for the South African Revenue Service (1991), that it will depend in fact or in law what the nature of trade of the entity in question is. Taking this principle into account it could be assumed that one of the factors that should be scrutinised when classifying advertising cost is the nature of the entity in question in order to ensure the correct classification thereof. Bourke's Estate v The Commissioner For The

South African Revenue Service (1991), further clarifies that the most important element for the qualification of an asset as fixed or floating capital is the nature of the trade in which the asset is employed.

The disqualification of capital expenditure according to section 11(a) of The Act, is related to fixed capital expenditure and not floating capital expenditure. Williams (2011:209) is of the opinion that fixed capital is everything related to the improvement, establishment or additions of the income earning machinery of an entity, while floating capital may be regarded as expenses that are an element of the costs related to the performance of income earning activities.

From the principles established in these cases it may be understood that there is not only one type of capital but rather two; this realisation should be applied when determining the nature of advertising cost. If one is able to establish whether advertising cost should be classified as fixed capital or floating capital, one obstacle is eliminated from the classification process.

New State Areas Ltd v The Commissioner For The South African Revenue Service (1645) points out that the nature of a transaction plays an important role when the classification should be made between capital and revenue of nature. It goes further, by adding that the motive behind the expense has importance in the case where there is an application for the acquisition of a fixed capital asset. The *Oxford Dictionary* defines a transaction and nature respectively as "an instance of buying or selling something" and "The basic or inherent features, character, or qualities of something". Therefore, understanding the exact nature of a transaction is important to avoid misunderstanding of what is involved in the nature of the transaction.

Expenses related to the acquisition of fixed capital are classified as capital even if these are not a fixed once-off payment but rather apportioned over a period as instalments (New State Areas Ltd v The Commissioner for the South African Revenue Service (1645). The New State Areas case also emphasised the fact that no distinction may be made between the expenditure related to fixed or floating capital in regard to the carrying on of a trade, which is one of the elements of the general deductions formula as per the Act. The

reason for this difficulty stems from both fixed capital and floating capital producing income for the entity. This case adopts the principle that for an expense to be seen as fixed capital, it has to bring about some form of improvement, addition or establishment of income earning plant or machinery, as opposed to floating capital being expenses incurred in the process of the income earning activities, as established in other cases, such as Bourke's Estate v The Commissioner For The South African Revenue Service (1991).

After it is determined that advertising cost is either fixed or floating capital, it should then be decided if the cost is closely related to the income earning activities of an entity or the income earning structure. The determination between fixed and floating capital consequently goes hand in hand with the differentiation between income earning activities and income earning structure. The importance of differentiating between costs related to income earning activities and costs related to income earning structure is discussed and analysed with reference to applicable case law.

5.2.3 Cost related to income earning activities

One of the requirements set out in the general deductions formula as per sections 11(a) and 23(g) of The Act is that the costs should be related to trade, consequently being part of the income producing or earning activities of an entity.

When examining South African case law as related to cost related to income earning activities, a prominent case in this regard is that of The Commissioner for the South African Revenue Service v African Oxygen Ltd (1963). This case indicates that expenses acquired that are incidental in relation to the activities which produce income will be of a revenue nature. The case further states that expenses related to the acquisition or creation of an income earning structure or a capital asset will be interpreted as capital of nature. If the indications that may be found in The Commissioner for the South African Revenue Services v African Oxygen Ltd (1963) case could and would be applied to the means of incurring advertising cost, this would assist the

classification process by ensuring that attention is given to the difference between income and earning activity and an income earning concern.

Principles established in different court cases should not be used against each other but rather with each other, like bricks in a wall, in order to support one another. Vallambrosa Rubber Co Ltd v Farmer (1910), found that for the classification of cost, it should be kept in mind that a once-off expense could be classified as capital cost while costs that are repeated annually, are of a revenue nature.

Provisions in the Act related to advertising have been identified; these may be found under the general deductions formula s 11(a) and s 23(g).

5.3 INTERNATIONAL COURT CASES

The following paragraphs include the analysis and interpretation of principles that have been established in international court cases. The principles discussed were used in the classification process of advertising as capital or revenue of nature.

The principles discussed also formed part of the guidelines suggested to ensure greater accuracy of the outcome of the classification process.

5.3.1 Capital versus revenue

According to Fullers Bay of Islands Ltd v The Commissioner of Inland Revenue (New Zealand: 2004) expenses which are linked to the acquisition of a capital asset, are not deductible for taxation purposes. In this case, the taxpayer argued that although the expense is linked to a capital asset, it should be regarded as an expense on its own, and not as capital of nature.

In the abovementioned case, the expense in question concerned legal fees that were incurred for the purpose of obtaining a contract that would bring about an enduring benefit for the company by way of income derived from ferry fees. It was thus further argued that the aim of the expense incurred was for the contract negotiations to be successful, in order to secure the contract that would have an inflow of income as a result. It was, however, stated in the

appeal by the taxpayer that the expense was not incurred to obtain a capital asset, since the asset in this case was the ferry itself as the ferry could be identified as the income producing asset.

The court was of the opinion that the expenses in relation to the legal fees could be seen as a set-up cost for the capital asset. This notion led to an indication that the cost is capital of nature since the contract would cause a new income stream into the business. A distinction was made between the business structure and the ordinary process of business. It appeared that the contract would result in regular income and it was therefore concluded that the contract, in its own capacity, would constitute a substantial addition to the structure of the business by way of the regular returns derived from ferry trips. The outcome of this case outlined the fact that the legal cost would in fact be of a capital nature after taking all aspects of the tax law into consideration. It also stipulated that a contract which is valid for more than 5 years might possibly be seen as capital of nature. It has been established in the Anglo Persian Oil Co Ltd v Dale (1931:219) that an enduring benefit is a benefit that endures in a way similar to fixed capital. Furthermore, it should not be regarded as an enduring benefit, if it only relieves the entity of a revenue payment. The Anglo case (1931:219) also state that an enduring benefit is not always a physical asset, it can be compared to getting rid of a lease or onerous capital.

If the principles established in these court cases are to be applied to advertising cost, it is arguable that a major advertising campaign that lasts for an extended period may be seen as capital of nature, since it will cause an inflow of income to the business and it may be regarded that it will have an enduring benefit as a result. It should also be considered that although the contract mentioned in the case of Fullers Bay of Islands Ltd v The Commissioner of Inland Revenue (New Zealand: 2004) was successfully entered and would cause an inflow of income into the business, the income is not reliably measurable at a specific amount. An advertising campaign aims to attract consumers to buy a product or make use of a service, which will most likely result in an inflow of income to the business in question; however the income that will be derived from the advertising campaign will not be reliably measurable. This is similar to the situation in the Fullers Bay of Islands Ltd v The Commissioner of Inland Revenue case (New Zealand: 2004). After taking the outcome of this case into

consideration it appeared as if advertising cost may, in certain circumstances, similarly to the legal fees dealt with in the case, be seen as capital of nature.

5.3.2 Periodical payments

If an expense is a once off payment, it is in most cases classified as capital of nature. However, costs in relation to fixed capital, as opposed to floating capital, would be regarded as capital of nature regardless of these not being a once-off payment. This principle was established in The Commissioner of Inland Revenue v Adam (United Kingdom: 1990), and also emphasises the fact that even if the cost of an asset is payable in instalments, the instalments would still be classified as capital of nature. Together with the application of the principles established in The Commissioner of Inland Revenue v Adam (United Kingdom: 1990) case on advertising cost, this led to the idea that although monthly payments are made by a company in order to keep an advertising campaign running, there was a possibility that such payments may be seen as capital of nature as opposed to revenue of nature.

5.3.3 Objective of the expense

The Tucker v Granada Motor Way Services Ltd case (United Kingdom: 1979) indicates that it is not only important to know for what the expense was incurred, but it is also of crucial importance to understand the objective of the expense. If the expense may directly be linked to a capital asset, it will also be classified as capital of nature. Lawson v Johnson Matthey (United Kingdom: 1982) emphasised that when an expense is classified as capital or revenue of nature, the most important factor to examine was not the purpose of the expense but rather the effect of the expense. If advertising cost is taken into consideration together with this principle, it becomes evident that the effect of the cost incurred should be determined before the classification of advertising as capital or revenue can take place.

5.3.4 Expenditure related to intangibles

With reference to the conclusion reached in Chapter 3, it was assumed that advertising cost may be classified as an intangible asset in certain cases.

When a business expense is incurred, the aim is to generate an inflow of benefits to the entity.

In the case where business expenses are related to an intangible item, it is very important to determine whether the intangible item has an enduring benefit. If the expense is of such a nature that it has an enduring benefit that will cause an inflow of benefits to the entity, it will be classified as capital of nature. This principle has been established in numerous court cases such as Heather v P E Consulting Group Ltd (United Kingdom: 1972), Anglo-Persian Oil Company Ltd v Dale (Australia: 1931) and The Commissioner of Inland Revenue v Carron Company (Australia: 1931). The following paragraph consists of a summary of the principles established from the case law that has been examined.

5.4 SUMMARY OF PRINCIPLES ESTABLISHED IN COURT CASES

Table 5-1 is a comparison of the South African court cases that were interpreted and include the issue that was dealt with in the case, the outcome of the case and the principle established in the case that is used as a guideline for modern tax.

Table 5-1: Comparison and analysis of South African case law

Issue	Case	Outcome	Principle
Capital and capital of nature	The Commissioner For The South African Revenue Services v George Forest Timber Company Ltd (1924).	Capital cannot be defined and "of a capital nature" is not clear.	Capital and "of a capital nature" should only be used as guidance and not as a definite outcome.

Table 5-1: Comparison and analysis of South African case law (continued)

Issue	Case	Outcome	Principle
Capital and Capital of nature	Sub-Nigel Ltd v The Commissioner For The South African Revenue Services (1948). Vallambrosa Rubber Co Ltd v Farmer (1910).	A fixed definition of capital is absent.	It is unachievable to attempt a fixed definition for capital.
Fixed and floating capital	The Commissioner For The South African Revenue Services v George Forest Timber Company Ltd (1924).	Fixed capital is described as remaining complete while floating capital is seen as capital used in the production process.	Fixed capital can also be prone to replacement thus questioning the difference between fixed and floating capital.
Fixed or floating capital	Bourke's Estate v The Commissioner For The South African Revenue Services (1991).	The determination between fixed and floating capital should be based on the type of trade.	Fixed and floating capital can be identified only in relation to the nature of trade that the asset is used for.
Fixed or floating capital	New State Areas Ltd v The Commissioner For The South African Revenue Services (1645).	The type of transaction plays a role in the classification between capital and revenue of nature.	The type of transaction should be taken into account to determine if it is for the purpose of fixed or floating capital.

