The general meaning of “extenuating circumstances” for the purposes of section 76(2)(a) of the Income Tax Act

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Abstract

The additional tax (referred to as a “penalty” by the judiciary), which may be imposed in terms of section 76(1) of the Income Tax Act ("the Act") when a taxpayer is in default, can be very harsh (Up to 200% of the tax correctly chargeable). The Commissioner may remit any penalty imposed as he sees fit. However, when there was intent on the part of the taxpayer to evade the payment of tax, the Commissioner may not remit the 200% penalty, unless he is of the opinion that there are “extenuating circumstances”.

This article examines the general meaning, as interpreted by the courts, of the “extenuating circumstances” that may be taken into account for the purposes of remission of penalties in terms of section 76(2)(a) of the Act.

Key words

Remission of penalties Versagtende omstandighede
Extenuating circumstances Mitigating circumstances

1 Introduction

In the case of Lutterworth Rugby Football Club v Commissioner of Customs, (MAN/86/405), a football club successfully disputed the argument of the revenue authorities that the bar takings of the club were underdeclared. The tax tribunal appointed to hear the appeal declined to impose tax or penalties on the club on the basis that the bar was not run as a commercial activity as it “was often staffed by volunteers not necessarily numerate or even sober. Confusion as to charges and change could easily occur” (MAN/86/405:406).
The Lutterworth decision, although a foreign decision (but which carries persuasive authority with a South African court), illustrates the general principle that, if there are special circumstances in a case, the moral blameworthiness of a taxpayer for the underdeclaration of income can be substantially reduced and may in some instances even be regarded as non-existent. Section 76(2)(a) of the Act recognises this general principle and makes special provision for the remission of the additional tax that may be imposed on a defaulting taxpayer in terms of section 76(1). The additional tax is hereinafter referred to as a “penalty”, because the judiciary generally uses this term interchangeably with the words “additional tax” for the purposes of Section 76 (CIR v Da Costa (47 SATC 87)).

2 Object of article

The object of this article is to examine the general concept and meaning of “extenuating circumstances” as applied in income tax matters for the purpose of the remission of penalties in terms of section 76(2)(a) of the Income Tax Act, No. 58 of 1962 (“the Act”).

3 Research method

The research method adopted consists of a literature review, analysis of the relevant provisions of the Act together with court decisions, both local and foreign, which relate, directly and indirectly, to the objective.

4 Remission of penalties in terms of section 76

A penalty imposed in terms of section 76(1) can be very harsh - as much as 200% of the amount of the tax defaulted. However, section 76(2)(a) provides for the following relief:

“The Commissioner may remit the additional charge imposed under subsection (1) or any part thereof as he may think fit: Provided that, unless he is of the opinion that there were extenuating circumstances, he shall not so remit if he is satisfied that any act or omission of the taxpayer referred to in paragraph (a), (b) or (c) of subsection (1) was done with intent to evade taxation.”

In addition, section 76(2)(c) provides that:

“Notwithstanding the provisions of this subsection, the Commissioner may either before or after an assessment is issued agree with the taxpayer on the amount of the additional charge to be paid, and the amount so agreed upon shall not be subject to any objection and appeal.”
Section 76(2)(a), read in conjunction with section 76(2)(c), can be analysed as follows:

(a) If the taxpayer had no intention to evade the payment of tax, the Commissioner has the discretion to remit the whole or part of the 200% penalty that has been imposed, but he is not obliged to remit the penalty even if there was no intent on the part of the taxpayer to evade tax. It is, however, highly unlikely that, where there was no intention to evade tax and the taxpayer has given a satisfactory explanation for the default, the Commissioner would not remit the penalty, at least in part.

(b) If the Commissioner is satisfied that the taxpayer did intend to evade the payment of tax, he may not remit the 200% penalty imposed, unless he is of the opinion that there are “extenuating circumstances”. If the Commissioner should find that there were “extenuating circumstances”, he may remit the 200% penalty as he sees fit.