Table 5-1: Comparison and analysis of South African case law (continued)

Issue	Case	Outcome	Principle
Cost related to income earning activities	The Commissioner For The South African Revenue Services v African Oxygen Ltd (1963).	Expenses acquired that are incidental to income earning activities will be of a revenue nature, while expenses related to an income earning concern will be of a capital nature.	The difference between income earning activity and income earning concern needs to be certain before classification can take place.
Once off payments	Vallambrossa Rubber Co Ltd v Farmer (1910).	Expenditure that occurred only once may be seen as capital expenditure.	Cost that is repeated will be seen as revenue of nature and cost that occurs once off may be seen as capital of nature.

Source: Own research

Table 5-2 illustrates the principles that were identified after analysing and interpreting international case law that could be used for the classification process of advertising as capital or revenue of nature.

Table 5-2: Principles established in international case law

Reason for court case	Case	Principles
Capital versus revenue	Fullers Bay of islands Ltd v Commissioner of Inland Revenue (2004).	Contracts for a period of 5 or more years is usually capital of nature It should be determined if the expense incurred will cause a substantial inflow of benefits into the company, if so it will be capital of nature
Periodical payments	Commissioner of Inland Revenue v Adam (1990).	Costs related to fixed capital will be seen as capital of nature even if it is not a once off payment
Objective of the expense	Tucker v Granada Motor Way Services Ltd & Lawson v Johnson Matthey plc (1979).	It is not only important to know for what the expense has been occurred but it is also important to understand the objective and effect of the expense
Expenditure related to intangibles	Heather v P E Consulting Group Ltd (1972) & Anglo- Persian Oil Company Ltd v Dale (1931) & The Commissioner of Inland Revenue v Carron Company (1931).	It is important to determine if the intangible item has an enduring benefit
Enduring benefit	Anglo- Persian Oil Company Ltd v Dale (1931).	An enduring benefit should be compared to fixed capital

Source: Own research

The principles that could be established from the discussion of national and international court cases in paragraph 5.2 and 5.3 are summarised in Tables 5-1 and 5-2. Paragraph 5.5 presents the conclusion of Chapter 5.

5.5 CONCLUSION

Using South African case law and the principles established in these cases, it was possible to secure some guidelines to use for the purpose of the classification of advertising cost as capital or revenue of nature. This contributed to the study by solving one of the research objectives: determining guidelines for the classification process as set out in Chapter 1. These are as follows:

1. Capital and the reference "capital of nature" should not be used as a definite outcome but as guidance for the purpose of classifying advertising cost as capital of nature or revenue of nature

2. The terms fixed and floating capital should be used with reference to the nature of the trade in which such an asset is employed before an expense can be classified as fixed or floating capital

3. The nature of the transaction should be taken into account in order to determine if it should be treated as fixed or floating capital. After this distinction is made it will be possible to continue with the classification process of advertising cost as capital or revenue of nature

4. The difference between an income earning activity and an income earning structure should be taken into account before advertising cost can be classified as capital or revenue of nature

5. Costs incurred once-off may be seen as capital of nature, while costs that are recurrent may be seen as revenue of nature. This principle may be used in order to establish whether the advertising cost in question should be classified as capital or revenue of nature.

6. An enduring benefit should be regarded as a benefit that endures in the same way that fixed capital endures. If advertising can be established as an enduring benefit it will be possible to classify it as capital of nature.

More guidelines may be established by using principles established in international court cases as summarised in Table 5-2. These follow:

1. The duration of the period which the advertisement or advertising campaign lasts or may be useful for the entity should be taken into consideration when determining if the item is capital or revenue of nature.

2. If possible, a determination should be made regarding the amount of benefits that the advertisement or advertising campaign will have as a result.

3. The cost related to the advertisement or advertising campaign does not have to be a once-off payment in order for it to qualify as an asset.

4. It is of vital importance to understand the reason and aim of the expense that has been incurred for the purpose of advertising. It should be determined exactly why the advertisement came into being and what the entity intends to achieve by the advertisement or advertising campaign.

The guidelines should be and were used together and not as individual items in order to make the classification as accurate as possible. The nine guidelines that were identified from the applicable case law were used as the study progressed in order to assist in the classification process.

One crucial research objective achieved in this chapter was the setting of guidelines that may be used in order to make the classification process of advertising as capital or revenue of nature easier, resulting in more accurate classification.

Chapter 6 focuses on the role that advertising plays in the South African economy by shedding light on the growth of advertising revenue of companies listed on the JSE and trading in the media, entertainment and broadcasting markets.

CHAPTER 6
ANALYSIS AND INTERPRETATION OF ANNUAL FINANCIAL RECORDS OF JSE LISTED COMPANIES

6.1 INTRODUCTION

The conclusion reached in Chapter 3 is that advertising may be classified as an asset or an intangible asset for accounting purposes. Chapter 4 found that there are various methods that are followed for the treatment of advertising cost for tax purposes in the different tax acts of countries around the world. Advertising cost may be classified as capital or revenue of nature. Depending upon the specific circumstances of the transaction, the guidelines established in Chapter 5 should be used to accurately determine the nature of the specific transaction in question.

The fact that advertising may be recognised as an asset or intangible asset for accounting purposes as established in Chapter 3, together with the tax treatment of advertising cost as found in Chapter 4, should be used and combined with the principles set out in Chapter 5. The information from these three chapters should be combined and used together as a whole instead of separately. Through a combination of the accounting treatment, tax treatment and the principles set out, a more accurate outcome will be achieved when determining the nature of advertising cost.

As indicate, advertising cost may be ascertained as capital or revenue of nature, according to the principles established from national and international court cases in Chapter 5. The five guidelines established in Chapter 5 are illustrated in Table 5-1. These may be used when determining how advertising cost can be classified. However, as pointed out above, these guidelines should not be used in isolation when making this decision.

Chapter 6 consists of one main section that may be identified as the indirect impact of advertising revenue on the South African economy in order to

determine the role that advertising plays in this economy. It was necessary to analyse data collected from companies listed on the JSE that trades in the media, entertainment and broadcasting markets to determine the importance of the role of advertising in the South African economy.

The purpose of this chapter was to establish the role of advertising in the South African economy and its results were used to highlight the importance of understanding the classification of advertising for tax purposes. If one is able to establish the existence of a growing trend in revenues derived from advertising, this would contribute to the understanding of the growing importance of advertising in South Africa.

The aim of this chapter was to achieve the research objective set out in Chapter 1. The findings in Chapter 6 may be used in conjunction with the guidelines established in Chapters 3, 4 and 5. The results of Chapter 6 were used to support the importance of classifying advertising into capital or revenue of nature. The combinations of the other chapter's results offer a more accurate approach to determining the classification of advertising cost as capital or revenue of nature. The financial statements of JSE listed companies were scrutinised for line items that are closely related to revenues generated from advertising and the growth of such revenues over the last three financial years: 2011, 2013 and 2014.

Four companies, as listed on the JSE, were chosen for these research purposes:

- African Media Entertainment Limited
- Hosken Consolidated Investments Limited
- Kagiso Media Limited
- Naspers Limited.

The reason these four companies were selected was that:

- They trade in the media, entertainment and broadcasting markets
- the analysis of the financial reports could focus on income derived from these companies' advertising activities.

To this end:

- the financial statements of each of the four companies were analysed in isolation to determine the trends in advertising revenue in the specific company
- thereafter, the results of the analysis of each individual company were compared and combined
- the said combination and comparison of the results helped to form a conclusion to the financial situation of the advertising market in South Africa.

The analysis of the annual financial records was carried out in order to emphasise the point made in Chapter 3 regarding the importance of advertising in South Africa and the role that advertising is playing in the economy of South Africa. As mentioned in paragraph 3.4, the advertising market is revealing a growing trend and the goal of the analysis of the annual reports (with the focus on line items relating to advertising cost) is to demonstrate this. The findings in Chapter 6 were intended to do so, with the ultimate aim of strengthening the importance of classifying advertising cost correctly for tax purposes.

6.2 AFRICAN MEDIA ENTERTAINMENT LIMITED (AME)

To determine if there is a growth in the annual advertising revenue derived from advertising activities by AME, line items in the annual financial reports that are closely related to advertising revenue were analysed and interpreted.

6.2.1 Company overview: AME

AME focuses on radio broadcasting and using radio as a tool for advertising (African Media Entertainment, 2014:1). It is a JSE listed company which trades in the media and entertainment sector. The group structure is illustrated in Diagram 5-1. The companies in which AME has holdings, do not trade on the JSE. The group consists of two main divisions: radio sales and radio broadcasters. These are illustrated in Diagram 5-1 to offer insight in understanding the scope of the company's business.

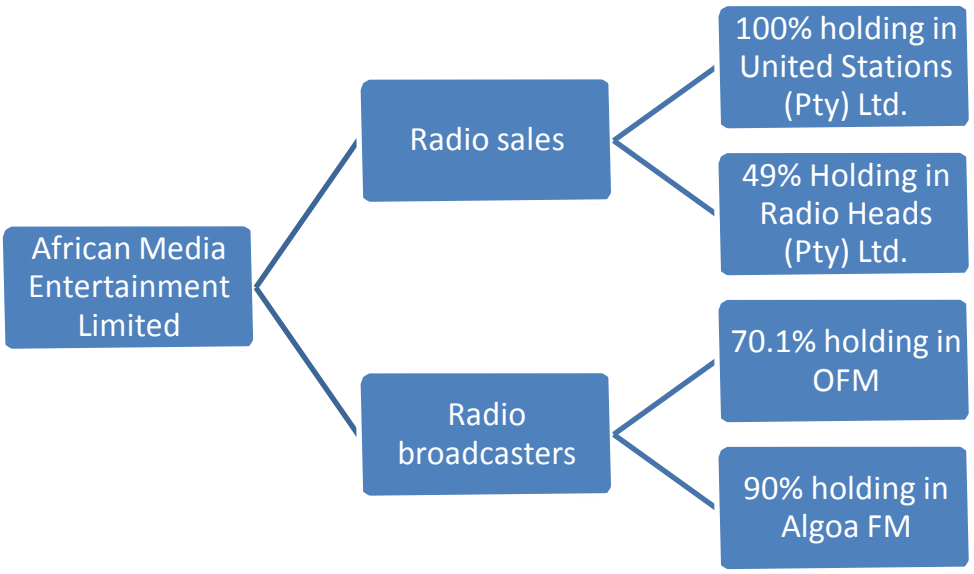


Diagram 6-1: Business structure of AME

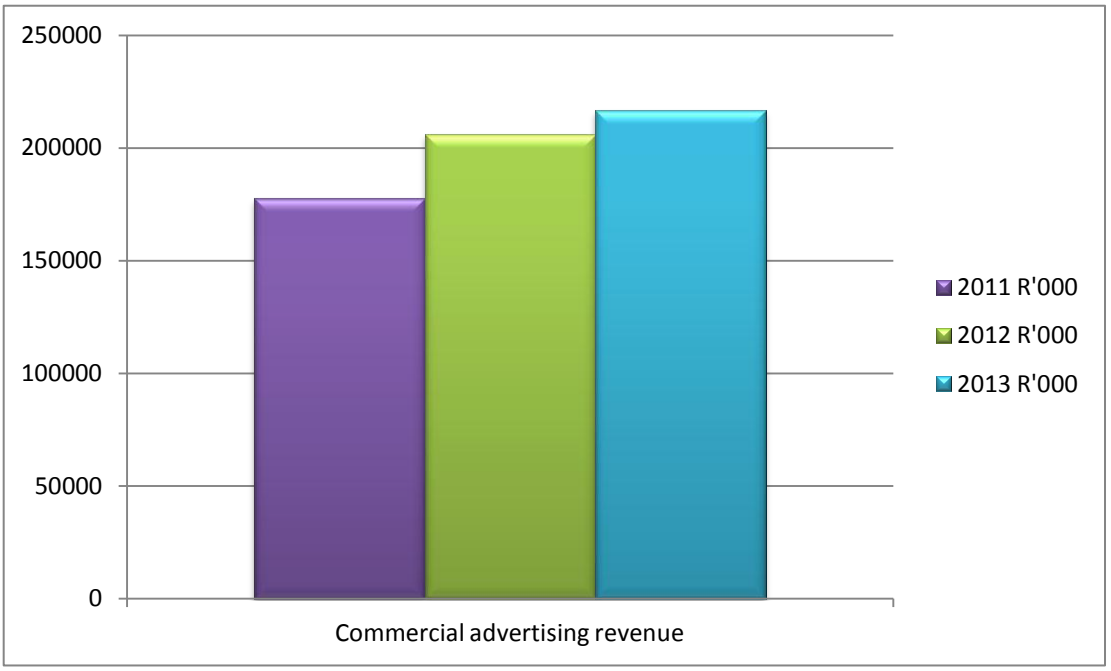
Source: AME Annual financial report (2012:2)

AME has shareholdings in radio sales and radio broadcasters. These companies include:

- OFM
- Algoa FM
- United Stations (Pty) Ltd
- Radio Heads (Pty) Ltd.

6.2.2 Analysis and interpretation of AME annual financial reports

AME (paragraph 6.3 refers) recognises revenue received from commercial advertising according to when the advertising material is aired. Graph 6-1 is used to indicate the trends in revenue derived from commercial advertising revenue over the past three financial periods, from 2011 to 2013.



Graph 6-1: Commercial advertising revenue

Source: AME annual financial report (2011:37) (2012:38) (2013:39)

From Graph 6-1 it may be observed that the revenue generated by commercial advertising has demonstrated a growing tendency over the past three financial periods. The reasons behind the growth of commercial advertising during 2011 could be that the escalation of revenue from OFM's advertising was due to the use of better digital technology and other radio promotions (AME annual financial report, 2011). The increase in commercial advertising could further have been caused by KAYA FM's sales recently being taken over by United Stations, in which AME has a 100% shareholding, as indicated in Diagram 6-1. According to information gathered in the annual financial reports (2011) KAYA FM plays a significant role in the business development of AME.

A growth in advertising platforms during 2011 affords an indication of more advertising opportunities and resources, in effect causing a further increase in commercial advertising revenues. United Stations was able to increase its resource base because of this increased revenue. There is an opportunity for United Stations to enlarge its capacity in the upcoming financial periods for this reason.

The increase in revenue generated from advertising for 2012 is mostly attributable to the growth in digital advertising from OFM (AME has a 70.1% shareholding as illustrated in Diagram 6-1). It is indicated in the annual financial report (2012) that United Stations performed extremely well, causing it to achieve better results than the rest of the market and generating high revenues.

Digital advertising continued to indicate a steady growth rate during 2013, according to the directors' report (Annual Financial Report, 2013). The performance of United Stations caused them to bring in higher revenues than originally anticipated. AME is of the opinion that the combination of brand specific advertising and the exceptional revenues brought in by United Stations ensured that AME revealed a growing trend in commercial advertising in 2013.

Revenues generated by this activity revealed a growth of 16.18% from the 2011 financial period to the end of the 2012 financial period. In the 2013 financial period the trend surpassed the 2012 figure by an increase of 5.15%.

6.3 HOSKEN CONSOLIDATED INVESTMENTS LIMITED (HOSKEN)

In this paragraph, the research focuses on the overview of Hosken, as well as the analysis and interpretation of the annual financial reports for the financial periods of 2011, 2012 and 2013. This portion of the study aimed to determine, by analysing the annual financial reports, if a growth in advertising revenue could be demonstrated.

6.3.1 Company overview – Hosken

According to Forbes (2012:1) Hosken was founded in 1973. In a nutshell, it is an investment company that focuses on the importance of black empowerment in South Africa. It is listed on the JSE and trades in the media and entertainment markets.

The investments that the company holds relates to various sectors such as:

- interactive gaming
- hotels and leisure
- media and broadcasting
- mining
- clothing
- transport
- properties.

The business segments of which Hosken comprises, according to the official website of Hosken (2013:1), are:

- Gaming, hotels and leisure
- Media and broadcasting
- Transport
- Diversified investments
- Energy
- Property and exhibitions
- Food and beverages
- Industrial
- Services and technology.

The group structure of Hosken Consolidated Investment is illustrated in Diagram 6-2. The group structure is divided into two portions: the listed and the unlisted companies. The focus of the study was solely on the listed companies; therefore Diagram 6-2 shows just the listed companies. Diagram 6-2 is used to illustrate the companies in which Hosken has holdings.

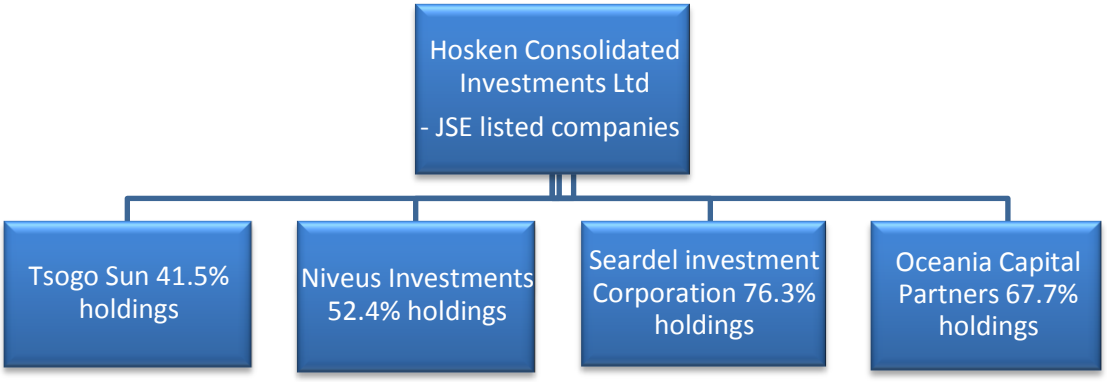


Diagram 6-2: Group structure listed companies Source: Hosken annual financial report (2013)

Diagram 6-2 indicates that Hosken holds shares in 4 JSE listed companies:

- Tsogo Su,
- Niveus
- Seardel
- Oceania.

Other companies that have not been included in Diagram 6-2 due to the fact that they are not listed on the JSE but that still form part of the Hosken group are:

- Sabido investments (63% holding)
- Golden Arrow Bus Services (100% holding)
- HCI Coal (100% holding)
- HCI Properties (100% holding)
- Montauk Energy Holdings (90% holding)
- Syntell (55% holding).

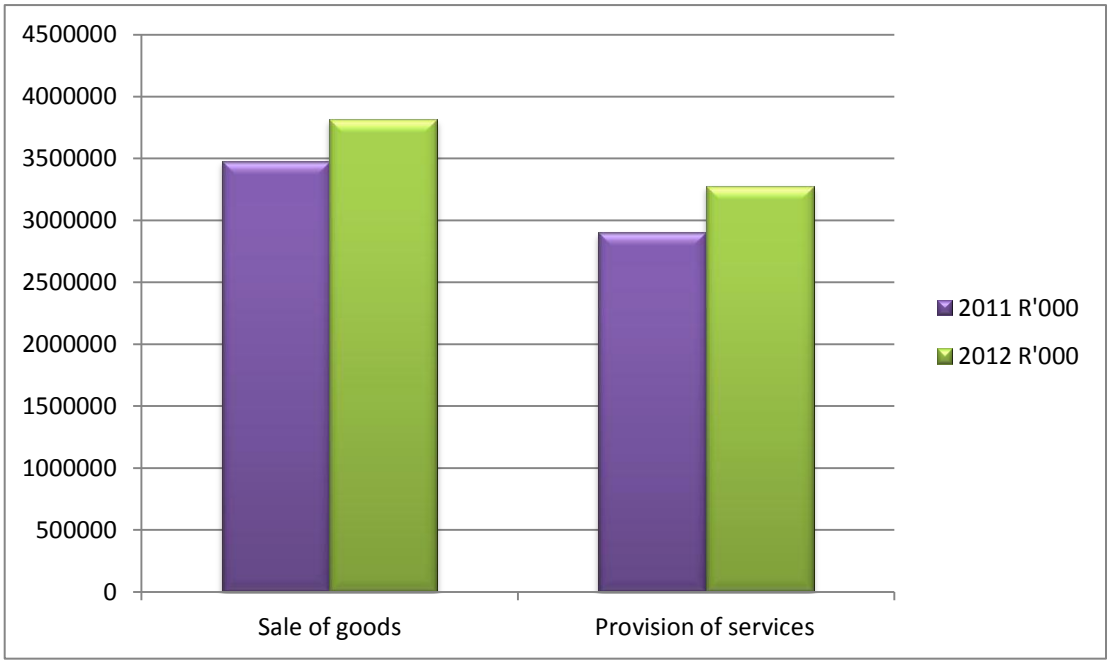
Hosken has revealed significant increases in headline earnings because of increased revenue from the broadcasting and publishing segments of this group (Benjamin, 2012:1).

Hasenfuss (2012:1) also refers to the reason for increased headline earnings by Hosken being due to revenue growth from advertising and subscriptions. In

the following paragraphs, the revenue derived from advertising that Benjamin (2012:1) refers to is discussed.

6.3.2 Analysis and interpretation of annual financial reports: Hosken

Hosken recognises revenue from television and radio advertising over the period of either the start of the contract and over the period consisting of the rest of the contract. The financial records of Hosken do not show revenue received from advertising as an individual line item in the statement of profit or loss and other comprehensive income. Revenue received by Hosken is measured at fair value, indicating that advertising revenue will also be measured in this manner.