(c) The Commissioner is nevertheless competent to impose a penalty (of up to 200% of the amount of the default in tax, or even not to impose a penalty) by agreement with the taxpayer even where there was intent on the part of the taxpayer to evade tax.

(d) When the taxpayer and the Commissioner have agreed on the amount of the penalty to be imposed, the taxpayer may not thereafter appeal against the penalty agreed upon to the Special Court for Hearing Income Tax Appeals (“Special Court”) or to any other court (High Court). However, any penalty imposed by the Commissioner without the agreement of the taxpayer is subject to appeal to the Special Court and the Special Court may substitute its own penalty for that of the Commissioner (CIR v Da Costa (47 SATC 87)).

The main problem areas that arise from the analysis of section 76(2)(a) are:

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1 Nestadt J, in CIR v Di Cicco (47 SATC 199), stated that the intention to evade tax is not a sine qua non for the operation of section 76(1). Carelessness or negligence or even inadvertence on the part of the taxpayer brings section 76(1) into play. He continued as follows (47 SATC 199:205):

“In other words, then, no particular form of mens rea is required. The question is simply whether, objectively considered, there was an omission of an amount which ought to have been included or an incorrect statement.”

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Firstly, if there is no intention to evade tax, but a taxpayer has committed a section 76(1) offence, what factors are taken into account or should be taken into account by the Commissioner or, on appeal, by the courts in deciding whether any penalty imposed should be remitted (and do these factors bear the same meaning as “extenuating circumstances”)?

Secondly, what constitutes “extenuating circumstances” for the purpose of remission of penalties in the case of a deliberate intent on the part of a taxpayer to evade the payment of tax?

It is beyond the scope of this article to devote special attention to the level of penalties imposed once “extenuating” or other factors are found to be present. The reader will nevertheless be able to draw preliminary conclusions in this regard, because, in appropriate cases, the level of the penalty imposed will be mentioned in relation to the “extenuating circumstances” that were found to be present.

The controversial issue of permitting the Commissioner and the taxpayer to agree on the amount of the penalty (even when the taxpayer intended to evade the payment of tax) will also not be discussed in this article, because it is assumed that the Commissioner will always act in a bona fide manner and use, but not abuse, the discretionary power granted to him. In addition, because any agreement reached between the Commissioner and the taxpayer is confidential and not open to objection and appeal, there is no public record from which the researcher can obtain such information and upon which he can base his comment on the practice. In fact, in terms of section 4 of the Act, the Commissioner is obliged to preserve secrecy in regard to all matters that come to his attention.

Section 75A overrides section 4, but only in very limited circumstances. It provides that the Commissioner may from time to time publish for general information the name, particulars of the tax offence committed, amount of tax and additional tax involved and particulars of the fine or penalties imposed on a taxpayer that has been convicted of a tax offence in terms of sections 75 or 104 or paragraph 11A(7) or 30 of the Fourth Schedule or paragraph 19 of the Seventh Schedule of the Act or the common law. It is imperative to note that there must be a conviction in a court of law. The Special Court for Hearing Income Tax Appeals cannot and does not convict a tax defaulter in terms of section 75 or in terms of the other provisions mentioned above. Rather, the Court imposes additional tax or penalties in terms of section 76 of the Act.

Therefore, for the Commissioner to be able to publish the details of a tax offender in terms of section 75A of the Act, he should prosecute him through the ordinary courts and obtain a conviction. This route can be followed after the Special Court has confirmed a penalty that had been
imposed by the Commissioner or the Special Court has substituted the penalty of the Commissioner with its own penalty (as was done in Van der Walt v S (52 SATC 186)) or the Commissioner may proceed directly through the criminal court system.