Graph 6-2: Revenue growth from 2011 to 2013 derived from sale of goods and services rendered

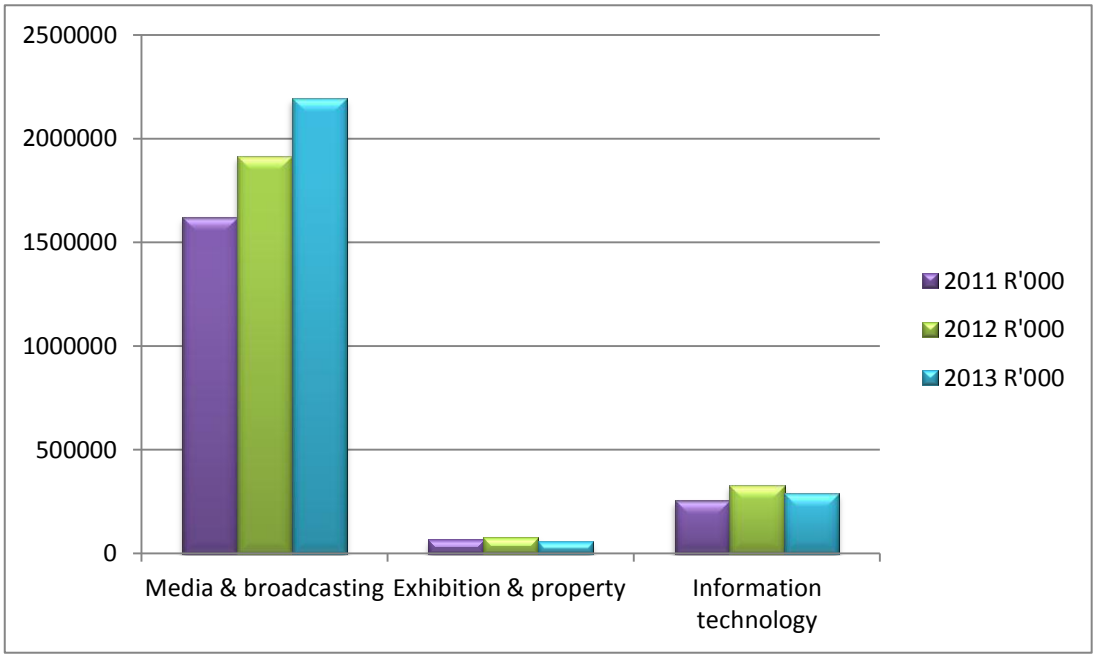
Source: Hosken Annual Financial Report (2011:52) (2012:65)

Revenue generated from the sale of goods and the provision of services are not itemised as separate entries in the Annual Financial Report of 2013, but rather as one consolidated total of revenue: in other words, the data do not specifically classify advertising revenue as an individual line item. If the total revenue from goods sold or services rendered was to be used in isolation as a deciding factor of whether advertising revenue shows a growing tendency, it

might be inaccurate. The data could therefore not be used to complete the analysis of Hosken's Annual Financial Reports, since it would have differed from the analysis done in this chapter on the other three JSE listed companies.

The company indicated an increase in revenue received from the sale of goods from 2011 to 2012 as indicated in Graph 6-2; however, it is not stipulated what part of this revenue is attributable to advertising. It was therefore necessary to make a closer examination of the company's Annual Financial Report and to focus on the different sources of revenue that may be linked to advertising.

Graph 6-3 indicates the different sources of revenue that may be linked to advertising. The period in which the data illustrated in Graph 6-3 were collected from the Annual Financial Reports of the 2011, 2012 and 2013 financial periods. The three sources that were measured in Graph 6-3 are: media and broadcasting, exhibition and property and information technology.



Graph 6-3: Revenue generated from media and broadcasting, exhibition and property and information technology

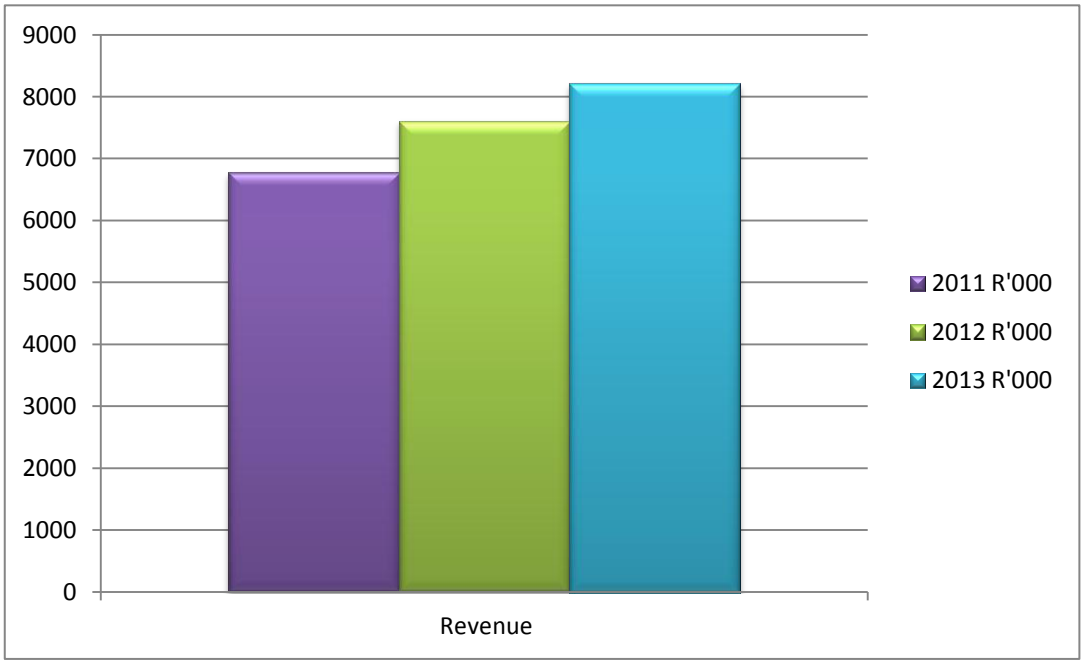
Source: Hosken Annual Financial Report (2011:58) (2012:80) (2013:79)

Revenue received from media and broadcasting was clearly the most important source of revenue as indicated in Graph 6-3. An outstanding growth in revenue from 2012 to 2013 was notable. This was mainly due to an increase in revenue generated from media and broadcasting as well as subscription revenue growth of 15%. Media and broadcasting indicated a growth of 18.18% from 2011 to 2012 and demonstrated a further growth of 14.55% from 2012 to 2013 as shown in Graph 6-3.

The total revenue consists of income received from:

- sale of goods
- revenue received from services
- revenue collected from advertising activities.

The total revenue of the 2011, 2012 and 2013 financial periods is shown in Graph 6-4. Revenue from advertising is included in the total revenue since there was no separate indication for advertising in the annual financial records of the company.



Graph 6-4: Group revenue growth

Source: Hosken Annual Financial Report (2011:54) (2012:80) (2013:79)

An indication of a strong, growing trend in media and broadcasting is demonstrated in Graph 6-4. Graph 6-4 also indicates that their growth was responsible for the production of major revenues for the company. If the revenue derived from media and entertainment was compared to the revenue derived from exhibition and property and information technology, it would be clear that a large portion of Hosken's total revenue is attributable to the media and broadcasting section.

The total revenue of Hosken increased by 12.20% from the 2011 financial period to the 2012 financial period and revealed an increase of 7.90% from 2012 to 2013. These increases are also indicated in Graph 6-4.

6.4 KAGISO MEDIA LTD (KAGISO)

An overview of Kagiso, which includes the group structure of the company, follows. Its Annual Financial Report for the financial periods of 2011, 2012 and 2013 was analysed and interpreted with the focus on revenue collected as a result of advertising activities.

6.4.1 Company overview: Kagiso

- Kagiso functions in four segments and specialises in radio and television broadcasting (Kagiso Official Website, 2014:1). The four segments of which the business consists, are:
- Broadcasting
- Content
- Information
- New media.

The group structure of Kagiso's broadcasting segment is illustrated in Diagram 6-3. In the broadcasting segment, two main divisions, radio and television, are indicated. Diagram 6-3 illustrates the two divisions and the various holdings that Kagiso Media has in both the television and radio broadcasting industries. Information collected from the official site of Kagiso Media Limited (2014:1) was used to determine the group structure of the

company. The structure illustrated in Diagram 6-3 is merely an illustration of the broadcasting segment. The other segments are easily separable and have therefore been omitted.

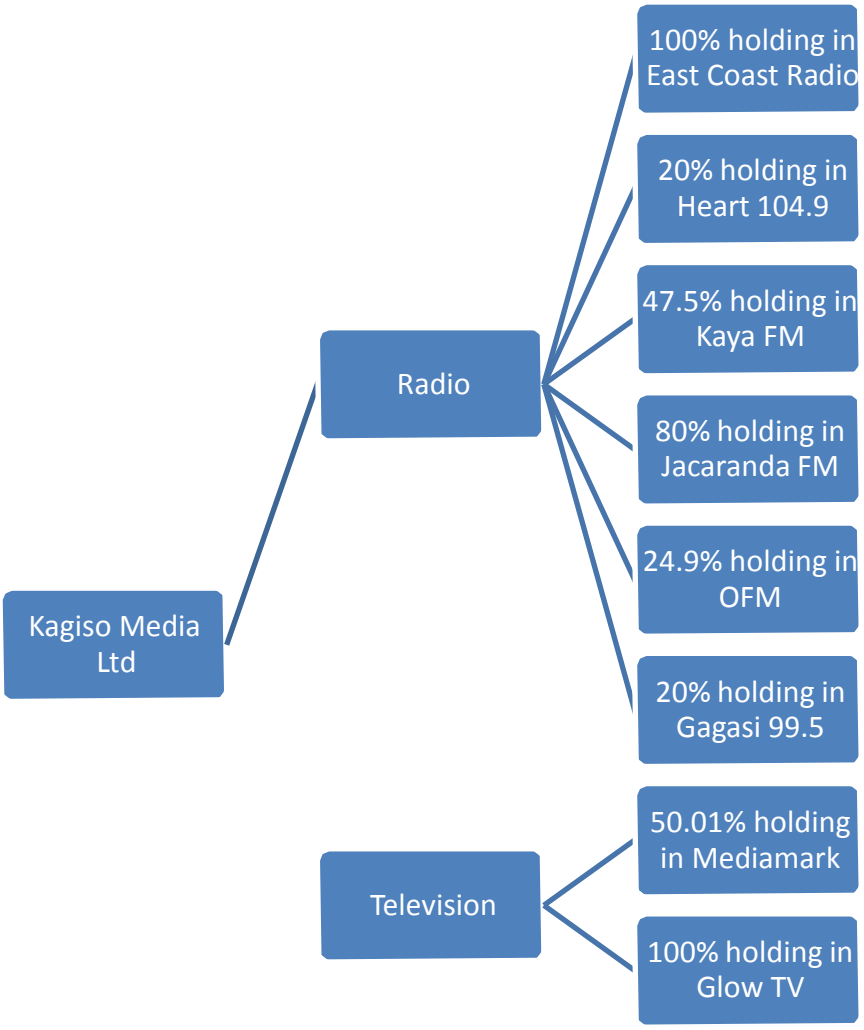


Diagram 6-3: Kagiso Broadcasting group structure

Source: Own research

Diagram 6-3 makes it clear that Kagiso has holdings in many radio stations around South Africa. The stations in which Kagiso holds more than 50% are East Coast Radio and Jacaranda FM. Kagiso media is the sole holder of Glow TV and holds 50.01% of Mediamark.

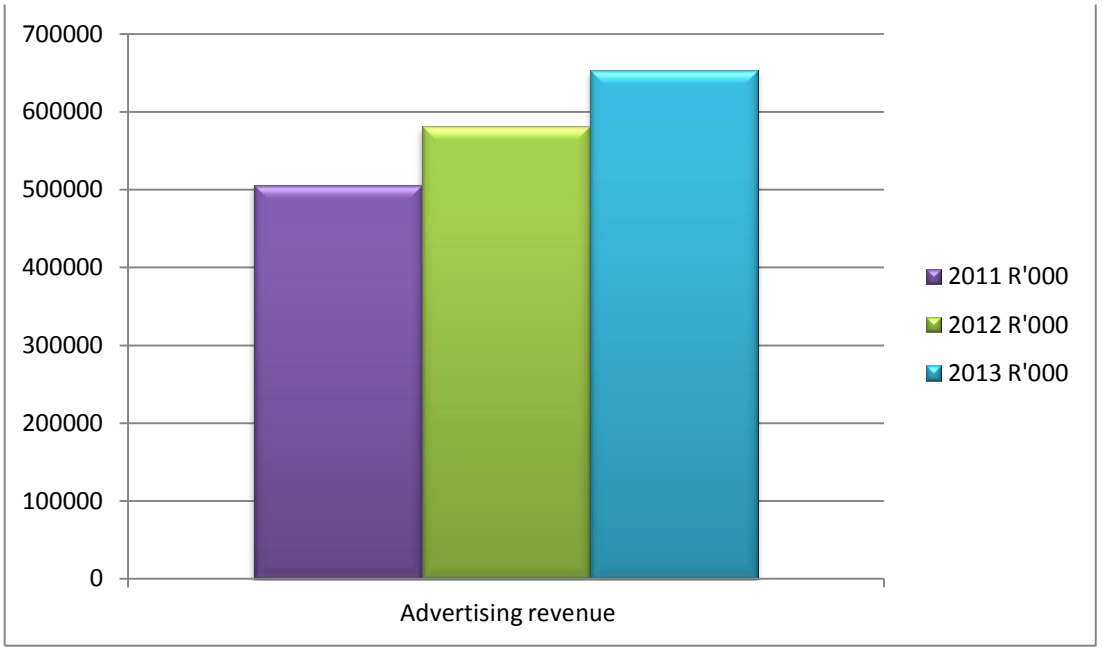
The annual financial records of Kagiso will be analysed in the following paragraph in order to determine if there is a growing tendency in terms of advertising revenue generated by the company. The focus of the analysis of

the financial records will be on line items that are in relation to advertising revenue.

6.4.2 Analysis and interpretation of annual financial records: Kagiso

Kagiso recognises revenue generated by the sale of radio airtime as soon as the advertising material is actually broadcast. Revenue collected from annual subscriptions, from the group's specialist publishing products which includes outdoor advertising contracts, is recognised over the period stipulated by the subscription contract.

The annual financial records of Kagiso indicate revenue generated from advertising activities as a separate line item. Graph 6-5 illustrates the growth of revenue collected from advertising for the 2011, 2012 and 2013 financial periods. The Graph was drawn from data collected from the Annual Financial Reports of Kagiso.

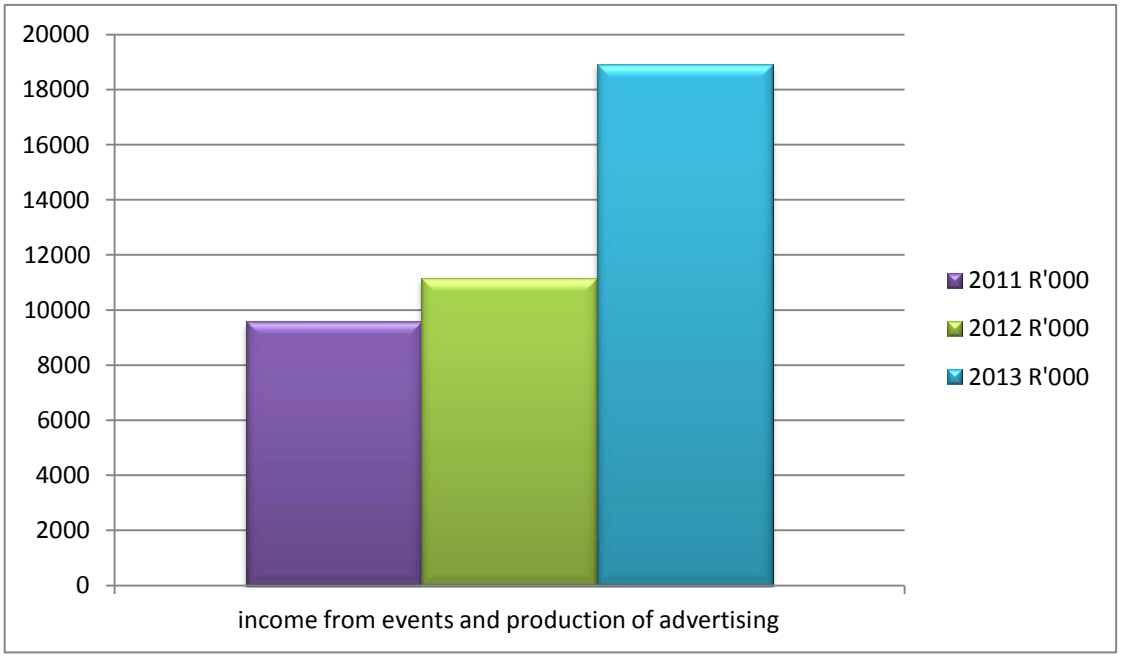


Graph 6-5: Advertising revenue of Kagiso

Source: Kagiso Annual Financial Report (2011:117) (2012:101) (2013:97)

Graph 6-5 indicated revenue generated by advertising. This has grown by 14.72% from the 2011 financial period to the 2012 financial period while a further growth of 12.47% was calculated from the data given in Graph 6-5.

The annual financial records of Kagiso also account for income derived from events and production of advertisements, illustrated in Graph 6-6. Graph 6-6 was drawn up with data collected from the Annual Financial Records for the financial periods of 2011, 2012 and 2013.



Graph 6-6: Income of Kagiso from events and production of advertising

Source: Kagiso Annual Financial Report (2011:117) (2012:101) (2013:97)

Income received from events and production of advertisements as illustrated in Graph 6-6 indicated a growth spurt from 2012 to 2013. The income from events and production increased from 2011 to 2012 by 16, 53% and continued to evidence a growing trend, resulting in an exceptional increase of 69, 34% from 2012 to 2013.

Graph 6-6 visually illustrates these factors. There was a dramatic growth spurt in 2013, but no specific reason for this event was recorded (Kagiso Annual Financial Report: 2013).

6.5 NASPERS LIMITED (NASPERS)

The focal points of paragraph 6.5 are the analysis and interpretation of the annual financial records of Naspers as well as an overview of the company. The analysis and interpretation of the annual financial records of Naspers were expected to shed light on the income stream from their advertising and the growth over the past three financial periods: 2011, 2012 and 2013. The overview of the company provides the group structure of Naspers.

6.5.1 Company overview: Naspers

According to the Naspers Official website (2014:1) it is currently part of the top 10 listed companies trading on the JSE. The company only listed on the JSE in 1994, 79 years after it was first established in 1915, in Cape Town (Naspers Official Website, 2014). Naspers is also listed on the London Stock Exchange (LSE).

The primary functions of Naspers are located in the following markets:

- Internet services, focusing on ecommerce
- Pay television
- Print media
- Technology.

Naspers has not only South African shareholdings but also international ones; however, only the South African group structure of Naspers is illustrated in Diagram 6-4. The Naspers group structure is divided into four categories: print, internet, pay TV and technology, as illustrated in Diagram 6-4.

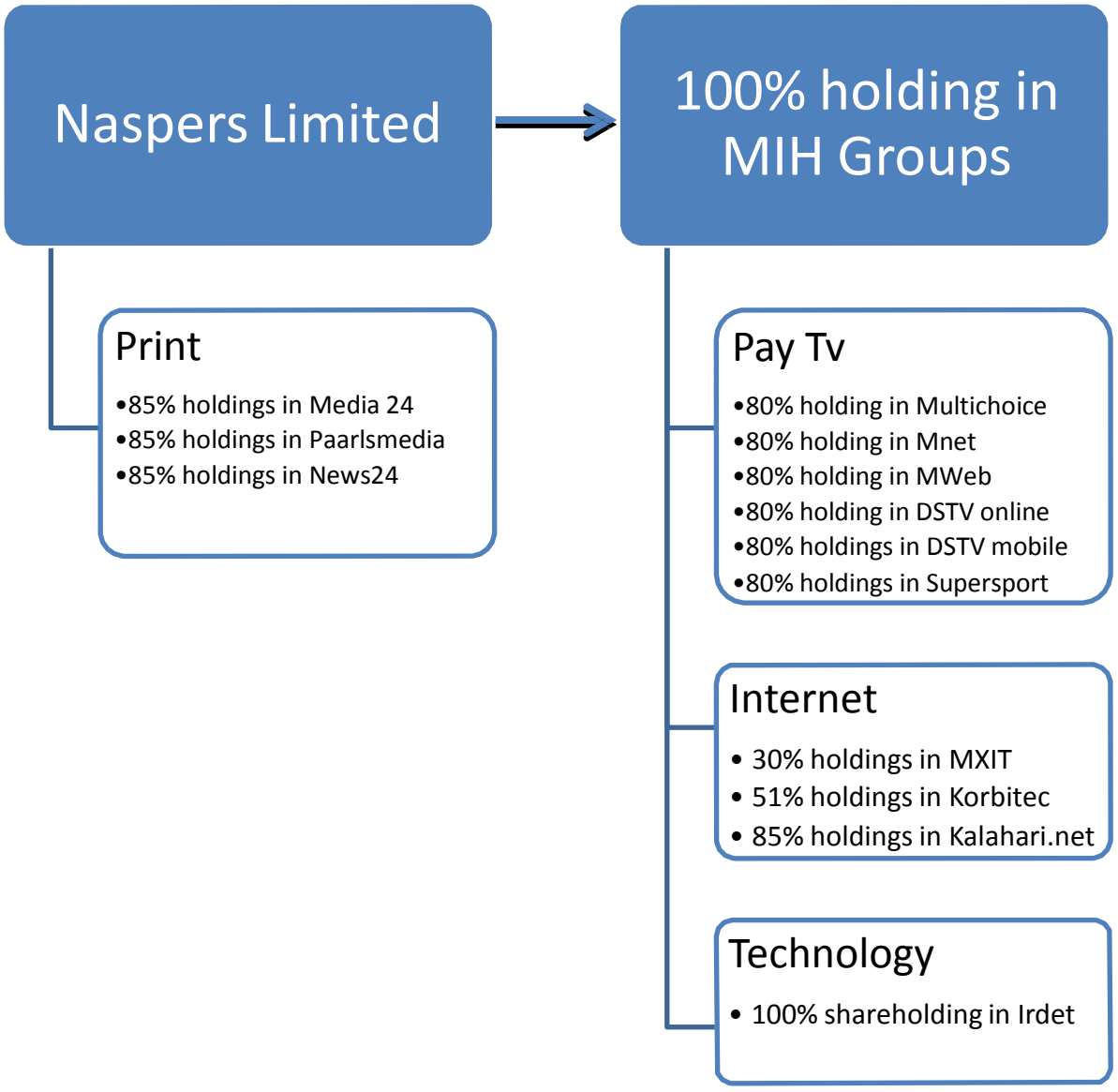


Diagram 6-4: Naspers group structure

Source: Naspers Official Website (2014:1)