The Commissioner may not publish a tax offender’s name in a case in which the offender has agreed with the Commissioner on the amount of the penalty, because the taxpayer would not have been convicted of a stipulated offence. This applies even if the Special Court imposes a penalty. Nevertheless, should the taxpayer appeal to the High Court (formerly known as the Supreme Court) against a Special Court decision, the name or identity of the taxpayer may be published.

Anyone that contravenes the secrecy provisions of the Act is guilty of an offence and is liable, upon conviction, to a fine or even to imprisonment for a period not exceeding two years.

5 The general meaning of “extenuating circumstances”

5.1 Introduction

AA Landman (1984:108), in an article in which he examines aspects of additional tax (commonly referred to as penalties), correctly remarks that there is no definition of “extenuating circumstances”. He is of the opinion that the generally accepted meaning of the phrase can be found in R v Biyana, (1938 ECD 310:311) in which Landsdown JP said:

“In our view an extenuating circumstance . . . is in fact associated with the crime which serves in the mind of reasonable men to diminish, morally albeit not legally, the degree of the prisoner’s guilt.”

Landman also submits (1984:108) that the Afrikaans wording that is used in the Act for “extenuating circumstances” (the English version of the Act was signed and is consequently the official version), namely “versagende omstandighede”, is a broader concept than its English equivalent. Its meaning includes circumstances that are mitigatory and it should therefore not be used. He defines the distinction between the two concepts as follows (1984:108):

“Broadly the distinction between extenuating circumstances and mitigatory circumstances is that the former relate to the circumstances present at the commission of the ‘crime’ whilst the latter would embrace all other circumstances including those which are present at the time punishment is considered.”
He further submits (1984:108), in support of his argument, that the legislature intended that only the narrow meaning should be used, because:

"The emphasis on the past tense in section 72(2)(a) of the Act – ‘there were extenuating circumstances’ – restricts the relevant circumstances to those which were present at the stage of the default."

5.2 Interpretation of “extenuating circumstances” by the courts in income tax matters

Ogilvie Thompson JA, in the Appellate Division case of SIR v Somers Vine (29 SATC 179), held in his majority judgement that, in construing the meaning of words, it is possible to refer to the unsigned version of the Act. He said that (29 SATC 179:187):

"While the English text of the (Income Tax) Act is the signed version, it is . . . in my opinion permissible to refer to the Afrikaans text."

Van Den Heever JA, in CIR v Da Costa (47 SATC 87:97), went even further when he stated:

". . . regard may be had not only to the extenuating circumstances but to all relevant factors."

In addition, the judge in ITC 1612 (59 SATC 180:186) used the words “mitigating circumstances” rather than the phrase “extenuating circumstances” in relation to the remission of penalties in terms of section 76(2)(a).

Based on the views of Ogilvy Thompson JA (that the meaning ascribed to the Afrikaans wording is permissible in interpreting the meaning to be ascribed to it in English, even if the legislation was signed in English and could bear a different meaning), Van den Heeer JA and Conradie J, in ITC 1612 (59 SATC 180), submitted that the distinction between the two phrases (“extenuating circumstances” and “mitigatory circumstances”) is merely an academic debate in income tax matters. In practice there is no distinction.

It is furthermore submitted that the court is not restricted to the relevant circumstances that existed at the time of the default, but regard can be had to circumstances that arise subsequently. In ITC 1430 (50 SATC 51:56), Mullins J made the following comments in this regard:
“Nor does it seem to me that the Special Court is restricted to evidence of facts existing as at the date of assessment or of imposition of the additional charges. This would be the situation in an ordinary civil or criminal appeal, where the court on appeal is confined solely to the record. . . . There seems therefore to be no logical reason why we should not consider the facts existing as at the date of the appeal in exercising our powers on appeal . . . . It would, for example, require us to sit with blinkers if we were obliged to close our minds to the fact of the supervening death of the taxpayer, (author’s underlining) as well as to certain other facts to which I shall refer.”

Mullins J referred to the “other facts” that he felt obliged to consider (50 SATC 51:58), namely that the taxpayer was married and had four minor children, and that his estate was apparently insolvent to the extent of R19 613 (which amount included penalties of R66 195). If the penalties were to be remitted, the estate might just be solvent, because the R19 613 insolvency amount did not include administration expenses, liquidation costs or possible claims for the maintenance of the taxpayer’s four minor children. He went even further by stating that, if the penalties were not remitted, the concurrent creditors and the minor children would be prejudiced and it would be them, rather than the deceased taxpayer, that would be punished.

It is submitted that Mullins J, together with Van den Heefer JA, have succeeded in shaping the meaning of “extenuating circumstances” for the purposes of section 76(2)(a) to include factors not normally regarded as “extenuating circumstances” in criminal law cases. The fine line, although lip service is sometimes paid to it, between “extenuating circumstances” and other factors that are taken into account in deciding the level of the penalty to be imposed, has also been blurred. It is submitted that this is a fair and equitable way to approach the matter, as was illustrated in CIR v Da Costa (47 SATC 87).

In the aforementioned case, the taxpayer was an immigrant of humble origin and had had little schooling. Through hard work he ultimately established a thriving corner-cafe business. He entrusted the bookkeeping and the handling of his tax returns to a firm of accountants that he regarded as possessing the necessary knowledge and skill regarding such matters. After an investigation by the Commissioner’s office, the taxpayer’s income was found to be understated and tax of approximately R15 500 owing. A penalty of 100% (or in terms of a legalistic perspective, a 50% remission) was imposed on the taxpayer in spite of the fact that the Commissioner’s representative made it clear that no intention to deceive was being imputed against the taxpayer in his personal capacity. The basis for the penalty was that the taxpayer should be punished for the deceit of his agents.
The Special Court took the view that, because the taxpayer’s agents had acted with intent to evade tax, the penalty could not be remitted unless “extenuating circumstances” were found to prevail. The extract from the Special Court judgement, quoted with the approval of the Appellate Division (47 SATC 87:96-97) is enlightening in regard to what the Special Court (and the Appellate Division) regarded as “extenuating circumstances”, namely:

“The taxpayer, it appears, is a man of 59 years of age who, when he migrated to South Africa, was a farm labourer. He had no more than four to five years of schooling. He acquired his “corner cafe” by paying off the purchase price in instalments, working seven days a week for 12 to 13 hours a day. He has five children, two of whom are still at school. He has paid the additional normal tax and the penalty of R15 590.00. He appeared to the court to be a man without guile and patently honest, who believed that by entrusting the bookkeeping of his business and the handling of his tax to people whom he regarded as professionals in the field of accounting and taxation matters, he was doing all that was required of him with regard to the payment of tax. Ignorance, naivete, semi-literacy, and a simple-minded (albeit misplaced) confidence in an apparently reputable firm of accountants, together with a single-minded devotion to the task of making a living for his wife and children they were rearing all constitute strong, indeed very strong, extenuating circumstances.”

However, Van den Heever JA was not convinced that the Special Court had adopted the correct approach in imputing the intent to evade tax from the accountants to the taxpayer. He commented that the key words of section 76(2)(a) are “any act or omission of the taxpayer . . . done with intent to evade taxation”, applied only to an actual and not also an imputed intention of the taxpayer. However, he found it unnecessary to decide this point.

This point was considered by the judge in ITC 1486 (53 SATC 39) (in relation to the Sales Tax Act, No. 103 of 1978, which has similar wording to the Income Tax Act in provisions relating to the imposition of penalties). He held that the intent of a few employees could not be imputed to the taxpayer, but that some blameworthiness attached to the taxpayer in that the taxpayer failed to exercise proper supervision over its employees. The court was of the opinion that (53 SATC 39:48):

“If the Legislature had wished to attribute the intent of the employee to the taxpayer it could easily have so provided and in the absence of such provision this is not to be
Van den Heever JA also dealt with the submission of the Commissioner’s representative that the Special Court erred in taking into account the taxpayer’s financial position as an “extenuating circumstance”. He dismissed the submission as follows (47 SATC 87:97-98):

“The short answer is that the court did not do so. Having found that there were extenuating circumstances, the court merely said that a penalty of R3 000 could not conceivably ‘be regarded as trifling to a person of the taxpayer’s means, enjoying the life-style he does’.”