Diagram 6-4 indicates that Naspers has 100% shareholding in:

- The MIH
- Irdet,

Naspers also has 85% shareholding in:

- Media 24
- News 24

- Paarlmedia
- Kalahari.net.

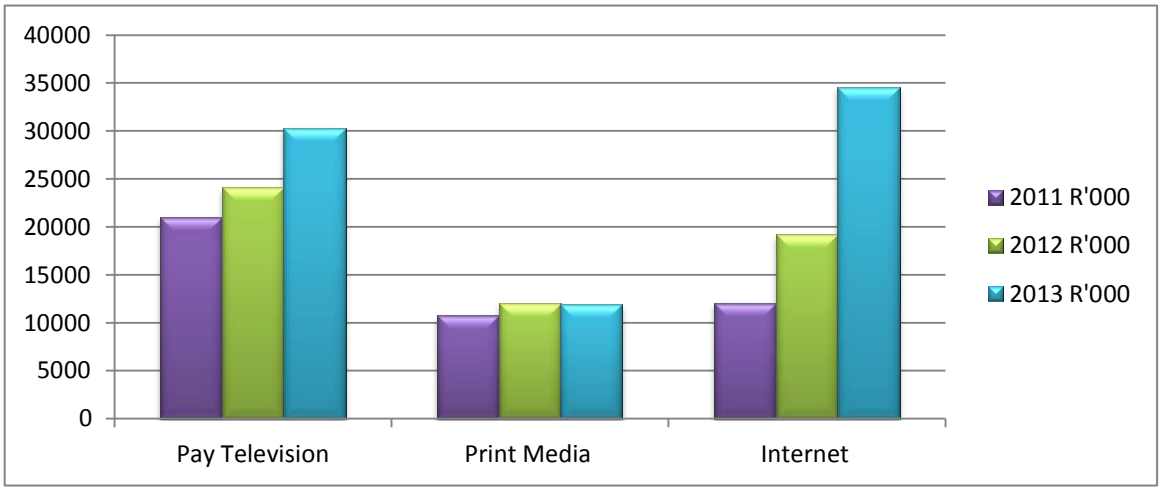
Naspers has 80% shareholding in:

- MultiChoice
- MNet
- MWeb
- DSTV online
- DSTV mobile
- SuperSport.

Thirty percent (30%) of Mixit is held by Naspers, as is 51% of Korbitec.

6.5.2 Analysis and interpretation of annual financial records of Naspers

Graph 6-7 depicts the trends in revenues of Naspers from pay TV, print media and Internet. The data used in Graph 6-7 was referenced from the data accumulated from its Annual Financial Records for the 2011, 2012 and 2013 financial periods.



Graph 6-7: Revenues of Naspers from pay TV, print media and internet

Source: Naspers Annual Financial Report (2011:137) (2012:132) (2013:128)

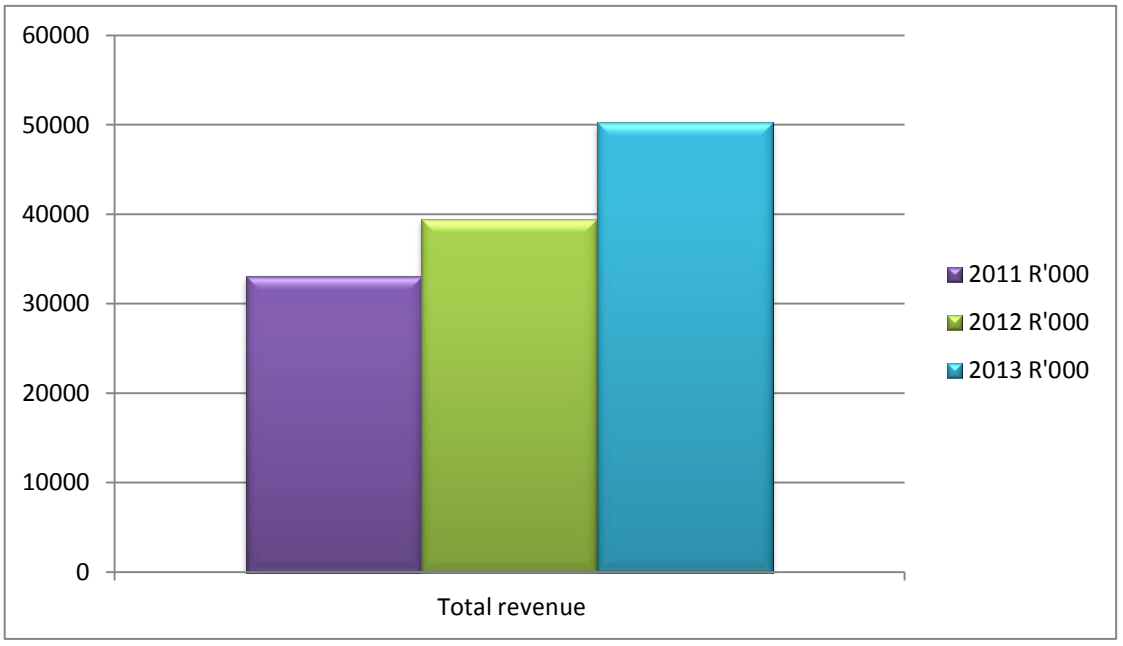
Naspers recorded a slow growth in revenue derived from advertising in the 2011 financial period, while pay TV indicated a growth rate of 32% in the same financial period (Annual Financial Records, 2011). Naspers's Annual Financial Report (2011) indicated a growth in advertising. Revenue from internet and technology advertising increased substantially, while revenues from print media improved just slightly (Annual Financial Records, 2011).

During the 2012 financial period, revenues generated from advertising activities continued to display a growing trend despite advertising in print media being strained (Annual Financial Reports, 2012). This correlates with Graph 6-7 where it may be observed that the internet segment of Naspers is the segment with highest growth rate in the 2012 financial period; however, pay TV remained the segment generating the highest returns. Pay television showed a growth of 14, 59% during the 2011 to 2012 financial period, while print media showed an increase of 12, 20% for the same period and the internet segment indicated impressive growth of 58,7% from 2011 to 2012.

According to the Annual Financial Report (2013) there was an increase in revenue from ecommerce. The reason for the increase was the expansion of ecommerce during that financial period. As illustrated in Graph 6-7, it is clear that the segment which brought the most revenue into the company was the internet segment. It is evident in Graph 6-7 that revenues from the internet segment exceeded revenues derived from pay TV. The Annual Financial Records (2013) of Naspers also state that this occurrence is the first in the history of the company. Print media had a slight decline in revenues as may be observed in Graph 6-7; the Naspers' Annual Financial Records (2013) links this to their clients' cut in advertising budgets.

The internet revenue growth could be partially attributed to the increased revenues derived from Kalahari.net as a result of new product lines that were launched by the site during the 2011 financial period (Annual Financial Records, 2013). Pay television indicated growth of 25, 85% during the 2011 to 2012 financial period, while print media showed a decrease of 1, 15% for the same period and the internet segment indicated excellent growth of 80,21% from 2011 to 2012.

The total growth in overall revenue of Naspers is illustrated in Graph 6-8. Graph 6-8 was compiled with data gathered from the Annual Financial Records of Naspers for the past three financial periods: 2011, 2012 and 2013.



Graph 6-8: Total revenue of Naspers

Source: Naspers Annual Financial Report (2011:40) (2012:38) (2013:130)

Graph 6-8 illustrates a growth in the total revenue of Naspers. A growing trend was demonstrated by the three financial periods illustrated in Graph 6-8. The significant growth in overall revenue in 2013 is most likely due to the extreme increase in revenues generated from the internet segment of the company as illustrated in Graph 6-7. The total revenue from the 2011 financial period to the 2012 financial period showed a growth of 14.59%, while 2012 to 2013 indicated a growth of 27, 25%. As illustrated in Graph 6-8, there was an overall increase in the total revenue of Naspers for the past three years.

6.6 CONCLUSION

Four JSE listed companies were selected: AME, Hosken, Kagiso Media and Naspers. These companies trade within the media, broadcasting and entertainment market. The annual financial reports of 2011, 2012 and 2013 were used for the purpose of the analysis.

From the analysis of the Annual Financial Reports of the companies, it was clear that there was a growth in revenue derived from advertising activities. Due to the fact that all four of these major JSE listed companies revealed a growth in such revenue, it is possible to refer to this phenomenon as an indication of a burgeoning advertising market in South Africa.

The findings in this chapter contributed to the identification of the role of advertising in the economy of South Africa. The classification of advertising as capital or revenue of nature is clearer if the importance of advertising in the economy is understood. Chapter 6, together with Chapter 3, indicated the role of advertising not only in South Africa but also around the world; however Chapter 6 focused only on the South African advertising market.

This chapter solved one of the questions posed in the problem statement regarding the role and development of advertising, as stated in Chapter 1 of the study. After interpreting all the information gathered from the analysis of Annual Financial Reports for the past three years, it was possible to state that advertising does indeed play an increasing role in the South African economy. Chapter 7 is a summary of all the findings gathered throughout the study. It includes recommendations and suggestions for further studies. The achievement of the research objectives is addressed in Chapter 7.

CHAPTER 7
CONCLUSION AND RECOMMENDATIONS

7.1 INTRODUCTION

Chapter 7 concludes the research undertaken, suggestions are made for further research and answers to the questions as set out in Chapter 1 are summarised:

- When can advertising cost be seen as capital of nature? (paragraph 7.3)
- Can advertising cost be classified as an asset or intangible asset? (paragraph 7.3.1)
- Is there a link between advertising costs and long term benefits arising from advertising? (Darral, 1976:345) (paragraph 7.3)
- Does advertising cost have long term benefits? (Hassens, 2011:2).

In this chapter and in accordance with the primary objective as set out in Chapter 1, guidelines, as established in this study from the analyses of national and international tax acts and court cases, are summarised in Table 7-1 and 7-2. This summary was made not only to assist with the classification of advertising cost for tax purposes but also to investigate whether advertising cost should, for accounting purposes, be regarded as an asset or an intangible asset (paragraphs 7.3 and 7.3.1).

In accordance with the primary objective of the study, the following secondary objectives are then addressed:

- To determine when and why advertising cost may be ascertained as capital or revenue of nature, according to the Act, as well as establishing the guidelines for the classification of advertising cost (paragraph 7.4).

Furthermore, the research methods that were used for the purpose of the study as well as the implications thereof are summarised. Limitations faced by

the study are identified and recommendations for further research are made based on the said identified limitations.

7.2 FOCUS OF THE STUDY

The elements relating to advertising, as discussed in Chapter 3, play an important role leading to a better understanding of advertising and its place in the economy, not only of South Africa but worldwide. All the research undertaken during the progression of the study provides a contribution towards an improved understanding of the classification of advertising cost for tax purposes as capital or revenue of nature.

The classification of advertising cost may be described as a complex process that has to take a number of elements into consideration. The classification of advertising cost cannot be decided in isolation using just a few key factors.

The problem posed by this study, as referred to in Chapter 1, paragraph 1.2, indicated that there has not been enough research done on the classification of advertising cost for tax purposes. There are many grey areas that leave room for the inaccurate classification of advertising cost which may be attributed to the lack of research as well as the lack of detail found in The Act which was analysed in paragraph 4.6 (Moodley, 2011:57).

7.3 ROLE AND DEVELOPMENT OF ADVERTISING

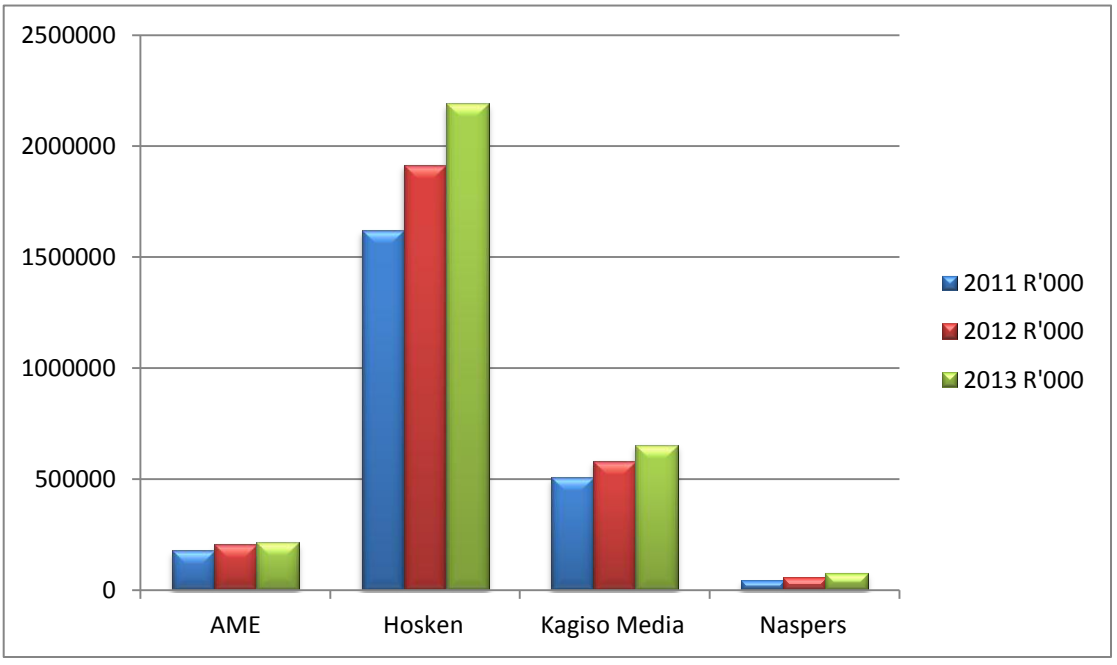
Chapter 3 shed light on the role of advertising in economies around the world. It is necessary to understand this in order to acquire an overview of the importance of advertising. From the research undertaken there it was clear that advertising is indicating an increase in development around the world and, based on this premise, it was considered safe to assume that the tax related to advertising is also increasing.

Owing to the growth in advertising and thus the growth of tax related to advertising it was easy to identify the importance of the correct classification of advertising cost for tax purposes. Incorrect classification will lead to incorrect tax payments as well as violations of tax rules. Research, as set out

in Chapter 6, provided insight on the advertising market of South Africa. The advertising companies of South Africa that are listed on the JSE were investigated to sketch a picture of the developing tendencies of the South African advertising market.

From the research carried out in Chapter 6 it could be seen that the advertising market in South Africa is showing such tendencies, adding to the importance of the correct classification of advertising cost for tax purposes, since enormous amounts of tax may be miscalculated due to the wrong classification, even having an impact on the South African economy.

Graph 7.1 illustrates the growth of the advertising market in South Africa by illustrating the growth of advertising revenues in the JSE listed companies from data gathered in Chapter 6 of the study.



Graph 7-1: Growth in advertising revenue

Source: Own research

From this Graph it is easy to deduce that there is a definite upward trend in advertising in South Africa. There was increased advertising revenue from 2011 to 2013 in all four companies.

In terms of the knowledge gathered from the research reported in Chapter 3 regarding the development of advertising around the world, combined with the findings of Chapter 6, guidelines are needed for the correct classification of advertising cost for tax purposes in order to achieve the research objectives. Graph 7-1 is also an indication that advertising markets will continue to flourish in the future in South Africa. The following paragraph will focus on the important factors that need to be taken into consideration for the purpose of the classification process of advertising as capital or revenue of nature; this is in reference to the research objective posed in Chapter 1.

7.4 IMPORTANT FACTORS TO CONSIDER WHEN CLASSIFYING ADVERTISING COST

The research in Chapters 4, 5 and 6 indicated that there are numerous factors that may be used in order to classify advertising cost as accurately as possible for tax purposes. A brief summarised discussion of the factors that have been identified, and which need to be taken into account for the classification process of advertising cost as capital or revenue of nature, follows.

7.4.1 Accounting treatment of advertising cost

Some of the areas focused on in Chapter 3 are the recognition of advertising cost as an asset and intangible asset for accounting purposes as well as the role that advertising plays around the world in different economies. In Chapter 3, paragraph 3.5, an analysis was performed to determine how advertising may be recognised in accounting. The recognition criteria, as set out by IFRS, have been used together with the accounting definitions of an asset and an intangible asset to determine if advertising may be recognised as one or the other.

The analysis of advertising cost resulted in the realisation that advertising may be seen as an asset or an intangible asset rather than just recognising it as an expense. To determine whether advertising should be recognised as one of these three possibilities, the specific circumstances of each scenario need to be taken into consideration.

A suggested solution was reached in Chapter 3 that answers the research objective as stated in Chapter 1, paragraph 1.3.1. This concluded that advertising may be seen as an asset or intangible asset depending on the specific circumstances.

7.4.2 Guidelines from case law

South African case law, as well as international case law that may have an impact on how advertising cost should be classified for tax purposes, was identified and discussed in Chapter 5. One of the research objectives as set out in Chapter 1, paragraph 1.3 was to establish guidelines that can be used for the classification process of advertising cost together with relevant case law.

Nine guidelines were identified for the purpose of the classification process and are set out in Chapter 5, with a summarised version of them in Table 7-1.

Table 7-1: Guidelines established from case law

National and international case law	Guideline established
National	The term capital should not be used as a definite outcome; it should rather be used in guiding the classification of advertising as capital or revenue of nature.
National	The reference to fixed and floating capital should be used in line with the nature of the trade in which the asset is used in. An expense may solely be classified as fixed or floating capital after the trade has been identified.
National	The type of transaction needs to be taken into account when deciding whether it qualifies as fixed or floating capital. After this has been ascertained, the classification process is able to continue in classifying advertising cost as capital or revenue of nature.

Table 7-1: Guidelines established from case law *(continued…)*

National and international case law	Guideline established
National	Income earning activities and income earning concerns need to be identified before advertising cost may be classified for tax purposes.
National	Once-off payments may be seen as capital of nature while cost that is re-occurring may be seen as revenue of nature.
National	An enduring benefit should be compared to fixed capital and not to revenue payments.
International	The length of the period in which the advertisement may be useful for the entity should be taken into account before deciding if the cost should be capital or revenue of nature.
International	The estimated amount of benefits that will be a result of the advertising campaign should be calculated if it is possible. In the case where the benefits are substantially larger than the cost that has been incurred these may be seen as capital of nature.
International	The cost incurred does not necessarily have to be a once- off payment in order for it to be classified as capital of nature.
International	The reason for the expense that has been incurred needs to be clearly understood. It is important to understand exactly why the advertising expense has been incurred and what it aimed to achieve.

Source: Own research

The guidelines summarised in Table 7-1 should not be used in isolation, but should be used together with all the other elements that have been identified throughout the study for the purpose of the given classification process. The guidelines summarised in Table 7-1 contribute to the study by creating principles that may be used to determine how advertising cost should be classified.

From the information provided in Table 7-1, the term capital or capital of nature should not be used as a final outcome that cannot be debated. Determining whether the cost incurred for advertising qualifies as a fixed or floating capital item is of great importance: this will help to understand the nature of the cost, which contributes to the understanding of how advertising cost should be classified for tax purposes.

One of the guidelines set out in Table 7-1 highlights the importance of understanding the income earning activities of the entity in question versus the income earning structure. Only after the difference has been established will it be possible to clearly understand if advertising is a capital asset for that specific entity.

A guideline established from national case law in Chapter 5, paragraph 5.3.2 indicates that recurring payments should not be seen as capital of nature; however another guideline established from international case law indicates that not all such payments regarding advertising should be seen as revenue of nature. These two guidelines are an example of why the guidelines should not be used in isolation. Two guidelines that should also be followed are the length of the period during which the advertisement may prove useful for the entity and the amount of estimated benefits that it will yield as a result. The longer the period and the higher the benefits, the more likely it is that the cost may be classified as capital of nature.

The final guideline that was established and summarised in Table 7-1 is related to the clear understanding of why the cost has been incurred and what exactly the aim of this cost is. These guidelines will help to ensure that advertising cost is classified as accurately as possible for tax purposes. The correct classification of advertising cost will lead to less violation of the TAA as well as more accurate tax calculations. When determining if the advertising cost in question is capital or revenue of nature it is important to look at all the guidelines together in order to achieve the most accurate outcome.