These words imply that once “extenuating circumstances” have been found to be present, then, even in the most blatant cases of tax evasion, other factors can be taken into account in determining the level of the penalties to be imposed.

The courts have often said that there is no room for equity in taxation. If a person falls within the letter of a provision, he is taxable, no matter how inequitable it may seem. However, judges love to find an equitable solution, if at all possible. In CIR v Nemajim (Pty) Ltd (45 SATC 241:267), Corbett JA, with some sense of smug satisfaction, commented as follows:

“It has been said that ‘there is no equity about a tax’. While this may in many instances be a relevant guiding principle in the interpretation of fiscal legislation, there is nevertheless a measure of satisfaction to be gained from a result which seems equitable, both from the point of view of the taxpayer and from the point of view of the fiscus. And it may be fairly inferred that such a result is in conformity with the intention of the legislature.”

Perhaps Van den Heever JA and Mullins J were giving expression to these sentiments when defining, very liberally, the meaning of “extenuating circumstances” for the purposes of section 76(2)(a) of the Act. It is submitted that with the very harsh penalties that are prescribed for tax evasion, and with the taxpayer at an unfair advantage regarding the burden of proof2 the judiciary have correctly endeavoured to lessen

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2 In terms of section 82 of the Act, the onus of proof is on the taxpayer. However, in view of the harsh penalties that may be imposed on a defaulting taxpayer, this reverse onus may be unconstitutional (in terms of various sections of the Constitution of South Africa Act, No. 108 of 1996) in cases in which penalties are imposed. This issue is not discussed since it is considered to be beyond the scope of the article.
“Extenuating circumstances” – the general meaning

the burden of the taxpayer by including in the interpretation of “extenuating circumstances” factors that are not normally taken into account for criminal law purposes.

Landman (1984:108) also argues that section 76(1) emphasises the subjective state of mind of the taxpayer at the time of the act or omission referred to in that section. While this is entirely true, it is obvious that it is a very difficult task to read the mind of the taxpayer at the time of the act or omission. Justice Salmond, speaking in the Privy Council around 1860, is reputed to have said: “the thought of man is not triable for the Devil himself knoweth not the thought of man” (Desco Electronic Software).

The fact that intention can sometimes only be established with some degree of certainty by reference to objective factors has been demonstrated in many tax cases, especially in cases dealing with the question whether or not a receipt, for the purposes of the definition of “gross income” in section 1 of the Act, is of a capital nature. In Malan v KBI (43 SATC 1), the court held that a person’s ipse dixit is not conclusive, and inferences may be drawn from the surrounding circumstances. Grosskopf J (43 SATC 1:7) indicated that a taxpayer’s ipse dixit as to his intention might not be accepted by the court, not because his honesty is doubted, but because:

“Mense se bedoelings is dikwels wisselend, ongevorm en ongeformuleer, en hul ex post facto getuienis daaroor, hoewel eerlik, is dikwels onbetroubaar, of bestaan uit blote rekonstruksie.”

Prior to this case, Miller J, in ITC 1185 (35 SATC 122:123-4), had commented that:

“The taxpayer’s evidence under oath and that of his witnesses must necessarily be given full consideration and the credibility of the witnesses must be assessed as in any other case which comes before the court. But direct evidence of intent and purpose must be weighed and tested against the probabilities and the inferences normally to be drawn from the established facts.”