7.4.3 Important facts from international income tax acts

Chapter 4 of the study focussed only on the different tax treatments of advertising cost around the world. Countries from the Commonwealth organisation, the BRICS initiative as well as the United Kingdom and the United States of America have been used for the gathering of information related to the tax treatment of advertising.

The key points identified from the analysis of the different tax acts were summarised in Chapter 4, Table 4-3. These may be used for future development of the sections of The Act that relate to the classification of advertising. South Africa can learn from the rest of the world regarding the tax treatment of advertising. The abovementioned key points are already components of different tax acts; it is thus possible for South Africa to determine the efficiency thereof in other countries before implementing them locally.

From the tax acts analysed, it was found that 17 of these specifically provide in some manner or other for advertising cost. A summary of the central facts that were found in Chapter 3 was provided in Table 7-2 which identifies these key points, and indicates the frequency of the key point identified, as well as whether The Act makes similar provisions.

Table 7-2: Summary of key points identified from international tax act analysis

Key point	Popularity	South Africa
There is a deduction available for expenses that are in relation to trade; if this amount has been incurred in the production of taxable income it may be deducted for tax purposes.	This provision is made in all the tax acts that have been analysed.	Section 11(a) of The Act is similar to the provisos made in international tax acts

Table 7-2: Summary of key points identified from international tax act analysis

Key point	Popularity	South Africa
Advertising is a specific deduction.	17 of the 41 of the tax acts that have been analysed contain sections that relate to the specific deduction of advertising cost.	Section 23(g) only give deductions to the extent of trade. There is no specific deductions for advertising in South Africa.
The possibility of advertising as capital of nature is addressed.	This possibility is addressed in 5 out of the 17 tax acts.	S11 (a) gives an indication that expenditure (in general, including advertising) may be of a capital nature. Section 23(g) only give deductions to the extent of trade and no indication of capital nature.
Advertising that has a long lasting benefit or is of a long lasting nature will not be deductible.	The tax act of the United Kingdom makes provision for this eventuality.	There is no specific section of The Act that stipulates these circumstances.
A limitation on the deduction of advertising cost: 15% on the total income.	The tax act of China makes provision for the limitation of advertising cost.	The Act does not have any similar provision for advertising cost.

Table 7-2 is merely a summary of the most pertinent key points. Chapter 3 contains all the provisions made by the various tax acts, in detail and should therefore Table 7-2 should be read together with Chapter 3. It is evident from the research in Chapter 3 that not many tax acts provide specifically for the deduction of advertising cost. However, all of the tax acts have a provision for the deduction of expenses related to the income earning activities of advertising which is in line with the provisions in section 11(a) and 23(g) of The Act. Section 23(g) provides for deductions to the extent of trade. There is no specific deductions for advertising in South Africa.

Most of the tax acts that have been analysed do not mention the possibility of advertising being capital of nature. Nevertheless, this does not mean that advertising is definitely not capital of nature. The omission of this possibility of advertising may be due to amounts that do not qualify as deductible expenditure with regard to expenses incurred for the production of income as being less easily identifiable. It may therefore not be necessary to specifically mention the possible capital nature of advertising cost. It is, nonetheless, necessary to look at the principles established from case law (paragraph 7.3.2), owing to the fact that it is not possible to determine whether advertising cost may be seen as capital of nature from analysing tax acts of other countries.

7.4.4 National provision for advertising cost

It was established in Chapter 3 that The Act makes provision for allowable deductions if the expense is related to the income earning activities of an entity; this provision is made under section 11(a) read together with section 23(g). Section 11(a) read together with section 23(g) has a few criteria that have to be met before an expense is deductible, as follows:

- "There must be expenses or losses recorded"
- The above must have "actually been incurred"
- The above must have occurred "during the year of assessment"
- The expenses and losses must have been "incurred in the production of income"
- The expenses and losses should "not be of a capital nature"
- The above must either in part or in full be expended "for the purpose of trade"

All of the abovementioned criteria have to be met before an expense is allowed as a deduction. These criteria are similar to those set out in most of the international tax acts that were analysed in this study. Section 11(a) read together with section 23(g) may provide for the deduction of costs relating to advertising.

However, while this deduction is not allowed in the case where advertising cost is capital of nature, the Act does not give any detailed description of when advertising cost may be qualified as such. The classification process that has been established in order to achieve the secondary research objective follows.

7.5 THE CLASSIFICATION PROCESS FOR ADVERTISING COST AS CAPITAL OR REVENUE OF NATURE IN SOUTH AFRICA

The process for classification was developed in order to help achieve the research objectives as set out in Chapter 1, by combining all the research carried out during the progression of the study.

The primary objective of the study, as set out in paragraph 1.3, indicates that there would be an investigation executed during the progression of the study regarding the circumstances under which advertising could be classified as capital or revenue of nature. The illustrated process of Diagram 7-1 is used to achieve this objective.

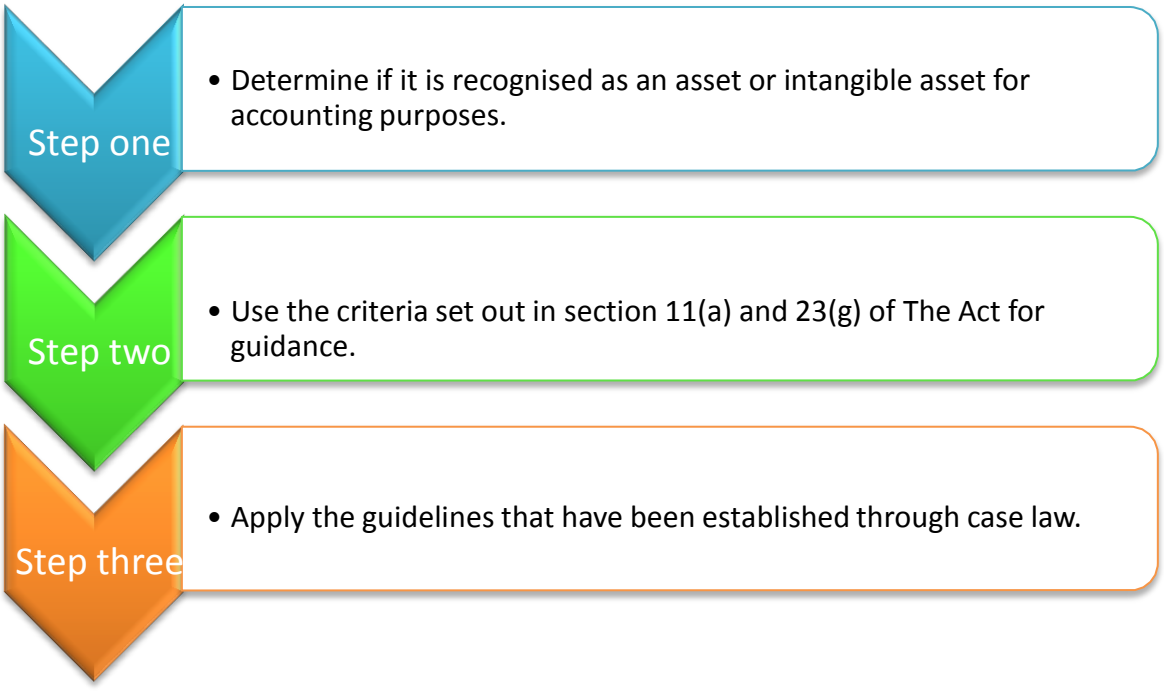


Diagram 7-1: The process of classifying advertising as capital or revenue of nature

Source: Own research

As illustrated in Diagram 7-1, there are three steps involved in the process of classifying advertising cost as capital or revenue of nature. Further details follow.

Step one

Determine whether advertising may be recognised as an asset or intangible asset for accounting purposes

The definitions for both assets and intangible assets should be considered to determine how advertising may be recognised for accounting purposes

A further factor to keep in mind concerns the recognition criteria for an asset and intangible asset.

Step two

Apply the rules set out in section 11(a) together with section 23(g) of The Act to identify if advertising qualifies as a deduction.

If there is uncertainty regarding advertising being capital of nature, the guidelines in step three should be applied.

Step three

Apply the guidelines set out in Chapter 7, paragraph 7.3.2 to the specific circumstances in order to gain a more accurate idea of the possibility of advertising cost being classified as capital of nature.

The three abovementioned steps indicate the process that may be used to classify advertising cost as capital or revenue of nature. These steps should be taken after the circumstance of each individual scenario has been evaluated. They have been formulated with the aim of classifying advertising cost more accurately as capital or revenue of nature and should not be used

individually; this should thus rather be considered a process that assists in classifying advertising as accurately as possible.

It was established in Chapter 4 that section 11(a) and 23(g) do not contain detail regarding when advertising cost could be regarded as capital of nature. The three steps may be used to determine this.

The following paragraph offers a short overview of the research methodology applied throughout the study, as discussed in Chapter 2.

7.6 RESEARCH METHODOLOGY AND LIMITATIONS

The research methodology that was applied for the purpose of this study has been discussed in Chapter 2, paragraph 2.3. A mixed method approach was followed involving qualitative and quantitative investigations.

The qualitative research method was applied by way of an analysis of national and international tax acts. The focus of the analysis of the tax acts was on provisions that might be applicable to the classification of advertising cost as capital or revenue of nature as well as possible deductions available for advertising cost.

Both national and international case law related to the classification of advertising cost as capital or revenue of nature was investigated. The investigation of case law formed a component of the qualitative part of the applied research methodology. The second element of the study, involving a qualitative approach, was used in Chapter 3 which focuses on the role of advertising in the economy as well as the development thereof in various countries.

Quantitative research was performed by way of scrutinising the annual financial records of four South African JSE listed companies that trade in the media, broadcasting and entertainment markets. The aim of the quantitative research undertaken in Chapter 6 was to highlight the growing role of the advertising market in the South African economy.

The research methodology discussed was applied throughout the study. The use of a mixed method approach resulted in very few limitations for the study. Those limitations encountered as a result of the selected research method were identified and discussed in Chapter 2. Areas that need further study are recommended in the next paragraph.

7.7 RECOMMENDATIONS FOR FURTHER STUDY

Throughout the study, certain areas were identified that could be considered for future research. In the case where advertising cost was successfully identified as capital of nature, it may be necessary to determine if there should be a capital allowance for advertising.

More research could be performed on the long term benefits of advertising for an entity. If these benefits could be identified or determined, this would result in a more simplified classification process.

The impact of advertising on the South African economy would prove useful for tax purposes as well. Research on this topic is limited in South Africa and is thus suggested for further research. Further research is recommended regarding the depreciation and capital allowance granted for advertising if it should be recognised as an asset for accounting purposes and classified as capital of nature for tax purposes.

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