Even when the taxpayer has not committed fraud or evaded tax, the courts, in determining whether penalties imposed should be remitted, ask whether there are “extenuating circumstances”. In ITC 1518 (34 SATC 113), a fairly large penalty was imposed by the judge in spite of the fact that the Court found that the taxpayers’ returns were not submitted as a result of the oversight of the auditors concerned. The Special Court held that even careless or thoughtless conduct on the part of the taxpayer falls within the ambit of section 76(1), but because the auditors were at fault, “extenuating circumstances” did exist.
Again in *ITC* 1576 (56 SATC 1), in which case the taxpayer had only disclosed 12% of his taxable income, the Special Court held that there was no intent on the part of the taxpayer to evade tax. The taxpayer had contended that his bookkeeper was to blame. The bookkeeper testified that the errors that had been made were entirely the result of his mistakes or negligence. Although the taxpayer had not succeeded in proving that there had been no fault on his part in the form of negligence, his reliance on the bookkeeper was regarded as an “extenuating circumstance”.

6 Summary and conclusion

The general meaning of the phrase “extenuating circumstances” is broader than that used in criminal law (*CIR v Da Costa* 4787 (47 SATC 87)) and incorporates the often-used phrase “mitigating circumstances” (*ITC* 1612 (59 SATC 180)). It even extends to circumstances that arise subsequent to the default act or omission (*ITC* 1430, (50 SATC 51)). The state of mind of the defaulting taxpayer at the time that the act or omission was committed, and even subsequently, is vital. It should be established from the taxpayer’s *ipse dixit* (subjective test) and be weighed and tested against the probabilities and inferences drawn from the established facts (objective factors) (*ITC* 1185 (35 SATC 122)).

Even in cases in which the court found that there had been no intent on the part of the taxpayer to evade tax, but that there had been carelessness or even negligence on his part, the courts refer to “extenuating circumstances” as a justification for the remission of penalties (*ITC* 1518 (54 SATC 113); *ITC* 1576 (56 SATC 1)). It can therefore be concluded that once penalties have been imposed, even in cases in which the taxpayer had not intended to evade the payment of tax, the factors that the Court considers to justify the remission of a penalty are all included in the generic term “extenuating circumstances” or, in Afrikaans, “versagtende omstandighede”.

From the cases analysed in this article, a list of what the courts regard as “extenuating circumstances” begins to emerge. The extent of the penalty will normally not be determined by a single factor. Rather, it is submitted as a general proposition that the greater the number of prevailing “extenuating circumstances” that can be identified in favour of the taxpayer, the larger the remission of the penalty will be.

Some of the “extenuating circumstances” that have influenced the level of the penalty are:

- Reliance on a tax advisor, bookkeeper, accountant or member of staff.
- Personal circumstances: lifestyle, financial means.
“Extenuating circumstances” – the general meaning

- Supervening death of the taxpayer, insolvency.
- Ignorance of the law.
- Illiteracy, naivety.
- Conduct, character, attitude, behaviour.
- Negligence, carelessness.
- Effect on offender.
- Age.

In the Lutterworth case (MAN/86/405), it was found that even numeracy and sobriety (or rather the lack thereof) constituted “extenuating circumstances”.

As a result of the limited scope of this article, the above-mentioned list should not be regarded as exhaustive. New factors or circumstances may in the future be recognised as “extenuating” by the courts. In fact, it is submitted that the new Constitution of South Africa (Constitution of the Republic of South Africa Act, No. 108 of 1996) could be the catalyst for such a process in the future, for example if a taxpayer should plead that his or her political views constituted “extenuating circumstances”. It is also not the intention to imply that if a factor is present, which had previously been regarded as an “extenuating circumstance”, that factor would be regarded as “extenuating” in all circumstances. In addition, aggravating circumstances could be a consideration in a case that leads the judge to the conclusion that the previously recognised “extenuating circumstances” should be completely disregarded or accorded little weight in determining the level of the penalty to be imposed.

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